



## **PRIMARY ENERGY RECYCLING CORPORATION**

**Unaudited Interim Consolidated Financial Statements  
(In US Dollars)**

**Three Months Ended March 31, 2011 and 2010**

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**Primary Energy Recycling Corporation**  
**CONSOLIDATED STATEMENTS OF FINANCIAL POSITION**  
(In thousands of U.S. dollars)  
(Unaudited)

<b>ASSETS</b>	March 31, 2011	December 31, 2010	January 1, 2010
<b>Current assets:</b>			
Cash and cash equivalents	\$ 24,585	\$ 22,405	\$ 24,290
Accounts receivable	6,924	7,836	7,604
Inventory, net	1,000	1,005	991
Other current assets	1,492	1,243	833
<b>Total current assets</b>	<b>34,001</b>	<b>32,489</b>	<b>33,718</b>
<b>Non-current assets:</b>			
Property, plant and equipment, net (Note 6)	179,738	180,503	188,286
Intangible assets, net (Note 7)	34,737	40,166	61,881
Restricted cash (Note 3)	2,693	2,991	3,729
Deferred tax asset, net (Note 15)	4,432	4,941	-
Investment in joint venture (Note 16)	66,197	66,721	71,329
Other non-current assets (Note 17)	1	4	220
<b>Total assets</b>	<b>\$ 321,799</b>	<b>\$ 327,815</b>	<b>\$ 359,163</b>
<b>LIABILITIES AND EQUITY</b>			
<b>Current liabilities:</b>			
Accounts payable	\$ 867	\$ 361	\$ 253
Short-term debt (Note 8)	32,476	30,343	24,451
Due to affiliates (Note 18)	624	639	478
Accrued property taxes	2,615	1,965	2,356
Accrued expenses	3,757	2,068	2,232
<b>Total current liabilities</b>	<b>40,339</b>	<b>35,376</b>	<b>29,770</b>
<b>Non-current liabilities:</b>			
Long-term debt (Note 8)	29,028	37,796	73,777
Deferred income tax liability, net (Note 15)	-	-	13,507
Asset retirement obligations (Note 10)	2,651	2,604	2,426
<b>Total liabilities</b>	<b>72,018</b>	<b>75,776</b>	<b>119,480</b>
<b>Equity</b>			
<b>Equity attributable to equity owners of the company</b>			
Common stock: no par value, unlimited shares authorized; 134,118,561 issued and outstanding at March 31, 2011, December 31, 2010 and January 1, 2010	274,479	274,479	274,479
Contributed surplus	3,316	3,316	-
Accumulated shareholders' deficit	(109,065)	(107,784)	(120,656)
	168,730	170,011	153,823
<b>Non-controlling interest</b> (Note 12)	<b>81,051</b>	<b>82,028</b>	<b>85,860</b>
<b>Total equity</b>	<b>249,781</b>	<b>252,039</b>	<b>239,683</b>
<b>Total liabilities and equity</b>	<b>\$ 321,799</b>	<b>\$ 327,815</b>	<b>\$ 359,163</b>

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

**Primary Energy Recycling Corporation**  
**CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**  
*(In thousands of U.S. dollars, except share and per share amounts)*  
*(Unaudited)*

	Three Months Ended March 31,	
	2011	2010
<b>Revenue:</b>		
Capacity	\$ 9,018	\$ 9,018
Energy service	3,764	4,242
	12,782	13,260
<b>Expenses:</b>		
Operations and maintenance	2,743	2,057
General and administrative	2,331	2,324
Employee benefits (Note 22)	560	566
Depreciation and amortization	7,558	7,566
<b>Total operating expenses</b>	13,192	12,513
<b>Equity in earnings of joint venture</b> (Note 16)	1,011	835
<b>Operating income</b>	601	1,582
<b>Other (expense) income</b>		
Interest expense (Note 9)	(1,843)	(2,808)
Realized and unrealized loss on derivative contracts (Note 17)	(4)	(147)
Loss on derecognition (Note 6)	(500)	-
<b>Loss before income taxes</b>	(1,746)	(1,373)
Income tax expense (Note 15)	(512)	(315)
<b>Net loss and comprehensive loss</b>	\$ (2,258)	\$ (1,688)
<b>Net loss and comprehensive loss attributable to:</b>		
Owners of the Company	\$ (1,281)	\$ (770)
Non-controlling interest (Note 12)	(97)	(918)
	\$ (2,258)	\$ (1,688)
<b>Net loss and comprehensive loss per share attributable to owners of the company:</b>		
Weighted average number of shares outstanding - basic and diluted	134,118,561	134,118,561
<b>Basic and diluted net loss per share</b> (Note 14)	\$ (0.01)	\$ (0.01)

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**Primary Energy Recycling Corporation**  
**CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY**  
*(In thousands of U.S. dollars)*  
*(Unaudited)*

	<u>Attributable to equity owners of the company</u>					
	<u>Common stock</u>	<u>Contributed surplus</u>	<u>Accumulated deficit</u>	<u>Total</u>	<u>Non-controlling interest</u>	<u>Total equity</u>
<b>Balance - January 1, 2010</b>	\$ 274,479	\$ -	\$ (120,656)	\$ 153,823	\$ 85,860	\$ 239,683
Net loss and comprehensive loss for the three months ended March 31, 2010	-	-	(770)	(770)	(918)	(1,688)
<b>Balance - March 31, 2010</b>	<u>\$ 274,479</u>	<u>\$ -</u>	<u>\$ (121,426)</u>	<u>\$ 153,053</u>	<u>\$ 84,942</u>	<u>\$ 237,995</u>
<b>Balance - January 1, 2011</b>	\$ 274,479	\$ 3,316	\$ (107,784)	\$ 170,011	\$ 82,028	\$ 252,039
Net loss and comprehensive loss for the three months ended March 31, 2011	-	-	(1,281)	(1,281)	(977)	(2,258)
<b>Balance - March 31, 2011</b>	<u>\$ 274,479</u>	<u>\$ 3,316</u>	<u>\$ (109,065)</u>	<u>\$ 168,730</u>	<u>\$ 81,051</u>	<u>\$ 249,781</u>

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

**Primary Energy Recycling Corporation**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(In thousands of U.S. dollars)  
(Unaudited)

	Three Months Ended March 31,	
	2011	2010
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Net loss and comprehensive loss for the period	\$ (2,258)	\$ (1,688)
Adjustments for:		
Depreciation and amortization	7,558	7,566
Loss on derecognition	500	-
Realized and unrealized loss on derivative contracts	4	147
Equity in (earnings) of joint venture	(1,011)	(835)
Non-cash interest expense	690	1,108
Income tax expense	512	315
Distributions from investment in joint venture	1,535	2,071
	<u>7,530</u>	<u>8,684</u>
Net change in non-cash working capital balances	2,177	679
Net cash provided by operating activities	<u>9,707</u>	<u>9,363</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Change in restricted cash	298	-
Capital expenditures	(594)	-
Net cash used in investing activities	<u>(296)</u>	<u>-</u>
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Payments of deferred financing costs	-	(319)
Payments for stock issuance costs associated with the Rights Offering	-	(285)
Payments of fees associated with the Recapitalization	-	(9)
Repayment of debt	(7,231)	(10,162)
Net cash used in financing activities	<u>(7,231)</u>	<u>(10,775)</u>
Net increase (decrease) in cash	2,180	(1,412)
Cash and cash equivalents - beginning of period	22,405	24,290
Cash and cash equivalents - end of period	<u>\$ 24,585</u>	<u>\$ 22,878</u>
<b>Supplemental disclosure of cash flow information:</b>		
Cash paid during the period for interest	\$ 1,160	\$ 1,706

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

**Primary Energy Recycling Corporation**  
**NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS**  
*(In thousands of U.S. dollars unless specified, except share and per share amounts)*  
*(Unaudited)*

**1. General information**

Primary Energy Recycling Corporation (“PERC” or “the Company”) was incorporated on June 10, 2005 under the laws of the Province of Ontario and continued under the laws of British Columbia, and its head office is located at 2215 S. York Road, Oak Brook, IL 60523. The address of its registered office is Suite 1600, Cathedral Place, 925 West Georgia Street, Vancouver, British Columbia, Canada V6C 3L2. The Company initiated business activity on August 24, 2005 and owns 85.7% of the common membership interests of Primary Energy Recycling Holdings LLC (“PERH”). PERH, headquartered in Oak Brook, Illinois, indirectly owns and operates three recycled energy projects, one clean heat and power project and a 50% interest in a pulverized coal facility, all located in the United States (collectively, the “Projects”). The Projects have a combined electrical generating capacity of 283 megawatts and a combined steam generating capacity of 1.8 MMlbs/hour. PERH creates value for its customers by recycling recoverable heat and by product fuels from industrial and electric generation processes and converting it into reliable and economical electricity and thermal energy for resale back to its customers. For additional information with respect to the business, please see the Company’s public filings including its most recent annual information form available on SEDAR at [www.sedar.com](http://www.sedar.com).

**2. Basis of preparation and adoption of International Financial Reporting Standards (“IFRS”)**

These interim consolidated financial statements have been prepared in accordance with IFRS applicable to the preparation of interim financial statements, including IAS 34 and IFRS 1. Subject to certain transition elections disclosed in note 4, the Company has consistently applied the same accounting policies in its opening IFRS statement of financial position at January 1, 2010 and throughout all periods presented, as if these policies had always been in effect. Note 4 discloses the impact of the transition to IFRS on the Company’s reported financial position, financial performance and cash flows, including the nature and effect of significant changes in accounting policies from those used in the Company’s consolidated financial statements for the year ended December 31, 2010.

The policies applied in these interim consolidated financial statements are based on IFRS issued and outstanding as of May 10, 2011, the date the Board of Directors approved these statements. Any subsequent changes to IFRS, that are given effect in the Company’s annual consolidated financial statements for the year ending December 31, 2011 could result in restatement of these interim consolidated financial statements, including the transition adjustments recognized on change-over to IFRS.

The March 31, 2011 interim consolidated financial statements are the Company’s first financial statements prepared under IFRS, with a transition date to IFRS of January 1, 2010. Consequently the comparative figures for 2010 and the Company’s statement of financial position as of January 1, 2010 have been restated to comply with IFRS. Note 4 provides reconciliations to IFRS from the previously published Canadian generally accepted accounting principles (“Canadian GAAP”) financial statements. In addition, IFRS 1 on first time adoption allows certain exemptions from retrospective application of IFRS in the opening statement of financial position that are also explained in Note 4.

The interim consolidated financial statements should be read in conjunction with the Company’s Canadian GAAP annual financial statements for the year ended December 31, 2010.

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**NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS**  
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**3. Basis of measurement and significant accounting policies**

The principal accounting policies applied in the preparation of these consolidated financial statements are as follows:

***Basis of measurement***

These consolidated interim financial statements have been prepared under the historical cost convention except for the revaluation of certain financial assets to fair value including derivative instruments.

The preparation of financial statements in accordance with IAS 34 requires the use of certain critical accounting estimates. It also requires management to exercise judgment in the process of applying the Company's accounting policies. Management bases its estimates on historical experience and other assumptions, which it believes are reasonable. If actual amounts are ultimately different from these estimates, the revisions are included in the Company's results of operations for the period in which the actual amounts become known.

***Critical accounting estimates and judgments***

The preparation of financial statements requires the Company to make estimates and assumptions concerning the future that affect the reported amounts of assets and liabilities and by definition will seldom equal actual results. The estimates and judgments that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

***Property plant and equipment***

***Estimated useful lives***

Management estimates the useful lives of property, plant and equipment based on the period during which the assets are expected to be available for use. The amounts and timing of recorded expenses for amortization of property, plant and equipment for any period are affected by these estimated useful lives. The estimates are reviewed at least annually and are updated if expectations change as a result of physical wear and tear, technical or commercial obsolescence and legal or other limits to use. It is possible that changes in these factors may cause significant changes in the estimated useful lives of the Company's property, plant and equipment in the future. (See note 6)

***Asset retirement obligations***

Provisions for asset retirement obligations require the assessment of the amounts that the Company will have to pay and assumptions in terms of timing and discount rate. (See note 10)

***Income taxes***

Estimation of income taxes included an evaluation of the recoverability of deferred tax assets based on an assessment of the Company's ability to utilize the underlying future tax deductions against future taxable income before they expire. The Company's assessment is based upon existing tax laws and estimates of future taxable income. If the assessment of the Company's ability to utilize the underlying future tax deductions changes, the Company would be required to recognize more or fewer of the tax deductions as assets, which would decrease or increase the income tax expense in the period in which the determination is made. (See note 15)

***Consolidation***

The financial statements of the Company consolidate the accounts of PERC and its subsidiaries. Inter-company transactions, balances and unrealized gains on transactions between related companies are eliminated. Unrealized losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred.

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Subsidiaries are all entities over which the Company has the power to govern the financial and operating policies, which is generally the case if the Company holds shares representing more than one half of the voting rights. Subsidiaries are fully consolidated from the date on which control is transferred to the Company. They are de-consolidated from the date on which the Company ceases to control the entity.

***Revenue recognition***

The Company operates its facilities under certain tolling and operation and maintenance agreements with its customers. These agreements with customers qualify as operating lease arrangements for accounting purposes. Substantially all of the Company's buildings and equipment serve as rental property under these operating leases.

Revenue from these agreements consists of Capacity Revenue and Energy Service Revenue. Capacity revenue represents the fixed revenue amounts established in the tolling agreements with the Company's customers and is billed on a monthly basis. Energy Service revenue represents the revenue earned based on measurements of services performed and delivered during each period. Energy Services Revenue is recorded as services are delivered. Revenue is recorded on the accrual basis and may include estimates for services delivered.

***Operating expenses***

Operating expenses in the consolidated statement of comprehensive income have been classified using the nature rather than functional designation as the Company believes it is more representative of business operations. The categories of expenses are operations and maintenance, general and administrative, employee benefits and depreciation and amortization. Operations and maintenance expenses are comprised of costs incurred to operate the facilities and include expenditures for water and boiler treatment chemicals, equipment rental and calibration, contracted services, maintenance related expenditures related to cleaning and repair as well as environmental costs. General and administrative expenses are comprised of administrative support, insurance, professional fees, management fees, property taxes and other. Employee benefit expenses are outlined in note 22.

***Non-controlling interest***

Non-controlling interest represents an equity interest in subsidiaries owned by an outside party. The share of net assets of subsidiaries attributable to the non-controlling interest is presented as a component of equity. Their respective share of net income and comprehensive income is recognized directly in equity. Changes in the parent company's ownership interest in subsidiaries that do not result in a loss of control are accounted for as equity transactions.

***Cash and cash equivalents***

Cash and cash equivalents include cash in hand and other short-term highly liquid investments with original maturities of three months or less.

***Restricted cash***

Restricted cash is segregated from cash balances for purposes of the consolidated statement of cash flows and consolidated statement of financial position as, the restricted cash balance is required to be maintained separately under the terms of the Company's Credit Facility (as described below) as a debt service reserve and is not part of the Company's cash management activities.

***Inventory***

The Company maintains a certain level of spare parts inventory at its facilities. This inventory is stated at the lower of cost and net realizable value and is classified in current assets. Inventory cost is determined using weighted average costing. Net realizable value is the estimated selling

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price in the ordinary course of business, less applicable selling expenses. As spare parts are consumed the expense is recognized in profit and loss. Major spare parts and standby equipment are capitalized in property, plant and equipment and depreciated.

***Property, plant and equipment***

Property, plant and equipment are stated at cost, less accumulated depreciation and any accumulated impairment losses. The cost of an asset is comprised of its purchase price or construction cost, any costs directly attributable to bringing the asset into operation, estimated cost of any decommissioning obligation, if any, and, for qualifying assets, borrowing costs. The purchase price or construction cost is the aggregate amount paid and the fair value of any other consideration given to acquire the asset.

Expenditures for major overhauls and inspections are capitalized and depreciated over the expected time horizon until the next overhaul. The carrying amount of the replaced part is de-recognized. All other repairs and maintenance are charged to the consolidated statement of comprehensive income during the financial period in which they are incurred.

Depreciation is charged so as to write off the cost or valuation of assets, other than land and properties under construction, over their estimated useful lives, using the straight-line method, on the following bases.

Buildings	28 years
Leasehold improvements	Lesser of lease term or life of improvement
Machinery and equipment	28 years
Capitalized overhauls	4 to 10 years
Vehicles	3 to 5 years
Office equipment	3 to 7 years
Fixtures and fittings	3 to 7 years

***Impairment of non-financial assets***

Property, plant and equipment and intangible assets are tested for impairment when events or changes in circumstances indicate that the carrying amount may not be recoverable. Long-lived assets that are not amortized are subject to an annual impairment test. For the purpose of measuring recoverable amounts, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units or CGUs). The recoverable amount is the higher of an asset's fair value less costs to sell and value in use (being the present value of the expected future cash flows of the relevant asset or CGU). An impairment loss is recognized for the amount by which the asset's carrying amount exceeds its recoverable amount.

***Intangible assets***

The Company's intangible assets consist of contract rights which represent the value assigned to existing customer contracts at the date of their acquisition. They have a finite useful life and are carried at cost less accumulated amortization which is calculated using the straight-line method over their estimated useful lives. The expected useful lives of assets are reviewed on an annual basis and, if necessary, changes in useful lives are accounted for prospectively.

***Foreign currency***

The functional currency of the Company is the U.S. dollar and all amounts presented in these financial statements and notes contained herein are presented in U.S. dollars, unless otherwise specified.

**Primary Energy Recycling Corporation**  
**NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS**  
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***Borrowings***

Borrowings are recognized initially at fair value, net of transaction costs incurred. Borrowings are subsequently stated at amortized cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognized in the consolidated statement of comprehensive income over the period of the borrowings using the effective interest method.

Borrowings are classified as current liabilities unless the Company has an unconditional right to defer settlement of the liability for at least 12 months after the financial position date.

***Provisions***

Provisions for environmental restoration, restructuring costs and legal claims are recognized when: the Company has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation and the amount can reliably be estimated.

Provisions are measured using management's best estimate required to settle the obligation at the end of the reporting period and are discounted to present value where the effect is material.

***Asset retirement obligations***

Asset Retirement Obligations ("AROs") are recognized for all legal and constructive obligations to retire or decommission an existing asset and remediate facilities. The fair value of estimated asset retirement obligations is recognized in the consolidated statement of financial position when identified and a reasonable estimate of fair value can be made. The asset retirement cost, equal to the estimated fair value of the asset retirement obligation, is capitalized as part of the cost of the related long-lived asset. The fair value of the asset retirement obligation depends on the total undiscounted amount of the estimated cash flows required to settle the obligations and the appropriate risk-adjusted discount rate used to discount the estimated cash flows to fair value. The asset retirement costs are amortized over the asset's estimated useful life and included in depreciation expense on the consolidated statement of comprehensive income. Increases in the asset retirement obligation resulting from the passage of time are recorded as accretion of asset retirement obligation, and are included in finance costs in the consolidated statement of comprehensive income. Actual expenditures incurred are charged against the accumulated obligation. The methods and assumptions used to determine the fair value of the asset retirement obligation are evaluated at least on an annual basis. Any resulting changes in fair value are recorded as of the financial position date and changes to the amount of future accretion are recorded prospectively.

***Income tax***

Income tax comprises current and deferred tax. Income tax is recognized in the statement of comprehensive income. Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted, or substantively enacted, at the end of the reporting period, and any adjustment to tax payable in respect of previous years.

Deferred tax is recognized in respect of temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. Deferred income tax is determined on a non-discounted basis using tax rates and laws that have been enacted or substantively enacted at the financial position date and are expected to apply when the deferred tax asset or liability is settled. Deferred tax assets are recognized to the extent that it is probable that the assets can be recovered. Valuation allowances are provided against deferred tax assets where recovery is not considered probable. Deferred income tax assets and liabilities are presented as non-current. Tax on income in interim periods is accrued using the tax rate that would be applicable to expected total annual earnings.

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***Derivative financial instruments and hedging activities***

Derivatives are carried at fair value and are reported as assets where they have a positive fair value and liabilities where they have a negative fair value. Derivatives may be embedded in other financial instruments or contracts. Derivatives embedded in other financial instruments are valued as separate derivatives when their economic characteristics and risks are not clearly and closely related to those of the host contract unless such contracts relate to normal course operations and qualify for the normal purchase and sale exemption in accordance with appropriate accounting standards.

***Accounting for joint ventures***

The Company's interest in a jointly controlled entity is accounted for under the equity method. Under the equity method, the investment in an associate is initially recognized at cost and the carrying amount is increased or decreased to recognize the investor's share of the profit or loss of the investee after the date of acquisition. The investor's share of the profit or loss of the investee is recognized in the investor's profit or loss. Distributions received from an investee reduce the carrying amount of the investment. At the date of transition, and on an ongoing basis, the Company evaluates for indicators of impairment of its investment in joint ventures. As of March 31, 2011, the Company has not identified any such indicators.

***Financial instruments***

The Company's financial instruments consist of cash and cash equivalents, accounts receivable and payable, an interest rate cap contract and debt. The Company does not enter into financial instruments for trading or speculative purposes. Financial assets are classified as available-for-sale, held-to-maturity, loans and receivables. Initially, all financial assets and financial liabilities must be recorded on the consolidated of financial position at fair value. Subsequent measurement is determined by the classification of each financial asset and financial liability. At each reporting date, the Company assesses whether there is objective evidence that a financial asset is impaired. Impairment losses on financial assets carried at amortized cost are reversed in subsequent periods if the amount of the loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized.

***Accounts receivable***

Trade receivables are stated at fair value as reduced by appropriate allowances for estimated losses. Estimates for doubtful accounts are provided for as necessary based on the aging category and specific knowledge of the customer's ability to pay.

***Accounts payable***

Trade payables are obligations to pay for goods or services that have been acquired in the ordinary course of business from suppliers. Accounts payable are recorded at fair value and are classified as current liabilities if payment is due within one year or less. If not, they are presented as non-current liabilities.

***Leasing – lessor activities***

The Company has certain tolling and operation and maintenance agreements with its customers that are deemed to qualify as leases. The terms of the agreements do not transfer the risks and rewards of ownership and are therefore classified as operating leases. The Company records the fixed payments from these agreements as revenue on a straight-line basis over the term of the relevant lease.

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee.

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**NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS**  
*(In thousands of U.S. dollars unless specified, except share and per share amounts)*  
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**Common Stock**

Outstanding common shares of the Company (“Common Shares”) are classified as equity.

**Income (loss) per share**

Basic income (loss) per Common Share is computed by dividing net income (loss) available to owners of the Company by the weighted average number of Common Shares outstanding. Diluted income (loss) per share is computed by dividing net income (loss) available to owners of the Company by the weighted average number of Common Shares outstanding adjusted to include the potentially dilutive effect of outstanding stock options, if not anti-dilutive. Potential Common Shares are calculated using the treasury stock method and represent incremental shares issuable upon exercise of the Company’s outstanding stock options.

**Stock-based compensation**

The Company accounts for stock-based compensation using a fair value based method with respect to all stock-based awards. The fair value of options granted is determined at the date of grant using the Black-Scholes option pricing model. Compensation expense is recorded over the vesting period or immediately upon grant when options vest immediately.

**New accounting standards issued but not yet effective**

Certain new accounting standards and IFRS Interpretation Committee (IFRIC) interpretations have been published that are mandatory for accounting periods beginning on or after January 1, 2011. The Company’s assessment of the impact of these new standards and interpretations is set out below.

IFRS 7, *Financial Instruments – Disclosures* (IFRS 7), has been amended and will be effective for financial periods beginning on or after July 1, 2011. The amendments increase the disclosure requirements for transactions involving transfers of financial assets, for example using receivables, investments or equity to settle transactions. These amendments are intended to provide greater transparency around risk exposures of transactions when a financial asset is transferred and the transferor retains some level of continuing exposure in the asset. The amendments also require disclosures where transfers of financial assets are not evenly distributed throughout the period. It is not anticipated that these amendments to IFRS 7 will have a significant effect on the Company’s disclosures as it is the Company’s practice to settle transactions in cash. However, if the Company enters into other types of transfers of financial assets in the future, disclosure regarding those transfers may be affected.

IFRS 9, *Financial Instruments* (IFRS 9), was issued by the IASB on November 12, 2009 and will replace IAS 39, *Financial Instruments: Recognition and Measurement*. IFRS 9 is effective for annual periods beginning on or after January 1, 2013. The Company is currently evaluating the impact of IFRS 9; however it is not expected to have a material effect on the consolidated financial statements of the Company.

IAS 12, *Income Taxes*, has been amended and will be effective for financial periods beginning on or after January 1, 2012. The amendments to IAS 12 are not expected to affect the Company’s consolidated financial statements.

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*(In thousands of U.S. dollars unless specified, except share and per share amounts)*  
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**4. Transition to IFRS**

***Basis of transition to IFRS – application of IFRS***

These interim consolidated financial statements for the period ended March 31, 2011 are the Company's first financial statements prepared under IFRS. For all accounting periods prior to this, the Company prepared its financial statements under Canadian GAAP. In accordance with IFRS 1-First time adoption of IFRS, certain disclosures related to the transition to IFRS are provided in this note and are prepared under IFRS as set out in Note 2.

The Company has applied IFRS 1 in preparing these interim consolidated financial statements. In preparing these interim consolidated financial statements, the Company has applied the mandatory exceptions and elected certain of the optional exemptions from full retrospective application of IFRS as allowed under IFRS 1.

The Company has taken the following exemptions:

*Business combinations*

In accordance with IFRS transitional provisions, the Company elected to apply IFRS related to business combinations prospectively from January 1, 2010. As such, Canadian GAAP balances relating to business combinations entered into before that date have been carried forward without adjustment.

The following table provides a reconciliation of equity and comprehensive income as previously reported under Canadian GAAP to IFRS:

	<u>Note</u>	<u>December 31, 2010</u>	<u>March 31, 2010</u>	<u>January 1, 2010</u>
Equity as reported under Canadian GAAP		\$ 170,730	\$ 153,349	\$ 154,044
IFRS adjustments increase (decrease):				
Restatement of property, plant and equipment to reflect impact of IFRS requirements	a	(338)	(603)	(456)
Impact of IFRS conversion on long-term incentive compensation	h	(35)	-	-
Impact of recognizing deferred tax in accordance with IAS 12	c	(399)	221	170
Pro-rata allocation of IFRS adjustments to non-controlling interest	d	53	86	65
Reclassification of non-controlling interests	d	<u>82,028</u>	<u>84,942</u>	<u>85,860</u>
Total equity under IFRS		<u>\$ 252,039</u>	<u>\$ 237,995</u>	<u>\$ 239,683</u>

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The following table provides a reconciliation of the Consolidated Statement of Financial Position as previously reported under Canadian GAAP to IFRS:

	Note	December 31, 2010			March 31, 2010			January 1, 2010		
		Cdn		IFRS	Cdn		IFRS	Cdn		IFRS
		GAAP	Adjustment		GAAP	Adjustment		GAAP	Adjustment	
<b>ASSETS</b>										
<b>Current assets</b>										
Cash and cash equivalents	b	\$ 22,467	\$ (62)	\$ 22,405	\$ 22,981	\$ (103)	\$ 22,878	\$ 24,536	\$ (246)	\$ 24,290
Accounts receivable	b	9,330	(1,494)	7,836	9,434	(1,831)	7,603	9,532	(1,928)	7,604
Inventory, net		1,005	-	1,005	955	-	955	991	-	991
Current portion of future tax asset	c	745	(745)	-	1,027	(1,027)	-	1,003	(1,003)	-
Other current assets	b	1,243	-	1,243	561	(46)	515	833	-	833
		<u>34,790</u>	<u>(2,301)</u>	<u>32,489</u>	<u>34,958</u>	<u>(3,007)</u>	<u>31,951</u>	<u>36,895</u>	<u>(3,177)</u>	<u>33,718</u>
<b>Non-current assets</b>										
Property, plant and equipment, net	a,b	209,935	(29,432)	180,503	216,988	(30,853)	186,135	219,377	(31,091)	188,286
Intangible assets, net	b	76,754	(36,588)	40,166	94,912	(38,459)	56,453	100,964	(39,083)	61,881
Restricted cash		2,991	-	2,991	3,729	-	3,729	3,729	-	3,729
Long-term portion of interest rate swap contracts		4	-	4	39	-	39	186	-	186
Non-current deferred tax asset, net	c	4,595	346	4,941	-	-	-	-	-	-
Investment in joint venture	b	-	66,721	66,721	-	70,093	70,093	-	71,329	71,329
Other non-current assets		-	-	-	21	-	21	34	-	34
<b>Total assets</b>		<u>\$ 329,069</u>	<u>\$ (1,254)</u>	<u>\$ 327,815</u>	<u>\$ 350,647</u>	<u>\$ (2,226)</u>	<u>\$ 348,421</u>	<u>\$ 361,185</u>	<u>\$ (2,022)</u>	<u>\$ 359,163</u>
<b>LIABILITIES</b>										
<b>Current liabilities</b>										
Accounts payable		\$ 361	\$ -	\$ 361	\$ 236	\$ -	\$ 236	\$ 253	\$ -	\$ 253
Short-term debt	g	32,672	(2,329)	30,343	34,763	(3,451)	31,312	28,341	(3,890)	24,451
Due to affiliates	h	804	35	839	47	-	47	478	-	478
Accrued property taxes	b	2,083	(118)	1,965	3,044	(197)	2,847	2,520	(164)	2,356
Accrued expenses	b	2,467	(399)	2,068	2,310	(399)	1,911	2,631	(399)	2,232
		<u>38,187</u>	<u>(2,811)</u>	<u>35,376</u>	<u>40,400</u>	<u>(4,047)</u>	<u>36,353</u>	<u>34,223</u>	<u>(4,453)</u>	<u>29,770</u>
<b>Non-current liabilities</b>										
Long-term debt	g	35,467	2,329	37,796	54,343	3,451	57,794	69,887	3,890	73,777
Net long-term portion of future tax liability	c	-	-	-	15,057	(1,248)	13,809	14,680	(1,173)	13,507
Asset retirement obligations		2,604	-	2,604	2,470	-	2,470	2,426	-	2,426
<b>Total liabilities</b>		<u>76,258</u>	<u>(482)</u>	<u>75,776</u>	<u>112,270</u>	<u>(1,844)</u>	<u>110,426</u>	<u>121,216</u>	<u>(1,736)</u>	<u>119,480</u>
<b>Non-controlling interests</b>	d	82,081	(82,081)	-	85,028	(85,028)	-	85,925	(85,925)	-
<b>EQUITY</b>										
Common stock		274,479	-	274,479	274,479	-	274,479	274,479	-	274,479
Contributed surplus		3,316	-	3,316	-	-	-	-	-	-
Accumulated shareholders' deficit	i	(107,065)	(719)	(107,784)	(121,130)	(296)	(121,426)	(120,435)	(221)	(120,656)
Non-controlling interest	d	-	82,028	82,028	-	84,942	84,942	-	85,860	85,860
<b>Total equity</b>		<u>170,730</u>	<u>81,309</u>	<u>252,039</u>	<u>153,349</u>	<u>84,646</u>	<u>237,995</u>	<u>154,044</u>	<u>85,639</u>	<u>239,683</u>
<b>Total liabilities &amp; equity</b>		<u>\$ 329,069</u>	<u>\$ (1,254)</u>	<u>\$ 327,815</u>	<u>\$ 350,647</u>	<u>\$ (2,226)</u>	<u>\$ 348,421</u>	<u>\$ 361,185</u>	<u>\$ (2,022)</u>	<u>\$ 359,163</u>

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The following table provides a reconciliation of the Consolidated Statement of Comprehensive Income for the Year Ended December 31, 2010 and for the three months ended March 31, 2010 as previously reported under Canadian GAAP to IFRS:

	Note	Year ended December 31, 2010			Three months ended March 31, 2010		
		Cdn		IFRS	Cdn		IFRS
		GAAP	Adj		GAAP	Adj	
<b>Revenue</b>							
Capacity		\$ 36,071	\$ -	\$ 36,071	\$ 9,018	\$ -	\$ 9,018
Energy Service	b	25,164	(8,452)	16,712	6,323	(2,081)	4,242
		61,235	(8,452)	52,783	15,341	(2,081)	13,260
<b>Expenses</b>							
Operations and maintenance	a,b,f,h	13,968	(2,256)	11,712	2,625	(568)	2,057
General and administrative	b,e,f,h	10,088	(1,220)	8,868	2,604	(280)	2,324
Non-cash stock based compensation	f	3,316	(3,316)	-	-	-	-
Employee benefits expense	f	-	5,421	5,421	-	566	566
Depreciation and amortization	a,b	33,712	(3,443)	30,269	8,428	(862)	7,566
<b>Total operating expenses</b>		61,084	(4,814)	56,270	13,657	(1,144)	12,513
<b>Equity in earnings of joint venture</b>	b	-	3,899	3,899	-	835	835
<b>Operating income</b>		151	261	412	1,684	(102)	1,582
<b>Other (expense) income</b>							
Interest expense, net	e	(9,618)	(178)	(9,796)	(2,763)	(45)	(2,808)
Realized and unrealized loss on derivative hedge contracts		(182)	-	(182)	(147)	-	(147)
<b>Loss before income taxes and non-controlling interest</b>		(9,649)	83	(9,566)	(1,226)	(147)	(1,373)
Income tax benefit (expense)	c	19,175	(569)	18,606	(366)	51	(315)
<b>Income (loss) before non-controlling interest</b>		9,526	(486)	9,040	(1,592)	(96)	(1,688)
Non-controlling interest	d	3,844	(3,844)	-	897	(897)	-
<b>Net income (loss) and comprehensive income (loss)</b>		\$ 13,370	\$ (4,330)	\$ 9,040	\$ (695)	\$ (993)	\$ (1,688)
<b>Net income (loss) and comprehensive income (loss) attributable to:</b>							
Owners of the Company		\$ -	\$ -	\$ 12,872	\$ -	\$ -	\$ (770)
Non-controlling interest		-	-	(3,832)	-	-	(918)
		\$ -	\$ -	\$ 9,040	\$ -	\$ -	\$ (1,688)

Explanation of the effect of the transition to IFRS:

The following explains the material adjustments to the consolidated statement of financial position and consolidated statement of comprehensive income as a result of the transition to IFRS.

*(a) Property, plant and equipment*

Under IFRS, capitalization is required for significant parts of an item of property, plant and equipment (including major inspections and overhaul expenditures) having significant cost and a useful life and/or depreciation method for the respective component that is different from the remainder of the asset. All significant components that have the same useful life and depreciation method have been grouped together and depreciated to their residual values over their useful lives.

IFRS requires that major overhaul and inspection costs be capitalized and depreciated to expense (and the replaced element derecognized). Previously, these costs were expensed under Canadian GAAP.

The Company's transition adjustment resulted in a \$0.5 million net decrease in property, plant and equipment at the transition date, January 1, 2010, and a corresponding decrease in equity of \$0.5 million. These adjustments have been reflected on the January 1, 2010 opening statement of financial position. Under IFRS accounting methods for property, plant and equipment,

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depreciation expense for the Company for the year ended December 31, 2010 and three months ended March 31, 2010 decrease by \$0.6 million and \$0.2 million, respectively. There were also corresponding decreases in equity as of December 31, 2010 and March 31, 2010. In addition, during 2010 the Company capitalized \$0.7 million of previously expensed overhaul costs. See investment in joint venture (b) for additional depreciation adjustments for the respective periods.

*(b) Investment in joint venture*

The Company's investment in PCI Associates (a joint venture) was previously accounted for under the proportionate consolidation accounting method. Since the transition to IFRS, this investment is accounted for under the equity method. Under the proportionate consolidation accounting method, the financial position and comprehensive income line items of the joint venture are consolidated into the same line items of the Company. Under the equity method, the respective financial position amounts of the joint venture are netted into one total and reported as a net investment ("Investment in Joint Venture") in the long term assets section of the consolidated statement of financial position. The consolidated statement of comprehensive income activity is also netted into a single total and is reported as "Equity in Earnings of Joint Venture" above the operating income (loss) line.

The reconciliation of the proportionate consolidation method of accounting to the equity method for the Company's investment in PCI Associates is as follows:

	<u>December 31, 2010</u>	<u>March 31, 2010</u>	<u>January 1, 2010</u>
Cash and cash equivalents	\$ 62	\$ 103	\$ 246
Accounts receivable	1,494	1,831	1,928
Other current assets	-	46	-
Property, plant and equipment	29,094	30,250	30,635
Intangible assets, net	36,588	38,459	39,083
Accrued expenses	(517)	(596)	(563)
Investment in joint venture	<u>\$ 66,721</u>	<u>\$ 70,093</u>	<u>\$ 71,329</u>

  

	<u>Year Ended December 31, 2010</u>	<u>Three Months Ended March 31, 2010</u>
Tolling Revenue	\$ 8,452	\$ 2,081
Operations and maintenance expense	(370)	(189)
Real estate and personal property tax	(74)	(33)
Insurance expense	(61)	(15)
Professional fees	(12)	-
Depreciation and amortization	(4,036)	(1,009)
Net income	<u>\$ 3,899</u>	<u>\$ 835</u>

*(c) Deferred tax assets (liabilities) classification under IFRS*

Under IFRS, deferred income tax balances are required to be classified as non-current. Accordingly, current deferred income tax reported under Canadian GAAP of \$1.0 million at January 1, 2010 (\$1.0 million at March 31, 2010 and \$0.7 million at December 31, 2010, respectively) has been reclassified as non-current under IFRS.

Additionally, the tax impact of other IFRS transition adjustments resulted in a cumulative change to deferred taxes of \$0.2 million in the consolidated statement of financial position as of the January 1, 2010 transition date, and a \$0.6 million tax expense impact and a \$0.05 million tax benefit impact in the consolidated statement of comprehensive income for the year ended December 31, 2010 and three months ended March 31, 2010, respectively.

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*(d) Non-controlling interest*

IAS 27 - *Consolidated and Separate Financial Statements* requires that non-controlling interests' share of the net assets of subsidiaries is included in equity and their share of the comprehensive income of subsidiaries is allocated directly to equity. Under Canadian GAAP, non-controlling interests were presented as a separate item between liabilities and equity in the statement of financial position and the non-controlling interests' share of income and other comprehensive income were deducted in calculating net income and comprehensive income of the entity. Non-controlling interest of \$85.9 million at January 1, 2010, \$85.0 million at March 31, 2010 and \$82.1 million at December 31, 2010, as determined under Canadian GAAP has been reclassified to equity.

IFRS adjustments of \$0.06 million have been allocated to the non-controlling interests as of January 1, 2010. Additionally, the consolidated statement of comprehensive income reflects an allocation of IFRS adjustments to the non-controlling interest for the year ended December 31, 2010 and the three months ended March 31, 2010 totaling \$0.01 million and \$0.02 million, respectively.

*(e) Asset Retirement Obligations*

Where discounting of Asset Retirement Obligations is used, the carrying amount of a provision increases in each period to reflect the passage of time. IFRS requires that this increase be recognized as borrowing cost and recorded as interest expense in the consolidated statement of comprehensive income. The Company previously recorded accretion of the liability as a general and administrative cost. In accordance with IFRS, \$0.2 million and \$0.04 million has been reclassified from general and administrative expenses to interest expense in the consolidated statement of comprehensive income for the year ended December 31, 2010 and the three months ended March 31, 2010, respectively.

*(f) Employee benefit expense*

Expenses totaling \$5.4 million and \$0.6 million for the year ended December 31, 2010 and the three months ended March 31, 2010, respectively, have been separately stated representing employee benefit expenses for the respective periods. For the year ended December 31, 2010, the following costs have been reclassified representing employee benefit expenses: \$1.2 million of operations and maintenance expenses, \$0.9 million of general and administrative expenses and \$3.3 million of non-cash stock based compensation. For the three month period ended March 31, 2010, the following costs have been reclassified representing employee benefit expenses: \$0.4 million of operations and maintenance expenses and \$0.2 million of general and administrative expenses.

*(g) Debt*

For all periods presented, the balances of long term debt and short term debt have been adjusted to reclassify the portion of deferred financing fees that are deemed to be short term in nature.

*(h) Long-term incentive compensation*

Long-term incentive compensation has been adjusted by \$0.04 million to reflect IFRS accounting adjustments at December 31, 2010 in the consolidated statement of financial position and for the year ended December 31, 2010 in the consolidated statement of comprehensive income.

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*(i) Accumulated shareholders deficit*

The following is a summary of transition adjustments to the Company's accumulated shareholders' deficit from Canadian GAAP to IFRS:

	<u>Note</u>	<u>December 31, 2010</u>	<u>March 31, 2010</u>	<u>January 1, 2010</u>
Accumulated shareholders' deficit as reported under Canadian GAAP		\$ (107,065)	\$ (121,130)	\$ (120,435)
IFRS adjustments increase (decrease):				
Restatement of property, plant and equipment to reflect impact of IFRS requirements	a	(338)	(603)	(456)
Impact of IFRS conversion on long-term incentive compensation	h	(35)	-	-
Impact of recognizing deferred tax in accordance with IAS 12	c	(399)	221	170
Pro-rata allocation of IFRS adjustments to non-controlling interest	d	53	86	65
Accumulated shareholders' deficit under IFRS		<u>\$ (107,784)</u>	<u>\$ (121,426)</u>	<u>\$ (120,656)</u>

***Adjustments to the statements of cash flows***

The transition from Canadian GAAP to IFRS resulted in a change in total operating cash flows and to total cash as a result of the change in accounting for the PCI Associates joint venture for the comparative periods ended March 31, 2011 and 2010 as discussed in (b) investment in joint venture. In addition, operating cashflows for year ended December 31, 2010, were impacted by the capitalization of previously expensed overhaul costs which were reflected as capital expenditures in investing cash flows for the same period. There was no impact on cash used in financing activities.

**5. Financial risk management**

*Financial risk factors*

The Company's activities expose it to a variety of financial risks: market risk (interest rate risk), credit risk, liquidity risk and capital risk. The Company's overall risk management program focuses on the unpredictability of financial markets and seeks to minimize potential adverse effects on the Company's financial performance. The Company uses derivative financial instruments to hedge certain risk exposures.

Risk management is carried out by management under policies approved by the board of directors. The audit committee evaluates and manages financial risks in close co-operation with the Company's management.

*Market risk*

The Company is subject to interest rate risks for debt that has variable interest rates. In conjunction with the November 13, 2009 debt refinancing, the Company entered into an interest rate cap transaction under the terms of the Credit Facility such that the borrowing rate is capped at rates increasing from 2.25% currently in effect to 5.00% during the last year of the three-year term of the interest rate cap. The notional amount of the interest rate cap declines over the term of the Credit Facility to correspond with the anticipated reduction in the amount of debt outstanding. The fair value of the interest rate cap at March 31, 2011 and December 31, 2010 was a de minimis amount.

*Credit risk*

The Company's financial assets that are exposed to credit risk consist primarily of cash and cash equivalents and accounts receivable. The Company, in its normal course of business, is exposed to credit risk from its customers. Risks associated with concentrations of credit risk with respect to accounts receivable are based on the credit rating of customers and the generally short payment terms.

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*Liquidity risk*

Management measures liquidity risk through its review of current financial ratios against financial covenants contained in its debt agreements to determine if there are appropriate actions that can be employed to mitigate liquidity issues. As discussed in Note 8, the Credit Facility matures on October 23, 2014.

*Capital risk*

The capital of the Company is comprised of debt and common stock. The capital requirements of the Company are evaluated on an ongoing basis to determine what is required to support the Company's financial objectives and strategic plan. The Company carries an amount of cash on hand that is reflective of working capital requirements and the principal and interest payment obligations under its Credit Facility. The objectives for managing capital are to safeguard the Company's ability to operate as a going concern and to provide a return to shareholders.

The Company's debt balances are subject to certain financial covenant ratios at a subsidiary level. The level of equity and debt maintained by the Company has also been determined based on the Company's evaluation of existing and future operational results and the future plans for the Company. The Company's capital structure is monitored in relation to economic conditions and the risk characteristics of the Company's assets. In order to maintain or adjust the capital structure, the Company may issue new Common Shares, obtain new or additional debt financing or sell assets to pay down debt. Management expects that any significant acquisition or development opportunities would most likely be financed by a combination of debt and equity.

*Fair value estimation*

The carrying values of cash and cash equivalents, trade and other receivables, trade and other payables and other liabilities approximate their respective fair values due to their short maturity. The fair value of bank debt approximates carrying value as the debt has a floating interest rate.

**6. Property, plant and equipment**

Property, plant and equipment consist of the following:

	<b>Buildings</b>	<b>Plant machinery &amp; equipment</b>	<b>Total</b>
<b>Cost</b>			
at January 1, 2010	\$ 21,746	\$ 204,589	\$ 226,335
Additions (Disposals)	-	769	769
at December 31, 2010	\$ 21,746	\$ 205,358	\$ 227,104
Additions (Disposals)	-	865	865
at March 31, 2011	<u>\$ 21,746</u>	<u>\$ 206,223</u>	<u>\$ 227,969</u>
<b>Accumulated depreciation</b>			
at January 1, 2010	\$ (2,940)	\$ (35,109)	\$ (38,049)
Charges for the period	(1,204)	(7,348)	(8,552)
at December 31, 2010	\$ (4,144)	\$ (42,457)	\$ (46,601)
Charges for the period	(188)	(1,442)	(1,630)
at March 31, 2011	<u>\$ (4,332)</u>	<u>\$ (43,899)</u>	<u>\$ (48,231)</u>

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	Plant machinery & equipment		Total
	Buildings		
<b>Net book value</b>			
At January 1, 2010	\$ 18,806	\$ 169,480	\$ 188,286
At December 31, 2010	<u>\$ 17,602</u>	<u>\$ 162,901</u>	<u>\$ 180,503</u>
At March 31, 2011	<u>\$ 17,414</u>	<u>\$ 162,324</u>	<u>\$ 179,738</u>

For each of the three months ending March 31, 2011 and 2010, the Company recognized depreciation expense of \$2.1 million. During the first quarter of 2011, the Company completed an overhaul at North Lake. The associated costs have been capitalized in property plant and equipment and will be depreciated over an estimated time period coinciding with the next scheduled overhaul. The Company had previously capitalized related overhaul costs of \$1.0 million. The undepreciated balance of \$0.5 million existing at March 31, 2011 was written off as a loss on derecognition in the consolidated statement of comprehensive income for the quarter ended March 31, 2011, as the future economic benefits associated with the prior overhaul can no longer be realized.

#### 7. Intangible assets

	Contract Values	Accumulated Amortization	Net Book Value
at January 1, 2010	\$ 157,822	\$ (95,941)	\$ 61,881
Amortization charges	-	(21,715)	(21,715)
at December 31, 2010	<u>\$ 157,822</u>	<u>\$ (117,656)</u>	<u>\$ 40,166</u>
Amortization charges	-	(5,429)	(5,429)
at March 31, 2011	<u>\$ 157,822</u>	<u>\$ (123,085)</u>	<u>\$ 34,737</u>

Contract rights represent the value assigned to existing customer contracts at the date of the acquisition and are amortized on a straight line basis over a weighted average term of eight years. For each of the three months ending March 31, 2011 and 2010, the Company recorded contract value amortization of \$5.4 million.

#### 8. Debt

Long-term debt consists of the following:

	March 31, 2011	December 31, 2010	January 1, 2010
Credit Facility	\$ 64,135	\$ 71,366	\$ 105,000
Deferred finance fees	(2,631)	(3,227)	(6,772)
Less:			
Reclassification of debt outstanding under the Credit Facility to short-term debt	(34,474)	(32,672)	(28,341)
Reclassification of deferred finance fees to short-term debt	1,998	2,329	3,890
Total long-term debt	<u>\$ 29,028</u>	<u>\$ 37,796</u>	<u>\$ 73,777</u>

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Maturities of debt are based upon quarterly mandatory payments and projections of excess cashflow, which are subject to change based on results of operations and other factors. The estimated principal payments are as follows:

	March 31, 2011	December 31, 2010	January 1, 2010
2010 .....	\$ -	\$ -	\$ 28,341
2011 .....	24,666	32,672	38,547
2012 .....	36,208	38,694	38,112
2013 .....	3,261	-	-
Total .....	<u>\$ 64,135</u>	<u>\$ 71,366</u>	<u>\$ 105,000</u>

*Credit facility*

On October 23, 2009, PERH, through its subsidiary Primary Energy Operations LLC ("PEO"), entered into a \$105.0 million secured term loan facility (the "Credit Facility"). On November 13, 2009, the Company borrowed \$105.0 million available under the Credit Facility. The net proceeds of the Credit Facility together with a portion of the proceeds from the Company's rights offering were applied to fully retire the \$131.0 million outstanding under its then existing credit facility.

The Credit Facility has a five-year term and accrues interest at an interest rate equal to, at PEO's option, an adjusted LIBOR rate (subject to a 2.0% minimum) plus 4.5% or an alternate base rate (subject to a 3.0% minimum) plus 3.5%. The loan is subject to 0.25% quarterly mandatory amortization payments and quarterly prepayments of principal equal to 100% of PEO's excess cash flow (as defined in the Credit Facility) for the period. The Company has classified approximately \$34.5 million of borrowings under the Credit Facility as short-term debt at March 31, 2011. This amount represents approximately \$0.5 million of required principal repayments and approximately \$34.0 million of estimated principal prepayments based upon anticipated excess cash flows (as defined in the Credit Facility). The debt outstanding under the Credit Facility is guaranteed by PERH and PEO's wholly-owned subsidiaries (collectively, the "Guarantors") and secured by a pledge of substantially all of PEO's and the Guarantors' real and personal property. The Credit Facility also contains financial covenants requiring PEO to meet certain maximum leverage and minimum fixed charge coverage ratios, as well as other covenants. These covenants may limit the Company's ability to, among other things, incur additional secured or unsecured debt, pay dividends, make acquisitions or other investments, make capital expenditures, sell or otherwise dispose of certain assets, enter into sale and leaseback transactions and enter into mergers or consolidations. The cost of borrowing (including fees) for the Company is approximately 6.9% based on current LIBOR. As of March 31, 2011, the Company was in compliance with its debt covenants under the Credit Facility.

*Deferred financing fees*

The Company capitalizes costs associated with the issuance of debt instruments. These costs are being amortized to interest expense over the estimated term of the debt using the effective interest method. Financing costs totaling \$7.4 million associated with debt issued on November 13, 2009 under the Credit Facility have been capitalized and are being amortized over the term of the Credit Facility using the effective interest method, which reflects anticipated debt repayment activity. For the three months ended March 31, 2011 and 2010, the Company amortized \$0.6 million and \$1.1 million, respectively, of deferred financing fees.

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**9. Interest expense**

Interest expense for the three months ending March 31, 2011 and 2010 is comprised of the following:

	Three Months Ended March 31,	
	2011	2010
Interest expense:		
Credit Facility	\$ 1,153	\$ 1,700
Amortization of deferred financing fees	642	1,063
Accretion of asset retirement obligations	48	45
Interest expense	<u>\$ 1,843</u>	<u>\$ 2,808</u>

**10. Asset retirement obligations**

Certain of the Company's subsidiaries have contractual obligations to remove all buildings and equipment associated with the ground leases related to their facilities. The Company initially estimated these liabilities based upon an independent valuation. Management has evaluated the methods and assumptions used to measure the fair value of recorded obligations and determined that they are reasonable as of March 31, 2011. The total undiscounted cash flows required to satisfy the legal obligations are estimated to be \$13.2 million and are expected to be incurred in 2033. These amounts were discounted by a risk-adjusted borrowing rate of 7.32%. For the three months ended March 31, 2011 and 2010, the Company recognized accretion expense of \$0.05 million and \$0.05 million, respectively, and depreciation expense of \$0.01 million and \$0.01 million, respectively. As of March 31, 2011, December 31, 2010 and January 1, 2010, the balance of the asset retirement obligation liability was \$2.7 million, \$2.6 million and \$2.4 million, respectively, and the balance of the related asset was \$0.5 million, \$0.5 million and \$0.5 million, respectively.

**11. Commitments and contingencies**

*Environmental Matters*

The Company's operations are subject to a number of federal, state and local laws and regulations relating to the protection of the environment and the safety and health of personnel and the public. Some of the Company's operations require environmental permits and controls to prevent and reduce air and water pollution, and these permits are subject to modification, renewal and revocation by issuing authorities. These requirements relate to a broad range of activities, including:

- discharge of pollutants into the air, water and soil;
- identification, generation, storage, handling, transportation, disposal, record keeping, labeling and reporting of, and the emergency response in connection with, hazardous and toxic materials and wastes including asbestos;
- safety and health standards, practices and procedures that apply to the workplace and the operation of facilities; and
- appropriate hazard assessment with associated emergency preparedness and response capabilities.

In June of 2010, the Company's Cokenergy facility received a Notice of Violation and Finding of Violation ("NOV/FOV") from the United States Environmental Protection Agency ("USEPA") contending violations of its Title V permit under the Clean Air Act. The Title V permit outlines,

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among other things, emission limits and reporting requirements for sulfur dioxide (“SO<sub>2</sub>”) and opacity. The NOV/FOV alleges that Cokenergy has exceeded limits set under its Title V permit for SO<sub>2</sub> emissions and opacity at certain times. The Company has evaluated the USEPA’s allegations and found substantially all of them to be malfunctions or emergency occurrences that were also reported and resolved under an agreed order with the Indiana Department of Environmental Management in September 2008. The Company has met with the USEPA and presented supporting compliance information. The Company, at the USEPA’s request, subsequently prepared and submitted further documentation supporting its position, and is awaiting their response. While management does not anticipate that this matter will have a significant adverse impact to the Company, the ultimate outcome cannot be predicted.

**12. Non-controlling interest**

CPI USA Holdings LLC, a wholly-owned subsidiary of CPI USA Ventures LLC (the “Manager”) holds 22,388,491 common membership interests, or approximately 14.3%, of PERH and the Company holds 134,118,561 common membership interests, or approximately 85.7%, of PERH. With the exception of special distributions from PERH to the Company to fund certain ongoing public company and corporate expenses and costs, all holders of common membership interests of PERH are entitled to receive distributions on a pro rata basis when and if declared by the board of managers of PERH. Each common membership interest of PERH is entitled to one vote.

**13. Common stock**

As of May 10, 2011, a total of 134,118,561 Common Shares of the Company were issued and outstanding. Each Common Share is entitled to one vote. In addition, options to purchase 5.5 million Common Shares are outstanding. (See note 21)

**14. Basic and diluted net loss per share attributable to owners of the Company**

Basic net loss per share is computed by dividing the net loss for the period attributable to the owners of the Company by the weighted average number of Common Shares outstanding during the period. Diluted net loss per share is computed by dividing the net loss for the period, by the weighted average number of Common Shares outstanding and, when dilutive, adjusted for the effect of all potentially dilutive shares, including stock options, on an as-if-converted basis.

The following table sets forth the computation for basic and diluted net loss per share:

	Three Months Ended March 31,	
	2011	2010
<b>Numerator:</b>		
Basic and diluted net loss	\$ (1,281)	\$ (770)
<b>Denominator:</b>		
Denominator for basic and diluted - weighted average number of Common Shares outstanding	134,118,561	134,118,561
<b>Basic and diluted loss per share:</b>		
Basic and diluted net loss per share	\$ (0.01)	\$ (0.01)

Options to purchase 5.5 million Common Shares were outstanding for the period ending March 31, 2011. For the three months ended March 31, 2011 and 2010, there were no differences in the weighted average number of Common Shares outstanding used for basic and diluted net loss per share as the effect of all potentially dilutive Common Shares outstanding was anti-dilutive.

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**15. Income tax**

Income tax expense is recognized based on management's best estimate of the weighted average annual income tax rate expected for the full financial year. The estimated average annual rate (federal and state) used for each of the three months ended March 31, 2011 and March 31, 2010 was 40.5%.

Income tax expense consists of the following:

	Three Months Ended March 31,	
	2011	2010
<b>Current tax provision:</b>		
Federal	\$ 2	\$ 13
State	-	-
Total current tax	<u>2</u>	<u>13</u>
<b>Deferred tax provision:</b>		
Federal	403	239
State	107	63
Total deferred tax	<u>510</u>	<u>302</u>
Total tax expense	<u>\$ 512</u>	<u>\$ 315</u>

The principal items which cause the Company's effective tax rate to be different than the Canadian statutory tax rate of 28.5% for 2011 and 31.0% for 2010 are the effect of the inclusion of the U.S. federal and state income taxes that are greater than the Canadian statutory tax rate and the change in the valuation allowance on the net operating loss. These items are summarized as follows:

	Three Months Ended March 31,	
	2011	2010
Income tax at		
Canadian statutory rate:	\$ 312	\$ 456
Additional tax from		
operations in countries with		
different income tax rates	131	121
Valuation allowance	-	(262)
Other	69	-
Total tax expense	<u>\$ 512</u>	<u>\$ 315</u>

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Significant components of the deferred tax assets and (liabilities) are as follows:

	<u>As of March 31, 2011</u>	<u>As of December 31, 2010</u>	<u>As of January 1, 2010</u>
<b>Deferred tax assets</b>			
Accrued expenses	\$ 881	\$ 745	\$ 1,003
Asset retirement obligation	920	904	1,266
Intangible assets	10,409	9,886	7,983
Stock-based compensation	715	784	-
Tax credit carryforwards	13	11	168
Other	354	352	272
Net operating loss	19,743	19,792	20,288
Valuation allowance	-	-	(20,288)
<b>Total deferred tax assets</b>	<u>33,035</u>	<u>32,474</u>	<u>10,692</u>
<b>Deferred tax liabilities</b>			
Property, plant and equipment	(22,287)	(21,372)	(19,254)
Investment in PCI Associates	(6,316)	(6,161)	(4,945)
<b>Total deferred tax liabilities</b>	<u>(28,603)</u>	<u>(27,533)</u>	<u>(24,199)</u>
<b>Net deferred tax asset (liability)</b>	<u>\$ 4,432</u>	<u>\$ 4,941</u>	<u>\$ (13,507)</u>

As of March 31, 2011, the Company has a U.S. net operating loss carryforward of approximately \$48.7 million that will start to expire in 2026. As of December 31, 2010 the Company released the valuation allowance on its U.S. net operating losses as it is more likely than not that the tax benefit of the net operating loss carryforward will be utilized. The release of the valuation allowance was primarily based on the expectation of future taxable income due to the reduction in interest expense as a result of the Company's recapitalization in 2009. During 2010, the Company determined that \$32.6 million of income recognized on the cancellation of debt in 2009 is not taxable for U.S. purposes. Based on this determination, the Company recorded an additional net operating loss carryforward of \$32.6 million which has been fully reserved for as of March 31, 2011.

In addition, the Company has net operating losses of approximately Cdn\$47.0 million for Canadian tax purposes that will begin to expire in 2028. A full reserve has been placed against this asset as the Company does not anticipate realizing a benefit from these losses.

At March 31, 2011 and December 31, 2010, the net long-term deferred tax asset balance was \$4.4 million and \$4.9 million, respectively. At January 1, 2010, the net long-term deferred tax liability balance was \$13.5 million.

#### **16. Investment in joint venture**

The Company has an indirect ownership interest in a joint venture through PERH's wholly-owned subsidiary Harbor Coal LLC ("Harbor Coal"). Harbor Coal owns a 50% interest in PCI Associates, a partnership that operates a pulverized coal facility. The investment is accounted for using the equity method. The carrying value of Harbor Coal's interest in PCI Associates reflects a purchase price allocation to adjust the values ascribed to long-term assets to fair value as of the Company's initial public offering date of August 24, 2005. The excess purchase price allocated to property, plant and equipment and intangible assets has been recorded in the books of Harbor Coal. The consolidated financial statements for each of the three months ended March 31, 2011 and 2010 include \$0.8 million of related depreciation and amortization which is reflected in equity in earnings of joint venture. At March 31, 2011, December 31, 2010 and January 1, 2010, the Company's investment in joint venture was \$66.2 million, \$66.7 million and \$71.3 million, respectively.

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PCI Associates provides services to one customer. Under the agreement with this customer, except for certain defined shared expenses (property taxes, insurance and depreciation), operating expenses are assumed by the site host subject to specified thresholds. Operating expenses above the specified thresholds are shared ratably. On December 22, 2010, the PCI Associates partnership agreement was amended retroactively to October 1, 2010. Beginning on October 1, 2010, Harbor Coal's share of the revenue of PCI Associates, which is based on tons of coal consumed multiplied by a fixed rate per ton, was reduced by two dollars per ton. In exchange, all operation and maintenance expenses subsequent to July 1, 2010 were assumed by the site host.

For each of the three months ended March 31, 2011 and 2010, Harbor Coal's recorded share of PCI Associates, depreciation was \$0.2 million. For the three months ended March 31, 2010, Harbor Coal's share of excess operating expenses of PCI Associates was \$0.2 million.

The financial information for Harbor Coal's 50% share of PCI Associates is as follows:

	<u>March 31, 2011</u>	<u>December 31, 2010</u>	<u>March 31, 2010</u>	<u>January 1, 2010</u>
Current assets	\$ 2,065	\$ 1,556	\$ 1,980	\$ 2,174
Non-current assets	10,786	10,973	11,534	11,721
Current liabilities	541	518	596	563
Non-current liabilities	-	-	-	-

  

	<u>Three Months Ended March 31,</u>	
	<u>2011</u>	<u>2010</u>
Revenue	\$ 2,059	\$ 2,081
Operations and maintenance expenses	-	189
Property taxes, insurance and depreciation expenses	226	235
Net income	1,833	1,657
Cash flows provided by operating activities	\$ 1,507	\$ 1,928
Cash flows used in investing activities	-	-
Cash flows used in financing activities	(1,535)	(2,071)

## 17. Derivative instruments and hedging activities

The Company has historically utilized certain derivative instruments to enhance its ability to manage financial risk relating to interest rate exposure. Derivative instruments are entered into for periods consistent with the related underlying exposure.

On November 12, 2009 the Company entered into an interest rate cap transaction pursuant to provisions of the Credit Facility for \$0.3 million. The interest rate cap has a three-year term. The interest rate cap transaction establishes a series of quarterly interest rate caps with the notional amount of each quarterly cap based upon the amount of anticipated debt outstanding under the Credit Facility. The quarterly interest rates increase from the 2.25% currently in effect up to 5.00% during the last year of the three-year term of the interest rate cap. The notional amounts reduce over time based upon anticipated debt reductions. The contract does not qualify as a cash flow hedge for accounting purposes and the change in fair value is recorded in income. As of March 31, 2011 and December 31, 2010, the fair value of the interest rate cap was a de minimus amount. As of January 1, 2010, the fair value of the interest rate cap was \$0.2 million.

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**18. Related party transactions**

The Company has a management agreement in place with the Manager (the "Management Agreement") with an initial term ending in 2025. The Manager provides various accounting, tax, administrative and operational services to the Company and its subsidiaries under terms of the Management Agreement. Beginning on September 1, 2009, the annual management fee was set at \$3.0 million, subject to annual adjustment for inflation. For the three months ended March 31, 2011 and 2010, the Company recorded management fees of \$0.9 and \$0.7 million, respectively, in connection with the Management Agreement. In addition, there are certain costs that the Company manages. If the amount of these costs exceeds \$1.25 million, subject to annual adjustments for inflation, any excess costs are to be incurred by the Company.

As of March 31, 2011, December 31, 2010 and January 1, 2010, the Company had a net payable due to the Manager and its affiliates of \$0.6 million, \$0.6 million and \$0.5 million, respectively. The outstanding balances were subsequently settled.

**19. Compensation of key management**

Key management includes the company's directors and members of executive management. Compensation awarded to key management included:

	Three Months Ended March 31,		Year Ended
	2011	2010	December 31, 2010
Salaries and employee benefits	\$ 100	\$ 66	\$ 319
Director compensation	75	85	369
Share-based payments	-	-	3,316
Total compensation of key management	<u>\$ 175</u>	<u>\$ 151</u>	<u>\$ 4,004</u>

Under terms of the amended management agreement, compensation costs associated with certain dedicated employees of the Manager and the Company's CEO (along with certain other costs) are subject to reimbursement from the Manager up to an annual limit of \$1.25 million (adjusted annually for inflation). Amounts incurred in excess of the reimbursement threshold are the responsibility of the Company. The ratable share of estimated annual excess cost is accrued on a quarterly basis.

**20. Segment reporting**

The Company owns and operates facilities designed to recycle waste energy under one operating segment. The Company serves as a single source of supply for its customers' related requirements. The Company's operations are located in the United States. All sales revenue is generated from the same geographic area.

**21. Stock-based compensation**

On August 24, 2010, the Company established a stock option plan (the "Stock Option Plan") that was approved by the Company's shareholders on October 15, 2010. The plan is administered by the Company's Board of Directors which has the authority to determine: the number of options awarded (subject to the maximum allowed of 5.5 million); to whom the options are awarded; the exercise price and the term and vesting conditions of the options. Under the Stock Option Plan, options can only be granted to eligible officers and employees of the Company and each option provides the holder with the right to acquire one Common Share. The exercise price of an option may not be lower than the closing price of the Common Shares on the TSX on the trading day

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immediately preceding the date of the grant. The stock price at date of grant was Cdn\$0.94. The term of an option may not exceed 10 years from the date of the grant.

On August 24, 2010, the Board of Directors awarded a total of 5.5 million options to Mr. John Prunkl, the President and Chief Executive Officer of the Company, subject to approval of the Stock Option Plan by the Company's shareholders. All of the options granted to Mr. Prunkl vested immediately and are defined as incentive stock options for U.S. tax purposes. The exercise price of the first option to acquire 5.0 million Common Shares is Cdn\$1.00 with a fair value at the date of measurement of \$0.61. The exercise price of the second option to acquire 0.5 million Common Shares is Cdn\$1.20 with a fair value at the date of measurement of \$0.56. For the year ended December 31, 2010, the Company recognized a total of \$3.3 million in non-cash stock based compensation expense associated with the grants issued under the Stock Option Plan, based on the estimated fair value of the options on the grant date. At March 31, 2011 there were 5.5 million options currently exercisable with a weighted average exercise price of \$1.01. As of the grant date, the options had a weighted average fair value measurement of \$0.61. The fair value of the respective options was determined by the Black-Scholes option pricing model using the assumptions noted in the following table.

Stock price at date of fair value measurement	Cdn\$1.09
Volatility	40%
Risk-free rate	2.79%
Expected term (in years)	10
Dividend yield	0%

Annualized volatility was based upon volatility of comparable stocks with a longer trading history. As of March 31, 2011, all options available under the plan have been granted. Shareholder approval will be required to increase the number of Common Shares available under the plan.

**22. Employee benefits expense**

	Three Months Ended March 31,		Year Ended
	2011	2010	December 31, 2010
Salaries and employee benefits	\$ 409	\$ 429	\$ 1,381
Medical benefit expenses	34	25	106
Retirement benefit expenses	42	27	249
Director compensation	75	85	369
Share-based payments	-	-	3,316
<b>Employee benefits expense</b>	<b>\$ 560</b>	<b>\$ 566</b>	<b>\$ 5,421</b>

Under the terms of the Management Agreement, executive management functions of the Company are provided by certain employees of the Manager who are solely dedicated to the Company's activities and who report to the President and Chief Executive Officer. The associated compensation costs along with certain other management costs are subject to reimbursement from the Manager up to an annual limit of \$1.25 million (adjusted annually for inflation). Amounts incurred in excess of the annual limit are the responsibility of the Company. The ratable share of estimated annual excess cost is accrued on a quarterly basis. For the period ended December 31, 2010, the Company recorded \$0.6 million of costs in excess of the reimbursement limit. Additionally, the Company pays an annual management fee to the Manager for providing certain accounting, tax, administrative and operational services.

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**23. Subsequent events**

*North Lake contract renewal and upgrade*

On May 3, 2011, the Company announced that it finalized the long term renewal and extension of the tolling agreement for the North Lake facility. The term of the agreement is for the remaining useful life (economic or functional) of the facility, which is expected to exceed 30 years. The site host may, however, terminate the agreement if it permanently ceases operations of the blast furnace that supplies steam to North Lake. Terms of the agreement require the site host to supply North Lake with steam produced from waste blast furnace gas inclusive of steam from a new boiler which is currently being constructed by the site host. In addition, the contract requires the Company to expand the capacity of its North Lake facility by 20 percent to 90 megawatts. The Company's estimated cost of the capacity expansion is \$10.0 - \$12.0 million and will be completed in two phases. The first phase was comprised primarily of an overhaul of the steam turbine was completed in March of 2011. The second phase will allow for the expansion of the capacity of the facility and is expected to be completed during the second or third quarter of 2012 to coincide with the completion of the site host's new boiler.

North Lake's revenue under the agreement is 100% variable, with North Lake only being entitled to payment for the energy it produces. The price per megawatt hour increases each year at a fixed annual escalation rate. As a mechanism to stabilize revenues from year-to-year, in years 3 to 15 of the agreement, the price the site host pays for electricity in a particular year is increased if the amount of electricity produced in the previous year is below the baseline production level established for the facility. North Lake is entitled to receive a moderate financial bonus if the actual demonstrated capacity of the facility after completion of the upgrade equals or exceeds 90 MW and will incur a moderate financial penalty if the actual demonstrated capacity after completion of the upgrade is below 89 megawatts. For each quarter that availability (the time when the facility is available to produce electricity) exceeds 96%, the site host has agreed to pay North Lake an availability bonus.

North Lake remains responsible for all operation and maintenance costs of the facility and has agreed to retain the site host (on a cost reimbursement basis) to provide routine operation and maintenance services. If the North Lake facility requires any repair due to the site host's failure to perform its obligations under the terms of the agreement, the site host will be required to reimburse North Lake for all reasonable costs incurred by North Lake to perform such repairs. If the North Lake facility requires repairs, North Lake has the option (but not the obligation) in certain cases to offer the facility to the site host for purchase at a price set out in a schedule to the agreement.

*Share consolidation*

On May 5, 2011, the Company announced a 3 to 1 Common Share consolidation with an effective date to be on or about May 19, 2011. The Company will consolidate all of its outstanding Common Shares on the basis of one post-consolidation Common Share for three existing Common Shares. Accordingly, the 134,118,561 Common Shares currently issued and outstanding will be consolidated into approximately 44,706,187 Common Shares. The number of Common Shares reserved for issuance under the Company's stock option plan and the number of Common Shares into which the outstanding options will be exercisable will be proportionally reduced to reflect the three-to-one consolidation ratio and the applicable exercise price will be proportionally increased. The number of deferred share units to which directors are entitled will also be consolidated on a 3 to 1 basis. The indirect percentage interest in PERH held by the Manager remains unchanged at 14.3%.