



Management Discussion and Analysis August 10, 2010

For the second quarter and six-month period ended June 30, 2010

This Management Discussion and Analysis ("MD&A") should be read in conjunction with ProSep Inc.'s ("ProSep" or the "Company") Unaudited Interim Consolidated Financial Statements for the three and six-month periods ended June 30, 2010 and 2009 and should also be read with the Company's Annual Audited Consolidated Financial Statements and MD&A for the year ended December 31, 2009.

Regulatory Filings

The Company's continuous disclosure material including interim filings, annual MD&A and Audited Consolidated Financial Statements, Annual Information Form and Notice of Annual Shareholder Meeting and Proxy Circular are available at www.sedar.com and on the Company's website at www.prosepinc.com.

Caution Regarding Forward-Looking Statements

This MD&A may contain forward-looking statements, including statements regarding the business and anticipated financial performance of ProSep. These statements are based, among others, on management's current assumptions, expectations, estimates, objectives, plans and intentions regarding projected revenues and expenses, the economic and industry environments in which the Company operates or which could affect its activities, the Company's ability to attract new clients and consumers as well as its operating costs, raw materials and energy supplies which are subject to a number of risks and uncertainties. Forward-looking statements can generally be identified by the use of the conditional tense, the words "may", "should", "would", "believe", "plan", "expect", "intend", "anticipate", "estimate", "foresee", "objective" or "continue" or the negative of these terms or variations of them or words and expressions of similar nature. Actual results could differ materially from the conclusion, forecast or projection stated in such forward-looking information. These statements are subject to a number of risks and uncertainties that may cause actual results to differ materially from those contemplated by the forward-looking statements. Some of the factors that could cause such differences include but are not limited to the Company's ability to develop, manufacture, and successfully commercialize value-added equipment and services, the availability of funds and resources to continue its operations and pursue its projects, legislative or regulatory developments, competition, technological change, changes in government and economic policy, inflation and general economic conditions in geographic areas where ProSep operates. These and other factors should be considered carefully and undue reliance should not be placed on the forward-looking statements.

Use of estimates

In the course of the preparation of financial statements in conformity with Canadian generally accepted accounting principles ("GAAP"), management must make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and revenues and expenses for the period. Actual results could differ from these estimates.

All amounts are in Canadian Dollars unless otherwise specified.

Non-GAAP Measurements

This MD&A contains the terms "earnings before interest, taxes, depreciation and amortization" ("EBITDA") and "Net Invested Working Capital" ("NIWC") which should not be considered as an alternative to or more meaningful than net earnings or cash flow from operating activities as determined in accordance with GAAP as an indicator of the Company's performance. These terms do not have any standardized meaning as prescribed by GAAP. ProSep's determination of EBITDA and NIWC may not be comparative to that reported by other companies.

Management uses EBITDA, among other measures, to assess the operating performance of the ongoing businesses without the effects of depreciation expense. The Company excludes depreciation expenses since they largely depend on the accounting methods and assumptions a company uses, as well as on non-operating factors such as the historical cost of capital assets. The following table reconciles EBITDA with net income.

	Three months ended June 30,		Six months ended June 30,	
	2010	2009	2010	2009
	\$	\$	\$	\$
Net loss	(304,679)	(7,147,852)	(1,609,384)	(9,132,368)
Plus				
Future tax provision (recovery)	43,701	(111,945)	(510,760)	(28,372)
Current tax provision	(369,293)	145,752	(367,242)	185,085
Amortization	392,461	394,707	770,968	770,179
Net Financial charges	364,518	692,745	1,166,828	2,031,233
Increase in fair value of long-term investments	(375,000)	-	(375,000)	-
Impairment of Goodwill	-	6,500,000	-	6,500,000
EBITDA (loss)	(248,292)	473,407	(924,590)	325,757

NIWC is also used by management to analyze the total amount invested to support outstanding contracts and is defined as the sum of restricted cash related to letters of guarantee, receivables, inventories and prepaid expenses less the sum of the accounts payable, accrued liabilities and deferred revenue.

The following table shows the calculation of this non-GAAP measure.

	June 30, 2010	December 31, 2009
	\$	\$
Restricted cash	5,144,359	2,022,940
Receivables	14,627,168	12,807,205
Inventories	462,312	392,709
Prepaid expenses	612,312	665,162
Total (a)	20,846,151	15,888,016
less		
Accounts payable and accrued liabilities	12,233,784	12,836,057
Deferred revenue	401,696	71,796
Total (b)	12,635,480	12,907,853
Net Invested Working Capital (a minus b)	8,210,671	2,980,163

Comparative Figures

If applicable, comparative figures for the financial information related to the three and six-month periods ended June 30, 2009 have been reclassified to conform with the June 30, 2010 presentation.

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1. OVERALL PERFORMANCE

1.1 Highlights of the Quarter Ended June 30, 2010 and Subsequent Events

Financial:

- Revenues of \$8.7 million, a decrease of 7% when compared to \$9.3 million for the corresponding period of 2009. Year-to-date, revenues amount to \$18 million, a 20% reduction from the \$22.5 million generated during the first half of 2009.
- Gross margin of \$2.6 million (30% of revenues) compared to \$3.7 million (40%) for the corresponding period of 2009. Year-to-date, gross margin stands at \$5.1 million (29%) compared to \$6.9 million (31%) for the same period last year.
- Net loss of \$0.3 million compared with a net loss of \$7.1 million for the corresponding period of 2009. Year-to-date, net loss amounts to \$1.6 million compared to \$9.1 million for the same period last year. Included in both the 2009 2nd quarter and year-to date net losses were a \$6.5 million goodwill impairment and debt conversion and settlement cost amounting to \$2.1 million.
- Existing and new shareholders participated in a private placement for gross proceeds of \$3.7 million. Ongoing support from Fondation and Cycle Capital Fund I, L.P., which respectively own 21.8% and 18.9% of issued and outstanding shares post transaction, continues to be key to the execution of the **Company's business plan**.

Operational and corporate:

- Announced approximately \$3.2 million in new contracts during the quarter to supply process equipment to large national and international oil and gas producers.
- Concluded the first sales of conventional produced water treatment equipment after introducing this new offering in 2009.
- Announced the appointment of two highly regarded directors, Claude Fontaine, Q.C. and Joseph Wilson, to the **Company's Board of Directors**.
- **Successfully completed the ProDry's development phase with industry partners Total, Statoil and ConocoPhillips**. Results showed high performance and robustness.
- Sales backlog stood at \$9.8 million on July 1, 2010.
- Subsequent to the quarter end, ProSep announced an additional US\$6.6 million in new contracts. (see section 1.2)

1.2 Material Events and Important Subsequent Events

In this section, all material events and commitments for the three-month period are presented, followed by information on important subsequent events, up to the date of this MD&A.

On August 9, 2010 the Company announced it was awarded a \$4.1 million (U.S) contract to supply a gas dehydration system system for a natural gas development project located in the South China Sea. On the same date the Company announced it was awarded a contract valued at \$0.5 million (U.S.) to supply a chemical injection package for a leading engineering and construction services provider.

July 8, 2010 ProSep announced it was awarded a \$2.0 million (U.S.) contract to provide process engineering and specialized internals for crude separation solution to be installed at **a super major oil and gas producer's steam-assisted gravity drainage (SAGD) facility located in Alberta's oil sands**.

On May 19, 2010 ProSep announced the appointment of two new highly regarded directors. Claude Fontaine, Q.C. a former senior partner at Ogilvy Renault LLP and **one of Canada's most recognized lawyers in corporate law, commercial law, and mergers and acquisitions**. Mr. Fontaine served on many Boards of Directors including at Petro-Canada until its merger with Suncor Energy Inc. Also joining **ProSep's Board** is Mr. Joseph Wilson,

recently retired after serving as Senior Vice President — Global Ventures for NATCO, a worldwide leader in process solutions to the oil and gas industry acquired by Cameron. Mr. Wilson is a member of IPAA, NOIA, PESA, SPE and API.

On May 18, 2010 ProSep closed a private placement for aggregate gross proceeds of \$3,700,501 for which it issued a total of 28,465,385 common shares at a purchase price of \$0.13. The private placement, initially announced on May 6, 2010 was concluded in two tranches: a first tranche, announced on May 7, 2010 for gross proceeds of \$2,650,001 and a second and final tranche announced on May 18, 2010 for an additional \$1,050,500. Gross proceeds from the private placement will be used for working capital purposes. ProSep also announced it obtained an advance income tax ruling confirming it is a qualified issuing corporation and that the common shares issued in the second tranche of the private placement will qualify under the Québec Stock Savings Plan II (QSSP II).

On May 17, 2010 ProSep announced that it was awarded a \$2.2 million (U.S.) contract to supply a 75,000 barrel per day (BPD) produced water treatment package for installation on an offshore facility in the South China Sea.

On May 3, 2010 ProSep announced it was awarded a contract to supply a water treatment system to Dragados Offshore for a Pemex platform located in the Gulf of Mexico. Designed to treat 800 barrels of water per day, the system will remove free oil from the storm water/wash water drain system.

2. COMPANY OVERVIEW

2.1 Business Overview

ProSep designs, develops, manufactures, and commercializes process solutions to treat, separate and purify oil, gas, and water for the oil & gas (O&G) upstream industry. ProSep has a wide range of conventional and proprietary process equipment sold in units or in packages to O&G producers and engineering procurement **and construction firms (“EPC”) with or without process warranties.**

Global Business Model: ProSep is a solutions provider supplying high efficiency process equipment packages with process warranty.

ProSep provides:

- In-house engineering from process to details; and
- Direct and hands-on involvement with project management that includes fabrication, assembly, commissioning and services

ProSep operates around the world in the most important O&G service hubs with operations in Houston (USA), Bergen (Norway), Fusa (Norway), Kuala Lumpur (Malaysia), and Manama (Bahrain). The head office is in Montreal (Canada).

ProSep has approximately 100 employees, mainly technical sales people, process engineers, product engineers and project managers. ProSep also has workers in its new 55,000 square foot assembly shop located in Houston.

2.2 Corporate Model and Sales Network

ProSep has three diversified **business units that promote the Company’s solutions across all regional markets. Each business unit has developed its own specific expertise and reputation by tailoring the Company’s solutions to the markets it serves.** Each business unit has its own team of engineers and experienced sales people including a network of agents.



2.3 Business Environment and Strategy

In 2009, the global upstream O&G market contracted significantly with the global financial crisis, recession and depressed energy demand. The International Energy Agency (IEA) estimated that upstream CAPEX spending in 2009 fell by approximately \$90 billion, or by 22%¹ as many capital intensive projects were rendered uneconomical with the then prevailing price levels and recessionary environment. As of the second quarter of 2009, **ProSep's backlog was affected by this situation**, which translated into lower order intake (revenues) up to the most recent quarter.

Upstream capital spending recovering in 2010

The economic recovery has prompted the IEA to reiterate its forecast for growth in global oil demand. The agency indicated in its monthly Oil Market Report (released mid-July 2010) that demand would reach an average of 86.5million bpd this year, up from 84.93 million last year, although consumption in Europe still looks weak. Looking into 2011, the IEA predicts oil demand to grow exclusively on non-OECD demand, to 87.8 million bpd, with OECD demand continuing to decline (-0.5% or -0.2 mbpd)². The organisation also forecasts an average price of \$79.40 per barrel of oil in 2011.

For 2010, the upstream oil and gas industry is back to growth after almost two years of decline. IHS, a leading **source of industry information, forecasts an 8% growth in E&P investments at the world's leading publicly traded oil and gas producers**³ to \$353 billion, while Barclays Capital forecasts the increase to be closer to 9% and reach \$335 billion⁴ by the end of this year.

In line with the expected recovery, the Company continues to experience an increase in the number of requests for quotation and has been invited to tender on large projects. This trend is being observed across **the Company's operations** and the Company believes its backlog will follow the industry and could start improving in the second half of 2010 and more significantly into 2011.

¹ Aliza Fan Dutt, senior equity analyst at IHS Herold quoted in a June 15, 2010 article "E&P Capital Moving from Offshore to Onshore US – Report", in Rigzone.

² IEA's Oil Market Report published July 13, 2010. www.omrpublic.iea.org

³ IHS Herold 2010 Global Upstream Capital Spending Report

⁴ Barclays Capital Capital Original E&P Spending Survey mid-year update, June 2010

The Deepwater Horizon accident that occurred in the Gulf of Mexico led the Minerals Management Service (MMS) to institute, on May 27, 2010, a moratorium on deepwater drilling of the Coast of the United States. Until the risks involved in deepwater drilling activities are better understood by regulators, it is still unclear how this accident and subsequent oil spill will affect industry regulation and operations. It can be reasonably speculated that the **increased attention on the oil and gas industry should accelerate the industry's willingness** to invest in more efficient and sustainable technologies to mitigate the environmental impact of its activities.

Because of its global operations and limited activity in the deepwaters of the Gulf of Mexico, ProSep has not been affected by the Deepwater Horizon accident. The Company therefore has limited exposure to an extended moratorium and/or increased scrutiny of future deepwater drilling activities in the US. It is, however, too early to assess the future impact of this accident on the global offshore industry. ProSep remains **cautiously optimistic about the industry's renewed growth and will continue to target areas of strong demand**, such as South East Asia and Western Canada, and look at expanding its offering in new promising regions such as Latin America.

It remains clear that, in order to meet projected demand growth⁵ for fossil fuels, the industry will need to increase its investments to raise net capacity. The **world's conventional proven reserves are depleting and** new discoveries are mostly unconventional, and thus will require newer treatment technologies. As downhole improvements such as drilling, fracking and enhanced recovery have changed the profile of the industry, ProSep believes that innovative process solutions are needed to continue improving the economics of oil and gas production and face increased regulatory and environmental standards.

To achieve its growth objective, ProSep will continue to focus on its core business. In 2009, the Company expanded its produced water treatment offering and invested in a larger state-of-the-art manufacturing facility. As a result, ProSep is able to package its various solutions for and bid on larger projects. This strategy started delivering results with recent produced water treatment sales, the supply of an important technology component for a high profile carbon capture project, and a \$13 million CO₂ gas treatment system. ProSep will also continue to expand its offering in new markets such as Western Canada and support its growing South East Asian business operations. By accelerating the validation cycle of promising technologies, ProSep plans to substantially differentiate its offering from the competition. By working to position the Company as a market leader in technology oriented process solutions, this key differentiation factor should lead to improved gross margins in a highly competitive environment.

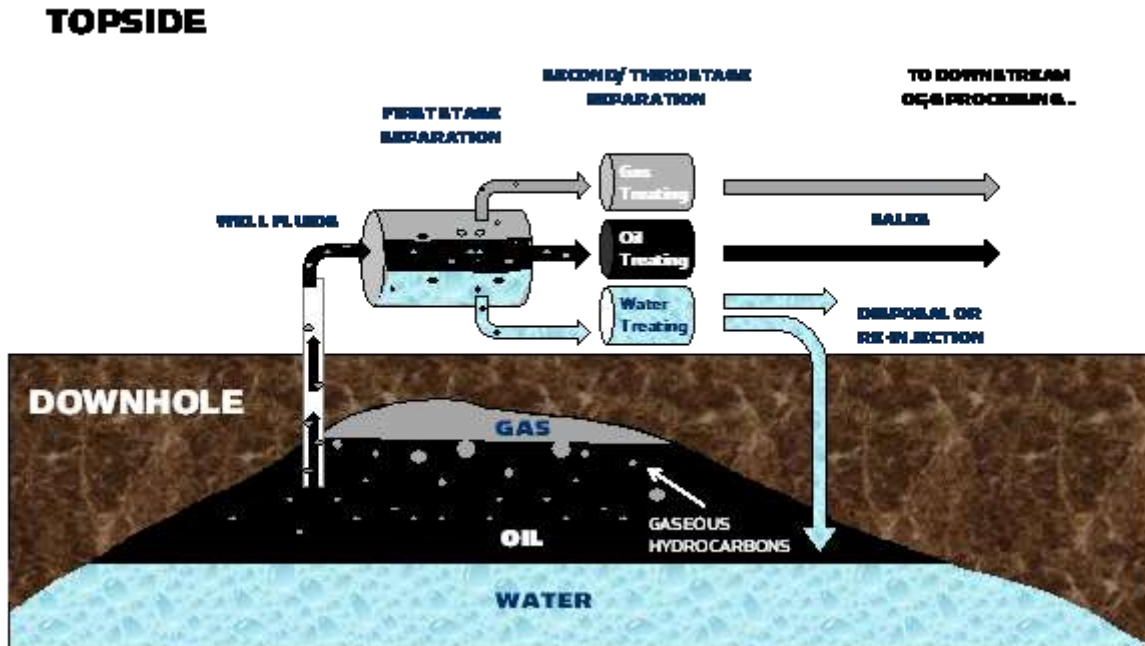
As the oil and gas equipment industry is entering a new economic cycle, ProSep must face and manage robust competition and increased pressure on gross margins. The challenge this year will be to position the Company on a solid profitability track to benefit from increasing market opportunities.

⁵ www.upstreamonline.com, May 31, 2010 « IEA sees 2010 boost in energy spend »

3. PRODUCTS

3.1 Market Segments and Product Penetration

ProSep's international team of engineers has developed extensive knowledge of process solutions for the upstream O&G treatment market. The Company's expertise lies in the development of technically advanced separation solutions destined to treat gas, oil and produced water for upstream production activities.

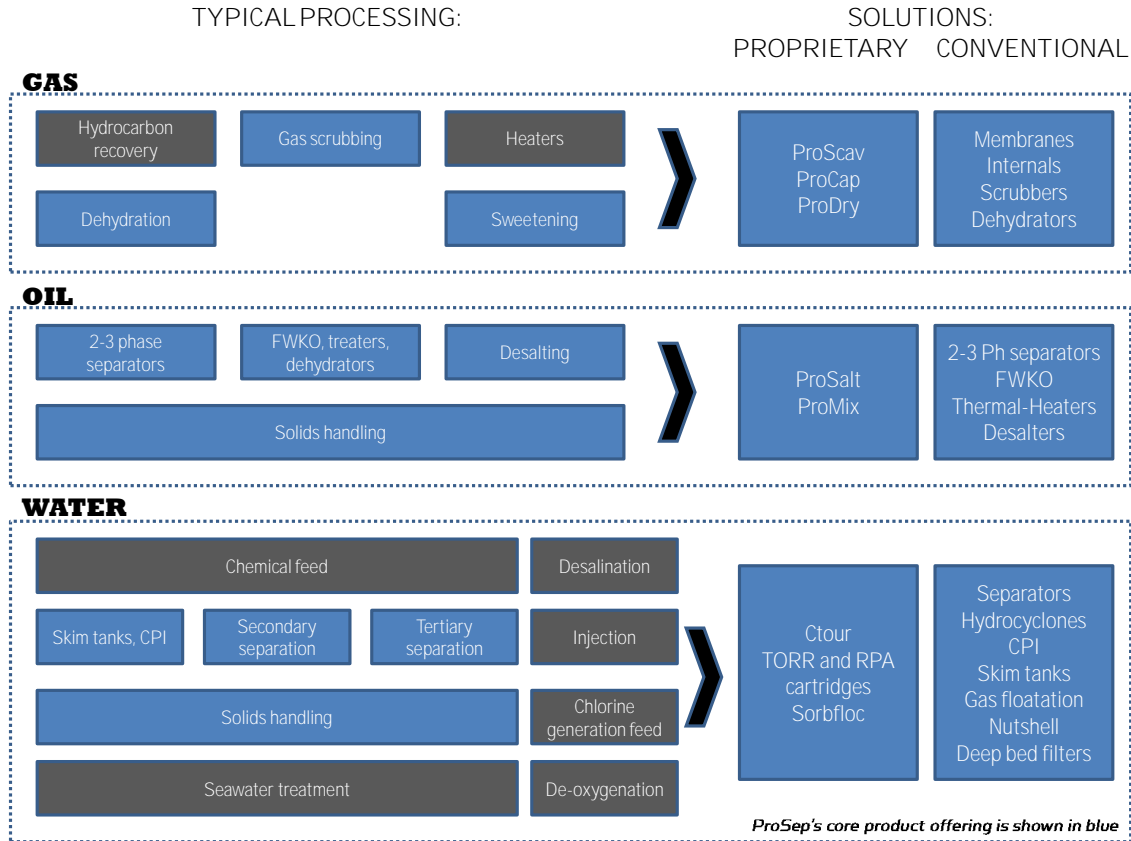


Topside Oil and Gas Separation

Whether recovered from onshore or offshore production facilities, the extracted hydrocarbon stream (oil, gas, water and solids) is brought to the surface (topside) to be processed and separated. Oil must be cleaned of salt and dissolved gas and other components; gas must be stabilized and cleaned of all liquids and unwanted components such as hydrogen sulphide and carbon dioxide before being commercialized. Produced water needs to be treated to remove all dissolved components, organic materials and solids before being disposed of or used for re-injection.

3.2 Product and Services Overview

ProSep designs customer specific solutions by utilizing its wide range of equipment to separate, treat, and polish well fluids and gas before they can be sent downstream for further refining, be disposed of, or used for re-injection. The following is a diagram of the Company's core product offering/penetration:



Process Design Experts:

ProSep’s process engineers developed a wide range of complementary branded proprietary and conventional technologies. Offered as individual equipment or complete custom-designed packages, ProSep’s technically advanced process solutions are used by O&G producers around the world to optimize separation and treatment of produced water, oil and gas. ProSep’s solutions offer environmental and economic efficiencies, allowing oil and gas producers to meet industry and regulatory requirements while optimizing profitability. The company believes this is an important and unique value-added proposition as the industry faces increasing production challenges such as diminishing production at older wells, difficult production environments, unconventional resources, and increasing use and co-production of water.

For a complete list and description of the Company’s conventional and proprietary offering, refer to the most recent Annual Information Form document available at www.sedar.com and www.prosepinc.com.

4. RESULTS OF OPERATIONS

4.1 Contracts

Sales originate from several contracts supplying conventional and proprietary gas, oil and water treatment systems to both large international oil and gas companies (“IOC”) and national oil and gas companies (“NOC”). ProSep’s systems have been delivered and installed on onshore and offshore oil and gas fields around the world.

Table of announced contracts since January 2009

Date	Value	Product	Customer	End User
Jan. 2009	US\$3.7 M	Fuel gas package	*: Major EPC firm	*: Asia Offshore IOC
Feb. 2009	US\$1.2 M	Separator	Worley Parsons	BP Exploration
March 2009	US\$2.0 M	Fuel gas package	Powertium/MMHE	Petronas
March 2009	US\$2.1 M	Gas membrane units	Whiting Petroleum	Whiting Petroleum
May 2009	\$1.4 M	ProDry "JIP"	Total, Statoil, Con.Phil.	-
July 2009	\$1 M	ProSalt, ProDry	BP, Con.Phil, Maersk	BP, Con.Phil, Maersk
October 2009	US\$12.9 M	Gas separation	Ecopetrol	Ecopetrol
January 2010	\$1 M	Water treatment (TORR)	*	*: Asia Offshore NOC
January 2010	US\$3.5 M	Gas membrane	*	*: US Onshore producer
January 2010	\$3.6 M	Water treatment (CTour)	*	*: Offshore super major
March 2010	\$0.4 M	Proprietary mixer for CO2 capture project	Statoil, Norske Shell, Gassnova	Statoil, Norske Shell, Gassnova
May 2010	n/a	Water treatment	Dragados	Dragados-Pemex
May 2010	US \$2.2 M	Water treatment	*	*: Asia Offshore
July 2010	US \$2.0 M	Engineering and specialized internals for crude separation	*	*: Super major producer in Canadian Oil Sand market
August 2010	US \$0.5M	Chemical injection package	*	*: Asia Pacific
August 2010	US \$4.1M	Gas dehydration	*	*: Asia Pacific

*: Information could not be revealed for competitive reasons.

4.2 Revenues

	US operations	European & Middle East operations	Asia Pacific operations	Consolidation & Inter segment eliminations	Consolidated operations
	\$	\$	\$	\$	\$
Three-month periods ended June 30					
2010 Revenues	5,442,085	1,997,773	1,254,485	(41,347)	8,652,996
2009 Revenues	5,211,215	1,486,889	2,791,023	(173,156)	9,315,971
Six-month periods ended June 30					
2010 Revenues	11,025,116	4,227,849	2,859,036	(51,315)	18,060,686
2009 Revenues	15,230,525	2,660,067	5,027,075	(414,916)	22,502,751

Three-month period ended June 30:

For the three-month period ended June 30, 2010, the company reported revenues of \$8,652,996, a 7% decrease from \$9,315,971 for the three-month period ended June 30, 2009. Affected by delays in the completion of contracts as well as unfavourable exchange rates, the Asia Pacific operations reported a negative revenue growth during the quarter, offsetting increased revenues from the *US* and *European and Middle East operations*.

ProSep's US operations generated revenues of \$5,442,085 during the quarter ended June 30, 2010, an increase of 4% from \$5,211,215 reported in 2009. The increase in sales is caused by the advancement of the Ecopetrol and Whiting Petroleum contracts, despite the unfavourable US currency exchange rate that

negatively affected revenues by approximately \$0.8M. During the second quarter of 2010, the average currency conversion rate for sales concluded at the US operations was 1.03 CAD/USD compared to 1.17 CAD/USD in 2009. In this quarter, the US operations contributed 63% to **the Company's** consolidated sales compared to 56% in the previous year.

The *European and Middle East operations* reported revenues of \$1,997,773 during the second quarter of 2010, representing an increase of 34% from the \$1,486,889 reported in the corresponding period of 2009. This increase is mainly due to the advancement of the \$3.6M order for a proprietary CTour produced water treatment system for an offshore redevelopment project located on the Norwegian Continental Shelf as well as the RPA cartridge orders for a TORR system installed in the North Sea on the Triton Platform.

Asia Pacific operations' revenues for the first quarter of 2010 were \$1,254,485, a decrease of 55% when compared to \$2,791,023 in 2009. Delays in the contractual completion of the glycol regeneration package, which were partly caused by change orders and requisitions, has limited the operations' ability to recognize more revenue. Unfavourable exchange rates for a contract signed in the US also accounts for the loss in revenue, explaining about 5% of the total decrease. CAPEX programs, however, remain quite strong in the region supported by national oil companies that are looking to mitigate the overall decline in oil production and bolster gas reserves and production. Since the end of the second quarter, the Company announced USD 6.6M in new contracts.

Six-month period ended June 30:

For the six-month period ended June 30, 2010, the Company reported revenues of \$18,060,686, a 20% decrease from \$22,502,751 in 2009. This decrease is mostly attributed to the Company's US operations, where revenues were impacted by a loss of approximately \$2M due to the unfavourable exchange rate. These operations were also affected by a lower order intake due to residual weakness in upstream capital expenditure programs as well as increased competition in the market.

The *European and Middle-East operations* reported revenue of \$4,227,849, a 59% increase from the \$2,660,067 reported during the six-month period in 2009. Increased revenue from these operations correlates both to the proprietary CTour system and the aforementioned TORR RPA cartridges.

Asia Pacific operations' revenues for the first two quarters of 2010, at \$2,859,036, were down 43% when compared to the 2009 figure of \$5,027,075. As previously mentioned, the unfavourable exchange rate of a contract signed in US dollars, reduced the amount of reported revenues attributable to progress on this contract; however, a greater factor in the reduction of revenue was the delay in the completion of the contract, which was caused by change orders and part ordering.

4.3 Cost of Goods Sold and Gross Margin

Three-month period ended June 30

		US Operations	European & Middle East operations	Asia Pacific operations	Corporate Office	Consolidation & Inter segment eliminations	Consolidated operations
		\$	\$	\$	\$	\$	\$
2010	Cost of goods sold	4,094,664	897,571	1,130,792	-	(41,347)	6,081,680
	Gross margin	1,347,421	1,100,202	123,693	-	-	2,571,316
		25%	55%	10%			30%
2009	Cost of goods sold	3,040,813	534,633	2,197,233	-	(173,156)	5,599,523
	Gross margin	2,170,402	952,256	593,790	-	-	3,716,448
		42%	64%	21%			40%

Led by the European and Middle East operations, which **are focusing on the Company's proprietary product** offering, the Company reported a consolidated gross margin of 30% of revenues at \$2,571,316 in the second quarter of 2010 compared to 40% of revenues at \$3,716,448 for the three-month period ended June 30, 2009. In 2009, unusually high consolidated quarterly margins were due to savings in the commissioning of projects and increased labor component compared to material input of contracts delivered.

The US Operations reported a lower gross margin of \$1,347,421, or 25% of revenues, compared to \$2,170,402 or 42% of revenues in 2009. Most of the 2010 second quarter margin was derived from the Whiting Petroleum and Ecopetrol gas skids. The decrease in gross margin percentage is mostly attributed to unplanned savings in the commissioning of projects that was recorded in the second quarter of 2009. With the exclusion of this element, the margin reported in 2009 would have been comparable to the margin reported in 2010.

As previously stated, *European & Middle East operations* contributed positively to the consolidated second quarter 2010 gross margin with \$1,100,202, or 55% of revenues, compared to \$952,256 or 64% of the revenues during the corresponding quarter of 2009. Its current profitability derives from the proprietary CTour produced water treatment system contract announced in January 2010 in addition to the delivery of the TORR RPA cartridges for installation in the North Sea. The high margins in 2009's second quarter were primarily derived from projects with high labour components compared to material input in the contract mix.

Asia Pacific operations reported a second quarter 2010 gross margin of \$123,693, or 10%, compared to **\$593,790 or 21% during the corresponding quarter of 2009. This quarter's unusually low gross margin** was caused by the unplanned extra costs of one contract and the delays prompted by change orders. Extra costs accounted for are in line with the revenue and cost recognition methodology used by the Company. Excluding these unplanned extra costs, the Q2-2010 margin would have been in the 20% range, a better reflection of gross margin levels.

Six-month periods ended June 30

		US Operations	European & Middle East operations	Asia Pacific operations	Corporate Office	Consolidation & Inter segment eliminations	Consolidated operations
		\$	\$	\$	\$	\$	\$
2010	Cost of goods sold	8,470,261	1,865,491	2,626,624	-	(51,315)	12,911,061
	Gross margin	2,554,855	2,362,858	232,412	-	-	5,149,625
		23%	56%	8%			29%
2009	Cost of goods sold	10,785,126	1,374,639	3,824,782	-	(414,916)	15,569,631
	Gross margin	4,445,399	1,285,428	1,202,293	-	-	6,933,120
		29%	48%	24%			31%

For the six-month period ended June 30, 2010, gross margin represented 29% of revenues, or \$5,149,625, compared with 31% or \$6,933,120 the year before.

Gross margins as a percentage of revenues at the *US operations* decreased from 29% in the six-month period ended June 30 2009 to 23% this year. As mentioned above, the differences in margins are explained by unplanned and non-recurring cost savings in the commissioning of projects recorded in the second quarter of 2009.

Gross margins as a percentage of revenues at the *European & Middle-East operations* were 56% on a year-to-date basis, up from 48% for the corresponding period in 2009. The improved gross margin reflects the contribution of the CTour produced water contract as well as delivery of the TORR RPA cartridges.

Gross margins as a percentage of revenues at the *Asia Pacific operations* were 8% for the two first quarters of 2010 compared to 24% in 2009. This year's unusually low gross margin was caused by unplanned extra costs on one contract as well as delays due to change orders.

Expenses and EBITDA

Expenses and EBITDA* for the 3-month periods ended June 30, 2010 and 2009

	2010 \$	2009 \$
Revenue	8,652,996	9,315,971
Sales and marketing	498,580	631,672
Research and development	90,129	139,137
General and administrative	2,230,899	2,472,232
	2,819,608	3,243,041
EBITDA (loss)	(248,292)	473,407

Expenses and EBITDA* for the 6-month periods ended June 30, 2010 and 2009

	2010 \$	2009 \$
Revenue	18,060,686	22,502,751
Sales and marketing	1,009,668	1,105,651
Research and development	151,919	300,633
General and administrative	4,912,628	5,201,079
	6,074,215	6,607,363
EBITDA (loss)	(924,590)	325,757

* 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. Please refer to section called non-GAAP measurement

EBITDA was negative at \$248,292 for the three-month period ended June 30, 2010 compared to \$473,407 for the same period in 2009. The decline in EBITDA of \$721,699 is largely attributed to a lower order intake, delays in contract completion due to change orders, unplanned extra costs on contracts in the *Asia Pacific operations*, and 2009's positive impact in relation to savings in commissioning costs. Unfavourable currency exchange rates also contributed to the lower EBITDA level, with a global net impact of approximately \$0.2M.

When comparing the six-month periods ended June 30, the EBITDA was negative \$924,590 in 2010 compared to \$325,757 in 2009. The decrease of \$1.3 million in the year to date EBITDA is explained by the reasons outlined above.

Sales and Marketing Expenses

Sales and marketing expenses were \$498,580, or 5.8% of revenues for the three-month period ended June 30, 2010 compared to \$631,672, or 6.7% for the same period in 2009. For the six-month period ended June 30, 2009, sales and marketing expenses were \$1,009,668 (5.5% of revenue) compared to \$1,105,651 (4.9% of revenue) in the previous year. Reduction in costs is mostly caused by the lower US exchange rate in relation to the costs incurred at the US operations. The majority of these expenses relate to salaries, marketing, promotions, and travel activities.

Research and Development Expenses

Research and development expenses decreased to \$90,129 in the three-month period ended June 30, 2010 from \$139,137 the year before. For the six-month period ended June 30, 2010, these expenses stood at \$151,919, a decrease of close to 50% from the \$300,633 reported a year before. Higher allocation of R&D resources to direct costs of commercial and R&D projects explain these variances.

Development activities are conducted under the umbrella of joint industry partnerships (“JIP”) with super major oil and gas companies. This is a highly efficient collaboration model that allows the Company to develop pioneering technologies by addressing a fair portion of project financing needs and validates market interest before the applications reach commercialization. The Company retains all property rights including technology, patents, and licensing fees relating to future sales of all products developed.

General and Administrative Expenses

General and administrative expenses were \$2,230,899 for the three-month period ended June 30, 2010, a 10% reduction over the \$2,472,232 reported a year before. For the period ended June 30, 2010, G&A expenses were \$4,912,628, compared to \$5,201,079 in the corresponding period of 2009. Reduction in both the second quarter and year to date expenditures is directly related to **the Company’s** continued efforts in monitoring costs. The reduction was also caused by the higher allocation of costs to projects in our European and Middle-East operations and lower US exchange rate used to convert the expenses into Canadian currency. However, cost reduction was abated by the extra costs associated with the US operations moving into a new shop, for which rent began in the second half of 2009. The majority of the general and administrative expenses relate to salaries (including benefits), professional fees (which include regulatory fees, legal fees, accounting and audit fees, investor and public relation fees, and consulting fees), and expenses related to office infrastructure.

4.4 Goodwill impairment

In the second quarter of 2009, the Company performed a testing of the goodwill valuation in light of the anticipated impact of the balance sheet restructuring initiative. As such, the Company determined that the anticipated value of ProSep was below its carrying value. Accordingly, an impairment charge of \$6.5 million was recorded in June of 2009. No further goodwill impairment was recognized in 2010.

4.5. Increase in fair value of ABCP

During this quarter, the Company recognized a \$375,000 increase in the value of its investment in Notes held since January 2009 following the restructuring of the asset-backed commercial paper. This increase in value reflects the effect of the market indicators as of June 30, 2010 on the valuation technique used by the Company.

4.6 Financial Charges

Total financial charges were \$364,518 for the quarter ended June 30, 2010 compared to \$692,745 for the same period of 2009. On a year to date basis, the total financial charges stood at \$1,166,828 compared to \$2,031,233 in 2009. The decrease in both the quarter and year to date figures is attributed to reduced interest expenses on long-term debt in relation to the balance sheet restructuring initiative completed in the third quarter of 2009. Overall, this initiative reduced the principal amount of the indebtedness by \$7.8 million, the short-term debt repayment obligations by over \$2.4 million, and provided \$3.9 million of cash representing net gross proceeds from the Rights Offering.

4.7 Income Tax

Total income taxes recoverable were \$325,592 in the three-month period ended June 30, 2010 compared to a provision of \$33,807 in the three-month period ended June 30, 2009. For the six-month period ended June 30, 2010, total income taxes recoverable were \$878,002 compared to a provision of \$156,713 a year ago. The tax recovery arose from the net loss reported at our US operations. This compares to the net profit from these operations in 2009. The **Company's operating revenues and expenses** are reported by various operations located around the world and are subject to various fiscal jurisdictions. Some of the subsidiaries are profitable, while others have yet to generate net income and some have accumulated tax losses.

4.8 Net Loss

During the second quarter of 2010, the Company reported a net loss of \$304,679 (\$0.00 per share), **compared to last year's second quarter net loss of \$7,147,852 (\$0.11 per share)**. On a year-to-date basis, net loss stands at \$1,609,384 (\$0.01 per share) for 2010 compared to \$9,132,368 (\$0.14 per share) for the first half of last year. In 2009, net loss was affected by a \$6.5 million goodwill impairment charge resulting from the balance sheet restructuring initiative concluded in the third quarter of 2009.

Basic and diluted losses per share were calculated using the weighted-average number of common shares outstanding during the period: 169,861,137 shares for the period ended June 30 2010 and 64,443,451 shares for the corresponding period of 2009.

4.9 Foreign Currency Translation Adjustment (Part of Comprehensive Loss)

During the second quarter of 2010, the Company recorded a positive foreign currency translation adjustment of \$1,198,957, resulting from the conversion of the balance sheet of the foreign subsidiaries into Canadian currency. The conversion of bank debts denominated in the Norwegian Kroner, which depreciated in relation to the Canadian dollar, **predominately accounted for this quarter's positive currency translation**; in addition, the conversion of the US operations' **goodwill** denominated in US dollars, which appreciated in relation to the Canadian dollar, also contributed to the positive currency translation. In the fourth quarter of 2009, following several significant changes, the Company reconsidered the functional currency of each of the Company's domestic and foreign operations and concluded that all of the foreign subsidiaries were self-sustaining. The underlying changes in measurement currencies of the foreign subsidiaries were accounted for prospectively, effective October 2009, with no change to previously reported results or balances. As such, no amount was accounted for in regards to the foreign currency translation adjustment of the first quarter of 2009.

4.10 Legal Proceedings

The Company was the defendant in a claim made by Westend Enviro Consultants in the Supreme Court of British Columbia on March 31, 2006 for damages relating to breach of contract and fraudulent misrepresentation in an amount totalling \$280,000. This claim was settled in the first quarter of 2010 for a total amount of \$102,000 (plus interest). As a provision covering substantially all this amount had been recorded in the previous year, this settlement had no significant impact on the results of the Company in 2010.

5. SUMMARY OF QUARTERLY RESULTS

Selected Quarterly Financial Performance

	2010		Year Ending December 31, 2009				Year Ending December 31, 2008			
	Q2	Q1	Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1
Revenue (000 \$)	8,653	9,408	9,730	9,186	9,316	13,187	14,799	12,548	15,141	9,117
Net income (loss) (000 \$)	(304)	(1,305)	(1,306)	(3,440)	(7,148)	(1,985)	27 ²	1,848 ¹	(162)	(3,338)
Basic EPS ¹ (loss) (\$)	(0.00)	(0.01)	(0.01)	(0.02)	(0.11)	(0.03)	0.00	0.03	(0.00)	(0.05)
Diluted EPS (\$)	n/a	n/a	n/a	n/a	n/a	n/a	0.00	0.03	n/a	n/a

*EPS: Earnings per share

¹Net income includes a reversal of \$1.3 million of warranty provision.

²Net income includes a further reversal of \$1.3 million of warranty provision.

6. BALANCE SHEET ITEMS

6.1 Assets

Total short term assets at June 30, 2010 were \$26,869,138, representing an increase of \$2,539,552 from the December 31, 2009 amount of \$24,329,586. At the end of June 2010, the Company had \$4,870,248 in cash and cash equivalents, compared to \$7,689,695 at December 31, 2009. At June 30, 2010, the Company had restricted cash in relation to the issuance of letters of guarantee (“LGs”) required to receive advance payments on contracts that amounted to \$5,144,359. This increase from \$2,022,940 at December 31, 2009, is related to new LGs issued for the Ecopetrol contract. The Company’s receivables were \$14,627,168 at June 30, 2010, an increase of \$1,819,963 from \$12,807,205 at December 31, 2009. This increase is in line with the advancement of work on contracts in all operations. Other than the increase in income tax recoverable, largely due to the lower profitability of the US operations (please refer to section 4.7 above), no major changes occurred in other short-term asset accounts since the beginning of the year.

Total long-term investments were \$3,729,775 at June 30, 2010, reflecting an increase of \$ 375,000 in the market value and the reclassification of the embedded put option value in the long term debt (see note 7 of the financial statements for more details).

Goodwill totalled \$15,364,522 at June 30, 2010, compared to \$15,195,645 at December 31, 2009. This variation is due to changes in foreign exchange conversion rates as goodwill is recorded in the local currency of each operating unit. Total intangible assets were \$8,433,893 at June 30, 2010, compared to \$8,918,517 in December of 2009. This decrease relates to amortization with an offsetting impact due to the current foreign exchange conversion rates.

6.2 Liabilities

Total liabilities at June 30, 2010 were \$32,389,651, representing a difference of \$1,043,027 from the December 31, 2009 amount of \$33,432,678. The net variance is predominantly caused by a greater amount drawn on the line of credit, reduced by lower accounts payable, accrued liabilities and the scheduled payments made on the DnB NOR term credit facility.

6.3 Equity

The Company's net equity at June 30, 2010 was \$23,364,682, compared to \$19,962,631 at December 31, 2009. This increase results from the equity issuance during the second quarter less the net loss and other comprehensive loss reported in the first two quarters of 2010.

7. OFF BALANCE SHEET ARRANGEMENTS

The Company did not enter into off balance sheet arrangements during the the six-month period ended June 30, 2010 other than the LGs issued in the normal course of business in relation to contracts with customers.

8. LIQUIDITY AND CAPITAL RESOURCES

8.1 Cash Flows

Operating Activities

Despite a lower net loss, the Company generated a negative cash flow from operations of \$2,838,865 during the quarter ended June 30, 2010, compared to a negative \$3,707,142 the year before. For the six-month period ended June 30, 2010 cash flow from the operations was negative \$3,493,724 a slight improvement over the negative \$3,960,362 reported in 2009. The improved cash flow mainly relates to lower investment in operating working capital required to support ongoing contracts.

Investing Activities

Investments during the second quarter of 2010 are mostly comprised of restricted cash, related to the issuance of an LG required to receive an advance payment on the Ecopetrol contract.

Financing Activities

The second quarter of 2010 financing activities are mostly comprised of the inflow of \$3,563,344 related to the net proceeds received from the private placement and additional drawings on the line of credit to finance operations. Second quarter and year-to-date 2009 financing activities included the release of restricted cash required under the credit facility with DnB Nor. On April 29, 2009, the Company agreed to a new covenant structure on this credit facility.

8.2 Liquidities and Working Capital

At June 30, 2010 the Company had \$4,870,248 in cash and cash equivalents compared to \$7,689,695 at December 31, 2009.

At June 30, 2010, the Company also had \$5,144,359 of restricted cash in relation to the Ecopetrol contract for the issuance of LGs. It is anticipated that this amount will become available to fund the operations of the Company in the fourth quarter of 2010 as the underlying contract is completed.

At June 30, 2010, the Company had net invested working capital (NIWC – see definition on page 2) of \$8,210,671, or 23%, of 12 months rolling sales, compared to \$2,980,163 at December 31, 2009 (7% of annual sales). The significant increase of approximately \$5.2M in NIWC was primarily caused by the increased restricted cash in relation to the Ecopetrol contract, as well as higher receivables related to the current work

on contracts. The NIWC represents the total net investment made by the Company to support outstanding contracts. Management actively monitors the NIWC in order to ensure it is at its lowest possible.

As previously demonstrated, the level of NIWC can be volatile depending on the structure and progress of contracts. The NIWC is financed through cash on hand and a bank line of credit, and is reduced by customer advances or progress payments on contracts. In some cases, such advances or payments require the issuance of LGs using the DnB NOR 15 million NOK credit facility (approximately \$2.5M at June 30, 2010), assistance provided by Export Development Canada (“EDC”), or simply by pledging cash to secure the issuance of such LGs. At June 30, 2010 the total (DnB, EDC and LGs secured by restricted cash) outstanding LGs amounted to \$10,180,528 (\$5,589,867 at December 31, 2009). As mentioned above, this amount will become available to fund the operations of the Company in October and November 2010. As sales are migrating to countries where the Company does not have a physical presence, it is anticipated that increased levels of NIWC and LGs will be required.

The Company intends to finance its future NIWC requirements from cash on hand, cash flow from operating activities, bank credit lines, assistance from EDC and funds from external sources such as equity issuance. In light of the requirement to further invest in NIWC in the second quarter, DnB NOR granted on May 11, 2010, a temporary additional capacity of 18 million NOK (approximately \$3 million) to 48 million NOK (approximately \$8.2 million) on the overdraft facility that matured on July 30. In exchange for this temporary increase, the capacity on the guarantee facility was reduced temporarily until the end of July by 6 million NOK (approximately \$1 million) to 9 million NOK (approximately \$1.5 million). The temporary capacity was repaid on July 30 using part of the proceeds from the private placement closed during the second quarter for total gross proceeds of approximately \$3.7 million.

8.3 Bank Overdraft Facilities and Obligations under Financial Liabilities

ProSep’s Bank Credit Facility at June 30, 2010

Lender	Description	Currency	Capacity (CAD)	Drawn (CAD)	Available (CAD)
DnB NOR	Overdraft	NOK/USD	\$7,852,761	\$5,922,938	\$1,929,823
	Guarantee facility	NOK	\$1,472,393	\$1,359,047	\$113,346

8.3.1 Financial Covenants

At June 30, 2010 the Company complied with its financial covenants. Under the current covenant structure, the Company must make a full repayment of its line of credit for a period of three weeks before December 1, 2010.

8.3.2 Obligation under Financial Liabilities

ProSep’s Debt and Credit Facility Repayment Schedule at June 30, 2010

	Carrying Amount	One to nine months	Nine to twelve months	One to five years	More than five years
DnB bank credit facility	\$5,922,938	\$1,014,963	\$4,907,975	-	-
DNB NOR long-term credit facility	\$3,680,982	\$736,196	\$736,197	\$2,208,589	-
Convertible unsecured debenture	\$3,628,391	-	-	\$3,628,391	-
Revolving credits with National Bank	\$4,710,339	\$53,797	-	\$4,656,542	-
Other	\$82,330	\$62,152	\$7,857	\$12,321	-
Total	\$18,024,980	\$1,867,108	\$5,652,029	\$10,505,843	-

9. TRANSACTIONS WITH RELATED PARTIES

During the three and six-month periods ended June 30, 2010, the Company did not have any transactions with related parties.

10. DESCRIPTION OF CAPITAL STRUCTURE

The Company's authorized share capital consists of an unlimited number of common shares, of which 191,721,295 common shares are issued and outstanding at June 30, 2010. During the second quarter of 2010, the Company issued 28,465,385 new shares at a price of \$0.13 for total gross proceeds of approximately \$3.7 million. Following this transaction, Fondaction and Cycle Capital Fund I, L.P., respectively own 21.8% and 18.9% of the total issued and outstanding shares.

At June 30, 2010, there were outstanding options to purchase 420,000 common shares of the Company issued pursuant to ProSep's stock option plan at a weighted average exercise price of \$0.31 per share.

The Company grants restricted share units to attract, retain, and motivate key personnel, and reward officers and employees for significant performance and distributable cash flow growth. Each restricted share unit is equal in value to one common share of the Company. The shares will be issued from the treasury of the Company. The number of shares reserved at any time must not exceed 10% of the aggregate number of outstanding shares.

At June 30, 2010, 7,181,713 restricted share units were issued and outstanding.

At June 30, 2010, warrants to purchase 4,460,242 common shares of the Company at a weighted average exercise price of \$0.44 per share were outstanding.

At June 30, 2010, convertible debentures with a nominal amount of \$3,953,500 were outstanding. These debentures mature on July 16, 2014 and can be converted into 13,178,333 common shares, representing a conversion price of \$0.30 per share.

11. IFRS CHANGEOVER PLAN

As described in the last annual MD&A, the Company has established a changeover plan to adopt IFRS by 2011. Based on the work performed to date, the differences identified between IFRS and Canadian GAAP are not expected to have a material impact on our reported results and financial position. In addition, the effects on the Company's commercial activities in terms of financial covenants, contractual agreements, incentive plans, budgeting, and financial risk management strategies, for example, have been assessed as relatively minor to date. Accordingly, efforts with respect to the areas of training, and internal and external communications are expected to be minor. During the second quarter of 2010, the Company reviewed its existing accounting systems and procedures along with its internal control over financial reporting and disclosure control processes, concluding that they would not need significant modification because of the Company's conversion to IFRS. However, there may be significant changes to the financial statements because of IFRS accounting principles and provisions for first time adoption.

Initial adoption of International Financial Reporting Standards

IFRS 1 *First-time Adoption of International Financial Reporting Standards* puts forth guidance for the initial adoption of IFRS. Under IFRS 1, the standards apply retrospectively at the transition date with all adjustments to assets and liabilities taken to retained earnings, unless certain exemptions are applied. The Company has to date decided to take the following optional exemptions provided by IFRS 1. All other available exemptions have been considered either not applicable or not significant to the Company.

Business Combinations

The Company will elect not to apply IFRS 3(R) *Business Combinations* retrospectively to business combinations that occurred prior to January 1, 2010. Accordingly, such business combinations will not be restated.

Employee benefits

The Company will not elect to apply IAS 19 *Employee Benefits* retrospectively to its defined benefit plan. It will therefore recognize to opening deficit all actuarial gains/losses at January 1, 2010 on its plan.

Cumulative translation adjustment (CTA)

The Company will elect to use the option to reset its cumulative foreign currency translation adjustment account to nil at January 1, 2010, with the balance being recognized to opening deficit.

Share-based payment transactions

The Company will elect to use the option that allows not to apply retrospectively the requirements of IFRS 2 *Share-Based Payments* to equity instruments granted on or before November 2, 2002 or which vested before January 1, 2010.

Compound financial instruments

The Company will elect to use the exemption whereby it does not need to separate the two portions of a compound instrument in accordance with IAS 32 *Financial Instruments: Presentation* when the liability component is no longer outstanding at January 1, 2010.

Expected Areas of Significance

No areas of significance besides those previously described in the last Annual MD&A, namely impairment of assets, have been identified. It should be remembered that our analysis of possible changes is still in process, and that not all decisions have been made where choices of accounting policies are available. Until our analyses and choices are finalized, the Company is not able to reliably quantify the impacts expected on our consolidated financial statements for these differences.

We note also that the standard-setting bodies that promulgate IFRS and, to a lesser extent, Canadian GAAP, continue to have significant ongoing projects that could affect the ultimate differences between Canadian **GAAP and IFRS and their impact on the Company's consolidated financial statements in future years.** There are a significant number of ongoing projects at the International Accounting Standards Board that may become requirements after 2011, and that could be adopted earlier in order to reduce the number of accounting changes in the future. Such projects that may be relevant to the Company include Liabilities, Employee Future Benefits, Revenue Recognition, and Leases. Depending on the timing of the publication of the final standards that may arise from those projects and their impact on the Company, opportunities to early adopt any such new standard will be assessed during 2010 and 2011. We have processes in place to ensure that these potential changes are monitored and evaluated. The future impact of IFRS will also depend on the particular prevailing circumstances in those years. The differences described are those existing based on Canadian GAAP and IFRS today.

The Company's IFRS project continues to be on target to meet the changeover date.

12. CRITICAL ACCOUNTING ESTIMATES

Please refer to the June 30, 2010 consolidated financial statements as well as the annual 2009 MD&A for an extended discussion on critical accounting estimates.

13. INTERNAL CONTROLS

In order to comply with the Canadian Securities Administrators' National Instrument 52-109 ("NI 52-109"), the Company has conducted an evaluation of the design of its disclosure controls and procedures and internal control over financial reporting. The implementation of NI 52-109 involves a continuous improvement process, which has led the Company to ensure that all relevant processes and controls are documented.

Internal Control over Financial Reporting

Management is responsible for establishing and maintaining adequate internal control over financial reporting to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with GAAP.

Internal control over financial reporting includes policies and procedures that pertain to the maintenance of records, which, in reasonable detail, accurately and fairly reflect the transactions, provide reasonable assurance that transactions are recorded as necessary and therefore permit the preparation of consolidated financial statements in accordance with determined authorizations. This provides reasonable assurance regarding prevention or timely detection of unauthorized use of assets that could have a material effect on our consolidated financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Projections of any evaluation of the effectiveness of our internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate due to changes in conditions or the degree to which policies and procedures are adhered.

At December 31, 2009, management had evaluated the design of its internal controls over financial reporting as defined in NI 52-109, and based on that evaluation, had determined that certain aspects of its internal controls over financial reporting were not designed effectively, but were instead mitigated by compensating procedures. As part of the evaluation conducted, the Company has implemented entity-level controls that are in accordance with the COSO control framework. This results in a much greater level of confidence in the mitigating controls to compensate for the identified deficiencies. The control deficiencies identified by the Company did not result in adjustments to our consolidated financial statements for the quarter ended June 30, 2010. **Management's assessment had identified the following significant deficiencies along with related remediation:**

Entity-Level Controls

During the course of 2009, the Company had ensured its entity-level controls were maintained in accordance with the COSO control framework. The entity-level controls have continuously evolved during the last financial year as the Company finalized implementing the previously identified entity-level controls. The Company now regularly reviews and continues to update on a quarterly basis policies to ensure that they

remain relevant and up to date. Amended policies are communicated to appropriate employees of the Company on a timely basis.

In order to mitigate the risks of entity-level controls inherent to the continuously changing business, management has maintained the following activities:

- Communication with employees and management about their roles and responsibilities in regards to internal control over financial reporting;
- Production of bi-weekly management reports;
- Bi-weekly management committee meetings;
- Bi-weekly disclosure committee meetings (included in management committee meetings);
- Full-time availability of all policies and procedures to employees, managers, and directors;
- Evaluation of the design of internal controls and continuous implementation of additional controls to ensure an increased level of confidence;
- Monthly financial statements are established by the corporate controller and reviewed and analyzed by all vice-presidents, the CFO and the President and CEO. An analytic review is provided with the financial statements in order to explain variances between actual and budget figures; and
- Quarterly financial statements along with all related documents are reviewed by members of the audit committee and approved by the Board of Directors.

In summary, the Company has implemented a number of controls during the year ended December 31, 2009, and those controls are continuing to be applied in the current financial year. The Company will be testing the implemented controls to validate their effectiveness and performance as part of the annual certification process in the fourth quarter of the year.

Segregation of Duties

As part of the effectiveness assessment as of December 31, 2009, the Company had determined that the controls within its accounting and finance department were deficient in the segregation of duties; such deficiencies are inherent to its small size. Due to the limited number of personnel in the accounting and finance department, certain financial personnel had incompatible duties that allowed for the creation, review, and processing of certain financial data without independent review and authorization.

To mitigate this risk, we continue to implement improved monitoring systems as well as other procedures to prevent potential fraud, properly assign roles and responsibilities to employees to maximize segregation of **duties within the limited environment, and rely on procedures and controls as described in “Entity-Level Controls” above.**

It should be noted that some of the deficiencies mentioned above are related to the size of the Company. Management is nevertheless committed to establishing effective internal controls over financial reporting and will continue to assess existing controls and implement additional controls as deemed necessary.

14. SELECTED RISKS

During the quarter ended June 30, 2010 risks, proposed remedies, and risk management practices have not materially changed. Refer to the 2009 annual MD&A for a complete list of risks and proposed remedies.



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