PyroGenesis Canada Inc.

Condensed
Interim Financial Statements

Three Months Ended March 31, 2014 and 2013

(Unaudited)

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 condensed interim financial statements for the period ended March 31, 2014.

PyroGenesis Canada Inc.

Condensed Interim Statements of Financial Position

(Unaudited)

As at	**March 31, 2014 $**	December 31, 2013 $
Assets		
Current assets		
Cash	**52,253**	1,182,835
Accounts receivable *[note 4]*	**301,152**	361,304
Sales tax receivable	**34,904**	21,809
Costs in excess of billings *[note 5]*	**410,497**	286,403
Inventories	**185,774**	180,442
Investment tax credits receivable	**120,094**	101,938
Prepaid expenses and deposits *[note 6]*	**105,630**	112,530
Total current assets	**1,210,304**	2,247,261
Non-current assets		
Property and equipment *[note 7]*	**713,828**	732,788
Intangible assets *[note 8]*	**3,841,554**	4,190,823
Total assets	**5,765,686**	7,170,872
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities *[note 9]*	**1,195,463**	1,155,657
Current portion of obligation under finance lease	**2,763**	2,763
Billings in excess of costs and profits on uncompleted contracts *[note 11]*	**2,070,787**	2,462,604
Total current liabilities	**3,269,013**	3,621,024
Non-current liabilities		
Obligation under finance lease	**5,433**	6,139
Loans - other *[note 12]*	**8,215,982**	8,153,723
Total liabilities	**11,490,428**	11,780,886
Shareholders' deficiency *[note 13]*		
Common shares	**13,138,554**	13,138,554
Warrants reserve	**1,778,999**	1,778,999
Contributed surplus	**2,375,386**	2,325,386
Other equity	**24,844**	24,844
Deficit	**(23,042,525)**	(21,877,797)
	(5,724,742)	(4,610,014)
	5,765,686	7,170,872

Going concern disclosure, related party transactions, subsequent event *[notes 1,16, and 19]*

These condensed interim financial statements were approved and authorized for issuance by the Board of Directors on May 30, 2014

Approved on behalf of the board:

"P. Peter Pascali" *P. Peter Pascali*

"Alan Curleigh" *Alan Curleigh*

The accompanying notes form an integral part of the condensed interim financial statements.

PyroGenesis Canada Inc.

Condensed Interim Statements of Comprehensive Loss

(Unaudited) Three months ended March 31	**2014** **$**	2013 $
Revenue	**806,425**	1,141,143
Cost of sales and services *[note15]*	**832,410**	979,852
Gross margin	**(25,985)**	161,291
Expenses		
Selling, general and administrative *[note15]*	**946,918**	1,002,822
Research and development *[note15]*	**99,601**	17,393
Financing charges	**92,259**	95,215
	1,138,778	1,115,430
Loss from operations	**(1,164,763)**	(954,139)
Other income	**35**	-
Comprehensive loss	**(1,164,728)**	(954,139)
Basic and diluted loss per share	**(0.02)**	**(0.02)**
Weighted average number of common shares outstanding - basic and diluted *[note 17]*	**67,198,649**	**63,538,649**

The accompanying notes form an integral part of the condensed interim financial statements.

PyroGenesis Canada Inc.

Condensed Interim Statements of Changes in Deficiency

(Unaudited)
Three months ended March 31

	Number of Class A common shares	Class A common share capital $	Warrants reserve $	Contributed surplus $	Other Equity $	Deficit $	Total $
Balance - December 31, 2013	**67,198,649**	**13,138,554**	**1,778,999**	**2,325,386**	**24,844**	**(21,877,797)**	**(4,610,014)**
Share-based payments	**-**	**-**	**-**	**50,000**	**-**	**-**	**50,000**
Comprehensive loss during the period	**-**	**-**	**-**	**-**	**-**	**(1,164,728)**	**(1,164,728)**
Balance – March 31, 2014	**67,198,649**	**13,138,554**	**1,778,999**	**2,375,386**	**24,844**	**(23,042,525)**	**(5,724,742)**
Balance - December 31, 2012	63,538,649	12,249,527	1,497,948	1,663,090	24,844	(17,889,720)	(2,454,311)
Expired warrants *[Note 13 (ii)]*	-	-	(55,408)	55,408	-	-	-
Share-based payments	-	-	-	145,840	-	-	145,840
Comprehensive loss during the period	-	-	-	-	-	(954,139)	(954,139)
Balance - March 31, 2013	63,538,649	12,249,527	1,442,540	1,864,338	24,844	(18,843,859)	(3,262,610)

The accompanying notes form an integral part of the condensed interim financial statements.

PyroGenesis Canada Inc.

Condensed Interim Statements of Cash Flows

(Unaudited) Three months ended March 31	**2014** **$**	2013 $
Cash flows provided by (used in)		
Operating activities		
Comprehensive loss	**(1,164,728)**	(954,139)
Items not requiring an outlay of cash:		
Share-based payments	**50,000**	145,840
Depreciation on property and equipment *[note 7]*	**41,907**	48,333
Amortization of intangible assets *[note 8]*	**349,269**	349,269
	(723,552)	(410,697)
Net change in non-cash operating working capital items *[note 14]*	**(445,636)**	(1,165,810)
	(1,169,188)	(1,576,507)
Investing activity		
Purchase of property and equipment *[note 7]*	**(22,947)**	-
Financing activities		
Repayments of obligation under finance lease	**(706)**	(682)
Proceeds from (repayment of) loans - other	**62,259**	(54,723)
	61,553	(55,405)
Decrease in cash	**(1,130,582)**	(1,631,912)
Cash - beginning of period	**1,182,835**	2,195,571
Cash - end of period	**52,253**	563,659

Supplemental disclosure of expenses and cash flow information *[note 14]*

The accompanying notes form an integral part of the condensed interim financial statements.

1. Nature of operations and going concern disclosure

(a) Nature of operations

PyroGenesis Canada Inc. (the "Company"), incorporated under the laws of the Canada Business Corporations Act, was formed by the amalgamation of PyroGenesis Canada Inc. with Industrial Growth Income Company ("IGIC") on July 11, 2011. The Company owns patents of advanced waste treatment systems technology and provides design, development, manufacturing and commercialization of advanced plasma processes. 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 condensed interim financial statements were approved and authorized for issuance by the Board of Directors on May 30, 2014.

(b) Going concern

These condensed interim financial statements have been prepared on the going concern basis, which presumes that the Company will be able to realize its assets and discharge its liabilities in the normal course of business for the foreseeable future.

The Company has incurred recurring losses to date, with $1,164,728 of losses occurring in 2014 and has an accumulated deficit of $23,042,525 at March 31, 2014. In addition, the Company's current liabilities exceed its current assets as at March 31, 2014 in the amount of $2,058,709. These conditions indicate the existence of a material uncertainty that may cast significant doubt on the Company's ability to continue as a going concern.

In the future, it may be necessary for the Company to raise additional capital to fund its operations and continued development and introduction of new products to its family of products. To date, the Company has raised financing through successive issuances of equity. There is no certainty that the Company will continue to raise additional financing or expand its sales to fund its operations.

The condensed interim financial statements have been prepared on a going concern basis and do not include any adjustments to the amounts and classifications of the assets and liabilities that might be necessary should the Company be unable to achieve its plan and continue in business. If the going concern assumption were not appropriate for these condensed interim financial statements then adjustments would be necessary to the carrying value of assets and liabilities, the reported expenses and the condensed interim statements of financial position classifications used. The impact on the condensed interim financial statements 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 audited annual financial statements for the year ended December 31, 2013.

(b) Functional and Presentation Currency

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

(c) Basis of measurement

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

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

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 audited annual financial statements as at and for the year ended December 31, 2013, except for the following new accounting pronouncements:

Adopted and future accounting policies

(a) New standards, interpretations and amendments adopted on January 1, 2014

On January 1, 2014, the Company adopted the following new or amended IFRS standards and Interpretations of IFRS ("Interpretations") that are mandatory for application from that date. The adoption of these new or amended IFRS standards 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 periods.

IFRS 7 – Financial instruments: disclosures and IAS 32 – Financial instruments: presentation

Financial assets and financial liabilities may be offset, with the net amount presented in the statement of financial position, only when there is a legally enforceable right to set off and when there is either an intention to settle on a net basis or to realize the asset and settle the liability simultaneously. The amendments to IAS 32, issued in December 2011, clarify the meaning of the offsetting criterion "currently has a legally enforceable right to set off" and the principle behind net settlement, including identifying when some gross settlement systems may be considered equivalent to net settlement.

IAS 36 – Impairment of assets

The amendments to IAS 36, issued in May 2013, require:

- Disclosure of the recoverable amount of impaired assets; and
- Additional disclosures about the measurement of the recoverable amount when the recoverable amount is based on fair value less costs of disposal, including the discount rate when a present value technique is used to measure the recoverable amount.

IAS 39 – Financial Instruments: Recognition and measurement

The amendments to IAS 39, issued in June 2013, clarify that notation of a hedging derivative to a clearing counterparty as a consequence of laws or regulations or the introduction of laws or regulations, does not terminate hedge accounting.

IFRIC 21 – Levies

In May 2013, the IASB issued IFRIC 21. Within IFRIC 21, a levy is defined as an outflow of resources embodying economic benefits that is imposed by governments on entities in accordance with legislation (i.e. laws and/or regulations), other than:

- those outflows of resources that are within the scope of other standards (such as income taxes that are within the scope of IAS 12); and
- fines or other penalties that are imposed for breaches of the legislation.
  'Government' refers to government, government agencies and similar bodies whether local, national or international. IFRIC 21 provides an interpretation of the requirements in IAS 37 for the recognition of liabilities for obligations to pay levies that are within the scope of IFRIC 21.

3. Significant accounting policies (continued)

(b) Recent accounting pronouncements and amendments not yet effective

The Company has not yet applied the following new or amended IFRS standards and interpretations that have been issued as at March 31, 2014 but are not yet effective. The Company does not plan to early adopt any of these new or amended standards and interpretations.

IFRS 2 – Share-based payment

The amendments to IFRS 2, issued in December 2013, clarify the definition of "vesting conditions", and separately define a "performance condition" and a "service condition". A performance condition requires the counterparty to complete a specified period of service and to meet a specified performance target during the service period. A service condition solely requires the counterparty to complete a specified period of service. The amendments are effective for share-based payment transactions for which the grant date is on or after July 1, 2014.

IFRS 8 – Operating segments

The amendments to IFRS 8, issued in December 2013, require an entity to disclose the judgments made by management in applying the aggregation criteria for reportable segments. The amendments will only affect disclosure and are effective for annual periods beginning on or after July 1, 2014.

IAS 16 – Property, plant and equipment

The amendments to IAS 16 and IAS 38, issued in December 2013, clarify how an entity calculates the gross carrying amount and accumulated depreciation when a revaluation is performed. The amendments are effective for annual periods beginning on or after July 1, 2014.

IFRS 9 – Financial instruments

IFRS 9 introduces new requirements for the classification and measurement of financial assets. IFRS 9 requires all recognized financial assets that are within the scope of IAS 39 – *Financial Instruments: Recognition and Measurement* to be measured at amortized cost or fair value in subsequent accounting periods following initial recognition. Specifically, financial assets that are held within a business model whose objective is to collect the contractual cash flows that are solely payments of principal and interest on the principal outstanding are generally measured at amortized cost at the end of subsequent accounting periods. All other financial assets including equity investments are measured at their fair values at the end of the subsequent accounting periods.

Requirements for classification and measurement of financial liabilities were added in October 2010 and they largely carried forward existing requirements in IAS 39, Financial Instruments – Recognition and Measurement, except that fair value changes due to credit risk for liabilities designated at fair value through profit or loss would generally be recorded in other comprehensive income.

IFRS 9 was amended in November 2013, to (i) include guidance on hedge accounting, (ii) allow entities to early adopt the requirement to recognize changes in fair value attributable to changes in an entity's own credit risk, from financial liabilities designated under the fair value option, in OCI, without having to adopt the remainder of IFRS 9, and to (iii) remove the previous mandatory effective date for adoption of January 1, 2015. The standard was later amended to introduce a new mandatory effective date for adoption of January 1, 2018 with early adoption permitted.

IAS 24 – Related party disclosures

The amendments to IAS 24, issued in December 2013, clarify that a management entity, or any member of a group of which it is a part, that provides key management services to a reporting entity, or its parent, is a related party of the reporting entity. The amendments also require an entity to disclose amounts incurred for key management personnel services provided by a separate management entity. This replaces the more detailed disclosure by category required for other key management personnel compensation. The amendments will only affect disclosure and are effective for annual periods beginning on or after July 1, 2014.

4. Accounts receivable

Accounts receivable are carried on the condensed interim statements of financial position net of an allowance for doubtful accounts. This allowance 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. No amounts are impaired at March 31, 2014 and December 31, 2013.

Details of accounts receivable were as follows:

	March 31, 2014 $	December 31, 2013 $
1 – 30 days	**48,409**	315,486
30 – 60 days	**-**	4,500
61 – 90 days	**-**	20,745
Greater than 90 days	**251,670**	19,505
Total	**300,079**	360,236
Other receivable	**1,073**	1,068
	301,152	361,304

5. Costs in excess of billings

The Company had one contract in which the billings to date were less than the total costs incurred and recognized profits of $782,281 as at March 31, 2014 and $658,187 as at December 31, 2013 [Note 10].

6. Prepaid expenses and deposits

	March 31, 2014 $	December 31, 2013 $
Deposits	**57,530**	57,530
Prepaid expenses	**48,100**	55,000
	105,630	112,530

7. Property and equipment

	Computer hardware $	Computer software $	Machinery $	Torch asset under construction $	Leasehold improvements $	Equipment under finance lease $	Total $
Cost:							
Balance at December 31, 2013	**162,747**	**209,287**	**1,545,260**	**-**	**67,903**	**14,326**	**1,999,523**
Additions	**9,689**	**13,258**	**-**	**-**	**-**	**-**	**22,947**
Disposals	**-**	**-**	**-**	**-**	**-**	**-**	**-**
Balance at March 31, 2014	**172,436**	**222,545**	**1,545,260**	**-**	**67,903**	**14,326**	**2,022,470**
Accumulated depreciation :							
Balance at December 31, 2013	**(146,624)**	**(186,682)**	**(909,591)**	**-**	**(16,446)**	**(7,392)**	**(1,266,735)**
Depreciation	**(2,359)**	**(3,654)**	**(31,783)**	**-**	**(3,395)**	**(716)**	**(41,907)**
Balance at March 31, 2014	**(148,983)**	**(190,336)**	**(941,374)**	**-**	**(19,841)**	**(8,108)**	**(1,308,642)**
Net book value	**23,453**	**32,209**	**603,886**	**-**	**48,062**	**6,218**	**713,828**

	Computer hardware $	Computer software $	Machinery $	Torch asset under construction $	Leasehold improvements $	Equipment under finance lease $	Total $
Cost:							
Balance at December 31, 2012	157,594	203,114	1,545,260	925,417	67,903	14,326	2,913,614
Additions	5,153	6,173	-	314,408	-	-	325,734
Disposals	-	-	-	(1,239,825)[(i)]	-	-	(1,239,825)
Balance at December 31, 2013	162,747	209,287	1,545,260	-	67,903	14,326	1,999,523
Accumulated depreciation :							
Balance at December 31, 2012	(135,540)	(167,163)	(750,674)	-	(2,865)	(4,527)	(1,060,769)
Depreciation	(11,084)	(19,519)	(158,917)	-	(13,581)	(2,865)	(205,966)
Balance at December 31, 2013	(146,624)	(186,682)	(909,591)	-	(16,446)	(7,392)	(1,266,735)
Net book value	16,123	22,605	635,669	-	51,457	6,934	732,788

(i) Torch asset under construction was sold during 2013 to the other partner in the joint operation [note 10]. The asset was assessed at the time of sale for impairment and $581,638 was charged to comprehensive loss.

8. Intangible assets

Intangible assets consist of the following:

2014	**Intellectual property $**
Cost:	
Balance at December 31, 2013 and March 31, 2014	**8,409,051**
Accumulated amortization:	
Balance at December 31, 2013	**(4,218,228)**
Amortization	**(349,269)**
Balance at March 31, 2014	**(4,567,497)**
Net book value	**3,841,554**

2013	Intellectual property $
Cost:	
Balance at December 31, 2012 and December 31, 2013	8,409,051
Accumulated amortization:	
Balance at December 31, 2012	(2,821,155)
Amortization	(1,397,073)
Balance at December 31, 2013	(4,218,228)
Net book value	4,190,823

9. Accounts payable and accrued liabilities

	March 31, 2014 $	December 31, 2013 $
Accounts payable - trade	**362,244**	471,466
Accrued liabilities	**700,909**	550,522
Accounts payable - shareholder	**59,602**	29,537
Accounts payable - trust beneficially owned by a shareholder	**72,708**	104,132
	1,195,463	1,155,657

10. Joint operation

In 2011, the Company entered into an agreement with another company to share costs, benefits and risks associated with the development of a pilot plasma destruction unit which was included in Property and equipment in Note 7, as Torch asset under construction.

Prior to December 14, 2013, the Company had a 50% share in the joint operation.

On December 14, 2013, the Company entered into an agreement, whereby the Company agreed to sell its 50% ownership share in the pilot plasma destruction unit and related receivables and payables to its joint operation partner for a sum of $750,000, of which $600,000 is payable in 2014 upon the achievement of established milestones. At December 14, 2013, the asset was transferred from Property and equipment to Inventory, and an impairment loss of $581,638 was recorded prior to the transfer. In addition, revenues and cost of sales of $658,187, and costs in excess of billings of $286,403 were recorded at the time of sale. During 2014, the Company incurred costs in the amount of $124,094 in the advancement of its established milestones which has been recorded against Costs in excess of billings.

11. Billings in excess of costs and profits on uncompleted contracts

The amount to date of costs incurred and recognized profits less recognized losses for construction projects in progress amounted to $5,211,059 (December 31, 2013 - $4,528,715).

Payments received on contracts in progress were $7,031,846 (December 31, 2013 - $6,741,319).

Amounts billed and not yet received on contracts in progress of $250,000 (December 31, 2013 – $250,000) are included in accounts receivable.

12. Loans – other

	March 31, 2014	December 31, 2013
	$	$
Balance of sale - company under common control (i)	**7,828,226**	7,771,698
Amounts payable - trust beneficially owned by a shareholder (ii)	**387,756**	382,025
	8,215,982	8,153,723
Current portion	**-**	-
	8,215,982	8,153,723

(i) Balance of sale – company under common control is payable in monthly instalments of $40,000 from April 1, 2011 until December 31, 2040 with interest at an implicit rate of 4.753% per annum. The implicit rate of interest was based on the present value of cash flows having the same value as the intangible assets at the time of sale. The fair value of the intangible assets was based on an external independent valuation.

The face value of the balance of sale at March 31, 2014 was $13,408,416 ($13,438,416 at December 31, 2013).

Various amendments were made during 2012 and 2013 to defer and reduce monthly installments.

The unpaid amount of interest for the three months ended March 31, 2014 was added back to the balance of sale – company under common control in the amount of $56,528. (2013 - $Nil).

12. Loans – other (continued)

In the event that the Company should conclude a financing in excess of $3,000,000 before April 1, 2015, all deferred amounts will become immediately due and payable on the closing date of the financing. Additionally, in the event of any change within the Company that would be considered material by the holder of the balance of sale, such as a change in management, any and all amounts outstanding will become immediately due and payable on the date of the material change notwithstanding whether due or not at that date.

(ii) Amounts payable - trust beneficially owned by a shareholder is unsecured, bear interest at 6% and are not repayable before July 1, 2015. However, in the event that the Company should conclude a financing in excess of $3,000,000 before July 1, 2015, the full amount will become immediately due and payable on the closing date of the financing.

13. Shareholders' equity

Authorized:

The Company is authorized to issue an unlimited number of Class A common shares without par value.

Issues during 2014:

(i) None.

Issues during 2013:

(i) On December 20, 2013, the Company completed a private placement in which 3,660,000 units were issued at a price of $0.35 each for gross process of $1,281,000. Each unit consisted of one common share and one share purchase warrant exercisable at the strike price of $0.55 per common share until December 20, 2015. In the event that the volume weighted average price of the common shares on the TSX Venture Exchange is equal to or greater than $1.00 for a period of twenty (20) consecutive days, then the exercise period of the warrants will be reduced to 30 days from the first day following such 20-day period.

In accordance with the Black Scholes pricing model, the Company has allocated a value of $0.092 to each purchase warrant for a total value of $336,459 which has been credited to warrants reserve. The following assumptions under the Black Scholes model were used to arrive at this fair value.

Risk free interest rate	1.11%
Expected volatility	102%
Expected dividend yield	Nil
Expected life	2 years

Share issue costs associated with this transaction of $55,514 were paid in cash.

(ii) On March 29, 2013, the broker warrants issued with the private placement that occurred on March 29, 2012 expired.

13. Shareholders' equity (continued)

(iii) 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) of total share capital over a twelve month period.

On May 30, 2013, 100,000 options with an exercise price of $0.22 per share were granted. These options vest over one year starting on the date of grant. The value of each option under the Black Scholes pricing model is $0.057 for a total fair value of $5,342 of which $668 has been expensed and credited to contributed surplus in the current period ($Nil in 2013). The following assumptions under the Black Scholes model were used to arrive at the fair value:

Risk free interest rate	1.41%
Expected volatility	102%
Expected dividend yield	Nil
Expected life	5 years
Exercise price	$0.22
Forfeiture rate	5%

Stock option plan

The option activity, under the share option plan and information concerning outstanding and exercisable options, is as follows:

	Options issued	Weighted Average exercise price $
Balance – December 31, 2012	**4,576,000**	**0.27**
Options granted	**-**	**-**
Options forfeited	**-**	**-**
Balance – March 31, 2013	**4,576,000**	**0.27**
Options granted	**100,000**	**0.22**
Options forfeited	**(162,000)**	**0.28**
Balance – December 31, 2013	**4,514,000**	**0.27**
Options granted	**-**	**-**
Options forfeited	**(148,000)**	**0.33**
Balance – March 31, 2014	**4,366,000**	**0.27**

13. Shareholders' equity (continued)

As at March 31, 2014, the outstanding options, as issued under the stock option plan to directors, officers, employees and consultants for the purchases of one common share per option, are as follows:

Outstanding	Exercisable	Weighted averaged exercise price	Expiry date
500,000	300,000	0.800	July 2016
550,000	315,000	0.175	September 2017
210,000	128,000	0.150	September 2017
3,006,000	1,512,800	0.210	November 2017
100,000	50,000	0.220	May 2018
4,366,000	2,305,800	0.271	

Warrants

At March 31, 2014, the following exercisable warrants were outstanding:

	Granted	Exercisable	Weighted average exercise price	Expiry date
Balance – December 31, 2012	**4,734,274**	**4,734,274**	**$1.17**	
Expired	**(309,719)**	**(309,719)**	**$0.80**	
Warrants issued	**-**	**-**	**-**	
Balance – March 31, 2013	**4,424,555**	**4,424,555**	**$1.20**	**March 29, 2015**
Expired	**-**	**-**	**-**	
Warrants issued	**3,660,000**	**3,660,000**	**$0.55**	**December 20, 2015**
Balance – December 31, 2013	**8,084,555**	**8,084,555**	**$0.91**	
Expired	**-**	**-**	**-**	
Warrants issued	**-**	**-**	**-**	
Balance – March 31, 2014	**8,084,555**	**8,084,555**	**$0.91**	

14. Supplemental disclosure of expenses and cash flow information

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

For the three months ended March 31	**2014** **$**	2013 $
Decrease (increase) in:		
Accounts receivable	**60,152**	(83,119)
Sales tax receivable	**(13,095)**	36,889
Costs in excess of billings	**(124,094)**	-
Inventories	**(5,332)**	-
Investment tax credits receivable	**(18,156)**	(12,000)
Prepaid expenses and deposits	**6,900**	(10,512)
Increase (decrease) in:		
Accounts payable and accrued liabilities	**39,806**	(736,475)
Billings in excess of costs and profits on uncompleted contracts	**(391,817)**	(360,593)
	(445,636)	(1,165,810)

14. Supplemental disclosure of expenses and cash flow information (continued)

(ii) Interest and income taxes paid:

For the three months ended March 31	**2014**	2013
	$	$
Interest paid	**-**	-
Income taxes	**-**	-

15. Other information

Cost of sales and services includes the following items:

For the three months ended March 31	**2014**	2013
	$	$
Amortization of intangible assets	**349,269**	349,269
Employee compensation	**213,747**	224,074
Investment tax credits	**(18,156)**	(12,000)
Subcontracting	**3,202**	9,853
Direct materials	**163,056**	319,742
Utilities	**39,558**	20,065
Rent	**43,536**	43,536
Other expenses	**38,198**	25,313
	832,410	979,852

Selling, general and administrative includes the following items:

For the three months ended March 31	**2014**	2013
	$	$
Depreciation on property and equipment	**41,907**	48,333
Share-based payments	**50,000**	145,840
Employee compensation	**519,671**	547,378
Office and general	**80,190**	91,939
Professional fees	**165,435**	91,674
Travel	**39,365**	38,573
Other expenses	**50,350**	39,085
	946,918	1,002,822

Research and development includes the following items:

For the three months ended March 31	**2014**	2013
	$	$
Employee compensation	**122,420**	44,978
Subcontracting	**8,500**	10,583
Materials and equipment	**15,686**	974
Government grants	**(48,067)**	(39,299)
Other expenses	**1,062**	157
	99,601	17,393

16. Related party transactions

Rent was charged by a trust beneficially owned by a shareholder of the Company in the amount of $27,228 (2013 - $26,880). A balance due of $72,708 (December 31, 2013 - $104,132) is included in accounts payable and accrued liabilities.

Interest on amounts payable was charged by a trust beneficially owned by a shareholder of the Company in the amount of $5,731 (2013 - $7,198). The balance of interest that has not been paid of $107,673 (December 31, 2013 - $101,942) is included in loans - other.

Interest on balance of sale was charged by a company under common control in the amount of $86,528 (2013 - $88,079).

Fees of $30,000 were charged by directors (2013 - $19,506). A balance of $12,399 (December 31, 2013 – $22,167) is included in accounts payable and accrued liabilities.

Total compensation to key management consisted of salaries of $204,123 (2013 - $191,750) and pension contributions of $2,115 (2013 - $2,145). A balance of $98,184 (December 31, 2013 - $44,264) is included in accounts payable and accrued liabilities.

17. Loss per share

Basic loss per share amounts are calculated by dividing net loss for the period attributable to common shareholders by the weighted average number of common shares outstanding during the period.

The net loss and weighted average number of common shares used in the calculation of loss per share are as follows:

	2014	2013
	$	$
Net loss for the period	**1,164,728**	(954,139)
Weighted average number of Class A common shares - basic and diluted	**67,198,649**	63,538,649
Basic and diluted loss per share	**(0.02)**	(0.02)

The diluted weighted average number of shares is calculated assuming the proceeds that arise from the exercise of outstanding and in the money options and warrants are used to purchase Class A common shares of the Company at their average market price for the period. For the three months end March 31, 2014 and March 31, 2013, potential shares from all outstanding options and warrants have been excluded from the calculation of diluted loss per share as their inclusion is considered anti-dilutive in periods when a loss is incurred.

18. Financial instruments

As part of its operations, the Company carries a number of financial instruments. It is management's opinion that the Company is not exposed to significant interest, currency or credit risks arising from these financial instruments except as otherwise disclosed. The Company's overall risk management program focuses on the unpredictability of the financial market and seeks to minimize potential adverse effects on the Company's financial performance. The Company does not use derivative financial instruments to hedge these risks.

Foreign currency risk

The Company enters into transactions denominated in US Dollars for which the related revenues, expenses, accounts receivable and accounts payable and accrued liabilities balances are subject to exchange rate fluctuations.

As at March 31, 2014, the following items are denominated in foreign currencies

	US $	**CDN $**
Cash	**3,681**	**4,065**
Accounts receivables	**10,598**	**11,765**
Accounts payable and accrued liabilities	**(50,115)**	**(53,354)**
Total	**(35,836)**	**(37,524)**

As at December 31, 2013, the following items are denominated in foreign currencies:

	US $	**CDN $**
Cash	67,841	72,178
Accounts payable and accrued liabilities	(96,482)	(101,308)
Total	(28,641)	(29,130)

Foreign currency risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates. Management has implemented a policy to manage foreign exchange risk by using its purchases in U.S. dollars as a natural hedge against its revenue stream. Therefore the Company does not hold derivative financial instruments to manage the fluctuation of exchange rate risk.

Sensitivity analysis

At March 31, 2014, if the US Dollar changes by 10% against the Canadian dollar with all other variables held constant, the impact on after-tax loss for the three months ended March 31, 2014 would have been $3,600 (December 31, 2013 – $2,900).

18. Financial instruments (continued)

Credit concentration

As at March 31, 2014, one customer accounted for 77% (2013 – two customers for 64%) of revenues from operations and two customers accounted for 80% (December 31, 2013 – three customers for 90%) of the accounts receivable, representing the Company's major credit risk exposure. The Company believes that there is no unusual exposure associated with the collection of these receivables. The Company manages its credit risk by performing credit assessments of its customers and provides allowances for potentially uncollectible accounts receivable. The Company does not generally require collateral or other security from customers on accounts receivable.

Fair value of financial instruments

The classification of financial instruments at their carrying amount and fair values is as follows:

March 31, 2014	**Carrying value**			**Fair value**
	Fair value through profit or loss $	**Available for sale $**	**Loans and receivables $**	**Total $**
Financial assets:				
Cash	**52,253**	**-**	**-**	**52,253**
Accounts receivable	**-**	**-**	**301,152**	**301,152**
Sales tax receivable	**-**	**-**	**34,904**	**34,904**
Costs in excess of billings	**-**	**-**	**410,497**	**410,497**
Investment tax credit receivable	**-**	**-**	**120,094**	**120,094**
	52,253	**-**	**866,647**	**918,900**

March 31, 2014	**Carrying value**		**Fair value**
	Fair value through profit or loss $	**Other liabilities $**	**Total $**
Financial liabilities:			
Accounts payable and accrued liabilities	**-**	**1,195,463**	**1,195,463**
Loans - other	**-**	**8,215,982**	**7,597,755**
Obligation under finance lease	**-**	**8,196**	**8,196**
	-	**9,419,641**	**8,801,414**

18. Financial instruments (continued)

December 31, 2013	Carrying value			Fair value
	Fair value through profit or loss $	Available for sale $	Loans and receivables $	Total $
Financial assets:				
Cash	1,182,835	-	-	1,182,835
Accounts receivable	-	-	361,304	361,304
Sales tax receivable	-	-	21,809	21,809
Costs in excess of billings	-	-	286,403	286,403
Investment tax credit receivable	-	-	101,938	101,938
	1,182,835	-	771,454	1,954,289

December 31, 2013	Carrying value		Fair value
	Fair value through profit or loss $	Other liabilities $	Total $
Financial liabilities:			
Accounts payable and accrued liabilities	-	1,155,657	1,155,657
Loans - other	-	8,153,723	7,242,025
Obligation under finance lease	-	8,902	8,902
	-	9,318,282	8,406,584

The fair value of financial assets traded in active markets that are based on quoted market prices at the close of trading, which consists of cash, are classified as Level 1. A financial instrument is regarded as quoted in an active market if quoted prices are readily and regularly available from an exchange, dealer, broker, industry group, pricing service or regulatory agency and those prices represent actual and regularly occurring market transactions on an arm's length basis. The quoted market price used for financial assets held by the Company is the current bid price.

The fair value of financial assets and liabilities not traded in active markets that are based on unobservable inputs are classified as Level 3. A fair value measurement developed using a present value technique might be categorized within Level 3, depending on the inputs that are significant to the entire measurement and the level of the fair value hierarchy within which those inputs are categorized. If an observable input requires an adjustment using an unobservable input and that adjustment results in a significantly higher or lower fair value measurement, the resulting measurement would be categorized within Level 3 of the fair value hierarchy. The Company's Level 3 liability consists of an interest-free balance of sale - company under common control ("balance of sale") (presented under "loans - other"). The main inputs for the Company's internally developed valuation for its interest-free balance of sale include:

18. Financial instruments (continued)

- principal repayment schedule of the balance of sale;
- the principal (or most advantageous) market for the balance of sale;
- perspective of market participants at the measurement date:
- an estimate of future cash flows to (installments to be paid to) the holder of the balance of sale;
- expectations about possible variations in the amount and timing of the cash flows representing the uncertainty inherent in the timing of future principal repayments on the balance of sale;
- the time value of money, represented by the rate on risk-free monetary assets that have maturity dates or durations that coincide with the period covered by the cash flows and pose neither uncertainty in timing nor risk of default by the Company;
- the price for bearing the uncertainty inherent in timing and repayment of the balance of sale (i.e. a risk premium);
- typical discount rate for credit risk, default risk, liquidity risk and other concerns associated with debt investments.

The valuation technique makes the maximum use of market inputs and relies as little as possible on entity-specific inputs. The valuation technique appropriately considers the availability of data with which to develop inputs that represent the assumptions that market participants would use when pricing the asset and the level of the fair value hierarchy within which the inputs are categorized. Some of the inputs to the valuation model may not be market observable. Credit rating and financial position information for the Company may or may not be published or available. Accordingly, the fair value determination of the balance of sale follows a level 3 valuation methodology.

The Company uses a present value technique to estimate the fair value of the balance of sale. The Company uses expected cash flows (i.e., installment amounts) that are not risk-adjusted and a discount rate adjusted to include the risk premium that market participants require. The discount rate used for this technique is derived from observed rates of return for comparable assets or liabilities that are traded in the market. Accordingly, the most likely installment schedule is discounted at an observed or estimated market rate. Under the valuation method used by the Company, the expected installments are not adjusted for market risk. Rather, the adjustment for that risk is included in the discount rate. Thus, the expected installments are discounted at an expected rate of return of 5.698% (6.192% at December 31, 2013) (equivalent to the average yield on corporate bonds deemed to have a similar credit rating and a maturity date in our about 2040, yielding a fair value of approximately $7,210,000 ($6,860,000 at December 31, 2013) for the balance of sale.

The aggregate fair value of the balance of sale decreases by approximately $610,000 ($570,000 in 2013) for every 1% increment in the discount rate and increases by approximately $700,000 ($660,000 in 2013) for every 1% decrement in the discount rate.

The income approach (i.e., a present value technique that takes into account the future cash flows that a market participant would expect to receive from holding the debt instrument as an asset) was used to determine the fair value of the balance of sale. The market approach (i.e., using prices and other relevant information generated by market transactions involving identical liabilities) and the cost approach (i.e., the amount that would be required currently to extinguish the liability) could not be used to determine the fair value of the balance of sale. The output of a model is always an approximation of a value that cannot be determined with certainty. Accordingly, the valuation technique employed may not fully reflect all factors relevant to the liabilities the Company has.

18. Financial instruments (continued)

Liquidity risk

Liquidity risk is the risk that the Company will encounter difficulty in meeting obligations associated with financial liabilities that are settled by delivery of cash or another financial asset. The Company's ability to continue as a going concern is dependent on management's ability to raise required funding through future equity issuances and to generate positive cash flows from operations. The Company manages its liquidity risk by forecasting cash flows from operations and anticipating any investing and financing activities. Management and the Board of Directors are actively involved in the review, planning and approval of significant expenditures and commitments.

The following table summarizes the contractual maturities of financial liabilities as at March 31, 2014:

Financial liability	Total	Less than 1 year	1-3 years	Over 3 years	With no specific maturity
Accounts payable and accrued liabilities	**1,195,463**	**1,195,463**	**-**	**-**	**-**
Loans - other	**8,215,982**	**-**	**1,562,999**	**6,652,983**	**-**
Obligation under finance lease	**8,196**	**2,763**	**5,433**	**-**	**-**
	9,419,641	**1,198,226**	**1,568,432**	**6,652,983**	**-**

The following table summarizes the contractual maturities of financial liabilities as at December 31, 2013:

Financial liability	Total	Less than 1 year	1-3 years	Over 3 years	With no specific maturity
Accounts payable and accrued liabilities	1,155,657	1,155,657	-	-	-
Loans - other	8,153,723	-	1,289,505	6,864,218	-
Obligation under finance lease	8,902	2,763	6,139	-	-
	9,318,282	1,158,420	1,295,644	6,864,218	-

19. Subsequent event

On May 22, 2014, the Company completed a private placement in which 5,812,366 units were issued at a price of $0.60 per unit for gross proceeds of $3,487,420. Each unit consists of one common share and one-half of one common share purchase warrant (each whole Common Share purchase warrant, a “Warrant”). Each Warrant entitles its holder to acquire an additional Common Share (each, a “Warrant Share”) at an exercise price of $0.85 per Warrant Share for a period of 18 months following the closing of the Offering. Each Unit will be subject to a statutory hold period of four months and one day from the closing date of the Offering which expires on Sept 23, 2014.The warrants will be subject to accelerated expiry provisions, such that if at any time after the completion of the hold period, the closing price of the common shares on the TSX Venture is at least $1.20 per common share for a period of 20 consecutive trading days, the Company may accelerate the expiry date of the warrants, in which event the warrants will expire upon the date which is 20 days following the date the Company provides written notice of the accelerated expiry to holders.

The agent was paid a 7% cash commission totalling $195,119. The agent received 325,198 compensation options. Each compensation option is exercisable for one unit at the issue price of $0.60 for a period of 18 months from the closing of the offering.

The Company intends to use the net proceeds from the offering for general corporate purposes, working capital and development projects relating to recent business development efforts. The offering is subject to the final approval of the TSX Venture Exchange.

Also on May 22, 2014, the Company announced that it has entered into an agreement with its related party creditor, Phoenix Haute Technology Inc. ("Phoenix"), whereby the Company has requested and Phoenix has agreed to the Company issuing 7,500,000 common shares at a deemed price of $0.80 in payment of $6 million owing by the Company to Phoenix. The completion of this transaction is subject to the final approval of the TSX Venture Exchange.

The above subsequent events were press released by the Company on May 22, 2014.