quarterly report

july august september

Q3 2008

TSO3

INDEX

MESSAGE FROM THE CHIEF EXECUTIVE OFFICER

Steady revenue growth, product development progress and reduced expenses

Dear Shareholders:

During the third-quarter ending September 30, 2008, TSO_3 continued the sales momentum it has been building since early second quarter. I expect this sales trend to continue during the fourth quarter thanks to, among other developments, new planned product enhancements, a promising vendor partnership agreement with a U.S. group purchasing organization and increased account segmentation marketing efforts.

In addition, our sales growth is also supported by our refocused marketing strategy announced last June, as well as the accreditation recently obtained by TSO_3 to market our Sterizone® *125L* Ozone Sterilizer to some 225 U.S. Government health care facilities, including military and veteran hospitals.

In the third quarter, TSO_3 recorded $725,257 in revenues from the sale of five sterilizer units and accessories, compared to sales of two units and accessories and revenues of $281,525 during the same quarter in 2007.

Sales were generated in each month of the third-quarter. This follows steady sales during each month of the second quarter, resulting in six consecutive months of sustained revenue growth. Sales for the first nine-months of 2008 reached $1,853,584. This is up from $1,055,401 for the same period in 2007.

New initiatives show results

Various commercial, operational and technological initiatives implemented in the second quarter continued to produce positive results in the third quarter. These measures included better alignment of TSO_3's products to suit market needs and the optimization of financial resources, resulting in efficiency gains and operating cost reductions.

Expense reductions initiated early in the second quarter have reduced the monthly burn-rate by about $150,000 as previously announced in June, which after one-time expenses including severance, are now being realized for the remainder of the year. This will enable TSO_3 to conserve liquidities in a difficult financial market, while at the same time benefiting from rising revenues.

Progress has also been made in reducing the sales and order/installation cycles, allowing TSO_3 to capture sales sooner and permit customers to begin using our sterilization system more rapidly. These efforts will translate into nearer-term and ongoing after-sale revenues from consumables and service contracts.

R&D achievements

R&D product development efforts have shown encouraging results. In particular, the Company is confident that current programs for expanding use of our Sterizone® *125L* Ozone Sterilizer will produce positive results.

In support of our focused selling efforts, our R&D group is also continuing to make progress on product improvements desired by customers for packaging and wraps (consumables) and for easier installation.

Vendor partner agreement

In early October, we were proud to announce that the Company was selected as a vendor partner by the Mid-Atlantic Group Network of Shared Services (MAGNET), one of the oldest and largest group purchasing organizations in the United States. East coast-based MAGNET, serves 11,000 healthcare providers including 750 acute care hospitals, by offering access to a contract portfolio of high-quality capital equipment and services. As a vendor partner, TSO_3 will supply MAGNET's members with its low temperature ozone sterilization system for hospital environments.

New President and CEO

At the beginning of October, TSO_3 was pleased to announce the appointment of Mr. Ric Rumble as President and Chief Executive Officer of the Company effective October 14, 2008. Mr. Rumble, who prior to this appointment held the position of President of BERCHTOLD Corporation, has more than 25 years of executive experience in the North American and global medical device industry.

Ric has a long and impressive track record in healthcare sterilization market, and within the medical device industry, including delivering significant and sustained revenue and earnings growth, leading successful new commercial strategies and negotiating and integrating large-scale acquisitions.

To ensure a smooth leadership transition, I will stay on with the Company in an advisory role to the new CEO for a brief period. During my tenure as Interim President and CEO, I have greatly enjoyed working with the talented and dedicated TSO_3 team to put the foundation in place for the Company's future growth and prosperity. I wish Ric and his team great success in building this innovative and dynamic enterprise to new heights.

W. Barry McDonald
Interim President and Chief Executive Officer

ANALYSIS OF FINANCIAL SITUATION AND OPERATING RESULTS

The following information must be read in conjunction with the audited financial statements and accompanying notes.

OVERVIEW

Founded in June 1998, TSO_3 (the "Company") has developed a unique new sterilization process that uses ozone as the sterilizing agent. The first device resulting from this technological platform, the Sterizone® *125L* Ozone Sterilizer, has been designed to sterilize the new generation of surgical and diagnostic instruments made of heat-sensitive polymers. After receiving approval from Health Canada on May 3, 2002, the Company obtained clearance from the United States Food and Drug Administration (FDA) to sell the Sterizone® *125L* Ozone Sterilizer and the accompanying Chemical Indicator on September 3, 2003.

INTERNAL SALES FORCE

The Company relies on its direct sales force to support its commercial sales strategy. This team can profit from the contribution of sales professionals predominantly in the United States, who have extensive experience selling capital equipment to both operating rooms and central sterilization departments in hospitals.

SUMMARY OF OPERATING RESULTS
Period ended September 30 (unaudited)

	THIRD QUARTER		NINE MONTHS	
	2008	2007	**2008**	2007
SALES	**$725,257**	$281,525	**$1,853,584**	$1,055,401
EXPENSES				
Operating	**715,927**	431,548	**1,874,377**	1,246,332
Sales & marketing	**732,574**	1,055,463	**2,943,083**	3,039,599
Research and development	**549,962**	438,415	**1,634,592**	1,267,439
Administrative	**773,096**	725,911	**2,828,598**	2,303,356
Financial	**6,092**	4,342	**18,309**	11,048
	2,777,651	2,655,679	**9,298,959**	7,867,774
OPERATING LOSS	**2,052,394**	2,374,154	**7,445,375**	6,812,373
OTHER REVENUES	**203,535**	331,424	**708,952**	1,066,486
NET LOSS	**$1,848,859**	$2,042,730	**$6,736,423**	$5,745,887
BASIC AND DILUTED NET LOSS PER SHARE	**$0.04**	$0.04	**$0.14**	$0.13
WEIGHTED AVERAGE NUMBER OF SHARES OUTSTANTDING	**47,863,402**	47,790,928	**47,863,402**	44,473,596

OPERATING RESULTS

Three and nine-month periods ended September 30, 2008, compared with the three and nine-month periods ended September 30, 2007.

Sales

Sales for the three-month period ended September 30, 2008 amounted to $725,257 representing the sale of five sterilizers and related accessories, compared to $281,525, representing the sale of two sterilizers and related accessories for the same period in 2007. For the nine-month period ended September 30, 2008, 11 sterilizers and accessories were sold for total sales of $1,853,584, compared to five sterilizers and accessories in 2007 for total sales of $1,055,401.

OPERATING RESULTS (CONT'D)

Operation

For the three-month period ended September 30, 2008, Operating expenses were $715,927 compared to $431,548 for the same period in 2007. Operating expenses are related to manufacturing and after-sales service department. The variance between the two periods is because of an increase in the cost of goods sold due to a superior number of devices sold. For the nine-month period ended September 30, 2008, Operating expenses amounted to $1,874,377 compared to $1,246,332 for the same period in 2007. The variance is also explained by an increase in the cost of goods sold, due to a superior number of devices sold.

Sales and Marketing

Sales and Marketing expenses amounted to $732,574 for the three-month period ended September 30, 2008 compared to $1,055,463 for the same period in 2007. The variance between the two periods is mainly because of a decrease in salaries, fees related to hiring personnel and expenses due to a reduction in the number of regional sale managers following a reorganization implemented last June. Conversely, professional fees increased between the two periods. For the nine-month period ended September 30, 2008, Sales and Marketing expenses amounted to $2,943,083 compared to $3,039,599 for the corresponding period in 2007. This variance is also explained by a decrease in salaries, fees related to hiring personnel and expenses. Conversely, professional fees increased between the two periods.

Research and Development

For the three-month period ended September 30, 2008, R&D expenses before tax credits amounted to $549,962 compared to $438,415 for the same period in 2007. The variance between the two periods is from the results of the addition of six new employees to the R&D department following a reorganization implemented last June and an increase in material purchases and professional fees. For the nine-month period ended September 30, 2008, R&D expenses amounted to $1,634,592 compared to $1,267,439 for the corresponding period in 2007. The variance between the two periods is also due to an increase in salaries, material purchases and professional fees.

Administrative

Administrative expenses amounted to $773,096 for the three-month period ended September 30, 2008 compared to $725,911 for the same period in 2007. The variance between the two periods is due to an increase in professional fees. Conversely, salaries and expenses related to stock-based compensation decreased between the two periods. For the nine-month period ended September 30, 2008, Administrative expenses amounted to $2,828,598 compared to $2,303,356 for the corresponding period in 2007. The increase between the two periods is due to a severance payment in 2008 and from an increase in professional fees. Conversely, expenses related to stock-based compensation decreased also between the two periods.

Other Revenues

For the three-month period ended September 30, 2008, the Company realized other revenues of $203,535 compared to $331,424 for the same period in 2007. The variance between the two periods is due to a decrease in investment revenues. For the nine-month period ended September 30, 2008, the Company realized other revenues of $708,952 compared to $1,066,486 for the corresponding period in 2007. The variance between the two periods is also due to a decrease in investment revenues, as well as a decrease in grants received.

Net Loss

The Company recorded a net loss of $1,848,859 or $0.04 per share for the third quarter of 2008, compared to a net loss of $2,042,730, also $0.04 per share for the same period in 2007. For the nine-month period ended September 30, 2008, net loss amounted to $6,736,423 or $0.14 per share, compared to $5,745,887, or $0.13 per share for the same period in 2007.

SELECTED ELEMENTS

	SEPTEMBER 30		DECEMBER 31		
	2008	2007	2007	2006	2005
Cash, Cash equiv. and Temporary Investments	**$18,697,032**	$27,837,259	$26,205,174	$7,308,782	$14,595,003
Accounts Receivable	**$1,880,193**	$940,077	$975,011	$811,119	$344,302
Inventories	**$2,791,106**	$2,848,385	$2,996,409	$3,387,837	$3,303,258
Assets	**$27,950,918**	$35,995,447	$34,487,951	$15,743,739	$22,587,034
Deferred Revenues	**$330,617**	$140,501	$145,878	$75,709	$961,826
Share Capital and Contributed Surplus	**$80,987,896**	$80,509,820	$80,681,660	$52,148,977	$50,656,921
Shareholders' Equity	**$26,645,952**	$35,035,959	$33,041,196	$14,624,330	$20,609,717

Liquid Assets and Financial Situation

As of September 30, 2008, cash, cash equivalents and temporary investments amounted to $18,697,032 and accounts receivable to $1,880,193 for a total of $20,577,225 compared to $28,777,336 as of September 30, 2007.

Account Receivable

Accounts Receivable as of September 30, 2008, amounted to $1,880,193 compared to $940,077 for the same period in 2007. The difference between the two periods is due to an increase in accounts receivable.

Deferred Revenues

Deferred Revenues as of September 30, 2008, amounted to $330,617 compared to an amount of $140,501 as of September 30, 2007. The item *Deferred Revenues* reflects financial transactions related to parts, warranties and service contracts not yet recognized as revenues. The increase between the two periods is explained by amounts received for service contracts.

REQUIRED CAPITAL AND CONTRACTUAL COMMITMENTS

Required capital payments and the various contractual commitments in the coming fiscal year are as follows:

	2008	2009	2010	2011	2012	2013
Operating leases and service contracts	**$101,157**	$74,808	$52,587	$8,610	$3,120	$260

SUMMARY OF QUARTERLY RESULTS

	2008			2007				2006	
($000 except loss/ share)	**Q3**	Q2	Q1	Q4	Q3	Q2	Q1	Q4	Q3
Sales	**725**	1,037	91	676	281	575	199	434	34
Other Revenues	**204**	203	301	399	331	561	174	242	150
Net Loss	**1,848**	2,728	2,160	2,166	2,043	1,634	2,069	1,967	2,013
Net Loss per share (basic and diluted)	**0.04**	0.05	0.05	0.04	0.04	0.04	0.05	0.05	0.06

This figure shows the quarterly evolution of sales and other income as well as losses. The item *Net Loss per Share* has not improved for the past nine quarters. Besides the item *Net Loss* showed the effects of the reorganization started last June during the third quarter, compared to the previous quarter.

CAPITAL RESOURCES

The Company principally uses its capital to finance operating expenses, commercialisation fees, marketing expenses, R&D expenses, administrative expenses, working capital and capital expenditures. Historically, the Company has funded its activities through several rounds of public and private financing, as well as from various government subsidies. Since its inception in June 1998, the Company has raised more than $70,000,000 from the sale of its equity.

CAPITAL RESOURCES (cont'd)

For the three-month period ended September 30, 2008, the monthly burn-rate was approximately $700,000. In recent months, the Company has implemented measures to decrease its cash burn rate and the third quarter of 2008 allowed the Company to evaluate the effects of these measures. The Company believes that its current liquid assets are sufficient to finance its activities through 2010.

In March 2007, the Company closed a round of financing. Included in this financing 4,600,000 whole warrants were issued. These warrants entitling the holder to purchase one common share of the Company at a price of $3.00/share until March 8, 2009.

The Company has a line of credit with which it can obtain advances up to a maximum of $350,000.

The Company invests its liquidities in fixed-income securities offered by governmental, paragovernmental and municipal entities as well as from companies that have high credit ratings. These securities are chosen according to the schedule of foreseen expenses and according to interest rates. Also, the Company does not hold investments in Asset Backed Commercial Paper that are not guaranteed by financial institutions or by the Government.

As of September 30, 2008, the number of outstanding shares was 47,863,402.

OFF-BALANCE SHEET TRANSACTION

The Company made no off-balance sheet transaction during the third quarter of 2008.

TRANSACTIONS WITH RELATED PARTIES

The Company leases its premises from a corporation owned by some of the Company's shareholders.

Over the first three quarters of 2008 and 2007 and the last two complete fiscal years, the Company has made the following related transactions, assessed at fair market value:

	SEPTEMBER 30		DECEMBER 31	
	2008	2007	2007	2006
Rent	**$46,171**	$44,524	$59,365	$57,804
Other Rent-related Expenses	**56,931**	53,699	67,069	76,431
	$103,102	$98,223	$126,434	$134,235

As of September 30, 2008, no amount was included in accounts payable related to a related party as well as in 2007.

CRITICAL ACCOUNTING POLICIES

The Company financial statements are prepared in accordance with Generally Accepted Accounting Principles in Canada ("G.A.A.P."). The Company's critical accounting policies include the use of estimates, revenue recognition, the recording of research and development expenses and the determination of the useful lives or fair value of goodwill and intangible assets. Some of our critical accounting policies require the use of judgment in their application or require estimates of inherently uncertain matters.

Estimation and principal Accounting Policies

There has been no significant change to estimation and accounting policies since December 31, 2007, except to comply with the new accounting standards described hereafter. For a detailed description of the new accounting standards, refer to the corresponding section of our 2007 Annual report available on the SEDAR website (www.sedar.com).

ACCOUNTING CHANGES

Impact of adopting new accounting standards

On January 1, 2008 the company adopted the new accounting standards issued by the Canadian Institute of Chartered Accountants (CICA): “Capital Disclosures” (section 1535), “Inventories” (section 3031), “Financial Instruments – Disclosure” (section 3862) and “Financial Instruments – Presentation” (section 3863). The new standards were applied prospectively without restatement of comparative financial statements.

1) Inventories: Section 3031 provides guidance on the determination of cost and its subsequent recognition as an expense, including any write-down to net realizable value. It also provides guidance on the cost formulas that are used to assign costs to inventories.

On January 1, 2008, the Company adjusted the following balance sheet items in order to comply with the new accounting standard:

	SEPTEMBER 30	
	2008	2007
Increase (decrease)		
Balance sheet		
Inventories	**$34,943**	$ -
Statement of deficit		
Accounting changes	**($34,943)**	$ -

Since this standard came into effect, the Company has been recording its raw materials inventory at the lower of cost and net realizable value. In the past, the Company recorded raw materials inventory at the lower of cost and replacement value.

2) Capital: Section 1535, “Capital Disclosures”, establishes standards for disclosing information about an entity’s capital and how it is managed. It describes the disclosure requirements of the entity’s objectives, policies and processes for managing capital, the quantitative data relating to what the entity regards as capital, whether the entity has complied with capital requirements, and, if it has not complied, the consequences of such non-compliance.

   Since the standard came into effect, the Company has been presenting relevant information about capital management in the “Share capital” note.

ACCOUNTING CHANGES (CONT'D)

Impact of adopting new accounting standards (cont'd)

3) Financial Instruments: Sections 3862 and 3863 place heightened importance on disclosure, enabling financial statement users to assess the nature and extent of the risks associated with the financial instruments to which the Company is exposed and the manner in which it manages these risks.

LIQUIDITY AND FINANCIAL RESOURCES

Management believes that it will be able to raise the necessary long-term capital to achieve the Company's corporate objectives. However, the availability of these financial resources cannot be guaranteed.

VOLATILITY OF SHARE PRICE

Company share prices are subject to volatility. Financial and scientific results that differ from analysts' projections may lead to significant variations in the price of Company shares.

PERSPECTIVES

The Company works in an industry dominated by multinational companies that market primarily two low temperature sterilization technologies: Ethylene Oxyde and Hydrogen Peroxide. The Company's primary target markets are central sterilization departments in hospitals. This is, by nature, a conservative market where sales cycles are long as a result of administrative procedures. To address these realities, the Company relies on a combination of factors. First, the technology brings to the market a unique sterilization process that provides efficiency, economy and safety. Second, the Company relies on its own sales force, comprised of sales professionals who have extensive experience selling capital equipment to hospitals.

PERSPECTIVES (CONT'D)

In parallel, the sterilization equipment manufacturers must adjust to market demands and respond to changes in medical devices – design and construction. This requires TSO_3 continue the work necessary to guarantee ongoing compatibility with heat and moisture sensitive instruments.

On June 5, 2008 the Company announced that it would be realigning resources and re-focusing marketing activities to enhance its rate of market penetration and sales growth for 2008 and beyond. These initiatives will also allow the Company to significantly reduce its operating expense rate thanks to more efficient use of sales and marketing resources. These initiatives impact four areas: (1) a segmentation of the market targeting firstly North American hospitals; (2) a reorganization of the sales team to allow senior management to concentrate their efforts more effectively on qualified prospects ("poised purchaser"); (3) a reduction in the cash burn rate by the end of 2008; (4) a realignment of R&D programs to better address market needs and adding additional resources to accelerate the development of our competitive advantages.

On October 6, 2008, TSO_3 announced the appointment of Mr. R.M. (Ric) Rumble as President and Chief Executive Officer of the Company, effective October 14. Mr. Rumble, who prior to this appointment held the position of President of BERCHTOLD Corporation, has more than 25 years of executive experience in global medical device and sterilization market segment, including prior general management positions within STERIS Corporation, Global Health Care Sterilization Business.

In addition, a significant portion of the Company's revenues are received in US dollars. The fluctuation of the exchange rate in favour of the Canadian dollar versus the US dollar negatively affects the Company bottom line. This reality is offset by the fact that approximately 20% of Company expenses are paid out in US dollars.

RATE RISK AND SEGMENTED INFORMATION

Interest rate risk

Interest rate risk exists when interest rate fluctuations modify the cash flows of the Company's investments.

As of September 30, 2008, if the Canadian dollar had weakened 10 percent against the U.S. dollar with all other variables held constant, after-tax net loss and other comprehensive loss for the nine-month period would have been $66,708 lower. Conversely, if the Canadian dollar had strengthened 10 percent against the U.S. dollar with all other variables held constant, after-tax net loss and other comprehensive income would have been $66,708 higher.

RATE RISK AND SEGMENTED INFORMATION (CONT'D)

Operational Foreign Exchange Risk

For the first nine months of 2008, 54% of the Company's sales were in Canadian dollars compared to 28% for the same period in 2007.

Segmented Information

Operating revenues according to geographic area are as follows:

	SEPTEMBER 30	
	2008	2007
Canada	**$1,009,259**	$298,254
United States	**844,325**	757,147
	$1,853,584	$1,055,401

RISK FACTORS

Risks related to operating activities

The Company's activities entail certain risks and uncertainties inherent to the industry in which it operates. However, management has implemented a risk-reduction strategy that addresses:

Risks associated with international operations

TSO_3 must carry out the majority of its sales outside of Quebec and Canada, either in the United States. The necessity of marketing on an international scale puts the Company in a position of direct competition with firms that possess networks and resources greater than its own. Nothing guarantees that the marketing campaigns implemented by the Company for international markets, alone or with strategic alliances, will be successful. The operations of TSO_3 at an international level could be negatively affected by factors such as Canadian and United States foreign trade policies, investments and taxes, foreign exchange rate controls and fluctuations, political instability and increased payment periods. One or more of these factors could have a significantly negative effect on the financial situation and results of the Company.

Compatibility, Biocompatibility and Research and Development Projects

All sterilization processes can affect medical instruments or alter their key properties over a period of time. Taking into consideration the nature of the devices to be sterilized and the oxidative effects on devices in contact with ozone, TSO_3 limits to a minimum the frequency and duration that the devices are exposed to ozone. Nevertheless, oxidization can produce several effects, depending on the material. In order to fully establish the true commercial value of its sterilization process, the Company must demonstrate the compatibility of its technology with a wide range of medical instruments. Even though the tests and studies undertaken to date by TSO_3 have shown that its ozone sterilization process is compatible with the majority of medical instruments currently used in the hospital environment, the Company must maintain ongoing studies in this respect. Besides, the Company can not guarantee the success of its different R&D projects.

Dependency on key personnel

TSO_3 believes that its success will continue to depend on its ability to attract and retain qualified managers and other key personnel. Losing a key employee could have a major negative impact on TSO_3.

Management of Business Growth

Achieving its short-term objectives could launch the Company into a phase of significant and rapid growth and force it to considerably increase its personnel, the number of partners, cash flow and operating capacity.

Intellectual Property and Counterfeiting Risks

The success of the Company is based on its unique technology. TSO_3 relies on a combination of patents, trade secrets, non-disclosure agreements and various contractual provisions in order to protect its technology. Nothing guarantees that these measures will be sufficient to protect any illegal appropriation or infringement of its technology by a third party.

Competition Risks

The Company's products face intense competition. Many of our competitors have greater financial resources and marketing capabilities than our own. TSO_3's competitors and potential competitors may succeed in developing products and processes that are more effective and less expensive to use than any products or processes the Company may develop or licence, or that may render TSO_3's products or processes obsolete. The high level of competition in the sterilization industry could force the Company to reduce the price at which it sells its products or require TSO_3 to spend more time and money to market its products.

Product Liability Issues

In the health sector, lawsuits, often claiming substantial damages, are becoming increasingly common. In particular, in the United States, lawsuits are filed by patients, employees or beneficiaries against healthcare providers, as well as authorities operating and managing hospitals in the private and public sectors. During these proceedings, claimants could allege and blame the non-sterility of certain instruments or defective functioning of products sold, installed or derived from TSO_3's technology. To address the problems associated with such lawsuits, the Company is of the opinion that it has the necessary insurance coverage.

Cash Equivalents and Temporary Investments

The Company is exposed to various types of risks, including those related to the use of financial instruments. To manage the risks included in the various types of investments that make up cash equivalents and temporary investments, controls were put in place, particularly those related to cash and risk management policy. These measures aim primarily to optimize cash flow performance while reducing the main risks to which the Company is exposed, as described below:

Market Risk

Market risk is the risk that the value of a financial instrument will fluctuate as a result of changes in the parameters underlying their measurement, particularly interest rates and market prices.

Interest Rate Risk

Interest rate risk exists when interest rate fluctuations modify the cash flows of the Company's investments.

Cash Equivalents and Temporary Investments (cont'd)

Interest Rate Risk (cont'd)

As of September 30, 2008, if interest rates at that date had been 50 basis points lower and all other variables constant, after-tax net loss and other comprehensive loss for the period would have been $29,631 lower, arising mainly from a decrease in the fair value of fixed rate financial assets classified as held for trading. If interest rates had been 50 basis points higher and all other variables constant, after-tax net loss and other comprehensive loss for the period would have been $29,419 higher, arising mainly from an increase in the fair value of fixed rate financial assets classified as held for trading. Net loss has sensitivity similar to the interest rate decrease than to the increase because of investments with capped interest rates.

Credit Risk

The use of financial instruments can create a credit risk that is the risk of financial loss resulting from counterparty's inability or refusal to fully discharge its contractual obligations. The Company's credit risk management policies include the authorization to carry out investment transactions with recognized financial institutions, with credit ratings of at least A and higher, in either bonds, money market funds or guaranteed investment certificates according to Standard and Poor's Agency. Consequently, the Company manages credit risk by complying with established investment policies. The Company establishes investment policies that are reviewed, regularly updated and approved. These policies define the credit risk limits based on the characteristics of the counterparties. As of September 30, 2008, the investments of the Company were all quoted by a recognized agency.

Concentration Risk

Concentration risk exists when investments are made with multiple entities that share similar characteristics or when a large investment is made with a single entity. As of September 30, 2008, the Company was holding more than 66% of its cash equivalents portfolio in money market funds.

RISK FACTORS (CONT'D)

Liquidity Risk

Liquidity risk represents the possibility of the Company not being able to raise the funds needed to meet financial commitments at the appropriate time and under reasonable conditions. The Company manages this risk by maintaining permanent and sufficient liquidity to meet current and future financial obligations, under both normal and exceptional circumstances. The funding strategies used to manage this risk include turning to capital markets to carry out issues of equity and debt securities.

DISCLOSURE CONTROLS AND PROCEDURES

The Chief Executive Officer and the Chief Financial Officer of the Company are responsible for establishing and maintaining the Company's controls and disclosure procedures. They are assisted in this responsibility by the Company's Communication Committee, which is composed of members of Senior Management, the Director of Communications and IR, as well as the Company's legal advisor. As required by Securities Legislation, the CEO and the CFO have conducted an evaluation of the controls and procedures regarding information disclosure and have concluded that these controls and procedures are effective.

In addition, since October 1, 2008, the Company has been using a new computer program for both its financial and manufacturing processes. This change has allowed the Company to implement new computerized internal controls and, consequently, revise certain procedures. As with the former system, the management is of the opinion that this new ERP system meets entirely the Company's obligations to implement controls and procedures regarding information disclosure and internal control of financial information.

PROSPECTIVE STATEMENT

This document contains certain prospective statements that reflect the Company's current expectations concerning future activities. These prospective statements include risks and uncertainties. Actual results can differ considerably from the results, as previously described in this report, expected by the Company. Investors are advised to consult the Company's quarterly and annual reports, as well as the filing of the Company's annual information form for more details on the risks and uncertainties related to these prospective statements. The reader must not unduly rely upon the Company's prospective statements. The Company is not obliged to update these prospective statements.

PROSPECTIVE STATEMENT (CONT'D)

This Management Report has been prepared as of October 29, 2008. Additional information on the Company is available through regular filing of press releases, annual reports, quarterly financial statements and the Annual Information Form on the SEDAR website (www.sedar.com).

EXAMINATION OF THE FINANCIAL STATEMENTS

The Quarterly Financial Statements have not been audited by the External Controller.

Marc Boisjoli, M.Sc.
Vice President, Finance and Chief Financial Officer

October 29, 2008

QUARTERLY FINANCIAL STATEMENTS

The Quarterly Financial Statements have not been reviewed by External Auditors

STATEMENT OF EARNINGS
Periods ended September 30 (unaudited)

	THIRD QUARTER		NINE MONTHS	
	2008	2007	**2008**	2007
SALES	**$725,257**	$281,525	**$1,853,584**	$1,055,401
EXPENSES				
Operating	**715,927**	431,548	**1,874,377**	1,246,332
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Financial	**6,092**	4,342	**18,309**	11,048
	2,777,651	2,655,679	**9,298,959**	7,867,774
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OTHER REVENUE	**203,535**	331,424	**708,952**	1,066,486
NET LOSS	**$1,848,859**	$2,042,730	**$6,736,423**	$5,745,887

EARNINGS PER SHARE
Periods ended September 30 (unaudited)

	THIRD QUARTER		NINE MONTHS	
	2008	2007	**2008**	2007
NET LOSS	**$1,848,859**	$2,042,730	**$6,736,423**	$5,745,887
NUMBER OF SHARES				
Weighted average number of outstanding shares [1)]	**47,863,402**	47,790,928	**47,863,402**	44,473,596
LOSS PER SHARE				
Basic	**$0.04**	$0.04	**$0.14**	$0.13
Diluted	**$0.04**	$0.04	**$0.14**	$0.13

(1) The calculation of the weighted average number of outstanding shares is determines as a function of the number of outstanding common shares based on the fraction of the period during which the shares were outstanding.

The weighted average number of outstanding shares is the same number used in the calculation of the diluted net loss per share since including potential common shares in the computation of the diluted per share amount of a loss is always anti-dilutive.

STATEMENTS OF CONTRIBUTED SURPLUS

Periods ended September 30 (unaudited)

	THIRD QUARTER		NINE MONTHS	
	2008	2007	**2008**	2007
Balance, beginning of period	**$7 667,566**	$8,171,801	**$7,471,369**	$4,999,850
Options exercised	**-**	(7,680)	**-**	(34,742)
Warrants exercised	**-**	(1,058,163)	**-**	(1,292,410)
Warrants related to the financing	**-**	-	**-**	2,819,051
Compensation Options	**-**	-	**-**	281,520
Stock-based Compensation	**110,039**	173,894	**306 236**	506,583
Balance, end of period	**$7,777,605**	$7,279,852	**$7,777,605**	$7,279,852

STATEMENTS OF DEFICIT

Periods ended September 30 (unaudited)

	THIRD QUARTER		NINE MONTHS	
	2008	2007	**2008**	2007
Balance, beginning of period	**$52,493,085**	$43,429,718	**$47,640,464**	$37,524,647
Change in accounting policies	**-**	-	**(34,943)**	(20,216)
Restated deficit	**$52,493,085**	$43,429,718	**$47,605,521**	$37,504,431
Share issue expenses	**-**	1,413	**-**	1,942,023
Compensation Options	**-**	-	**-**	281,520
Net loss	**$1,848,859**	$2,042,730	**$6,736,423**	$5,747,887
Balance, end of period	**$54,341,944**	$45,473,861	**$54,341,944**	$45,473,861

BALANCE SHEET as of

	September 30, 2008 (unaudited)	December 31 2007 (audited)	September 30, 2007 (unaudited)
CURRENT ASSETS			
Cash and cash equivalents	**$18,349,321**	$22,081,727	$25,301,676
Temporary investments	**347,711**	4,123,447	2,535,583
Accounts receivable	**1,880,193**	975,011	940,077
Inventories	**2,791,106**	2,996,409	2,848,385
Prepaid expenses	**257,340**	139,410	178,034
	23,625,671	30,316,004	31,803,755
PROPERTY, PLANT AND EQUIPMENT	**804,194**	508,118	522,215
INTANGIBLE ASSETS	**3,521,053**	3,663,829	3,669,477
	$27,950,918	$34,487,951	$35,995,447
CURRENT LIABILITIES			
Accounts payable and accrued liabilities	**$974,349**	$1,300,877	$818,987
Deferred revenues	**330,617**	145,878	140,501
	1,304,966	1,446,755	959,488
SHAREHOLDERS' EQUITY			
Share capital	**73,210,291**	73,210,291	73,229,968
Contributed surplus	**7,777,605**	7,471,369	7,279,852
Deficit	**(54,341,944)**	(47,640,464)	(45,473,861)
	26,645,952	33,041,196	35,035,959
	$27,950,918	$34,487,951	$35,995,447

STATEMENTS OF CASH FLOWS
Periods ended September 30 (unaudited)

	THIRD QUARTER		NINE MONTHS	
	2008	2007	**2008**	2007
OPERATING ACTIVITIES				
Net loss	**($1,848,859)**	($2,042,730)	**($6,736,423)**	($5,745,887)
Adjustment for :				
Amortization of property, plant and equipment	**52,360**	37,889	**141,068**	105,723
Amortization of intangible assets	**59,031**	57,082	**176,387**	169,659
Change in the value of temporary investments	**(7,683)**	-	**(87,215)**	-
Stock-based compensation	**110,039**	173,894	**306,236**	506,583
Gain on disposal of property, plant and equipment	**-**	-	**(8,124)**	457
	($1,635,112)	($1,773,865)	**($6,208,071)**	($4,963,465)
Changes in non-cash operating working items	**(425,847)**	(33 ,396)	**(959,598)**	206,190
Impact of new standards	**-**	-	**34,943**	-
Cash flows used in operating activities	**(2,060,959)**	(1,807,261)	**(7,132,726)**	(4,757,275)
INVESTING ACTIVITIES				
Acquisiton of temporary investments	**(4 000 000)**	1,477,384	**(5,503,000)**	(9,535,583)
Disposal of temporary investments	**6,349,950**	-	**9,365,951**	7,000,000
Acquisition of property, plant and equipment	**(77,802)**	(41,773)	**(437,448)**	(237,787)
Acquisition of intangible assets	**(16,143)**	(42,364)	**(33,611)**	(127,394)
Disposal of property, plant and equipment	**-**	-	**8,428**	-
Cash flows used in investing activities	**(2,256,005)**	1,393,247	**3,400,320**	(2,900,764)
FINANCING ACTIVITIES				
Options exercised	**-**	10,200	**-**	50,765
Warrants exercised	**-**	4,033,250	**-**	4,521,975
Share issue expenses	**-**	(1,413)	**-**	(1,942,023)
Share issue	**-**	-		23,000,000
Cash flows used in financing activities	**-**	4,042,037	**-**	25,630,717
INCREASE IN CASH AND CASH EQUIVALENTS	**195,046**	3,628,023	**(3,732,406)**	17,972,678
Cash and cash equivalents at beginning	**18,154,275**	21,673,653	**22,081,727**	7,328,998
CASH AND CASH EQUIVALENTS AT THE END	**$18,349,321**	$25,301,676	**$18,349,321**	$25,301,676
Comprised of :				
Cash	**$18,349,321**	$2,713,125	**$18,349,321**	$2,713,125
Temporary investments less than three months	**-**	22,588,551		22,588,551
Temporary investments more than three months	**347,711**	2,535,583	**347,711**	2,535,583
CASH, CASH EQUIVALENTS AND TEMPORARY INVESTMENTS	**$18,697,032**	$27,837,259	**$18,697,032**	$27,837,259

The accompanying notes are in integral part of the financial statements

Critical Accounting Policies

The unaudited financial statements are prepared in accordance with Canadian generally accepted accounting principles for interim financial statements and do not include all the information required for complete financial statements. Interim results may not necessarily be indicative of results anticipated for the entire year. Moreover, they do not include all the information presented in the annual financial statements. The unaudited financial statements are consistent with the policies outlined in the Company's audited financial statements for the year ended December 31, 2007.

The interim financial statements and related notes should be read in conjunction with the Company's audited financial statements for the year ended December 31, 2007.

Certain of the prior periods comparative amounts have been reclassified to conform to the current period.

ACCOUNTING CHANGES

Impact of adopting the new accounting standards

On January 1, 2008 the company adopted the new accounting standards issued by the Canadian Institute of Chartered Accountants (CICA): "Capital Disclosures" (section 1535), "Inventories" (section 3031), "Financial Instruments – Disclosure" (section 3862) and "Financial Instruments – Presentation" (section 3863). The new standards were applied prospectively without restatement of comparative financial statements.

1) Inventories: Section 3031 provides guidance on the determination of cost and its subsequent recognition as an expense, including any write-down to net realizable value. It also provides guidance on the cost formulas that are used to assign costs to inventories.

ACCOUNTING CHANGES (CONT'D)

Impact of adopting the new accounting standards (cont'd)
On January 1, 2008, the Company adjusted the following balance sheet items in order to comply with the new accounting standard:

	SEPTEMBER 30	
	2008	2007
Increase (decrease)		
Balance sheet		
Inventories	**$34,943**	$-
Statement of deficit		
Accounting changes	**($34,943)**	$-

Since this standard came into effect, the Company has been recording its raw materials inventory at the lower of cost and net realizable value. In the past, the Company recorded raw materials inventory at the lower of cost and replacement value.

2) Capital: Section 1535, "Capital Disclosures", establishes standards for disclosing information about an entity's capital and how it is managed. It describes the disclosure requirements of the entity's objectives, policies and processes for managing capital, the quantitative data relating to what the entity regards as capital, whether the entity has complied with capital requirements, and, if it has not complied, the consequences of such non-compliance.

   Since the standard came into effect, the Company has been presenting relevant information about capital management in the "Share capital" note.

3) Financial Instruments: Sections 3862 and 3863 place heightened importance on disclosure, enabling financial statement users to assess the nature and extent of the risks associated with the financial instruments to which the Company is exposed and the manner in which it manages these risks.

FINANCIAL INSTRUMENTS

Cash equivalents and temporary investments

The Company is exposed to various types of risks, including those related to the use of financial instruments. To manage these risks included in the various types of investments that make up cash equivalents and temporary investments, controls were put in place, particularly those related to cash and risk management policy. These measures aim primarily to optimize cash flow performance while reducing the main risks to which the Company is exposed, as described below.

Market Risk

Market risk is the risk that the value of a financial instrument will fluctuate as a result of changes in the parameters underlying their measurement, particularly interest rates and market prices.

Interest Rate Risk

Interest rate risk exists when interest rate fluctuations modify the cash flows of the Company's investments.

As of September 30, 2008, if interest rates at that date had been 50 basis points lower and all other variables constant, after-tax net loss and other comprehensive income for the period would have been $29,631 lower, arising mainly from a decrease in the fair value of fixed rate financial assets classified as held for trading. If interest rates had been 50 basis points higher and all other variables constant, after-tax net loss and other comprehensive income for the period would have been $29,419 higher, arising mainly from an increase in the fair value of fixed rate financial assets classified as held for trading. Net loss has sensitivity similar to the interest rate decrease than to the increase because of investments will capped interest rates.

Credit Risk

The use of financial instruments can create a credit risk that is the risk of financial loss resulting from a counterparty's inability or refusal to fully discharge its contractual obligations. The Company's credit risk management policies include the authorization to carry out investment transactions with recognized financial institutions, with credit ratings of at least A and higher, in either bonds, money market funds or guaranteed investment certificates according to Standard and Poor's. Consequently, the Company manages credit risk by complying with established investment policies. The Company establishes investment policies that are reviewed, regularly updated and approved. These policies define the credit risk limits based on the characteristics of the counterparties. The investments of the Company were all quoted by a recognized agency and met the Company's investment policy criteria.

Concentration Risk

Concentration risk exists when investments are made with multiple entities that share similar characteristics or when a large investment is made with a single entity. As of September 30, 2008, the Company was holding more than 66% of its cash equivalents portfolio in a money market fund.

Liquidity Risk

Liquidity risk represents the possibility of the Company not being able to raise the funds needed to meet financial commitments at the appropriate time and under reasonable conditions. The Company manages this risk by maintaining permanent and sufficient liquidity to meet current and future financial obligations, under both normal and exceptional circumstances. The funding strategies used to manage this risk include turning to capital markets to carry out issues of equity and debt securities.

	SEPTEMBER 30	
	2008	2007
Commercial paper and bonds, maturing at various dates through January 2009 and having an average yield of 3.26%	**$6,197,662**	$4,572,154
Money market funds	**11,906,502**	$20,551,980
	$18,104,164	$25,124,134
Distributed as follows :		
Cash equivalents	**$17,756,453**	$22,588,551
Temporary investments	**347,711**	2,535,583
	$18,104,164	$25,124,134

Cash equivalents are presented on the balance sheet under "Cash and cash equivalents." This item comprises $592,868 in cash and $17,756,453 in cash equivalents, for a total of $18,349,321 ($25,301,676 in 2007).

FINANCIAL INSTRUMENTS (CONT'D)

Foreign currency exchange rate risk
Foreign currency exchange risk exists when financial assets are denominated in foreign currency.

As of September 30, 2008, if the Canadian dollar had weakened 10 percent against the U.S. dollar with all other variables held constant, after-tax net income and other comprehensive income for the nine-month period would have been $66,708 lower. Conversely, if the Canadian dollar had strengthened 10 percent against the U.S. dollar with all other variables held constant, after-tax net income and other comprehensive income would have been $66,708 higher.

SHARE CAPITAL

	SEPTEMBER 30			
	2008		2007	
Issued and paid	**Number**		Number	
Balance at beginning	**47,863,402**	**$73,210,291**	36,800,853	$47,149,127
New issue	**-**	**-**	9,200,000	20,180,949
Options exercised	**-**	**-**	27,999	85,507
Warrants exercised	**-**	**-**	1,834,550	5,814,385
Balance at end	**47,863,402**	**$73,210,291**	47,863,402	$73,229,968

Other comprehensive income

According to Section 1530 "Comprehensive Income", the Company must present a Statement of Comprehensive Income. Given that the Company has classified all of its financial instruments as financial instruments held for trading, no change had to be recognized in comprehensive income. Consequently, the net loss is equal to total comprehensive income.

Capital management

The Company uses its capital to finance research and development activities, operating, administrative and marketing expenses, working capital and capital assets. Historically, the Company has financed activities through rounds of public and private financing as well as government grants. According to its capacities and prevailing market conditions, the Company could finance, in whole or in part, its long-term assets through long-term debt.

For the three-month period ended September 30, 2008, the monthly burn-rate was approximately $700,000. In recent months, the Company has recently implemented measures to decrease its cash burn rate and the third quarter of 2008 allowed the Company to evaluate the effects of these measures. The Company believes that its current liquid assets are sufficient to finance its activities through 2010.

The Company has a line of credit through which it can obtain advances up to a maximum of $350,000. To maintain this line of credit, the Company must respect certain ratios, more specifically its working capital ratio as well as the net value of its capital. Although the line of credit remains undrawn, the Company reviews these ratios every month. As of September 30, 2008, these ratios were met.

Each quarter, the Company reviews the loss-per-share ratio with the objective of improving this ratio. Over the years, this ratio has been maintained at a steady level.

Stock options and Warrants

As of July 30, 2008, the Company has granted 50,000 stock options to a Company supplier. These options entitle the holder to subscribe to common shares of the Company at a price of $0.61 until July 30, 2013. The fair value of stock options is $0.33 per share.

As of July 30, 2008, the Company has granted 12,000 stock options to certain employees of the Company. These options, which vest over three years, entitle the holder to subscribe to common shares of the Company at a price of $0.61 until July 30, 2018. The fair value of stock options is $0.42 per share.

SHARE CAPITAL (CONT'D)

Stock options and Warrants (cont'd)

The Black-Scholes options pricing model was developed for use in estimating the fair value of traded options which have no vesting restrictions and are fully transferable, a practice significantly different from how stock options are granted by the Company. In addition, option pricing models require the input of highly subjective assumptions including the expected stock price volatility. Any changes in the assumptions can materially affect the fair value estimate.

The fair value of the options at the grant date is estimated using the Black-Scholes option pricing model under the following weighted average assumptions:

	2008
Risk free interest rate	**3.26 %**
Expected volatility	**59.9 %**
Life	**6,8 Years**
Expected dividend yield	**0 %**

The weighted average fair value of options granted is established at $0.71.

Stock options and Warrants varied as follows:

	SEPTEMBER 30, 2008	
	NUMBER	WEIGHTED AVERAGE EXERCISE PRICE
Stock options		
Outstanding at the beginning of nine-month period	**2,494,430**	**$2.18**
Granted	**327,000**	**$1.29**
Exercised	**-**	**-**
Cancelled	**(315,201)**	**$2.54**
	2,506,229	**$2.02**
Warrants		
Outstanding at the beginning of nine-month period	**5,060,000**	**$2.95**
Granted	**-**	**-**
Exercised	**-**	**-**
Expired	**(460,000)**	**$2.50**
	4,600,000	**$3.00**
Oustanding at the end of period	**7,106,229**	**$2.66**
Exercible at the end of the period	**6,607,845**	**$2.70**

HEADQUARTERS
TSO_3 Inc.
2505, avenue Dalton
Québec (Québec)
Canada G1P 3S5

Telephone: 418 651-0003
Fax: 418 653-5726

www.tso3.com
Ticker Symbol: TOS (TSX)

COMMUNICATIONS AND
INVESTOR RELATIONS

Telephone: 418 651-0003, Ext. 237
Fax: 418 653-5726
E-mail: ir@tso3.com