



ANNUAL INFORMATION FORM
for the Year Ended October 31, 2006

January 29, 2007

PRESENTATION OF INFORMATION

As used in this Annual Information Form, the term "Patheon" or "Company" means Patheon Inc. and its subsidiaries as of the most recent financial year ended on October 31, 2006 on a consolidated basis, unless the context otherwise requires, and "Patheon Inc." refers to Patheon Inc. on an unconsolidated basis.

Unless otherwise stated, all information is as of October 31, 2006 and all currency references are in U.S. dollars.

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FORWARD-LOOKING STATEMENTS

This Annual Information Form contains forward-looking statements which reflect management's expectations regarding Patheon's future growth, results of operations, performance (both operational and financial) and business prospects and opportunities. Where possible words such as "plans," "expects" or "does not expect," "budget," "forecasts," "anticipates" or "does not anticipate," "believes," "intends" and similar expressions or statements that certain actions, events or results "may," "could," "would," "might" or "will" be taken, occur or be achieved, have been used to identify these forward-looking statements. Although the forward-looking statements contained in this Annual Information Form reflect management's current assumptions based upon information currently available to management and based upon what management believes to be reasonable assumptions, Patheon cannot be certain that actual results will be consistent with these forward-looking statements. A number of factors could cause actual results, performance, or achievements to differ materially from the results expressed or implied in the forward-looking statements, including those listed in the "Risk Factors" section of this Annual Information Form. These factors should be considered carefully and readers should not place undue reliance on the forward-looking statements. Forward-looking statements necessarily involve significant known and unknown risks, assumptions and uncertainties that may cause Patheon's actual results, performance, prospects and opportunities in future periods to differ materially from those expressed or implied by such forward-looking statements. These risks and uncertainties include, among other things: risks related to the market demand for client products; credit and client concentration; the ability to identify and secure new contracts; regulatory matters, including compliance with pharmaceutical regulations; management of expanded operations; international operations risks; currency; competition; product liability claims; intellectual property; environmental; financial restructuring; restrictive covenants; going-concern uncertainty; substantial financial leverage; interest rates; and conditions of MOVA's tax exemptions. See "Risk Factors," Although Patheon has attempted to identify important risks and factors that could cause actual actions, events or results to differ materially from those described in forward-looking statements, there may be other factors and risks that cause actions, events or results not to be as anticipated, estimated or intended. There can be no assurance that forward-looking statements will prove to be accurate, as actual results and future events could differ materially from those anticipated in such statements. Accordingly, readers should not place undue reliance on forward-looking statements. These forward-looking statements are made as of the date of this Annual Information Form and, except as required by law, Patheon assumes no obligation to update or revise them to reflect new events or circumstances.

CORPORATE STRUCTURE

NAME, ADDRESS AND INCORPORATION

Patheon Inc. is a corporation existing under the *Canada Business Corporations Act*. The registered office of Patheon Inc. is located at 7070 Mississauga Road, Suite 350, Mississauga, Ontario, Canada, L5N 7J8.

INTERCORPORATE RELATIONSHIPS

Set out below is a list of the principal subsidiaries of Patheon Inc. and their respective jurisdictions of incorporation. All subsidiaries referred to in the list below are wholly owned subsidiaries of Patheon Inc.

Name of Corporation	Jurisdiction
Patheon Inc.	Canada
Patheon International Inc.	Ontario, Canada
Patheon Pharmaceuticals Inc.	Delaware, U.S.A.
Patheon Pharmaceuticals Services Inc.	Delaware, U.S.A.
Patheon Italia S.p.A.	Italy
Patheon UK Limited	England
Patheon France S.A.S.	France
MOVA Pharmaceutical Corporation	Puerto Rico, U.S.A.
CEPH International Corporation	Puerto Rico, U.S.A.
MOVA Real Estate Corporation	Puerto Rico, U.S.A.

GENERAL DEVELOPMENT OF THE BUSINESS

THREE-YEAR HISTORY

Over the last three years, Patheon has continued to build on its vision to be the leader in pharmaceutical manufacturing. Patheon strives to be the preferred commercial manufacturing and pharmaceutical development services partner to the global pharmaceutical industry. Patheon's strategy is focused on providing "best-in-class" manufacturing and development services, effectively balancing high product quality and reliability of supply with cost.

Prior to fiscal 2006, a key aspect of Patheon's strategy was to expand capacity, expertise and capabilities, positioning the Company to be the preferred manufacturing services partner to the pharmaceutical industry. The culmination of this strategy was the acquisition of MOVA Pharmaceutical Corporation and certain affiliates in December 2004 which included three manufacturing facilities in Puerto Rico. More recently, the Company has focused on growing its business internally. Organic growth has been achieved through expanding the level of business from existing clients, attracting new clients, entering into commercial manufacturing agreements for newly approved products for which the Company has provided development services, and broadening its service offering to include differentiated and specialized technologies and capabilities.

Fiscal 2006 was one of the Company's most challenging years, as a result of operational challenges, disappointing financial results and related financial issues, and management changes. These issues required a significant amount of management's attention in fiscal 2006. The Company was required to negotiate amendments to certain financial covenants under its North American credit facilities in order to ensure that the Company remained in compliance. The amendments cover monthly reporting periods through March 31, 2007. On September 11, 2006, the board of directors of the Company formed a special committee of independent directors to evaluate strategic and financial alternatives for the Company. As at the date hereof, this process is ongoing. Management changes at the executive level throughout fiscal 2006 placed further pressure on senior management and the overall operational effectiveness of the Company. A chronology of significant events of fiscal 2006 is set out below:

- *December 12, 2005* – Patheon announced that its subsidiary, CEPH International Corporation, resumed normal production of Omnicef® at its Carolina, Puerto Rico facility, following

implementation of a plan developed by CEPH to respond to an FDA warning letter received in September 2005.

- *December 15, 2005* – New credit facilities were put in place in the aggregate amount of \$290 million to refinance existing debt of Patheon Inc. and its U.S. subsidiaries (including the Puerto Rican subsidiaries). New credit facilities were also put in place for its wholly-owned subsidiary in Italy in the amount of €28.5 million.
- *March 6, 2006* – New Chief Financial Officer, Douglas L. Ludwig, was appointed, replacing Rodger Roden who was appointed on September 23, 2005.
- *May 8, 2006* – Patheon announced the retirement of Robert Tedford, its Chief Executive Officer, ten months earlier than the previously announced intended retirement date. The Company also announced that Board of Directors had established the Office of the Chief Executive Officer to carry out the CEO's responsibilities on an interim basis until a new CEO was appointed. The Office of the Chief Executive Officer would consist of Peter A.W. Green, Chairman of the Board of Patheon Inc., Nick A. DiPietro, President and Chief Operating Officer, and Douglas L. Ludwig, Chief Financial Officer and Executive Vice-President.
- *June 2, 2006* – Patheon announced the initiation of a performance enhancement program aimed at improving the productivity and cost effectiveness of Patheon's operations.
- *July 24, 2006* – Patheon issued an update to its outlook for the third quarter ending July 31, 2006, and for fiscal 2006 following the voluntary suspension of production of a high-volume product at its Caguas, Puerto Rico facility due to stability-related issues and a temporary disruption in the supply of an ingredient for another product. The Company also advised that it had commenced discussions with the lenders under its North American credit facilities to amend certain financial covenants provided for in those facilities, in light of these financial results and to provide for greater financial flexibility as it implemented its performance enhancement program.
- *July 31, 2006* – Patheon announced that it had reached an agreement with its lenders under its North American credit facilities to amend the credit agreement following the Company's announcement on July 24, 2006 with respect to the results for the third quarter ending July 31, 2006.
- *September 11, 2006* – Patheon announced the formation of a special committee, comprised of the four independent members of the Board, to evaluate a range of strategic and financial alternatives for the Company. Patheon also announced the appointment of Riccardo Trecroce, Patheon's General Counsel, Secretary and Executive Vice-President, Administration, as Chief Executive Officer. The Office of the Chief Executive Officer was disbanded. Douglas L. Ludwig, Chief Financial Officer and Executive Vice-President, advised the company of his decision to resign. Nicholas Dowd, Vice-President and Controller assumed the responsibilities of the Chief Financial Officer on an interim basis while the Company began a search for a successor Chief Financial Officer.
- *September 14, 2006* – Patheon announced that, for the third quarter of fiscal 2006, it had recognized a \$254.7 million non-cash asset impairment charge, principally in respect of goodwill, depreciable intangible assets and tangible capital assets related to its MOVA Pharmaceutical operations. The Company had determined that the carrying value of these assets was impaired as a result of the continuing deterioration of MOVA's financial results

during the quarter, and the effect of the charge was to write these assets down to their estimated fair value.

- *September 25, 2006* – New Chief Financial Officer, John H. Bell, was appointed.
- *October 16, 2006* – Patheon announced amendments to certain financial covenants under its North American credit facilities. The amendments to the North American credit agreement established amended financial covenants, including trailing 12-month debt-to-EBITDA covenants. The amended covenants, to be satisfied monthly, cover a six-month period from October 31, 2006 to March 31, 2007.

In January 2006, Patheon entered into a five-year master supply agreement with Merck & Co., Inc. (NYSE: MRK) to provide commercial manufacturing and pharmaceutical development services. Merck selected Patheon as one of Merck's strategic partners for commercial manufacturing and pharmaceutical development services.

The new master supply agreement is designed to facilitate the inclusion of additional products and projects as Merck implements a new strategic plan, which includes leveraging external capabilities and capacity. As a strategic partner for Merck, Patheon will be provided the opportunity to participate in future commercial manufacturing and appropriate product development projects.

Merck awarded Patheon three new projects as the first step in this new relationship. One project is a late-stage development product for Patheon's Caguas, Puerto Rico, facility. A second project involves activity at Patheon's Cincinnati facility and a third project involves activity at Patheon's Toronto Region Operations in Mississauga, Canada. These projects are expected to generate commercial revenues for Patheon in fiscal 2007, if regulatory approvals for these products are obtained within the planned timelines. Patheon is currently providing development services in connection with these projects.

Management's primary goals for fiscal 2007 are:

- to successfully complete Patheon's strategic and financial alternatives review process, implementing a long-term improvement to the Company's financial structure; and
- to continue to implement Patheon's performance enhancement program, achieving identifiable EBITDA improvements as a result of cost savings from global procurement initiatives, improved manufacturing efficiencies and a reduction in global workforce size.

DESCRIPTION OF THE BUSINESS

GENERAL

Patheon is a leading provider of commercial manufacturing and pharmaceutical development services ("PDS") to the international pharmaceutical industry, employing more than 5,600 people. Patheon produces both prescription ("R_x") and over-the-counter ("OTC") drugs for its clients. Patheon owns or leases and operates: (i) 10 manufacturing facilities in North America: four facilities in the U.S., comprising three in Puerto Rico and one in Cincinnati, Ohio, and six facilities in and around Toronto, Ontario, Canada, together comprising approximately 2,208,000 square feet of capacity; and (ii) four manufacturing facilities in Europe: Monza (near Milan) and Ferentino (near Rome), Italy; Swindon (near London), U.K.; and Bourgoin-Jallieu (near Lyon), France, which together comprise approximately 1,053,000 square feet of capacity.

PHARMACEUTICAL DEVELOPMENT

The pharmaceutical development services provided by Patheon include most of the dosage form development services typically required by companies conducting clinical trials and preparing for full-scale commercial production of a new drug. Background information on the new drug development process is described in Appendix A. In providing its pharmaceutical development services, Patheon is able to: (i) develop an appropriate dosage form; (ii) develop analytical methods; (iii) manufacture to client specifications the proposed new drug product during the regulatory drug approval process; (iv) manufacture pilot batches of proposed new drug products for the regulatory drug approval process; and (v) provide scale-up and technology transfer services designed to validate that a drug can be manufactured commercially. Since the beginning of fiscal 2001, 17 new pharmaceutical products developed by Patheon's PDS operations unit have received regulatory approval and have progressed to commercial manufacturing, three of which are among the world's top 200 selling R_x drugs. Three products received approval and were launched in fiscal 2006, all of which have contributed to Patheon's commercial manufacturing revenues.

Patheon offers pharmaceutical development services at five facilities in North America and Europe. In addition to possessing pharmaceutical development capabilities for a broad range of dosage forms, each of Patheon's PDS units provides a different specialized pharmaceutical development capability (high-potency, sterile, lyophilization and controlled-release). At October 31, 2006, Patheon was working on a total of 171 projects for its clients, including five drug candidates at the NDA stage. The growing PDS team included, at the end of fiscal 2006, more than 500 scientists and technical staff, with approximately 71 holding doctoral degrees. Patheon's development scientists have extensive development experience with a wide variety of pharmaceutical dosage forms.

COMMERCIAL MANUFACTURING

Patheon provides manufacturing services for a broad range of products in several dosage forms and packaging formats in accordance with client specifications. Depending on the particular client, Patheon may be responsible for most or all aspects of the manufacturing and packaging process, from sourcing raw materials and packaging components to delivering the finished product in consumer-ready form to the client.

Patheon's commercial manufacturing activities relate primarily to R_x and OTC products in solid, semi-solid and liquid dosage forms and the manufacture of R_x products in various sterile dosage forms. Conventional dosage forms include both coated and uncoated compressed tablets, hard shell gelatin capsules, powders, ointments, creams, gels, syrups, suspensions, solutions and suppositories. Conventional sterile dosage forms include aseptically filled liquids or terminally sterilized liquids and powders filled in ampoules, vials, bottles or pre-filled syringes. Sterile lyophilized products are also manufactured in both vials and ampoules. Patheon's manufacturing operations personnel are experienced in working on a wide variety of dosage forms. Patheon also operates a segregated sterile (injectable) cephalosporin powder filling facility at its Swindon Operations site in the United Kingdom. The combination of oral cephalosporin capabilities at our Carolina facility, the existing sterile cephalosporin capabilities at Swindon and the new 65,000 sq. ft. lyophilization plant dedicated to lyophilized cephalosporin products that Patheon constructed in Swindon in fiscal 2006 will allow it to provide a full range of dosage forms for this important category of antibiotics. The new facility in Swindon represented an investment of \$29 million during fiscal 2006, which was shared with our client.

In fiscal 2006, Patheon's facilities were audited by 199 separate client audit teams, representing both prospective and existing clients. Audits by prospective clients permit these prospective clients to gain confidence that Patheon's operations are conducted in accordance with applicable regulatory

requirements. Audits by existing clients permit these clients to reaffirm that Patheon's operations, as they relate to their products, are conducted in accordance with these requirements. These audits contribute to Patheon's ongoing improvement of manufacturing and development practices. In addition, 22 regulatory audits were conducted at the Patheon's sites in North America and Europe during fiscal 2006.

CLIENTS

Client Mix

Patheon serves a client base of over 200 pharmaceutical and biotechnology companies, including 19 of the world's 20 largest pharmaceutical companies (such as sanofi-aventis, Novartis AG and Roche Holdings AG); ten of the 20 largest biotechnology companies (such as Amgen Inc. and Gilead Sciences, Inc.); and seven of the 20 largest specialty pharmaceutical companies (such as Watson Pharmaceuticals, Inc. and Sepracor, Inc.).

During the fiscal years ended October 31, 2006 and 2005 only two clients accounted for more than 10% of Patheon's total revenues. As a percentage of Patheon's total revenues, these clients accounted for 12.7% and 12.3% in 2006 (2005 – 15.6% and 12.0%).

Patheon believes that the risks related to its reliance on its major clients are reduced by a number of factors, including:

- (a) the negotiation of long-term manufacturing agreements with these clients;
- (b) the fact that manufacturing services for these clients are not concentrated at a single facility or on a single product;
- (c) the diversity of products and projects undertaken by Patheon: in fiscal 2006, Patheon manufactured more than 700 products in connection with more than 2,000 stock keeping units across a wide range of therapeutic categories and dosage forms; and
- (d) the expansion of PDS units in both Europe and North America: by increasing the variety of service activities, Patheon is increasing its client base, thereby lowering the risk of depending on a small number of clients for a significant portion of its revenues.

Client Purchase Commitment Process

Patheon's commercial manufacturing clients generally provide a yearly forecast of anticipated product demand. Clients also deliver firm purchase orders, typically three months prior to scheduled production, after which time clients may adjust contract quantities or delivery dates within certain limits, provided that Patheon is reimbursed for any expenses incurred in connection with the adjustment. Upon delivery to Patheon of a client purchase order confirming the quantity and delivery date, the order is scheduled for production.

Patheon has commercial manufacturing services contracts, typically with multi-year terms, with its clients. These contracts formalize the standard business arrangements outlined above, including production based on the delivery of firm purchase orders. In addition, the contracts generally provide for six to 18 months' advance notice for the transfer or discontinuance of any product. The client assumes liability for all material commitments made in accordance with purchase orders. Patheon maintains the right to negotiate increases in prices based on extraordinary market changes in material costs. The anticipated revenues to be generated by Patheon's major client agreements are not

determinable with any precision as volumes are based on the client's market demands from time to time.

Patheon's pharmaceutical development services are provided on a fee-for-service basis. Patheon typically responds to a request for proposals and, if the proposal is accepted, it normally forms the basis of the contract with the client. Frequently, the scope of work in the initial contract changes over the life of the project in response to research results and client needs.

COMPETITION

Pharmaceutical and biotechnology companies looking to outsource commercial manufacturing services evaluate several factors in determining whether to outsource, including whether there is adequate in-house capacity or capability and the comparative costs between manufacturing internally or outsourcing. Some specialty pharmaceutical companies make a strategic decision not to develop in-house manufacturing capabilities, preferring to focus their capital and human resources on research and development of potential new products and sales and marketing of existing products.

If a company is considering outsourcing commercial manufacturing services, several factors go into choosing the preferred service provider. These factors include security of supply (quality record, regulatory compliance record and financial stability of the service provider), service (on-time delivery record and flexibility in manufacturing) and cost-effective manufacturing (prices and a commitment to continuous improvement). Competition in the OTC commercial manufacturing and packaging market has a greater emphasis on price and service than other factors. Competition in the R_x manufacturing market tends to have a greater emphasis on security of supply and service factors.

Pharmaceutical and biotechnology companies looking to outsource product development services evaluate several factors in selecting a service provider. These factors include scientific personnel, knowledge and experience of the organization in dosage form development, availability of a broad range of equipment from small to large scale, timely delivery of clinical materials, compliance with cGMP, regulatory compliance record, cost effective services and financial stability of the service provider.

Commercial Manufacturing

In North America and Europe, Patheon's competition includes: (i) companies, both public and private, that are not focused on contract manufacturing, but provide this service as part of a range of services to the pharmaceutical industry; (ii) companies that focus on contract manufacturing, but offer services in a limited number of dosage forms; and (iii) large pharmaceutical companies that offer third-party manufacturing services to fill excess capacity. In addition, in Europe there are a large number of privately owned, dedicated outsourcing companies that serve only their local or national markets.

Pharmaceutical Development

The pharmaceutical development services market is composed of a range of participants: (i) a large number of laboratories, which offer only a limited range of development services generally at a small scale; (ii) providers focused on specific technologies and/or dosage forms; and (iii) a few fully integrated companies that can provide the full complement of services necessary to develop, scale-up and manufacture a wide range of dosage forms.

SUPPLY ARRANGEMENTS

Patheon's clients specify the components, raw materials and packaging materials required for products and, in some cases, specify the suppliers from which Patheon must purchase these inputs. Materials for the Cincinnati Operations originate primarily in the U.S. For production at the Canadian sites, Patheon obtains packaging components from Canadian suppliers, but due to limited availability in Canada, most raw materials originate from U.S. sources. Components and packaging materials for production at the Monza and Ferentino (Rome) Operations are sourced primarily in Italy but also from other European sources. Materials for the Swindon and Bourgoin-Jallieu Operations are primarily sourced in the U.K. and France, respectively, along with other European markets. Materials for the Puerto Rico-based sites are sourced primarily from Puerto Rico and mainland U.S.A. Most of the materials required by Patheon for its commercial manufacturing business are readily available. In most cases, the clients supply the active pharmaceutical ingredient to Patheon at no cost to Patheon.

ENVIRONMENTAL AND HEALTH & SAFETY MATTERS

Patheon is subject to environmental legislation in the jurisdictions in which it operates. These laws regulate air emissions, water discharges and the storage, handling and disposal of solid and hazardous wastes. Patheon has the necessary environmental licences, permits, certificates of approval and other authorizations, except for certain licenses that need to be issued in light of changes in operations at certain facilities. Patheon has applied for these licenses and anticipates that they will be issued in due course. Patheon is in compliance, in all material respects, with applicable environmental laws and regulations.

Patheon is subject to health and safety legislation in the jurisdictions in which it operates. These laws regulate working conditions, safety procedures, training, exposure to hazardous materials, first aid requirements and injury reporting. Patheon is in compliance, in all material respects, with applicable environmental laws and regulations.

Patheon has an environmental, health and safety management system consisting of comprehensive programs and procedures, which ensure that Patheon's environmental, health and safety policies are fully implemented in accordance with applicable legislative requirements. Patheon has dedicated the required resources to implement and monitor the environmental, health and safety management system to ensure compliance.

Patheon has incurred and will continue to incur costs relating to compliance with applicable environmental and health and safety laws and regulations. Although compliance with these laws and regulations has not had a material adverse effect on Patheon's operations or financial condition, there can be no assurance that such compliance in the future will not have such an effect.

INTELLECTUAL PROPERTY

Patheon does not normally obtain or own patents or trademarks with respect to its manufacturing processes, other than standard protections with respect to trade names and Patheon logos. Many of the formulations used by Patheon in manufacturing products to client specifications are subject to patents or other protections owned or licensed by the relevant client. Patheon typically enters into mutual confidentiality agreements with clients that own or are registered users of patented formulations.

Patheon has developed and continues to develop knowledge and expertise in the provision of pharmaceutical development and commercial manufacturing services ("know-how"). This know-how

is normally not patentable, but it is valuable in that it enhances Patheon's ability to provide high-quality services to its clients.

SEASONAL VARIABILITY OF RESULTS

Revenues from some of Patheon's OTC and R_x commercial manufacturing services and its pharmaceutical development services have been traditionally lower in Patheon's first fiscal quarter, being the three months ending January 31. Patheon attributes this to several factors, including: (i) many clients reassess their need for additional product in the last quarter of the calendar year in order to use existing inventories of products; (ii) the lower production of seasonal cough and cold remedies; (iii) many small pharmaceutical and small biotechnology clients involved in PDS projects limit their project activity toward the end of the calendar year in order to reassess progress on their projects and manage cash resources; and (iv) the Patheon-wide plant shut-down during a portion of the traditional holiday period in December and January. In addition, the introduction and marketing of new client products traditionally occurs during Patheon's second fiscal quarter.

SOCIAL POLICIES

Integrity, respect and excellence are the core principles that govern the way Patheon operates its business. These principles are documented in a Code of Business Conduct developed to communicate Patheon's values and to provide guidelines for addressing issues and questions related to Patheon's business practices. The Code of Business Conduct was adopted by the Board of Directors of Patheon Inc. to serve as a guide to Patheon personnel worldwide, including employees, consultants, board members and agents. Patheon continues to communicate the Code of Business Conduct to employees at each of its facilities by distributing copies to all new employees, complemented by presentations as necessary to reinforce the principles of the Code of Business Conduct and their application.

In July 2005, Patheon engaged EthicsPoint, Inc. to act as Patheon's external service provider with respect to a confidential whistleblower program and the program was rolled out to the employees during fiscal 2006. The program is both telephone and web based. Employees may use this service to report any activities they suspect may be in violation of the Patheon Code of Business Conduct, including matters relating to accounting, internal accounting controls and auditing. As part of the implementation process for this service it became apparent that certain laws in France and Italy will not allow Patheon to offer this service to employees of Patheon France S.A.S. and Patheon Italia S.p.A.

RISK FACTORS

Certain risk factors that may affect Patheon are described below. These risks and uncertainties are not the only ones facing Patheon. Additional risks and uncertainties not currently known to Patheon or that Patheon currently considers immaterial may also impair the operations of Patheon.

Market Demand for Clients' Products

Patheon is dependent on demand for the products it manufactures on behalf of its clients and on the ability of its clients to successfully market and obtain coverage and reimbursement for their products. Demand for clients' products can be adversely affected by, among other things, the loss of patent protection, the emergence of competing products, the degree to which health authorities subsidize payment for a particular product and changes in the marketing strategies for such products.

Competing generic products often emerge as a product approaches the end of its patent protection period. Patheon's revenues for fiscal 2006 were negatively impacted by the loss in patent protection

for Zocor[®]. In addition, the molecule patent protection for Omnicef[®], a product that Patheon manufactures for Abbott Laboratories, Inc., is scheduled to expire in May 2007 (a second patent covering a particular crystalline form expires in December 2011). Abbott is currently engaged in litigation with one of its competitors that is attempting to launch a generic version of Omnicef[®]. If one or more competing generic products is launched, Patheon's revenues for the manufacturing of Omnicef[®] are likely to be significantly reduced.

Patheon may be materially adversely affected by any reduction in market demand for Omnicef[®] or other products that Patheon manufactures for its clients. There can be no assurance that production volumes of key products and related revenues will be maintained or that changes in product mix will not materially adversely affect profitability.

Credit and Client Concentration

A substantial portion of the Company's services are provided to a relatively small number of clients. During the year ended October 31, 2006, two clients accounted for more than 10% of the Company's total revenues (12.7% and 12.3%, respectively; 15.6% and 12.0% in 2005) and approximately 60.5% (64.4% in 2005) of revenues were derived from its 10 largest clients. This client concentration increases credit risk and other risks associated with particular clients and particular products, including risks related to market demand for client products, and regulatory and other operating risks. The Company's earnings were significantly adversely affected in fiscal 2006 as a result of the loss of revenues from a generic product where the Company's client lost a major customer and a temporary suspension during the third quarter of production and shipments of a major product because of stability concerns. Disruptions in the production of these or other major products could materially adversely impact Patheon's results of operations in the future.

Potential New Manufacturing Services/Development Agreements

There can be no assurance that Patheon will be able to continue to identify and secure new opportunities to enter into acceptable long-term manufacturing services agreements or that it will be able to fund any required capital expenditures related to such opportunities. Additionally, Patheon's pharmaceutical development services projects are primarily short-term projects of one to two years, and there can be no assurance that Patheon will be able to continue to identify and secure new projects.

Regulatory Matters Affecting Manufacturing and Pharmaceutical Development Services

Patheon is required to comply with the regulatory requirements of the national and international regulatory bodies having jurisdiction in the countries where they manufacture products or where their clients' products are distributed. As a result, most of Patheon's facilities are subject to regulation by the FDA, and certain of Patheon's facilities are subject to regulation by the HPFB, the MHRA, the EMEA and other regulatory bodies. These regulatory requirements impact many aspects of Patheon's operations, including manufacturing, labeling, packaging, adverse event reporting, storage and record keeping related to clients' products. In addition, if new legislation or regulations are enacted or existing legislation or regulations are amended or are interpreted or enforced differently, Patheon may be required to obtain additional approvals or operate according to different manufacturing standards. This may require Patheon to change its manufacturing techniques or make capital improvements to its facilities. There can be no assurance that Patheon will be able to meet all of the applicable regulatory requirements in the future. If Patheon fails to comply with applicable regulatory requirements, it may be subject to fines, suspension or withdrawal of regulatory approvals, product recalls, seizure of products, debarment, exclusion, disgorgement of profits, operating restrictions and criminal prosecution, as well as the loss of contracts and resulting revenue losses.

Patheon's pharmaceutical development projects often involve products that must undergo safety and clinical evaluations before they are approved as commercial therapeutic products. The regulatory authorities having jurisdiction in the countries in which its clients intend to market their products may delay approval of a product or determine that the product is not approvable. There can be no assurance that the pharmaceutical development projects and their related revenues for Patheon will be maintained.

Pharmaceutical products commercially manufactured by Patheon are subject to ongoing regulatory review following the receipt of marketing authorization. The regulatory authorities having jurisdiction in the country in which the product is marketed may withdraw the marketing authorization, either temporarily or permanently, for health or safety concerns related to the use of the product. The subsequent discovery of previously unknown problems with any of Patheon's clients' products may result in restrictions on the product, including withdrawal of the product from sale. There can be no assurance that production volumes of key products and related revenues for Patheon will be maintained.

Management of Expanded Operations

Patheon has experienced, and in accordance with its strategy Patheon may continue to experience, significant growth in a relatively short period of time. Managing such growth could place a significant burden on managerial, financial and other resources of Patheon. The ability of Patheon to manage future growth will depend on its ability to attract, train, motivate and manage key employees and to continue to implement and improve operations, financial and management information systems, procedures and controls. In particular, Patheon's success will depend to a significant degree on senior management's contributions and its ability to retain and attract key management and other highly skilled technical personnel. Any failure by Patheon to manage its growth could have a material adverse effect on its business, financial condition and results of operation.

International Operations

Patheon's operations are subject to the risks of doing business in several countries in North America and Europe including, but not limited to, varying economic and political conditions, cultures and business practices, tax rates, possible restrictions on the transfer of funds, employee turnover, labour unrest, longer payment cycles and the burdens and costs of compliance with laws of a variety of countries. There can be no assurance that these factors will not have an adverse effect on business, financial conditions and results of operations of Patheon.

Exposure to Foreign Currency Risk

The activities of Patheon are conducted in several currencies — Canadian dollars and U.S. dollars for the Canadian operations, U.S. dollars for the U.S. operations and euros and British sterling for the European countries.

Since the European and U.S. operations conduct business principally in their respective local currencies, the exposure to foreign currency gains and losses is not significant. However, revenues and operating expenses of the Canadian operations are transacted in Canadian and U.S. dollars. As a result, significant long-term strengthening of the Canadian dollar against the U.S. dollar could adversely affect the profitability of the Canadian operations of Patheon and its consolidated financial results, subject to the ability to increase prices for services or to reduce costs. The strengthening of the Canadian dollar relative to the U.S. dollar adversely affected Patheon's EBITDA margins in fiscal 2006.

Competition

Some of Patheon's competitors may have substantially greater financial, marketing, technical or other resources than Patheon. Additional competition may emerge and may, among other things, result in a decrease in the fees paid for services, which would affect profitability of Patheon. One of the many factors affecting competition is the current excess of industry capacity available to potential competitors manufacturing drugs in solid and semi-solid dosage forms.

Product Liability Claims

Patheon may be subject to liability claims by those who purchase its services and end consumers of the products it manufactures. Historically, Patheon has been able to obtain liability insurance for the operation of their respective businesses. However, there can be no assurance that existing liability insurance will be adequate or that it will be able to be maintained or that all possible claims that may be asserted against Patheon will be covered by insurance. A partially or completely uninsured claim, if successful and of sufficient magnitude, could have a material adverse effect on Patheon, financial condition and results of operations of Patheon.

Intellectual Property

Patheon relies on unpatented proprietary know-how and continuing technological innovation in providing pharmaceutical development and commercial manufacturing services. Although Patheon requires its employees to enter into confidentiality agreements prohibiting them from disclosing its proprietary information or technology, these agreements may not provide meaningful protection for Patheon's trade secrets and proprietary know-how. Further, people who are not party to confidentiality agreements may obtain access to Patheon's trade secrets or know-how. Others may independently develop similar or equivalent trade secrets or know-how. If Patheon's proprietary information is divulged to third parties, including its competitors, Patheon's competitive position could be harmed.

Potential Environmental Liabilities

The facilities in Puerto Rico have been utilized over a period of years as manufacturing facilities and have certain known or potential conditions that may require remediation in the future. Management believes that the potential remediation costs for the Caguas and Carolina facilities in Puerto Rico are not likely to be material. With respect to the Manatí facility, where there may be greater potential for remediation costs to be incurred, management believes these costs are likely to be covered by a contractual indemnity and guarantee for contamination that was granted to MOVA at the time it acquired the site from the prior owner, a global pharmaceutical company. There can be no assurance, however, that remediation costs will not be material or that these costs will be covered by contractual indemnity or that Patheon will be able to successfully enforce this indemnity in the future.

Financial Restructuring

On September 11, 2006, Patheon announced that its board of directors had formed a special committee to review strategic and financial alternatives for the Company. As of the date hereof, the strategic and financial alternatives review process is ongoing. There can be no assurance that the strategic and financial alternatives review process will be successfully concluded or will result in a transaction or other material development involving the Company. If Patheon is not able to implement a long-term improvement in its capital structure as a result of this review, it anticipates that, in the absence of further amendments to its North American credit agreement, it will be in default of covenants under its North American loan facilities as at April 30, 2007 and it may not be

able to continue as a going concern. See "—Restrictive Covenants" and "—Going Concern Uncertainty". Even if the Company is able to complete a transaction that improves its capital structure, the transaction may result in equity dilution, may result in higher aggregate interest costs, and/or may restrict the Company's operational flexibility. In addition, the Company expects to incur substantial repositioning expenses in fiscal 2007 in connection with the strategic and financial alternatives review, the amount of which will depend in part on the outcome.

Restrictive Covenants

Patheon's credit facilities contain financial and operating covenants that limit Patheon management's discretion with respect to certain business matters. Financial covenants include covenants requiring the borrower thereunder to satisfy certain financial ratios, including covenants in respect of the debt-to-EBITDA ratio, a consolidated fixed charge coverage ratio and a minimum consolidated tangible net worth. Operating covenants restrict, among other things, Patheon's ability to incur additional indebtedness, to grant liens against its property, to complete mergers, acquisitions and asset sales, to make capital expenditures, to pay dividends or make certain other payments, to transact with its subsidiaries, to change the nature of its business, to amend documents related to other material indebtedness, to create new subsidiaries, to prepay or repurchase subordinated indebtedness, to undertake speculative transactions, to increase operating lease obligations, to change auditors (other than to a nationally recognized accounting firm) and to become the general partner in a partnership. A breach of any of these covenants, ratios or restrictions could result in an event of default under the credit facilities and any other agreements that include cross-default provisions.

Certain covenants in the Company's North American credit agreement were amended in July 2006 and again in October 2006 to permit the Company to remain in compliance as at July 31, 2006 and October 31, 2006, respectively. The amended covenants under the October 2006 agreement, which are to be satisfied monthly, cover a five-month period from October 31, 2006 to March 31, 2007. If Patheon is not able to implement a long-term improvement in its capital structure in connection with its strategic and financial alternatives review, it anticipates that, in the absence of further amendments to its North American credit agreement, it will be in default of covenants under its North American loan facilities as at April 30, 2007. Any such default would also cause a cross default under the Company's U.K. subsidiary's credit facility. The aggregate amount outstanding under the Company's North American and U.K. credit facilities as at October 31, 2006 was \$269.9 million. Even if the Company is able to improve its capital structure such that it is not in default of the financial covenants under its North American credit facilities as at April 30, 2007 or is able to negotiate further amendments to prevent such a default, there can be no assurance that the Company will be able to remain in compliance with its financial and other covenants in future periods.

Upon the occurrence of an event of default under any of the Company's credit facilities, the lenders could elect to declare all amounts outstanding under such indebtedness, together with accrued interest, to be immediately due and payable. If the lenders were to do so, there can be no assurance that the assets of Patheon would be sufficient to repay that indebtedness and any other debt.

Going Concern Uncertainty

As at October 31, 2006, the Company had a working capital deficiency of \$175.8 million, including \$263.8 million of long-term debt that has been reclassified as current, which was required under Canadian GAAP because a violation of the covenants under these credit facilities at a future compliance date within one year of that date was not unlikely. Patheon's financial statements as at and for the fiscal year ended October 31, 2006 include a going concern uncertainty note stating that the Company's ability to continue as a going concern is uncertain and is dependent upon the

successful outcome of Patheon's strategic and financial alternatives review. If the Company were to be unable to continue as a going concern, it might be unable to realize the carrying value of its assets, which has been determined based on the going-concern assumption, and the amount of its liabilities might exceed the amount of the realized value of its assets in a liquidation.

Substantial Financial Leverage

Patheon's total long-term debt and other bank indebtedness as at October 31, 2006 was \$349.6 million, and its financial leverage ratio (the ratio of total debt to equity) of 1.4 to 1. The Company's substantial financial leverage poses risks to it. Debt service requirements in future periods may be higher than in prior years as a result of a number of factors, including higher interest rates under refinanced debt, increased borrowing and increases in floating interest rates (see "—Interest Rate Risks"). In addition, the Company may incur substantial fees from time-to-time in connection with debt amendments or refinancing. If Patheon's cash flow is not sufficient to service its debt and adequately fund its business, it may be required to seek further additional financing or refinancing, or to dispose of assets. There is no assurance that any of these alternatives could be effected on satisfactory terms, or at all. In addition, Patheon's financial leverage could impair its ability to respond to operational challenges, changing business and economic conditions and new business opportunities, and may make it vulnerable in the event of a downturn in its business.

Interest Rate Risks

The Company has exposure to movements in interest rates. At October 31, 2006, approximately 93% (2005 – 83%) of the Company's total debt portfolio was subject to movements in floating interest rates. Assuming no change to the structure of the debt portfolio, the sensitivity to interest rate changes is as follows:

	<u>Approximate Impact on Pre-Tax Earnings and Cash Flow</u>
Change of 1% in floating interest rates	\$3.3 million

Conditions of MOVA's Tax Exemptions

MOVA's operations benefit from tax exemptions under the *Puerto Rico Tax Incentives Act of 1998*. The terms of these exemptions include commitments with respect to employment levels at each of MOVA's facilities, and the applicable income tax rates vary depending on these employment levels. Complying with the terms of these exemptions may restrict Patheon's operational flexibility in the future. MOVA's existing tax agreements expire between 2007 and 2017. Patheon has submitted applications to have its Puerto Rican tax incentives refreshed to be effective as of December 31, 2007. The effect will be to extend the Caguas and Carolina grants for a 10-year period and the Manati grant for a 15-year period from December 31, 2007. The Company has received a comfort letter from the appropriate government ministries in support of its applications. Although Patheon expects to be able to continue to renew or replace these agreements, there can be no assurance that it will be able to do so on terms favourable to Patheon, or at all.

DIVIDEND POLICY

Patheon Inc. has not paid dividends on its common shares during the three fiscal years ended October 31, 2006, October 31, 2005 and October 31, 2004. Patheon Inc.'s current policy is to not pay dividends on its common shares, preferring to reinvest its cash to enhance its growth. Patheon's credit facilities include covenants that restrict the ability to pay dividends, and financial covenants that may indirectly restrict the ability to pay dividends.

DESCRIPTION OF CAPITAL STRUCTURE

Patheon Inc.'s authorized share capital consists of an unlimited number of common shares and an unlimited number of class I preferred shares, issuable in series, of which 92,950,688 common shares and no preferred shares were issued and outstanding as at January 29, 2007. At October 31, 2006, Patheon Inc. had 3,949,815 stock options outstanding, of which 3,617,304 were exercisable.

Common Shares

Holders of common shares are entitled to dividends on a *pro rata* basis if, as and when declared by Patheon Inc.'s Board of Directors. Subject to the rights of the holders of any other class of Patheon Inc.'s shares entitled to receive dividends in priority to or rateably with the holders of common shares, Patheon Inc.'s Board of Directors may declare dividends on the common shares to the exclusion of any other class of Patheon Inc.'s shares. On the liquidation, dissolution or winding-up of Patheon Inc., holders of common shares are entitled to participate rateably in any distribution of Patheon Inc.'s assets, subject to the rights of holders of any other class of Patheon Inc.'s shares entitled to receive Patheon Inc.'s assets on such a distribution in priority to or rateably with the holders of common shares. Holders of common shares are entitled to receive notice of and attend all annual and special meetings of Patheon Inc.'s shareholders, other than separate meetings of holders of any other class or series of shares, and to one vote at shareholders' meetings in respect of each common share.

Preferred Shares

Class I Preferred Shares ("Preferred Shares") in the capital of Patheon Inc. may be issued from time to time in one or more series, each series comprising the number of shares and having the designation, rights, privileges, restrictions and conditions determined by Patheon Inc.'s board of directors. The Preferred Shares rank prior to the common shares with respect to the payment of dividends and distributions in the event of the liquidation, dissolution or winding-up of Patheon. Except as required by law or as may be allowed in respect of specific series of Preferred Shares when dividends are in arrears, the holders of the Preferred Shares are not entitled to receive notice of, to attend or to vote at any meeting of Patheon Inc.'s shareholders.

MARKET FOR SECURITIES

TRADING PRICE AND VOLUME

Patheon Inc.'s common shares are traded on the Toronto Stock Exchange ("TSX") under the trading symbol "PTI." The following table sets forth the reported high and low trading prices (in Canadian Dollars) and trading volumes of the common shares of Patheon Inc. on the TSX for each month of the fiscal year ending October 31, 2006.

Patheon Inc Common Shares

Month	Low (\$)	High (\$)	Volume Traded
November, 2005	6.24	6.99	7,725,764
December, 2005	5.13	6.57	17,804,884
January, 2006	5.23	7.62	8,826,906
February, 2006	6.37	8.13	11,362,481
March, 2006	6.34	7.22	4,827,601
April, 2006	6.95	7.57	3,439,547
May, 2006	6.82	7.90	7,382,078
June, 2006	6.66	8.22	3,734,406
July, 2006	5.02	8.44	5,656,978
August, 2006	5.05	6.28	4,068,243
September, 2006	4.76	5.99	5,357,324
October, 2006	4.98	5.50	5,909,992

DIRECTORS AND OFFICERS

EXECUTIVE OFFICERS

The names and municipalities of residence of Patheon's executive officers and the offices held by them in Patheon Inc. as of January 29, 2007 are set out below.

Name & Municipality of Residence	Office
RICCARDO TRECROCE ⁽¹⁾ Oakville, Ontario, Canada	Chief Executive Officer
NICK A. DIPIETRO ⁽²⁾ St. Catharines, Ontario, Canada	President, Chief Operating Officer & Director
JOHN H. BELL ⁽³⁾ Toronto, Ontario, Canada	Chief Financial Officer
CLIVE V. BENNETT ⁽⁴⁾ Niagara-on-the-Lake, Ontario, Canada	President, Patheon U.S.A.
ALDO BRACA ⁽⁵⁾ Latina, Italy	President, Patheon Europe
SHABBIR T. ANIK, PH.D. ⁽⁶⁾ Los Altos, California, USA	President Global PDS & Chief Scientific Officer
MICHAEL S. HARDING ⁽⁷⁾ St. Catharines, Ontario, Canada	Executive Vice-President, Global Quality Operations and Chief Operating Officer of MOVA Pharmaceutical Corporation
KEVIN D. DUFFY ⁽⁸⁾ Philadelphia, Pennsylvania, USA	Executive Vice President, Global Sales and Marketing and Business Development
STEVEN LIBERTY ⁽⁹⁾ Oakville, Ontario, Canada	Senior Vice-President, Operations, Canada

Name & Municipality of Residence	Office
TOM L. FERGUSON ⁽¹⁰⁾ Fort Erie, Ontario, Canada	Senior Vice-President, Global Information Technology
ROY WIESCHKOWSKI ⁽¹¹⁾ Kleinburg, Ontario, Canada	Senior Vice-President, Corporate Human Resources and Environmental, Health & Safety
NICHOLAS DOWD ⁽¹²⁾ Mississauga, Ontario, Canada	Vice-President and Controller
COLIN MINCHOM, PH.D. ⁽¹³⁾ Mississauga, Ontario, Canada	Vice-President, PDS Canada
MURRAY SNEDDEN ⁽¹⁴⁾ Aurora, Ontario, Canada	Vice-President and Treasurer
GREGORY B. SHEPHERD ⁽¹⁵⁾ Kitchener, Ontario, Canada	Secretary and Associate General Counsel

Notes:

- ⁽¹⁾ Mr. Trecroce was appointed Chief Executive Officer on September 10, 2006 and was appointed General Counsel, Secretary & Executive Vice-President, Administration effective June 26, 2006. Prior to that he was General Counsel, Secretary and Senior Vice-President, Administration. He resigned as Secretary on September 10, 2006.
- ⁽²⁾ Mr. DiPietro was appointed President and Chief Operating Officer in 1996.
- ⁽³⁾ Mr. Bell joined Patheon as Chief Financial Officer on September 25, 2006. Prior to that Mr. Bell was the Chief Financial Officer of BBi Enterprises LP from 2001 to 2005.
- ⁽⁴⁾ Mr. Bennett was also President and Chief Operating Officer of MOVA Pharmaceutical Corporation from August 1, 2005 until July 31, 2006. Prior to being appointed as President, Patheon U.S.A., Mr. Bennett was President, Patheon North America.
- ⁽⁵⁾ Mr. Braca was appointed President, Patheon Europe effective January 6, 2004; prior to that, Mr. Braca was Executive Vice-President, European Business Development and President, Patheon Italia S.p.A.
- ⁽⁶⁾ Dr. Anik was appointed as President, Global PDS & Chief Scientific Officer on April 11, 2005; prior to that, he was Executive Vice President, PDS & Chief Scientific Officer of Patheon.
- ⁽⁷⁾ Mr. Harding was appointed Chief Operating Officer of MOVA Pharmaceutical Corporation on August 24, 2006. Prior to that Mr. Harding was Executive Vice-President, Global Quality Operations; prior to that, he was Senior Vice-President, Global Quality Operations.
- ⁽⁸⁾ Mr. Duffy joined Patheon as Executive Vice-President, Global Sales, Marketing and Business Development on October 16, 2006. Prior to that, Mr. Duffy was Chief Relations Officer and Executive Vice President, Global Business Development with Omnicare Clinical Research in Philadelphia.
- ⁽⁹⁾ Mr. Liberty joined Patheon as Senior Vice-President, Operations, Canada on November 1, 2005. Prior to that, Mr. Liberty was Executive Director & General Manager of AstraZeneca Pharmaceuticals' Westborough Supply Site in Massachusetts, U.S.A.
- ⁽¹⁰⁾ Mr. Ferguson was appointed Senior Vice-President, Global Information Technology effective January 6, 2004; prior to that, he was Vice-President, Information Technology.
- ⁽¹¹⁾ Mr. Wieschkowski was appointed Senior Vice-President, Corporate Human Resources and Environment, Health & Safety on September 26, 2006. Prior to that Mr. Wieschkowski was Vice-President, Corporate Human Resources; prior to that, Mr. Wieschkowski was Senior Director, Corporate Human Resources; and, prior to that, was Director, Human Resources - North America.
- ⁽¹²⁾ Mr. Dowd was appointed Vice-President and Controller on December 13, 2005; prior to that, he was Director, Corporate Development.
- ⁽¹³⁾ Dr. Minchom was appointed Vice-President, PDS, Canada effective June 2, 2004; prior to that, he was Group Director, PDS Operations.
- ⁽¹⁴⁾ Mr. Snedden was appointed Vice-President and Treasurer effective August 21, 2006; prior to joining Patheon as Treasurer on February 10, 2003, Mr. Snedden was Treasurer of the Oxford Properties Group of Companies.
- ⁽¹⁵⁾ Mr. Shepherd was appointed as Secretary on September 10, 2006. Mr. Shepherd is Patheon's Associate General Counsel, having joined Patheon on January 27, 2003. Prior to that, Mr. Shepherd was Associate General Counsel – Corporate with Clarica Life Insurance Company.

DIRECTORS

The names and municipalities of residence of the directors of Patheon Inc., including their terms of office and committee memberships as of January 29, 2007 are set out below together with their principal occupations during the past five years. Each of the director's term of office shall expire immediately prior to the election of directors at the Annual General Meeting of Shareholders on April 19, 2007.

Name & Municipality of residence	Director since	Committee membership	Principal Occupation during past five years
PETER A.W. GREEN Campbellville, Ontario, Canada	1996	<ul style="list-style-type: none"> • Special Committee • Audit • Corporate Governance • Compensation and Human Resources 	Corporate Director
NICK A. DIPIETRO St. Catharines, Ontario, Canada	1993	<i>Not Applicable</i> ⁽¹⁾	President and Chief Operating Officer, Patheon
GEORGE PLODER Mississauga, Ontario, Canada	1992	<ul style="list-style-type: none"> • Special Committee • Audit • Corporate Governance 	Corporate Director
JOAQUÍN B. VISO San Juan, Puerto Rico, U.S.A.	2004	<i>Not Applicable</i> ⁽¹⁾	From August 2005 to present: Chairman, MOVA Pharmaceutical Corporation (pharmaceutical company); prior to August 2005, President and Chief Executive Officer, MOVA Pharmaceutical Corporation
DEREK J. WATCHORN Schomberg, Ontario, Canada	1998	<ul style="list-style-type: none"> • Special Committee • Corporate Governance • Compensation and Human Resources 	From October 2004 to present: President & Chief Executive Officer, Retirement Residences Real Estate Investment Trust and Trustee of IPC US Real Estate Investment Trust (asset and property management); From January 2003 to June 2004: Executive Vice-President, Strategic Initiatives, Canary Wharf Group plc (commercial property company); from September 2001 until January 2003, senior partner of the law firm Davies, Ward Phillips & Vineberg LLP
GREGORY C. WILKINS Toronto, Ontario, Canada	2003	<ul style="list-style-type: none"> • Special Committee • Audit • Corporate Governance 	From February 2003 to present: Chief Executive Officer & President, Barrick Gold Corporation (international gold mining company); From June 2001 to February 2003: Financial Consultant.

⁽¹⁾ Members of management are not members of any Committees of the Board

SHAREHOLDINGS OF DIRECTORS AND EXECUTIVE OFFICERS

As at January 29, 2007, Patheon's directors and executive officers as a group beneficially owned, directly or indirectly, approximately 11,356,036 common shares of Patheon Inc., representing 12.2% of the outstanding common shares.

CEASE TRADE ORDERS, BANKRUPTCIES, PENALTIES OR SANCTIONS

Mr. Green has previously been appointed as a director and officer of companies that have financial difficulties to assist such companies with financial restructuring, proposals or compromise arrangements. In this capacity, Mr. Green was appointed a director of Phillip Services Corp., which made a proposal under chapter 11 of the U.S. Bankruptcy Code and the *Companies Creditors'*

Arrangement Act (Canada) in 1999 and briefly became the Chairman and Chief Executive Officer of Norigen Inc., which went into receivership in August, 2001.

Mr. Ploder is a director, President and Chief Executive Officer of Vital Retirement Living Inc., a reporting issuer in the provinces of British Columbia, Alberta and Ontario. On June 20, 2003, a cease trade order was issued against Vital for failure to file annual audited financial statements for the fiscal year ended December 31, 2002 and first quarter interim financial statements for the period ended March 31, 2003.

AUDIT COMMITTEE INFORMATION

COMPOSITION OF THE AUDIT COMMITTEE

The Audit Committee is comprised of the following three members: George L. Ploder, Peter A.W. Green and Gregory C. Wilkins. The Board of Directors has determined that each member of the Audit Committee is independent of management and free from any interest and any business or other relationship that could, or could reasonably be perceived to, reasonably interfere with the director's ability to exercise his independent judgment and act in the best interests of Patheon.

RELEVANT EDUCATION AND EXPERIENCE

All of the members of the Audit Committee are Chartered Accountants and as such are financially literate. Each of the Audit Committee members: (i) is fully cognizant of the accounting principles used by Patheon to prepare its financial statements; (ii) has the ability to assess the general application of such accounting principles in connection with the accounting for estimates, accruals and reserves; (iii) has practical experience preparing, auditing, analyzing or evaluating financial statements; and (iv) has an understanding of internal controls and procedures for financial reporting.

In determining whether a director: (i) is "financially literate," the Board of Directors considers whether the director has the ability to read and understand a balance sheet, an income statement, a cash flow statement and the notes attached thereto; and (ii) has "accounting or related financial experience," the Board of Directors considers whether the director has the ability to analyze and interpret a full set of financial statements, including the notes attached thereto, in accordance with Canadian generally accepted accounting principles.

PRE-APPROVAL POLICIES AND PROCEDURES

On an annual basis the Audit Committee pre-approves a specified list of non-audit related services that may be performed during a particular fiscal year and establishes maximum fee levels for the various types of services listed. Amounts to be expended above these levels require specific Audit Committee approval.

EXTERNAL AUDITOR SERVICE FEES (all amounts listed below are in Canadian Dollars)

FISCAL YEAR	AUDIT FEES	AUDIT-RELATED FEES	TAX FEES	ALL OTHER FEES
2006	\$1,074,000	\$155,000	\$28,000	\$37,000
2005	\$1,051,000	\$341,000	\$76,000	\$81,000

AUDIT COMMITTEE CHARTER

Patheon Inc.'s Audit Committee Charter was most recently updated on June 2, 2005 and a copy is provided in Appendix C to this Annual Information Form.

REGULATORY ACTIONS

FDA WARNING LETTER

On September 16, 2005 CEPH International Corporation (“CEPH”), a part of the MOVA group that operates its facility in Carolina, Puerto Rico, received a warning letter from the FDA. The warning letter claimed that variations in assay, fill-weight, content uniformity and related issues for a suspension product manufactured by CEPH indicated a failure by CEPH to comply with current Good Manufacturing Practices (cGMP’s) of the U.S. Federal Food, Drug and Cosmetic Act. The affected product was powder for oral suspension, Omnicel[®] OP 250mg/5mL and 125mg/5mL. The capsule product was not affected. After receipt of the warning letter, CEPH voluntarily suspended production of the Omnicel powder for oral suspension product while it resolved the matters.

After filing a response letter to the FDA on October 6, 2005, the FDA responded to CEPH on October 11, 2005 (received by CEPH on October 18, 2005) stating that it had found that the commitments to the corrective actions outlined in CEPH’s response letter would address the FDA’s concerns raised in the warning letter.

On December 12, 2005 Patheon confirmed that CEPH had resumed normal production and shipments to its client of Omnicel[®] oral powder for suspension. This followed qualification of new equipment and validation of processes for manufacturing of the product in accordance with the plan proposed by CEPH in its response of October 6, 2005.

The FDA concluded an inspection of the Carolina facility in June 2006 and in August 2006 the site’s compliance status was changed from Official Action Indicated to a status of Voluntary Action Indicated. As a result the site is back on a full FDA approval status.

INTERESTS OF MANAGEMENT IN MATERIAL TRANSACTIONS

Mr. Joaquín B. Viso, who together with his wife jointly owns approximately 11.2% of the outstanding Patheon shares and is a director of Patheon Inc. is a controlling shareholder of Alara Pharmaceutical Corporation (“Alara”) which has two contractual commercial relationships with MOVA Pharmaceutical Corporation. One of these agreements involves a significant product for MOVA. According to the terms of the commercial manufacturing agreement, the right to place orders for such product has been assigned to a third party who purchases this product directly from MOVA; however, the New Drug Application (NDA) for such product remains the property of Alara. This commercial manufacturing agreement has a 17 year term, expiring in 2019 and grants MOVA the right to manufacture 85% of the worldwide requirements for such product for the term of the agreement.

The Company has agreed, through Patheon Italia S.p.A. and/or Patheon BV, to hold an interest of 18% in Pharma Services Provider srl and BSP Pharmaceuticals srl (collectively, “Project Onco”). Project Onco is an oncology production facility in Latina, Italy that will specialize in the provision of third party manufacturing of cytotoxic products. Patheon’s aggregate direct or indirect investment in Onco is not to exceed € million. Mr. Aldo Braca, President, Patheon Europe, and/or his immediate family members either directly or indirectly through entities controlled by Mr. Braca and/or his immediate family members will hold an aggregate interest of 47% in Project Onco.

TRANSFER AGENT AND REGISTRAR

The registrar and transfer agent for Patheon's common shares is Computershare Investor Services Inc. with transfer facilities in the cities of Halifax, Montreal, Toronto, Winnipeg, Calgary and Vancouver.

MATERIAL CONTRACTS

Other than contracts entered into in the ordinary course of business, Patheon has not entered into any material contracts during the fiscal year 2006 or any material contracts entered into prior to the 2006 fiscal year that remain in effect.

INTERESTS OF EXPERTS

NAMES OF EXPERTS

The auditors of Patheon are Ernst & Young LLP, Chartered Accountants. Patheon's consolidated financial statements as at October 31, 2006 and for the year then ended have been filed under National Instrument 51-102 in reliance on the report of Ernst & Young LLP, Chartered Accountants, given on their authority as experts in auditing and accounting.

INTERESTS OF EXPERTS

Patheon's audit committee obtained written confirmation from Ernst & Young LLP confirming that they are independent with respect to the Company within the meaning of the Rules of Professional Conduct of the Institute of Chartered Accountants of Ontario.

ADDITIONAL INFORMATION

Additional information, including information regarding directors' and officers' remuneration and indebtedness, principal holders of Patheon's securities and options to purchase securities, is contained in Patheon's Management Information Circular in respect of Patheon's annual general meeting held on March 9, 2006, and filed on SEDAR (www.sedar.com) in compliance with securities regulations and prior to such meeting. Additional financial information is provided in the consolidated financial statements and management's discussion and analysis for the year ended October 31, 2006, filed on SEDAR.

Patheon will provide to any person, upon request to the Secretary, the following documents:

- (a) when the securities of Patheon are in the course of a distribution under a preliminary short-form prospectus or a short form prospectus:
 - (i) one copy of the latest annual information form, together with one copy of any document, or the pertinent pages of any document, incorporated therein by reference;
 - (ii) one copy of the comparative financial statements of Patheon for its most recently completed financial year for which financial statements have been filed, together with the accompanying report of the auditor, and one copy of the most recent interim financial statements of Patheon that have been filed, if any, for any period after the end of Patheon's most recently completed financial year;

- (iii) one copy of the information circular of Patheon in respect of its most recent annual meeting of shareholders that involved the election of directors or one copy of any annual filing prepared instead of that information circular, as appropriate; and
 - (iv) one copy of any other documents that are incorporated by reference into the preliminary short form prospectus or the short form prospectus and are not required to be provided under paragraphs (i) to (iii) above; or
- (b) at any other time, one copy of any of the documents referred to in paragraphs (a)(i), (ii) and (iii) above, provided that Patheon may require the payment of a reasonable charge if the request is made by a person or company who is not a security holder of Patheon.

Additional information about Patheon may be found on SEDAR at www.sedar.com.

APPENDIX A

BACKGROUND ON THE DRUG DEVELOPMENT PROCESS

In order for a new drug to be sold in any country it must meet the country's regulatory standards, which ensure that the drug product is both safe and effective. In North America and Europe, the regulatory agencies that must approve a new drug's use include the U.S. Food and Drug Administration ("FDA"), the Health Products and Food Branch of Health Canada ("HPFB") and the European Medicines Evaluation Agency ("EMA") representing the European Union and the national regulatory agencies of member states. Both the drug and the processes by which it is developed, tested and manufactured must meet stringent regulatory requirements.

The process for a drug requiring FDA approval is described below, and this process is substantially similar for other regulatory agencies:

Discovery

The first step in the drug development process is the discovery of a new molecular entity ("NME") to treat a targeted disease. The drug discovery process requires a significant amount of time and financial investment.

Pre-Clinical Studies

Prior to evaluation in humans, pre-clinical studies are carried out on the NME. Pre-clinical studies involve laboratory evaluations of the NME characteristics and animal studies to assess the safety of the NME and to demonstrate the effectiveness of the NME against the targeted disease.

Investigation New Drug Application (IND)

This application is submitted to the FDA after completion of pre-clinical studies. The IND contains the results of pre-clinical studies and describes how a drug will be evaluated in human subjects. The IND must be approved before human clinical trials can be conducted.

Clinical Trials & Pharmaceutical Development

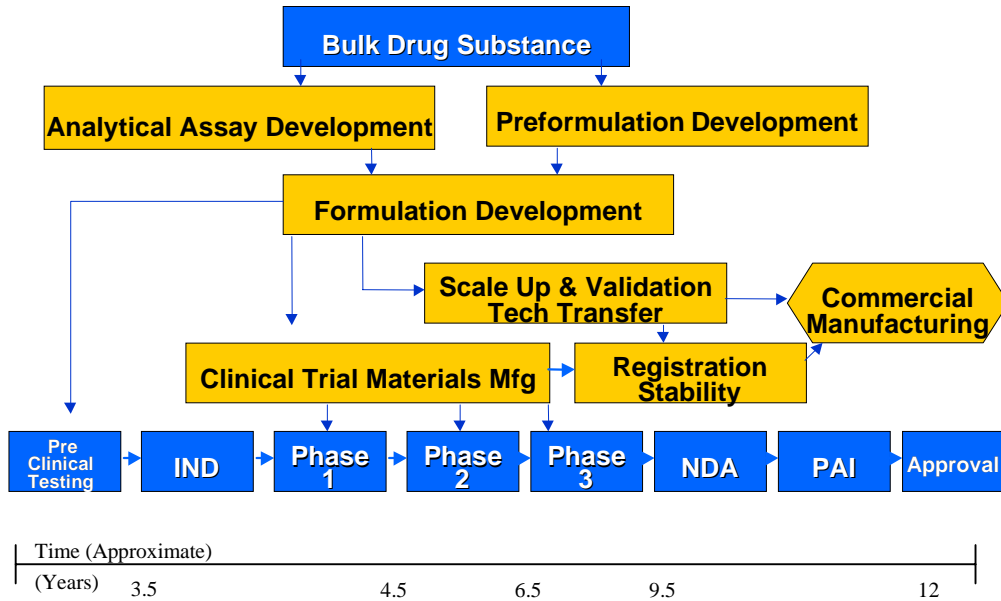
During the drug development process, an NME must undergo safety and clinical evaluation before it is approved as a commercial therapeutic product. The NME must pass through Phase I, Phase II and Phase III clinical trials prior to receiving approval. An essential part of this process is the development of an appropriate dosage form (for example, tablets, capsules or injectables).

The development of a dosage form moves in tandem with the clinical evaluation of the drug. Early formulations are used to establish therapeutic safety and efficacy. Commercial dosage formulations are developed as the NME enters Phase II clinical trials. Scale-up to commercial manufacturing batch sizes culminates in the manufacture of registration and validation batches to support regulatory filings and the launch of the commercial product.

Developing an appropriate dosage form, preparing necessary clinical trial materials and scaling-up the dosage form manufacturing to commercial scale are all part of the development process. Through these activities, it must be demonstrated that the drug can be consistently manufactured at commercial batch sizes in accordance with applicable regulatory requirements. The data recorded during development activities are included in the Chemistry, Manufacturing and Controls section of the required New Drug Application ("NDA") for the FDA. A drug must meet regulatory requirements at

all phases of the clinical trial and drug development processes or it will not be approved for human use.

The following chart shows the phases of pharmaceutical development as they relate to the clinical trial approval process:



Pre-Approval Inspection ("PAI")

Following the completion of the clinical trials, an NDA is submitted to the FDA for marketing approval. During the review process, a PAI may be conducted on the manufacturing facility listed in the NDA for the commercial manufacturing of the new drug. Those portions of the facility involved in the manufacture of the new drug may be inspected for compliance with cGMP and approved before the new drug can be marketed. Upon approval, the new drug is available for physicians to prescribe.

Post-Marketing Approval (Phase IV)

In certain cases, additional post-marketing studies are required to evaluate the long-term effects of the new drug. In all cases, companies must continue to monitor and report any adverse reactions.

Commercial Manufacturing

Commercial manufacturing in the case of Patheon relates to the manufacturing and packaging of finished dosage forms of approved drug products destined for consumer use.

APPENDIX B

GLOSSARY OF TECHNICAL TERMS

The text following the technical terms reproduced in this glossary does not in any way modify the meanings of such terms and is explanatory only.

Analytical Assay	Analytical assay is a laboratory procedure used to measure the amount of a drug substance or other component of interest contained in a drug product or pharmaceutical ingredient.
cGMPs:	Current Good Manufacturing Practices. This is a constantly evolving system of manufacturing practices adopted and implemented by companies in the pharmaceutical industry. These practices, when taken in conjunction with quality control testing, are designed to ensure that each dosage unit of every drug performs as expected when used by a patient. From time to time, standards for good manufacturing practices are promulgated by regulatory agencies such as the FDA, HPFB, MEA and EMEA.
Clinical Trials:	Studies of a drug product in humans designed to evaluate the safety and efficacy of a new drug in a particular disease condition. Clinical trials are only conducted after extensive pre-clinical studies.
Contract Research Organization (CRO):	An organization that manages clinical studies and related regulatory matters for pharmaceutical companies.
EMA:	The European Medicines Evaluation Agency is the regulatory agency which controls all aspects of the development, manufacture and commercialization of drug products for the countries of the European Union. Each country of the European Union also has its own national regulatory agency which works within the umbrella of the EMA.
FDA:	The Food and Drug Administration is the regulatory agency which controls all aspects of the development, manufacture and commercialization of drug products in the U.S. New drugs cannot be developed, or marketed for sale in the U.S. without FDA approval.
Health Products and Food Branch (HPFB):	HPFB is part of Health Canada and is the regulatory body that oversees the drug development process in Canada. New drugs cannot be marketed for sale in Canada without HPFB approval.
IND:	Investigational New Drug application. This application, submitted to the FDA, describes how a drug will be evaluated in human subjects and must be submitted before human clinical trials can be conducted. It also contains the results of pre-clinical studies.
Lyophilization:	In this process, a drug in solution is frozen and subjected to low pressure within a controlled sterile environment. The water is removed by sublimation and the drug is dried in a very gentle manner which protects sensitive molecules from degradation. Lyophilization is also known as freeze drying.

MHRA:	The Medicines and Healthcare Products Regulatory Agency is the national drug regulatory agency of the U.K.
NDA:	New Drug Application. The document submitted to the FDA to approve a drug. The NDA is required to include, among other information, preclinical and clinical data; it includes a Chemistry, Manufacturing and Controls Section which describes the dosage form, the manufacturing process and information relating to the proposed manufacturer and packager of the drug.
NDS:	New Drug Submission. Submitted to the HPFB to approve a drug, an NDS is the Canadian equivalent of an NDA.
OTC drugs:	Over-the-Counter drugs are available for sale to the general public without a physician's prescription.
PAI:	Pre-Approval Inspection. This is the FDA's inspection of a proposed manufacturer's facilities and control system during that agency's review of an NDA. This inspection is carried out as part of the agency's decision making process as to the marketability of the drug.
Phase I clinical trials:	Studies conducted on a small number of healthy volunteers to determine a drug's safety in a healthy population.
Phase II clinical trials:	Studies carried out on a larger number of patient volunteers to determine a drug's safety, efficacy and dosage range in a patient population which demonstrates a particular disease condition.
Phase III clinical trials:	Studies carried out on a sufficiently large number of patient volunteers to prove statistically that the drug is safe and effective when taken as prescribed for the treatment of a specific disease condition.
Pre-clinical studies:	Laboratory evaluations and animal studies used to assess the safety of a new drug prior to evaluation in healthy human volunteers.
Preformulation:	The chemical and physical characterization of the drug substance and the selection of an appropriate dosage form.
R _x drugs:	Prescription drugs are only available to the general public with a physician's prescription.
Scale-up and technology transfer:	The transfer of the manufacturing process from the development stage in the laboratory or pilot plant to commercial production.
Stock-keeping unit (SKU):	This refers to the particular package type and size used in the consumer distribution of a particular product.
Validation:	The planned and documented act of demonstrating that the operation of any equipment, use of any material or the implementation of any procedure, process or system will consistently lead to the expected results within pre-established limits.

APPENDIX C

AUDIT COMMITTEE CHARTER

This charter governs the operations of the *audit committee* of Patheon Inc. (the “Corporation”).

1. Definitions

1.1 Definitions of certain terms used in this charter are set out in Schedule A. Such terms are indicated in this charter in italics.

2. Audit Committee Responsibilities

2.1 Relationship with External Auditor

The external auditor must report directly to the *audit committee*.

2.2 Audit Committee Responsibilities

(1) The *audit committee* is responsible for recommending to the board of directors:

(a) the external auditor to be nominated for the purpose of preparing or issuing an auditor's report or performing other audit, review or attest services for the Corporation; and

(b) the compensation of the external auditor.

(2) The *audit committee* is directly responsible for overseeing the work of the external auditor engaged for the purpose of preparing or issuing an auditor's report or performing other audit, review or attest services for the Corporation, including the resolution of disagreements between management and the external auditor regarding financial reporting.

(3) The *audit committee* must pre-approve all *non-audit services* to be provided to the Corporation or its subsidiary entities by the Corporation's external auditor.

(4) The *audit committee* must review the Corporation's financial statements, *MD&A* and annual and interim earnings press releases before the Corporation publicly discloses this information.

(5) The *audit committee* must be satisfied that adequate procedures are in place for the review of the Corporation's public disclosure of financial information extracted or derived from the Corporation's financial statements, other than the public disclosure referred to in subsection (4), and must periodically assess the adequacy of those procedures.

(6) The *audit committee* must establish procedures for:

(a) the receipt, retention and treatment of complaints received by the Corporation regarding accounting, internal accounting controls, or auditing matters; and

(b) the confidential, anonymous submission by employees of the Corporation of concerns regarding questionable accounting or auditing matters.

(7) The *audit committee* must review and approve the Corporation's hiring policies regarding partners, employees and former partners and employees of the present and former external auditor of the Corporation.

2.3 De Minimis Non-Audit Services

The *audit committee* may satisfy the pre-approval requirement in subsection 2.2(3) if:

- (a) the aggregate amount of all the *non-audit services* that were not pre-approved is reasonably expected to constitute no more than five per cent of the total amount of fees paid by the Corporation and its subsidiary entities to the Corporation's external auditor during the fiscal year in which the services are provided;
- (b) the Corporation or the *subsidiary entity* of the Corporation, as the case may be, did not recognize the services as *non-audit services* at the time of the engagement; and
- (c) the services are promptly brought to the attention of the *audit committee* of the Corporation and approved, prior to the completion of the audit, by the *audit committee* or by one or more of its members to whom authority to grant such approvals has been delegated by the *audit committee*.

2.4 Delegation of Pre-Approval Function

(1) The *audit committee* may delegate to one or more independent members the authority to pre-approve *non-audit services* in satisfaction of the requirement in subsection 2.2(3).

(2) The pre-approval of *non-audit services* by any member to whom authority has been delegated pursuant to subsection (1) must be presented to the *audit committee* at its first scheduled meeting following such pre-approval.

2.5 Pre-Approval Policies and Procedures

The *audit committee* may satisfy the pre-approval requirement in subsection 2.2(3) if it adopts specific policies and procedures for the engagement of the *non-audit services*, if:

- (a) the pre-approval policies and procedures are detailed as to the particular service;
- (b) the *audit committee* is informed of each non-audit service; and
- (c) the procedures do not include delegation of the *audit committee's* responsibilities to management.

3. Composition of the Audit Committee

3.1 Composition

- (1) The *audit committee* must be composed of a minimum of three members.
- (2) Every *audit committee* member must be a director of the Corporation.

(3) Subject to sections 3.2, 3.3, 3.4 and 3.5, every *audit committee* member must be *independent*.

(4) Subject to sections 3.4 and 3.7, every *audit committee* member must be *financially literate*.

3.2 Controlled Companies

(1) An *audit committee* member that sits on the board of directors of an *affiliated entity* is exempt from the requirement in subsection 3.1(3) if the member, except for being a director (or member of a board committee) of the Corporation and the *affiliated entity*, is otherwise *independent* of the Corporation and the *affiliated entity*.

(2) Subject to section 3.6, an *audit committee* member is exempt from the requirement in subsection 3.1(3) if:

(a) the member would be *independent* of the Corporation but for the relationship described in paragraph 1.4(1)(b) of Schedule A;

(b) the member is not an *executive officer*, general partner or managing member of a person or company that

(i) is an *affiliated entity* of the Corporation, and

(ii) has its securities trading on a *marketplace*;

(c) the member is not an *immediate family member* of an *executive officer*, general partner or managing member referred to in paragraph (b), above;

(d) the member does not act as the chair of the *audit committee*; and

(e) the board determines in its reasonable judgement that

(i) the member is able to exercise the impartial judgement necessary for the member to fulfill his or her responsibilities as an *audit committee* member, and

(ii) the appointment of the member is required by the best interests of the Corporation and its shareholders.

3.3 Events Outside Control of Member

Subject to section 3.8, if an *audit committee* member ceases to be *independent* for reasons outside that member's reasonable control, the member is exempt from the requirement in subsection 3.1(3) for a period ending on the later of:

(a) the next annual meeting of the Corporation, and

(b) the date that is six months from the occurrence of the event which caused the member to not be *independent*.

3.4 Death, Disability or Resignation of Member

Subject to section 3.8, if the death, disability or resignation of an *audit committee* member has resulted in a vacancy on the *audit committee* that the board of directors is required to fill, an *audit committee* member appointed to fill such vacancy is exempt from the requirements in subsections 3.1(3) and (4) for a period ending on the later of:

- (a) the next annual meeting of the Corporation, and
- (b) the date that is six months from the day the vacancy was created.

3.5 Temporary Exemption for Limited and Exceptional Circumstances

Subject to section 3.6, an *audit committee* member is exempt from the requirement in subsection 3.1(3) if:

- (a) the member is not an individual described in subsection 1.4(1) of Schedule A;
- (b) the member is not an employee or officer of the Corporation, or an *immediate family member* of an employee or officer of the Corporation;
- (c) the board, under exceptional and limited circumstances, determines in its reasonable judgement that
 - (i) the member is able to exercise the impartial judgement necessary for the member to fulfill his or her responsibilities as an *audit committee* member, and
 - (ii) the appointment of the member is required by the best interests of the Corporation and its shareholders;
- (d) the member does not act as chair of the *audit committee*; and
- (e) the member does not rely upon this exemption for a period of more than two years.

3.6 Majority Independent

The exemptions in subsection 3.2(2) and section 3.5 are not available to a member unless a majority of the *audit committee* members would be *independent*.

3.7 Acquisition of Financial Literacy

Subject to section 3.8, an *audit committee* member who is not *financially literate* may be appointed to the *audit committee* provided that the member becomes *financially literate* within a reasonable period of time following his or her appointment.

3.8 Restriction on Use of Certain Exemptions

The exemptions in sections 3.3, 3.4 and 3.7 are not available to a member unless the Corporation's board of directors has determined that the reliance on the exemption will not materially adversely affect the ability of the *audit committee* to act independently and to satisfy the other requirements of this charter.

4. Authority of the Audit Committee

4.1 Authority

The *audit committee* has the authority

- (a) to engage independent counsel and other advisors as it determines necessary to carry out its duties,
- (b) to set and pay the compensation for any advisors employed by the *audit committee*, and
- (c) to communicate directly with the internal and external auditors.

5. General

5.1 Subject to by-laws, etc.

The provisions of this charter are subject to the provisions of the by-laws of the Corporation and to the applicable provisions of the *Canada Business Corporations Act* and any other applicable legislation.

5.2 Annual Review of Charter

On an annual basis, the Board will review the recommendations of the Corporate Governance Committee with respect to this charter. The Board will approve those changes to this charter that it determines are appropriate.

Approved by the Board of Directors
Patheon Inc.
June 2, 2005

SCHEDULE A

DEFINITIONS AND INTERPRETATION

1.1 Definitions

"audit committee" means the committee established by and among the board of directors of the Corporation for the purpose of overseeing the accounting and financial reporting processes of the Corporation and audits of the financial statements of the Corporation, and, if no such committee exists, the entire board of directors of the Corporation;

"audit services" means the professional services rendered by the Corporation's external auditor for the audit and review of the Corporation's financial statements or services that are normally provided by the external auditor in connection with statutory and regulatory filings or engagements;

"executive officer" of an entity means an individual who is:

- (a) a chair of the entity;
- (b) a vice-chair of the entity;
- (c) the president of the entity;
- (d) a vice-president of the entity in charge of a principal business unit, division or function including sales, finance or production;
- (e) an officer of the entity or any of its subsidiary entities who performs a policy-making function in respect of the entity; or
- (f) any other individual who performs a policy-making function in respect of the entity;

"immediate family member" means an individual's spouse, parent, child, sibling, mother or father-in-law, son or daughter-in-law, brother or sister-in-law, and anyone (other than an employee of either the individual or the individual's immediate family member) who shares the individual's home;

"marketplace" means

- (a) an exchange,
- (b) a quotation and trade reporting system,
- (c) a person or company not included in paragraph (a) or (b) that
 - (i) constitutes, maintains or provides a market or facility for bringing together buyers and sellers of securities,
 - (ii) brings together the orders for securities of multiple buyers and sellers, and
 - (iii) uses established, non-discretionary methods under which the orders interact with each other, and the buyers and sellers entering the orders agree to the terms of a trade, or
- (d) a dealer that executes a trade of an exchange-traded security outside of a marketplace, but does not include an inter-dealer bond broker;

"MD&A" has the meaning ascribed to it in National Instrument 51-102;

"National Instrument 51-102" means National Instrument 51-102 *Continuous Disclosure Obligations*; and

"non-audit services" means services other than audit services.

1.2 Meaning of Affiliated Entity, Subsidiary Entity and Control

(1) For the purposes of this charter, a person or company is considered to be an affiliated entity of another person or company if

- (a) one of them controls or is controlled by the other or if both persons or companies are controlled by the same person or company, or
- (b) the person is an individual who is
 - (i) both a director and an employee of an affiliated entity, or
 - (ii) an executive officer, general partner or managing member of an affiliated entity.

(2) For the purposes of this charter, a person or company is considered to be a subsidiary entity of another person or company if

- (a) it is controlled by,
 - (i) that other, or
 - (ii) that other and one or more persons or companies each of which is controlled by that other, or
 - (iii) two or more persons or companies, each of which is controlled by that other; or
- (b) it is a subsidiary entity of a person or company that is the other's subsidiary entity.

(3) For the purpose of this charter, "control" means the direct or indirect power to direct or cause the direction of the management and policies of a person or company, whether through ownership of voting securities or otherwise.

(4) Despite subsection (1), an individual will not be considered to control the Corporation for the purposes of this charter if the individual:

- (a) owns, directly or indirectly, ten per cent or less of any class of voting securities of the Corporation; and
- (b) is not an executive officer of the Corporation.

1.3 Meaning of Independence

(1) An audit committee member is independent if the member has no direct or indirect material relationship with the Corporation.

(2) For the purposes of subsection (1), a “material relationship” is a relationship which could, in the view of the Corporation's board of directors, be reasonably expected to interfere with the exercise of a member's independent judgement.

(3) Despite subsection (2), the following individuals are considered to have a material relationship with the Corporation:

- (a) an individual who is, or has been within the last three years, an employee or executive officer of the Corporation;
- (b) an individual whose immediate family member is, or has been within the last three years, an executive officer of the Corporation;
- (c) an individual who:
 - (i) is a partner of a firm that is the Corporation's internal or external auditor,
 - (ii) is an employee of that firm, or
 - (iii) was within the last three years a partner or employee of that firm and personally worked on the Corporation's audit within that time;
- (d) an individual whose spouse, minor child or stepchild, or child or stepchild who shares a home with the individual:
 - (i) is a partner of a firm that is the Corporation's internal or external auditor,
 - (ii) is an employee of that firm and participates in its audit, assurance or tax compliance (but not tax planning) practice, or
 - (iii) was within the last three years a partner or employee of that firm and personally worked on the Corporation's audit within that time;
- (e) an individual who, or whose immediate family member, is or has been within the last three years, an executive officer of an entity if any of the Corporation's current executive officers serves or served at that same time on the entity's compensation committee;
- (f) an individual who received, or whose immediate family member who is employed as an executive officer of the Corporation received, more than \$75,000 in direct compensation from the Corporation during any 12 month period within the last three years.

(4) Despite subsection (3), an individual will not be considered to have a material relationship with the Corporation solely because

- (a) he or she had a relationship identified in subsection (3) if that relationship ended before March 30, 2004; or
- (b) he or she had a relationship identified in subsection (3) by virtue of subsection (8) if that relationship ended before June 30, 2005.

(5) For the purposes of clauses (3)(c) and (3)(d), a partner does not include a fixed income partner whose interest in the firm that is the internal or external auditor is limited to the receipt of fixed amounts of compensation (including deferred compensation) for prior service with that firm if the compensation is not contingent in any way on continued service.

(6) For the purposes of clause (3)(f), direct compensation does not include:

- (a) remuneration for acting as a member of the board of directors or of any board committee of the Corporation, and
- (b) the receipt of fixed amounts of compensation under a retirement plan (including deferred compensation) for prior service with the Corporation if the compensation is not contingent in any way on continued service.

(7) Despite subsection (3), an individual will not be considered to have a material relationship with the Corporation solely because the individual or his or her immediate family member

- (a) has previously acted as an interim chief executive officer of the Corporation, or
- (b) acts, or has previously acted, as a chair or vice-chair of the board of directors or of any board committee of the Corporation on a part-time basis.

(8) For the purpose of section 1.3, the word “Corporation” includes a subsidiary entity of the Corporation and a parent of the Corporation.

1.4 Additional Independence Requirements

(1) Despite any determination made under section 1.3, an individual who

- (a) accepts, directly or indirectly, any consulting, advisory or other compensatory fee from the Corporation or any subsidiary entity of the Corporation, other than as remuneration for acting in his or her capacity as a member of the board of directors or any board committee, or as a part-time chair or vice-chair of the board or any board committee; or
- (b) is an affiliated entity of the Corporation or any of its subsidiary entities, is considered to have a material relationship with the Corporation.

(2) For the purposes of subsection (1), the indirect acceptance by an individual of any consulting, advisory or other compensatory fee includes acceptance of a fee by

- (a) an individual's spouse, minor child or stepchild, or a child or stepchild who shares the individual's home; or
- (b) an entity in which such individual is a partner, member, an officer such as a managing director occupying a comparable position or executive officer, or occupies a similar position (except limited partners, non-managing members and those occupying similar positions who, in each case, have no active role in providing services to the entity) and which provides accounting, consulting, legal, investment banking or financial advisory services to the Corporation or any subsidiary entity of the Corporation.

(3) For the purposes of subsection (1), compensatory fees do not include the receipt of fixed amounts of compensation under a retirement plan (including deferred compensation) for prior service with the Corporation if the compensation is not contingent in any way on continued service.

1.5 Meaning of Financial Literacy

For the purposes of this charter, an individual is financially literate if he or she has the ability to read and understand a set of financial statements that present a breadth and level of complexity of accounting issues that are generally comparable to the breadth and complexity of the issues that can reasonably be expected to be raised by the Corporation's financial statements.