

# MANAGEMENT'S DISCUSSION AND ANALYSIS

This Management Discussion and Analysis ("MD&A") should be read in conjunction with the audited consolidated financial statements and related notes for the year ended December 31, 2007 included herein, which have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP") and presented in Canadian dollars. In this MD&A, "IMRIS", the "Company", "we", "our" and "us" are used to refer to IMRIS Inc.

This MD&A contains forward-looking statements about future events or future performance and reflects management's expectations and assumptions regarding our growth, results of operations, performance and business prospects and opportunities. Such forward-looking statements reflect management's current beliefs and are based on information currently available to us. In some cases, forward-looking statements can be identified by terminology such as "may", "would", "could", "will", "should", "expect", "plan", "intend", "anticipate", "believe", "estimate", "predict", "potential", "continue" or the negative of these terms or other similar expressions concerning matters that are not historical facts. In particular, statements regarding our future operating results, economic performance and product development efforts are or involve forward-looking statements.

A number of factors could cause actual events, performance or results, including those in respect of the foregoing items, to differ materially from the events, performance and results discussed in the forward-looking statements. In evaluating these statements, readers should

specifically consider various factors, including the risks outlined under "Risks and Uncertainties" which may cause actual events, performance or results to differ materially from any forward-looking statement. Although the forward-looking statements contained in this MD&A are based on what management considers to be reasonable assumptions, there can be no assurance that actual events, performance or results will be consistent with these forward-looking statements, and management's assumptions may prove to be incorrect. These forward-looking statements are made as of the date of this MD&A and we do not intend, and do not assume any obligation, to update or revise them to reflect new events or circumstances.

Unless otherwise indicated, this MD&A of our financial results for the year ended December 31, 2007 is as at March 7, 2008.

## Overview

IMRIS is a global leader in providing fully integrated surgical imaging solutions designed to measurably improve patient outcomes. The company's flagship product, *IMRISneuro*, is a fully integrated operating room that combines IMRIS' patented magnet mover technology and IMRIS' surgical information management system to provide surgeons with near real-time high resolution MR images during a surgical procedure, enabling them to make better decisions with the ultimate goal of improving patient outcomes.

Surgical imaging is the ability to obtain images of patient anatomy during the course of surgical or

interventional procedures. In the past, surgeons relied on pre-operative images to plan a surgical procedure and post-operative images to confirm whether they had achieved the desired results. More recently, surgical imaging systems have been introduced that provide surgeons with current images of patient anatomy while the surgical procedure is still in progress. Using the information provided by these real-time images, surgeons can make effective adjustments to the surgical procedure while it is in progress, often leading to improved patient outcomes and reducing the likelihood that repeat surgeries will be needed.

The benefits of surgical MR imaging are particularly recognized in the field of neurosurgery. Due to the invasive nature of brain surgery and the importance of minimizing disturbance to healthy brain tissue, neurosurgical procedures particularly benefit from MRI's unique ability to distinguish between diseased and healthy brain tissue.

Our *IMRISneuro* system adopted a novel approach to surgical MR imaging based on three principles; patient safety, surgical efficiency and financial utility. *IMRISneuro* uses our patented technology to move the MRI scanner to the patient, rather than moving the patient to the scanner, while the surgery is in progress. The MRI scanner is moved on an overhead set of rails from an adjacent suite into the operating room and is positioned directly over the patient at the appropriate time during the surgical procedure. The patient therefore does not need to be moved for scanning, reducing the associated risks to the patient while maintaining optimum patient



positioning. At the same time, since the MRI scanner is only present inside the operating room for a few minutes while scanning, the surgical team is afforded unrestricted access to the patient and does not need to use special MR-compatible instruments for the surgery. Finally, when not in use during surgery, the MRI scanner is located in an adjacent room and can be used to provide diagnostic MR imaging, thereby ensuring that the hospital obtains maximum utility from its MRI equipment.

*IMRISneuro* has been validated by leading neurosurgeons around the world for use in world-class neuroscience centers and has become the market leading surgical MR imaging system. Since the delivery of our first commercial system in September 2005, we have won over 90% of the new orders worldwide for high-field surgical MRI systems for which we competed. To date, we have sold sixteen systems, with eight units installed at customer sites: seven in the United States and one in Canada, and an additional eight systems on order and pending installation.

## IMRIS Business Model

The purchase and installation of an *IMRISneuro* system represents a significant capital project for our customers. The price of an integrated *IMRISneuro* system ranges from approximately \$3.5 million to \$7.5 million, depending on the room configuration and the level of integration services. In addition to the purchase of our equipment, our customers may require a further \$1 million to \$3 million or more in additional capital expenditures for room construction and ancillary operating room equipment.

Our sales process requires that we engage with a number of different stakeholders within and outside the hospital including representatives from neurosurgery, radiology, facilities management and administration. As a result, the sales cycle associated with the marketing of our systems is both complex and lengthy, with a typical sales cycle of more than 12 months from initial customer engagement to our receipt of a purchase order. Our sales are typically based on a fixed price with provisions included for additional charges relating to customer requested changes and/or additions.

Following the receipt of a customer purchase order, the delivery and installation cycle for one of our systems typically ranges from five months to eight months or more depending in part on the configuration of our system, but also dependent on the amount of additional construction work that may be required to be completed by the customer. Our delivery cycle includes a phase for initial design and obtaining of permits, structural site construction activities carried out by the hospital and our RF Shielding subcontractor, installation of our overhead rail system, the delivery and installation of the MRI scanner and the remaining system components and final testing and integration of the system.

Given this lengthy delivery cycle, our terms of sale are such that we invoice our customers for the system in installments spread over a number of milestones. These milestones typically include a deposit at the time of order; and a percentage of the total system price upon each of delivery of the equipment, completion of installation and final acceptance. Due to the project nature of our system sales, we recognize revenues and

related cost of sales on a percentage-of-completion basis as the system is installed.

As a result of our short operating history and the limited number of systems sold to date as well as the high dollar value associated with each sale, revenues recorded from quarter to quarter may vary significantly depending on the number and nature of active projects in any given period. We expect that quarter over quarter results in the future may continue to fluctuate for these reasons.

## 2007 Operating Highlights and Outlook

Fiscal 2007 marked a significant period of corporate activity for IMRIS and included the following highlights:

- We installed four *IMRISneuro* systems, doubling the number of systems installed in the field to eight units at the end of the year.
- We received new orders for seven additional systems in 2007, increasing our order backlog from \$19.6 million as at December 2006 to \$31.7 million at the end of the year.
- We received purchase orders from our first two international customers during the year. We received an order from the Reliance Group for the new Kokilaben Dhirubhai Ambani Hospital (KDAH) in Mumbai India and an order from the Peoples Liberation Army (PLA) Hospital in Beijing, China.
- We opened sales offices in Mumbai and in Beijing in conjunction with the receipt of these new orders, providing us with a presence in each of these emerging markets.
- We completed the regulatory approvals for all configurations of *IMRISneuro* in Canada (Health Canada), the United States (FDA), Europe (CE), Australia and other markets.
- We launched the development

of *IMRIScardio*, a surgical imaging system for use in interventional cardiac procedures. We expect to complete the development and obtain regulatory approval to market this product in early 2009.

- We completed our Initial Public Offering in November (the "offering").

These recent developments continue to validate the strength of our core product offering and demonstrate the strong market position we have

developed as a leader in surgical MR imaging for neurosurgical applications. In addition, our ability to apply our core technology to cardiovascular applications reflects the versatility of our core technology and we believe this will open an additional market for our products in future.

In November 2007, our initial public offering raised gross proceeds of \$40 million. The successful completion

of the offering marked the beginning of a new and important phase in our corporate development. The proceeds from the offering are being utilized to fund the sales and marketing plans for the *IMRISneuro* surgical suite for the next two years, to fund the development of new products and applications during this period, and to fund our general corporate and working capital needs.

## SUMMARY OF SELECTED FINANCIAL INFORMATION

The following table sets forth selected financial information for the dates and periods indicated and should be read in conjunction with our audited consolidated financial statements and notes for the year ended December 31, 2007.

Statement of Operations and Balance Sheet (In CDN dollars) (Unaudited)	Year Ended December 31, 2007	Year Ended December 31, 2006	225 day period ended December 31, 2005
Sales	17,445,058	4,304,138	6,394,530
Cost of sales	15,180,438	2,673,942	5,682,139
Gross Profit	2,264,620	1,630,196	712,391
As a percentage of sales	13.0%	37.9%	11.1%
Operating expenses			
Administration	5,300,845	2,893,314	1,205,592
Sales and marketing	3,497,318	2,336,674	1,094,188
Customer support and operations	3,899,824	1,268,260	325,647
Research and development	3,334,511	2,257,691	1,476,250
Amortization	940,632	625,455	105,196
	16,973,130	9,381,394	4,206,873
Loss before the following	(14,708,510)	(7,751,198)	(3,494,482)
Interest income (expense)	222,545	52,590	(48,417)
Amortization of finance costs	-	(141,033)	(12,821)
Foreign exchange (loss) gain	(84,228)	(116,255)	7,965
Net income (loss) for the period	(14,570,193)	(7,955,896)	(3,547,755)
Basic and fully diluted income (loss) per share	(0.75)	(0.64)	(0.42)
<b>Balance Sheet Data</b>			
Cash and cash equivalents	30,803,989	2,912,694	855,190
Total assets	48,649,231	14,616,002	11,739,156
Customer deposits	7,135,834	5,543,665	987,048
Long-term debt	211,593	385,466	429,085
Total liabilities	11,381,390	7,778,181	2,656,377
Shareholders' equity	37,267,841	6,837,821	9,082,779



## Operating Results

### Sales

Sales for the 2007 year were \$17.4 million, an increase of \$13.1 million or 305% over the prior year. The increase in revenues for the 2007 year was attributable to an increase in *IMRISneuro* system installations, with four systems being delivered in 2007 versus one system installation having been completed in the previous year.

Sales for the 2007 year included \$16.9 million of revenues associated with new *IMRISneuro* system deliveries and \$0.5 million of revenues associated with service contracts.

### Gross Profit

The gross profit for the 2007 year was \$2.3 million, an increase of \$0.6 million over the prior period due to the higher system revenues, however the gross profit, as a percentage of sales, decreased from 38% in 2006 to 13% in 2007. This decrease in gross profit percentage was primarily due to discounted prices provided to two strategic customers who have agreed to act as demonstration and visitation sites for prospective customers and include a loss of approximately \$1 million resulting from non-product related costs recorded in the third quarter on the installation of room finishes for one of these customers.

### Operating expenses

Operating expenses for the year were approximately \$17 million, an increase of approximately \$7.6 million or 81% over the previous year. This increase is reflected across all major functional areas of the company including administration, sales and marketing, customer support and operations and research

and development. A substantial amount of the increases in these departmental expenses is attributable to increased staff levels. We have expanded our teams in all functional areas to address the anticipated growth in demand for our products.

At the departmental level, administrative expenses increased by approximately \$2.4 million from \$2.9 million in 2006 to \$5.3 million in 2007. This increase is primarily comprised of increased staff-related expenses of approximately \$1.4 million comprised of increased salary and benefits as well as higher recruiting costs attributable to the higher staffing levels; increased occupancy costs of approximately \$0.4 million relating to the relocation of company operations to a larger facility; increased professional fees of approximately \$0.7 million associated with our ERP implementation and the costs associated with the defense of a lawsuit which was settled in 2007.

Sales and marketing expenses increased by approximately \$1.2 million from \$2.3 million in 2006 to \$3.5 million in 2007. This increase is entirely attributable to the increase in sales staff and the opening of our sales office in China.

Customer support and operations expense increased by approximately \$2.6 million from \$1.3 million in 2006 to \$3.9 million in 2007. A substantial amount of this increase relates to increased staff levels to meet the ramp-up in production and system installations.

Research and development expenses, before deducting related investment tax credits, were approximately \$3.6 million in 2007, an increase of approximately \$0.7 million over the prior year. A substantial amount of this increase relates to

increased staff levels to support the commercialization of the *IMRISneuro* and the early development work on our *IMRIScardio* system. During 2007 we recorded \$0.2 million of research and development tax credits versus \$0.6 million in 2006, reducing our net research and development expenses to \$3.3 million for 2007 as compared to \$2.3 million for 2006.

Amortization expenses increased by approximately \$0.3 million from \$0.6 million in 2006 to \$0.9 million in 2007. The increased amortization expense results primarily from the addition of an *IMRISneuro* test lab and a customer demonstration suite in mid 2006.

### Net loss for the period

Our net loss increased for the year ended December 31, 2007 was \$14.6 million, an increase of \$6.6 million over the prior year. This was mainly due to the ramping up of staff levels and other spending levels in order to position the company to meet the anticipated growth in demand for our products.

## Summary of Quarterly Results

In CDN dollars	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
Unaudited	2006	2006	2006	2006	2007	2007	2007	2007
Sales	208,194	150,852	379,112	3,565,980	3,566,293	2,484,586	7,969,788	3,424,391
Cost of sales	140,607	168,571	279,590	2,085,174	2,637,464	2,318,242	7,267,342	2,957,391
Gross Profit	67,587	(17,719)	99,522	1,480,806	928,829	166,344	702,446	467,000
As a percentage of sales	32.5%	-12.0%	26.3%	41.5%	26.0%	6.7%	8.8%	13.6%
Operating expenses								
Administration	432,969	740,881	630,522	1,088,942	834,894	1,406,200	1,269,774	1,789,977
Sales and marketing	430,404	576,567	558,312	771,391	687,250	1,006,347	735,273	1,068,448
Customer support and operations	191,976	195,225	517,436	363,623	769,203	1,195,937	979,915	954,769
Research and development	368,794	632,806	682,744	573,347	943,983	866,634	697,512	826,381
Amortization	48,456	54,220	69,209	453,570	214,131	232,788	245,132	248,581
	1,472,599	2,199,699	2,458,223	3,250,873	3,449,461	4,707,906	3,927,606	4,888,156
Loss before the following	(1,405,012)	(2,217,418)	(2,358,701)	(1,770,067)	(2,520,632)	(4,541,562)	(3,225,160)	(4,421,156)
Interest income (expense)	(5,766)	11,356	22,191	24,809	5,892	3,830	(11,545)	224,368
Amortization of finance costs	(12,821)	(12,821)	(12,821)	(102,570)	-	-	-	-
Foreign exchange (loss) gain	(13,441)	(162,546)	(20,747)	80,479	1,883	8,900	(222,632)	127,622
Net income (loss) for the period	(1,437,040)	(2,381,429)	(2,370,078)	(1,767,349)	(2,512,857)	(4,528,832)	(3,459,337)	(4,069,166)
Basic and fully diluted earnings (loss) per share	(0.13)	(0.21)	(0.19)	(0.12)	(0.17)	(0.26)	(0.17)	(0.16)

As noted in the IMRIS Business Model section above, as a consequence of the limited number of systems sold to date and the high dollar value associated with each sale, our revenues from quarter to quarter may vary significantly. The revenues for the first three quarters of 2006 were largely related to maintenance services, while in the fourth quarter of 2006 we delivered one new system. During 2007 we installed four systems spread over the year; however deliveries of equipment and related revenue recognition were higher in the third quarter of the year.

Our operating expenses have risen steadily quarter over quarter over the last eight quarters, as we have increased our staff in all functional areas to address the anticipated growth in demand for our products.

In the second quarter of 2007 our operating expenses increased fairly sharply from \$3.4 million in the preceding quarter to \$4.7 million, and then came back down to \$3.9 million in the third quarter of the year. The higher expenses in the second quarter 2007 included higher than usual professional fees including fees associated with our ERP implementation and legal fees associated with the defense of a legal action that has been settled.

### Outlook

Since the formation of the company in May 2005, we have focused our efforts on gaining market acceptance for our products and on ensuring the successful delivery of each customer installation by developing core competencies across all facets

of the organization. Our efforts to date have been rewarded with significant market acceptance for our *IMRISneuro* product suite, which is best reflected in our growing sales results and order backlog. Our solution's key benefits of high resolution MR images, improved patient safety, enhanced surgical efficiency and increased financial viability for our customers' position us well to capitalize on a growing market opportunity for surgical imaging.

Our strategies for near-term growth and value-creation include the continued expansion of our efforts to commercialize our *IMRISneuro* products by increasing our geographic coverage within the U.S.A, Asia and Europe and by developing highly focused marketing



programs that target neurosurgeons and neurosurgical facilities. We also intend to develop our *IMRIScardio* product suite, which we believe will open an entirely new market and

revenue stream for the company. Our longer term objectives include continued innovation and development of high value imaging solutions for specific surgical

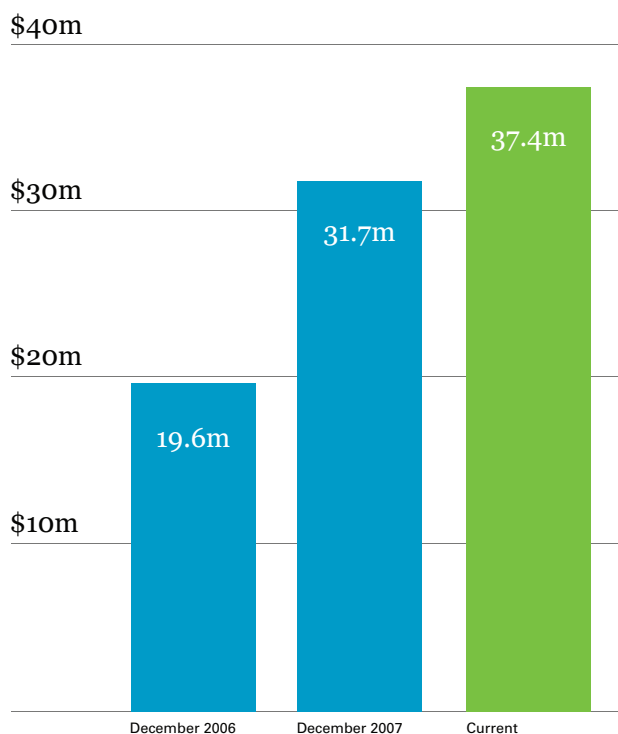
applications, the strengthening of our technology base and competitive barriers, and the growth of recurring revenue sources.

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## Order Backlog

For order book purposes, the order backlog is defined as the unrecognized portion of the revenues to be recorded from confirmed system orders, plus the next twelve months of revenues to be derived from executed service contracts.

During the fourth quarter 2007, we received orders for an additional \$6.8 million increasing our order backlog to \$31.7 million as at December 31, 2007 compared to \$19.6 million as at December 31, 2006. Subsequent to the year-end, we have received an additional purchase order bringing the order backlog as at the date of this MD&A to \$37.4 million. This backlog includes approximately \$1.4 million of unrecognized revenues for two systems which were near completion at the end of the 2007 year and that are expected to be completed early in the first quarter of 2008 as well as orders for eight additional systems.



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## Liquidity and Capital Resources

Our principal capital needs are for funding scientific research and development programs, supporting our sales and marketing activities and funding capital expenditures and working capital. The Company has financed its cash requirements

primarily through issuances of securities, advance deposits from customers associated with new customer orders, and scientific research and development investment tax credits.

We had cash or cash equivalents of \$30.8 million as at December 31, 2007, representing an increase of

approximately \$27.9 million from the balance of \$2.9 million at the beginning of the year. The increase in cash primarily resulted from the recent closing of our initial public offering in November 2007, which provided approximately \$35.9 million in additional share capital (net of related brokerage commissions and expenses).

We believe that the proceeds from the public offering will provide IMRIS with sufficient capital resources over the near-to medium-term to continue our efforts to develop the market for our *IMRISneuro* products, to develop

and launch our *IMRIScardio* products, to build the sales pipeline for our products and to fund our general corporate and working capital needs. The following table sets forth the summary statement of cash flows for

the periods indicated and should be read in conjunction with our audited consolidated financial statements and notes thereto for the year ended December 31, 2007.

### Statement of Cash Flows

(In CDN dollars)

#### Year Ended December 31

	2007	2006	Change
Cash flows:			
From Operating Activities	(15,735,872)	(354,705)	(15,381,167)
From Financing Activities	44,371,181	5,546,542	38,824,639
Used in Investing Activities	(744,014)	(3,134,333)	2,390,319
Net increase (decrease)	27,891,295	2,057,504	25,833,789
Cash and Cash Equivalents, opening	2,912,694	855,190	
Cash and Cash Equivalents, closing	30,803,989	2,912,694	

### Operating Activities

The cash used in operating activities was approximately \$15.7 million for 2007. The cash used in the year was comprised of the operating loss (excluding non-cash related items) for the year of approximately \$13.2 million and a \$2.5 million increase in working capital. The net increase in working capital relates to an increase in accounts receivable of \$4.1 million and increased inventory levels of \$2.1 million due to the higher sales activity. These were partially offset by a \$1.6 million increase in customer deposits for recent order

commitments and a \$2.2 million increase in accounts payable and accrued liabilities.

Company's operating losses and to provide working capital for future requirements.

### Financing Activities

Cash provided from financing activities was approximately \$44.4 million for the year which was primarily comprised of common share issuances of approximately \$8.7 million prior to the November public offering, and approximately \$35.7 million in net proceeds raised under the public offering. Proceeds from share issuances and the public offering have been used to fund the

### Investing Activities

The cash used in investing activities was approximately \$0.7 million for the year representing capital equipment purchases primarily related to additional operations and test equipment, demonstration room equipment and computer hardware and office furnishings for the increased staffing levels.

## Long-term Debt and Contractual Obligations

### Long-Term Debt

	December 31, 2007	December 31, 2006
Long-term debt (current and long term portions)	\$ 211,593	\$ 385,466



The long-term debt is comprised of an initial \$495,000 loan under the NRC Industrial Research Assistance Program ("NRC IRAP") for certain research and development activities.

The loan facility is unsecured, non-interest bearing and repayable quarterly at a rate of 1% of gross revenues for the preceding quarter until repaid. We expect that the entire

outstanding balance of \$211,593 will be repaid in 2008 and have therefore classified it as current.

## Lease Commitments

We have lease commitments in respect of office and manufacturing space as set out below:

	Current Facilities	Previous Facilities	Total
2008	\$ 402,754	\$ 72,224	\$ 474,978
2009	402,754	60,187	462,940
2010	402,754		402,754
2011	428,858		428,858
2012	447,504		447,504

During the 2006 year we moved to a new facility. While we still have lease commitments for our previous facility, we have sublet this space to a third party for terms similar to those in the original lease agreement.

## Outstanding Share Data

The following table sets forth our outstanding share data as at the dates given:

	Authorized	December 31, 2007	December 31, 2006
Common shares	unlimited	\$ 65,985,620 (27,348,013 common shares)	\$ 18,107,332 (14,943,986 common shares)
Preferred shares	unlimited	Nil	Nil
Contributed surplus	-	\$ 576,065	\$ 140,876

As at December 31, 2007 a total of 3,399,300 stock options were outstanding under the Company's stock option plan.

## Financial Instruments

Our financial instruments consist of cash and cash equivalents, short-term investments, accounts and other receivables, accounts payable, accrued liabilities and long-term debt.

We are subject to credit risk with respect to our accounts receivable to the extent debtors do not meet their

obligations and foreign exchange risk with respect to financial instruments denominated in a currency other than the Canadian dollar.

Our short-term investments at December 31, 2007 were \$31.4 million and were invested in short-term commercial paper and treasury bills. Of this total, \$0.5 million was denominated in United States Dollars.

Our accounts receivable at December 31, 2007 were \$4.2 million and were all current (less than 60 days). Of this total, \$1.8 million were denominated in United States Dollars.

## Related Party Transactions

We lease air travel time from 5343381 Manitoba Ltd., a company which is wholly owned by Centara Corporation, a major shareholder of IMRIS. The amount charged to travel expenses with respect to transactions conducted on a cost recovery basis with this related party during the year was \$640,654 versus \$307,314 during the prior year and the amount charged to deferred share issuance costs was \$35,799 versus \$nil in the prior year.

As at December 31, 2007, the balance payable to this related party was \$88,466 versus \$240,000 as at December 31, 2006.

## Critical Accounting Policies and Estimates

The preparation of financial statements in accordance with GAAP requires us 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 year. Among the accounting estimates described in the notes to the financial statements, we consider the accounting estimates used in the determination of recognized revenues, the calculation of investment tax credits receivable, the value of goodwill and the valuation of stock options to be critical. Our results as determined by actual events could differ materially from the previously mentioned estimates.

## Revenue recognition

We recognize revenues for our system sales on a percentage-of-completion basis as the system is installed. The percentage-of-completion is determined by the ratio of actual costs incurred to date to the estimated cost of completion for the project. In the event that the actual costs of completion differ from the estimated cost we have used in determining the percentage-of-completion, recognized revenues may be over or under-estimated until all costs have been incurred and the project is complete. Funds received from our customers in advance of meeting the criteria for recognition of revenues are recorded as customer deposits until the revenue is recognized. Revenues recognized in advance of the criteria for invoicing to our customer are recorded as unbilled receivables. Accordingly, the reported amounts shown on the balance sheet under customer deposits or unbilled receivables may be over or understated.

## Investment tax credits

The Company is entitled to Canadian federal and provincial investment tax credits, which are earned as a percentage of eligible current and capital research and development expenditures incurred in each taxation year. Investment tax credits are recognized when realization of the tax credits is reasonably certain either as an item on the statement of operations or a reduction in deferred development costs depending on where the original costs which give rise to the credits have been recorded. The estimated amounts receivable that we record are subject to audit by the Canada Revenue Agency and therefore the actual amounts received may differ from our estimate.

## Value of goodwill

We recorded goodwill on the purchase of the assets of a predecessor company. The value of goodwill is tested for impairment annually or more frequently if an event or circumstance occurs which we feel may result in an impairment of the value of goodwill.

## Stock based compensation plan

From time to time we issue stock options to employees, directors, officers or consultants. We have adopted the recommendations of Section 3870 of the Canadian Institute of Chartered Accountants' Handbook, "Stock Based Compensation and Other Stock Based Payments". Options granted to employees are valued at the grant date using the Black-Scholes option pricing model which requires management to make assumptions as to volatility, exercise date and vesting. The value of the options is expensed over the estimated life of the option. Options granted to non-employees are valued at the grant date using the Black-Scholes option pricing model. The options are expensed at the time the goods are received or services performed, or over the vesting period.

## Changes in Accounting Policies

As described in Note 2 of the audited consolidated financial statements for the year ended December 31, 2007, the Canadian Institute of Chartered Accountants (CICA) issued Section 3855 Financial Instruments – Recognition and Measurement; Section 3861 Financial Instruments – Disclosure and Presentation; Section 1530 Comprehensive Income; Section 3251 Equity and Section 3865 Hedges. The Company adopted



the new accounting standards as policy effective January 1, 2007. The changes in accounting policy were applied in accordance with transitional provisions contained in each of the applicable sections.

The Financial Instrument standards provide guidance on the recognition, measurement and classification of financial assets and liabilities. These standards also require all derivatives be recognized on the balance sheet at their fair value and specifies how financial instrument gains and losses are to be presented. The Company has identified all financial instruments currently being utilized and disclosed accordingly in Note 2. This classification of certain balance sheet accounts had no impact on the Company's financial statements.

The Comprehensive Income section establishes standards for the presentation and disclosure of items in comprehensive income which will be recorded as a component of shareholders' equity. The Company does not have any items that required separate recognition as other comprehensive income and therefore the adoption of this section had no impact on the Company's financial statements.

The Hedges section establishes new accounting standards on when and how hedge accounting may be applied. The Company currently does not use derivative instruments and therefore the adoption of this section had no impact on the Company's financial statements.

## CEO and CFO Certifications

As a TSX listed company, IMRIS is required to comply with certain disclosure requirements as outlined in Multilateral Instrument 52-109 – Certification of Disclosure in Issuers' Annual and Interim Filings ("MI 52-109"). In accordance with MI 52-109, management advises the following:

### Disclosure Controls and Procedures

Commencing with the filing of our financial statements for the year ended December 31, 2007, our Chief Executive Officer and Chief Financial Officer became responsible for certifying certain matters having to do with the Company's disclosure controls and procedures. Our disclosure controls are those internal systems, controls and procedures that have been established to provide reasonable assurance that the material information used internally and disclosed externally is reliable and timely.

The principal forms of information and means of disclosure in IMRIS which are governed by our disclosure controls and procedures are our continuous disclosure obligations under security regulations, our periodic news releases, our web site and our investor relations materials and presentations. These materials are prepared by senior management, including the Chief Financial Officer. All materials disclosed are reviewed by the Chief Financial Officer and the Chief Executive Officer.

The Chief Executive Officer and the Chief Financial Officer have evaluated the effectiveness of our disclosure controls and procedures as at the December 31, 2007, and have

concluded that the disclosure controls and procedures are effective in that they provide reasonable assurance that material information relating to the issuer, including its consolidated subsidiary, is made known to us.

### Control over Financial Reporting

Management of the Company is responsible for establishing and maintaining adequate internal control over financial reporting. Internal control over financial reporting is a process designed by, or under the supervision of, the Chief Executive Officer (CEO) and the Chief Financial Officer (CFO) (the "Certifying Officers") and effected by the Board of Directors, management and other personnel to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles.

Commencing with the filing of our financial statements for the year ended December 31, 2007, our Chief Executive Officer and Chief Financial Officer of IMRIS also, as a result of the Company's becoming a reporting issuer under securities legislation, became responsible for certifying that they have designed, or have caused to have designed under their supervision, internal controls over financial reporting ("ICFR") to a standard which provides reasonable assurance of the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles.

Commencing with the filing of our financial statements for the year ended December 31, 2007 and as a result of our becoming

a public company, each of the Certifying Officers is also required to certify that they have designed, or have caused to have designed under their supervision, internal controls over financial reporting ("ICFR") to a standard which provides reasonable assurance of the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. As disclosed in the next paragraph, IMRIS is currently in the process of completing its re-assessment of its current ICFR design. Based on the Company's anticipated timing of the completion of this re-assessment, IMRIS applied in November 2007 to the Manitoba Securities Commission (the "MSC"), as lead jurisdiction on behalf of all other Canadian securities commissions, for an exemption from the ICFR certification requirements, in order to permit the Certifying Officers to file a modified form of certificate acknowledging that the Company's design re-assessment was still in progress. In response, IMRIS and the Certifying Officers were advised by the MSC on behalf of the Canadian securities commissions to withdraw the application, deliver the certifications in the required standard form and disclose the status of the ICFR design re-assessment in this MD&A, in accordance with the provisions of Staff Notice 52-316 of the Canadian Securities Administrators ("CSA"). Under Staff Notice 52-316, an ICFR certification must be delivered in the required standard form, but if deficiencies in ICFR exist, such deficiencies are required to be disclosed in the issuer's MD&A. In reliance on this guidance from the MSC, the next two paragraphs contain our disclosures relating to the annual ICFR certification to be delivered by our Certifying Officers.

The Company has implemented and designed an internal control environment and procedures to support the Company's financial reporting requirements. In response to the fact that it is now public, management has also undertaken, a project to challenge the existing design of the Company's ICFR and to prepare additional and/or revised documentation supporting the Company's ICFR. The Company has only been a reporting issuer from the date of our initial public offering in November 2007; accordingly we have not completed this reassessment. Our current assessment of the design of our ICFR has not identified any material weaknesses in ICFR. We expect to fully complete this reassessment prior to reporting our results for the first quarter of 2008. We will report changes in our ICFR each quarter, if any, that have materially affected, or are reasonably likely to materially affect, the Company's ICFR.

Due to its inherent limitations, internal control over financial reporting may not prevent or detect misstatements on a timely basis as such systems can only be designed to provide reasonable as opposed to absolute assurance. Also projections of any evaluation of the effectiveness of internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate. As a result it is possible that there are weaknesses in our internal controls which may be material.

## Risks and Uncertainties

The operating results, business prospects and financial position of the Company are subject to a number of risks and uncertainties. Risks relating to our business include: our long sales cycle, high unit price and limited quarterly installations; our limited operating history and accumulated deficit; our lack of product diversity; our dependence on our suppliers; the development of *IMRIScardio* and industry focus; our reliance on key personnel; the lack of supporting clinical data; market competition and technological advances; patent protection and trade secrets; intellectual property litigation; our shift from research and development to commercialization; our ability to manage growth; foreign exchange fluctuations; additional financing requirements; and regulatory matters. If any of the events described as risks or uncertainties actually occurs, our business, prospects, financial condition and operating results would likely suffer, possibly materially. We have listed several of the more significant risks and uncertainties which may affect the business below, however for a more comprehensive list of the risks and uncertainties affecting the business, readers are advised to refer to our final prospectus filed on October 26, 2007 in connection with the initial public offering or to the Company's Annual Information Form for the year ended December 31, 2007, both of which are available at [www.sedar.com](http://www.sedar.com).

### Long sales cycle, high unit price and limited quarterly installations

The long sales cycle as well as the high unit price of the *IMRISneuro* system, among other factors, may contribute to substantial fluctuations in our quarterly operating results.



Because of the high unit price of the *IMRISneuro* system and the relatively limited number of units installed each quarter, each installation currently represents a significant component of our revenue for a particular quarter. If we lose a single customer order or if customers defer installation of an *IMRISneuro* system for even a short period of time, recognition of a significant amount of revenue may be lost or deferred to a subsequent period. Given our operating costs are relatively fixed, our inability to recognize revenue in a particular quarter may adversely affect our profitability in that quarter.

We expect that revenues from a limited number of new customers will account for a large percentage of total revenues in future quarters. Our ability to attract new customers will depend on a variety of factors, including the capability, safety, efficacy, ease of use, price, quality and reliability of our products and effective sales, support, training and service. In addition, if we are unable to fulfill our current purchase orders and other commitments on a timely basis or at all, market acceptance of our products could be adversely affected and hospitals may instead purchase our competitors' products. The loss or delay of individual orders or failure to add new customers could have a significant impact on future revenues and operating results.

#### **Limited operating history and accumulated deficit**

We began our operations in 2005. Accordingly, we have a limited operating history from which investors can evaluate our business and prospects. We have a large accumulated deficit, we expect future losses, and we may not achieve or maintain profitability. We have incurred substantial losses since

inception and we expect to incur additional operating losses in the near term, primarily as a result of the expansion of our marketing and sales efforts, the research and development costs of our *IMRIScardio* solution and the additional costs of operating as a public company. The extent of our future losses and the timing of profitability are highly uncertain, and we may never achieve profitable operations. If the time required to generate significant revenues and achieve profitability is longer than anticipated, we may not be able to continue our operations. Our prospects must be considered in light of the risks and uncertainties encountered by an early-stage company in the continuously-evolving surgical imaging market. If we cannot successfully address these risks, our business and financial condition would suffer.

#### **Lack of product diversity**

Currently, our only commercially available product is the *IMRISneuro* system. We expect to generate substantially all of our revenue for the foreseeable future from sales of the *IMRISneuro* system and multiyear service plans for the *IMRISneuro* system. If we are unable to sustain or grow sales of the *IMRISneuro* system, we may not generate sufficient revenue to support our business. Accordingly, we are dependent on our ability to market and sell the *IMRISneuro* system. Any factor materially and/or adversely affecting our ability to market and sell the *IMRISneuro* system or pricing and demand for the *IMRISneuro* system may have a material and adverse effect on our financial condition and results of operations.

#### **Development of *IMRIScardio***

We are planning to leverage the *IMRISneuro* technology platform to target a second major application area, interventional cardiovascular procedures. We intend to work with our partner and supplier, Siemens AG, to develop the *IMRIScardio* system, which is aimed initially at the near real-time assessment of cardiovascular interventions. Development of *IMRIScardio* will require integration of our MR imaging system with a fluoroscope, appropriate modifications of our MR compatible surgical table, the development of appropriate surgical coils and other unforeseen adaptations. There is no assurance that we will be able to successfully develop or commercialize the *IMRIScardio* system, or that demand for the *IMRIScardio* system will meet our expectations.

#### **Dependence on suppliers**

The *IMRISneuro* system is designed around the Siemens MRI scanner, with its associated software, diagnostic coils and controls and represents a key component. We currently depend on Siemens to supply the MRI scanner at the core of our *IMRISneuro* system under an OEM re-sale agreement. Our agreement with Siemens was entered into as of November 2005 for a five-year term with automatic renewal annually thereafter, subject to six months advance written notice of termination by either party. The agreement may be terminated earlier in the event of insolvency or equivalent proceedings against either party or in the event of a change of control or similar sale transaction affecting IMRIS where the buyer or controlling shareholder is a direct competitor to Siemens. If for any reason we could not obtain MRI

scanners from Siemens, there is no certainty that we could find another vendor willing to supply an MRI scanner for *IMRISneuro* and a change in the MRI scanner would require a major redesign of the *IMRISneuro* system, which could take a year or more to implement. We are also dependant on Siemens to provide ongoing support and maintenance services to our customers under contract to IMRIS. If Siemens' services became unavailable, any resulting service issues could disrupt our customer relationships and cause damage to our reputation.

We purchase certain other components of our system from outside vendors, including radio-frequency shielding systems, certain hardware components for our surgical information management system and operating room booms and lights. For the majority of our system components, we do not have long-term supply contracts with the suppliers; however, we attempt to establish dual sourcing for most of these other components of our system and we believe that we would be able to establish alternative sources for these components, subject to any regulatory qualifications, as may be required.

It is possible that a disruption of the supply of these components could result in increased costs and delays in deliveries of *IMRISneuro* systems, which could adversely affect our reputation and results of operations. Additionally, any transition to alternate manufacturers or suppliers would likely result in operational problems and increased expenses and could delay the shipment of, or limit our ability to provide our products.

### Competition and technological advances

The surgical imaging industry is subject to intense and increasing competition and rapidly evolving technologies. Many government, academic and business entities are investing substantial resources in research and development of treatments and new products that may render surgical imaging obsolete, including radiation treatment, new drug treatments and gene therapy. Successful developments that result in new approaches for treatments could reduce the attractiveness of our products or render them obsolete. MRI competes with other surgical imaging technologies such as CT,

fluoroscopy and ultrasound for market share in the overall surgical imaging market.

The market for neurosurgical MR imaging is highly competitive, with a number of companies providing competing surgical MRI systems. Many of these competitors are large medical system suppliers which have considerably greater resources at their disposal to advance the development of their MRI systems. These competitors or other companies may at any time develop new or improved surgical imaging solutions. Alternatively, these competitors may choose to increase their respective market share by changing their pricing model or by lowering the price of their surgical imaging solutions or ancillary supplies. If we are unable to address these competitor tactics by either continuing to enhance and improve our current product(s) or we are unable to maintain or increase our selling price in the face of competition, there can be no assurance that the Company will be able to maintain its desired market share or achieve its financial objectives.