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Questioning Market Leaders For Long Term Investors

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COMPANY INTERVIEW

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Cansolv Technologies Inc.

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Cansolv Technologies Inc.



*This is a TWST
Interview with Colin
Ryan, CFO of Cansolv
Technologies Inc.*

SECTOR – POLLUTION & TREATMENT CONTROLS

(WAR614) TWST: Could you begin by giving us a brief overview of Cansolv Technologies?

Mr. Ryan: Cansolv Technologies Inc. was founded in 1997 by a group of entrepreneurial technology developers from Union Carbide (now Dow Corporation). This team had worked together in the late 1980s and early 1990s developing CANSOLV SO₂ Scrubbing, a chemistry-enabled process for flue gas cleaning. The genius of this technology is that it took a chemical process widely used in natural gas processing and made it work for scrubbing pollutants from industrial flue gases. After five years of development and \$30 million dollars, Union Carbide terminated the CANSOLV program as it realigned its corporate strategy. Cansolv Technologies purchased the technology in 1997. After successfully completing the development, CTI signed the first license in 1999 and the first three plants started up in 2002. All three have met or exceeded their performance targets for emissions and energy usage. CTI is currently designing the largest CANSOLV scrubber to date for commissioning in 2006. Several others are in the planning and engineering stages.

People often ask me what a CANSOLV scrubber looks like. It is an integrated package of process equipment including, pumps, heat exchangers, an absorption tower and the piping and

controls to tie it all together. Depending on the size and gas flow, the capital cost of the unit may be between \$3 and \$50 million. On a typical project CTI will earn between 10% and 25% of the total amount for engineering, a license, special equipment and the chemical absorbent. We have intentionally limited our scope of supply to the highest value and most knowledge intensive parts of the project as these carry the highest margins and require the smallest investment in working capital. Channel partners and third parties provide the balance of the project scope. When the unit is up and running, recurring yearly revenues to CTI are between 1% and 2% of the capital cost.

The market for industrial capital goods is an interesting one. It is cyclical and ebbs and flows with cycle of business investment. Furthermore, clients are risk averse given the size of the individual investments and the multi-year commitment it entails. So the product development and technology adoption cycle in our market tends to be long, averaging about 15 years. We actually beat the average when we commissioned our first three units 13 years after the kickoff of the CANSOLV research program. But now we're there and the technological risk perceived by our clients is much lower, which has given us improved traction in the marketplace.

TWST: Who are your customers? Is it everybody?

Mr. Ryan: We sell to everyone with an industrial smokestack. This includes manufacturing, utilities oil and gas and mining and metallurgical firms. Our first adopters were Conoco-Philips, Bayer and Noranda. Our next round of projects is for clients of similar stature.

TWST: As you look at Cansolv's business over the next couple of years, what changes or developments do you anticipate?

Mr. Ryan: What clients are looking for in this market is value for their money. This is showing up as increased interest for engineered pollution control solutions rather than traditional cookie cutter technologies. This has given rise to the most recent buzzword in our business which is "multi-pollutant control." Given that firms have to comply with ever more stringent standards for SO_x, NO_x, mercury, particulates, volatile organic compounds and other pollutants in their exhaust gases, they are demanding technologies that can kill two or more birds with one stone. Millions of dollars in capital and operating costs can be saved doing this. Our SO₂-NO_x-Mercury R&D program has positioned us to respond to this trend.

Another trend that is beneficial to our business and shows no sign of abating is the volatility of natural gas. Prices keep setting records and demand follows apace. What we are seeing now is a greater consensus that the price of gas will stay high. This favors heavy fuel fired power generation with the required pollution control technology. One of the most exciting projects we were asked to quote was a petroleum coke fired cogen plant in the most restrictive air pollution district in the world. This will prove in no uncertain terms that pollution control has come of age and that we can indeed burn coal or coke as cleanly as natural gas.

Because our business is fundamentally affected by environmental legislation, we are always scanning the horizon to see what is around the corner. The Clear Skies Agreement, which will likely be passed in one form or another in 2005 will give considerable lift to our market even if it falls short of the original targets for SO₂, NO_x and mercury.

TWST: What are Cansolv's competitive advantages and what sets it apart from your competition?

Mr. Ryan: The short answer is best in class performance, flexibility and cost. The Cansolv SO₂ scrubbing process can reduce SO₂ in a gas stream 10 thousand fold, that is to say from 10% down to 10 parts per million. Instead of using a consumable absorbent such as lime, the Cansolv Process recycles the absorbent up to 50,000 times, making the secondary effluent from our process extremely low. Furthermore, our SO₂ and NO_x processes can be engineered to work for constraints such as limited plot space, limited water resources or production of a specific value added sulfur byproducts including elemental sulfur and sulfuric acid.

"CTI signed the first license in 1999 and the first three plants started up in 2002. All three have met or exceeded their performance targets for emissions and energy usage. CTI is currently designing the largest CANSOLV scrubber to date for commissioning in 2006. Several others are in the planning and engineering stages."

TWST: What are the greatest opportunities for Cansolv over the next, say, two to three years? Is there a chain of events that could lead Cansolv to substantially exceed expectations in the future?

Mr. Ryan: There are several trends providing some lift for us in the marketplace. As I mentioned before, the rise in the price of natural gas appears to be permanent and reflective of generally tight supply situation. This will tip the scales once again toward heavy fuels and they will have to be designed with state of the art emissions control. Secondly, impending federal mercury legislation and lower caps for SO₂ and NO_x emissions (Clear Skies or equivalent) are setting the stage for a great

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Corporate Business Description

Cansolv Technologies (CTI) is a leading provider of low effluent regenerable emission control technologies (SO₂, NO_x, Mercury and CO₂). The company was formed in 1997 as a spinoff of Union Carbide's CANSOLV SO₂ scrubbing process. CTI acquired the rights to the process and has since developed new processes for simultaneously scrubbing both NO_x and mercury and capturing CO₂ from industrial flue gases.

The groundbreaking regenerable SO₂ process has been installed in commercial applications in the US, Canada and Belgium, achieving scrubbing performance to below 10 parts per million SO₂ with liquid effluent of less than 0.5% of the SO₂ load.

The largest CANSOLV SO₂ Scrubber to date (equivalent to a 200 MWe coal fired power plant) is currently being designed for an oil refinery scrubbing application. The first CANSOLV multipollutant SO₂-NO_x-Mercury) scrubber is scheduled for April 2005 commissioning. It will be built by COALSOLV, a CTI joint venture and marketing partner

CoalSolv is a joint venture created to serve the specific needs of coal fired power and industrial boiler operators. The partnership draws from a broad knowledge base covering coal mining & handling, ash handling, emissions control, process engineering, project management and plant operations. CoalSolv offers complete Build-Own-Operate CANSOLV emission control units including:

- CANSOLV® SO₂ Scrubbing
- CANSOLV® SO₂-NO_x & SO₂-NO_x-Mercuryβ CANSOLV® AquaNO_x™ & AquaNO_x-Mercury
- CANSOLV® CO₂ Capture

Contact: CoalSolv LLC Attn: Steve Sears, President, 4 North Fourth Street Richmond, Virginia 23219 Tel.: 804-782-1633

Products

Regenerable scrubbing processes are designed to restore the absorbent to its original state such that it can be used again. CANSOLV processes are engineered for durability, lasting 50000 absorption cycles (or 10 years). NO_x regeneration yields nitrogen while SO₂ regeneration creates a pure stream of pure SO₂

CANSOLV® SO₂ Scrubbing System

The CANSOLV® SO₂ Scrubbing System is the leading regenerable sulfur dioxide (SO₂) scrubbing process. This patented technology uses an aqueous amine solution to achieve high efficiency selective absorption of sulfur dioxide from a large variety of gas streams. The scrubbing by-product is pure, water saturated SO₂ gas recovered by steam stripping. The process is similar to conventional amine-based gas treating units in refineries and natural gas processing. The CANSOLV® SO₂ Scrubbing System and absorbent have excellent health and safety properties. The regenerable absorbent eliminates the high cost of consumable absorbents, while its high capacity and selectivity reduce capital costs. Effluents from the process are minimal.

CANSOLV® SO₂SAFE™ System

The CANSOLV® SO₂SAFE™ System, which is an extension of the CANSOLV® SO₂ Scrubbing System process, reduces the hazard of SO₂ storage and transport by dissolving the gas in a high capacity solvent, instead of compressing it to liquid state, thereby limiting the release of gaseous SO₂ in case of a leak or spill. For more information concerning the CANSOLV® SO₂SAFE™ process, please refer to Abstract 3—The SO₂SAFE™ Technology for Storage and Transport of Sulfur Dioxide.

decade to come in the US. In Europe, the IPPC (Integrated Pollution Prevention and Control) legislative framework will create demand in Europe as well. In the oil and gas sector, low sulfur gasoline and diesel regulation is creating demand for extra sulfur recovery capacity which in turn provides opportunities for CTI.

“CTI is poised to grow along three axes: from taking market share by exploiting our technological advantage, from growing our project product-service mix to better serve clients outside our beachhead market, from providing value added aftermarket services such as remote monitoring and operation as well as laboratory solvent analysis.”

TWST: Would you introduce us to your key management team?

Mr. Ryan: Cansolv was founded by some extraordinary people six years ago and they are still the people running it today. Dr. Leo Hakka, our Chief Technology Officer, is a leading gas absorption chemist with 20 patents to his credit over a distinguished 40 year career in the field. Dr. Paul Parisi, our VP Engineering, led the team that successfully brought the invention from the lab to the field and made the business case for CANSOLV SO₂ Scrubbing in the oil and gas sector. His marketing work allowed CTI to secure a beachhead in the refinery market. John Sarlis, our Vice President of R&D, is a leading sulfur expert and process designer. He has successfully negotiated research partnerships that have leveraged CTI’s own research capability and have brought in new knowledge essential to improving our processes. On the business side, the team is rounded out by our President, Marcel Ayotte, and myself. Marcel is a seasoned R&D and operations manager from Union Carbide and founder of CTI. He has managed

CTI’s relationships with investors, government, suppliers and clients as well as running the back office and during the startup phase of the company. I joined the firm in May 2003 as CFO to structure the next round of expansion financing and lend project expertise to the group.

TWST: What has been the funding history of Cansolv and who have been the investors?

Mr. Ryan: Cansolv was initially financed by a local labor sponsored VC fund. At a later financing round in 2000 Dr. Harvey Griggs, a Toronto-based angel, joined the ranks of CTI investors. Harvey is a serial entrepreneur and CTI is his seventh private investment. He has taken an active role in each and they have all been profitable investments.

TWST: Where do you find yourselves spending most of your time these days?

Mr. Ryan: My primary mandate is to raise expansion stage capital and that has me working very hard putting together the business plan and then marketing it to investors. I have recently started doing the latter and I am now fielding a lots of calls and requests for information from investors.

I also spend a lot of time on business development which involves sourcing and negotiating development, marketing and distribution contracts essential to carrying out our corporate strategy. On this front, one of our main concerns right now is working out our marketing and distribution plan for East Asia.

TWST: What are the major concerns or risks facing Cansolv Technologies now and possibly in the future? What can go wrong?

Mr. Ryan: We have some concerns about how our intellectual property finds its way to some parts of the world. We are very committed to offering the technology to all regions that can benefit from it. To do so, we need to structure

marketing and distribution in such a way as to protect our IP in countries where there is a history of patent infringement

TWST: What's to stop another player from coming in and challenging Cansolv Technologies?

Mr. Ryan: In our business the barriers to entry are extremely high. Consider that the initial adopter of a gas cleaning technology is investing several million dollars. If he chooses a new technology because it promises better performance, the perceived technological risk can easily erase the benefits of better performance in the project analysis. So getting the first job is extraordinarily difficult and this is why industrial technologies have traditionally very long development times. Thankfully, CTI is past that step and we are safely now in the category of proven technologies.

Looking at barriers to entry and competition from our current position, our technology is by a good margin the leading regenerable scrubbing technology on the market. It is protected by patents and trademarks and CANSOLV is now a recognized brand in our space. Finally, if an attempt was made to create a competing process that mimicked our technology, it would be very hard for them to acquire the knowledge to deliver it. We have considerable knowledge assets in the form of pilot and commercial plant data, computer models for process simulation, engineering processes and of course our people. To put it in software terms, it would be tough to crack our code and repackage it. This is not to say that we are complacent about this. We are keenly aware of competitive threats and we have taken several steps to ensure adequate protection of our business.

TWST: Is your own background more in business or in science or engineering?

Mr. Ryan: I have a degree in mechanical engineering from McGill University and an MBA from HEC Montreal. I come from a project management background focused on integrating technologies into process industries. As such, I analyzed the risk and return profile of large project investments for my clients. I am therefore very much at home with the operational, financial and technological issues that CTI's clients face and that is really why the firm was such a good fit for me.

TWST: How well is the company understood by potential investors?

Mr. Ryan: Not well at all. Part of the reason for this is the complexity of the market and the way it is affected by commodity prices, gas prices and the regulatory environment. The other misunderstood part of our business is the relationship between players in the project value chain. I do a lot of work explaining this to investors as I believe it is key to understanding the value in Cansolv Technologies.

In terms of our business model, CTI is best understood as an industrial process equivalent of an ERP software provider. We are akin to the software developer and others do the integration, hardware and network infrastructure. Yet like the software developer, we license to the end user and as such we are at the top of the value chain. The client chooses us first and foremost.

TWST: If you were to sit down today with a group of potential investors, what two or three reasons would you give them for making a commitment to the company?

Mr. Ryan: Investors in small firms are fundamentally concerned with growth and CTI is poised to grow along three axes: from taking market share by exploiting our technological advantage, from growing our project product-service

mix to better serve clients outside our beachhead market, from providing value added aftermarket services such as remote monitoring and operation as well as laboratory solvent analysis.

Up to 2003, it has made sense for CTI to limit our scope of involvement in project delivery to minimize our capital requirements while the technology was being proven out by the first adopters. Now as we look from the top of the value chain, there are areas where our involvement will allow us to achieve cost reductions as we deliver more projects. This will allow us to achieve revenue and profit growth while passing on savings to our clients and making our technology available to a broader range of users.

I'd like to underline the opportunity for aftermarket service growth as well. If one looks at technology providers like IBM, GE, United Technologies and others, a key driver of revenue and profit growth in the last 15 years has been value added aftermarket services. While it may be slightly premature to compare us to S&P 500 companies, the logic is the same: we know our technology best and we are best positioned to support our clients in using it. Providing aftermarket service has the compound advantage of bringing information from the field back to the R&D process

and supporting us to improve our product. Services are definitely in our future.

TWST: Are there any other points of discussion that I may have left out?

Mr. Ryan: One of the things that I'd like to talk about is CTI's partnerships.. Last year we formed Coalsolv LLC, a joint venture with Massey Energy (NYSE:MEE) and HG Engineering to deliver our technology to industrial and utility sector coal users. We are currently working on agreements for marketing and distribution in Asia and Europe as well. We are also working with R&D and technology partners to leverage our internal capability in these areas.

TWST: Thank you. (KL)

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