

**ProSep Inc.**  
**Unaudited Consolidated Interim Financial Statements**  
**For the three-month period**  
**ended March 31, 2010**

ProSep Inc.  
Consolidated statements of loss and comprehensive loss  
(unaudited)

Statement of Loss	Three months ended March 31,	
	2010	2009
	\$	\$
Revenue	9,407,690	13,186,780
Cost of goods sold	6,829,381	9,970,108
Gross margin	2,578,309	3,216,672
<b>Expenses</b>		
Sales and marketing	511,088	473,979
Research and development	61,790	161,496
General and administrative	2,681,729	2,728,847
	3,254,607	3,364,322
Income before the following items:	(676,298)	(147,650)
Net financial charges (Note 3)	802,310	1,338,488
Amortization	378,507	375,472
Loss before income taxes	(1,857,115)	(1,861,610)
Current tax provision	2,051	39,333
Future tax provision (recovery)	(554,461)	83,573
Income taxes	(552,410)	122,906
Net loss	(1,304,705)	(1,984,516)
<i>Weighted average number of shares (basic and diluted)</i>	<i>163,255,910</i>	<i>64,443,451</i>
<i>Basic and diluted loss per share (Note 5)</i>	<i>(0.01)</i>	<i>(0.03)</i>

Statement of Comprehensive Loss

	2010	2009
	\$	\$
Net loss	(1,304,705)	(1,984,516)
Foreign currency translation adjustment	98,354	-
Comprehensive loss	(1,206,351)	(1,984,516)

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

**ProSep Inc.**  
**Consolidated balance sheets**  
**(unaudited)**

	<b>March 31,</b>	Audited December 31,
	<b>2010</b>	2009
	\$	\$
<b>Assets</b>		
Current assets		
Cash	6,345,680	7,689,695
Restricted cash (Note 6)	2,292,315	2,022,940
Receivables	11,510,953	12,807,205
Inventories	375,446	392,709
Prepaid expenses	700,535	665,162
Income tax recoverable	536,529	544,177
Future income tax assets	399,451	207,698
	<b>22,160,909</b>	24,329,586
Long-term investment (Note 7)	3,424,775	3,425,000
Property and equipment	1,489,916	1,526,561
Goodwill	14,804,176	15,195,645
Intangible assets	8,518,203	8,918,517
Future income tax assets	60,646	-
	<b>50,458,625</b>	53,395,309
<b>Liabilities</b>		
Current liabilities		
Bank credit facilities (Note 8)	4,789,741	5,006,206
Accounts payable and accrued liabilities	11,729,768	12,836,057
Deferred revenue	206,398	71,796
Current portion of long term debt (Note 9)	1,711,577	1,672,602
	<b>18,437,484</b>	19,586,661
Long-term debt (Note 9)	11,388,262	11,689,450
Future income tax liabilities	1,330,093	1,661,127
Pension obligation (Note 10)	527,790	495,440
	<b>31,683,629</b>	33,432,678
<b>Shareholders' equity</b>		
Share capital	72,010,934	72,010,934
Contributed surplus	11,518,228	11,499,512
Accumulated other comprehensive income	1,998,865	1,900,511
Deficit	<b>(66,753,031)</b>	(65,448,326)
	<b>18,774,996</b>	19,962,631
	<b>50,458,625</b>	53,395,309

**Approved by the Board**

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

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

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**ProSep Inc.**  
**Consolidated statements of contributed surplus**  
**(unaudited)**

	<b>Three-month period ended March 31, 2010</b>				
	Stock-based compensation	Warrants	Conversion feature of loans	Other	Total contributed surplus
	\$	\$	\$	\$	\$
Contributed surplus, beginning of period	2,909,496	660,828	171,560	7,757,628	11,499,512
Stock-based compensation and restricted share units (Note 4)	87,386	-	-	-	87,386
Vested restricted share units (Note 4)	(68,670)	-	-	-	(68,670)
Contributed surplus, end of period	<u>2,928,212</u>	<u>660,828</u>	<u>171,560</u>	<u>7,757,628</u>	<u>11,518,228</u>

	<b>Three-month period ended March 31, 2009</b>				
	Stock-based compensation	Warrants	Conversion feature of loans	Other	Total contributed surplus
	\$	\$	\$	\$	\$
Contributed surplus, beginning of period	2,548,774	8,000,821	1,977,544	-	12,527,139
Stock-based compensation and restricted share units	62,902	-	-	-	62,902
Contributed surplus, end of period	<u>2,611,676</u>	<u>8,000,821</u>	<u>1,977,544</u>	<u>-</u>	<u>12,590,041</u>

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**ProSep Inc.**  
**Consolidated statements of deficit and accumulated other comprehensive income**  
**(unaudited)**

<b>Deficit</b>	<b>Three months ended March 31,</b>	
	<b>2010</b>	<b>2009</b>
	\$	\$
Deficit, beginning of period	(65,448,326)	(48,485,076)
Net loss	(1,304,705)	(1,984,516)
Deficit, end of period	(66,753,031)	(50,469,592)

**Accumulated other comprehensive income**

	<b>2010</b>	<b>2009</b>
		\$
Balance, beginning of period	1,900,511	-
Foreign currency translation adjustment	98,354	-
Balance, end of period	1,998,865	-

As of March 31, 2010, the sum of deficit and Accumulated other comprehensive income is \$64,754,166.

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

**ProSep Inc.**  
**Consolidated statements of cash flows**  
**(unaudited)**

**Three months ended**  
**March 31,**

	<b>2010</b>	<b>2009</b>
	<b>\$</b>	<b>\$</b>
<b>Operating activities</b>		
Net loss	(1,304,705)	(1,984,516)
Interest received on long-term investment	1,752	298,526
Items not affecting cash		
Stock-based compensation	87,386	62,902
Amortization of property and equipment	197,952	205,795
Amortization of intangible assets	180,555	169,674
Accretion on long-term debt	14,486	164,994
Increase in fair value of long-term investment	-	(16,000)
Periodic pension cost in excess of contribution	61,270	54,381
Future income taxes (recovery)	(554,461)	83,573
Unrealized exchange loss	405,807	379,332
	<b>(909,958)</b>	<b>(581,339)</b>
Changes in operating working capital items	255,099	328,119
	<b>(654,859)</b>	<b>(253,220)</b>
<b>Investing activities</b>		
Restricted cash (Note 6)	(269,375)	-
Acquisition of property and equipment	(195,252)	(54,910)
	<b>(464,627)</b>	<b>(54,910)</b>
<b>Financing activities</b>		
Bank credit facilities (Note 8)	52,033	1,441,483
Repayment of long-term debt	(11,987)	(8,280)
	<b>40,046</b>	<b>1,433,203</b>
<b>Increase (Decrease) in cash</b>	<b>(1,344,021)</b>	<b>1,308,026</b>
<b>Effect of exchange rate on cash</b>	<b>(264,581)</b>	<b>182,953</b>
<b>Cash beginning of period</b>	<b>7,689,701</b>	<b>7,615,119</b>
<b>Cash end of period</b>	<b>6,345,680</b>	<b>8,923,145</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 periods ended March 31, 2010 and 2009**

**1. Financial Statement Presentation and Going Concern**

The unaudited interim consolidated financial statements 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, 2009.

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

The accompanying financial statements of ProSep Inc. (the "Company") 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 a loss of \$1,304,705 for the three-month period ended March 31, 2010, has an accumulated deficit of \$66,753,031 and has not so far generated positive cash flows from operations. In addition, the Company is also subject to certain restrictive covenants. At March 31, 2010, the Company was in breach of one of its financial covenants under the credit facility with DnB NOR. The Company has since obtained a long-term waiver for this breach (see Note 8). Accordingly, there exists significant doubt that the Company would be able to continue as a going concern as at March 31, 2010. These conditions require that the Company continues to seek non-operational sources of financing such as temporary additional credits obtained in April 2010 from the bank to finance working capital and the private placement completed in May 2010 (see Note 12), in order to achieve profitable operations in the future.

At March 31, 2010, the Company had a cash balance of \$6,345,680 and a restricted cash balance of \$2,292,315 that will be released on October 5, 2010. Taking into consideration the waiver obtained from DnB NOR (see Note 8) and the aforementioned private placement, the Company believes that it has 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. 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. Segments are based on geographical locations except for Corporate Office that was separated based on its distinct operations. US, European, Middle East and Asia Pacific operations relate to manufacturing and commercialization of process solutions. Corporate Office relates to head office activities in support of other segments. The former Product Development segment has been integrated into European & Middle-East Operations to represent the unit's operational functionality. Comparable information has been reclassified accordingly.

The accounting policies that apply to the reportable segments are the same as those described in accounting policies.

**ProSep Inc.**  
**Notes to the consolidated financial statements (Unaudited)**  
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*Revenue and Expenses by Business Units*

**For the three-month period ended March 31, 2010**

	US operations	European & Middle-East operations	Asia Pacific operations	Corporate Office	Consolidation & Inter segment eliminations	Consolidated operations
	\$	\$	\$	\$	\$	\$
Revenue	5,582,663	2,220,476	1,604,551	-	-	9,407,690
Revenue inter segment	368	9,600	-	-	(9,968)	-
Total revenue	5,583,031	2,230,076	1,604,551	-	(9,968)	9,407,690
Cost of goods sold	4,375,597	967,920	1,495,832	-	(9,968)	6,829,381
Gross margin	1,207,434	1,262,156	108,719	-	-	2,578,309
Operating expenses	1,380,759	874,578	173,708	825,562	-	3,254,607
EBITDA*	(173,325)	387,578	(64,989)	(825,562)	-	(676,298)

**For the three-month period ended March 31, 2009**

	US operations	European & Middle-East operations	Asia Pacific operations	Corporate Office	Consolidation & Inter segment eliminations	Consolidated operations
	\$	\$	\$	\$	\$	\$
Revenue	9,944,627	1,173,178	2,068,975	-	-	13,186,780
Revenue inter segment	74,683	-	167,077	-	(241,760)	-
Total revenue	10,019,310	1,173,178	2,236,052	-	(241,760)	13,186,780
Cost of goods sold	7,744,313	840,006	1,627,549	-	(241,760)	9,970,108
Gross margin	2,274,997	333,172	608,503	-	-	3,216,672
Operating expenses	1,381,060	878,490	207,649	897,123	-	3,364,322
EBITDA*	893,937	(545,318)	400,854	(897,123)	-	(147,650)

\* 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.

*Significant Customers*

Two clients of the US operations represented respectively 42.7% and 11.6% of the Company's revenue and one client of the European & Middle-East operations represented 17.5% of the Company's revenue for the three months ended March 31, 2010.

Three clients of the US Operations represented respectively 11%, 21% and 27% of the Company's revenue for the three months ended March 31, 2009.

**ProSep Inc.**  
**Notes to the consolidated financial statements (Unaudited)**  
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*Geographical Information*

	March 31,	
	2010	2009
	\$	\$
Sales to customers situated in:		
United States	1,464,506	6,141,939
Columbia	4,035,459	-
Kuwait	67,402	2,789,180
Malaysia	948,617	1,195,557
Venezuela	6,245	1,003,981
Norway	2,045,194	537,314
Other countries	840,267	1,518,809
	<u>9,407,690</u>	<u>13,186,780</u>

**3. Financial Charges**

	Three months ended March 31,	
	2010	2009
	\$	\$
Financial (income) charges, net		
Other financial liabilities		
Interest on long-term debt	193,557	471,315
Accretion on long-term debt	14,486	164,994
Other interest	152,879	177,553
Sub-total	<u>360,922</u>	<u>813,862</u>
Interest revenue on held for trading financial assets	(11,207)	(17,000)
Loss on foreign exchange	452,595	541,626
	<u>802,310</u>	<u>1,338,488</u>

**4. Restricted Share Units**

During the three-month period ended March 31, 2010, the Company granted 3,650,000 restricted share units at a weighted average value of \$0.17 per share for a total of \$620,500 (2,415,000 were granted during the year ended December 31, 2009 at a weighted average value of \$0.20 per share for a total value of \$483,925). The expense recorded in the consolidated statements of loss and credited to contributed surplus was \$87,386 for the three-month period ended March 31, 2010 (\$62,902 for the three-month period ended March 31, 2009). During the quarter, an amount of \$68,670 was paid in compensation of restricted share units that vested in December 2009 (381,500 share units) and was removed from contributed surplus.

	Three-month period ended March 31, 2010	Year ended December 31, 2009
	Number of restricted share units	Number of restricted share units
Balance, beginning of period	4,161,778	1,851,500
Granted	3,650,000	2,415,000
Forfeited	(400,278)	(104,722)
Vested	(381,500)	-
Balance, end of period	<u>7,030,000</u>	<u>4,161,778</u>

**ProSep Inc.**  
**Notes to the consolidated financial statements (Unaudited)**  
**For the three-month periods ended March 31, 2010 and 2009**

**5. 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: 163,255,910 shares for the three-month period ended March 31, 2010 (64,443,451 shares for the three-month period ended March 31, 2009).

As a result of the loss for the three-month period ended March 31, 2010, 4,460,242 potentially dilutive warrants, 420,000 potentially dilutive options and 7,030,000 potentially dilutive restricted share units as well as the convertible feature of the loan have not been included in the calculation of diluted loss per share because the effect would have been anti-dilutive (27,635,027 warrants, 436,500 options and 4,061,500 restricted share units as well as the convertible features of the debenture and secured loans during the period ending March 31, 2009).

**6. Restricted Cash**

At March 31, 2010, this restricted cash amounting to US\$2,256,660 (\$2,292,315) related to a letter of credit that will be released on October 5, 2010. On April 1, 2010, a letter of guarantee was issued for the same contract for an additional amount of \$2,616,502. Such letter of guarantee was secured by pledging cash on hand for the equivalent amount.

**7. Long term Investment and Related Credit facility**

**Estimate of Fair Value**

At March 31, 2010, the Company held the same Notes issued by Master Asset Vehicle II ("MAV 2") at December 31, 2009. Although there have been some isolated transactions since December 31, 2009, there were no active market quotations available at March 31, 2010. In fact, the Notes held by the Company have not traded in an active market since the restructuring of January 2009.

The fair value of the Notes at March 31, 2010 was determined using a methodology consistent with the one used as at December 31, 2009 which is based on management's judgment using available information and assumptions market participants would use in pricing such Notes 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. The Company used the following discount factors to evaluate the Notes:

Replacement Notes	March 31, 2010		December 31, 2009	
	Expected Yield	Market related Discount factors (Canada Bond rate plus)	Expected Yield	Market related Discount factors (Canada Bond rate plus)
Class A-1	284 basis points*	555 basis points	283 basis points**	590 basis points
Class A-2	284 basis points*	660 basis points	283 basis points**	705 basis points
Class B	284 basis points*	795 basis points	283 basis points**	850 basis points
Class C	0 basis points	2,795 basis points	0 basis points	2,350 basis points
Ineligible	0 basis points	201 basis points	0 basis points	203 basis points

\* March 31, 2010 bankers' acceptance swap rate of 3.34% minus 50 basis points

\*\* December 31, 2009 bankers' acceptance swap rate of 3.33% minus 50 basis points

The risk premiums added to the basic bankers' acceptance rates reflect liquidity, credit and other risks.

The fair value of the put options embedded in the credit facility with the National Bank of Canada at March 31, 2010 was estimated using a valuation technique that incorporates a probability-weighted approach, applied to discounted future cash flows of the underlying IA and Eligible Notes while considering: (i) the fair value of such Notes, (ii) the

**ProSep Inc.**  
**Notes to the consolidated financial statements (Unaudited)**  
**For the three-month periods ended March 31, 2010 and 2009**

maximum amount that can be drawn under the respective credit facilities, (iii) the recourse features of such drawings, and (iv) the discount rate relating to National Bank.

At March 31, 2010, management concluded that the fair value of the Notes and the embedded put options remained unchanged from the December 31, 2010 value.

The 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. While management believes that its valuation technique is appropriate under the circumstances, changes in significant assumptions, especially those relating to the probability of the scenarios, returns, credit risk and liquidity risk could significantly affect the value ascribed to the replacement notes in the future. Following the analysis, the Company identified that the discount rate related to Classes A-1 and A-2 of MAV 2, and the embedded put option on the IA Notes generate the vast majority of the volatility in the valuation model of the Notes and embedded put options fair value. For example, a 50 basis point increase or decrease in the discount rate for A-1 and A-2 Notes and the IA Notes put option would result in a \$93,235 change in the aggregate fair value.

**8. Bank Credit Facilities**

The Company has a bank credit facility with DnB NOR consisting of a senior overdraft facility of 30,000,000 NOK (\$5,126,978 at March 31, 2010) and a guarantee facility of 15,000,000 NOK (\$2,563,489 at March 31, 2010) to be used to provide customer guarantees against advances received under sales contracts. The bank credit facility outstanding is 28,026,690 NOK (\$4,789,741) at March 31, 2010 (27,719,866 NOK (\$5,006,206) at December 31, 2009) and is secured by the assets of the Company. The interest rate of 4.14% (3.96% in 2009) is the one month Norwegian Interbank Offered Rate (NIBOR) of 2.14% at March 31, 2010 (1.96% at December 31, 2009), plus 2% per annum.

The letters of guarantee outstanding amount to \$1,480,912 at March 31, 2010 (\$2,083,112 at December 31, 2009).

At March 31, 2010, TORR Acquisition Norway AS (wholly owned subsidiary of ProSep Inc.) was in breach of one of its financial covenants under the credit facility with DnB NOR. The Company has since obtained a long-term waiver for such covenant breach. In exchange for the waiver, the Company agreed to perform a full repayment of its line of credit for a period of three weeks before December 1, 2010. This covenant is related to two clean-down periods of no less than three weeks during a rolling twelve-month period, each clean-down period to be separated by at least eight weeks. As of March 31, 2010, the Company had performed one of the two required clean-down periods (see also Note 12, Subsequent Events).

**ProSep Inc.**  
**Notes to the consolidated financial statements (Unaudited)**  
**For the three-month periods ended March 31, 2010 and 2009**

**9. Long-term Debt**

	<b>March 31, 2010</b>	December 31, 2009
	<b>\$</b>	<b>\$</b>
Convertible unsecured subordinated debenture in the nominal amount of \$3,953,500, bearing interest at 13.25% payable every six months and maturing on July 16, 2014.	<b>3,615,011</b>	3,600,526
Revolving credit facilities with National Bank of Canada bearing interest at prime rate (2.25% at March 31, 2010) minus 1% payable monthly (Note 7).	-	-
- IA Notes facility, maturing in March 2011	<b>2,523,797</b>	2,523,797
- Less embedded put option	<b>(2,400,000)</b>	(2,400,000)
- Eligible Notes facility, first tranche, maturing in March 2012	<b>2,524,528</b>	2,524,753
- Eligible Notes facility, second tranche, maturing in March 2012	<b>2,132,014</b>	2,132,014
Obligations under capital leases	<b>90,209</b>	104,764
Credit facility with DnB NOR: The interest rate of 5.29% (5.11% in 2009) is the three month Norwegian Interbank Offered Rate (NIBOR) +3.00% and the principal amount is payable in 10 equal installments of 4,500,000 NOK (\$769,046 as of March 31, 2010) every 6 months. Expiration date is October 25, 2012.	<b>4,614,280</b>	4,876,198
	<b>13,099,839</b>	13,262,052
Current portion of long term debt	<b>(1,711,577)</b>	(1,672,602)
<b>Long-term debt</b>	<b>11,388,262</b>	11,689,450

**10. Pension Obligation**

For the three months ended March 31, 2010, the expense related to defined benefit pension plans amounted to \$55,858 (\$54,381 for the three months ended March 31, 2009).

**11. Contingencies**

In addition to the letters of guarantee disclosed in Note 8, the Company has an amount of \$3,433,166 (\$3,643,958 at December 31, 2009) of letters of guarantee outstanding with Export Development Canada.

The Company was defendant in a claim made by Westend Enviro Consultants ("Westend") for a total amount of \$280,000. The final settlement agreed on March 30, 2010, is as follows:

- \$108,000 is a refund of the amounts paid by Westend to the Company in January 2004 including a refund of GST.
- \$ 22,000 is interest on the refunded amount.

**12. Subsequent Events**

The bank credit facility with DnB NOR was increased in May 2010 by an amount of 18 million NOK (approximately \$3 million) for a total facility of 48 million NOK (approximately \$8.2 million) until the end of July 2010. In exchange for this temporary increase, the guarantee facility was reduced by 6 million NOK (approximately \$ 1 million) to 9 million NOK (approximately \$1.5 million).

In order to manage its net invested working capital requirements to fund current and anticipated contracts, ProSep closed a private placement of \$2.7M with a group of current and new shareholders in May 2010.