

LMS Medical Systems Inc.
2008 Annual Report



Table of Contents

Letter to Shareholders	1
LMS' Management Discussion and Analysis of Financial Condition and Results of Operations	2
Management's Responsibility for Financial Statements	20
Auditors' Report	21
Consolidated Financial Statements and accompanying notes, LMS Medical Systems Inc.	22

Letter to Shareholders

Our goal at LMS is to help reduce risk and achieve better outcomes so that families and their caregivers can enjoy safer deliveries. In 2007, our software solutions watched over approximately 175,000 births in hospital and physician clinic settings, representing growth of 67% over the previous year.

In support of this objective, LMS continued building the fundamentals which represent the cornerstones of the company's future namely: the strength of its products, their acceptance in the marketplace and, ultimately, the trust of its customers. Progress was made on all fronts.

Product Portfolio

LMS brought several flagship products to market: we announced the general availability of the seamless integration of our obstetrical solutions with the clinical platform of McKesson; we released the third application of our Clinical Situational Awareness® tools, CALM Patterns™; we completed major updates to our clinical information system. The delivery of these unique and innovative applications marks the completion of the software development phase in the company's lifecycle.

Market Acceptance

The Company has continued to grow its presence in the market. In the course of the past year, the company doubled the number of customers actively using our software solutions. LMS customers now approach the one hundred mark.

Customer satisfaction is the ultimate measure. Having met the criteria to be included in the early data section of the March 2008 KLAS Labor and Delivery (L&D) Solutions Report read by the healthcare industry, we were pleased to have received the highest performance score among all applications included in the report. It is so very gratifying to know that our customers appreciate the LMS experience, both from the perspective of our offerings and of our support services.

Business Results

Adoption produced positive business results. We increased our revenues by 74% over the previous year. In doing so we continued to grow our partnerships. In parallel, we have significantly reduced expenses and streamlined operations in order to focus on bottom line performance.

Outlook

This coming year will be dominated by a focus on growth. We will continue to strive for excellence with our technology and our people. We will reach out to additional business partners in our quest to highlight patient safety. We will be adding additional resources to our sales and marketing team as we look to double our footprint during the fiscal year. In return, these assets will drive our increasing presence in the marketplace, our revenue and ultimately shareholder value.



Diane Côté
President and Chief Executive Officer

LMS' MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

This management's discussion and analysis ("MD&A") is provided to assist readers in their assessment and understanding of the consolidated results of operations, the financial position and changes in cash flows of LMS Medical Systems Inc. ("LMS" or "the Company") for the three months and year ended March 31, 2008. This MD&A should be read in conjunction with the annual audited consolidated financial statements and the notes to the financial statements of LMS as at March 31, 2008 and for the year then ended, which are prepared in accordance with Canadian generally accepted accounting principles ("GAAP").

Note Regarding Forward-Looking Statements

Our MD&A contains forward-looking statements which reflect our Company's current expectations regarding future events. The forward-looking statements in this annual report, which includes this MD&A, describe our expectations on June 12, 2008. The forward-looking statements are often, but not always, identified by the use of words such as "seek", "anticipate", "plan", "estimate", "expect" and "intend" and statements that an event or result "may", "will", "should", "could" or "might" occur or be achieved and other similar expressions. These forward-looking statements involve risk and uncertainties, including the difficulty in predicting product approvals, acceptance of and demands for new products, the impact of the products and pricing strategies of competitors, delays in developing and launching new products, the regulatory environment, fluctuations in operating results and other risks, any of which could cause actual results, performance, or achievements to differ materially from the results discussed or implied in the forward-looking statements. Many risks are inherent in the industry; others are more specific to our Company. Investors should consult the "Risk Factors" section of the Company's Annual Information Form ("AIF"), as well as our Company's ongoing quarterly filings and annual reports for additional information on risks and uncertainties relating to these forward-looking statements. Investors should not place undue reliance on any forward-looking statements. We assume no obligation to update or alter any forward-looking statements whether as a result of new information, further events or otherwise.

As at June 12, 2008, there were 26,072,310 common shares outstanding, and 2,289,939 options, 371,290 deferred share units ("DSUs") and 2,238,137 warrants outstanding to purchase common shares. These figures exclude shares issuable under non-cash Bonus and Deferred Share Unit plans ("DSU Plan") (note 8 of the consolidated financial statements).

All dollar figures in this MD&A are in Canadian dollars unless otherwise indicated. "We", "us", "our", "the Company", "our Company" or "LMS" means LMS Medical Systems Inc. and our subsidiaries unless otherwise indicated. CALM® is a registered trademark of LMS Medical Systems Inc.

Overview

Since inception, we have been in the business of developing and commercializing a series of leading edge software-based products employed as decision support tools for obstetricians. Our proprietary software tools: CALM Clinical Information System™ ("CIS") and CALM Risk management and clinical decision support tools including: CALM Shoulder Screen™, CALM Curve™ and CALM Patterns™ address the critical unmet medical needs in labour and delivery settings. Based on advanced medical research focusing on the labour & delivery cycle, LMS' unique technology provides obstetrical teams and hospitals with state-of-the-art clinical decision support tools, assisting them in achieving clinical and cost effective interventions, while minimizing risks to the patients. Our core technology, CALM, emanated from research at the McGill University Faculty of Medicine, in Montréal, Québec, Canada, with Dr. Emily Hamilton, our VP Medical Research, as the principal investigator.

With a robust suite of products, in 2008 LMS focused its efforts on the expansion of its sales and distribution network and growth of its revenues. During the past year, LMS has achieved the following significant accomplishments:

Financial and corporate:

- We achieved record revenues of \$4.97 million, an increase of 74% over 2007.
- We increased the value of identified sales opportunities being pursued to \$31 million.
- Our backlog decreased to \$3.9 million in 2008 from \$4.4 million in 2007 due primarily to the recognition in the fourth quarter of fiscal 2008 of \$1.2 million of signed contracts that were previously in the backlog and accounted for as deferred revenue as a result of meeting the revenue recognition criteria.
- Included in total revenues of \$4.97 million for the year ended March 31, 2008 are revenues of a recurring nature totaling \$1.69 million, or 34% of total revenues compared to \$880,000 or 31% of total revenues for the year ended March 31, 2007.
- We completed a private placement generating \$2 million in gross cash proceeds.
- We received a score of 88.8 in the KLAS 2008 Labor and Delivery report, read by the healthcare IT industry. LMS met the criteria to be included in the early data section of the report. The prestigious and independent analysis of healthcare software by KLAS featured an extensive report on Labor and Delivery solutions in March 2008. Key evaluation criteria included the integration with hospital wide information systems, the range of functionality most important to health care providers, and client satisfaction with vendor software offerings and support services.

Product reach and acceptance:

- We significantly increased the number of new client installations, bringing our total client base from 53 in 2007 to 93 in 2008.
- We added new hospitals and insurance contracts to our client base.
- We entered into agreements with several partners, including Best Practices Medical Partners, MD Advantage and Women's Regional Health for the use of CALM Shoulder Screen by their insured OB/GYNs.
- Horizon Perinatal Care™ (“HPC”), the first seamlessly integrated perinatal information system achieved general availability. This system was developed in conjunction with our distributor. HPC is designed to support continuity of care between the labour and delivery department and other hospital departments and units.

Product development:

- CALM Patterns, an innovative risk management software tool specifically directed at the health of the fetus, achieved general availability. Fetal distress during labour is recognized as one of the greatest complexities of childbirth and therefore a significant issue insofar as risk management is concerned. CALM Patterns is a real time proprietary software tool that can, on a heartbeat to heartbeat basis, constantly analyze and present updated information to medical teams to assist in the identification of significant fetal distress.

Strategies for development

A sustained increase in our presence in the North American marketplace is expected to continue. We are focusing on the growth of our installed hospital base of our CIS through internal sales and marketing efforts. We are expanding the pipeline of our sales opportunities, by marketing our decision support tools to the insurance and risk management industry. Our decision support systems are available for distribution, as add-on features, to other parties interested in offering these new tools as part of their client offering within the clinical information systems or as stand alone products. We will focus our efforts on selling and marketing by increasing our sales force and marketing strategies.

Our key objectives for fiscal 2009 are to:

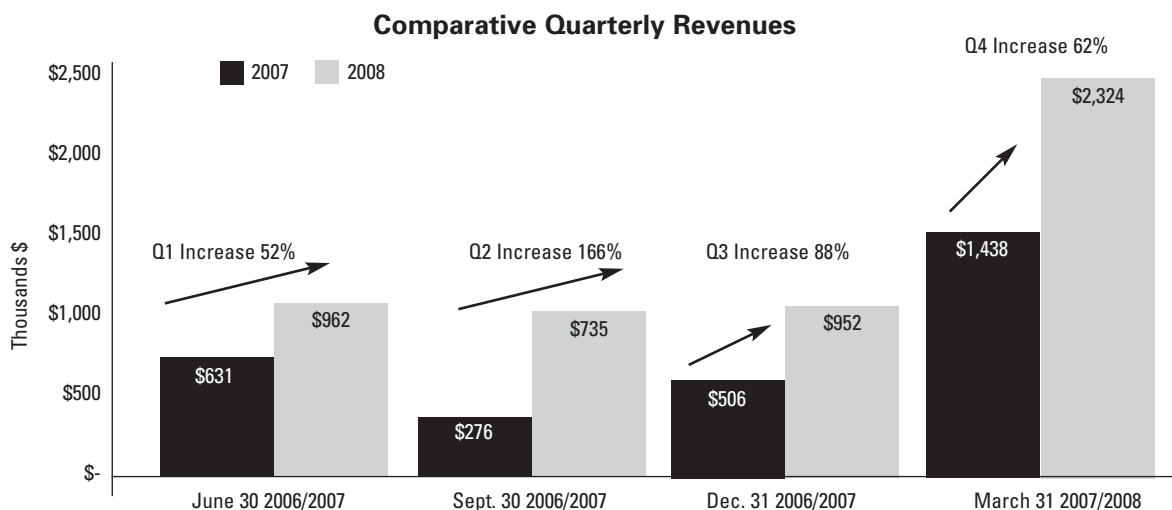
- Expand our revenue by increasing our sales team;
- Generate revenues from the private label OB solutions developed for our distributor;
- Commercialize CALM Patterns in the United States and Canada;
- Continue to dialogue with risk managers and insurance companies to raise their awareness of the role that our decision support tools can play in addressing medical/legal concerns in obstetrics;
- Expand the pipeline of additional business alliances, in order to open new market opportunities and extend the reach of our existing line of software and decision support tools.

Our operating results are primarily a function of the following factors:

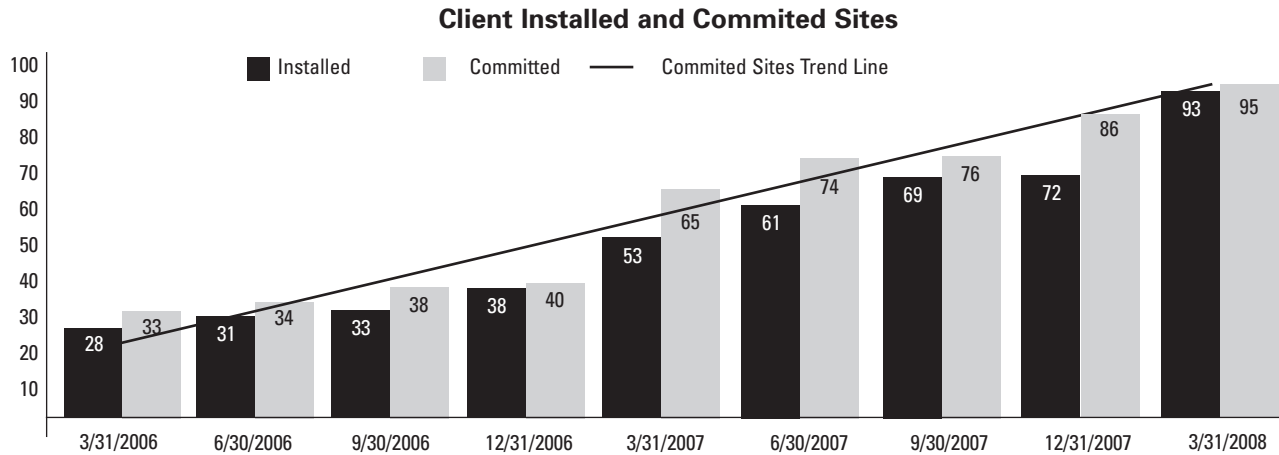
- Customer demand for our products and related revenues;
- Costs associated with sales and marketing efforts; and
- Expenses related to product development, which are driven by the time frame required to complete a project and staffing requirements.

Key Indicators

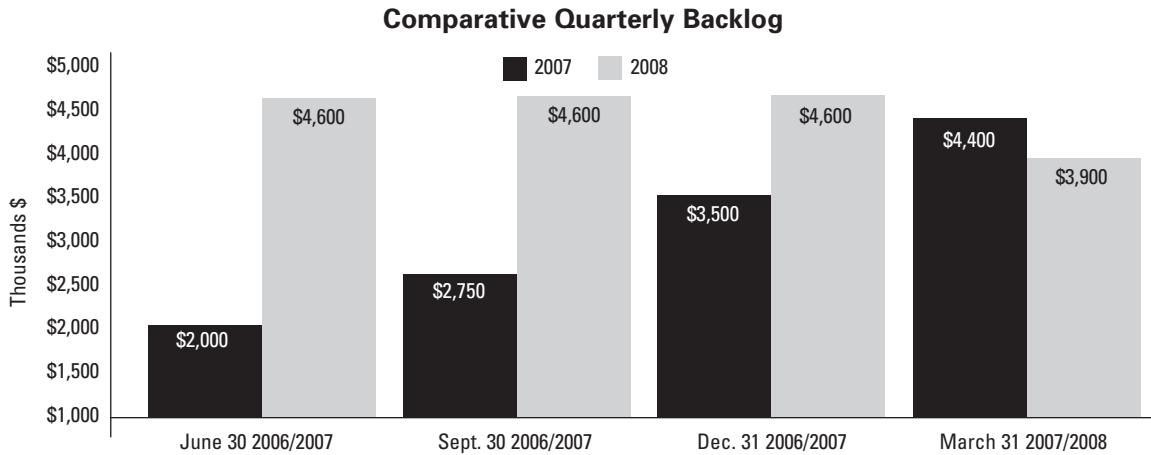
We have provided below, a historical perspective of key performance indicators for LMS. A detailed analysis is presented later in the MD&A.



Revenues in the fourth quarter of fiscal 2008 increased by 62% to \$2,324,000 from \$1,438,000 in the fourth quarter of fiscal 2007. Maintenance and technical revenues continue to grow and increased by 48% to \$1,782,000 for the year ended March 31, 2008 from \$1,204,000 for the year ended March 31, 2007. Revenues for the year ended March 31, 2008 increased by 74% to \$4,973,000 from \$2,851,000 for the year ended March 31, 2007.



Our committed (signed) and installed client base has grown on a consistent basis over the last eight quarters. The table above shows our committed and installed client base at the end of each period, on a cumulative basis. Client sites are defined as customers committed to use or are using one, several or all of our software products.



Our backlog represents signed contracts for the delivery of our software systems and all recurring technical and maintenance revenues. Our backlog also includes all deferred revenues, related to contracts for which not all revenue recognition criteria have been met. The backlog decreased from the end of the third quarter 2008 due to the recognition in the fourth quarter of fiscal 2008 of \$1.2 million of signed contracts that were previously in the backlog and accounted for as deferred revenue as a result of meeting the revenue recognition criteria, offset by additional contracts signed. At the end of the 2008 fiscal year, backlog included primarily signed contracts with respect to maintenance, training and decision support tools that were not completed or installed at the end of the year.

Going Concern

The accompanying MD&A and the audited consolidated financial statements have been prepared on a going concern basis. The going concern basis of presentation assumes that LMS will continue its operations for the foreseeable future and will be able to realize its assets and discharge its liabilities and commitments in the normal course of business.

LMS is a software development company and has not generated profits since its inception. Further, there can be no assurance that LMS will achieve profitability in the future. As at March 31, 2008, the Company had a working capital deficiency. To date, LMS has found its cash requirements primarily from software and technical support revenues, share and warrant issuances, loans payable, convertible debentures and investment tax credits. During the third quarter of fiscal 2008, we implemented a program to streamline operations to reduce operating cash expenses. During the fourth quarter of fiscal 2008, LMS obtained additional financing to fund its operations and sales activities. LMS may still require additional financing to fund its operations and sales activities. In addition, LMS's continuation as a going concern is dependent upon the continuing support of its distributors, customers and shareholders, attaining a satisfactory revenue level, continued sales to its existing customers, the start of profitable operations and the ability to generate sufficient cash from operations. These matters are dependent on a number of items beyond LMS's control and there is uncertainty about LMS's ability to successfully execute its plans. The accompanying MD&A and the audited consolidated financial statements do not reflect any adjustments in the carrying values of the assets and liabilities, the reported revenue and expenses and the balance sheet classifications used that would be necessary if the going concern assumption were not appropriate should LMS not be able to continue its normal course of business.

Selected Financial Information
For the three months and year ended March 31, 2008, 2007 and 2006

	For the three months ended		For the year ended March 31,		
	2008	2007	2008	2007	2006
	\$	\$	\$	\$	\$
Revenue					
Software licenses	1,599,581	898,642	3,190,918	1,586,078	866,718
Hardware	–	61,365	–	61,365	8,579
Technical support and other	724,332	477,722	1,781,931	1,203,822	707,207
Total revenues	2,323,913	1,437,729	4,972,849	2,851,265	1,582,504
Royalties and other direct costs	191,087	242,723	571,763	441,640	243,290
Revenues, net of royalties and other direct costs	2,132,826	1,195,006	4,401,086	2,409,625	1,339,214
Operating Expenses					
Research and development expenses	514,918	1,053,405	2,739,870	4,067,453	3,940,132
Investment tax credits	7,907	(28,986)	(82,093)	(123,986)	(327,227)
Net research and development	522,825	1,024,419	2,657,777	3,943,467	3,612,905
Administrative	735,693	683,132	2,626,984	2,798,352	2,776,919
Selling, marketing and product management	700,552	819,465	2,591,870	3,021,290	2,479,488
Customer support	247,071	224,887	959,068	926,358	952,248
Quality assurance	72,009	50,718	304,864	194,727	215,789
Stock option expense	102,918	135,829	422,369	560,889	735,070
Amortization of fixed assets and patents	61,849	122,843	300,065	380,420	246,947
Government grants	–	–	–	–	(107,787)
Foreign exchange loss (gain)	(2,924)	10,928	(43,948)	15,125	64,050
	2,439,993	3,072,221	9,819,049	11,840,628	10,975,629
Operating loss	(307,167)	(1,877,215)	(5,417,963)	(9,431,003)	(9,636,415)
Net financial expenses (income)	4,188	(17,648)	(28,117)	(118,892)	(230,243)
Net loss	(311,355)	(1,859,567)	(5,389,846)	(9,312,111)	(9,406,172)
Basic and diluted loss per share	(0.01)	(0.09)	(0.24)	(0.50)	(0.57)
Cash flow related to:					
Operating activities - before net changes in non-cash operating working capital	(153,538)	(1,709,270)	(4,182,797)	(7,953,206)	(7,774,816)
Operating activities - after net changes in non-cash operating working capital	(315,856)	(1,794,101)	(3,131,523)	(7,926,879)	(6,009,720)
Investing activities	(5,912)	963,213	(100,511)	(213,066)	8,693,256
Financing activities	1,709,325	2,264,159	1,682,521	6,017,738	(46,323)
Increase (decrease) in cash and cash equivalents	1,387,557	1,433,271	(1,549,513)	(2,122,207)	2,637,213
			March 31, 2008	March 31, 2007	March 31, 2006
			\$	\$	\$
Balance sheet data					
Cash and short term investments (see liquidity section for additional information)			1,859,482	3,383,995	5,481,202
Total assets			3,746,782	5,993,764	7,301,200
Total long-term debt (including current portion)			40,030	71,774	85,816
Total shareholders' equity			279,053	2,593,377	4,794,762

Selected Quarterly Financial Information

	2008				
	Q1	Q2	Q3	Q4	Total
Revenue	962	735	952	2,324	4,973
Operating Loss	2,090	1,755	1,266	307	5,418
Net Loss	2,076	1,741	1,261	312	5,390
Basic and Diluted Net Loss per Share	(0.10)	(0.08)	(0.06)	(0.01)	(0.24)

	2007				
	Q1	Q2	Q3	Q4	Total
Revenue	631	276	506	1,438	2,851
Operating Loss	2,594	2,397	2,563	1,877	9,431
Net Loss	2,550	2,361	2,541	1,860	9,312
Basic and Diluted Net Loss per Share	(0.15)	(0.13)	(0.14)	(0.09)	(0.50)

	2006				
	Q1	Q2	Q3	Q4	Total
Revenue	268	551	502	262	1,583
Operating Loss	2,527	2,184	2,080	2,845	9,636
Net Loss	2,462	2,133	2,017	2,794	9,406
Basic and Diluted Net Loss per Share	(0.15)	(0.13)	(0.12)	(0.17)	(0.57)

Results of operations**For the three-month period ended March 31, 2008 compared to the three-month period ended March 31, 2007****Summary overview for the fourth quarter of fiscal 2008**

Total expenses for the fourth quarter ended March 31, 2008 amounted to \$2,440,000 compared to \$3,072,000 for the fourth quarter ended March 31, 2007, a decrease of \$632,000 or 21%. These expenses include non-cash items of \$841,000 and \$537,000 for the three months ended March 31, 2008 and 2007, respectively. Non-cash items are defined as expenses with no cash outflow and include stock-based compensation, directors' compensation, amortization of fixed assets and patents, bonus expense and for 2008, management's salary plus 25% premium that was part of the streamlining of operations and paid in common shares or DSUs. The total non-cash items include \$706,000 for the three months ended March 31, 2008, which are recorded in current liabilities and are subject to shareholder approval at the 2008 annual shareholder meeting, at which time, these amounts will be transferred to equity. For the three months ended March 31, 2007, the total non-cash items in current liabilities amounted to \$387,000.

The combination of the increase in revenues in the fourth quarter of fiscal 2008 of \$886,000 and lower overall expenses of \$632,000 reduced the comparative operating loss by \$1,570,000 or 84% from \$1,877,000 in the fourth quarter of fiscal 2007 to \$307,000 in the fourth quarter of fiscal 2008. Decreases in research and development ("R&D") expenses of \$502,000 as well as lower selling, marketing and product management expenses of \$119,000 were offset by an increase of \$53,000 in administrative expenses and smaller increases in other expenses. A summary of historical information is presented below. A future anticipated expense summary is presented within the future outlook section of the MD&A.

Revenue

Revenues for the fourth quarter ended March 31, 2008 increased by 62% to \$2,324,000 from \$1,438,000 for the fourth quarter ended March 31, 2007. Software license revenue increased 78% to \$1,600,000 for the fourth quarter of fiscal 2008 from \$899,000 for the same period of fiscal 2007. During the fourth quarter of fiscal 2008, \$1,150,000 of signed contracts that were previously in the backlog and accounted for as deferred revenue were recognized as revenue as a result of meeting the revenue recognition criteria. Revenues from technical support, maintenance and other services were \$724,000 for the fourth quarter of fiscal 2008 compared to \$478,000 in the same period of fiscal 2007.

Royalties and Other Direct Costs

The expense for the three-month period ended March 31, 2008 decreased to \$191,000 compared to \$243,000 for the same period in 2007. In the fourth quarter ended March 31, 2008, we changed our method of installation thereby reducing our direct costs. These expenses include royalties, purchases of hardware and other direct costs related to achieving revenue.

Research and Development expenses

R&D expenses, before investment tax credits, amounted to \$515,000 for the quarter ended March 31, 2008 compared to \$1.05 million for the same period in 2007. Included in R&D expenses are \$115,000 and \$111,000 of non-cash items for the three months ended March 31, 2008 and 2007, respectively. The lower overall spending was primarily due to significant reductions in staffing and in the use

of external consultants, resulting from the completion of certain development projects, as well as a result of the streamlining of operations, implemented in the third quarter of fiscal 2008.

Investment tax credits, which are accounted for as a reduction of R&D expenses, amounted to an expense of \$8,000 for the three months ended March 31, 2008 compared to income of \$29,000 for the same period in 2007. The expense was recorded in the fourth quarter of fiscal 2008 to adjust the investment tax credit receivable balance for the fiscal year.

Administrative

Administrative expenses include compensation for the corporate, financial and administrative management of LMS, board of directors' compensation, audit and legal fees, fees associated with being a publicly listed company, as well as general operating expenses, such as rent and insurance. Administrative expenses for the three-month period ended March 31, 2008 were \$736,000 compared to \$683,000 for the three-month period ended March 31, 2007. Included in administrative expenses are \$376,000 and \$117,000 of non-cash items for the three months ended March 31, 2008 and 2007, respectively. The increase is due primarily to the effects of the streamlining of operations, implemented in the third quarter of fiscal 2008, whereby due to the achievement of milestones during the quarter, five months of salaries for certain members of management plus a 25% premium were accounted for during the fourth quarter of fiscal 2008, resulting in an expense of \$162,000 for the additional two months of salaries, offset by reductions in other administrative expenses totalling \$109,000.

Selling, Marketing and Product Management

Selling, marketing and product management expenses for the fourth quarter of fiscal 2008 were \$701,000 compared to \$819,000 for the same period in fiscal 2007, a decrease of \$119,000. Included in selling, marketing and product management expenses are \$124,000 and \$47,000 of non-cash items for the three months ended March 31, 2008 and 2007, respectively. Spending on selling and marketing expenses decreased as a result of lower marketing activities, reductions in product management staff and traveling expenses, offset slightly by an increase in commissions.

Customer Support

Customer support expenses for the three-month period ended March 31, 2008 were slightly higher at \$247,000 compared to \$225,000 for the same period in fiscal 2007. Included in customer support expenses are \$34,000 and a negligible amount of non-cash items for the three months ended March 31, 2008 and 2007, respectively.

Quality Assurance

Quality assurance expenses for the quarter ended March 31, 2008 were \$72,000 compared to \$51,000 for the same period in 2007. Included in quality assurance expenses are \$27,000 and \$4,000 of non-cash items for the three months ended March 31, 2008 and 2007, respectively.

Stock Option Expense

Stock option expense for the fourth quarter of fiscal 2008 amounted to \$103,000 compared to \$136,000 for the fourth quarter of fiscal 2007. The stock option expense is amortized over three years, resulting in approximately 60%, 30% and 10% of the stock option expense being recorded in the first, second and third year, respectively, from the date of grant.

Foreign Exchange

For the three-month period ended March 31, 2008, LMS incurred a foreign exchange gain of \$3,000 compared to a foreign exchange loss of \$11,000 for the same period in 2007 resulting from the fluctuation of the US dollar against the Canadian dollar.

Operating Loss and Net Loss

After considering the above expenses, our operating loss for the fourth quarter ended March 31, 2008 was \$307,000 compared to \$1.88 million for the same period in 2007.

We generated net interest expense of \$4,000 for the fourth quarter of fiscal 2008 compared to net interest income of \$18,000 in the same period of 2007, due to lower liquidities in 2008.

As a result, our net loss for the fourth quarter ended March 31, 2008 totalled \$311,000 (\$0.01 per share) compared with \$1.86 million (\$0.09 per share) for the same period in 2007.

For the year ended March 31, 2008 compared to the year ended March 31, 2007

Summary

Total expenses for the year ended March 31, 2008 amounted to \$9,819,000, a decrease of \$2,022,000 or 17% compared to the year ended March 31, 2007. These expenses include non-cash items of \$1,940,000 and \$1,818,000 for the years ended March 31, 2008 and 2007, respectively. The total non-cash items include \$706,000 for the year ended March 31, 2008, which are recorded in current liabilities and are subject to shareholder approval at the 2008 annual shareholder meeting, at which time, these amounts will be transferred to equity. For the year ended March 31, 2007, the total non-cash items in current liabilities amounted to \$387,000.

The combination of the increase in revenues in 2008 of \$2,122,000 and lower overall expenses of \$2,022,000 reduced the comparative operating loss by \$4,013,000 from \$9,431,000 in 2007 to \$5,418,000 in 2008. Decreases in R&D expenses of \$1,286,000 as well as lower selling, marketing and product management expenses and administrative expenses of \$601,000 were offset by smaller increases in other expenses. A summary of historical information is presented below. A future anticipated expense summary is presented within the future outlook section of the MD&A.

Revenue

Software license sales doubled to \$3.19 million for 2008 from \$1.59 million in 2007. Software revenues increased as a result of 40 new client installations, compared to 25 in 2007, bringing the current client installed base to 93, compared to 53 in 2007. Hardware revenue was nil in 2008 compared to \$61,000 in 2007. Technical support, maintenance services and consulting revenues increased to \$1.78 million from \$1.20 million in 2007. The increase in technical support revenue is a function of our increasing client installation base.

During the fourth quarter of fiscal 2008, \$1,150,000 of signed contracts that were previously in the backlog and accounted for as deferred revenue were recognized as revenue as a result of meeting the revenue recognition criteria. This, combined with the additional software installations being completed during the year, increased total revenues for the year ended March 31, 2008 by 74% to \$4.97 million from \$2.85 million in 2007.

We record distributor revenues net of distributor royalties. The majority of LMS revenues is generated in US dollars and as such, our revenues have been negatively affected by the continuing depreciation of the US dollar against the Canadian dollar. Approximately 93% (2007 - 85%) of our revenues are generated in the United States ("US"), with a balance generated from Canadian operations, which is a distribution we expect to continue. In addition, 85% (2007 - 73%) of our revenues are generated through a distributor.

Royalties and Other Direct Costs

Royalties and other direct costs totalled \$572,000 in 2008 compared to \$442,000 in 2007. This increase was due to a significantly large number of installations completed during 2008 and their related costs. These expenses include royalties, purchases of hardware and other direct costs related to achieving revenue.

Research and Development

R&D expenses, before investment tax credits, were \$2.74 million compared to \$4.07 million in 2007. Included in R&D expenses are \$255,000 and \$249,000 of non-cash items for the years ended March 31, 2008 and 2007, respectively. The overall expenses for the year decreased significantly as a result of a reduction in headcount of approximately 50%, amounting to a decrease of \$1.2 million in related expenses, offset slightly by an increase of \$80,000 in legal fees incurred for patent protection.

Investment tax credits, which are accounted for as a reduction of R&D expenses, totalled \$82,000 in 2008 compared to \$124,000 in 2007. The reductions are due to a lower number of R&D projects eligible for investment tax credits, given the commercialization of our products. All R&D costs are expensed as incurred for all periods presented.

Administrative

Administrative expenses for the year amounted to \$2.63 million compared to \$2.80 million for 2007. Included in administrative expenses are \$670,000 and \$437,000 of non-cash items for the years ended March 31, 2008 and 2007, respectively. The decrease is due to the streamlining of operations undertaken in the third quarter of fiscal 2008, with savings mainly in professional fees and traveling expenses.

Selling, Marketing and Product Management

Selling, marketing and product management expenses were \$2.59 million in 2008 compared to \$3.02 million in 2007. Included in selling, marketing and product management expenses are \$187,000 and \$110,000 of non-cash items for the years ended March 31, 2008 and 2007, respectively. The decrease is due to reductions in the marketing and product management departments as well as approximately \$100,000 less of traveling expenses incurred during 2008 compared to 2007.

Customer Support

Customer support expenses increased slightly to \$959,000 in 2008 from \$926,000 in 2007. Included in customer support expenses are \$66,000 and \$56,000 of non-cash items for the years ended March 31, 2008 and 2007, respectively.

Quality Assurance

Quality assurance expenses increased to \$305,000 in 2008 from \$195,000 in 2007, as a result of expenses incurred in 2008 for a non-recurring project related to software implementation. Included in quality assurance expenses are \$40,000 and \$25,000 of non-cash items for the years ended March 31, 2008 and 2007, respectively.

Stock option expense

We recorded \$422,000 in stock option expense in 2008 compared to \$561,000 in 2007. The fair value of the options granted in prior years was higher, resulting in a higher annual expense in those years. The stock option expense is amortized over three years, resulting in approximately 60%, 30% and 10% of the stock option expense being recorded in the first, second and third year, respectively, from the date of grant. The overall balance remaining to be amortized over the vesting period has now diminished.

Foreign Exchange

In 2008, we incurred a foreign exchange gain of \$44,000 compared to a loss of \$15,000 in 2007.

Operating Loss and Net Loss

After considering the above expenses, our operating loss for 2008 was \$5.42 million compared to \$9.43 million in 2007.

Net financial income totalled \$28,000 in 2008 compared to \$119,000 in 2007. The financial income represents primarily interest on excess cash balances, less interest relating to our long-term lease obligations.

As a result, the net loss for 2008 was \$5.39 million (\$0.24 per share) compared to \$9.31 million (\$0.50 per share) for 2007.

For the year ended March 31, 2007 compared to the year ended March 31, 2006

Summary

Our net loss for the year 2007 decreased to \$9.31 million from \$9.41 million in 2006. Increases in revenues of \$1.26 million were offset by higher direct costs, royalties, sales and marketing expenses of \$740,000. Increases in other expenses and a reduction in investment tax credits of \$203,000 accounted for the balance of the change.

Revenue

Our revenue for 2007 increased 80% to \$2.85 million from \$1.58 million in 2006. Software license sales increased to \$1.59 million from \$867,000 in 2006. Hardware revenue was \$61,000 compared to \$9,000 in 2006. Technical support, maintenance services and consulting revenues increased to \$1.20 million from \$707,000 in 2006.

Software revenues increased as a result of 25 new client installations, compared to 9 in 2006, bringing the current client installed base to 53, compared to 29 in 2006. The increase in technical support revenue is a function of our increasing client install base. With our core expertise in the clinical and labour management of obstetrical hospital systems, we are also expanding our services and consulting offerings, having realized \$100,000 of revenues from these sources in 2007. We record distributor revenues net of distributor royalties. Approximately 85% (2006 - 89%) of our revenues are generated in the United States, with a balance generated from Canadian operations, which is a distribution we expect to continue. In addition, 73% (2006 - 55%) of our revenues are generated through a distributor.

Royalties and Other Direct Costs

Royalties and other direct costs totalled \$442,000 in 2007 compared to \$243,000 in 2006. This increase was due to a greater number of installations completed during 2007 and related costs. These expenses include royalties, purchases of hardware and other direct costs related to achieving revenue.

Research and Development

R&D expenses, before investment tax credits, were \$4.07 million compared to \$3.94 million in 2006. The overall expenses for the year increased slightly as a result of higher non-cash bonus of \$98,000 and other items.

Investment tax credits, which are accounted for as a reduction of R&D expenses, totalled \$124,000 in 2007 compared to \$327,000 in 2006. Fiscal 2006 included \$67,000 related to excess investment tax credits received over the estimates for prior periods, with the remaining decrease explained by the lower amounts of R&D projects that are eligible for investment tax credits, as our products are commercialized. All R&D costs are expensed as incurred for all periods presented.

Administrative

Administrative expenses include compensation for the corporate, financial and administrative management of LMS, director compensation, general operating expenses, rent, insurance, audit and legal fees, as well as expenses directly related to being a publicly listed company. Overall administrative expenses were in line with prior year at \$2.80 million for 2007 compared to \$2.78 million in 2006.

Selling, Marketing and Product Management

As a result of increased sales activity, selling, marketing and product management expenses were \$3.02 million in 2007 compared to \$2.48 million in 2006. These increases were due to new employees in product and clinical management and increased expenses supporting these activities as well as increased commissions. Product management and clinical specialists focus on current and future product and service integration. Sales travel and other expenses increased somewhat, as they related to increased sales activities. Marketing expenses increased in 2007 as a result of new product introductions and related activities.

Customer Support

Expenses for this department were in line with the prior year at \$926,000 in 2007 compared to \$952,000 in 2006.

Quality Assurance

Expenses for this department decreased slightly to \$195,000 in 2007 from \$216,000, as a result of fewer regulatory activities in 2007.

Stock option expense

We accounted for \$561,000 in stock option expense in 2007 compared to \$735,000 in 2006. The fair value of the options granted in 2005 and 2006, was greater than in 2007, resulting in a higher annual expense in those years. The stock option expense is amortized over three years, resulting in approximately 60%, 30% and 10% of the stock option expense being recorded in the first, second and third year, respectively, from the date of grant. The overall balance remaining to be amortized over the vesting period has now diminished, and based on grants made to date, LMS will be recognizing \$247,000 in total or \$200,000 in 2008, \$42,000 in 2009 and the balance thereafter.

Government Grants

In 2006, we recorded \$108,000 related to a government grant which was received during the period, compared to nil in 2007.

Foreign Exchange

In 2006, we incurred a foreign exchange loss of \$64,000 compared to a loss of \$15,000 in 2007. This is due to the negative impact of the continued weakness of the US dollar compared to the Canadian dollar, our reporting currency.

Operating Loss and Net Loss

After considering the above expenses, our operating loss for 2007 was \$9.43 million compared to \$9.64 million in 2006.

Net financial income totalled \$119,000 in 2007 compared to \$230,000 for 2006. The financial income represents primarily interest on excess cash balances, less interest relating to our long-term lease obligations.

As a result, net loss for 2007 was \$9.31 million (\$0.50 per share) compared to \$9.41 million (\$0.57 per share) for 2006.

Cash flows**Summary of operating position**

	For the three months ended		For the year ended March 31,		
	March 31,		March 31,		
	2008	2007	2008	2007	2006
	\$	\$	\$	\$	\$
Cash flows related to operating activities					
Operating before net change in non-cash items	(153,538)	(1,709,270)	(4,182,797)	(7,953,206)	(7,774,816)
Net changes in non-cash operating working capital items	(162,318)	(84,831)	1,051,274	26,327	1,765,096
Cash flows related to operating activities	(315,856)	(1,794,101)	(3,131,523)	(7,926,879)	(6,009,720)

For the three-months ended March 31, 2008 compared to three-months ended March 31, 2007

Cash flows used in operations for the three-month period ended March 31, 2008 totaled \$316,000 compared to \$1.79 million used for the same period in fiscal 2007. The overall operating loss in the fourth quarter 2008 was \$1.57 million lower than in the fourth quarter 2007, and accounted primarily for the decrease of cash flows used in operations.

Cash flows related to investing activities were minimal at \$6,000 for the three months ended March 31, 2008, compared to \$963,000 for the same period in 2007. The difference relates mainly to the maturity of short-term investments of \$1.0 million in 2007. The cash flows used in the three month period ended March 31, 2008 relates to \$6,000 (2007 - \$56,000) of additions to fixed assets and patents.

Cash flows related to financing activities for the three months ended March 31, 2008 were an inflow of \$1.71 million compared to \$2.26 million in 2007. Private placements during the fourth quarters of fiscal 2008 and 2007, which generated net cash proceeds of \$1.74 million and \$2.27 million, respectively, were offset by payments on long-term lease obligations.

For the year ended March 31, 2008 compared to the year ended March 31, 2007

Cash flows used in operations totaled \$3.13 million in 2008 compared to \$7.93 million in 2007. The cash flow used in operations before non-cash working capital assets was \$4.18 million in 2008 and \$7.95 million in 2007. The majority of the variation in the non-cash items is explained by the collection of receivables and prepaid expenses in 2008 of \$502,000 (primarily trade accounts receivable) compared to a use of cash in 2007 of \$819,000, primarily from the increase in year-end receivables related to increased revenues. Payables related to the Bonus and DSU plans amounted to \$706,000, and are expected to be settled in shares or DSUs, but have been recorded as a current liability until required shareholder approval is obtained (see note 8 of the consolidated financial statements). Deferred revenues increased by \$153,000 whereas accounts payable and accrued liabilities decreased \$310,000 year over year.

Cash flows used in investing activities totaled \$101,000 in 2008 compared to of \$213,000 in 2007, related to additions to fixed assets and patents.

During 2008, we generated \$1.68 million (2007 - \$6.02 million) from financing activities. In 2008, we completed a private equity financing raising net proceeds of \$1.74 million (2007 - \$6.06 million). In 2008, we repaid \$36,000 in obligations due under capital lease obligations, compared to \$42,000 in 2007.

For the year ended March 31, 2007 compared to the year ended March 31, 2006

Cash flows used in operations totaled \$7.93 million in 2007 compared to \$6.01 million in 2006. The cash flow used in operations before non-cash working capital assets was comparable at \$7.95 million in 2007 and \$7.77 million in 2006. The majority of the variation in the non-cash items is explained by the collection of receivables and prepaid expenses in 2006 of \$1.32 million (primarily investment tax credits) compared to a use of cash in 2007 of \$819,000, primarily from the increase in year end receivables related to increased revenues. Liability related working capital balances were comparable, except for the \$387,000 increase in 2007 payables related to the Bonus and Deferred Share Unit plans, which are expected to be settled in shares, but have been recorded as accounts payable until required shareholder approvals are obtained (see note 8 of the consolidated financial statements).

Cash flows used in investing activities totaled \$213,000 in 2007 compared to an inflow of \$8.69 million in 2006. The difference relates mainly to the maturity in 2006 of short-term investments of \$8.96 million. The remainder of the cash flows used in the period relates to \$213,000, (2006 - \$220,000) of additions to capital assets and patents.

During 2007, we generated \$6.02 million from financing activities compared to the \$46,000 used in 2006. In 2007, we completed private equity financings raising net proceeds of \$6.06 million. In 2007, we repaid \$42,000 in obligations due under capital lease obligations, compared to \$46,000 in 2006.

Future outlook

Management is concentrating its efforts primarily on revenue ramp up, servicing of our growing customer base, cash flow break even and profitability.

We anticipate that the revenue growth will continue due to following factors:

- Expansion of our sales team anticipated in 2009.
- Our growing presence in the marketplace is the result of sales efforts with several hospital groups, the continued success of which should drive further additional revenue opportunities.
- Increases in revenues related to the CALM Clinical Information System and our risk management tools.
- Commercial release of interoperability components for a private branded product.
- As a result of increased system sales and our growing client base, revenues from maintenance and technical support service agreements are also expected to increase commensurate with the growth of our installed base.
- Additional revenues are expected from the commercial release of CALM Patterns this year.
- New products and business alliances are being pursued to develop additional market opportunities, thereby extending the reach of our existing line of software and risk management tools.

Expense Outlook Summary

In the third quarter of fiscal 2008, we streamlined operations. This plan will lead to lower expenditures in all areas, particularly in R&D activities and general and administrative expenses, with the exception of selling, marketing and product management.

Having recently brought to market key software deliverables, we are focusing on growing market presence and product acceptance. Sales, service training and software support for our distributors and healthcare industry clients become the priority. Shifting from software development to commercialization allows for reductions in development expenses and outside consultants.

Research and Development

We expect these expenditures to decrease by approximately \$500,000 for fiscal 2009 due to an anticipated static headcount.

Administrative

We expect these expenses to remain constant over the coming quarters.

Selling, Marketing and Product Management

We expect these expenditures to increase significantly by approximately \$800,000 to \$900,000 as a result of anticipated hires in the sales and marketing teams and marketing activities.

Customer Support

The streamlining of operations did not affect customer support and we expect these expenditures to remain at similar levels over the coming quarters.

Quality Assurance

We expect these expenditures to decrease during fiscal 2009, as a result of certain staffing and non essential expenditure reductions and reach \$50,000 for the upcoming fiscal year.

Liquidity and capital resources

Based on the current operating plan, we believe we will have sufficient resources to fund operations for the next twelve months.

To date, we have financed our operations, technology development, patent filings and capital expenditures primarily through the issuance of shares and convertible notes by way of private placements, by the receipt of investment tax credits earned on eligible expenditures, by loans and promissory notes from financial institutions and by capital leases. Since our inception, we have raised gross proceeds in excess of \$57 million from equity-based financings.

In light of the inherent uncertainties associated with our ability to secure sales, to invest in new projects, to expand and accelerate our product sales in the US and in other markets and to enter into additional business relationships, further financing was obtained during the fourth quarter of fiscal 2008 to support our operations in the future. Funding requirements may vary depending on a number of factors including our success in growing revenues, profits, cash flow break even and progress of our research and development program, the establishment of collaborations, the development of the international sector, and penetration rates in North America.

When additional funds are required, potential sources of financing include strategic relationships and public or private sales of our Common Shares. We do not have any committed sources of financing at this time and it is uncertain whether additional funding will be available when the need arises on terms that will be acceptable to us. If funds are raised by issuing additional Common Shares, or other securities convertible into our Common Shares, the ownership interests of our existing shareholders will be diluted. If we are unable to obtain financing when required, we will not be able to carry out our business plan, including marketing and distribution initiatives. We would have to significantly limit our operations and business, and our financial condition and results of operations would be materially harmed.

We may require additional financing to expand our operations and intend to raise funds from time to time. Funding requirements may vary depending on a number of factors, including the progress of our research and development program, the establishment of collaborations and the market acceptance of our products in North America and internationally.

From time to time, we may invest cash in liquid high-grade investment securities of Canadian Chartered banks or Canadian Government T-bills, with varying terms to maturity, taking into account operating, capital and cash-flow requirements. Any deviations from these types of investments need to be specifically authorized by the Board of Directors of LMS. LMS does not have any investments in asset backed commercial paper.

Under our contract with a distributor, we are entitled to receive amounts for contracts contained in our backlog. As at March 31, 2008, this amount, which does not qualify as a receivable under GAAP, amounted to \$646,000, representing additional future liquidity for LMS, as the deferred revenue liability related to this item is a non-cash item, which will be settled by delivery of our software products and services, in the normal course of operations.

Long-term debt and other cash obligations

As at March 31, 2008 we had no debt other than obligations under capital leases, which totalled \$44,000 and are repayable over the next 5 years.

Our other operating obligations originate from our operating leases. Our total contractual cash obligations are as follows:

	2009	2010	2011	2012	2013	Total
Capital Leases	39,000	5,000	–	–	–	44,000
Operating Leases	130,000	11,000	8,000	5,000	5,000	159,000
Total	169,000	16,000	8,000	5,000	5,000	203,000

Under a lease agreement, for our premises, ended February 2008, we were required to issue a letter of credit secured by an investment of an equivalent amount. The letter of credit was reimbursed in February 2008 upon termination of the lease and equalled \$25,000 at March 31, 2007. In addition, under an agreement with a bank, a \$50,000 investment is held as a security.

We lease approximately 9,300 square feet of office space in Montréal, Québec, Canada. In the fourth quarter of fiscal 2008, we renewed our lease for a term of seven months, commencing on March 1, 2008 and terminating on September 30, 2008. We are currently in discussions with our landlord to extend the lease further.

Other agreements

Prior to 2006, we entered into a license agreement with a third party in connection with databases to be used within our software products. The license agreement is renewable every year and provides non-transferable, non exclusive licenses and is subject to royalties on revenues of the third party derived from the product.

Distribution agreements

We are seeking to establish our proprietary software as the standard of practice in the industry. We intend to do this through the marketing efforts of our sales staff in Canada and the US. In addition, we intend to enter into distribution and marketing arrangements with third party distributors and marketers in new markets.

We are focusing on the growth of our installed hospital base for our CIS through internal sales and marketing efforts. We are expanding the pipeline of our sales opportunities by marketing our decision support tools and CIS to the insurance and risk management industry and different channels of distribution.

Our decision support systems are available for distribution, as add-on features, to other parties interested in offering these new tools as part of their client offering within their clinical information systems or as stand alone products.

Shareholders' Equity

As at March 31, 2008, the total Capital Stock of the Company was \$57.27 million compared to \$54.71 million in 2007. In fiscal 2008, Capital Stock increased \$2.56 million as a result of a private placement financing and \$760,000 in shares issued under the non-cash bonus plan. Contributed Surplus increased as a result of the expiry of warrants of \$41,000 (with a corresponding decrease in warrants balance) and an amount of \$422,000 related to stock based compensation that was recorded in the consolidated statement of operations. We also recorded non-cash expenses of \$215,000 related to the director's DSU plan and \$380,000 related to the share bonus plan (see note 8 of the consolidated financial statements), which have been included as an expenses in the statement of operations.

Bonus plan

In fiscal 2005, we established a bonus plan (the "Bonus Plan") that provides for annual awards to eligible executives and employees based on achievement of corporate and individual performance objectives. The award is paid in common shares and DSUs, the number of which is based upon dividing the total award by the five day average year-end closing market price of the common shares on the Toronto Stock Exchange ("TSX"). At the 2005 annual and special meeting of shareholders, the Bonus Plan was approved. At the 2006 annual general meeting, the maximum number of shares issuable under this plan was increased from 250,000 to 500,000. At the 2007 annual shareholder meeting, LMS shareholders approved the increase of the number of shares issuable under the Bonus Plan from 500,000 to 1,300,000.

For the year ended March 31, 2008, 562,438 (\$760,040) of the reserved shares were issued. 4,789 common shares issued and reserved, relating to employees who left since March 31, 2007, were cancelled and a balance of \$5,699 was applied against contributed surplus.

For the year ended March 31, 2008, LMS recorded bonus expense of \$380,000 for the 2008 fiscal year, expected to be paid in common shares or DSUs. As at March 31, 2008, shares reserved, available and unissued and approved by the shareholders under the Bonus Plan were 272,374 whereas the required number of shares to settle the 2008 bonus was 633,333. As a result of this shortfall, only a portion of the \$380,000, or \$163,424, representing 272,374 common shares was recorded within the shareholders' equity section as accruals for bonus expected to be paid by issuing common shares. The remaining balance due of \$216,576 was recorded as a current liability on the balance sheet. However, it will be proposed at the 2008 annual shareholder meeting to increase the number of shares available under the Plan, and if approved, this amount will be reversed and recognized in shareholders' equity upon issuance of 122,858 common shares totaling \$73,715 and 238,101 DSUs totaling \$142,861 by LMS. Should approval not be obtained, this amount will be paid out in cash.

As at March 31, 2008, LMS recorded \$129,762, representing 216,270 common shares, within the shareholders' equity section as accruals for bonus expected to be paid in common shares, for settlement of the suspended salaries of management, plus a 25% premium.

For the year ended March 31, 2007, LMS recorded total bonus expense related to the Bonus Plan in the amount of \$675,000. As at March 31, 2007, shares reserved, available and unissued and approved by the shareholders under the Bonus Plan were 250,510 whereas the required number of shares to settle the 2007 bonus is 567,227. As a result of this shortfall, only a portion of the \$675,000, or \$297,000, representing 249,580 common shares was recorded within the shareholders' equity section as accruals for bonus expected to be paid by issuing common shares. The remaining balance of \$378,000 was recorded as a current liability on the balance sheet.

At the August 2007 annual shareholder meeting, LMS shareholders approved the increase of the number of shares issuable under the Bonus Plan at which time the accrued balances were transferred to shareholders' equity. The difference of \$79,941 relating to the difference between the accrued as at March 31, 2007 and amount paid, by issuing shares, for the year ended March 31, 2007, was recorded as an adjustment of bonus expense in 2008. The difference arose from the increase in the share price between March 31, 2007 and August 9, 2007, the date of the approval of the plan change.

Deferred Share Unit Plan

In fiscal 2005, we established a DSU Plan that provides for the payment of director's quarterly compensation with DSUs. Each DSU is a right granted by LMS to an eligible director to receive one common share upon termination of service. The number of DSUs to be granted under the DSU Plan is determined by dividing the quarterly director compensation by the five day average quarter end closing market price of the common shares on the TSX. At the 2005 annual and special meeting of shareholders, the DSU Plan was approved. At the 2006 annual general meeting, the maximum number of DSUs issuable under this Plan was increased from 125,000 to 250,000. At the 2007 annual general meeting, the maximum number of DSUs issuable under this Plan was increased from 250,000 to 400,000. We have the option to remit either cash or common shares to settle the DSUs. Details related to the expenses recorded under the non-cash DSU for 2008, 2007 and 2006 are disclosed in the note 8 (v) of the consolidated financial statements.

Stock exchange listing requirements

As at March 31, 2008, LMS was listed on the TSX and the American Stock Exchange ("AMEX"). During 2007, LMS did not meet certain AMEX minimum listing requirements relating to its shareholders' equity and was notified by AMEX of this default. In May 2008, the Company's Board of Directors approved the voluntary delisting from the AMEX as part of management's plan to reduce costs. The delisting was completed on May 22, 2008. On June 5, 2008, LMS filed Form 15F with the US Securities and Exchange Commission to voluntarily terminate the registration of its common shares under section 12(g) of the US Securities Exchange Act of 1934, as amended. LMS continues to meet the TSX listing requirements.

Related party transactions

We enter into transactions in the normal course of business with a related company. These transactions are measured at the exchange amount. The related party transactions are for management fees and the expense amounted to \$216,342, \$192,300 and \$191,532 for the years ended March 31, 2008, 2007 and 2006, respectively. Balances due in connection with these transactions amount to \$104,167 as at March 31, 2008 and \$32,050 as at March 31, 2007.

Dividends

We do not anticipate paying dividends in the next fiscal year.

Critical Accounting Policies and Estimates

Our consolidated financial statements have been prepared in accordance with GAAP. The preparation of financial statements by management in accordance with GAAP requires the selection of accounting policies from existing acceptable alternatives. Our critical accounting policies and estimates include the following:

Revenue recognition

Revenue consists primarily of revenue from the sales of software licenses, hardware and technical support services. LMS recognizes revenue in accordance with the provision of the American Institute of Certified Public Accountants Statement of Position ("SOP") No. 97-2, Software Revenue Recognition.

We recognize revenue from software licenses and hardware when persuasive evidence of an arrangement exists, delivery, installation and client's acceptance have occurred, the sales price is fixed or determinable, and collection is probable.

Revenue from technical support services, which is generally paid in advance, is deferred and recognized ratably over the period for which the technical support service is provided. Other service and consulting revenues are recognized as services are provided.

Revenue on arrangements that includes multiple elements such as hardware, software licenses and technical support services is allocated to each element based on vendor specific objective evidence ("VSOE") of the fair value of each element. Allocated revenue for each element is recognized when revenue recognition criteria have been met for each element. VSOE is determined based on the price charged when each element is sold separately. If VSOE cannot be determined, and all other revenue recognition criteria have been met, revenues from multiple element managements are recognized ratably over the period for which the technical support service is provided. When VSOE of fair value of undelivered services is established subsequent to the outset of the arrangement, the deferred revenue relating to the arrangement is adjusted to the newly established VSOE or fair value of the undelivered services.

Research and development expenses and Investment Tax Credits

Research expenses are charged against income in the year of expenditure. Development expenses are charged against income in the period of expenditure unless a development project meets the criteria under GAAP for deferral and amortization.

Amounts received or receivable resulting from government assistance programs, including grants and investment tax credits for R&D, are reflected as reductions of the cost of assets or expenses to which they relate at the time eligible expenses are incurred, provided that there is reasonable assurance that the benefits will be realized. The risks of change to estimates for investment tax credits receivable relate to the acceptance of LMS R&D investment tax claims by government authorities. The claims, which contain several R&D projects, are made on an annual basis and may take in excess of one year to be finalized and completed. In reviewing the claim, the government authorities take into consideration two primary factors in assessing the eligibility of the investment tax credit claim: (1) the technical aspects of the projects claimed must meet the specific scientific criteria and (2) the claim must contain only the eligible expenses related to projects described in the tax filings. The risk of change to the estimate relates to the fact that certain projects or expenses involve judgment and could be disallowed because of one or both of the factors identified above are not met. Any favourable or unfavourable adjustment that may result following assessment by government authorities is recorded to income in the subsequent period when such assessment is performed.

As at March 31, 2008, our investment tax credit receivables recorded amount to \$84,000 relating to our current year claim. To date, substantially all of our investment tax credits claimed filed and assessed by the government authorities have been accepted favourably as submitted.

Stock-based compensation plan

As a result of amendments made in October 2003 to the provisions of the Canadian Institute of Chartered Accountants (“CICA”) Handbook Section 3870, effective November 1, 2003, we changed our method of accounting for employee stock-based compensation and decided to adopt the fair value based method of accounting for all our stock-based compensation. We adopted these changes using the prospective application transitional alternative in accordance with the transitional provisions of CICA Handbook Section 3870. Accordingly, the fair value based method is applied to awards granted, modified or settled on or after November 1, 2003. Prior to the adoption of the fair value based method, LMS, as permitted by Section 3870, had chosen to continue the existing policy of recording no compensation cost on the grant of stock options to employees.

When stock options are exercised, capital stock is credited by the consideration paid together with the related portion previously credited to contributed surplus when compensation costs were charged against income. The prospective method omits the effects of awards granted, modified or settled before November 1, 2003.

We provide pro forma disclosure of the compensation costs based on the fair value method for awards granted prior to November 1, 2003 under the employee stock option plan (see note 8(iii) of the consolidated financial statements).

Stock-based compensation expense and pro forma disclosure of the stock-based compensation expense for all options granted under our stock option plans, as well as Deferred Share Units and warrants, is determined using the fair value method computed with the Black-Scholes option pricing model. The related expense is recognized over the vesting period of such options, allowing for forfeitures, estimated by management.

Income taxes

LMS follows the liability method of accounting for income taxes. Under this method, future income tax assets and liabilities are determined based on the differences between the financial reporting and tax bases of assets and liabilities and are measured using substantively enacted tax rates and laws that are expected to be in effect in the periods in which the assets or liabilities are expected to be realized or settled. Changes in these balances are included in net earnings of the period in which they arise.

Impairment of long-lived assets

When events or changes in circumstances indicate the carrying amount of a long-lived asset or group of assets held for use, including capital assets and patents, may not be recoverable, an impairment loss is recognized when the carrying amount of those assets exceeds the sum of the undiscounted future cash flows related to them. The impairment loss is included in the statement of operations and the carrying value of the asset or group of assets is reduced to its fair value as determined by the sum of the discounted future cash flows related to those assets. The impairment loss is presented within the amortization expense of the related assets.

Changes in accounting policies

The CICA issued Handbook Section 1530, “Comprehensive Income,” which establishes standards for reporting and display of comprehensive income; Section 3855, “Financial Instruments - Recognition and Measurement,” which establishes standards for the recognition and measurement of all financial instruments, provides a characteristic-based definition of a derivative instrument, provides criteria to be used to determine when a financial instrument should be recognized, and provides criteria to be used to determine when a financial liability is considered to be extinguished; and Section 3865, “Hedges,” which establishes standards of

when and how hedge accounting may be applied. Hedge accounting is optional. The new standards are applicable for years beginning on or after October 1, 2006, and accordingly, LMS adopted them in the first quarter of 2008. The adoption of these new provisions did not have a significant impact on LMS' consolidated financial statements. Expanded disclosures regarding the application of the aforementioned pronouncements are made in note 2 of the consolidated financial statements.

Effective April 1, 2007, LMS adopted the new recommendations of the CICA Handbook Section 1506, "Accounting Changes." Under these new recommendations, voluntary changes in accounting policy are permitted only when they result in the financial statements providing reliable and/or relevant information. These recommendations also require changes in accounting policy to be applied retrospectively unless doing so is impracticable, require prior period errors to be corrected retrospectively, require enhanced disclosures about the effects of changes in accounting policies, estimates and errors on the financial statements, and require the disclosure of new primary sources of GAAP that have been issued but not yet effective. The adoption of this Section did not have a significant impact for the year ended March 31, 2008.

New Accounting Pronouncements

Capital Disclosures

CICA Handbook Section 1535, "Capital Disclosures," requires disclosure of an entity's objectives, policies and processes for managing capital, quantitative data about what the entity regards as capital and whether the entity has complied with any capital requirements and, if it has not complied, the consequences of such non-compliance. This standard is effective for interim and annual financial statements relating to fiscal years beginning on or after October 1, 2007, specifically April 1, 2008 for LMS. LMS will disclose this information in its consolidated financial statements for the first quarter of fiscal 2009.

Financial Instruments Disclosures

CICA Handbook Section 3862, "Financial Instruments - Disclosures," increases the disclosures currently required that will enable users to evaluate the significance of financial instruments for an entity's financial position and performance, including disclosures about fair value. In addition, disclosure is required of qualitative and quantitative information about liquidity risk and market risk. The quantitative disclosures must also include a sensitivity analysis for each type of market risk to which an entity is exposed, showing how net income and other comprehensive income would have been affected by reasonable possible changes in the relevant risk variable. This standard is effective for interim and annual financial statements relating to fiscal years beginning on or after October 1, 2007, specifically April 1, 2008 for LMS. LMS will disclose additional information in its consolidated financial statements for the first quarter of fiscal 2009.

Financial Instruments Presentation

CICA Handbook Section 3863, "Financial Instruments - Presentation," replaces the existing requirements on presentation of financial instruments which have been carried forward unchanged to this new Section. This standard is effective for interim and annual financial statements relating to fiscal years beginning on or after October 1, 2007, specifically April 1, 2008 for LMS and is not expected to have an impact on the consolidated financial statements.

General Standards on Financial Statement Presentation

CICA Handbook Section 1400, "General Standards on Financial Statement Presentation," has been amended to include requirements to assess and disclose an entity's ability to continue as a going concern. The changes are effective for LMS for interim and annual financial statements beginning on or after January 1, 2008, specifically April 1, 2008 for LMS and is not expected to have an impact on the current going concern note disclosure.

Goodwill and Intangible Assets

CICA Handbook Section 3064, "Goodwill and Intangible Assets," replaces Section 3062, "Goodwill and Other Intangible Assets," and Section 3450, "Research and Development Costs." It establishes financial reporting for goodwill, start up costs and other intangible assets. This standard is effective for interim and annual financial statements beginning on or after April 1, 2009. LMS is currently assessing the impact of adoption of this standard on the consolidated financial statements.

International Financial Reporting Standards

The Accounting Standards Board has a strategic plan for financial reporting in Canada whereby Canadian GAAP will converge with International Financial Reporting Standards ("IFRS") over the period ending March 31, 2011. After this transitional period, the Company will cease to use Canadian GAAP and will adopt IFRS. The Company is monitoring this transition to IFRS and is analyzing the impact that the adoption of IFRS will have on the audited consolidated financial statements.

Evaluation of disclosure controls and procedures

As of March 31, 2008, an evaluation of the effectiveness of the issuer's disclosure controls and procedures (as such term is defined under the rules adopted by the Canadian securities regulatory authorities) was carried out by management, under the supervision of, and with the participation of, the Company's Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO"). Based upon that evaluation, the CEO and CFO concluded that as of such date, LMS's disclosure controls and procedures were effective such that information relating to LMS required to be disclosed by us in the reports which we file or submit to such regulatory authorities (a) is recorded, processed, summarized and reported within the time periods specified under applicable securities laws, and (b) is accumulated and communicated to our management, including our CEO and CFO, to allow timely decisions regarding disclosure.

Internal controls over financial reporting

During the 2008 fiscal year, LMS documented and assessed the design of internal controls over financial reporting. The design of internal controls over financial reporting was evaluated and defined in Multilateral Instrument 52-109. Based on the results of this evaluation, the CEO and CFO attested that the internal controls over financial reporting are designed to provide reasonable assurance that its financial reporting is reliable and that LMS's consolidated financial statements were prepared in accordance with Canadian GAAP.

Management also concluded that during the year ended March 31, 2008, no changes were made to internal controls over financial reporting that would have materially affected, or would be reasonably considered to materially affect those controls.

Off-balance sheet arrangements

We do not have any off-balance sheet arrangements at March 31, 2008.

Foreign operations and foreign currency transactions

A large portion of our revenues and some of our expenses are generated in the US. From April 1, 2004 to March 31, 2008, the Canadian dollar has appreciated against the US dollar by approximately 13%. The continued weakness of the US dollar has a negative effect on our revenues, offset somewhat by the expenses generated in the US.

Risk factors

For a more detailed discussion of risk factors that could materially affect our results of operations and financial condition, please refer to our AIF.

Other MD&A requirements

All relevant information related to our Company is filed, in Canada, electronically at www.sedar.com.

Consolidated Financial Statements

LMS Medical Systems Inc.

As at March 31, 2008 and March 31, 2007 and for the years ended March 31, 2008, 2007 and 2006

Management's Responsibility for Financial Statements

We are responsible for the preparation and integrity of the LMS consolidated financial statements and all other financial information contained in the Annual Report. These consolidated financial statements have been prepared in accordance with accounting principles generally accepted in Canada and necessarily include some amounts that are based on our best estimates and judgement. We consider that the consolidated financial statements present fairly in all material respects the financial position of LMS, the results of its operations and cash flows. Financial information contained elsewhere in this Annual Report is consistent with the information contained in the financial statements.

To fulfill our responsibility, we have developed and maintain internal accounting controls and established policies and procedures designed to ensure the reliability of financial information and safeguarding of assets. The internal control systems and financial records are subject to review by the external auditors during the examination of the consolidated financial statements.

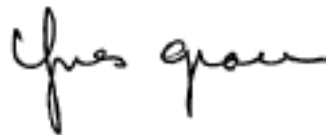
The Board of Directors oversees our performance over financial reporting and internal controls. The Board of Directors carries out its responsibility with regard to the consolidated financial statements through the Audit Committee.

The Audit Committee, which is composed exclusively of outside directors, meets regularly with the external auditors, and with management, to discuss accounting policies and practices, internal control systems, the scope of audit work and to assess reports on audit work performed. The external auditors have free and direct access to the Audit Committee, with or without the presence of management, to discuss results of their audits and any recommendations that they have for improvements in internal controls, the quality of financial reporting and any other matters of interest. Our consolidated financial statements have been reviewed and approved by the Board of Directors on the recommendation of the Audit Committee.

June 12, 2008



Diane Côté
President and Chief Executive Officer



Yves Grou, CA
Chief Financial Officer

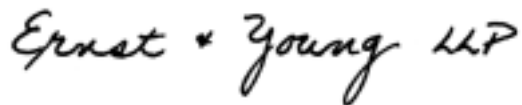
AUDITORS' REPORT

To the Shareholders of LMS Medical Systems Inc.

We have audited the consolidated balance sheets of **LMS Medical Systems Inc.** (the "Company") as at March 31, 2008 and 2007 and the consolidated statements of operations, deficit and cash flows for each of the years in the three-year period ended March 31, 2008. These financial statements are the responsibility of LMS Medical Systems Inc.'s management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of LMS Medical Systems Inc. as at March 31, 2008 and 2007 and the results of its operations and its cash flows for each of the years in the three-year period ended March 31, 2008 in accordance with Canadian generally accepted accounting principles.



Chartered Accountants
Montréal, Canada
May 16, 2008

Consolidated Financial Statements
LMS Medical Systems Inc.

Incorporated under the Canada Business Corporations Act

CONSOLIDATED BALANCE SHEETS

(See Note 1 - Description of Business, Going Concern and Basis of Presentation)

<i>As at March 31 (In Canadian dollars)</i>	2008	2007
	\$	\$
ASSETS		
Current assets		
Cash and cash equivalents (<i>note 8 (i)</i>)	1,809,482	3,358,995
Short-term investments	50,000	25,000
Accounts receivable (<i>notes 3, 12</i>)	1,106,864	1,567,463
Investment tax credits receivable (<i>note 13</i>)	84,000	124,000
Prepaid expenses	104,271	106,042
Total current assets	3,154,617	5,181,500
Investments - restricted (<i>note 9 (iv)</i>)	50,000	75,000
Fixed assets (<i>notes 4, 7</i>)	230,664	500,308
Patents (<i>note 5</i>)	311,501	236,956
Total assets	3,746,782	5,993,764
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities		
Accounts payable and accrued liabilities (<i>notes 6, 10, 12</i>)	1,042,110	1,351,635
Leasehold inducements (<i>note 9 (i)</i>)	-	62,818
Amounts due under the bonus and deferred share unit plans (<i>notes 8 (iv), (v)</i>)	705,635	387,000
Current portion of deferred revenues and deposits from distributors (<i>note 9 (iii)</i>)	1,650,825	1,168,238
Current portion of obligations under capital leases (<i>note 7</i>)	35,336	35,186
Total current liabilities	3,433,906	3,004,877
Deferred revenues and deposits from distributors (<i>note 9 (iii)</i>)	29,129	358,922
Obligations under capital leases (<i>note 7</i>)	4,694	36,588
Total long-term liabilities	3,467,729	3,400,387
Shareholders' equity		
Capital stock (<i>note 8 (i)</i>)	57,271,326	54,706,512
Warrants (<i>notes 8 (i), (ii)</i>)	679,328	411,333
Contributed surplus (<i>notes 8 (ii), (iii)</i>)	3,187,050	2,729,235
Accruals for expected bonus to be paid in Common Shares (<i>note 8 (iv)</i>)	293,186	297,000
Deferred share units (<i>note 8 (v)</i>)	538,948	419,816
Deficit	(61,690,785)	(55,970,519)
Total shareholders' equity	279,053	2,593,377
Total liabilities and shareholders' equity	3,746,782	5,993,764

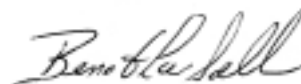
Commitments and contingencies (*note 9*)

The accompanying notes are an integral part of these consolidated financial statements.

On behalf of the Board:



Diane Côté
Director



Benoit La Salle
Director

Consolidated Financial Statements
LMS Medical Systems Inc.

Incorporated under the Canada Business Corporations Act

CONSOLIDATED STATEMENTS OF OPERATIONS

Years ended March 31,
(In Canadian dollars)

	2008	2007	2006
	\$	\$	\$
Revenue			
Software licenses (note 12)	3,190,918	1,586,078	866,718
Hardware	–	61,365	8,579
Technical support services, consulting and other (note 12)	1,781,931	1,203,822	707,207
Total revenues	4,972,849	2,851,265	1,582,504
Royalties and other direct costs	571,763	441,640	243,290
Revenues, net of royalties and other direct costs	4,401,086	2,409,625	1,339,214
Operating expenses			
Research and development expenses	2,739,870	4,067,453	3,940,132
Investment tax credits (note 13)	(82,093)	(123,986)	(327,227)
Net research and development expenses	2,657,777	3,943,467	3,612,905
Administrative (note 10)	2,626,984	2,798,352	2,776,919
Selling, marketing and product management	2,591,870	3,021,290	2,479,488
Customer support	959,068	926,358	952,248
Quality assurance	304,864	194,727	215,789
Stock option expense (notes 8 (iii))	422,369	560,889	735,070
Amortization of fixed assets	274,099	360,033	231,224
Amortization of patents	25,966	20,387	15,723
Government grant	–	–	(107,787)
Foreign exchange loss (gain)	(43,948)	15,125	64,050
Total operating expenses	9,819,049	11,840,628	10,975,629
Operating loss	(5,417,963)	(9,431,003)	(9,636,415)
Interest on long-term debt	19,796	9,218	9,121
Interest revenue and other income	(47,913)	(128,110)	(239,364)
Net loss and comprehensive loss	(5,389,846)	(9,312,111)	(9,406,172)
Basic and diluted loss per share	(0.24)	(0.50)	(0.57)
Weighted average number of common shares			
- basic and diluted	22,229,790	18,558,265	16,530,831

The accompanying notes are an integral part of these consolidated financial statements.

Consolidated Financial Statements**LMS Medical Systems Inc.**

Incorporated under the Canada Business Corporations Act

CONSOLIDATED STATEMENTS OF DEFICIT

Years ended March 31,
(In Canadian dollars)

	2008	2007	2006
	\$	\$	\$
Deficit, beginning of year	(55,970,519)	(45,971,000)	(36,564,828)
Net loss	(5,389,846)	(9,312,111)	(9,406,172)
Shares and warrant issue costs <i>(note 8(i))</i>	(330,420)	(687,408)	–
Deficit, end of year	(61,690,785)	(55,970,519)	(45,971,000)

The accompanying notes are an integral part of these consolidated financial statements.

Consolidated Financial Statements
LMS Medical Systems Inc.

Incorporated under the Canada Business Corporations Act

CONSOLIDATED STATEMENTS OF CASH FLOWS

Years ended March 31,
(In Canadian dollars)

	2008 \$	2007 \$	2006 \$
OPERATING ACTIVITIES			
Net loss	(5,389,846)	(9,312,111)	(9,406,172)
Adjustments for non-cash items:			
Amortization expense	300,065	380,420	246,947
Amortization of leasehold inducements	(62,818)	(72,295)	–
Stock based compensation (note 11)	934,753	1,050,780	1,384,409
Consulting expense (note 8 (i))	35,049	–	–
	(4,182,797)	(7,953,206)	(7,774,816)
Net changes in non-cash operating working capital items (note 11)	1,051,274	26,327	1,765,096
Cash flows related to operating activities	(3,131,523)	(7,926,879)	(6,009,720)
INVESTING ACTIVITIES			
Purchase of investments - restricted (note 9 (iv))	–	(75,000)	(50,000)
Maturity of investments - restricted (note 9 (iv))	25,000	100,000	–
Purchase of short-term investments	(25,000)	(2,050,153)	–
Maturity of short-term investments	–	2,025,153	8,963,583
Additions to fixed assets	–	(146,895)	(123,719)
Additions to patents	(100,511)	(66,171)	(96,608)
Cash flows related to investing activities	(100,511)	(213,066)	8,693,256
FINANCING ACTIVITIES			
Repayment of long-term debt, obligations under capital lease (notes 4, 7)	(36,199)	(42,208)	(46,323)
Issuance of capital stock	1,740,000	6,556,623	–
Issuance of warrants	260,000	122,525	–
Shares and warrant issue costs	(281,280)	(619,202)	–
Cash flows related to financing activities	1,682,521	6,017,738	(46,323)
Net change in cash and cash equivalents	(1,549,513)	(2,122,207)	2,637,213
Cash and cash equivalents, beginning of year	3,358,995	5,481,202	2,843,989
Cash and cash equivalents, end of year	1,809,482	3,358,995	5,481,202
Supplementary information			
Interest paid	16,928	9,218	9,121
Investment tax credits received	122,093	259,986	1,250,115

The accompanying notes are an integral part of these consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2008 (In Canadian dollars)

1. DESCRIPTION OF BUSINESS, GOING CONCERN AND BASIS OF PRESENTATION**Description of business**

LMS Medical Systems Inc. ("LMS" or the "Company") is incorporated under the *Canada Business Corporations Act*. Since inception, LMS has been actively developing and commercializing a series of leading edge software-based products to be used as decision support tools for obstetricians. LMS's pipeline of proprietary software tools addresses critical unmet medical needs in labour and delivery settings. While continuing to pursue its core research and development of new software tools, LMS has also been strengthening its product development as well as the implementation and enlargement of its sales and distribution network.

Going Concern and Basis of Presentation

The accompanying audited consolidated financial statements have been prepared on a going concern basis. The going concern basis of presentation assumes that LMS will continue operations for the foreseeable future and will be able to realize its assets and discharge its liabilities and commitments in the normal course of business.

LMS is a software development company and has not generated profits since inception. Further, there can be no assurance that LMS will achieve profitability in the future. As at March 31, 2008, the Company had a working capital deficiency. To date, LMS has financed its cash requirements primarily from software and technical support revenues, share and warrant issuances, loans payable, convertible debentures and investment tax credits. During the third quarter of fiscal 2008, LMS implemented a program to streamline operations and reduce operating cash expenses. During the fourth quarter of fiscal 2008, LMS obtained additional financing to help fund its operations and sales activities (note 8(i)). LMS may still however require additional financing to fund its operations and sales activities. In addition, LMS's continuation as a going concern is dependent upon the continuing support of its distributors, customers and shareholders, attaining a satisfactory revenue level, continued sales to its existing customers, the start of profitable operations and the ability to generate sufficient cash from operations. These matters are dependent on a number of items beyond LMS's control and there is uncertainty about LMS's ability to successfully execute its plans. These consolidated financial statements do not reflect any adjustments in the carrying values of the assets and liabilities, the reported revenue and expenses and the balance sheet classifications used that would be necessary if the going concern assumption were not appropriate should LMS not be able to continue its normal course of business.

2. SIGNIFICANT ACCOUNTING POLICIES

These consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP"). The preparation of financial statements by management in accordance with GAAP requires the selection of accounting policies from existing acceptable alternatives. The significant accounting policies used in their preparation are as follows:

Use of estimates

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at year-end and the reported amounts of revenues and expenses during the period. Actual results may vary, and such differences may be material.

Consolidated financial statements

These consolidated financial statements include the accounts of LMS and its wholly-owned subsidiaries, LMS Medical Systems Ltd. and LMS Medical Systems (USA) Inc. All significant intercompany balances and transactions have been eliminated on consolidation.

Cash and cash equivalents

Cash and cash equivalents are classified as held-for-trading and are valued at their fair market value. Cash and cash equivalents consist of cash on hand, bank balances and cash equivalents with an initial maturity date of less than three months.

Short-term investments

Short-term investments are classified as assets held-to-maturity and are recorded initially at their fair values. After their initial fair value measurement, they are measured at amortized cost using the effective interest rate method. Short-term investments consist of commercial paper.

2. SIGNIFICANT ACCOUNTING POLICIES (Cont'd)

Allowance for doubtful accounts

The Company establishes an allowance for doubtful accounts sufficient to cover probable and reasonably estimated losses. The Company establishes its estimates based on the aging of the accounts receivable balances and historical write-off experience, net of recoveries. If collections are lower, actual write-offs may be greater than initially expected.

Investments - restricted

Cash and short-term investments that are subject to restrictions that prevent its use for current purposes are presented as investments - restricted within the long-term assets section. After their initial fair value measurement, they are measured at amortized cost using the effective interest rate method.

Research and development expenses and investment tax credits

Research expenses are charged against income in the year of expenditure. Development expenses are charged against income in the year of expenditure unless a development project meets the criteria under GAAP for deferral and amortization.

Amounts received or receivable resulting from government assistance programs, including grants and investment tax credits for research and development ("R&D"), are reflected as reductions of the cost of assets or expenses to which they relate at the time eligible expenses are incurred, provided that there is reasonable assurance that the benefits will be realized. The risks of change to estimates for investment tax credits receivable relate to the acceptance of LMS R&D investment tax claims by government authorities. The claims, which contain several R&D projects, are made on an annual basis and may take in excess of one year to be finalized and completed. In reviewing the claim, the government authorities take into consideration two primary factors in assessing the eligibility of the investment tax credit claim: (1) the technical aspects of the projects claimed must meet the specific scientific criteria; and (2) the claim must contain only the eligible expenses related to projects described in the tax filings. The risk of change to the estimate relates to the fact that certain projects or expenses involve judgment and could be disallowed because of one or both of the factors identified above are not met. Any favourable or unfavourable adjustment that may result following assessment by government authorities is recorded to income in the subsequent period when such assessment is performed.

Fixed assets

Fixed assets are recorded at cost and are amortized over their estimated useful lives using the following methods and rates:

	Methods	Rates
Computer hardware	Declining balance	30%
Computer software	Straight-line	2 years
Furniture and fixtures	Declining balance	20%
Office equipment	Declining balance	20%
Leasehold improvements	Straight-line	Over the term of the lease
Computer hardware under capital lease	Straight-line	3 years
Office equipment under capital lease	Straight-line	3 years

Patents

Costs related to patents and registration of trademarks are recorded at cost if capitalization criteria are met. Amortization is provided over their estimated useful lives on a straight-line basis over 15 years.

Impairment of long-lived assets

When events or changes in circumstances indicate the carrying amount of a long-lived asset or group of assets held for use, including capital assets and patents, may not be recoverable, an impairment loss is recognized when the carrying amount of those assets exceeds the sum of the undiscounted future cash flows related to them. The impairment loss is included in the statement of operations and the carrying value of the asset or group of assets is reduced to its fair value as determined by the sum of the discounted future cash flows related to those assets. The impairment loss is presented within amortization expense of the related assets.

Income taxes

LMS follows the liability method of accounting for income taxes. Under this method, future income tax assets and liabilities are determined based on the differences between the financial reporting and tax bases of assets and liabilities and are measured using substantively enacted tax rates and laws that are expected to be in effect in the periods in which the assets or liabilities are expected to be realized or settled. Changes in these balances are included in net earnings of the period in which they arise. A valuation allowance is provided to the extent that it is more likely than not that future income tax assets will not be realized.

2. SIGNIFICANT ACCOUNTING POLICIES (Cont'd)

Stock-based compensation

As a result of amendments made in October 2003 to the provisions of the Canadian Institute of Chartered Accountants (“CICA”) Handbook Section 3870, effective November 1, 2003, LMS changed its method of accounting for employee stock-based compensation and decided to adopt the fair value based method of accounting for all its stock-based compensation. LMS adopted these changes using the prospective application transitional alternative in accordance with the transitional provisions of CICA Handbook Section 3870. Accordingly, the fair value based method is applied to awards granted, modified or settled on or after November 1, 2003. Prior to the adoption of the fair value based method, LMS, as permitted by Section 3870, had chosen to continue its existing policy of recording no compensation expense on the grant of stock options to employees.

When stock options are exercised, capital stock is credited by the consideration paid together with the related portion previously credited to contributed surplus when compensation costs were charged against income. The prospective method omits the effects of awards granted, modified or settled before November 1, 2003.

LMS provides pro-forma disclosure of the compensation costs based on the fair value method for awards granted prior to November 1, 2003 under the employee stock option plan (*see note 8(iii)*).

Stock-based compensation expense and pro-forma disclosure of the stock-based compensation expense for all options granted under the LMS's stock option plans, as well as Deferred Share Units and warrants, is determined using the fair value method computed with the Black Scholes option pricing model. The related expense is recognized over the vesting period of such options, allowing for forfeitures, estimated by management.

Share issuance costs

Share and equity instrument issue costs are recorded as an increase in deficit.

Earnings per share

Basic earning per share (“EPS”) is calculated using the weighted average number of common shares outstanding during the year. Diluted EPS is calculated using the treasury stock method.

The shares to be issued under the Deferred Share Unit Plan (“DSU Plan”) are included in the computation of basic loss per share since shares issuable after a mere passage of time are not contingently issuable. The shares to be issued under the bonus plan (the “Bonus Plan”) are included in the computation of basic loss per share when such bonus awards are approved by the Board of Directors. The options and warrants to purchase common shares, as well as those shares to be issued under the Bonus Plan, were not included in the computation of the diluted loss per share because the effect would be anti-dilutive.

Revenue recognition

Revenue consists primarily of revenue from the sales of software licenses, hardware and technical support services. LMS recognizes revenue in accordance with the provisions of the American Institute of Certified Public Accountants Statement of Position (“SOP”) No. 97-2, *Software Revenue Recognition*.

LMS recognizes revenue from software licenses and hardware when persuasive evidence of an arrangement exists, delivery, installation and client's acceptance have occurred, the sales price is fixed or determinable, and collection is probable.

Revenue from technical support services, which is generally paid in advance, is deferred and recognized rateably over the period for which the technical support service is provided. Other service and consulting revenues are recognized as services are provided.

Revenue on arrangements that includes multiple elements such as hardware, software licenses and technical support services is allocated to each element based on vendor specific objective evidence (“VSOE”) of the fair value of each element. Allocated revenue for each element is recognized when revenue recognition criteria have been met for each element. VSOE is determined based on the price charged when each element is sold separately. If VSOE cannot be determined, and all other revenue recognition criteria have been met, revenues from multiple element arrangements are recognized rateably over the period for which the technical support service is provided. When VSOE of fair value of undelivered services is established subsequent to the outset of the arrangement, the deferred revenue relating to the arrangement is adjusted to the newly established VSOE of fair value of the undelivered services.

2. SIGNIFICANT ACCOUNTING POLICIES (Cont'd)

Foreign currency translation

The functional currency of LMS and its US subsidiary is the Canadian dollar. Accounts in foreign currencies have been translated into Canadian dollars using the temporal method. Under this method, monetary assets and liabilities denominated in foreign currencies are translated to Canadian dollars at the rates in effect at the balance sheet date. Other assets and liabilities are translated at the rates prevailing at the transaction dates. Revenues and expenses are translated at average rates prevailing during the period, except for amortization, which is translated at exchange rates prevailing when the related assets were acquired. Gains and losses arising from fluctuations in exchange rates are reflected in net earnings of the year.

Changes in accounting policies

Effective April 1, 2007, the Company adopted the following CICA Handbook Sections:

a) Section 3855, "Financial Instruments - Recognition and Measurement"

Provides guidance on the recognition and measurement of financial assets, liabilities and derivative financial instruments. This new standard requires that all financial assets and liabilities be accounted for using one of the following available accounting models: held-to-maturity, available-for-sale, loans and receivables, held-for-trading or other liabilities, and derivative financial instruments meeting certain recognition criteria, are initially measured at fair value.

Changes in the fair value of financial instruments classified or designated as held-for-trading and recognized derivative financial instruments not qualifying for hedge accounting are charged or credited to the statement of operations for the relevant period, while changes in the fair value of financial instruments classified as available-for-sale are charged or credited to other comprehensive income. After their initial fair value measurement, held-to-maturity, loans and receivables and other liabilities are measured at amortized cost using the effective interest rate method.

The standard requires LMS to make certain elections, upon initial adoption of the new rules, regarding the accounting model to be used to account for each financial instrument. Transaction costs for held-for-trading financial instruments must be expensed as incurred. Transaction costs incurred in connection with the issuance of other financial instruments may either be capitalized and presented as a reduction of the carrying value of the related financial instrument or expensed as incurred. If capitalized, transaction costs must be amortized to income using the effective interest method. This Section does not permit the restatement of financial statements of prior periods on adoption of this standard. LMS has elected to expense transaction costs incurred in connection with the issuance of other financial instruments.

Following is a summary of the accounting model LMS has elected to apply to each of its significant categories of financial instruments outstanding as of April 1, 2007:

Financial assets	Classification	Measurement
• Cash and cash equivalents	Held-for-trading	Fair value
• Short-term investments	Held-to-maturity	Amortized cost
• Investments	Held-to-maturity	Amortized cost
• Accounts receivable	Loans and receivables	Amortized cost
• Accounts payable	Other financial liabilities	Amortized cost
• Amounts due under the bonus and deferred share unit plans	Other financial liabilities	Amortized cost

The adoption of this standard had no impact on the opening consolidated balance sheet or the consolidated statement of operations of the year.

b) Section 1530, "Comprehensive Income", along with Section 3251, "Equity"

Amending Section 3250, "Surplus", require enterprises to present comprehensive income and its components as well as net income in their financial statements. Further, they require enterprises to separately present changes in equity during the period as well as components of equity at the end of the period, including comprehensive income. The adoption of these Sections did not have any impact on LMS's financial statements.

c) Section 3865, "Hedges"

Allows optional treatment providing that hedges be designated as either fair value hedges, cash flow hedges or hedges of a self-sustaining foreign operation. Since LMS does not currently have any hedging programs in place, the adoption of this Section did not have any impact on LMS's financial statements.

2. SIGNIFICANT ACCOUNTING POLICIES (Cont'd)

d) Section 1506, "Accounting Changes"

Under these new recommendations, voluntary changes in accounting policy are permitted only when they result in the financial statements providing reliable and/or relevant information. These recommendations also require changes in accounting policy to be applied retrospectively unless doing so is impracticable, require prior period errors to be corrected retrospectively, require enhanced disclosures about the effects of changes in accounting policies, estimates and errors on the financial statements, and require the disclosure of new primary sources of GAAP that have been issued but not yet effective. The adoption of this Section did not have a significant impact for the year ended March 31, 2008.

NEW ACCOUNTING PRONOUNCEMENTS

The new accounting pronouncements described below will be adopted by LMS in fiscal 2009 or future years.

Capital Disclosures

CICA Handbook Section 1535, "Capital Disclosures", requires disclosure of an entity's objectives, policies and processes for managing capital, quantitative data about what the entity regards as capital and whether the entity has complied with any capital requirements and, if it has not complied, the consequences of such non-compliance. This standard is effective for interim and annual financial statements relating to fiscal years beginning on or after October 1, 2007, specifically April 1, 2008 for LMS. LMS will disclose this information in its consolidated financial statements for the first quarter of fiscal 2009.

Financial Instruments Disclosures

CICA Handbook Section 3862, "Financial Instruments - Disclosures", increases the disclosures currently required that will enable users to evaluate the significance of financial instruments for an entity's financial position and performance, including disclosures about fair value. In addition, disclosure is required of qualitative and quantitative information about liquidity risk and market risk. The quantitative disclosures must also include a sensitivity analysis for each type of market risk to which an entity is exposed, showing how net income and other comprehensive income would have been affected by reasonably possible changes in the relevant risk variable. This standard is effective for interim and annual financial statements relating to fiscal years beginning on or after October 1, 2007, specifically April 1, 2008 for LMS. LMS will disclose this information in its consolidated financial statements for the first quarter of fiscal 2009.

Financial Instruments Presentation

CICA Handbook Section 3863, "Financial Instruments - Presentation", replaces the existing requirements on presentation of financial instruments which have been carried forward unchanged to this new Section. This Section is effective for interim and annual financial statements relating to fiscal years beginning on or after October 1, 2007, specifically April 1, 2008 for LMS and is not expected to have an impact on the consolidated financial statements.

General Standards on Financial Statement Presentation

CICA Handbook Section 1400, "General Standards on Financial Statement Presentation", has been amended to include requirements to assess and disclose an entity's ability to continue as a going concern. The changes are effective for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2008, specifically April 1, 2008 for LMS and is not expected to have an impact on the current going concern note disclosure.

Goodwill and Intangible Assets

CICA Handbook Section 3064, "Goodwill and Intangible Assets," replaces Section 3062, "Goodwill and Other Intangible Assets," and Section 3450, "Research and Development Costs." It establishes financial reporting for goodwill, start up costs and other intangible assets. This standard is effective for interim and annual financial statements beginning on or after April 1, 2009. LMS is currently assessing the impact of the adoption of this standard on the consolidated financial statements.

International Financial Reporting Standards

The Accounting Standards Board has a strategic plan for financial reporting in Canada whereby Canadian GAAP will converge with International Financial Reporting Standards ("IFRS") over the period ending March 31, 2011. After this transitional period, the Company will cease to use Canadian GAAP and will adopt IFRS. The Company is monitoring this transition to IFRS and is analyzing the impact that the adoption of IFRS will have on the audited consolidated financial statements.

3. ACCOUNTS RECEIVABLE

	2008	2007
	\$	\$
Trade accounts receivable	1,020,700	1,406,264
Commodity taxes	54,766	144,485
Other receivables	31,398	16,714
	1,106,864	1,567,463

No allowance for doubtful accounts has been recorded for the years presented.

4. FIXED ASSETS

	Cost	Accumulated amortization	Net carrying Value
	\$	\$	\$
2008			
Computer hardware	747,415	636,236	111,179
Computer software	272,994	245,847	27,147
Furniture and fixtures	146,726	104,298	42,428
Office equipment	102,143	83,254	18,889
	1,269,278	1,069,635	199,643
Computer hardware under capital leases	64,737	33,716	31,021
	1,334,015	1,103,351	230,664
2007			
Computer hardware	747,415	588,589	158,826
Computer software	277,993	141,505	136,488
Furniture and fixtures	146,726	92,009	54,717
Office equipment	102,143	76,597	25,546
Leasehold improvements	135,113	69,245	65,868
	1,409,390	967,945	441,445
Computer hardware under capital leases	76,642	23,985	52,657
Office equipment under capital leases	34,373	28,167	6,206
	1,520,405	1,020,097	500,308

During 2008, fixed assets, having a cost and accumulated amortization of \$190,845 (\$770,998 in 2007) and net carrying value of nil, were written off.

The acquisitions under capital leases for the years ended March 31, 2008, 2007 and 2006 totalled \$4,455, \$28,166 and \$48,476, respectively.

5. PATENTS

	2008	2007
	\$	\$
Patents	389,520	289,009
Accumulated amortization	(78,019)	(52,053)
	311,501	236,956

6. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

	2008	2007
	\$	\$
Trade accounts payable (note 10)	311,490	384,838
Accrued liabilities	272,722	285,272
Salaries, benefits, commissions and vacation accruals	457,898	681,525
	1,042,110	1,351,635

7. OBLIGATIONS UNDER CAPITAL LEASES

	2008	2007
	\$	\$
Obligations under capital leases bearing interest at rates ranging from 7% to 33%, repayable in monthly principal and interest instalments ranging from \$186 to \$1,323, guaranteed by the leased assets with carrying values of \$30,758	40,030	71,774
Less: Current portion of obligations under capital leases	(35,336)	(35,186)
	4,694	36,588

7. OBLIGATIONS UNDER CAPITAL LEASES (Cont'd)

Payments required over the next years are as follows:

	\$
2009	39,046
2010	4,821
2011	373
Total future minimum payments	44,240
Less: Interest	(4,210)
	40,030

8. CAPITAL STOCK**Authorized**

An unlimited number of common shares without par value.

Changes in common shares issued and outstanding are summarized as follows:

(i) Issued and paid

	Number	Common shares	\$
March 31, 2005	16,503,177		47,616,028
Issued under the Bonus Plan	13,872		33,986
Issued under the DSU plan	6,400		15,680
March 31, 2006	16,523,449		47,665,694
Issued in private placements	4,470,229		6,556,623
Issued under the Bonus Plan	235,046		484,195
March 31, 2007	21,228,724		54,706,512
Issued in private placements	4,000,000		1,740,000
Issued under the Bonus Plan	562,438		760,640
Issued under the DSU plan	18,211		29,125
Issued under a consulting agreement	46,667		35,049
March 31, 2008	25,856,040		57,271,326

During the years ended March 31, 2008, 2007 and 2006, LMS completed the following capital stock transactions:

2008

During 2008, 4,000,000 common shares, 1,000,000 subscriber warrants and 189,000 broker warrants were issued in a private placement for a total consideration of \$2,000,000. The warrants are exercisable for one common share at a strike price of \$0.60 for a period of five years from the date of issue.

LMS valued the subscriber warrants at \$260,000 using the Black-Scholes option pricing model with the following assumptions: expected average life of five years, fair value of \$0.55 per common share, volatility factor of 0.519, dividend yield of nil and risk-free interest rate of 3.86%. This warrant consideration has been included in the warrants balance (*note 8(ii)*).

LMS valued the broker warrants at \$49,140 using the Black-Scholes option pricing model with the following assumptions: expected average life of five years, fair value of \$0.55 per common share at grant date, volatility factor of 0.519, dividend yield of nil and risk-free interest rate of 3.86%. This warrant consideration has been recorded as a share issue cost within deficit and a corresponding credit in warrants balance (*note 8(ii)*).

Issuance costs, including the broker warrants related to the above transaction totalled \$330,420 and were recorded within deficit.

As at March 31, 2008, a cash amount of \$694,609 was held in trust by LMS' legal counsel relating to the above mentioned private placement. This amount was subsequently received in April 2008.

During 2008, 562,438 and 18,211 common shares were issued under the LMS Bonus and DSU Plans related to prior year Bonus and DSU (*note 8 (iv)* and (*v*)), at a fair value consideration at the time of issue of \$760,640 and \$29,125, respectively.

During 2008, 46,667 common shares were issued to a consultant in satisfaction of a consulting agreement, at a fair value consideration at the time of issue of \$35,049.

8. CAPITAL STOCK (Cont'd)

During the third quarter of fiscal 2008, management of LMS made a collective decision to temporarily suspend a portion of their salaried compensation for the remainder of fiscal 2008. Upon meeting certain milestones, the Board of Directors elected to pay the suspended salaries, including a 25% premium, either in the form of LMS common shares or in the form of deferred share units (“DSUs”) (*note 8(v)*). As at March 31, 2008, LMS recorded \$129,762, representing 216,270 common shares, within the shareholders' equity section as accruals for bonus expected to be paid by issuing common shares (*note 8 (iv)*), and \$413,295, representing 688,825 DSUs, within the current liabilities section as amounts due under the bonus and DSU plan (*note 8(v)*), for settlement of the aforementioned suspended salaries and the 25% premium. This last amount is subject to shareholder approval at the 2008 annual shareholders' meeting, at which time, it will be transferred to capital stock. Should approval not be obtained, this amount will be paid out in cash.

In February 2008, LMS's Board of Directors approved, subject to shareholders' approval, a Shareholders' Rights Plan (“the Plan”), which will trigger the issuance of one right per share issued should a single shareholder become the beneficial owner of 20% or more of LMS's common shares, other than as permitted in the Plan.

2007

During 2007, 4,470,229 common shares and 422,500 subscriber warrants were issued in three separate private placements for a total consideration of \$6,679,148.

As part of the first placement, LMS issued 1,250,000 common shares at \$2 per common share for a total consideration of \$2,500,000.

As part of the second placement, LMS issued 845,000 common shares and 422,500 subscriber warrants for a total consideration of \$1,563,250. The subscriber warrants have a three year life and an exercise price of \$1.50 per share. LMS valued these warrants at \$122,525 using the Black-Scholes option pricing model with the following assumptions: expected average life of three years, fair value of \$1.16 per common share, volatility factor of 0.44, dividend yield of nil and risk-free interest rate of 3.98%. This warrant consideration has been included in the warrants balance (*note 8(ii)*).

As part of the third placement, LMS issued 2,375,229 common shares at \$1.10 per common share for a total consideration of \$2,615,898. In connection with this third placement, LMS also issued 166,266 broker warrants with a three year life and an exercise price of \$1.29 per share. LMS valued these warrants at \$68,206 using the Black Scholes option pricing model with the following assumptions: expected average life of three years, fair value of \$1.25 per common share, volatility factor of 0.44, dividend yield of nil and risk-free interest rate of 3.95%. This warrant consideration has been recorded as a share issue cost within deficit and a corresponding credit in warrants balance (*note 8(ii)*).

In addition, 235,046 common shares were issued under the LMS Bonus Plan (*note 8 (iv)*), at the amount determined under the Bonus Plan for 2006 of \$484,195.

Issuance costs, including the warrants related to above transactions totalled \$687,408 and were recorded within deficit.

2006

During 2006, 13,872 and 6,400 common shares were issued under the LMS Bonus and DSU Plans (*note 8 (iv)* and (*v*)), at a fair value consideration at the time of issue of \$33,986 and \$15,680, respectively.

(ii) Warrants

	Number	\$
Balance as at March 31, 2005	1,117,177	397,592
Expired	(492,494)	(163,565)
Balance as at March 31, 2006	624,683	234,027
Issued in connection with private placements (<i>note 8 (i)</i>)	588,766	190,731
Expired	(40,427)	(13,425)
Balance as at March 31, 2007	1,173,022	411,333
Issued in connection with a private placement (<i>note 8 (i)</i>)	1,189,000	309,140
Expired	(123,885)	(41,145)
Balance as at March 31, 2008	2,238,137	679,328

8. CAPITAL STOCK (Cont'd)

Each warrant allows its holder to acquire one common share and have the following characteristics:

Exercise price \$	Number #	Remaining life in years
0.60	1,189,000	4.9
1.29	166,266	1.9
1.50	422,500	2.0
3.23	432,249	0.7
3.32	8,122	0.6
4.85	20,000	1.5
	2,238,137	

When warrants expire or are exercised, the carrying value of the warrants is credited to contributed surplus or capital stock, respectively.

(iii) Stock option plan

In 2005, LMS created a stock option plan for employees, directors and certain external consultants. Pursuant to the terms of the plan, the Board of Directors is authorized to grant to directors, officers, and employees of LMS and its subsidiaries, as well as to other persons who provide ongoing management or consulting services to LMS or its subsidiaries, options to acquire common shares of LMS at such prices as may be fixed at the time of the grant, provided however that the option exercise price shall not be less than the closing sale price of LMS's common shares on the Toronto Stock Exchange ("TSX") on the last trading day prior to the grant of the option.

Options granted under the new plan are non-assignable and non-transferable, have a maximum term of 10 years and generally vest over three years. The new plan was approved at the shareholders' annual and special meeting held on September 15, 2004 and the maximum number of options that can be granted under the new stock option plan was fixed at 2,149,942. At the 2007 annual shareholder meeting, the option pool was increased by 1,034,000 to 3,183,942.

Black-Scholes option model assumptions and expense details

LMS determined the fair value of options using the Black-Scholes option pricing model with the following weighted average assumptions:

	2008	2007	2006
Expected life	5	5	5
Fair value of common shares	\$1.42	\$1.84	\$2.26
Dividend yield	Nil	Nil	Nil
Volatility	0.489	0.44	0.427
Risk free interest rate	4.46%	4.22%	3.07%
Number of options granted	775,000	382,000	335,593
Fair value of stock options granted	\$475,309	\$245,480	\$318,000

LMS records the related stock option expense over the vesting period using the graded vesting method.

During the year ended March 31, 2008, the Company's Board of Directors authorized the issue of an additional 785,000 of stock options, of which 775,000 were granted during the year.

Included in the 775,000 options granted in 2008 are 150,000 options issued to a consultant under a service agreement. Half of these options, or 75,000, vested immediately upon signing of the agreement and the expense of \$20,250 was recognized. The second half, or 75,000, may vest at a specific date as agreed to in the agreement, only upon reaching certain milestones. The exercise price of these options is \$0.53 and they expire on February 11, 2013.

8. CAPITAL STOCK (Cont'd)

The changes to number of stock options granted and their weighted average exercise price are as follows

	Number	Weighted average exercise price \$
March 31, 2005	1,386,499	4.30
Granted	335,593	2.26
Expired	(42,722)	(3.26)
Cancelled	(115,973)	(3.87)
March 31, 2006	1,563,397	3.92
Granted	382,000	2.12
Expired	(280,991)	(4.59)
Cancelled	(64,800)	(3.45)
March 31, 2007	1,599,606	3.39
Granted	775,000	1.33
Cancelled	(84,667)	(2.24)
March 31, 2008	2,289,939	2.74

OPTIONS OUTSTANDING				OPTIONS EXERCISABLE	
Exercise price	Number Outstanding as at March 31, 2008	Weighted average contractual Life	Weighted average exercise price \$	Number Exercisable as at March 31, 2008	Weighted average exercise price \$
0.53-0.58	225,000	4.9	0.55	75,000	0.53
1.50-1.70	550,000	4.2	1.66	-	-
1.80-2.06	337,333	2.9	1.98	179,111	1.91
2.25-2.45	235,359	2.4	2.40	176,906	2.38
3.69-4.00	146,403	1.5	3.95	146,403	3.95
4.28-4.62	795,844	1.3	4.30	795,844	4.30
0.53-4.62	2,289,939	2.7	2.74	1,373,264	3.50

Pro-forma disclosure regarding the options issued prior to November 1, 2003 is as follows:

	2008 \$	2007 \$	2006 \$
Net loss attributable to common shares - basic and diluted	(5,389,846)	(9,312,111)	(9,406,172)
Additional stock option expense that would have been included in the determination of net loss if the fair value based method had been applied to all awards	-	6,964	64,532
Pro-forma net loss attributable to common shares - basic and diluted	(5,389,846)	(9,319,075)	(9,470,704)
Pro-forma basic and diluted loss per share	(0.24)	(0.50)	(0.57)

(iv) Bonus Plan

In fiscal 2005, LMS established the Bonus Plan that provides for annual awards to eligible executives and employees based on achievement of corporate and individual performance objectives. The award is paid in common shares and DSUs, the number of which is based upon dividing the total award by the five day average year-end closing market price of the common shares on the TSX. At the 2005 annual and special meeting of shareholders, the Bonus Plan was approved. At the 2006 annual general meeting the maximum number of shares issuable under the Bonus Plan was increased from 250,000 to 500,000. At the 2007 annual shareholder meeting, LMS shareholders approved the increase of the number of shares issuable under the Bonus Plan from 500,000 to 1,300,000.

2008

For the year ended March 31, 2008, 562,438 (\$760,640) of the reserved shares were issued. 4,789 common shares issued and reserved relating to employees who left subsequent to March 31, 2007, were cancelled and a balance of \$5,699 was applied against contributed surplus.

For the year ended March 31, 2008, LMS recorded bonus expense of \$380,000 for the 2008 fiscal year, expected to be paid in common shares or DSUs. As at March 31, 2008, shares reserved, available and unissued and approved by the shareholders under the Bonus Plan were 272,374 whereas the required number of shares to settle the 2008 bonus was 633,333. As a result of this shortfall, only a portion of the \$380,000, or \$163,424, representing 272,374 common shares was recorded within the shareholders' equity section as accruals for bonus expected to be paid by issuing common shares. The remaining balance of \$216,576 was recorded as

8. CAPITAL STOCK (Cont'd)

a current liability on the balance sheet. Upon proposal and approval by LMS shareholders at the next annual general meeting, this amount will be reversed and recognized in shareholders' equity upon issuance of 122,858 common shares totaling \$73,715 and 238,101 DSUs totaling \$142,861 by LMS. Should approval not be obtained, this amount will be paid out in cash.

As at March 31, 2008, LMS recorded \$129,762, representing 216,270 common shares, within the shareholders' equity section as accruals for expected bonus to be paid in common shares, for settlement of the suspended salaries of management and the 25% premium (*note 8(i)*).

2007

For the year ended March 31, 2007, LMS recorded total bonus expense related to the Bonus Plan in the amount of \$675,000. As at March 31, 2007, shares reserved, available and unissued and approved by the shareholders under the Bonus Plan were 250,510 whereas the required number of shares to settle the 2007 bonus was 567,227. As a result of this shortfall, only a portion of the \$675,000, or \$297,000, representing 249,580 common shares was recorded within the shareholders' equity section as accruals for bonus expected to be paid by issuing common shares. The remaining balance of \$378,000 was recorded as a current liability on the balance sheet. At the 2007 annual shareholder meeting, LMS shareholders approved the increase of the number of shares issuable under the Bonus Plan from 500,000 to 1,300,000, at which time the accrued balances at March 31, 2007 were transferred to shareholders' equity. A difference of \$79,941 arose resulting from the increase in the share price between March 31, 2007 and August 9, 2007, the date of the approval of the Plan change. This difference was recorded as an adjustment to the bonus expense in 2008.

2006

For the year ended March 31, 2006, LMS has recorded bonus expense related to the Bonus Plan in the amount of \$485,373, with a corresponding credit within the shareholders' equity section.

(v) Deferred Share Unit Plan

In fiscal 2005, LMS established the DSU Plan that provides for the payment of director's quarterly compensation with DSUs. Each DSU is a right granted by LMS to an eligible director to receive one common share upon termination of service. The number of DSUs to be granted under the DSU Plan is determined by dividing the quarterly director compensation by the five day average quarter end closing market price of the common shares on the TSX. At the 2005 annual and special meeting of shareholders, the DSU Plan was approved. At the 2006 annual general meeting, the maximum number of DSUs issuable under this plan was increased from 125,000 to 250,000. LMS has the option to remit either cash or common shares to settle the DSUs. At the 2007 annual general meeting, the shareholders approved the increase of the number of DSUs issuable under this plan from 250,000 to 400,000. As well, the shareholders approved the following amendments to the DSU Plan: (a) to add full-time officers and employees as eligible participants; (b) to permit eligible officers and employees to elect to receive all or a portion of any bonus under the Company's Bonus Plan in the form of DSUs; and (c) permit officers to elect to receive a portion of their annual base salary in the form of DSUs.

2008

Following the approval of the increase of the number of shares issuable under the DSU Plan from 250,000 to 400,000 at the 2007 annual general meeting, the accrued balance of \$9,000 at March 31, 2007 was transferred to shareholders' equity. A difference of \$2,798 relating to the difference between the accrued balance as at March 31, 2007 and the amount paid by issuing shares in the year ended March 31, 2008, was recorded as an adjustment to the directors' compensation expense in 2008. The difference arose from the increase in the share price between March 31, 2007 and August 9, 2007, the date of the approval of the Plan change.

For the year ended March 31, 2008, LMS recorded total director compensation expense under the DSU Plan of \$215,021. As at March 31, 2008, shares reserved, available and unissued and approved by the shareholders under the DSU Plan were 147,379 whereas the required number of shares to settle the 2008 DSU director compensation was 277,008. As a result of this shortfall, only a portion of the \$215,021, or \$139,257, representing 147,379 DSUs was recorded within the shareholders' equity section under the DSU balance. The remaining balance of \$75,764 was recorded as a current liability on the balance sheet.

During the third quarter of fiscal 2008, management at LMS made a collective decision to temporarily suspend a portion of their salaried compensation for the balance of fiscal 2008. Upon meeting certain milestones, the Board of Directors elected to pay a portion of the suspended salaries, including a 25% premium, in the form of LMS common shares (*note 8(i)*), and the remaining portion in the form of DSUs. As at March 31, 2008, LMS recorded \$413,295, representing 688,825 DSUs, within the current liabilities section as amounts due under the bonus and DSU Plan.

8. CAPITAL STOCK (Cont'd)

For the year ended March 31, 2008, LMS recorded bonus expense to be paid in common shares of \$237,139, representing 395,232 common shares (*note 8(iv)*) and \$142,861, representing 238,101 DSUs within the current liabilities section as amounts due under the bonus and DSU Plan.

2007

For the year ended March 31, 2007, LMS recorded total director compensation expense related to the DSU Plan of \$222,500. As at March 31, 2007, shares reserved, available and unissued and approved by the shareholders under the DSU Plan were 142,370 whereas the required number of shares to settle the 2007 DSU compensation is 148,920. As a result of this shortfall, only a portion of the \$222,500, or \$213,500, representing 141,365 common shares was recorded within the shareholders' equity section under the DSU balance. The remaining balance of \$9,000 was recorded as a current liability on the balance sheet.

In 2007, 8,028 DSUs, with a value of \$20,609 were cancelled at the request of a director, and director compensation was reduced by this amount.

2006

Prior to the approval of the DSU Plan by the shareholders, and as of March 31, 2005, LMS provided for the related directors' compensation expense of \$56,625 within accounts payable and accrued liabilities as there was an obligation to remit cash. Following the approval of the DSU Plan by the shareholders, LMS reduced accrued liabilities and increased the DSUs account for the DSUs conditionally granted prior to approval of the Plan. A difference of \$20,270 between the amount accrued at March 31, 2005 based on the then share price and the value of the related units issued upon shareholder approval in 2006 was recorded as a reduction in the DSU Plan balance and the related DSU expense in 2006.

Total director compensation expense for the year ended March 31, 2006 was \$206,250.

The changes to the DSU Plan balance, number of deferred share units outstanding and the weighted average price of grant or issue are as follows:

	DSU Plan balance \$	Number of DSU Units #	Weighted average price of DSU \$
Balance as at March 31, 2005	56,625	14,624	3.87
Units granted	206,250	93,006	2.22
Shares issued	(15,680)	(6,400)	(2.45)
Adjustment to DSU balance	(20,270)	-	-
Balance as at March 31, 2006 (presented within shareholders' equity)	226,925	101,230	2.39
Units granted	222,500	148,920	1.49
Units cancelled	(20,609)	(8,028)	(2.57)
Balance as at March 31, 2007 (\$9,000 presented within current payables and \$419,816 presented within shareholders' equity)	428,816	242,122	1.77
Units granted	771,177	1,203,934	0.64
Shares issued	(29,125)	(18,211)	(1.60)
Balance as at March 31, 2008	1,170,868	1,427,845	0.82

8. CAPITAL STOCK (Cont'd)

The following table summarizes the transactions in the Bonus and DSU Plans for the years ended March 31, 2008, 2007 and 2006.

	2008	2007	2006	For the year ended March 31, 2008					
				Recorded in the Statement of Operations ⁽¹⁾		Compensation in		Recorded in	
				DSUs	Common shares	Current liabilities	Shareholders' equity		
	\$	\$	\$	\$	\$	\$	\$		
Management's salary and premium	543,057	—	—	413,295	129,762	413,295	129,762		
Bonus expense	380,000	675,000	485,373	142,861	237,139	216,576	163,424		
Adjustment due to price variation	79,941	—	—	—	79,941	—	79,941		
	1,002,998	675,000	485,373	556,156	446,842	629,871	373,127		
Directors' Compensation	215,021	201,891	206,250	215,021	—	75,764	139,257		
	1,218,019	876,891	691,623	771,177	446,842	705,635	512,384		

(1) These amounts have been allocated to each department and are included in R&D expenses; administrative; selling, marketing and product management; customer support and quality assurance expenses.

(vi) Contributed surplus

	\$
Balance as at March 31, 2005	1,255,108
Stock option expense	735,070
Warrants expired (note 8 (ii))	163,565
Balance as at March 31, 2006	2,153,743
Stock option expense	560,889
Warrants expired (note 8 (ii))	13,425
Bonus plan adjustment	1,178
Balance as at March 31, 2007	2,729,235
Stock option expense	422,369
Warrants expired (note 8 (ii))	41,145
Cancellation of common shares (note 8 (iv))	(5,699)
Balance as at March 31, 2008	3,187,050

9. COMMITMENTS AND CONTINGENCIES**(i) Operating leases**

The minimum rentals payable under long-term operating leases for premises and equipment, exclusive of certain operating costs for which LMS is responsible, are as follows:

	\$
2009	129,622
2010	10,714
2011	8,410
2012	5,186
2013	4,754
	158,686

The rental expense for the years ended March 31, 2008, 2007 and 2006 were \$201,655, \$214,631 and \$225,844, respectively.

LMS leases approximately 9,300 square feet of office space provided by Standard Life Insurance Co. In 2006, LMS amended certain terms of the lease, entered into originally in 1997, and received \$135,113 of leasehold inducements in 2007, which were amortized over the remainder of the lease term ended in February 2008 (see note 9 (iv)). The lease was extended in early 2008 for a period of seven months, ending in September 2008.

(ii) License agreement

Prior to 2006, LMS entered into a license agreement with a third party in connection with databases to be used within its software products. The license agreement is renewable every year and provides non-transferable, non exclusive licenses and is subject to royalties on revenues of the third party derived from the product.

9. COMMITMENTS AND CONTINGENCIES (Cont'd)**(iii) Distribution agreements**

Under a value-added marketing agreement entered into on October 15, 2004 and ending in October 2009 with McKesson Information Systems LLC (“Distributor”), a US based company involved in the development and sale of integrated system tools for hospitals in North America, LMS is committed to interfacing its software with Distributor systems. In addition, LMS agreed not to enter into similar agreements with certain competitors of the Distributor. LMS has the right to interface its software products with other parties. In connection with this agreement, Distributor agreed to acquire licenses and advanced a cash consideration of US\$500,000 in 2004. During 2008, the conditions for revenue recognition for a portion of the advance were met, with the remaining balance of \$216,027 (US\$166,666) included in deferred revenues and deposits from distributors on the balance sheet as at March 31, 2008 (2007 - \$432,288 (US\$333,333)).

(iv) Letters of credit

Under the lease agreement for its premises (note 9 (i)), ended in February 2008, LMS was required to issue a letter of credit secured by an investment of an equivalent amount. The letter of credit was reimbursed in February 2008 upon termination of the lease and equalled \$25,000 at March 31, 2007. In addition, under an agreement with a bank, a \$50,000 (2007 - \$50,000) investment is held as a security. These amounts are presented as restricted non-current investments on the balance sheet.

(v) Claims and actions

In the normal course of its business, LMS may be exposed to various claims and actions, including product and service liabilities. These cases often have numerous uncertainties and the outcome of each case is unpredictable and may have a material impact on the consolidated financial statements of LMS. In the opinion of the Company, potential liabilities that may result from these actions are not expected to have a material adverse effect on the Company’s financial position or its results of operations.

(vi) Stock exchange listing requirements

As at March 31, 2008, LMS was listed on the TSX and the American Stock Exchange (“AMEX”). During 2007, LMS did not meet certain AMEX minimum listing requirements relating to its shareholders' equity and was notified by AMEX of this default. In May 2008, the Company's Board of Directors approved the voluntary delisting from the AMEX as part of management's plan to reduce costs. The delisting was completed on May 22, 2008. On June 5, 2008, LMS filed Form 15F with the US Securities and Exchange Commission to voluntarily terminate the registration of its Common Shares under section 12(g) of the Securities Exchange Act of 1934, as amended. LMS continues to meet the TSX listing requirements.

(vii) Indemnification of Directors and Officers

LMS indemnifies its directors and officers against claims reasonably incurred and resulting from the performance of their services to the Company, and maintains liability insurance for its directors and officers as well as those of its subsidiaries.

(viii) Insurance Contract

LMS maintains commercial liability insurance. The policy was renewed for a one-year period in January 2008 and is being financed. The amount financed is \$132,279, at a rate per annum of 9.60% from February 13, 2008 to January 13, 2009, with monthly payments of \$12,610, and is included in accounts payable and accrued liabilities.

10. RELATED PARTY TRANSACTIONS

LMS enters into transactions in the normal course of business with a related company having one common director. These transactions are measured at the exchange amount. The related party management fees expense amounted to \$216,342, \$192,300 and \$191,532 for the years ended March 31, 2008, 2007 and 2006, respectively. Balances due in connection with these transactions amount to \$104,167 as at March 31, 2008 (\$32,050 as at March 31, 2007).

11. SUPPLEMENTARY CASH FLOW INFORMATION

The net change in non-cash working capital balances related to operations is as follows:

	2008 \$	2007 \$	2006 \$
Decrease (increase) in current assets			
Accounts receivable	460,599	(1,004,027)	176,152
Investment tax credits receivable	40,000	136,000	922,888
Prepaid expenses	1,771	49,181	220,614
	502,370	(818,846)	1,319,654
Increase (decrease) in liabilities			
Accounts payable and accrued liabilities	(309,525)	(84,807)	241,619
Amounts due under the bonus and deferred unit plans <i>(note 8 (iv) and (v))</i>	705,635	387,000	-
Deferred revenue and deposits from distributors	152,794	542,980	203,823
	548,904	845,173	445,442
	1,051,274	26,327	1,765,096

Significant non-cash investing and financing activities

During 2008, LMS acquired \$4,455 in capital assets (2007 - \$28,166, 2006 - \$48,476) through obligations under capital leases. During fiscal 2006, the Company acquired software in an amount of \$107,000 by way of accounts payable.

Stock based compensation - cash flow disclosures

	2008 \$	2007 \$	2006 \$
Stock option expense <i>(note 8 (iii))</i>	422,369	560,889	735,070
Bonus expense in common shares <i>(note 8 (v))</i>	446,842	675,000	485,373
Bonus expense in DSUs <i>(note 8 (v))</i>	142,861	-	-
DSU expense for directors' compensation <i>(note 8 (v))</i>	215,021	222,500	206,250
DSU expense for management salaries <i>(note 8 (v))</i>	413,295	-	-
	1,640,388	1,458,389	1,426,693
Amounts of bonus expense included within current liabilities <i>(note 8 (iv))</i>	(216,576)	(378,000)	-
Amounts of DSU expense included within current liabilities <i>(note 8 (v))</i>	(489,059)	(9,000)	-
Total included within current liabilities	(705,635)	(387,000)	-
DSU units cancelled <i>(note 8 (v))</i>	-	(20,609)	-
Other adjustments - DSU <i>(note 8 (v))</i>	-	-	(20,270)
Other adjustment - Bonus Plan <i>(note 8 (iv))</i>	-	-	(22,014)
	-	(20,609)	(42,284)
Total included within equity	934,753	1,050,780	1,384,409

12. FINANCIAL INSTRUMENTS**Credit risk and economic dependence**

LMS continually evaluates its customers' credit standing and generally does not require a guarantee. As at March 31, 2008, a distributor represents 98% of trade accounts receivable (as at March 31, 2007 - a distributor represented 94% of trade accounts receivable) and is denominated in US dollars.

In 2008, revenue generated through a distributor represented 85% of total revenues (2007 - 73%). These revenues were billed in US dollars. In 2006, the distributor and one customer represented 77% of total revenues (distributor - 55%, one customer - 22%).

Cash and cash equivalents, investments - restricted and short-term investments, which consist of commercial paper as at March 31, 2008 bearing interest at 2.55% (2007 - 3.9%) are principally contracted with two Canadian chartered banks.

Fair values

The carrying values of cash and cash equivalents, short-term investments, accounts receivable, investment tax credits receivable, investments - restricted, accounts payable and accrued liabilities and amounts due under the Bonus and DSU Plans are a reasonable estimate of their fair values because of their short maturities.

12. FINANCIAL INSTRUMENTS (Cont'd)

The carrying value of the capital lease obligations approximates their fair value because management estimates that these capital leases with fixed interest rates have no significant difference between their fair value and their carrying value, based on rates currently available to LMS on capital leases with similar terms and remaining maturities.

Foreign exchange risk

As at March 31, 2008 and 2007, accounts receivable denominated in US dollars ("US \$") amounted to \$1,006,002 and \$1,408,729, respectively, (US \$980,031 and US \$1,220,101, respectively) and accounts payable and accrued liabilities and deposits from distributor denominated in US \$ amounted in aggregate to \$503,817 and \$807,741, respectively (US \$447,026 and US \$658,513, respectively). Also, cash and cash equivalents denominated in US \$ amounted to \$705,962 on March 31, 2008 and \$114,516 on March 31, 2007 (US \$687,737 and US \$99,182, respectively).

Interest rate risk

LMS is exposed to interest rate risk on its cash and cash equivalents as well as its investments. The Company is not exposed to interest rate risk on its capital lease obligations or interest bearing accounts payable, as these interest rates are fixed.

13. INCOME TAXES

The reconciliation of income tax computed at the statutory Canadian tax rates with income tax expense from operations is as follows:

	2008	2007	2006
	\$	\$	\$
Tax recovery at statutory rate	(1,814,000)	(3,090,000)	(2,990,000)
Increase (decrease) in income tax recovery resulting from:			
Non-deductible expenses	835,000	530,000	460,000
Québec non-taxable investment tax credits	(8,000)	(12,000)	(29,000)
Differences in effective rate attributable to income taxes	(30,000)	213,000	(833,000)
Other items	-	(373,000)	(1,437,000)
Unrecognized tax benefits from operating losses	1,082,000	2,732,000	4,829,000
Impact of current year temporary differences	(65,000)	-	-
	-	-	-

The tax effects of temporary differences and net operating losses that give rise to future income tax assets are as follows:

	2008	2007
	\$	\$
Future income tax assets		
Tax basis of capital assets and patents in excess of carrying value	367,000	437,000
Non-capital losses carried forward	11,995,000	12,933,000
Non-refundable federal investment tax credits	-	590,000
Research and development expenditures	1,619,000	1,491,000
Financing fees	255,000	374,000
Total future income tax assets	14,236,000	15,825,000
Valuation allowance	(14,236,000)	(15,825,000)
Net future income tax assets	-	-

Changes in investment tax credits receivable, and amounts recorded as a reduction of research and development expenses, for each year are summarized as follows:

	2008	2007	2006
	\$	\$	\$
Investment Tax Credits Receivable			
Balance at the beginning of the year	124,000	260,000	1,182,888
Estimated investment tax credits	84,000	124,000	260,000
Excess (reduction) of tax credits received over the estimates			
for prior years	(1,907)	(14)	67,227
Investment tax credits recognized in income	82,093	123,986	327,227
Amounts received	(122,093)	(259,986)	(1,250,115)
Balance at the end of the year	84,000	124,000	260,000

As at March 31, 2008, the investment tax credits receivable are related to investment tax credits estimated for the fiscal year ended March 31, 2008.

13. INCOME TAXES (Cont'd)

To date, substantially all of LMS's investment tax credits claimed, filed and assessed by the government authorities have been accepted favourably as submitted. LMS records investment tax credits receivable based on management's best estimates which are based on past experience and on the nature of the research and development projects and related eligible expenses. Any favourable or unfavourable adjustment that may result following assessment by government authorities will be recorded to income in the period when such assessment is performed.

LMS has accumulated share issuance expenses of approximately \$819,000 (2007 - \$1,130,000) that have not been deducted for income tax purposes as well as a non-refundable investment tax credit of approximately \$656,000 (2007 - \$590,000) related to R&D expenditures which may be utilized to reduce federal income taxes payable in the future years. Accumulated R&D expenses, with an unlimited carry-forward period, were \$3,943,000 (2007 - \$3,040,000) for federal and \$7,861,000 (2007 - \$7,580,000) for Quebec tax purposes. Also, LMS has non-capital tax losses which are available to reduce future taxable income. The tax benefits of the above items have been fully provided for by a valuation allowance.

The detail of the non-capital tax losses by expiration year is as follows:

	Loss carry-forwards			
	Federal \$	Québec \$	Ontario \$	USA \$
2009	5,377,000	5,318,000	-	-
2010	4,081,000	3,971,000	-	-
2014	1,800,000	1,798,000	-	-
2015	7,127,000	6,528,000	575,000	-
2026	6,218,000	5,852,000	331,000	-
2027	6,302,000	6,296,000	-	-
2028	2,439,000	1,382,000	1,057,000	-
Thereafter	-	-	-	5,790,000
	33,344,000	31,145,000	1,963,000	5,790,000

14. ENTREPRISE WIDE INFORMATION

Management has determined that principal activities of LMS operate in a single business segment and have been devoted to the development of leading-edge software based products to be used as decision support tools for obstetricians mainly in the US and in Canada. Information about geographic areas is as follows:

	Canada \$	USA \$	Total \$
March 31, 2008			
Revenue	335,455	4,637,394	4,972,849
Fixed assets and patents	533,480	8,685	542,165
March 31, 2007			
Revenue	422,516	2,428,749	2,851,265
Fixed assets and patents	726,101	11,163	737,264
March 31, 2006			
Revenue	165,528	1,416,976	1,582,504
Fixed assets and patents	727,468	13,871	741,339

15. COMPARATIVE FIGURES

Certain comparative figures have been reclassified to conform to the basis of presentation adopted in the current year.

This page has been deliberately left blank

This page has been deliberately left blank

This page has been deliberately left blank

