

Court File No. 32-153209

Hemosol Corp.

INTERIM RECEIVER'S FIRST REPORT TO COURT
December 12, 2005

**ONTARIO SUPERIOR COURT OF JUSTICE
(COMMERCIAL LIST)**

IN THE MATTER OF THE BANKRUPTCY AND INSOLVENCY ACT,
R.S.C. 1985, c. B.3, AS AMENDED

AND IN THE MATTER OF THE PROPOSAL OF
HEMOSOL CORP.

**FIRST REPORT TO THE COURT
SUBMITTED BY PRICEWATERHOUSECOOPERS INC.
IN ITS CAPACITY AS INTERIM RECEIVER OF THE ASSETS,
PROPERTY AND UNDERTAKING OF
HEMOSOL CORP. AND HEMOSOL LP**

INTRODUCTION

1. On November 24, 2005, Hemosol Corp. (“Corp”) and Hemosol LP (“LP”) each filed a Notice of Intention to Make a Proposal (“NOI”) pursuant to section 50.4(1) of the *Bankruptcy and Insolvency Act* (“BIA”). PricewaterhouseCoopers Inc. was named as Trustee under the Proposal in each case. Corp and LP will be referred to collectively herein as “Hemosol”.
2. On December 5, 2005, PricewaterhouseCoopers Inc. was appointed as interim receiver (the “Receiver”) of the assets, property and undertaking of Hemosol pursuant to the order of the Honourable Mr. Justice Campbell (the “Receivership Order”) granted pursuant to section 47.1 of the BIA. The Receivership Order, *inter alia*, authorized the borrowing of up to \$2 million by the Receiver and approved a process for the marketing and sale of the business and assets of Hemosol (the “Marketing Process”).

3. The purpose of this, the Interim Receiver's First Report, is to request the approval of this Honourable Court of an extension of the deadline for the filing of a proposal by Corp. In support of this request, the Receiver relies on the First Report of the Receiver filed under Court file number 32-153208, a copy of which is attached hereto as Appendix A.
4. Unless otherwise stated, all monetary amounts contained herein are expressed in Canadian Dollars. Capitalized terms used herein not otherwise defined are as defined in the Receivership Order.

The Receiver respectfully submits to the Court this, its First Report in Court file number 32-153209.

Dated this 12th day of December, 2005.

PricewaterhouseCoopers Inc.
In its capacity as Interim Receiver of
the assets, property and undertaking of
Hemosol Corp. and Hemosol LP



Nigel D. Meakin
Senior Vice President

Appendix A

**First Report of the Interim Receiver
Filed Under Court Number 32-153208**

Court File No. 32-153208

Hemosol LP

INTERIM RECEIVER'S FIRST REPORT TO COURT
December 12, 2005

**ONTARIO SUPERIOR COURT OF JUSTICE
(COMMERCIAL LIST)**

IN THE MATTER OF THE BANKRUPTCY AND INSOLVENCY ACT,
R.S.C. 1985, c. B.3, AS AMENDED

AND IN THE MATTER OF THE PROPOSAL OF
HEMOSOL LP

**FIRST REPORT TO THE COURT
SUBMITTED BY PRICEWATERHOUSECOOPERS INC.
IN ITS CAPACITY AS INTERIM RECEIVER OF THE ASSETS,
PROPERTY AND UNDERTAKING OF
HEMOSOL CORP. AND HEMOSOL LP**

INTRODUCTION

1. On November 24, 2005, Hemosol Corp. (“Corp”) and Hemosol LP (“LP”) each filed a Notice of Intention to Make a Proposal (“NOI”) pursuant to section 50.4(1) of the *Bankruptcy and Insolvency Act* (“BIA”). PricewaterhouseCoopers Inc. was named as Trustee under the Proposal in each case (the “Trustee”). Corp and LP will be referred to collectively herein as “Hemosol”.
2. On December 5, 2005, PricewaterhouseCoopers Inc. was appointed as interim receiver (the “Receiver”) of the assets, property and undertaking of Hemosol pursuant to the order of the Honourable Mr. Justice Campbell (the “Receivership Order”) granted pursuant to section 47.1 of the BIA. The Receivership Order, *inter alia*, authorized the borrowing of up to \$2 million by the Receiver and approved a process for the marketing and sale of the business and assets of Hemosol (the “Marketing Process”).

3. The purpose of this, the Interim Receiver's First Report is to report to the Court on:
 - (i) The impending delisting of the common shares of Corp by NASDAQ;
and
 - (ii) The progress of the Marketing Process;and to request the approval of this Honourable Court of:
 - (iii) an amendment to the Receivership Order in order to provide the Receiver with discretion in respect of the potential listing of Hemosol's real estate property for sale; and
 - (iv) an extension of the deadline for the filing of proposals by Corp and LP.
4. Unless otherwise stated, all monetary amounts contained herein are expressed in Canadian Dollars. Capitalized terms used herein not otherwise defined are as defined in the Receivership Order.

THE DELISTING OF CORP BY NASDAQ

5. Corp is a publicly traded company listed on the Toronto Stock Exchange ("TSX"), trading symbol HML, and on the National Association of Securities Dealers Automated Quotations stock market ("NASDAQ"), trading symbol HMSL.
6. On December 6, 2005, a NASDAQ Staff Determination letter was received stating that:

- (i) Corp was not in compliance with the NASDAQ requirements with respect to governance set forth in NASDAQ Marketplace Rules 4350(c)(1), 4350(c)(3), 4350(c)(4)(A) and 4350(d)(2) as a result of the resignation of Corp's board of directors:
 - (ii) That each of the deficiencies is a separate basis for delisting the common stock;
 - (iii) That the stock would be delisted on December 15, 2005, unless a hearing was requested in accordance with NASDAQ Marketplace Rule 4800; and
 - (iv) That as a result of Corp's insolvency proceedings, the trading symbol for the Corp's common stock was changed from HMSL to HMSLQ effective Thursday, December 8, 2005.
7. A further NASDAQ Staff Determination letter was received on December 8, 2005, stating that for the last thirty consecutive trading days, the common stock had not maintained a minimum market value of US\$5,000,000 and, as a result, Corp was not in compliance with the NASDAQ requirements set forth in NASDAQ Marketplace Rule 4450(a)(2). Corp was provided a period of 90 calendar days to regain compliance.
8. The Receiver has determined that, because of the magnitude of the costs involved in commencing and pursuing an appeal process, it will not request a hearing to appeal the NASDAQ Staff Determination Letters. As a result, the common shares of Corp. will be delisted by NASDAQ on December 15, 2005. The securities may trade on the OTC Bulletin Board provided a market maker makes the necessary application, although there can be no guarantee that trading will be available.

9. The Receiver has been in discussions with representatives of TSX in respect of Corp's TSX listing. TSX has informed the Receiver that it will be maintaining the listing and shares may continue to trade on the TSX.

PROGRESS OF THE MARKETING PROCESS

10. Since the appointment of the Receiver, both Hemosol and the Receiver have received enquiries from several parties expressing interest in the business and assets.

11. Paragraph 30(a) of the Receivership Order states:

“no later than December 9, 2005, the Interim Receiver shall have retained an investment banker or other advisor as shall have been approved by MDS Inc. and Laurus Master Funds, Ltd. (collectively, the “Lenders”) on terms of engagement acceptable to the Lenders to assist in the conduct of the Marketing Process”

12. Prior to the filing of the NOIs, Hemosol had been working with a number of investment bankers and advisors in connection with efforts to raise additional capital. In particular:

- (i) Aethena Global, Inc. ("Aethena") of Northbrook, Illinois in respect of Hemosol's plasma technology; and
- (ii) Nucleus GC (“Nucleus”) of Toronto, in respect of certain of Hemosol's early development stage technology (the “Pipeline”).

13. The Receiver consulted with both Hemosol personnel and the Lenders concerning the engagement of an investment banker in accordance with paragraph 30(a) of the Receivership Order and had concluded that, provided that suitable terms could be agreed, it would be beneficial and appropriate to engage Aethena for the marketing of the plasma and haemoglobin oxygen-carrier technologies.
14. The Receiver had a number of discussions with representatives of Aethena in respect of the Marketing Process and the terms under which Aethena would be prepared to accept an engagement.
15. The discussions left the Receiver with a number of concerns, including:
 - (i) That Aethena appeared to be predisposed to a particular kind of transaction relating to only certain assets, rather than being motivated to explore all potential opportunities and structures;
 - (ii) That compensation structure proposed by Aethena did not appear to the Receiver to provide the appropriate incentive to maximize value; and
 - (iii) That the minimum success fee being demanded by Aethena was believed to be significantly higher than the market practice for an engagement of this kind.
16. The Receiver discussed its concerns with senior personnel from PricewaterhouseCoopers Corporate Finance Inc., (“PwCCF”), the corporate finance practice of PricewaterhouseCoopers. These discussions confirmed the Receiver’s concerns as regards Aethena. PwCCF also confirmed to the Receiver that it would be prepared to undertake the mandate on a basis that would remove such concerns.

17. Pursuant to paragraph 30(a) of the Receivership Order, the Lenders must approve of the investment banker and the terms of its engagement. Accordingly, the Receiver informed the Lenders of its concerns and that the following alternatives were available:
 - (i) Engage Aethena to assist with the Marketing Process on the terms demanded by Aethena;
 - (ii) Engage PwCCF to assist with the Marketing Process on terms consistent with market practices, which would include a compensation structure significantly lower than that being demanded by Aethena; or
 - (iii) Provide the opportunity for others to provide proposals for the mandate, although this would inevitably result in a delay and would require an extension of the Marketing Process, which in turn would result in additional funding being necessary.
18. On December 9, 2005, Laurus Master Funds, Ltd. (“Laurus”) confirmed by e-mail that the terms proposed by Aethena were not acceptable. Further, Laurus advised that the terms proposed by PwCS were acceptable and that Laurus supported the engagement of PwCCF.
19. The Receiver did not receive written confirmation as to what terms were acceptable to MDS Inc. (“MDS”) on or before December 9, 2005, and accordingly, under the terms of paragraph 30(a) of the Receivership Order, the Receiver was unable to retain an investment banker or other advisor by December 9, 2005.
20. On December 11, 2005, MDS confirmed that the terms proposed by Aethena were not acceptable and that MDS supported the engagement of PwCCF.
21. Accordingly, on December 12, 2005, the Receiver engaged PwCCF to assist in the Marketing Process.

22. In addition, the Receiver is continuing its discussions with Nucleus in respect of its possible engagement to assist with the marketing of certain of the Pipeline technology, subject to the approval of terms by the Lenders.

AMENDMENT TO THE RECEIVERSHIP ORDER

23. Paragraph 30 of the Receivership Order states, *inter alia*, that:

“...the Receiver is authorized ***and directed*** to list for sale, or cause the Real Estate Agent to list for sale, no later than January 6, 2006, the land and building owned by Hemosol that form part of the Property (the “Real Property”)...”
{emphasis added}

24. This term was incorporated in the Receivership Order as it was a requirement of the financing to be provided by the Lenders to the Receiver.
25. Since its appointment, the Receiver has further considered this requirement and believes that it is both appropriate and in the best interests of the stakeholders that the Receiver be provided with the discretion to determine, in consultation with the Lenders:
- (i) The optimum strategy for the realization of the Real Property, which may or may not include a listing of the Real Property; and
 - (ii) The optimum date to list the Real Property for sale, if appropriate.
26. The Lenders have each agreed to the Receiver having such discretion, if authorized by the Court.
27. Accordingly, the Receiver respectfully seeks an amendment of the Receivership Order to delete the words “and directed” from the fifth last line of paragraph 30 of the Receivership Order.

EXTENSION OF THE DEADLINE FOR THE FILING OF PROPOSALS

28. Pursuant to section 50.4(8) of the BIA, LP and Corp must each file a proposal with the official receiver within thirty days after the filing of the NOI or they shall be deemed to have made an assignment in bankruptcy.

29. Paragraph 50.4(9) of the BIA states:

“(9) Extension of time for filing proposal – the insolvent person may, before the expiration of the thirty day period mentioned in subsection (8) or any extension thereof granted under this subsection, apply to the court for an extension, or further extension, as the case may be, of that period, and the court may grant such extensions, not exceeding forty-five days for any individual extension and not exceeding in the aggregate five months after the expiration of the thirty day period mentioned in subsection (8), if satisfied on each application that

(a) the insolvent person has acted, and is acting, in good faith and with due diligence;

(b) the insolvent person would likely be able to make a viable proposal if the extension being applied for were granted; and

(c) no creditor would be materially prejudiced if the extension being applied for were granted.”

30. Paragraph 3(t) of the Receivership Order states that the Receiver is empowered and authorized:

“(t) to apply for extensions of the date by which either or both of Hemosol Corp. and Hemosol LP must file a proposal, pursuant to section 50.4(9) of the BIA;”

31. The NOIs were filed on November 24, 2005. Pursuant to the Rules of Civil Procedure, where a deadline falls on a date that is not a business day, it is extended to the next business day. Accordingly, the deadline for the filing of proposals is December 27, 2005 (the "Proposal Deadline"), unless extended.
32. The date for the submission of expressions of interest pursuant to the Marketing Process approved by this Honourable Court is February 3, 2006. Corp and LP will not be able to make viable proposals prior to the completion of the Marketing Process.
33. Pursuant to section 50.4(9) of the BIA, this Honourable Court is authorized to grant a 45-day extension of the Proposal Deadline to February 10, 2006.
34. The Receiver believes that Hemosol has acted and is acting in good faith and with due diligence.
35. While, at this early stage, it is not possible to comment on the likelihood of success of the Marketing Process, the Receiver is hopeful that expressions of interest will be received that could form the basis for the filing of proposals.
36. The Receiver believes that if the Marketing Process is successful and a transaction, or series of transactions, can be consummated at an appropriate value, it is likely that viable proposals could be made.
37. If the extension is not granted, Corp and LP will be deemed to have made an assignment in bankruptcy on December 27, 2005. The Receivership Order authorizes borrowing of up to \$2 million by the Receiver to fund the receivership, including the Marketing Process. There is no guarantee that such funding would be available if Corp and LP are in bankruptcy. Furthermore, the bankruptcy of Corp and LP could have an adverse impact on the Marketing Process.

38. The Receiver believes that the successful conclusion of the Marketing Process is in the best interests of all stakeholders and that no creditor would be materially prejudiced by an extension of the Proposal Deadline to February 10, 2006.
39. Accordingly, the Receiver respectfully seeks an extension of the deadline for the filing of proposals by Corp and LP to February 10, 2006.

The Receiver respectfully submits to the Court this, its First Report.

Dated this 12th day of December, 2005.

PricewaterhouseCoopers Inc.
In its capacity as Interim Receiver of
the assets, property and undertaking of
Hemosol Corp. and Hemosol LP



Nigel D. Meakin
Senior Vice President