

CANADIAN SUPPLEMENT TO
RESTATED MANAGEMENT'S DISCUSSION AND
ANALYSIS

of Financial Condition and Results of Operations,
for the three months ended July 31, 2007

This document supplements the Restated Management's Discussion and Analysis for July 31, 2007 and has been prepared pursuant to Section 5.2 of National Instrument 51-102 – Continuous Disclosure Obligations



CANADIAN SUPPLEMENT TO JULY 31, 2007 INTERIM RESTATED MANAGEMENT'S DISCUSSION AND ANALYSIS

September 4, 2007

The interim unaudited financial statements of MDS Inc. (MDS or the Company) for the quarter ended July 31, 2007 are reported in United States (US) dollars and have been restated in accordance with US generally accepted accounting principles (US GAAP). As part of the Company's Canadian filing requirements, we are providing this supplement (Canadian Supplement) to our restated management's discussion and analysis (Restated MD&A) prepared in accordance with US GAAP that restates, based on financial information of MDS reconciled to Canadian generally accepted accounting principles (Canadian GAAP), those parts of our Restated MD&A that would contain material differences if they were based on financial statements prepared in accordance with Canadian GAAP. The Canadian Supplement should be read in conjunction with our restated unaudited financial statements and Restated MD&A included in our interim report for the three month period ended July 31, 2007 prepared in accordance with US GAAP (Restated Interim Report) and our 2007 annual financial statements and related MD&A included in our annual report for the fiscal year ended October 31, 2007 (Annual Report). Note 15 of our interim restated financial statements explains and quantifies the material differences between US GAAP and Canadian GAAP on the Company's financial condition and results of operations.

The following contains forward-looking statements and should be read in conjunction with the factors set forth in the "Caution regarding forward-looking statements" section of the 2007 annual MD&A contained in the Financial Review portion of our Annual Report.

This supplement has been prepared as of the date set out above and has not been updated to reflect new facts, events or circumstances since that date.

In addition to measures based on US GAAP and Canadian GAAP, we use terms such as adjusted earnings before interest, taxes, depreciation and amortization (adjusted EBITDA) and adjusted earnings per share (adjusted EPS). These terms are not defined by US GAAP or Canadian GAAP and readers should refer to "Use of non-GAAP measures" in our 2007 annual MD&A.

Amounts are in millions of US dollars, except per share amounts and where otherwise noted.

Summary of difference between US GAAP and Canadian GAAP

The differences between US GAAP and Canadian GAAP that have the most significant impact on the Company's financial condition and results of operations for the three month period ended July 31, 2007 include accounting for: joint ventures, investment tax credits, research and development, stock-based compensation and hedge contracts.

The primary difference between Canadian GAAP and US GAAP affecting the consolidated revenues and operating margin is that under Canadian GAAP proportionate consolidation is used to report the results of our joint ventures within MDS Analytical Technologies, whereas under US GAAP we apply the method of equity accounting. For the third quarter of 2007, we reported \$13 million less revenue and \$17 million less operating income under US GAAP than we would have reported under Canadian GAAP (\$13 million less and \$17 million less, respectively for the third quarter of 2006). Under US GAAP, the income from the joint ventures is included in equity earnings, which were \$15 million in the third quarter of 2007 (\$15 million in the third quarter of 2006). Under Canadian GAAP, this amount was included in operating income as part of the proportionate consolidation. There is no significant impact to adjusted EBITDA from this accounting difference.

Other differences in operating income and adjusted EBITDA are listed below.

- **Non-refundable investment tax credits (ITCs)** are treated as a reduction of expenditure under Canadian GAAP and a reduction of income tax under US GAAP. In the third quarter of 2007, there were \$1 million (\$3 million in the third quarter of 2006) of ITCs which when calculated based on US GAAP, increased our operating loss and reduced adjusted EBITDA, as compared to Canadian GAAP. This difference affects our three segments MDS Pharma Services, MDS Nordion and MDS Analytical

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- **Research and Development (R&D)** expenditures may be capitalized under Canadian GAAP if certain criteria are met, however these expenditures are expensed in the period they are incurred under US GAAP. In the third quarter of 2007, the \$5 million (\$3 million in third quarter of 2006) of R&D capitalized under Canadian GAAP resulted in a reduction of adjusted EBITDA when calculated based on US GAAP, compared to Canadian GAAP. In the second quarter of 2007, our operating loss was increased by \$3 million (\$2 million in third quarter of 2006) under US GAAP due to \$2 million (\$1 million of 2006) of amortization under Canadian GAAP relating to previously capitalized R&D. This difference affects our MDS Analytical Technologies segment in both 2006 and 2007, and MDS Pharma Services in 2006.
- Due to a difference in **valuation methods for stock-based compensation** under US GAAP and Canadian GAAP, our operating loss was reduced and adjusted EBITDA was higher by \$2 million for the third quarter of 2007 (nil in 2006) when calculated based on US GAAP, compared to Canadian GAAP. This difference only affects Corporate and Other.
- The other difference, which is described in Note 15 to our restated interim financial statements, is related to hedges.

There are no differences between US GAAP and Canadian GAAP in the adjustment used in calculating adjusted EBITDA and adjusted EPS for the third quarters of 2007 or 2006. In calculating adjusted EBITDA and adjusted EPS for the year-to-date, the significant changes to the adjusting items include the following two items:

- In 2007, capitalized R&D was charged to restructuring in MDS Pharma Services under Canadian GAAP. Under US GAAP, these expenditures may not be capitalized and therefore there is no adjustment.
- In 2006, under Canadian GAAP, ITCs were netted against MAPLE settlement in MDS Nordion. Under US GAAP these are treated as reduction to income tax. The adjustment related to MAPLE ITCs only impacts adjusted EBITDA

Management's discussion and analysis under Canadian GAAP

Please refer to the Company's previously filed Interim Report for July 31, 2007 for our corresponding management's discussion and analysis under Canadian GAAP. The differences between US GAAP and Canadian GAAP, described above, impact the discussion and analysis in each of the "MDS Inc.," "MDS Pharma Services", "MDS Nordion", "MDS Analytical Technologies" and "Corporate and Other" sections of our previously filed MD&A. The "Income taxes" section of our previously filed MD&A is primarily affected by the ITCs. The "US GAAP Reconciliation" section in our previously filed MD&A is superseded by the "Restatement to US GAAP" section of our Restated MD&A.

For additional information and details, readers are referred to the 2007 annual financial statements and management's discussion and analysis for 2007 and the Company's 2007 Annual Information Form (AIF), all of which are published separately and are available at www.mdsinc.com and at www.sedar.com. In addition, the Company's 40-F filing is available at www.sec.gov.