

PyroGenesis Canada Inc.

**Condensed Consolidated
Interim Financial Statements**

Three and Six Months Ended June 30, 2011 and 2010

(Unaudited)

PyroGenesis Canada Inc.

Three and Six Months Ended
June 30, 2011 and 2010

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UNAUDITED INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

In accordance with National Instrument 51-102 released by the Canadian Securities Administrators, the Company discloses that its auditors have not reviewed the unaudited consolidated financial statements for the period ended June 30, 2011.

PyroGenesis Canada Inc.

Condensed Consolidated Interim Statements of Financial Position

(Unaudited) At	June 30, 2011 \$	December 31, 2010 [note 15] \$	January 1, 2010 [note 15] \$
Assets			
<i>Current assets</i>			
Cash and cash equivalents	194,514	237,291	722,941
Deposits in escrow [note 11 (iv)]	3,596,375	-	-
Accounts receivable	576,252	576,551	868,525
Sales tax receivable	8,885	114,509	295,752
Investment tax credits receivable [note 6]	4,699,505	3,800,000	3,177,000
Prepaid expenses	42,850	49,239	27,164
	9,118,381	4,777,590	5,091,382
Machinery and equipment [note 7]	1,205,228	1,338,334	353,201
Licenses [note 8]	7,689,246	463,574	540,837
	18,012,855	6,579,498	5,985,420
Liabilities			
<i>Current liabilities</i>			
Bank indebtedness	3,861,000	3,341,000	1,190,000
Accounts payable and accrued liabilities [note 9]	2,253,610	1,497,833	1,041,437
Current portion of obligation under capital lease	-	3,873	13,315
Billings in excess of costs and profits on uncompleted contracts	447,664	57,413	2,423,911
Long-term debt - current portion [note 10]	120,000	-	-
	6,682,274	4,900,119	4,668,663
Non-interest bearing loans - company under common control	-	-	100,738
Obligation under capital lease	-	-	3,873
Loans - other	665,423	465,423	465,423
Long-term debt [note 10]	8,620,940	1,000,000	1,000,000
	15,968,637	6,365,542	6,238,697
Shareholders' equity [note 11]			
Common shares	9,118,454	4,026,588	2,472,271
Share capital - preferred	1,093,800	1,093,800	-
contributed surplus	110,306	-	-
Retained earnings	(8,278,342)	(4,906,432)	(2,725,548)
	2,044,218	213,956	(253,277)
	18,012,855	6,579,498	5,985,420

Approved on behalf of the board:

.....Director

.....Director

See accompanying Notes to the Financial Statements

PyroGenesis Canada Inc.

Condensed Consolidated Interim Statement of Operations and Comprehensive Loss

(Unaudited)

	Three months Ended June 30		Six Months Ended June 30	
	2011 \$	2010 \$	2011 \$	2010 \$
Revenue	167,054	1,928,911	1,374,705	3,857,566
Expenses				
Cost of sales and services	1,223,181	989,134	2,054,063	3,118,660
Selling, general and administrative	1,408,890	939,072	2,392,215	1,744,358
Financing charges	204,950	62,849	302,564	121,744
	2,837,021	1,991,055	4,748,842	4,984,762
Loss from operations	(2,669,967)	(62,144)	(3,374,137)	(1,127,196)
Other income	-	171	2,227	985
Net loss	(2,669,967)	(61,973)	(3,371,910)	(1,126,211)
Provision for future income taxes				
Total comprehensive loss - beginning of period	(5,608,375)	(3,789,786)	(4,906,432)	(2,725,548)
Total comprehensive loss - end of period	(8,278,342)	(3,851,759)	(8,278,342)	(3,851,759)
Loss per share <i>[note 15]</i>				
Basic	\$(0.053)	\$(0.001)	\$(0.069)	\$(0.024)
Weighted average number of shares outstanding	49,954,710	41,371,377	48,655,907	41,371,377

See accompanying Notes to the Financial Statements

PyroGenesis Canada Inc.

Condensed Consolidated Interim Statement of Changes in Equity

(Unaudited)

On March 22, 2011, the Class A shares were subdivided on a 21.08 for 1 basis. Prior year numbers have been restated to reflect the stock subdivision

	Number of common shares \$	Share capital \$	Number of preferred shares \$	Share capital \$	Contributed surplus \$	Deficit \$	Total equity \$
Balance - January 1, 2010	47,371,377	2,472,271	-	-	-	(2,725,548)	(253,277)
Total comprehensive loss for the period	-	-	-	-	-	(1,126,211)	(1,126,211)
Balance - June 30, 2010	47,371,377	2,472,271	-	-	-	(3,851,759)	(1,379,488)
Preferred shares issued	-	-	1,093,800	1,093,800	-	-	1,093,800
Cash deposit for shares	-	1,750,000	-	-	-	-	1,750,000
Share issue costs	-	(195,683)	-	-	-	-	(195,683)
Net loss during year	-	-	-	-	-	(1,054,673)	(1,054,673)
Balance - December 31, 2010	47,371,377	4,026,588	1,093,800	1,093,800	-	(4,906,432)	213,956
Non-brokered private placement <i>[note 11]</i>	312,500	250,000	-	-	-	-	250,000
Shares issued for deposit above	2,187,500	-	-	-	-	-	-
Convertible FIER loan <i>[note 11]</i>	-	1,000,000	-	-	-	-	1,000,000
Professional fees related to FIER loan	-	(103,102)	-	-	-	-	(103,102)
Private placement subscription receipts <i>[note 11]</i>	-	4,066,600	-	-	-	-	4,066,600
Commissions and fees private placement	-	(470,224)	-	-	-	-	(470,224)
Stock options private placement	-	(110,306)	-	-	110,306	-	-
Net loss during the period	-	-	-	-	-	(3,371,910)	(3,371,910)
	49,871,377	8,659,556	1,093,800	1,093,800	110,306	(8,278,342)	1,585,320
Purchase price of IGIC net assets	1,300,000	1,040,000	-	-	-	-	1,040,000
Share issuance costs	-	(581,102)	-	-	-	-	(581,102)
Balance - June 30, 2011	51,171,377	9,118,454	1,093,800	1,093,800	110,306	(8,278,342)	2,044,218

See accompanying Notes to the Financial Statements

PyroGenesis Canada Inc.

Condensed Consolidated Interim Statement of Cash Flows

(Unaudited)

	Three months Ended June 30		Six Months Ended June 30	
	2011 \$	2010 \$	2011 \$	2010 \$
Cash flows provided (used) by				
Operating activities				
Net loss and comprehensive loss	(2,669,967)	(61,973)	(3,371,910)	(1,126,211)
Items not requiring an outlay of cash:				
Expenses paid through issuance of options	-	-	110,306	-
Amortization of machinery and equipment	76,931	29,062	152,337	58,124
Amortization of licenses	348,312	25,111	410,754	38,632
	(2,244,724)	(7,800)	(2,698,513)	(1,029,455)
Net change in non-cash operating working capital items <i>[note 12]</i>	899,332	(1,614,514)	(3,249,844)	(654,638)
	(1,345,392)	(1,622,314)	(5,948,357)	(1,684,093)
Investing activities				
Increase in loan receivable - company under common control	-	107,150	-	-
Acquisition of patents	-	-	(7,636,426)	-
Purchase of machinery and equipment	(12,782)	(3,990)	(19,231)	(33,282)
Cash acquired as a result of amalgamation	-	-	471,202	-
	(12,782)	103,160	(7,184,455)	(33,282)
Financing activities				
Increase in bank indebtedness	800,000	1,340,000	520,000	1,340,000
Repayment of obligation under capital lease	-	-	(3,873)	(17,189)
Non-interest bearing loans company under common consideration	-	(100,738)	-	(100,738)
Increase in loans – other	200,000	-	200,000	-
(Repayment) proceeds from long-term debt	92,338	-	7,740,940	-
Proceeds from issuance of common shares	-	-	4,632,968	-
	1,092,338	1,239,262	13,090,035	1,222,073
Decrease in cash	(265,836)	(279,892)	(42,777)	(495,302)
Cash and cash equivalents - beginning of period	460,350	507,531	237,291	722,941
Cash and cash equivalents - end of period	194,514	227,639	194,514	227,639

See accompanying Notes to the Financial Statements

PyroGenesis Canada Inc.

Notes to the Condensed Consolidated Interim Financial Statements

(Unaudited)

For the three and six months ended June 30, 2011 and 2010

1. Nature of operations and going concern disclosure

(a) Nature of operations

PyroGenesis Canada Inc. (the "Company") was incorporated on June 5, 2006. The Company owns patents of advanced waste treatment systems technology and provides such systems to its clients. The Company is domiciled at 1744 William Street, Suite 200.

2. Basis of preparation

(a) Statement of compliance:

These condensed interim financial statements of the Company have been prepared in accordance with International Accounting Standard ("IAS") 34 Interim Financial Reporting. These International Financial Reporting Standards ("IFRS") condensed interim financial statements for part of the period covered by the IFRS annual financial statements and IFRS 1 First-time Adoption of International Financial Reporting Standards has been applied. These condensed interim financial statements do not include all of the necessary information required for full annual financial statements in accordance with IFRS.

Previously the Company prepared its interim and annual consolidated financial statements in accordance with Canadian generally accepted accounting principles ("Canadian GAAP").

An explanation of how the transition to IFRS has affected the Company's accounting policies as compared to those disclosed in the Company's annual audited Financial Statements for the period ended December 31, 2010 issued under GAAP is provided in Note 15 along with reconciliations presenting the impact of the transition to IFRS for the comparative periods of January 1, 2010, for the six months ended June 30, 2010, and for the twelve months ended December 31, 2010.

(b) Functional and Presentation Currency

These interim financial statements are presented in Canadian dollars, which is the Company's functional currency.

(c) Basis of measurement

The condensed interim financial statements have been prepared on the historical cost basis except for the following item in the statement of financial position:

- Financial instruments classified as fair value through profit or loss and available for sale are measured at fair value.

(d) On July 11, 2011, PyroGenesis amalgamated with Industrial Growth Income Corporation ("IGIC").

These financial statements have been prepared on the basis that the amalgamation was effective March 31, 2011.

Each holder of a PyroGenesis share received one amalgamation share. Each holder of an IGIC share received 0.32298 amalgamation shares. Upon Completion of the transaction IGIC shareholders owned approximately 2.2% of the amalgamation shares and PyroGenesis shareholders owned 97.8%. Accordingly, PyroGenesis was considered to be the acquirer. The amalgamation was accounted for using the purchase method.

The fair value of the shares issued to IGIC was based on the share value used in private placements.

The consideration of 1,300,000 shares at \$1,040,000 was allocated to identifiable assets and liabilities of IGIC as follows:

PyroGenesis Canada Inc.

Notes to the Condensed Consolidated Interim Financial Statements

(Unaudited)

For the three and six months ended June 30, 2011 and 2010

2. Basis of preparation - continued

	\$
Cash	467,790
Sales tax receivable	2,966
Accounts payable	(11,858)
Purchase price of net assets	458,898
Shares issue costs	581,102
Total consideration	1,040,000

IGIC share capital and contributed surplus have been eliminated upon consolidation. The purchase price of the net assets acquired has been recorded in share capital.

3. Significant accounting policies

(A) Revenue recognition

Revenues relating to research and equipment contracts are recognized on the percentage-of-completion basis. The degree of completion is assessed based on the proportion of labour costs incurred to date, in relation to performance, compared to total labour costs anticipated to provide the service and other deliverables required under the entire contract. Provisions are made for the entire amount of expected losses, if any, in the period in which they are first determinable. The percentage-of-completion method requires the use of estimates to determine the recorded amount of revenues and work-in-progress. Given this estimation process, it is possible that changes in future conditions could cause a material change in the recognized amount of revenues and unbilled work-in-progress and accrued expenses.

(B) Foreign currency translation

The financial statements are presented in Canadian dollars, which is the Company's functional currency. Foreign currency balances are translated at year-end exchange rates for monetary items and at historical rates for non-monetary items. Revenues and expenses are translated using average exchange rates prevailing at the time of the transaction. Translation gains or losses are included in the determination of operations and comprehensive loss.

(C) Financial instruments

Financial assets

i) Initial recognition

A financial instrument is any contract that gives rise to a financial asset of one party and a financial liability or equity instrument of another party. Financial assets and financial liabilities are recognized on the balance sheet when the Company becomes a party to contractual provisions of the instrument. On initial recognition, all financial instruments must be measured at fair value which is the amount of consideration that would be agreed upon in an arm's length transaction between knowledgeable willing parties who are under no compulsion to act. Subsequent to initial recognition, the fair value of financial instruments is dependent on the purpose for which the financial assets were acquired or issued, their characteristics and the Company's designation of such instruments. Transaction costs are included in the initial measurement of financial instruments except financial instruments classified as fair value through profit or loss.

IAS 39, Financial Instruments: Recognition and measurement require that all financial assets be classified as financial assets of fair values through profit or loss, held-to-maturity, available-for-sale or loans and receivables.

The Company's financial assets include cash and cash equivalents, deposits in escrow, accounts receivable and sales tax receivable and investment tax credits receivable.

PyroGenesis Canada Inc.

Notes to the Condensed Consolidated Interim Financial Statements

(Unaudited)

For the three and six months ended June 30, 2011 and 2010

3. Significant accounting policies - continued

ii) Subsequent measurement

Financial assets at fair value through profit or loss: Financial assets at fair value through profit or loss measured at fair value, with gains or losses, are recorded in the statement of operations and comprehensive income (loss) for the period in which they arise. A financial asset at fair value through profit or loss includes assets held for trading and financial assets that are so designated. Held-for-trading securities are usually held for a short term and are actively traded.

Loans and receivables: Loans and receivable financial assets are measured at amortized cost using the effective interest rate method. Interest income calculated using the effective interest rate method is recorded in financing income in the period in which it arises.

Gains and losses are recognized in the statement of operations and comprehensive income (loss) when these assets are impaired or derecognized.

Held-to-maturity: Non-derivative financial assets that are purchased and have a fixed maturity date and which management has the intention and the ability to hold to maturity are classified as held-to-maturity. These instruments are accounted for at amortized cost using the effective interest rate method and charged to income in the period of amortization. The Company currently does not hold any of these assets.

Gain and losses are recognized in the statement of operations and comprehensive income (loss) when the assets are impaired or derecognized.

Available-for-sale: Available-for-sale financial assets are non-derivative financial assets and are measured at fair value, except for investments in equity instruments that do not have a quoted market price in an active market, which are measured at cost. Unrealized gains and losses, including the effect of changes in foreign exchange rates, are recognized directly in Other Comprehensive Income. Upon derecognition of the financial asset, the cumulative gains or losses, previously recognized in Accumulated Other Comprehensive Income ("AOCI") are reclassified to net income.

Financial liabilities

i) Initial recognition

IAS 39, Financial Instruments: Recognition and Measurement requires that all financial liabilities be classified as: financial liabilities at fair value through profit or loss, loans and borrowings, or as derivatives designated as hedging instruments. Classification is determined at the time of initial recognition. Initially, financial liabilities are recognized at fair value.

The Company's financial liabilities include bank indebtedness, accounts payable and accrued liabilities, obligation under capital lease, loans and long-term debt.

ii) Subsequent measurement

Financial liabilities at fair value through profit or loss: Financial liabilities at fair value through profit or loss include financial liabilities that are held for trading (acquired for purpose of selling in the near term) or financial instruments that are so designated.

Financial liabilities are measured at fair value. Gains and losses on liabilities held-for-trading are recognized in earnings.

Loans and borrowings: Financial liabilities classified as loans and borrowings are measured at amortized cost using the effective interest method. Interest expense is recorded in financing expense in the period.

PyroGenesis Canada Inc.

Notes to the Condensed Consolidated Interim Financial Statements

(Unaudited)

For the three and six months ended June 30, 2011 and 2010

3. Significant accounting policies - continued

As a result, the following classifications were determined:

- i) Cash and cash equivalents, bank indebtedness and deposits in escrow are classified as financial assets at fair value through profit or loss.
- ii) Accounts receivable, sales tax receivable and investment tax credits receivable are classified as loans and receivables.
- iii) Accounts payable and accrued liabilities, loans and long-term debt, including interest payable, as well as capital lease obligations are classified as loans and borrowings, all of which are measured at amortized cost using the effective interest rate method.

(D) Impairment of financial assets

At each reporting date the carrying amounts of financial assets, other than those to be measured at fair value through profit or loss, are assessed to determine whether there is objective, significant evidence of impairment (e.g. a debtor is facing serious financial difficulties, or there is a substantial change in the technological, economic, legal or market environment of the debtor). For equity instruments, a significant or prolonged decline in fair value is objective evidence for a possible impairment. The Company has defined criteria for the significance and duration of a decline in fair value.

The amount of the impairment loss on loans and receivables is measured as the difference between the carrying amount of the asset and the present value of estimated future cash flows (excluding expected future credit losses that have not been incurred), discounted at the original effective interest rate of the financial asset. The amount of the impairment loss is recognized in profit or loss. If, in a subsequent reporting period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized, the previously recognized impairment loss is reversed and recognized in profit or loss. The impairment loss on loans and receivables is recorded using allowance accounts. The decision to account for credit risks using an allowance account or by directly reducing the receivable depends on the estimated probability of the loss of receivables. When receivables are assessed as uncollectible the impaired asset is derecognized.

If an available-for-sale financial asset is impaired, the difference between its cost (net of any principal payment and amortization) and its current fair value, less any impairment loss previously recognized in the statement of operations and comprehensive income (loss) is reclassified from direct recognition in equity to the statement of operations and comprehensive income (loss). Reversals with respect to equity instruments classified as available-for-sale are not recognized in the statement of operations and comprehensive loss. A reversal of an impairment loss on a debt instrument is reversed through the statement of operations and comprehensive income (loss) if the increase in fair value of the instrument can be objectively related to an event occurring after the impairment loss is recognized in income.

(E) Offsetting financial instruments

Financial assets and liabilities are offset and the net amount presented in the statement of financial position if, and only if, the Company has a legal right to offset the amounts and there is an intention to either settle on a net basis or to realize the assets and settle the liabilities simultaneously.

PyroGenesis Canada Inc.

Notes to the Condensed Consolidated Interim Financial Statements

(Unaudited)

For the three and six months ended June 30, 2011 and 2010

3. Significant accounting policies - continued

(F) Future income taxes

i) Current income tax

Current income tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted by the balance sheet date.

ii) Deferred income tax

The Company follows the liability method for calculating deferred income taxes. Differences between the amounts reported in the financial statements and the tax bases are applied to tax rates in effect to calculate the deferred tax liability. The effect of any change in income tax rates is recognized in the current period income. Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply to the period when the asset is realized or the liability is settled, based on tax rates and tax laws that have been enacted or substantively enacted by the balance sheet date. Discounting of deferred tax assets and liabilities is not permitted. Deferred tax assets and liabilities are offset if a legally enforceable right exists to set off current tax assets against current tax liabilities and the deferred taxes related to the same taxable entity and the same taxation authority. Deferred tax is provided in full for all temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements, except when the temporary differences arises from the initial recognition of goodwill, or of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss.

(G) Earnings (loss) per share

The basic loss per share is computed by dividing the net loss by weighted average number of common shares outstanding during the year. The diluted loss per share reflects the potential dilution of common share equivalents, such as outstanding stock options, in the weighted average number of common shares outstanding during the year, if dilutive. For this purpose, the treasury stock method is used for the assumed proceeds upon the exercise of stock options that are used to purchase common shares at the average market price during the year.

(H) Property, plant and equipment

Property, plant and equipment are measured at cost less accumulated depreciation and accumulated impairment losses if applicable. Cost includes expenditures that are directly attributable to the acquisition of the asset.

When major parts of an item of property, plant and equipment have different useful lives, they are accounted for separately.

Property, plant and equipment are amortized from the acquisition date.

Amortization is calculated using the declining balance method as follows:

Computer hardware	45%
Computer software	50%
Machinery	20%
Computer hardware under capital lease	45%

PyroGenesis Canada Inc.

Notes to the Condensed Consolidated Interim Financial Statements

(Unaudited)

For the three and six months ended June 30, 2011 and 2010

3. Significant accounting policies - continued

Depreciation methods, useful lives and residual values are reviewed at each financial year-end and adjusted prospectively if appropriate.

Gains and losses on derecognition (on disposal or when it is determined that there are no future economic benefits) of property, plant and equipment are determined by comparing the net disposal proceeds with the carrying amount of property, plant and equipment, and are recognized in the statement of operations and comprehensive income (loss) in the period of derecognition.

(I) Impairment - Non-financial assets

The carrying amounts of the Company's non-financial assets are assessed at each reporting date to determine whether there is an indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated.

The recoverable amount of an asset or cash-generating unit (CGU) is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. Assets that cannot be tested individually are grouped into the smallest independent group of assets that generate cash inflows from continuing use.

An impairment loss is recognized if the carrying amount of an asset or its CGU exceeds its recoverable amount. Impairment losses are recognized in the statement of operations and comprehensive income (loss). Impairment losses recognized in respect of the CGU are allocated first to reduce the carrying amount of goodwill allocated to the units, and then to reduce the carrying amounts on a pro-rata basis of the other assets in the unit.

Impairment losses recognized in prior periods are assessed at each reporting date as to whether there are any indications that the previously recognized losses may no longer exist or may be decreased. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognized for the asset in prior years.

(J) Government assistance and investment tax credits

Investment tax credits are comprised of scientific research and experimental development tax credits. Government assistance and investment tax credits are recognized when there is reasonable assurance of their recovery using the cost reduction method. Investment tax credits are subject to the customary approvals by the pertinent tax authorities. Adjustments required, if any, are reflected in the year when such assessments are received.

(K) Intangible assets

Acquired intangible assets are measured at cost on initial recognition. Following initial recognition, intangible assets are carried at cost less any accumulated amortization and any accumulated impairment losses.

Intangible assets with finite lives are amortized over the useful life of the asset and assessed for impairment whenever there is an indication of impairment. The amortization period and method for an intangible asset with a finite life is reviewed at least at each financial year end. Changes in useful life or consumption are accounted for by changing the amortization period or method, and are treated prospectively as changes in accounting estimates. Amortization expense on the intangible assets with finite lives is recognized in the statement of operations and comprehensive income (loss)

Gains or losses arising from derecognition are recognized in the statement of operations and comprehensive income (loss) at the time that the asset is derecognized.

PyroGenesis Canada Inc.

Notes to the Condensed Consolidated Interim Financial Statements

(Unaudited)

For the three and six months ended June 30, 2011 and 2010

3. Significant accounting policies - continued

Intangible assets represent that value of licences that were acquired from a related party during the period.

The estimated useful life of the licence acquired is 10 years. Amortization is calculated on a straight line basis over the life of the asset.

Research and development costs

Research costs are charged to earnings in the year they are incurred, net of related investment tax credits. Development costs are charged to earnings in the year they are incurred net of related investment tax credits unless they meet specific criteria related to technical, market and financial feasibility in order to be recognized as an intangible asset:

- the technical feasibility of completing the intangible asset so that it will be available for use or sale;
- its intention to complete and its ability to use or sell the asset;
- how the asset will generate future economic benefits;
- the availability of resources to complete the asset; and
- the ability to measure reliably the expenditure during development.

Amortization of the asset begins when development is complete. During the period of development, the asset is tested annually for impairment.

(L) Cash and cash equivalents

Cash and cash equivalents include short term investments with maturities of 90 days or less when acquired.

(M) General provisions

Provisions are recognized when the Company has a present obligation as a result of a past event, it is probable that an outflow of resources will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. The present value of expected future cash outflows is recognized as a liability and the increase to the liability due to the passage of time is recorded as a finance expense.

Warranty provision

At the time of sale, a warrant cost is recorded. The warranty provision is based on management estimates of the expected number of warranty claims and the expected cost of these claims. The warranty provision is based on past experience and on the nature of the contract.

(N) Leases

Leases where the Company assumes substantially all the risks and rewards of ownership are classified as finance leases. At the commencement of the lease, the leased property is measured at the lower of its fair value and the present value of the minimum lease payments.

Lease payments are apportioned between finance charges and reduction of the outstanding liability. So as to produce a constant periodic rate of interest on the remaining balance of the liability.

Operating lease payments are expensed in the statement of operations and comprehensive income (loss) on a straight line basis over the lease term.

PyroGenesis Canada Inc.

Notes to the Condensed Consolidated Interim Financial Statements

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For the three and six months ended June 30, 2011 and 2010

4. Significant accounting judgments, estimates and assumptions

The preparation of financial statements requires management to make judgments, estimates and assumptions based on currently available information that affect the reported amounts of assets, liabilities and contingent liabilities at the date of the financial statements and reported amounts of revenues and expenses during the reporting period. Estimates and judgments are continuously evaluated and are based on managements experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. However, actual results could differ from those estimated. By their very nature, these estimates are subject to measurement uncertainty and the effect on the financial statements of future periods could be material.

In the process of applying the Company's accounting policies, management has made the following judgments, estimates, and assumptions which have the most significant effect on the amounts recognized in the financial statements:

(a) Revenue recognition

Revenues relating to research and equipment contracts are recognized on the percentage-of-completion basis. The degree of completion is assessed based on the proportion of labour costs incurred to date, in relation to performance, compared to total labour costs anticipated to provide the service and other deliverables required under the entire contract. Provisions are made for the entire amount of expected losses, if any, in the period in which they are first determinable. The percentage-of-completion method requires the use of estimates to determine the recorded amount of revenues and work-in-progress. Given this estimation process, it is possible that changes in future conditions could cause a material change in the recognized amount of revenues and unbilled work-in-progress and accrued expenses.

(b) Warranty provision

At the time of sale, a warrant cost is recorded. The warranty provision is based on management estimates of expected number of warranty claims and the expected cost of these claims. The warranty provision is based on past experience and on the nature of the contract and is reviewed each reporting date by management. Should these estimates differ materially from actual warranty cost, the Company may incur costs that differ from the provision. Such costs are recorded in costs of sales and services.

5. Changes in accounting policies and practices

Recent accounting pronouncements

IFRS 9 Financial Instruments: Classification and Measurement

IFRS 9 as issued reflects the first phase of the IASB's work on the replacement of IAS 39 and applies to classification and measurement of financial assets and liabilities as defined in IAS 39. The standard is effective for annual periods beginning on or after January 1, 2013. The adoption of IFRS 9 is not expected to have a significant impact on the financial statements.

IFRS 13 Fair Value Measurements

IFRS 13 establishes a single source of guidance for fair value measurements, when fair value is required or permitted by IFRS. The key features of IFRS 13 include: a single framework for measuring fair value while requiring enhanced disclosures when fair value is applied, fair value would be defined as the "exit price", and concepts of "highest and best use" and "valuation premise" would be relevant only for non-financial assets and liabilities. IFRS 13 is effective for annual periods beginning on or after January 1, 2013 and early adoption is permitted. The Company has not yet assessed the impact of the new standard on the financial statements.

PyroGenesis Canada Inc.

Notes to the Condensed Consolidated Interim Financial Statements

(Unaudited)

For the three and six months ended June 30, 2011 and 2010

6. Government assistance

During the three and six month period ended June 30, 2011 research and development tax credits in the amount of \$393,472 and \$899,505 respectively (2010 - \$469,377 and \$938,754) have been included as a reduction of \$1,185,827 and \$1,914,760 respectively (2010 - \$679,830 and \$1,359,661) of related research and development expenses.

Government assistance received during the three and six month period ended June 30, 2011 in the amount of \$Nil and \$27,719 respectively (2010 - \$11,389 and \$22,779) respectively has been included as a reduction of related expenses.

Research and development tax credits in the amount of \$1,877,508 have been included as a reduction of \$2,719,321 of related research and development expenses incurred during the year ended December 31, 2010.

Government assistance received during the year ended December 31, 2010 in the amount of \$45,557 have been included as a reduction of related expenses.

7. Machinery and equipment

	Cost \$	Accumulated Depreciation \$	Net book value \$
Balance, January 1, 2010	683,597	330,396	353,201
Acquisitions	1,134,455	-	1,134,455
Depreciation for the period	-	149,322	(149,322)
Disposals	-	-	-
Balance, December 31, 2010	1,818,052	479,718	1,338,334
Acquisitions	19,231	-	19,231
Depreciation for the period	-	152,337	(152,337)
Disposals	-	-	-
Balance, June 30, 2011	1,837,283	632,055	1,205,228

8. Licenses

Intangible assets are made up of licenses as follows:

	Cost \$	Accumulated Amortization \$	Net book value \$
Balance, January 1, 2010	772,625	231,788	540,837
Acquisitions	-	-	-
Amortization for the year	-	77,263	(77,263)
Disposals	-	-	-
Balance, December 31, 2010	772,625	309,051	463,574
Acquisitions	7,636,426	-	7,636,426
Amortization for the period	-	410,754	(410,754)
Disposals	-	-	-
Balance, June 30, 2011	8,409,051	719,805	7,689,246

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(Unaudited)

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8. Licenses – continued

On March 19, 2011, an agreement was signed between PyroGenesis and a company controlled by a shareholder. Per the agreement, intellectual property and know-how was sold to PyroGenesis for \$14,280,000 from a company controlled by a shareholder and will be payable in equal monthly instalments of \$40,000. The payments commence on April 1, 2011 until December 31, 2040. The fair market value of this property is estimated to be \$7,636,426.

The intellectual property and know-how was amortized on a straight line basis over the remaining useful life of 5.79 years.

9. Accounts payable and accrued liabilities

	June 30, 2011 \$	December 31, 2010 \$
Accounts payable trade	975,333	495,357
Accrued liabilities	589,475	532,348
Accounts payable to a company under common control	172,220	167,132
Accounts payable - shareholder	386,035	150,000
Accounts payable - trust beneficially owned by the shareholder	130,547	152,996
	2,253,610	1,497,833

10. Long-term debt

Long term debt of \$7,636,426 was assumed on the sale of the licenses described in Note 8. This debt is payable in monthly instalments of \$40,000 from April 1, 2011 until December 31, 2040 and bears interest at an implicit rate of 4.85% per annum. Accrued interest from March 19, 2011 to June 30, 2011 of \$104,514 was added to this debt.

Long-term debt also includes a \$1,000,000 loan due June 30, 2012 with interest paid monthly at 15% per annum compounded monthly. The loan is secured by a second rank hypothec on the building which is beneficially owned by a person related to the controlling shareholders, an additional hypothec of \$75,000, and personal guarantees by the shareholders.

11. Shareholders' equity

- (i) On March 21, 2011, the holder of the 1,093,800 class F shares of PyroGenesis, waived and renounced any and all rights to receive dividends or redemption of these shares. Furthermore, the holder agreed to grant PyroGenesis the sole right to demand the exchange of all 1,093,800 class F shares for a total of 1,367,250 Class A shares of PyroGenesis.
- (ii) On March 22, 2011, the Class A shares of PyroGenesis were consolidated on a 0.0485097 for one basis and on March 29, 2011 the shares were subdivided on a 21.08 for one basis.
- (iii) On March 29, 2011, PyroGenesis completed a non brokered private placement for a total of 312,500 Class A shares at a price of \$0.80 per share for gross proceeds of \$250,000.

PyroGenesis Canada Inc.

Notes to the Condensed Consolidated Interim Financial Statements

(Unaudited)

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11. Shareholders equity - continued

- (iv) On March 30, 2011, PyroGenesis completed a private placement of 5,083,250 subscription receipts to acquire Class A shares at a subscription price of \$0.80 per subscription receipt for net proceeds of \$3,596,375 after a cash commission paid to the agents of \$296,786 and professional fees of \$173,438. On closing, the agents will receive 355,827 options at a price of \$0.80 which can be exercised until March 30, 2012.

In accordance with the Black Scholes pricing model, PyroGenesis has allocated a value of \$0.31 to the options for a total cost of \$110,306 which has been credited to contributed surplus. The following assumptions under the Black Scholes model were used to arrive at this cost:

Risk free interest rate	1.35%
Expected volatility	100%
Expected dividend yield	nil
Expected life	1 year

- (v) On March 22, 2011, FIER Croissance Durable ("FCD") signed a convertible debenture agreement with the company.

The \$1,000,000 convertible debenture is due December 31, 2012 and bears interest at 15% per annum. Interest on the debenture is due as of April 1, 2011. The convertible debenture will convert automatically into 1,388,889 shares upon the completion of the Qualifying Transaction. These statements have been prepared on the basis that the debenture will convert into shares. Net proceeds from the debenture were \$896,898 after payment of fees of \$103,102 which was charged against share capital.

PyroGenesis Canada Inc.

Notes to the Condensed Consolidated Interim Financial Statements

(Unaudited)

For the three and six months ended June 30, 2011 and 2010

11. Supplemental disclosure of expenses and cash flow information

Net changes in non-cash components of operating working capital

	<u>Three months ended June 30</u>		<u>Six months ended June 30</u>	
	2011	2010	2011	2010
	\$	\$	\$	\$
Decrease (increase) in:				
Deposits in escrow	-	-	(3,596,375)	-
Accounts receivable	(21,392)	192,967	299	90,559
Sales tax receivable	(5,919)	-	108,590	295,752
Investment tax credits receivable	(393,472)	(479,118)	(899,505)	(938,754)
Prepaid expenses	(10,686)	(5,000)	6,389	(5,000)
Increase (decrease) in:				
Accounts payable and accrued liabilities	883,137	440,064	740,507	341,602
Billings in excess of costs and profits on uncompleted contracts	447,664	(1,763,427)	390,251	(438,797)
	899,332	(1,614,514)	(3,249,844)	(654,638)

12. Other information

The Company is exposed to gains and losses as a result of foreign currency exchange fluctuations. Included in cost of sales and services is a foreign exchange loss of \$3,936 and a loss of \$13,107 for the three and six month period ended June 30, 2011 respectively (three and six month period ended June 30, 2010, a gain of \$30,205 and a loss of \$49,782 respectively).

13. Related party transactions

During the three and six months period ended June 30, 2011, rent was charged by a trust that is beneficially owned by some of the shareholders of the company in the amount of \$26,827 and \$56,321 respectively (2010 - \$29,493 and \$58,783). At June 30, 2011 these amounts were not paid and have been included in the accounts payable and accrued liabilities.

During the three and six months period ended June 30, 2011, interest on long-term debt was charged by a trust that is beneficially owned by some of the shareholders of the Company in the amount of \$4,300 and \$8,300 respectively (2010 - \$4,000 and \$8,000). Interest on long-term debt was also charged by a shareholder in the amount of \$2,500 and \$5,500 respectively (2010 - \$3,000 and \$6,000). Interest on long-term debt has not been paid and a balance of \$83,647 (2010 - \$44,390) is included in accounts payable and accrued liabilities.

During the three and six month periods ended June 30, 2011, fees of \$15,000 and \$30,000 respectively (2010 - \$15,000 and \$25,000) were paid to a director.

During the three and six month periods ended June 30, 2011, rent of \$110,100 and \$220,200 (2010 - \$110,100 and \$220,200) was paid to a company under common control. A balance due of \$172,219 (2010 - \$132,853) is included in accounts payable and accrued liabilities.

These transactions are in the normal course of business and are measured at the exchange amount which is the amount of consideration established and agreed to by the related parties.

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Notes to the Condensed Consolidated Interim Financial Statements

(Unaudited)

For the three and six months ended June 30, 2011 and 2010

14. Loss per share

Due to an expected loss for the entire current period, non incremental shares are included in calculating the dilutive loss per share because the effect would be anti-dilutive.

15. First time adoption of IFRS

The Company has prepared its financial statements in accordance with Canadian GAAP for all periods up to including the year ended December 31, 2010. These interim financial statements for the six month period ended June 30, 2011 are prepared in accordance with International Financial Reporting Standards ("IFRS"). The Company has prepared these condensed interim financial statements which comply with IFRS applicable for periods beginning on or after January 1, 2011 and the significant accounting policies meeting those requirements are described in note 3.

The Company has prepared its opening balance sheet using IFRS as at January 1, 2010, the date of transition to IFRS. IFRS 1 "First-time Adoption of International Financial Reporting Standards" allows first-time adopters certain exemptions from the general requirement to apply IFRS retrospectively.

Estimates:

Hindsight is not used to revise estimates.

Estimates that were previously made under Canadian GAAP were not revised for application of IFRS. An exception to this is, revisions to reflect differences in accounting policies.

PyroGenesis Canada Inc.

Notes to the Condensed Consolidated Interim Financial Statements

(Unaudited)

For the three and six months ended June 30, 2011 and 2010

15. First time adoption of IFRS - continued

The following is a reconciliation of the balance sheet at January 1, 2010 from Canadian GAAP to IFRS:

	Previous GAAP as at January 1, 2010 \$	Adjustments on Transition to IFRS \$	IFRS as at January 1, 2010 \$
Assets			
<i>Current assets</i>			
Cash and cash equivalents	722,941		722,941
Accounts receivable	868,525		868,525
Sales tax receivable	295,752		295,752
Investment tax credits receivable	3,177,000		3,177,000
Prepaid expenses	27,164		27,164
	5,091,382		5,091,382
Machinery and equipment	353,201		353,201
Licenses	540,837		540,837
	5,985,420		5,985,420
Liabilities			
<i>Current liabilities</i>			
Bank indebtedness	1,190,000		1,190,000
Accounts payable and accrued liabilities	1,041,437		1,041,437
Current portion of obligation under capital lease	13,315		13,315
Billings in excess of costs and profits on uncompleted contracts	2,423,911		2,423,911
	4,668,663		4,668,663
Non-interest bearing loans - company under common control	100,738		100,738
Obligation under capital lease	3,873		3,873
Loans - other	465,423		465,423
Long-term debt	1,000,000		1,000,000
	6,238,697		6,238,697
Shareholders' equity			
Share capital - preferred	2,472,271		2,472,271
Deficit	(2,725,548)		(2,725,548)
	(253,277)		(253,277)
	5,985,420		5,985,420

PyroGenesis Canada Inc.

Notes to the Condensed Consolidated Interim Financial Statements

(Unaudited)

For the three and six months ended June 30, 2011 and 2010

15. First time adoption of IFRS - continued

The following is a reconciliation of the balance sheet at June 30, 2010 from Canadian GAAP to IFRS:

	Previous GAAP as at June 30, 2010 \$	Adjustments on Transition to IFRS \$	IFRS as at June 30, 2010 \$
Assets			
<i>Current assets</i>			
Cash and cash equivalents	227,639		227,639
Accounts receivable	777,966		777,966
Financing charges	4,115,754		4,115,754
Prepaid expenses	32,164		32,164
	5,153,523		5,153,523
Machinery and equipment	328,359		328,359
Licenses	502,205		502,205
	5,984,087		5,984,087
Liabilities			
<i>Current liabilities</i>			
Bank indebtedness	2,530,000		2,530,000
Accounts payable and accrued liabilities	1,383,039		1,383,039
Billings in excess of costs and profits on uncompleted contracts	1,985,114		1,985,114
	5,898,153		5,898,153
Loans - other	465,423		465,423
Long-term debt	1,000,000		1,000,000
	7,363,576		7,363,576
Shareholders' equity			
Common shares	2,472,271		2,472,271
Deficit	(3,851,760)		(3,851,760)
	(1,379,489)		(1,379,489)
	5,984,087		5,984,087

PyroGenesis Canada Inc.

Notes to the Condensed Consolidated Interim Financial Statements

(Unaudited)

For the three and six months ended June 30, 2011 and 2010

15. First time adoption of IFRS - continued

The following is a reconciliation of the statement of comprehensive income (loss) for the three month period ended June 30, 2010 from Canadian GAAP to IFRS.

	Previous GAAP as at June 30, 2010 \$	Adjustments on Transition to IFRS \$	IFRS as at June 30, 2010 \$
Revenue	3,857,566		3,857,566
Expenses			
Cost of sales and services	3,080,028	38,632 ⁽⁴⁾	3,118,660
Selling, general and administrative	1,686,234	58,124 ⁽⁴⁾	1,744,358
Interest on long term debt	121,744	-	121,744
Amortization of machinery and equipment	58,124	(58,124) ⁽⁴⁾	-
Amortization of licenses	38,632	(38,632) ⁽⁴⁾	-
	4,984,762	-	4,984,762
Loss from operations	(1,127,196)	-	(1,127,196)
Other income	985	-	985
Net loss	(1,126,211)	-	(1,126,211)
Deficit - beginning of period	(2,725,548)	-	(2,725,548)
Deficit - end of period	(3,851,759)	-	(3,851,759)

PyroGenesis Canada Inc.

Notes to the Condensed Consolidated Interim Financial Statements

(Unaudited)

For the three and six months ended June 30, 2011 and 2010

15. First time adoption of IFRS - continued

The following is a reconciliation of the balance sheet at December 31, 2010 from Canadian GAAP to IFRS:

	Previous GAAP as at December 31, 2010 \$	Adjustments on Transition to IFRS \$	IFRS as at December 31, 2010 \$
Assets			
<i>Current assets</i>			
Cash and cash equivalents	237,291		237,291
Accounts receivable	576,551		576,551
Sales tax receivable	114,509		114,509
Investment tax credits receivable	3,800,000		3,800,000
Prepaid expenses	49,239		49,239
	4,777,590		4,777,590
Machinery and equipment	1,338,334		1,338,334
Licenses	463,574		463,574
	6,579,498		6,579,498
Liabilities			
<i>Current liabilities</i>			
Bank indebtedness	3,341,000		3,341,000
Accounts payable and accrued liabilities	1,497,833		1,497,833
Current portion of obligation under capital lease	3,873		3,873
Billings in excess of costs and profits on uncompleted contracts	57,413		57,413
	4,900,119		4,900,119
Loans - other	465,423		465,423
Long-term debt	1,000,000		1,000,000
	6,365,542		6,365,542
Shareholders' equity			
Share capital	4,026,588		4,026,588
Share capital - preferred	1,093,800		1,093,800
Deficit	(4,906,432)		(4,906,432)
	213,956		213,956
	6,579,498		6,579,498

PyroGenesis Canada Inc.

Notes to the Condensed Consolidated Interim Financial Statements

(Unaudited)

For the three and six months ended June 30, 2011 and 2010

15. First time adoption of IFRS - continued

The following is a reconciliation of the statement of comprehensive income (loss) for the year ended December 31, 2010 from Canadian GAAP to IFRS.

	Previous GAAP as at December 31, 2010 \$	Adjustments on Transition to IFRS \$	IFRS as at December 31, 2010 \$
Revenue	7,715,131	-	7,715,131
Expenses			
Cost of sales and services	6,160,056	77,263	6,237,319
Selling, general and administrative	3,242,047	149,323	3,391,370
Financing charges	292,126	-	292,126
Amortization of machinery and equipment	149,323	(149,323) ⁽⁴⁾	-
Amortization of licenses	77,263	(77,263) ⁽⁴⁾	-
	9,920,815	-	9,920,815
Loss from operations	(2,205,684)	-	(2,205,684)
Other income	24,800	-	24,800
Net loss	(2,180,884)	-	(2,180,884)
Deficit - beginning of period	(2,725,548)	-	(2,725,548)
Deficit - end of period	(4,906,432)	-	(4,906,432)

PyroGenesis Canada Inc.

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(Unaudited)

For the three and six months ended June 30, 2011 and 2010

15. First time adoption of IFRS - continued

Reconciliation of Canadian GAAP to IFRS - continued

IFRS requires an entity to reconcile equity, comprehensive income and cash flows from prior periods.

The first time adoption of IFRS did not have an impact on equity and cash flows. The adoption of IFRS resulted in some reclass adjustments to the statement of operations and comprehensive income (loss).

The following explains significant differences between previous historical Canadian GAAP accounting policies and IFRS accounting policies, that pertain specifically to the Company.

(1) property, plant and equipment

Canadian GAAP - The cost model is used for all property, plant and equipment

IFRS - May use either the cost model or a revaluation model

Reconciliation - The Company has elected to use the cost method and as such there is no impact to property, plant and equipment balances.

(2) Impairments

a) Recoverable amount

Canadian GAAP - Undiscounted expected future cash flows are compared to the carrying amount and an impairment loss, if any, is recorded for the excess of the carrying amount over the fair value.

IFRS - Impairment loss is based on the excess of the carrying amount over the recoverable amount. The recoverable amount is the higher of the assets fair value less costs value in use. Value in use is the discounted expected future cash flows from the asset.

Reconciliation - The Company determined that the adoption of this standard does not result in any changes to property, plant and equipment or intangible assets.

b) Reversal of impairments

Canadian GAAP - Reversals of impairment losses are disallowed.

IFRS - Reversals of certain impairment to assets losses other than goodwill, are allowed if certain criteria are met.

Reconciliation - The Company determined that the adoption of this standard does not result in any change to property, plant and equipment or intangible assets.

(3) Provisions

Canadian GAAP - A provision is required when payment is considered "likely" and can be reasonably estimated. For measurement purposes, the lower end of a range of estimates is used.

IFRS - A provision is required if the payment is considered "probable", which requires less certainty than the criteria Canadian GAAP assessment of "likely". For measurement purposes the mid-point of a range of estimates is used.

Reconciliation - The Company determined that the adoption of this standard does not result in any adjustments to the financial statements.

PyroGenesis Canada Inc.

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15. First time adoption of IFRS - continued

(4) Income statement presentation

Canadian GAAP - Income statement expenditure can be presented as a mix of classification by function and classification by nature.

IFRS - The income statement expenditure must all be classified by function or all be classified by nature.

Reconciliation -The Company has elected to classify expenses by function.

As a result, amortization of machinery and equipment has been reallocated to selling, general and administrative expense and amortization of licenses has been reallocated to costs of sales and services.