

UNAUDITED CONDENSED INTERIM 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 financial statements for the period ended September 30, 2012.

PyroGenesis Canada Inc.

Condensed Interim Statement of Financial Position

(Unaudited) At	September 30, 2012 \$	December 31, 2011 \$
Assets		
<i>Current assets</i>		
Cash and cash equivalents	1,124,249	481,396
Accounts receivable [note 5]	173,608	1,158,850
Sales tax receivable	72,446	64,531
Investment tax credits receivable [note 6]	399,931	1,944,518
Prepaid expenses	102,409	50,522
Total current assets	1,872,643	3,699,817
Machinery and equipment [note 7]	1,697,185	1,460,823
Licenses and intellectual property [note 8]	5,937,164	6,984,969
Total assets	9,506,992	12,145,609
Liabilities		
<i>Current liabilities</i>		
Bank indebtedness	-	240,000
Accounts payable and accrued liabilities [note 9]	2,002,095	2,414,353
Billings in excess of costs and profits on uncompleted contracts	850,762	606,202
Loans - other [note 11]	328,455	548,050
Long-term debt - current portion [note 12]	-	976,396
Total current liabilities	3,181,312	4,785,001
Loans - other [note 11]	7,680,953	7,762,388
Total liabilities	10,862,265	12,547,389
Shareholders' equity [note 13]		
Common shares	12,177,808	10,596,651
Contributed surplus	3,286,650	821,341
Other equity	-	30,966
Deficit	(16,819,731)	(11,850,738)
	(1,355,273)	(401,780)
	9,506,992	12,145,609

Approved on behalf of the board:

"P. Peter Pascali" P. Peter Pascali

"Alan Curleigh" Alan Curleigh

See accompanying Notes to the Financial Statements

PyroGenesis Canada Inc.

Condensed Interim Statement of Comprehensive Loss

(Unaudited)

	<u>Three months Ended</u>		<u>Nine Months Ended</u>	
	<u>September 30</u>		<u>September 30</u>	
	2012	2011	2012	2011
	\$	\$	\$	\$
Revenue	516,595	1,909,231	2,101,735	3,283,938
Expenses				
Cost of sales and services	1,121,276	1,962,530	3,652,438	4,201,592
Selling, general and administrative	1,041,685	1,932,554	3,093,902	3,987,970
Financing charges	96,392	179,209	334,503	606,710
	2,259,353	4,074,293	7,080,843	8,796,272
Loss from operations	(1,742,758)	(2,165,062)	(4,979,108)	(5,512,334)
Other income	177	44,639	10,115	46,863
Public company listing	-	(694,877)	-	(694,877)
Total comprehensive loss	(1,742,581)	(2,815,300)	(4,968,993)	(6,160,348)
Basic and fully diluted loss per share	\$(0.027)	\$(0.049)	\$(0.080)	\$(0.112)
Weighted average number of common shares outstanding – basic and diluted	63,538,649	57,308,730	62,090,909	54,923,320

See accompanying Notes to the Financial Statements

PyroGenesis Canada Inc.

Condensed Interim Statement of Changes in Equity

(Unaudited)

Nine months ended September 30

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 Brokers warrants, share purchase warrants, and options	Contributed surplus \$	Other \$	Deficit \$	Total equity \$
Balance - January 1, 2012	59,114,094	10,596,651	3,505,827	821,341	30,966	(11,850,738)	(401,780)
Short form prospectus	4,424,555	2,022,022	4,424,555	1,517,622	-	-	3,539,644
Cash payment – brokers – short form prospectus <i>[note 13]</i>	-	(234,000)	-	-	-	-	(234,000)
Warrant payment – brokers – short form prospectus <i>[note 13]</i>	-	(78,978)	309,719	78,978	-	-	-
Other professional fees related to short form prospectus <i>[note 13]</i>	-	(127,887)	-	-	-	-	(127,887)
Stock based compensation (Directors and management)	-	-	-	800,962	-	-	800,962
New stock option <i>[note 13]</i>	-	-	926,000	15,199	-	-	15,199
Repricing of stock options <i>[note 13]</i>	-	-	-	52,548	-	-	52,548
Options forfeited	-	-	(280,000)	-	-	-	-
Repayment of convertible FIER loan <i>[note 12]</i>	-	-	-	-	(30,966)	-	(30,966)
Expiry of agent's warrants <i>[note 13]</i>	-	-	(355,827)	-	-	-	-
Net loss during the period	-	-	-	-	-	(4,968,993)	(4,968,993)
Balance – September 30, 2012	63,538,649	12,177,808	8,530,274	3,286,650	-	(16,819,731)	(1,355,273)

...continued

See accompanying Notes to the Financial Statements

PyroGenesis Canada Inc.

Condensed Interim Statement of Changes in Equity (continued)

(Unaudited)

Nine months ended September 30

	Number of common shares	Common Share capital \$	Number of preferred shares	Preferred Share capital \$	Contributed surplus \$	AOCI \$	Deficit \$	Total equity \$
Balance - January 1, 2011	47,371,377	4,026,588	1,093,800	1,093,800	-	-	(4,906,432)	213,956
Non-brokered private placement <i>[note 13]</i>	312,500	250,000	-	-	-	-	-	250,000
Shares issued for deposit above	2,187,500	-	-	-	-	-	-	-
Convertible FIER loan <i>[note 13]</i>	1,388,889	1,000,000	-	-	-	-	-	1,000,000
Professional fees related to FIER loan	-	(103,102)	-	-	-	-	-	(103,102)
Private placement subscription receipts <i>[note 13]</i>	5,083,250	4,066,600	-	-	-	-	-	4,066,600
Commissions and fees private placement	-	(470,224)	-	-	-	-	-	(470,224)
Stock options private placement	-	(110,306)	-	-	110,306	-	-	-
Purchase price of IGIC net assets	1,300,000	1,040,000	-	-	-	-	-	1,040,000
Professional fees related to IGIC	-	(167,329)	-	-	-	-	-	(167,329)
Stock Option exercised <i>[note 13]</i>	103,328	64,063	-	-	-	-	-	64,063
Conversion of preferred shares <i>[note 13]</i>	1,367,250	1,093,800	(1,093,800)	(1,093,800)	-	-	-	-
Stock based compensation <i>[note 13]</i>	-	-	-	-	910,000	-	-	910,000
Net loss during the period	-	-	-	-	-	-	(6,160,348)	(6,160,348)
Balance - September 30, 2011	59,114,094	10,690,090	-	-	1,020,306	-	(11,066,780)	643,616

See accompanying Notes to the Financial Statements

PyroGenesis Canada Inc.

Condensed Interim Statement of Cash Flows

(Unaudited)

	<u>Three months Ended</u>		<u>Nine Months Ended</u>	
	September 30		September 30	
	2012	2011	2012	2011
	\$	\$	\$	\$
Cash flows provided (used) by				
Operating activities				
Net comprehensive loss	(1,742,581)	(2,815,300)	(4,968,993)	(6,160,348)
Items not requiring an outlay of cash:				
Public company listing	-	694,877	-	694,877
Expenses paid through issuance of options	451,664	910,000	868,709	799,696
Amortization of machinery and equipment	62,890	77,309	188,670	229,646
Amortization of licenses	349,268	352,297	1,047,805	763,051
	(878,759)	(780,817)	(2,863,809)	(3,673,078)
Net change in non-cash operating working capital items <i>[Note 14]</i>	1,501,890	3,999,413	2,302,329	4,340,991
	623,131	3,218,596	(561,480)	667,913
Investing activities				
Cash acquired as a result of amalgamation	-	-	-	333,887
Purchase of machinery and equipment	(191,203)	(333,166)	(425,032)	(352,399)
Proceeds from disposal of machinery and equipment	-	-	-	471,202
	(191,203)	(333,166)	(425,032)	452,690
Financing activities				
Decrease in bank indebtedness	-	(2,441,000)	(240,000)	(1,921,000)
Increase in convertible debenture	-	-	-	(3,873)
Repayment of obligation under capital lease	-	-	-	(26,428)
Repayment of loans - other	(25,933)	(226,428)	(301,030)	-
Due to joint operator	-	220,006	-	220,006
Repayment of long-term debt	-	(104,514)	(976,396)	-
Proceeds from equity issues	-	-	3,508,678	-
Costs related to short form prospectus	-	-	(361,887)	-
Proceeds from issuance of common shares	-	(217,041)	-	684,368
	(25,933)	(2,768,977)	1,629,365	(1,046,927)
Increase (decrease) in cash	405,995	116,453	642,853	73,676
Cash and cash equivalents - beginning of period	718,254	194,514	481,396	237,291
Cash and cash equivalents - end of period	1,124,249	310,967	1,124,249	310,967

Supplemental information *[Note 14]*

See accompanying Notes to the Financial Statements

PyroGenesis Canada Inc.

Notes to Condensed Interim Financial Statements

(Unaudited)

For the three and nine months ended September 30, 2012 and 2011

1. Nature of operations and going concern disclosure

(a) Nature of operations

PyroGenesis Canada Inc. (the "Company") was formed by the amalgamation of PyroGenesis Canada Inc. with Industrial Growth Income Corporation ("IGIC") on July 11, 2011 (Note 2). Information prior to this date, presented in these financial statements, represent the operations of PyroGenesis Canada Inc., a private company, (incorporated on June 5, 2006). The Company is an environmental solutions company that designs, develops and manufactures plasma waste-to-energy systems and plasma torch products. The Company is domiciled at 1744 William Street, Suite 200, Montreal, Quebec. The Company is publicly traded on the TSX Venture Exchange under the Symbol "PYR". These financial statements were approved and authorized for issuance by the Board of Directors on November 27, 2012.

(b) Going concern

These Financial statements have been prepared using International Financial Reporting Standards ("IFRS") applicable to a going concern, which contemplates the realization of assets and settlement of liabilities in the normal course of business as they become due.

Several adverse conditions and events cast substantial doubt upon the validity of this assumption. The company has a history of operating losses and negative cash flows and its ability to continue as a going concern is uncertain and is dependant on its ability to fund its working capital, complete the development of its products, and eventually to generate positive cash flows from the products that it has developed. Management plans to explore all alternatives possible, including equity financing.

These financial statements do not reflect the adjustments to the carrying values of assets and liabilities and the reported expenses and statement of financial position classifications that would be necessary were the going concern assumption inappropriate, and these adjustments could be material.

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 condensed interim financial statements do not include all of the necessary information required for full annual financial statements in accordance with IFRS and should be read in conjunction with the Company's annual financial statements for the year ended December 31, 2011.

(b) Functional and presentation currency

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

PyroGenesis Canada Inc.

Notes to Condensed Interim Financial Statements

(Unaudited)

For the three and nine months ended September 30, 2012 and 2011

2. Basis of preparation (continued)

(c) Basis of measurement

The 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 IGIC (the “Qualifying Transaction”).

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 as an acquisition of a non-trading shell company within the meaning ascribed by IFRS 2 – share based payment.

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:

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

IGIC share capital and contributed surplus have been eliminated upon consolidation. The excess of the purchase price over net assets acquired has been recorded as public listing expense.

An additional \$113,775 of professional fees related to the amalgamation was also recorded as public listing expenses.

3. Significant accounting policies

The accounting policies applied by the Company in these condensed interim financial statements are the same as those applied by the Company in its financial statements as at and for the year ended December 31, 2011.

a) Adoption of new and revised standards

On January 1, 2012, the Company adopted the new or amended IFRS and Interpretations of IFRS (“Interpretations”) that are mandatory for application from that date. Changes to the Company’s accounting policies have been made as required, in accordance with the transitional provisions in the respective IFRS and Interpretations. The adoption of these new or amended IFRS and Interpretations did not result in substantial changes to the Company’s accounting policies and had no material effect on the amounts reported for the current or prior financial years, except as disclosed below:

PyroGenesis Canada Inc.

Notes to Condensed Interim Financial Statements

(Unaudited)

For the three and nine months ended September 30, 2012 and 2011

3. Significant accounting policies (continued)

Amendments to IAS 1 - Presentation of Items of Other Comprehensive Income

The Amendments to IAS 1 Presentation of Items of Other Comprehensive Income (OCI) is effective for financial periods beginning on or after July 1, 2012.

The Amendments to IAS 1 changes the grouping of items presented in OCI. Items that could be reclassified to profit or loss at a future point in time would be presented separately from items which will never be reclassified. As the Amendments only affect the presentations of items that are already recognised in OCI, there is no impact on its financial position or performance.

IFRS 7 Financial instruments: disclosures

The amendment to IFRS 7, issued in October 2010, provides greater transparency around risk exposures relating to transfers of financial assets that are not derecognized in their entirety, and derecognized in their entirety, but with which the entity continues to have some continuing involvement. The amendment will only affect disclosure and is effective for annual periods beginning on or after July 1, 2011.

IAS 12 Income taxes

The amendment to IAS12, issued in December 2010, incorporates the SIC 21 Income taxes – Recovery of revalued non-depreciable assets consensus, which requires deferred tax liabilities/assets relating to revalued non-depreciable assets, to reflect the tax consequences of recovering the carrying amount through sales. It also introduces a rebuttable presumption that the carrying amount of investment property at fair value will be recovered through sale. The amendment, which supersedes IC 21, is effective for annual periods beginning on or after January 1, 2012. The Company is currently assessing the impact of this amendment on its financial statements.

b) Standards issued but not yet effective

The Company has not adopted the following standards and interpretations that have been issued but not yet effective:

<u>Description</u>	<u>Effective for annual periods beginning on or</u>
IAS 27 Separate Financial Statements	1 January 2013
IAS 28 Investments in Associates and Joint Ventures	1 January 2013
IFRS 10 Consolidated Financial Statements	1 January 2013
IFRS 11 Joint Arrangements	1 January 2013
IFRS 13 Fair Value Measurements	1 January 2013
Amendment to IFRS 7 - <i>Disclosure - Offsetting Financial Assets and Financial Liabilities</i>	1 January 2013
Amendment to IAS 32 - <i>Offsetting Financial Assets and Financial Liabilities</i>	1 January 2014
IFRS 9 Financial Instruments	1 January 2015

Except for the Amendments to IAS 1 and IFRS 12, the directors expect that the adoption of the other standards and interpretations above will have no material impact on the financial statements in the period of initial application. The nature of the impending changes in accounting policy on adoption of the Amendments to IAS 1 is described below.

PyroGenesis Canada Inc.

Notes to Condensed Interim Financial Statements

(Unaudited)

For the three and nine months ended September 30, 2012 and 2011

3. Significant accounting policies (continued)

IFRS 12 Disclosure of Interests in Other Entities

IFRS 12 is effective for financial periods beginning on or after January 1, 2013.

IFRS 12 is a new and comprehensive standard on disclosure requirements for all forms of interests in other entities, including subsidiaries, joint arrangements, associates, special purpose vehicles and other off balance sheet vehicles. IFRS 12 requires an entity to disclose information that helps users of its financial statements to evaluate the nature and risks associated with its interests in other entities and the effects of those interests on its financial statements. The Company is currently determining the impact of the disclosure requirements. As this is a disclosure standard, it will have no impact to the financial position and financial performance of the Company when implemented in 2013.

4. Comparative figures

The comparative financial statements have been reclassified from statements previously presented to conform to the presentation adopted in the current year.

5. Accounts receivable

Accounts receivable are carried on the balance sheet net of an allowance for doubtful accounts. This provision is established based on the company's best estimates regarding the ultimate recovery of balances for which collection is uncertain. Uncertainty of ultimate collection may become apparent from various indicators, such as a deterioration of the credit situation of a given client and delay in collection beyond the contractually agreed upon payment terms. Management regularly reviews accounts receivable, monitors past due balances and assesses the appropriateness of the allowance for doubtful accounts. The provision for 2012 was nil (2011 - nil).

Details of accounts receivable were as follows:

	September 30, 2012 \$	December 31, 2011 \$
1 – 30 days	1,192	251,916
30 – 60 days	-	63,778
61 – 90 days	-	7,338
Greater than 90 days	32,117	434,711
Total	33,309	757,743
Receivable from joint operator	138,035	401,107
Other receivable	2,264	-
Total accounts receivable	173,608	1,158,850

PyroGenesis Canada Inc.

Notes to Condensed Interim Financial Statements

(Unaudited)

For the three and nine months ended September 30, 2012 and 2011

6. Investment tax credits receivable

During the three and nine month period ending September 30, 2012, research and development tax credits in the amount of \$41,259 and \$119,061 respectively (2011 - \$100,000 and \$999,505) have been included as a reduction of \$143,321 and \$396,871 respectively (2011 - \$975,400 and \$1,845,427) of related research and development expenses.

7. Machinery and equipment

2012	Computer hardware \$	Computer software \$	Machinery \$	Computer hardware under capital lease \$	Torch asset under construction [note 10] \$	Total \$
Cost:						
Balance at January 1, 2012	129,370	202,883	1,545,260	25,859	359,269	2,262,641
Additions	2,366	230	-	-	422,436	425,032
Balance at September 30, 2012	131,736	203,113	1,545,260	25,859	781,705	2,687,673
Accumulated amortization:						
Balance at January 1, 2012	(92,603)	(131,328)	(552,028)	(25,859)	-	(801,818)
Amortization	(12,808)	(26,876)	(148,986)	-	-	(188,670)
Balance at September 30, 2012	(105,411)	(158,204)	(701,014)	(25,859)	-	(990,488)
Net book value	26,325	44,909	844,246	-	781,705	1,697,185
2011	Computer hardware \$	Computer software \$	Machinery \$	Computer hardware under capital lease \$	Torch asset under construction [note 10] \$	Total \$
Cost:						
Balance at January 1, 2011	113,765	139,497	1,538,931	25,859	-	1,818,052
Additions	15,605	63,386	6,329	-	359,269	444,589
Disposals	-	-	-	-	-	-
Balance at December 31, 2011	129,370	202,883	1,545,260	25,859	359,269	2,262,641
Accumulated amortization:						
Balance at January 1, 2011	(68,904)	(91,466)	(304,512)	(14,836)	-	(479,718)
Amortization	(23,699)	(39,862)	(247,516)	(11,023)	-	(322,100)
Disposals	-	-	-	-	-	-
Balance at December 31, 2011	(92,603)	(131,328)	(552,028)	(25,859)	-	(801,818)
Net book value	36,767	71,555	993,232	-	359,269	1,460,823

PyroGenesis Canada Inc.

Notes to Condensed Interim Financial Statements

(Unaudited)

For the three and nine months ended September 30, 2012 and 2011

8. Licences and intellectual property

Intangible assets are made up of licenses as follows:

2012	Licences \$	Intellectual property \$	Total \$
Cost:			
Balance at January 1, 2012	-	8,409,051	8,409,051
Accumulated amortization:			
Balance at January 1, 2012	-	1,424,082	1,424,082
Amortization	-	1,047,805	1,047,805
Balance at September 30, 2012	-	2,471,887	2,471,887
Net book value	-	5,937,164	5,937,164

2011	Licences \$	Intellectual property \$	Total \$
Cost:			
Balance at January 1, 2011	772,625	-	772,625
Additions	-	7,636,426	7,636,426
Reclassification on acquisition of property	(772,625)	772,625	-
Balance at December 31, 2011	-	8,409,051	8,409,051
Accumulated amortization:			
Balance at January 1, 2011	(309,050)	-	(309,050)
Amortization	(77,263)	(1,037,769)	(1,115,032)
Reclassification on acquisition of property	386,313	(386,313)	-
Balance at December 31, 2011	-	(1,424,082)	(1,424,082)
Net book value	-	6,984,969	6,984,969

On March 19, 2011, intellectual property and know-how was sold to PyroGenesis for \$14,280,000 from a company controlled by the Company's controlling shareholder and will be payable in equal monthly instalments of \$40,000 (Note 11) without interest. 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 is being amortized on a straight line basis over the remaining useful life at the time of acquisition of 5.79 years.

PyroGenesis Canada Inc.

Notes to Condensed Interim Financial Statements

(Unaudited)

For the three and nine months ended September 30, 2012 and 2011

9. Accounts payable and accrued liabilities

	September 30, 2012 \$	December 31, 2011 \$
Accounts payable trade	305,976	1,353,078
Accrued liabilities	1,248,528	588,714
Deductions at source	-	18,256
Accounts payable to a company under common control	2,058	40,751
Accounts payable - shareholder	346,591	160,000
Accounts payable - trust beneficially owned by the shareholder	98,942	7,595
Accounts payable - joint operator	-	245,959
	2,002,095	2,414,353

10. Joint operations

PyroGenesis entered into an agreement with another company to share costs, benefits and risks associated with the development of a pilot plasma destruction unit.

PyroGenesis has a 50% share in the joint operations. Activities to date have been the design, construction and assembly of a torch asset which is included in machinery and equipment (torch asset under construction) in Note 7.

11. Loans - other

	September 30, 2012 \$	December 31, 2011 \$
Balance of sale - company under common control	7,454,815	7,547,242
Amounts payable - shareholder	-	224,093
Amounts payable - trust beneficially owned by the shareholder	354,593	339,103
Promissory note payable - company under common control	200,000	200,000
	8,009,408	8,310,438
Current portion	328,455	548,050
	7,680,953	7,762,388

This balance of sale is payable in monthly instalments of \$40,000 from April 1, 2011 until December 31, 2040 and bears interest at an implicit rate of 4.753% per annum (see Note 8).

Amounts payable - shareholder and amounts payable - trust beneficially owned by the shareholder bear interest at 6% and have no set terms of repayment.

Promissory note payable - company under common control is non-interest bearing and is due December 2012.

PyroGenesis Canada Inc.

Notes to Condensed Interim Financial Statements

(Unaudited)

For the three and nine months ended September 30, 2012 and 2011

12. Long-term debt – current portion

	2012 \$	2011 \$
\$1,000,000 convertible debenture, including accumulated accretion of \$23,604 (2010 – nil)	-	976,396

On March 29, 2012, the convertible debt was repaid by the Company.

13. Shareholders' equity

2012

On March 29, 2012, the Company completed a short-form prospectus in which 4,424,555 units were issued at a price of \$0.80 each for gross process of \$3,539,644. Each unit consisted of one common share and a share purchase warrant exercisable at the strike price of \$1.20 per common share over the next 3 years.

In accordance with the Black Scholes pricing model, the Company has allocated a value of \$0.34 to the purchase warrants for a total cost of \$1,517,622 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	2.23%
Expected volatility	80%
Expected dividend yield	nil
Expected life	3 years

Share issue costs of \$234,000 were paid in cash to the agents, along with 309,719 of brokers warrants exercisable for a period of 12 months following the closing date.

In accordance with the Black Scholes pricing model, the Company has allocated a value of \$0.25 to the broker warrants for a total cost of \$78,978 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	2.23%
Expected volatility	80%
Expected dividend yield	nil
Expected life	1 year

On September 19, 2012, the Board of Directors approved:

- a re-pricing from \$0.80 to \$0.15 of 1,060,000 previously granted options;
- the issuance of 2,016,000 new options granted at \$0.15
- the issuance of 550,000 new options granted at \$0.175

Included in the issuance of 2,016,000 new options are 1,140,000 options for key management and Board members that signed a non-exercise agreement covering 1,140,000 previously issued options which had an exercise price of \$0.80.

The re-pricing resulted in a value per option of \$0.14 and a charge to operations of \$52,548 in the period ended September 30, 2012. The new options granted resulted in charge to operations of \$15,199 in the period ended September 30, 2012.

PyroGenesis Canada Inc.

Notes to Condensed Interim Financial Statements

(Unaudited)

For the three and nine months ended September 30, 2012 and 2011

13. Shareholders' equity (continued)

The following assumptions under the Black Scholes model were used to arrive at the cost.

Risk free interest rate	2.23%
Expected volatility	100%
Expected dividend yield	nil
Expected life	5 years
Exercise price	\$0.15

The Company also revised the forfeiture rate estimate to 5% from a former estimate of 2%.

2011

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

The \$1,000,000 debenture converted into 1,388,889 shares after the completion of the Qualifying Transaction. Net proceeds from the debenture were \$896,898 after payment of fees of \$103,102 which was charged against share capital.

- (iv) 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.
- (v) 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. The warrants were not exercised and have expired.

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

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13. Shareholders' equity (continued)

- (vi) On June 2, 2011, the 1,093,800 preferred shares were converted to 1,367,250 Class A common shares.
- (vii) On August 10, 2011, 103,328 stock option with an exercise price of \$0.62 were exercised by former officers of IGIC.
- (viii) The company has a stock option plan authorizing the Board of Directors to grant options to directors, officers, employees and consultants to acquire common shares of the company at a price computed by reference to the closing market price of the shares of the company on the business day before the company notifies the stock exchanges of the grant of the option. The number of shares which may be granted to any one person shall not exceed 5% (2% for consultants) over a twelve month period. The options will vest from the date of the grant to 18 months and expire within 5 years, as determined by the board, with exceptions for death, employment, etc.
- (ix) On July 20, 2011, two directors were granted the right to acquire an aggregate of 40,000 Common shares at an exercise price of \$0.80 per share. These shares will vest quarterly over four years starting on the date of grant. The value under the Black Scholes pricing model is \$.93 for a total cost of \$19,824 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	2.33%
Expected volatility	80%
Expected dividend yield	Nil
Expected life	5 years
Expected forfeiture rate	2%

- (x) On July 20, 2011, two directors were granted the right to acquire an aggregate of 200,000 common shares at an exercise price of \$0.80 per share. These shares will vest quarterly over four years starting on the date of grant. The value under the Black Scholes pricing model is \$.93 for a total cost of \$99,118 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	2.33%
Expected volatility	80%
Expected dividend yield	Nil
Expected life	5 years
Expected forfeiture rate	2%

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13. Shareholders' equity (continued)

- (xi) On July 20, 2011, two directors were granted options to acquire an aggregate of 900,000 shares, three officers were granted options to acquire an aggregate of 550,000 shares and 14 employees were granted options to acquire an aggregate of 1,460,000 shares.

All of these options have an exercise price of \$0.80 per share. Ten percent of these options are vested at the date of grant, 20% vest at the first anniversary of the grant, 30% vest at the second anniversary of the grant and 40% vest at the third anniversary of the grant.

The value under the Black Scholes pricing model is \$.93 for a total cost of \$791,058 which has been credited to contributed surplus. The following assumption under the Black Scholes model were used to arrive at this cost.

Risk free interest rate	2.33%
Expected volatility	80%
Expected dividend yield	Nil
Expected life	5 years
Expected forfeiture rate	2%

Broker warrants

At September 30, 2012, the following exercisable broker warrants were outstanding:

	Granted	Exercisable	Weighted averaged exercise price	Expiry date
Balance – January 1, 2011	-	-	-	
Warrants granted	355,827	355,827	\$0.80	March 30, 2012
Balance – December 31, 2011	355,827	355,827	\$0.80	
Expired	(355,827)	(355,827)		
Options granted	309,719	309,719	\$0.80	March 29, 2013
Balance – September 30, 2012	309,719	309,719	\$0.80	

Stock options

At September 30, 2012, the following exercisable stock options were outstanding:

Granted	Exercisable	Weighted averaged exercise price	Expiry date
120,000	120,000	\$0.80	December 2012
550,000	165,000	\$0.80	July 2016
1,140,000	342,000 (see note)	\$0.80	July 2016
3,076,000	837,100	\$0.15	September 2017
550,000	155,000	\$0.175	September 2017
5,436,000	1,619,100	\$0.246	

Note: These options are subject to a non-exercise agreement.

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13. Shareholders' equity (continued)

Share purchase warrants

At September 30, 2012, the following exercisable broker warrants were outstanding:

	Granted	Exercisable	Weighted averaged exercise price	Expiry date
Balance – January 1, 2012	-	-	-	
Warrants granted	4,424,555	4,424,555	\$1.20	March 29, 2015
Balance – September 30, 2012	4,424,555	4,424,555	\$1.20	

14. Supplemental disclosure of expenses and cash flow information

(i) *Net changes in non-cash components of operating working capital*

	Three months Ended September 30		Nine Months Ended September 30	
	2012 \$	2011 \$	2012 \$	2011 \$
Decrease (increase) in:				
Deposits in escrow	-	3,596,375	-	3,596,375
Accounts receivable	646,240	(515,271)	985,242	(514,972)
Sales tax receivable	(64,131)	5,919	(7,915)	123,393
Investment tax credits receivable	(41,259)	1,777,172	1,544,587	877,667
Prepaid expenses	(17,669)	8,000	(51,887)	14,389
Increase (decrease) in:				
Accounts payable and accrued liabilities	238,686	(482,252)	(412,258)	244,418
Billings in excess of costs and profits on uncompleted contracts	740,023	(390,530)	244,560	(279)
	1,501,890	3,999,413	2,302,329	4,340,991

(ii) *non-momentary transactions*

On March 19, 2011, the Company signed an agreement to purchase licenses from a company controlled by a shareholder having a fair market value of \$7,636,426. Long-term debt of \$7,636,426 was assumed on the sale.

PyroGenesis Canada Inc.

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15. 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 \$10,033 and \$12,088 for the three and nine month period ended September 30, 2012 respectively (2011 – a foreign exchange gain of \$27,808 and \$14,701 respectively).

During the three and nine month period ended September 30, 2012, the Company recorded salary expenses of \$445,470 and \$2,070,896 respectively (2011 - \$697,619 and \$2,829,578 respectively).

16. Related party transactions

During the three and nine month period ended September 30, 2012, rent was charged by a trust of which at least one of the trustees and beneficiaries is a shareholder and director of the Company in the amount of \$26,626 and \$86,055 respectively (2011 - \$26,827 and \$83,148). A balance due of \$86,055 (2011 - \$8,942) is included in accounts payable and accrued liabilities.

During the three and nine month period ended September 30, 2012, interest on long-term debt was charged by a trust of which at least one of the trustees and beneficiaries is a shareholder and director of the company in the amount of \$5,240 and \$15,490 respectively (2011 - \$4,230 and \$12,530). Interest on long-term debt was also charged by a shareholder in the amount of \$nil and \$2,498 respectively (2011 - \$2,855 and \$8,355). The balance of interest on long-term debt that has not been paid of \$15,490 (2011 - \$23,845) is included in loans - other.

During the three and nine month period ended September 30, 2012, interest on long-term debt was charged by a company under common control in the amount of \$88,827 and \$267,573 respectively (2011 - \$90,624 and \$90,624).

During the three and nine month period ended September 30, 2012, salaries to key management personal amounted to \$92,438 and \$317,885 respectively (2011 - \$110,423 and \$349,996).

During the three and nine month period ended September 30, 2012, fees of \$17,000 and \$61,522 respectively were charged by a director (2011 - \$24,502 and \$54,582). A balance of \$nil (2011 - \$6,679) is included in accounts payable and accrued liabilities.

During the three and nine month period ended September 30, 2012, rent of \$99,000 and \$276,200 (2011 - \$102,700 and \$322,900) was charged by a company under common control. A balance due of \$nil (2011 - \$10,188) is included in accounts payable and accrued liabilities.

During the three and nine month period ended September 30, 2012, royalties of \$nil and \$ nil respectively (2011 - \$nil and \$75,000) were charged by a company controlled by a shareholder.

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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17. Credit risk

Risk management

The company generates revenues from customers mainly in North America. The company performs credit evaluations of customers and generally does not require collateral. Allowances are maintained for potential losses. It is reasonably possible that the actual amount of loss, if any, incurred on accounts receivable will differ from management's estimate.

One customer made up 69% trade receivables (2011 - three customers accounted for 89%).

During nine month period ended September 30, 2012, one customer made up 45% of revenues from operation and the Joint operator made up 20% (2011 - one customer made up 32%, a second customer made up 23% and a third customer made up 21%).

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PyroGenesis Canada Inc.

Three and Nine Months Ended
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