PyroGenesis Canada Inc.

Condensed
Interim Financial Statements

Three and Six Months Ended June 30, 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 June 30, 2014.

PyroGenesis Canada Inc.

Condensed Interim Statement of Financial Position

(Unaudited)

As at	June 30, 2014 $	December 31, 2013 $
Assets		
Current assets		
Cash	**752,997**	1,182,835
Accounts receivable *[note 4]*	**423,106**	361,304
Sales tax receivable	**122,944**	21,809
Costs in excess of billings *[note 5]*	**642,290**	286,403
Inventories	**190,634**	180,442
Investment tax credits receivable	**137,257**	101,938
Prepaid expenses and deposits *[note 6]*	**476,218**	112,530
Total current assets	**2,745,446**	2,247,261
Non-current assets		
Property and equipment *[note 7]*	**688,775**	732,788
Intangible assets *[note 8]*	**3,492,286**	4,190,823
Total assets	**6,926,507**	7,170,872
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities *[note 9]*	**1,000,019**	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]*	**665,846**	2,462,604
Loans other – current portion *[note 12]*	**1,473,365**	-
Total current liabilities	**3,141,993**	3,621,024
Non-current liabilities		
Obligation under finance lease	**4,721**	6,139
Loans - other *[note 12]*	**752,491**	8,153,723
Total liabilities	**3,899,205**	11,780,886
Shareholders' equity (deficiency) *[note 13]*		
Common shares	**21,631,382**	13,138,554
Warrants reserve	**2,376,868**	1,778,999
Contributed surplus	**2,453,886**	2,325,386
Other equity	**24,844**	24,844
Deficit	**(23,459,678)**	(21,877,797)
	3,027,302	(4,610,014)
	6,926,507	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 August 29, 2014

Approved on behalf of the board:

[Signed by P. Peter Pascali] *P. Peter Pascali*

[Signed by Alan Curleigh] *Alan Curleigh*

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

PyroGenesis Canada Inc.

Condensed Interim Statement of Comprehensive Loss

(Unaudited)

	Three months ended June 30		Six months ended June 30	
	2014	2013	**2014**	2013
	$	$	**$**	$
Revenue	**1,958,534**	1,341,818	**2,764,959**	2,482,961
Cost of sales and services *[note15]*	**1,182,968**	1,146,397	**2,015,378**	2,126,249
Gross margin	**775,566**	195,421	**749,581**	356,712
Expenses				
Selling, general and administrative *[note15]*	**1,079,641**	1,005,746	**2,026,559**	2,008,568
Research and development *[note15]*	**29,099**	76,429	**128,700**	93,822
Financing charges	**85,045**	90,140	**177,304**	185,355
	1,193,785	1,172,315	**2,332,563**	2,287,745
Loss from operations	**(418,219)**	(976,894)	**(1,582,982)**	(1,931,033)
Other income	**1,066**	1,421	**1,101**	1,421
Comprehensive loss	**(417,153)**	(975,473)	**(1,581,881)**	(1,929,612)
Basic and diluted loss per share	**$(0.01)**	$(0.02**)**	**$(0.02)**	$(0.03)
Weighted average number of common shares outstanding - basic and diluted *[note 17]*	**72,967,821**	63,538,649	**70,099,172**	63,538,649

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

PyroGenesis Canada Inc.

Condensed Interim Statement of Changes in Equity (Deficiency)

(Unaudited)
Six months ended June 30

	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)**
Brokered private placement – *[note 13(i)]*	**4,645,699**	**2,787,419**	**-**	**-**	**-**	**-**	**2,787,419**
Non-brokered private placement – *[note 13(i)]*	**1,166,667**	**700,000**	**-**	**-**	**-**	**-**	**700,000**
Fair value warrants – *[note 13(i)]*	**-**	**(505,676)**	**505,676**	**-**	**-**	**-**	**-**
Brokers' fee - cash payment – *[note 13(i)]*	**-**	**(195,119)**	**-**	**-**	**-**	**-**	**(195,119)**
Broker warrants – *[note 13(i)]*	**-**	**(92,193)**	**92,193**	**-**	**-**	**-**	**-**
Legal fees related with private placement – *[note 13(i)]*	**-**	**(123,416)**	**-**	**-**	**-**		**(123,416)**
Additional fees related with private placement – *[note 13(i)]*	**-**	**(48,187)**	**-**	**-**	**-**	**-**	**(48,187)**
Debt to equity conversion – *[note 13(ii)]*	**7,500,000**	**6,000,000**	**-**	**-**	**-**	**-**	**6,000,000**
Debt to equity conversion- TSX Venture fee – *[note 13(i)]*	**-**	**(30,000)**	**-**	**-**	**-**	**-**	**(30,000)**
Shared-based payments	**-**	**-**	**-**	**128,500**	**-**	**-**	**128,500**
Comprehensive loss during the period	**-**	**-**	**-**	**-**	**-**	**(1,581,881)**	**(1,581,881)**
Balance – June 30, 2014	**80,511,015**	**21,631,382**	**2,376,868**	**2,453,886**	**24,844**	**(23,459,678)**	**3,027,302**

	Number of Class A common shares	Class A common share capital $	Warrants reserve $	Contributed surplus $	Other Equity $	Deficit $	Total $
Balance – December 31, 2012	63,538,649	12,249,527	1,497,948	1,663,090	24,844	(17,889,720)	(2,454,311)
Share-based payments	-	-	-	295,625	-	-	295,625
Expired warrants – *[note 13(iv)]*	-	-	(55,408)	55,408	-	-	-
Comprehensive loss during the period	-	-	-	-	-	(1,929,612)	(1,929,612)
Balance – June 30, 2013	63,538,649	12,249,527	1,442,540	2,014,123	24,844	(19,819,332)	(4,088,298)

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

PyroGenesis Canada Inc.

Condensed Interim Statement of Cash Flows

(Unaudited)

	Three months ended June 30		Six months ended June 30	
	2014	2013	**2014**	2013
	$	$	**$**	$
Cash flows provided (used) in				
Operating activities				
Comprehensive loss	**(417,153)**	(975,473)	**(1,581,881)**	(1,929,612)
Items not requiring an outlay of cash:				
Share-based payments	**78,500**	149,785	**128,500**	295,625
Depreciation on property and equipment *[note 7]*	**42,603**	45,461	**84,509**	93,794
Amortization of intangible assets *[note 8]*	**349,268**	349,268	**698,537**	698,537
	53,218	(430,959)	**(670,335)**	(841,656)
Net change in non-cash operating working capital items *[note 14]*	**(2,434,784)**	504,429	**(2,880,419)**	(661,381)
	(2,381,566)	73,470	**(3,550,754)**	(1,503,037)
Investing activity				
Purchase of property and equipment *[note 7]*	**(17,549)**	(59,059)	**(40,496)**	(59,059)
Financing activities				
Repayment of obligation under finance lease	**(712)**	(689)	**(1,418)**	(1,371)
Proceeds from (repayment of) loans - other	**9,874**	31,405	**72,133**	(23,318)
Proceeds from issuance of common shares	**3,487,419**	-	**3,487,419**	-
Costs related to issuance of common shares	**(366,722)**	-	**(366,722)**	-
Costs related to debt to equity conversion	**(30,000)**		**(30,000)**	
	3,099,859	30,716	**3,161,412**	(24,689)
Increase (decrease) in cash	**700,744**	45,127	**(429,838)**	(1,586,785)
Cash - beginning of period	**52,253**	563,659	**1,182,835**	2,195,571
Cash - end of period	**752,997**	608,786	**752,997**	608,786

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 August 29, 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 $1,581,881 of losses occurring in 2014 and has an accumulated deficit of $23,459,678 at June 30, 2014. In addition, the Company's current liabilities exceed its current assets as at June 30, 2014 in the amount of $396,547. 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.

(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 June 30, 2014 but are not yet effective. The Company does not plan to early adopt any of these new or amended standards and interpretations.

3. Significant accounting policies (continued)

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.

IFRS 15 – Revenue from Contracts with Customers

In May 2014, the IASB released IFRS 15, *Revenue from contracts with customers*, which supersedes IAS 11, *Construction Contracts*, IAS 18, *Revenues*, IFRIC 13, *Customer Loyalty Programs*, IFRIC 15, *Agreement for the Construction of Real Estate*, IFRIC 18, *Transfers of Assets from Customers* and SIC-31, *Revenue – Barter Transactions Involving Advertising Services*. The core principle of IFRS 15 is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. IFRS 15 will also result in enhanced disclosures about revenue, provide guidance for transactions that were not previously addressed comprehensively (for example, service revenue and contract modifications) and improve guidance for multiple-element arrangements. IFRS 15 will be effective for the Company's fiscal year beginning on January 1, 2017, with earlier application permitted. The Company has not yet assessed the impact of the adoption of this standard on its financial statements.

3. Significant accounting policies (continued)

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 June 30, 2014 and December 31, 2013.

Details of accounts receivable were as follows:

	June 30, 2014 $	December 31, 2013 $
1 – 30 days	**12,187**	315,486
30 – 60 days	**87,555**	4,500
61 – 90 days	**54,878**	20,745
Greater than 90 days	**263,435**	19,505
Total	**418,055**	360,236
Other receivable	**5,051**	1,068
Total accounts receivable	**423,106**	361,304

5. Costs in excess of billings

The Company had two contracts in which the billings to date were less than the total costs incurred. The recognized revenue on these contracts amounted to $1,014,076 as at June 30, 2014 and $658,187 as at December 31, 2013 [Note 10].

6. Prepaid expenses and deposits

	June 30, 2014 $	December 31, 2013 $
Deposits	**57,530**	57,530
Prepaid expenses	**418,688**	55,000
	476,218	112,530

7. Property and equipment

	Computer hardware $	Computer software $	Machinery $	Automobiles $	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	**11,573**	**13,258**	**-**	**15,665**	**-**	**-**	**40,496**
Disposals	**-**	**-**	**-**	**-**	**-**	**-**	**-**
Balance at June 30, 2014	**174,320**	**222,545**	**1,545,260**	**15,665**	**67,903**	**14,326**	**2,040,019**
Accumulated depreciation:							
Balance at December 31, 2013	**(146,624)**	**(186,682)**	**(909,591)**	**-**	**(16,446)**	**(7,392)**	**(1,266,735)**
Depreciation	**(4,824)**	**(7,308)**	**(63,567)**	**(587)**	**(6,790)**	**(1,433)**	**(84,509)**
Balance at June 30, 2014	**(151,448)**	**(193,990)**	**(973,158)**	**(587)**	**(23,236)**	**(8,825)**	**(1,351,244)**
Net book value	**22,872**	**28,555**	**572,102**	**15,078**	**44,667**	**5,501**	**688,775**

	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 June 30, 2014	**8,409,051**
Accumulated amortization:	
Balance at December 31, 2013	**(4,218,228)**
Amortization	**(698,537)**
Balance at June 30, 2014	**(4,916,765)**
Net book value	**3,492,286**

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

	June 30, 2014 $	December 31, 2013 $
Accounts payable - trade	**252,397**	471,466
Accrued liabilities	**701,725**	550,522
Accounts payable - shareholder	**45,897**	29,537
Accounts payable - trust beneficially owned by a shareholder	**-**	104,132
	1,000,019	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 $250,796 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 $6,933,769 (December 31, 2013 - $4,528,715).

Payments received on contracts in progress were $ 7,349,615 (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

	June 30, 2014 $	December 31, 2013 $
Balance of sale - company under common control (i)	**1,832,284**	7,771,698
Amounts payable - trust beneficially owned by a shareholder (ii)	**393,572**	382,025
	2,225,856	8,153,723
Current portion	**1,473,365**	-
	752,491	8,153,723

(i) Balance of sale – company under common control (“Balance of Sale”) arose from the purchase of the intangible assets in March 2011. Under the purchase agreement, the consideration was to be payable in monthly instalments of $40,000 from April 1, 2011 until December 31, 2040 with an implicit interest 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.

12. Loans – other (continued)

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

On May 23, 2014, the Company completed a share for debt transaction by issuing 7,500,000 common shares at a deemed price of $0.80 per common share to settle $6,000,000 of the carrying value of the Balance of sale, being the last two-hundred and eight-five and a half monthly payments owed by the Company under the purchase agreement.

The face value of the balance of sale at June 30, 2014 was $1,908,416 ($13,438,416 at December 31, 2013). As part of the May 23, 2014 debt to share conversion (see note 13(ii)), $11,420,000 of the face value of the balance of sale was settled.

The unpaid amount of interest for the six months ended June 30, 2014 was added to the Balance of Sale in the amount of $ 115,105 (2013 - $Nil).

The amount of deferred payments which resulted from the various amendments and contained within the face value of the balance of sale total $648,416 at June 30, 2014 ($478,416 at December 31, 2013).

On June 1, 2014, the Company signed an amending agreement to amend the terms and conditions of the balance of sale-company under common control. Based on the new amendment, each installment due on June 1, 2014 and thereafter shall resume at $40,000 per month. Furthermore staring on November 1, 2014, the Company shall commencement payments of $100,000 per month against the deferred payments due until said debt is fully paid.

(ii) Amounts payable - trust beneficially owned by a shareholder is unsecured and bears interest at 6%. As the Company concluded the May 22, 2014 private placement, the amounts became payable.

On June 1, 2014, the Company signed an amending agreement to amend the previous amending agreement to defer the debt owed. Based on the new agreement, starting January 1, 2015, the Company shall make payments of $75,000 per month until the amount payable has been fully paid.

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) On May 22, 2014, the Company completed a private placement in which 5,812,366 units were issued at a price of $0.60 each for gross process of $3,487,419. Each unit consisted of one common share and one-half of one common share purchase warrant, each whole Common Share purchase warrant ("Warrant Share") is exercisable at the strike price of $0.85 per common share expiring November 22, 2015 (18 months from the closing date). In the event that the volume weighted average price of the common shares on the TSX Venture Exchange is equal to or greater than $1.20 for a period of twenty (20) consecutive trading days, then 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 of holders. The common shares issued are subject to a four month and one day hold period from the date of issuance.

13. Shareholders' equity (continued)

In accordance with the Black Scholes pricing model, the Company has allocated a value of $0.087 to each purchase warrant for a total value of $505,676 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	18 months

On closing, the agents received a cash commission totalling $195,119, and 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 transaction.

In accordance with the Black Scholes pricing model, the Company has allocated a value of $0.283 to each compensation option based on the value of the underlying purchase warrant for a total value of $92,193 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	18 months

Share issue costs associated with this transaction of $171,603 were paid in cash.

(ii) On May 23, 2014, the Company completed a share for debt transaction by issuing 7,500,000 common shares at a deemed price of $0.80 per common share to settle $6,000,000 of the carrying value of the Balance of Sale (note 12 (i)). The common shares issued are subject to a four month and one day hold period from the date of issuance.

Share issue costs associated with this transaction of $30,000 were paid in cash.

Issues during 2013:

(iii) 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.

13. Shareholders' equity (continued)

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

(v) 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 $230 has been expensed and credited to contributed surplus in the current period ($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	**100,000**	**$0.22**
Options forfeited	**-**	**-**
Balance –June 30, 2013	**4,676,000**	**$0.27**
Options granted	**-**	**-**
Options forfeited	**(162,000)**	**$0.28**
Balance – December 31, 2013	**4,514,000**	**$0.27**
Options granted	**-**	**-**
Options forfeited	**(193,000)**	**$0.30**
Balance – June 30, 2014	**4,321,000**	**$0.27**

13. Shareholders' equity (continued)

As at June 30, 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
2,961,000	1,490,300	$0.210	November 2017
100,000	50,000	$0.220	May 2018
4,321,000	2,283,300	$0.271	

Warrants

At June 30, 2014, the following exercisable warrants were outstanding:

	Granted and Exercisable	Weighted average exercise price	Expiry date
Balance – December 31, 2012	4,734,274	$1.17	
Expired	(309,719)	$ 0.80	
Warrants issued	-	-	
Balance – June 30, 2013	4,424,555	$1.20	March 29,2015
Expired	-	-	
Warrants issued	3,660,000	$0.55	December 20, 2015
Balance – December 31, 2013	8,084,555	$0.91	
Expired	-	-	
Warrants issued	2,906,183	$0.85	November 22, 2015
Broker compensation options issued (note 13(i))	325,198	$0.60	November 22, 2015
Balance – June 30, 2014	11,315,936	$0.88	

14. Supplemental disclosure of expenses and cash flow information

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

	Three months ended June 30		Six months ended June 30	
	2014	2013	**2014**	2013
	$	$	**$**	$
Decrease (increase) in:				
Accounts receivable	**(121,954)**	(992,236)	**(61,802)**	(1,075,355)
Sales tax receivable	**(88,040)**	(54,860)	**(101,135)**	(17,971)
Costs in excess of billings	**(231,793)**	-	**(355,887)**	
Inventories	**(4,860)**	(205,405)	**(10,192)**	(205,405)
Investment tax credits receivable	**(17,163)**	168,179	**(35,319)**	156,179
Prepaid expenses and deposits	**(370,589)**	2,412	**(363,688)**	(8,100)
Increase (decrease) in:				
Accounts payable and accrued liabilities	**(195,444)**	290,297	**(155,638)**	(446,178)
Billings in excess of costs and profits on uncompleted contracts	**(1,404,941)**	1,296,042	**(1,796,758)**	935,449
	(2,434,784)	504,429	**(2,880,419)**	(661,381)

(ii) Interest and income taxes paid:

	Three months ended June 30		Six months ended June 30	
	2014	2013	**2014**	2013
	$	$	**$**	$
Interest paid	**79,229**	$87,698	**$165,758**	$175,777
Income taxes	**-**	-	**-**	-

15. Other information

Cost of sales and services includes the following items:

	Three months ended June 30		Six months ended June 30	
	2014	2013	**2014**	2013
	$	$	**$**	$
Amortization of intangible assets	**349,268**	349,268	**698,537**	698,537
Employee compensation	**313,410**	186,984	**527,157**	411,058
Investment tax credits	**(17,163)**	(7,700)	**(35,319)**	(19,700)
Subcontracting	**8,949**	5,135	**12,151**	14,988
Direct materials	**389,446**	566,205	**552,502**	885,947
Utilities	**14,788**	21,297	**54,346**	41,362
Rent	**46,935**	43,535	**90,471**	87,071
Other expenses	**77,335**	(18,327)	**115,533**	6,986
	1,182,968	1,146,397	**2,015,378**	2,126,249

Selling, general and administrative includes the following items:

	Three months ended June 30		Six months ended June 30	
	2014	2013	**2014**	2013
	$	$	**$**	$
Depreciation on property and equipment	**42,602**	45,461	**84,509**	93,794
Share-based payments	**78,500**	149,785	**128,500**	295,625
Employee compensation	**565,174**	528,744	**1,084,845**	1,076,122
Office and general	**78,886**	80,240	**159,076**	172,179
Professional fees	**215,959**	162,720	**381,394**	254,394
Travel	**42,138**	26,035	**81,503**	64,608
Other expenses	**56,382**	12,761	**106,732**	51,846
	1,079,641	1,005,746	**2,026,559**	2,008,568

Research and development includes the following items:

	Three months ended June 30		Six months ended June 30	
	2014	2013	**2014**	2013
	$	$	**$**	$
Employee compensation	**29,978**	81,169	**152,398**	126,147
Subcontracting	**7,610**	14,364	**16,110**	24,947
Materials and equipment	**3,101**	17,461	**18,787**	18,435
Government grants	**(12,316)**	(36,703)	**(60,383)**	(76,002)
Other expenses	**726**	138	**1,788**	295
	29,099	76,429	**128,700**	93,822

16. Related party transactions

During the three and six month period ended June 30, 2014, rent was charged by a trust beneficially owned by a shareholder of the Company in the amount of $28,461 and $55,689 respectively (2013 - $27,008 and $53,888). A balance due of $22,288 (December 31, 2013 - $104,132) is included in accounts payable and accrued liabilities.

During the three and six month period ended June 30, 2014, interest on amounts payable was charged by a trust beneficially owned by a shareholder of the Company in the amount of $5,816 and $11,547 respectively (2013 - $3,707 and $10,905). The balance of interest that has not been paid of $113,488 (December 31, 2013 - $101,942) is included in loans - other.

During the three and six month period ended June 30, 2014, interest on balance of sale was charged by a company under common control in the amount of $79,229 and $ 165,757 respectively (2013 - $87,698 and $175,777).

During the three and six month period ended June 30, 2014, fees of $21,000 and $51,000 respectively were charged by directors (2013 - $32,000 and $51,506). A balance of $9,000 (December 31, 2013 – $22,167) is included in accounts payable and accrued liabilities.

During the three and six month period ended June 30, 2014, total compensation to key management consisted of salaries of $206,309 and $410,432 respectively (2013 - $192,250 and $384,000) and pension contributions of $2,307 and $4,649 respectively (2013 - $2,153 and $4,298. A balance of $62,317 (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:

	Three months ended June 30		Six months ended June 30	
	2014	2013	**2014**	2013
	$	$	$	$
Net loss for the period	**(417,153)**	(975,473)	**(1,581,881)**	(1,929,612)
Weighted average number of Class A Common shares- basic and diluted	**72,967,821**	63,538,649	**70,099,172**	63,538,649
Basic and diluted loss per share	**(0.01)**	(0.02)	**(0.02)**	(0.03)

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 and six months ended June 30, 2014 and June 30, 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 June 30, 2014, the following items are denominated in foreign currencies

	US $	CDN Equivalent $
Cash	**55,458**	**59,187**
Accounts receivables	**141,186**	**154,198**
Accounts payable and accrued liabilities	**(58,916)**	**(64,237)**
Total	**137,728**	**149,148**

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 June 30, 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 six months ended June 30, 2014 would have been $14,000 (December 31, 2013 – $2,900).

18. Financial instruments (continued)

Credit concentration

As at June 30, 2014, three customers accounted for 83% (2013 – two customers for 76%) of revenues from operations and three customers accounted for 94% (December 31, 2013 – two customers for 89%) 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:

June 30, 2014	**Carrying value**			**Fair value**
	Fair value through profit or loss $	**Available for sale $**	**Loans and receivables $**	**Total $**
Financial assets:				
Cash	**752,997**	**-**	**-**	**752,997**
Accounts receivable	**-**	**-**	**423,106**	**423,106**
Sales tax receivable	**-**	**-**	**122,944**	**122,944**
Costs in excess of billings	**-**	**-**	**642,290**	**642,290**
Investment tax credit receivable	**-**	**-**	**137,257**	**137,257**
	752,997	**-**	**1,325,597**	**2,078,594**

June 30, 2014	**Carrying value**		**Fair value**
	Fair value through profit or loss $	**Other liabilities $**	**Total $**
Financial liabilities:			
Accounts payable and accrued liabilities	**-**	**1,000,019**	**1,000,019**
Loans - other	**-**	**2,225,856**	**2,103,572**
Obligation under finance lease	**-**	**7,484**	**7,484**
	-	**3,233,359**	**3,111,075**

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 10.0% (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 2017 for the June 30, 2014 fair value calculation and in or about 2040 for the December 31, 2013 fair value calculation, yielding a fair value of approximately $1,710,000 ($6,860,000 at December 31, 2013) for the balance of sale.

The aggregate fair value of the balance of sale decreases by approximately $140,000 ($570,000 in 2013) for every 1% increment in the discount rate and increases by approximately $180,000 ($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 June 30,2014:

Financial liability	**Total**	**Less than 1 year**	**1-3 years**	**Over 3 years**	**With no specific maturity**
Accounts payable and accrued liabilities	**1,000,019**	**1,000,019**	**-**	**-**	**-**
Loans - other	**2,225,856**	**1,473,365**	**752,491**	**-**	**-**
Obligation under finance lease	**7,484**	**2,763**	**4,721**	**-**	**-**
	3,233,359	**2,476,147**	**757,212**	**-**	**-**

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 July 16, 2014, the Company received a down payment of $440,000 on a contract to supply ten metal powder production platforms over an 18 month period for a contract value of $12,500,000.