

**ProSep Inc.**  
**Unaudited Consolidated Interim Financial Statements**  
**For the three and nine-month periods ended**  
**September 30, 2009**

ProSep Inc.  
Consolidated statements of income (loss) and comprehensive income (loss)  
For the three-month and nine-month periods ended September 30, 2009 and 2008

(Unaudited)

	Three months ended September 30,		Nine months ended September 30,	
	2009	2008	2009	2008
	\$	\$	\$	\$
<b>Revenue (Note 3)</b>	<b>9,186,352</b>	12,547,837	<b>31,689,103</b>	36,805,714
<b>Cost of goods sold</b>	<b>6,523,948</b>	8,399,117	<b>22,093,579</b>	26,387,629
<b>Gross margin</b>	<b>2,662,404</b>	4,148,720	<b>9,595,524</b>	10,418,085
<b>Expenses</b>				
Sales and marketing	539,185	491,551	1,644,836	1,481,606
Research and development	95,140	353,922	395,773	921,705
General and administrative	2,660,772	1,989,463	7,861,851	5,765,154
	<b>3,295,097</b>	2,834,936	<b>9,902,460</b>	8,168,465
	<b>(632,693)</b>	1,313,784	<b>(306,936)</b>	2,249,620
<b>Impairment of goodwill (Note 4)</b>	-	-	<b>6,500,000</b>	-
<b>Decrease (increase) in fair value of investment in ABCP</b>	<b>(400,000)</b>	-	<b>(400,000)</b>	450,000
<b>Financial charges (Note 5)</b>	<b>2,742,592</b>	(1,311,358)	<b>4,773,825</b>	1,213,864
<b>Amortization</b>	<b>410,637</b>	359,685	<b>1,180,816</b>	1,100,826
<b>Income (loss) before income taxes</b>	<b>(3,385,922)</b>	2,265,457	<b>(12,361,577)</b>	(515,070)
<b>Current tax provision (recovery)</b>	<b>(74,047)</b>	474,769	<b>111,038</b>	1,244,796
<b>Future tax provision (recovery)</b>	<b>128,383</b>	(56,856)	<b>100,011</b>	(107,474)
<b>Income taxes</b>	<b>54,336</b>	417,913	<b>211,049</b>	1,137,322
<b>Net income (loss) and comprehensive income (loss)</b>	<b>(3,440,258)</b>	1,847,544	<b>(12,572,626)</b>	(1,652,392)
<b>Weighted average number of shares (basic)</b>	<b>130,840,835</b>	62,556,566	<b>86,819,126</b>	62,556,566
<b>Weighted average number of shares (diluted)</b>		73,867,677		
<b>Basic and diluted earnings (loss) per share (Note 6)</b>	<b>(0.03)</b>	0.03	<b>(0.14)</b>	(0.03)

The accompanying notes are an integral part of these consolidated financial statements

**ProSep Inc.**  
**Consolidated balance sheets**  
**As at September 30, 2009 and December 31, 2008**  
**(Unaudited)**

	September 30, 2009	Audited December 31, 2008
	\$	\$
<b>Assets</b>		
Current assets		
Cash and cash equivalents	2,680,662	7,615,119
Restricted cash (Note 7)	-	1,037,846
Receivables (Note 8)	18,862,626	20,004,848
Inventories	464,751	669,881
Prepaid expenses	714,493	886,085
Income tax receivable	371,697	-
Future tax assets	202,145	-
	<b>23,296,374</b>	<b>30,213,779</b>
Restricted cash (Note 7)	-	3,158,986
Long-term investment (Note 9)	5,827,424	5,815,000
Property and equipment	1,665,132	1,856,279
Goodwill (Note 4)	13,907,126	20,407,126
Intangible assets	7,343,012	7,852,042
Future tax assets	-	192,398
	<b>52,039,068</b>	<b>69,495,610</b>
<b>Liabilities</b>		
Current liabilities		
Bank credit facilities (Note 10)	2,565,602	11,596,044
Accounts payable and accrued liabilities	11,688,820	20,953,507
Income tax payable	-	114,043
Deferred revenue	201,249	484,078
Current portion of long term debt (Note 12)	1,721,052	3,322,106
	<b>16,176,723</b>	<b>36,469,778</b>
Long-term debt (Note 12 (a))	15,018,084	12,087,493
Future tax liabilities	1,158,512	1,117,599
Pension obligation (Note 13)	415,717	289,838
	<b>32,769,036</b>	<b>49,964,708</b>
<b>Shareholders' equity</b>		
Share capital (Note 11)	72,010,934	55,488,839
Contributed surplus	11,401,667	12,527,139
Deficit	(64,142,569)	(48,485,076)
	<b>19,270,032</b>	<b>19,530,902</b>
	<b>52,039,068</b>	<b>69,495,610</b>

Going concern (Note 1)  
Contingent liabilities (Note 15)

**Approved by the Board**

" **Jacques L. Drouin**" ..... Jacques L. Drouin, Director

" **David Laidley**" ..... David Laidley, Director

The accompanying notes are an integral part of these consolidated financial statements

**ProSep Inc.**  
**Consolidated statements of contributed surplus**  
**For the nine-month periods ended September 30, 2009 and 2008**  
**(Unaudited)**

	<b>Nine months ended September 30, 2009</b>				Total contributed surplus
	Stock-based compensation	Warrants	Conversion feature of loans	Other	
	\$	\$	\$		\$
Contributed surplus as at December 31, 2008	2,548,774	8,000,821	1,977,544		12,527,139
Stock-based compensation	262,877	-	-		262,877
Induced conversion and settlement of convertible debentures (Note 12 (a))			(1,977,544)	417,635	(1,559,909)
Issuance of new convertible debentures (Note 12 (a))			171,560		171,560
<b>Contributed surplus as at September 30, 2009</b>	<b>2,811,651</b>	<b>8,000,821</b>	<b>171,560</b>	<b>417,635</b>	<b>11,401,667</b>

	<b>Nine months ended September 30, 2008</b>				Total contributed surplus
	Stock-based compensation	Warrants	Conversion feature of loans		
	\$	\$	\$		\$
Contributed surplus as at December 31, 2007	2,066,473	7,433,980	632,273		10,132,726
Stock-based compensation	338,438	-	-		338,438
Value of warrants issued from convertible debenture		566,841			566,841
Debenture convertible feature			1,345,271		1,345,271
<b>Contributed surplus as at September 30, 2008</b>	<b>2,404,911</b>	<b>8,000,821</b>	<b>1,977,544</b>		<b>12,383,276</b>

The accompanying notes are an integral part of these consolidated financial statements

**ProSep Inc.**  
**Consolidated statements of deficit**  
**For the nine-month periods ended September 30, 2009 and 2008**  
**(Unaudited)**

	Nine months ended September 30,	
	2009	2008
	\$	\$
Deficit, beginning of the period	(48,485,076)	(46,605,116)
Share issue costs (Note 11)	(886,470)	(254,903)
Inducement for debt conversion (Note 12 (a))	(2,198,397)	
Net loss and comprehensive loss	(12,572,626)	(1,652,392)
Deficit, end of the period	(64,142,569)	(48,512,411)

The accompanying notes are an integral part of these consolidated financial statements

**ProSep Inc.**  
**Consolidated statements of cash flows**  
**For the three-month and nine-month periods ended September 30, 2009 and 2008**

(Unaudited)

	Three months ended		Nine months ended	
	September 30,		September 30,	
	2009	2008	2009	2008
	\$	\$	\$	\$
<b>Operating activities</b>				
Net loss and comprehensive loss	(3,440,258)	1,847,544	(12,572,626)	(1,652,392)
Interests and principal received on investment in ABCP and replacement n	11,239	-	387,576	-
Items not affecting cash				
Stock-based compensation	100,163	83,719	262,877	338,438
Amortization of property and equipment	241,101	190,009	671,928	591,796
Amortization of intangible assets	169,679	169,676	509,031	509,030
Accreted interest	47,883	133,208	421,785	272,387
Impairment of goodwill	-	-	6,500,000	-
Decrease (increase) in fair value of investment in ABCP	(400,000)	-	(400,000)	450,000
Loss on debt induced conversion	2,071,543	-	2,071,543	-
Periodic pension cost in excess of contribution	35,255	10,783	125,879	32,399
Future income taxes	250,010	56,856	221,638	(107,474)
Change in fair value of derivative financial instruments	-	(179,571)	-	(143,550)
Unrealized exchange loss (gain)	(598,793)	(1,498,444)	(711,896)	(176,338)
	(1,512,178)	813,780	(2,512,265)	114,296
Changes in operating working capital items	(4,736,145)	(5,805,382)	(7,696,420)	(6,060,331)
	(6,248,323)	(4,991,602)	(10,208,685)	(5,946,035)
<b>Investing activities</b>				
Acquisition of property and equipment	(138,760)	(195,116)	(480,788)	(489,864)
	(138,760)	(195,116)	(480,788)	(489,864)
<b>Financing activities</b>				
Restricted cash released	-	-	4,196,832	-
Bank credit facilities	(236,356)	-	(1,835,292)	-
Increase in long term debt	-	-	67,906	4,762,473
Share issued (net of expenses)	4,113,530	-	4,113,530	(141,777)
Reimbursement of long-term debt and debt issue cost	(207,547)	(6,409)	(1,059,386)	(904,345)
	3,669,627	(6,409)	5,483,590	3,716,351
Effect of exchange rate on cash and cash equivalents	(37,596)	(43,790)	271,426	93,744
<b>Increase (Decrease) in cash and cash equivalents</b>	<b>(2,755,052)</b>	<b>(5,263,049)</b>	<b>(4,934,457)</b>	<b>(2,813,292)</b>
<b>Cash and cash equivalents, beginning of period</b>	<b>5,435,714</b>	<b>11,249,925</b>	<b>7,615,119</b>	<b>8,662,634</b>
<b>Cash and cash equivalents, end of period</b>	<b>2,680,662</b>	<b>5,943,086</b>	<b>2,680,662</b>	<b>5,943,086</b>

The accompanying notes are an integral part of these consolidated financial statements

**ProSep Inc.**

**Notes to the consolidated financial statements (Unaudited)**

**For the three-month and nine-month periods ended September 30, 2009 and 2008**

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**1. Financial statement presentation and going concern**

The unaudited interim consolidated financial statements of ProSep Inc. ("The Company") have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP") applicable to interim financial statements, following the same accounting policies as those outlined in Note 2 to the consolidated financial statements for the year ended December 31, 2008 with the exceptions disclosed in Note 2 below.

The interim financial statements should be read in conjunction with the most recent annual consolidated financial statements.

The accompanying financial statements have been prepared using Canadian generally accepted accounting principles applicable to a going concern, which assumes the Company will be able to realize the carrying value of its assets and discharge its liabilities in the normal course of operations.

The Company has incurred losses of \$12,572,626 for the nine-month period ended September 30, 2009, had an accumulated deficit of \$64,142,569 and has not, so far, generated positive cash flows from operations. In addition the Company is subject to several restrictive financial covenants. Such conditions require that the Company continuously seeks non operational sources of financing to fund its operations as well as work on achieving profitability in a near future. The Company has concluded in April a new covenant structure with DnB Nor allowing for the release of the \$3,339,022 (18 000 000 NOK) that was held in a separate escrowed bank account. The Company also accepted an offer from National Bank regarding revolving term loans totaling \$7,180,564 in replacement of the \$7,200,000 term loan due on April 30, 2009 (Notes 9 and 12).

As a result of these arrangements, the subsidiaries of ProSep Inc. are restricted from transferring funds in the form of dividends, loans or otherwise to ProSep Inc. in excess of \$3,7 million for fiscal year 2009.

Moreover, in light of the new covenant structure with DnB Nor, the Company has completed on July 16, 2009, a significant restructuring of the indebtedness of the parent company. The outcome has resulted in conversion (all or part) of the debentures into equity and recapitalizing the Company (Notes 11 and 12 ). On conclusion of these transactions, comprising indebtedness conversion in the principal amount of \$7,845,620 (closed on July 16, 2009) and the exercise for the share rights issue of \$5,000,000 (closed on August 24), the Company should have now sufficient liquidity to meet its obligations for the next twelve months.

While management believes the use of going concern assumptions is appropriate, the financial statements do not include any adjustments or disclosures that may be necessary should the Company not be able to continue as a going concern. If this were the case, these adjustments could be material.

**2. Changes in accounting policies**

*New accounting standards*

On January 1, 2009, the Company adopted the new recommendations of the Canadian Institute of Chartered Accountants ("CICA") Handbook Section 3064, Goodwill and Intangible Assets, which superseded Section 3062, Goodwill and Other Intangible Assets, and Section 3450, Research and Development Costs. The new standard provides guidance on the recognition, measurement, presentation and disclosure of goodwill and intangible assets subsequent to its initial recognition. The adoption of this new standard did not have a significant impact on the financial statements.

In January 2009, the CICA issued EIC-173, Credit Risk and the Fair Value of Financial Assets and Financial Liabilities, which requires the Company to consider its own credit risk as well as the credit risk of its counterparty when determining the fair value of financial assets and liabilities, including derivative instruments. The standard is effective for the first quarter of 2009 and is required to be applied retrospectively without restatement of prior periods. The adoption of this standard did not have an impact on the valuation of financial assets or liabilities.

*Future accounting standards*

In January 2009, the CICA issued Section 1601, Consolidated Financial Statements, and Section 1602, Non-controlling Interests, which together replace Section 1600, Consolidated Financial Statements. Section 1601 establishes standards for the preparation of consolidated financial statements. Section 1602 establishes standards for accounting for a non-controlling interest in a subsidiary in consolidated financial statements subsequent to a business combination. It is equivalent to the corresponding provisions of International Financial Reporting Standard ("IFRS"), IAS 27 (Revised), Consolidated and Separate Financial Statements.

In January 2009, the CICA also issued Section 1582, Business Combinations. This Section replaces the former Section 1581, Business Combinations. The new standard requires the acquiring entity in a business combination to recognize most of the assets acquired and liabilities assumed in the transaction at fair value including contingent assets and liabilities; and recognize and measure the goodwill acquired in the business combination or a gain from a bargain purchase. Acquisition-related costs are also to be expensed.

The sections apply to the Company to interim and annual consolidated financial statements relating to the fiscal year beginning on January 1, 2011 and to acquisitions for which the acquisition date is after January 1, 2011, respectively. Early adoption of both standards is permitted on a simultaneous basis. The company is currently evaluating the impact of the adoption of these new sections on the consolidated financial statements.

ProSep Inc.

Notes to the consolidated financial statements (Unaudited)

For the three-month and nine-month periods ended September 30, 2009 and 2008

3. Segmented Information

Operating segment

The Company designs, develops and manufactures process solutions to treat produced water, oil and gas for the upstream Oil and Gas industry. At the beginning of 2008, the Company has determined five reportable segments. Segments were based on geographic locations except for Product Development and Corporate Office which were separated based on their distinct operations. US operations, European & Middle-East operations and Asia Pacific operations relate to manufacturing and commercialization of process solutions. Product Development relates to research and development activities. Corporate Office relates to head office activities to support segments.

Revenue and expenses by business units

For the three-month period ended September 30, 2009

	US operations	European & Middle-East operations	Asia Pacific operations	Product Development activities	Corporate Office	Consolidation & Inter segment eliminations	Consolidated operations
	\$	\$	\$	\$	\$	\$	\$
Revenue	5,827,616	839,252	2,203,812	315,672	-	-	9,186,352
Revenue inter segment *	-	-	-	-	-	-	-
Total revenue	5,827,616	839,252	2,203,812	315,672	-	-	9,186,352
Cost of goods sold	4,307,571	175,183	1,745,753	295,441	-	-	6,523,948
Gross margin	1,520,045	664,069	458,059	20,231	-	-	2,662,404
Operating expenses	1,366,859	801,105	327,287	100,157	699,689	-	3,295,097
EBITDA**	153,186	(137,037)	130,772	(79,925)	(699,689)	-	(632,693)

For the three-month period ended September 30, 2008

	US operations	European & Middle-East operations	Asia Pacific operations	Product Development activities	Corporate Office	Consolidation & Inter segment eliminations	Consolidated operations
	\$	\$	\$	\$	\$	\$	\$
Revenue	10,960,215	1,178,563	232,751	176,308	-	-	12,547,837
Revenue inter segment *	-	-	168,172	-	-	(168,172)	-
Total revenue	10,960,215	1,178,563	400,923	176,308	-	(168,172)	12,547,837
Cost of goods sold	8,383,693	(274,120)	379,433	78,283	-	(168,172)	8,399,117
Gross margin	2,576,522	1,452,683	21,490	98,026	-	-	4,148,720
Operating expenses	994,197	571,365	158,167	326,475	784,733	-	2,834,936
EBITDA**	1,582,325	881,318	(136,677)	(228,449)	(784,733)	-	1,313,784

For the nine-month period ended September 30, 2009

	US operations	European & Middle-East operations	Asia Pacific operations	Product Development activities	Corporate Office	Consolidation & Inter segment eliminations	Consolidated operations
	\$	\$	\$	\$	\$	\$	\$
Revenue	20,983,458	2,925,566	7,056,877	723,202	-	-	31,689,103
Revenue inter segment *	74,683	166,223	174,010	-	-	(414,916)	-
Total revenue	21,058,141	3,091,789	7,230,887	723,202	-	(414,916)	31,689,103
Cost of goods sold	15,092,697	1,148,119	5,570,535	697,144	-	(414,916)	22,093,579
Gross margin	5,965,444	1,943,670	1,660,352	26,058	-	-	9,595,524
Operating expenses	4,055,447	2,323,324	772,976	400,790	2,349,923	-	9,902,460
EBITDA**	1,909,997	(379,655)	887,376	(374,731)	(2,349,923)	-	(306,936)

ProSep Inc.

Notes to the consolidated financial statements (Unaudited)

For the three-month and nine-month periods ended September 30, 2009 and 2008

3. Segmented information (continued)

Revenue and expenses by business units

For the nine-month period ended September 30, 2008

	US operations	European & Middle-East operations	Asia Pacific operations	Product Development activities	Corporate Office	Consolidation & Inter segment eliminations	Consolidated operations
	\$	\$	\$	\$	\$	\$	\$
Revenue	31,721,605	4,067,705	580,164	436,240	-	-	36,805,714
Revenue inter segment *	-	-	1,060,990	-	-	(1,060,990)	-
Total revenue	31,721,605	4,067,705	1,641,154	436,240	-	(1,060,990)	36,805,714
Cost of goods sold	24,343,891	1,484,605	1,398,014	222,110	-	(1,060,990)	26,387,629
Gross margin	7,377,714	2,583,101	243,140	214,131	-	-	10,418,085
Operating expenses	2,550,638	1,637,955	565,363	843,610	2,570,900	-	8,168,465
EBITDA**	4,827,076	945,146	(322,223)	(629,479)	(2,570,900)	-	2,249,620

\* These transactions were carried out at exchange amount which is the value established and accepted by the parties.

\*\* EBITDA is a non-GAAP measure and the Company defines it as earnings or loss from operations excluding depreciation and amortization, financial charges and income taxes.

Revenue originated from:

For the three-month period ended September 30, 2009

	US operations	European & Middle-East operations	Asia Pacific operations	Product Development activities	Corporate Office	Consolidation & Inter segment eliminations	Consolidated operations
	\$	\$	\$	\$	\$	\$	\$
United States	5,827,616	-	-	-	-	-	5,827,616
Norway	-	745,576	-	315,672	-	-	1,061,248
Canada	-	93,676	-	-	-	-	93,676
Malaysia	-	-	2,203,812	-	-	-	2,203,812
	5,827,616	839,252	2,203,812	315,672	-	-	9,186,352

One client from Asia Pacific operations represented 14.5% of the Company's revenue and two clients of US operations represented 15% and 13.5% of the Company's revenue for the three-month ended September 30, 2009.

For the three-month period ended September 30, 2008

	US operations	European & Middle-East operations	Asia Pacific operations	Product Development activities	Corporate Office	Consolidation & Inter segment eliminations	Consolidated operations
	\$	\$	\$	\$	\$	\$	\$
United States	10,960,215	-	-	-	-	-	10,960,215
Norway	-	1,100,719	-	176,308	-	-	1,277,027
Canada	-	77,844	-	-	-	-	77,844
Malaysia	-	-	400,923	-	-	(168,172)	232,751
	10,960,215	1,178,563	400,923	176,308	-	(168,172)	12,547,837

Four clients of US operations represented 25%, 22%, 13.5% and 12.5% of the Company's revenue for the three-month ended September 30, 2008.

ProSep Inc.

Notes to the consolidated financial statements (Unaudited)

For the three-month and nine-month periods ended September 30, 2009 and 2008

3. Segmented information (continued)

Revenue originated from:

For the nine-month period ended September 30, 2009

	US operations	European & Middle-East operations	Asia Pacific operations	Product Development activities	Corporate Office	Consolidation & Inter segment eliminations	Consolidated operations
	\$	\$	\$	\$	\$	\$	\$
United States	21,058,141	-	-	-	-	(74,683)	20,983,458
Norway	-	2,747,110	-	723,202	-	(166,223)	3,304,089
Canada	-	344,679	-	-	-	-	344,679
Malaysia	-	-	7,230,887	-	-	(174,010)	7,056,877
	21,058,141	3,091,789	7,230,887	723,202	-	(414,916)	31,689,103

Three clients of US operations represented 14%, 11% and 10.5% of the Company's revenue and one client from Asia Pacific operations represented 13.5% of the Company's revenue for the nine-month ended September 30, 2009.

For the nine-month period ended September 30, 2008

	US operations	European & Middle-East operations	Asia Pacific operations	Product Development activities	Corporate Office	Consolidation & Inter segment eliminations	Consolidated operations
	\$	\$	\$	\$	\$	\$	\$
United States	31,721,605	-	-	-	-	-	31,721,605
Norway	-	3,164,384	-	436,240	-	-	3,600,624
Canada	-	903,321	-	-	-	-	903,321
Malaysia	-	-	1,641,154	-	-	(1,060,990)	580,164
	31,721,605	4,067,705	1,641,154	436,240	-	(1,060,990)	36,805,714

Three clients of US operations represented 30%, 16% and 13% of the Company's revenue for the nine-month ended September 30, 2008.

Assets

As at September 30, 2009

	US operations	European & Middle-East operations	Asia Pacific operations	Product Development activities	Corporate Office	Consolidation & Inter segment eliminations	Consolidated operations
	\$	\$	\$	\$	\$	\$	\$
Total assets	27,283,092	8,484,662	7,348,116	-	8,923,198	-	52,039,068

As at December 31, 2008

Total assets	36,767,783	12,025,983	6,995,633	-	13,706,211	-	69,495,610
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Geographic information

	Three months ended		Nine months ended	
	September 30,		September 30,	
	2009	2008	2009	2008
	\$	\$	\$	\$
Sales to customers situated in:				
United States	3,253,729	5,956,021	12,050,804	12,363,798
Argentina	-	1,677,601	-	11,100,970
Kuwait	933,461	2,773,556	4,710,302	5,286,018
Malaysia	1,377,244	-	4,464,802	-
Venezuela	1,509	-	2,049,482	-
Other countries	3,623,427	2,140,659	8,413,713	8,054,928
	9,186,352	12,547,837	31,689,103	36,805,714

**4. Goodwill**

Goodwill represents the excess of the purchase price of an acquired business over the fair value of the identifiable assets acquired and liabilities assumed. Management tests for impairment of goodwill on an annual basis and at any other time if events occur or circumstances change that would indicate that it is more likely than not that the fair value of a reporting unit has been reduced below its carrying amount.

Factors considered important which could trigger an impairment review include, but are not limited to, significant underperformance relative to expected historical or projected future operating results, significant changes in the manner of use of the acquired assets or the strategy for the overall business, a downturn in the Canadian and international economies, significant negative industry or economic trends, a significant decline in the stock price for a sustained period and the Company's market capitalization relative to net book value.

The goodwill impairment test is a two-step process. Step one consists of a comparison of the fair value of a reporting unit with its carrying amount, including the goodwill allocated to the reporting unit. Measurement of the fair value of a reporting unit may be based on one or more fair value measures including present value techniques of estimated future cash flows and estimated amounts at which the unit as a whole could be bought or sold in a current transaction between willing parties. If the carrying amount of a reporting unit exceeds the fair value, step two requires the fair value of the reporting unit to be allocated to the underlying assets and liabilities of that reporting unit, resulting in an implied fair value of goodwill. Should the carrying amount of the goodwill of the reporting unit exceeds the implied fair value of that goodwill, an impairment loss equal to the excess will be recorded in net earnings (loss).

In the second quarter of 2009, in light of the Company's market capitalization and the balance sheet restructuring initiative (refer to note 11 and 12), the Company performed an interim testing of the goodwill valuation. Such test considered the estimated impact of the balance sheet restructuring initiative, comprised of \$7,845,620 principal amount of indebtedness conversion into shares and the share rights issue of \$5,000,000. The Company estimated the anticipated fair value of the Company using a price of \$0.13 per share which represented the conversion price of the debenture (announced in June 2009 and closed on July 16, 2009).

Based on the preliminary estimates of step one of the process, the Company determined in the second quarter that the anticipated value of Prosep is below its expected carrying value and that impairment loss of goodwill was probable. Accordingly, an impairment charge of \$6.5 million was estimated and recorded in the second quarter. This charge was allocated to the business units using their respective estimated value. Management has not yet performed step two due to time constraints, but will proceed in the future. This could result in potential further write down of goodwill.

**5. Financial charges**

	Three months ended		Nine months ended	
	September 30,		September 30,	
	2009	2008	2009	2008
	\$	\$	\$	\$
Financial charges				
Other financial liabilities				
Interest on long-term debt	150,101	522,724	999,469	1,318,690
Accretion on long-term debt	47,883	126,330	421,785	265,509
Interest charges	64,526	157,979	365,345	441,730
Sub-total	262,510	807,033	1,786,599	2,025,929
Held for trading				
Change in fair value of derivative financial instrument	-	(179,571)	-	(143,550)
Interest revenue on held for trading financial assets	(32)	(51,832)	(65,776)	(136,095)
Sub-total	(32)	(231,403)	(65,776)	(279,645)
Loss (gain) on foreign exchange	403,150	(1,886,988)	976,038	(532,420)
Loss on induced conversion and settlement of debts (Note 12 (a))	2,071,543		2,071,543	
Other	5,421		5,421	
	2,742,592	(1,311,358)	4,773,825	1,213,864

**ProSep Inc.**

**Notes to the consolidated financial statements (Unaudited)**

**For the three-month and nine-month periods ended September 30, 2009 and 2008**

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**6. Basic and diluted loss per share**

Basic and diluted loss per share has been calculated using the weighted-average number of common shares outstanding during the period: 86,819,126 shares for the nine-month period ended September 30, 2009 and 130,840,835 shares for the three-month period ended September 30, 2009 (62,556,566 shares for the three-month and six-month periods ended June 30, 2008).

As a result of the loss for the three-month and the nine-month periods ended September 30, 2009, 27,635,027 potentially dilutive warrants, 420,000 potentially dilutive options and 4,186,778 potentially dilutive restricted units have not been included in the calculation of diluted loss per share because the effect would have been anti-dilutive. For the nine-month period ended September 30, 2008, 27,635,027 potentially dilutive warrants, 2,109,000 potentially dilutive options and 1,680,000 potentially dilutive restricted share units have not been included in the calculation for the same reason. The debenture and secured loans convertible feature have not been taken into consideration because they would have had the same effect (Note 12).

**7. Restricted cash**

	<b>September 30, 2009</b>	<b>December 31, 2008</b>
	\$	\$
Restricted cash short term	-	<b>1,037,846</b>
Restricted cash long term	-	<b>3,158,986</b>
	-	<b>4,196,832</b>

On October 25, 2007, \$1,037,846 was deposited following the acquisition of Pure Group AS. This amount has been released and most of it was remitted to the former owners of Pure Group AS. In November 2008, 18,000,000 NOK (\$3,339,022) was required under the credit facility with DnB NOR. During the three-month period ended June 30, 2009, the Company agreed to a new covenant structure for its credit facility with DnB NOR. Pursuant to this new structure, this amount has been released.

**8. Receivables**

	<b>September 30, 2009</b>	<b>December 31, 2008</b>
	\$	\$
Trade accounts receivable	<b>9,242,755</b>	4,889,791
Unbilled receivables *	<b>9,093,209</b>	14,528,661
Sales taxes and other	<b>526,662</b>	586,396
	<b>18,862,626</b>	20,004,848

\* Unbilled receivables represent revenue recorded in accordance with revenue recognition criteria for which the amounts have not yet been invoiced.

**9. Long-term Investment in Master Asset Vehicle II Notes and related credit facilities**

At December 31, 2008, the Company held commercial paper ("ABCP") acquired on July 12, 2007, with a nominal value of \$9,000,000. During the month of August 2007, the ABCP market experienced liquidity problems. The maturity date of the ABCP held by the Company was August 14, 2007, and the amount due was not repaid.

The restructuring efforts of the Pan Canadian restructuring committee under the Companies' Creditors Arrangement Act led to a final restructuring, the closing of which occurred on January 21, 2009. As expected, the restructuring plan led to the replacement of the ABCP held by the Company by new floating rate notes that have maturities based on the maturities of the underlying assets. The key elements of the plan relevant to the Company are as follows:

- Creation of a new trust named "Master Asset Vehicle II" ("MAV 2"):
  - MAV 2 regroups the so-called 100% synthetic transactions, that is a combination of assets provided as collateral, credit default swaps and hybrid transactions, comprised of a combination of synthetic and traditional assets.
  - MAV 2 also includes the ineligible (subprime) assets originally associated with these transactions.
- Creation of five categories of notes for MAV 2 (A-1, A-2, B, C and IA).
- The IA notes are subdivided in multiple series of tracking notes that pass through to the holders the cash flows generated by the underlying assets.

According to the restructuring plan, the Company has received in January 2009 long-term floating rate MAV 2 notes (the "Notes") with the following nominal amounts:

	\$
Class A-1 Notes:	371,936
Class A-2 Notes:	4,291,318
Class B Notes:	778,993
Class C Notes:	168,316
Class IA, series 1 and 2 Notes:	3,365,062

The MAV 2 A-1, A-2, B and C Notes legally mature in 2056. However, the expected maturity date is in 2016. The Class A-1 and A-2 Notes have been originally rated A by DBRS. The Class A-2 Notes have however been downgraded to BBB (low) by DBRS on August 11, 2009 and remain Under Review with Negative Implications. The Class B and C Notes have not been rated nor have the Class IA Notes received by the Company. Further to credit events that have occurred in the underlying assets, the outstanding principal amount Class IA series 2 Notes has been reduced to zero. However, they remain eligible to the sales mechanism described under *Credit facility related to IA notes* described below.

The Notes are considered as new financial instruments and have been designated as held for trading and are classified as long-term investments.

Since the restructuring in January 2009, the Company has received cash payments totaling \$385,358 representing accrued interest on the ABCP for the period from August 2007 to January 2009, net of the estimated restructuring costs incurred by the Pan-Canadian restructuring committee. Interest and principal payments received on the Notes until September 30, 2009 total \$16,745.

In connection with the restructuring of the ABCP, the Company has entered into two credit facilities with the National Bank of Canada ("National Bank") in July 2009.

*Credit facility related to IA Notes*

This credit agreement provides for a \$2,523,797 revolving credit facility agreement representing an amount equal to 75% the nominal amount of such Notes. This credit facility is valid for a minimum of two years and bears interest at the prime rate less 1%. The agreement also grants to the Company the right to sell to National Bank the IA Notes at the end of two years with a guaranteed minimum sales price of 75% of the nominal amount of the notes. The proceeds from the sale have to be used to reduce the outstanding amount under the credit facility and any remaining balance under the credit facility is without recourse to the Company.

*Credit Facility related to Eligible notes*

This credit agreement provides for a \$4,656,767 revolving credit facility representing an amount equal to 83% of the total nominal amount of the MAV II Class A-1, A-2, B and C Notes (collectively the "Eligible Notes"). These credit facilities are valid for a minimum term of 3 years and also bear interest at the prime rate less 1%. The agreement provides for borrowings to be made under two tranches: a first tranche representing 45% of the nominal amount of the Eligible Notes and a second tranche representing 38% of the nominal amount of the Eligible Notes. It also grants the Company the right to sell to National Bank the Eligible Notes at the end of 3 years with a guaranteed minimum sales price of 45% of the nominal amount of the notes. The proceeds from the sale of the Eligible Notes have to be used to settle the first tranche and then the second tranche of the credit facility. Any remaining balance under the first tranche of the credit facility is without recourse to the Company.

**9. Long-term Investment in Master Asset Vehicle II Notes and related credit facilities (continued)**

The Company has granted a first ranking hypothecation to National Bank on the Notes. These two credit agreements will provide the Company with \$7,180,564 in long term financing facilities in replacement of the previous term loan that was secured with the ABCP which matured on April 30, 2009. As mentioned above, except for the second tranche of the Eligible Notes facility, the bank's recourse with respect to these new credit facilities will be limited to the Notes.

*Estimation of fair value*

The notes held by the company have not traded in an active market since the restructuring and as of September 30, 2009, there were no quotations from an active market available.

The fair value of the Notes as of September 30, 2009, was determined based on management's judgment using available information and assumptions market participants would use in pricing such Notes as at the balance sheet date. The Company reviewed information provided by DBRS and BlackRock, the administrator of MAV 2, including current and anticipated credit ratings, composition and valuation estimates of the underlying assets, the estimate of the extent of leverage in the transactions underlying the MAV 2 Notes and general economic conditions in considering the fair value of the investment.

The Company estimated the fair value of the Notes using the discounted cash flow evaluation technique based on observable market assumptions to the extent possible. The main assumptions are comprised of the anticipated interest coupons, anticipated maturity of the Notes and an appropriate discount rate considering the underlying risks. The estimated discount rate was determined based on observable market assumptions for similar securities. For the Notes backed by ineligible assets, the fair value was established taking into consideration the terms of the final agreement with National Bank ("National Bank") previously described. The Company used the following discount factors to evaluate the Notes:

Notes	Expected Yield	Market related Discount factors
Class A-1	248 basis points*	Canada Bond rate plus 620 basis points
Class A-2	248 basis points*	Canada Bond rate plus 710 basis points
Class B	248 basis points*	Canada Bond rate plus 850 basis points
Class C	248 basis points*	Canada Bond rate plus 1350 basis points
Class IA	0 basis points	Canada Bond rate plus 148 basis points

\* September 30, 2009 BA rate of 2.98% minus 50 basis points

The risk premiums added to the basic Canadian government bond rates reflect the liquidity, credit and other risks. Regarding the IA Notes, the nominal amount used in the yield and discount calculation was reduced by 25% to take into consideration the terms of the credit facility with National Bank of Canada except for the interest received of \$11,239 and \$387,576 for the three and nine month periods ended September 30, 2009 respectively.

Based on its assessment of fair values, the Company recognize an increase in fair value of investment in ABCP for \$400,000 during the three and nine month periods ended September 30, 2009 ((\$450,000) for the nine-month period ended September 30, 2008). The cumulative impairment charge represents \$3,069,000 since the acquisition of the original ABCP (34.1% of the nominal value).

The above estimated fair values may not be indicative of the ultimate net realizable value or the future fair value. Because of the uncertainty in the market, numerous reasonable assumptions exist. While management believes that its valuation technique is appropriate under the circumstances, changes in significant assumptions, especially those relating to returns, credit risk and liquidity risk could significantly affect the value ascribed to the Notes in the next quarters. Following the analysis, the Company identified that the discount rate related to Classes A-1 and A-2 of MAV 2, generate the vast majority of the volatility in the valuation model of the Notes' fair value. For example, a 50 basis point increase in the discount rate for A-1 and A-2 notes results in a \$88,500 decrease on the investments' value.

**10. Bank credit facilities**

The company has a bank credit facility with DnB NOR which consists of a senior overdraft facility of 30,000,000 NOK (\$5,565,037 at September 30, 2009) and a guarantee facility of 15,000,000 NOK (\$2,782,518 at September 30, 2009) to be used to provide customer guarantees against advances received under sales contracts. The bank credit facility outstanding is \$2,565,602 at September 30, 2009 (\$11,596,044 at December 31, 2008). The interest rate of 3.58% is the one month Norwegian Interbank Offered Rate (NIBOR) of 1.58%, plus 2% per annum on the overdraft facility.

The letters of guarantee outstanding amount to \$2,169,017 at September 30, 2009 (\$2,123,508 at December 31, 2008). There is no letter of credit outstanding at September 30, 2009 or at December 31, 2008.

**11. Share Capital**

	Number of shares	Amount \$
Balance, December 31, 2008 and June 30, 2009	64,443,451	55,488,839
Induced conversion of secured convertible loans due 2009 (note 12 (a))	11,538,460	3,087,117
Conversion of accrued interest on secured convertible loans due 2009 (note 12 (a))	5,131,693	667,120
Conversion of unsecured debentures due 2013 (note 12 (a))	17,469,230	2,271,000
Induced conversion of convertible unsecured subordinated debentures due 2013 (note 12 (a))	26,211,538	5,496,858
Issued pursuant to the exercise of rights (a)	38,461,538	5,000,000
Balance, September 30, 2009	163,255,910	72,010,934

(a) Pursuant to a short form prospectus dated July 14, 2009 and in parallel with the debt restructuring described in note 12 (a), the Company issued to its shareholders rights to subscribe for up to 76,923,077 common shares at a price of \$0.13 per common share. On August 24, 2009, the Company closed the rights offering and issued a total of 38,461,538 common shares for gross proceeds of \$5 million.

The transaction costs of \$886,470 allocated to the shares issued pursuant to the debt restructuring and the exercise of rights have been accounted for as an increase in the deficit (share issue expenses).

**ProSep Inc.**

**Notes to the consolidated financial statements (Unaudited)**

**For the three-month and nine-month periods ended September 30, 2009 and 2008**

**12. Long-term debt and interest payable**

	September 30, 2009		December 31, 2008	
	Loan \$	Interest payable \$	Loan \$	Interest payable \$
Secured convertible loans due by ProSep Inc. in the aggregate principal amount of \$1.5 million, bearing interest at 12% per annum compounded. (a)	-	-	979,540	649,540
Unsecured debenture due by ProSep Inc. in the principal amount of \$4 millions USD (\$5,036,000 as at June 30, 2009), bearing interest at 13.25% per annum. (a)	-	-	4,898,400	55,208
Credit facility with DnB NOR due by Torr Acquisition Norway AS, a wholly owned subsidiary of ProSep Inc. The interest rate of 4.88% is the three month Norwegian Interbank Offered Rate (NIBOR) +3.00% and the principal amount is payable in 10 equal instalments of 4 500 000 NOK (\$834,756 as of September 30, 2009) every 6 months. Expiration date is October 25, 2012.	5,843,289	57,226	6,318,006	98,447
Convertible unsecured subordinated debenture due by ProSep Inc. in the principal amount of \$5.1 million, bearing interest at 13%. (a)	-	-	3,108,165	110,283
Convertible unsecured subordinated debenture due by ProSep Inc. in the principal amount of \$3,953,500, bearing interest at 13.25% payable every six months and maturing on July 16, 2014. (a)	3,589,573	110,509	-	-
Revolving credit facilities with National Bank of Canada bearing interest at prime rate (2.25% at September 30, 2009) minus 1% payable monthly (Note 9).	7,180,564	-	-	-
Obligations under capital leases	125,710	-	105,488	-
	<b>16,739,136</b>	167,735	15,409,599	913,478
Current portion of long term debt and interest payable	<b>(1,721,052)</b>	(167,735)	(3,322,106)	(913,478)
<b>Long-term debt and interest payable</b>	<b>15,018,084</b>	-	12,087,493	-

(a) In connection with the rights issue described in Note 11, the Company completed on July 16, 2009, a significant restructuring of the indebtedness of the parent company. Pursuant to this restructuring, the secured convertible loans (principal amount of \$1.5 million maturing in October 2009), \$667,120 of accrued interest on these loans, the unsecured debentures (principal amount of US\$4 million maturing in June 2013) and the convertible unsecured subordinated debentures (principal amount of \$5.1 million maturing in April 2013) were ultimately converted into an aggregate of 60,350,921 common shares and unsecured subordinated debentures of a principal amount of \$3,953,500 convertible into common shares at a price of \$0.30 per share, bearing interest at 13.25% payable every six months and maturing on July 16, 2014

These transactions have been accounted for as either inducements to convert or settlements of the previous liabilities and losses on settlements totaling \$2,071,543 have been recognized in the consolidated statement of earnings and a charge of \$2,198,397 was recorded to deficit.

For accounting purposes, the new convertible debentures include a liability component and an equity component (the holders' conversion option). The initial fair value of the liability component of \$3,781,940 has been determined by discounting the future repayments at a discount rate which represent the estimated borrowing rate available to the Company for similar debentures having no conversion rights. The residual of the gross proceeds over the estimated initial fair value of the liability component was attributed to the conversion option (\$171,560).

The transaction costs allocated to the debenture issue have been accounted for as a reduction of the liability component (\$200,829).

**ProSep Inc.**

**Notes to the consolidated financial statements (Unaudited)**

**For the three-month and nine-month periods ended September 30, 2009 and 2008**

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**13. Pension Obligation**

For the three-month period ended September 30, 2009, an amount of \$35,255 has been recorded in the statement of loss to account for the increase in the pension obligation (\$10,783 for the three months ended September 30, 2008). For the nine-month period ended September 30, 2009, an amount of \$125,879 has been recorded in the statement of loss to account for the increase in the pension obligation (\$32,399 for the nine-month period ended September 30, 2008).

**14. Capital management**

The Company's business is not capital intensive, but is working capital intensive. During the past years, the Company has accumulated a large deficit. The objective of the Company is to achieve and maintain positive earnings and cash flow from operating activities as soon as possible and to maintain sufficient credit facilities to support growth.

During the quarter ended September 30, 2009, the Company entered into significant transactions that have affected the components of its capital, namely the refinancing on a long term basis of the former ABCP credit facility (see note 9), the restructuring of the debentures issued by the parent company (see note 12) and the rights offering (see note 11)

The Company defines capital as being equity plus debt, plus bank indebtedness, less cash and cash equivalents.

	<b>September 30,</b>	December 31,
	<b>2009</b>	2008
	\$	\$
Shareholders' equity	<b>19,270,032</b>	19,530,902
Bank credit facilities	<b>2,565,602</b>	11,596,044
Long term debt, including current portion	<b>16,739,136</b>	15,409,599
	<b>38,574,770</b>	46,536,545
Less cash and cash equivalents	<b>2,680,662</b>	7,615,119
Capital	<b>35,894,108</b>	38,921,426

**15. Contingent liabilities**

In addition to the letters of guarantee disclosed in Note 10, the Company has an amount of \$278,088 of letters of guarantee with Export Development Canada.

The Company is a defendant in a claim by Westend Enviro Consultants ("Westend") filed on March 31, 2006, claiming damages for breach of contract and fraudulent misrepresentation for a total amount of \$280,000. The Company filed a Statement of Defence on June 9, 2006 denying any liability. It is premature to assess the likelihood of successfully defending this claim. No amount has been accrued.

**16. Comparative figures**

Comparative figures for the consolidated financial statements for the three-month and nine-month periods ended September 30, 2008, and as at December 31, 2008 have been reclassified to conform with the September 30, 2009 presentation. The Company has allocated the goodwill and the other intangibles by business units and those values are shown as part of the total assets of each business unit.