

# **AQUILA RESOURCES INC.**

( an exploration stage enterprise )

## **CONSOLIDATED FINANCIAL STATEMENTS**

(Expressed in Canadian Dollars unless otherwise stated)

**DECEMBER 31, 2008**

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## **AUDITORS' REPORT**

**To the Shareholders of  
Aquila Resources Inc.:**  
( an exploration stage enterprise )

We have audited the consolidated balance sheets of Aquila Resources Inc. (the "Company", an exploration stage enterprise) as at December 31, 2008 and 2007 and the consolidated statements of loss, comprehensive loss and deficit and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2008 and 2007 and the results of its operations and cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

"Edmund Cachia & Co. LLP"  
CHARTERED ACCOUNTANTS  
Licensed Public Accountants  
Toronto, Ontario  
February 27th, 2009

# AQUILA RESOURCES INC.

( an exploration stage enterprise )

## Consolidated Balance Sheets

(Expressed in Canadian Dollars)

As at December 31

	2008	2007
<b>Assets</b>		
<b>Current</b>		
Cash and cash equivalents	\$ 2,138,518	\$ 13,416,459
Accounts receivable	64,809	78,280
Prepaid expenses	39,097	45,167
	2,242,424	13,539,906
Security deposit (Note 3)	129,095	120,977
Mineral Property Costs (Note 3)	28,252,770	18,136,287
Capital Assets (Note 4)	1,011,555	776,005
	\$ 31,635,844	\$ 32,573,175
<b>Liabilities</b>		
<b>Current</b>		
Accounts payable and accrued liabilities (Note 7)	\$ 211,629	\$ 919,386
<b>Shareholders' Equity</b>		
Share capital (Note 5)	36,286,711	36,461,711
Contributed surplus (Note 6)	4,464,173	3,826,573
Deficit	(9,326,669)	(8,634,495)
	31,424,215	31,653,789
	\$ 31,635,844	\$ 32,573,175

### Approved on Behalf of the Board:

"Edward J. Munden" Director

"Robin Dunbar" Director

See accompanying notes to the consolidated financial statements.

# AQUILA RESOURCES INC.

( an exploration stage enterprise )

## Consolidated Statements of Loss, Comprehensive Loss and Deficit

(Expressed in Canadian Dollars)  
for the years ended December 31

	2008	2007	Cumulative from the date of commencement of exploration stage January 16, 2004
<b>Expenses</b>			
Depreciation	\$ 7,439	\$ 252	\$ 28,563
Consulting	88,297	84,241	254,367
Directors' fees	91,607	85,250	176,857
Filing and regulatory fees	37,456	214,237	277,581
Foreign exchange (gain) loss	(410,208)	1,412,468	914,215
Interest and bank charges	3,759	1,671	95,460
Licenses, taxes and fees	-	85,000	85,000
Management fees	71,875	145,000	602,191
Office, general and administrative	88,278	68,747	255,566
Professional fees	84,261	119,640	420,509
Rent	22,352	22,384	55,232
Salaries and wages	183,080	147,938	891,437
Stock-based compensation	462,600	2,360,307	5,047,127
Travel and promotion	229,832	204,416	653,677
Write-down of mineral property costs	-	768,774	768,774
Loss before undernoted	960,628	5,720,325	10,526,556
Interest and other income	(268,454)	(880,285)	(1,199,887)
Net loss and comprehensive loss for the period	692,174	4,840,040	\$ 9,326,669
Deficit, beginning of period	8,634,495	3,794,455	
Deficit, end of period	\$ 9,326,669	\$ 8,634,495	
<b>Loss per common share</b>			
Basic and Diluted (Note 2)	\$ 0.01	\$ 0.07	
Basic	70,097,149	69,954,477	
Diluted	70,097,149	70,586,619	

See accompanying notes to the consolidated financial statements.

# AQUILA RESOURCES INC.

( an exploration stage enterprise )

## Consolidated Statements of Cash Flows

(Expressed in Canadian Dollars)  
For the years ended December 31

	2008	2007	Cumulative from the date of commencement of exploration stage January 16, 2004
<b>Cash flows from operating activities</b>			
Net loss for the period	\$ (692,174)	\$ (4,840,040)	\$ (9,381,054)
Adjustments for:			
Depreciation	7,439	252	28,563
Financing fee	-	-	20,424
Stock-based compensation	462,600	2,360,307	5,047,127
Interest accrual	-	-	1,913
Write-down of mineral property costs	-	768,774	768,774
Changes in non-cash working capital (Note 12)	(688,216)	620,626	(21,063)
Cash used in operations	(910,351)	(1,090,081)	(3,535,316)
<b>Cash flows from investing activities</b>			
Purchase of capital assets	(254,697)	-	(367,034)
Security deposit	(8,120)	-	(124,660)
Mineral properties - acquisition	(2,062,381)	(2,117,244)	(6,150,644)
Mineral properties - exploration	(8,042,392)	(7,496,351)	(19,391,208)
Cash used in investing	(10,367,590)	(9,613,595)	(26,033,546)
<b>Cash flows from financing activities</b>			
Issuance of common shares	-	452,600	34,165,883
Issue cost	-	(2,078)	(2,188,236)
Notes payable	-	-	117,110
Repayment of mortgages payable	-	(395,224)	(461,548)
Loans payable	-	-	74,171
Cash provided by financing	-	55,298	31,707,380
Net increase (decrease) in cash	(11,277,941)	(10,648,378)	2,138,518
Cash and cash equivalents, beginning of period	13,416,459	24,064,837	-
<b>Cash and cash equivalents, end of period</b>	<b>\$ 2,138,518</b>	<b>\$ 13,416,459</b>	<b>\$ 2,138,518</b>

Supplemental cash flow information (Note 15)

See accompanying notes to the consolidated financial statements.

**1. Nature of operations and going concern considerations:**

Aquila Resources Inc. (the "Company") was incorporated under the Business Corporations Act ("Canada") and is involved in the mineral exploration business and controls mineral and surface rights at the Back Forty Project located in Menominee County, Michigan.

The Company is in the business of exploring for and developing mineral properties. Substantially all of the efforts of the Company are devoted to these business activities. To date the Company has not earned significant revenues and is considered an exploration stage company. The Company has an accumulated deficit of \$9,326,669 (2007- \$8,634,495) as at December 31, 2008. The ability of the Company to carry out its business plan rests with its ability to secure equity and other financing.

These consolidated financial statements have been prepared on the basis of accounting principles applicable to a "going concern", which assume that the Company will continue in operation for the foreseeable future and will be able to realize its assets and discharge its liabilities in the normal course of operations. The business of mining and exploring for minerals involves a high degree of risk and there is no guarantee that the Company's exploration programs will yield positive results or that the Company will be able to obtain the necessary financing to carry out the exploration and development of its mineral property interests.

These consolidated financial statements do not reflect the adjustments to the carrying values of assets and liabilities, the reported expenses and balance sheet classifications that would be necessary should the going concern assumption be inappropriate. These adjustments could be material.

The recoverability of the carrying value of exploration properties and the Company's continued existence is dependent upon the preservation of its interests in the underlying properties, the development of economically recoverable reserves, the achievement of profitable operations, or the ability of the Company to raise additional financing, if necessary, or alternatively upon the Company's ability to dispose of its interests on an advantageous basis. Changes in future conditions could require material write-downs of the carrying values.

Although the Company has taken steps to verify title to the properties in which it has an interest, in accordance with industry standards for the current stage of exploration of such properties, these procedures do not guarantee the Company's title. Property title may be subject to government licensing requirements or regulations, unregistered prior agreements, undetected defects, unregistered claims, native land claims, and non-compliance with regulatory and environmental requirements.

**2. Significant Accounting Policies:****Principles of consolidation:**

These consolidated financial statements are prepared in accordance with generally accepted accounting principles in Canada. Summarized below are these policies considered significant to the Company. References to the Company included herein are inclusive of the accounts of Aquila Resources Inc.'s wholly-owned subsidiary Aquila Resources Corp. and its subsidiaries. All inter-company balances and transactions have been eliminated.

**Deferred mineral property costs:**

Property acquisition costs and related direct exploration costs are deferred until the properties are placed into mineral production, sold or abandoned. These costs will be amortized on the units-of-production basis over the estimated useful life of the properties following the commencement of production or written-off if the properties are sold, allowed to lapse, or abandoned.

Cost includes the cash, consideration paid and the fair market value of any common shares issued on the acquisition of mineral properties. Properties acquired under option agreements, whereby payments are made at the sole discretion of the Company, are recorded in the accounts at such time as the payments are made. The recorded cost of mineral claims and deferred exploration and development costs represent costs incurred and are not intended to reflect present or future values.

The recoverability of costs incurred on the exploration properties is dependent upon numerous factors including exploration results, environmental risks, commodity risks, political risks, and the Company's ability to attain profitable production. It is reasonably possible, based on existing knowledge, that changes in future conditions in the near-term could require a change in the determination of the need for, and amount of, any write down.

The Company reviews capitalized costs on its property interests on a periodic, or annual, basis and will recognize an impairment in value based upon current exploration results and upon management's assessment of the future probability of profitable revenues from the property or from the sale of the property. Management's assessment of the property's estimated current fair market value may also be based upon a review of other property transactions that have occurred in the same geographic area as that of the property under review and the assessment of the ability to recover capitalized costs based on technical, social and environmental issues.

Administrative costs, other than for those that are charged to deferred mineral property costs, are expensed as incurred.

**Capital assets:**

Capital assets consist of land and buildings, which are recorded at cost and buildings are depreciated on the declining-balance basis at a rate of 4% per annum.

Depreciation on assets used in exploration are capitalized to mineral property costs.

**Share capital:**

Common shares issued for non-monetary consideration are recorded at their fair market value based upon the price per share paid in the most recent prior sale of shares for cash. Costs incurred to issue common shares are deducted from share capital.

**Use of estimates:**

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Significant areas requiring the use of management estimates related to the continuing viability of mineral property interests, the determination of reclamation obligations, and rates for depreciation on capital assets, and assumptions used in the determination of the fair value of stock based compensation. Actual results could differ from these estimates. Management believes that the estimates are reasonable.

**Revenue recognition:**

Interest income is recognized on an accrual basis as it is earned.

**Assets retirement obligation:**

The Company recognizes a liability for an asset retirement obligation when it is determinable and calculates the liability based upon undiscounted future payments to be made. A corresponding amount is added to the carrying amount of the related long-term asset, and this amount is subsequently allocated to expense over its expected life. Adjustments will also be made in subsequent periods to changes in asset retirement obligations due to changes in estimates. As at December 31, 2008, the Company does not have any asset retirement obligations.

**Impairment of long-lived assets:**

Long-lived assets, including capital assets and other assets, are reviewed for impairment whenever events or changes in circumstances indicates that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized by the amount by which the carrying amount of the asset exceeds the fair value of the asset.

**Income taxes:**

The Company accounts for and measures future tax assets and liabilities in accordance with the asset and liability method.

Under this method, future tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amount of existing assets and liabilities and their respective tax bases. Future tax assets and liabilities are measured using the enacted or substantially-enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be reversed or settled. The effect on future tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the date of enactment or substantive enactment of the change. When the future realization of income tax assets does not meet the test of being more likely than not to occur, a valuation allowance in the amount of the potential future benefit is taken and no net asset is recognized. Assuming the Company's operations remain at the exploration stage, such an allowance will continue to apply fully for the foreseeable future to all potential income tax assets. Accordingly, the Company's accounting policy for the future income taxes currently has no effect on the consolidated financial statements of the fiscal periods presented.

**Stock-based compensation:**

The Company has a stock option plan, which is described in note 5(d). The Company uses the Black-Scholes option pricing model to estimate the fair value of each stock-option at the date of grant. Stock options that vest immediately are recorded at the date of grant. Stock options that vest over time are recorded over the vesting period using straight-line method. Stock option compensation is recognized as expense with a corresponding increase in contributed surplus. On exercise of the stock option, consideration received and the estimated fair value previously recorded in contributed surplus is recorded as share capital.

**Cash and cash equivalents:**

Cash and short-term investments with a remaining maturity of three months or less at the date of acquisition are classified as cash and cash equivalents. The Company places its cash and cash investments with institutions of high-credit worthiness.

Cash and cash equivalents comprise the following balance sheet amounts:

	<b>2008</b>	<b>2007</b>
Cash on hand and balances with banks	\$ 70,228	\$ 1,432,576
Short-term interest bearing investments	2,068,290	11,983,883
	<b>\$ 2,138,518</b>	<b>\$ 13,416,459</b>

**Loss per share:**

Basic loss per share is computed by dividing loss available to common shareholders by the weighted average number of common shares outstanding during the year. The treasury stock method is used to calculate diluted loss per share.

**Diluted loss per share:**

Diluted loss per share is similar to basic loss per share, except that the denominator is increased to include the number of additional common shares that would have been outstanding assuming that options and warrants with an average market price for the year greater than their exercise price are exercised and the proceeds used to repurchase common shares. The fully diluted loss per share has not been computed, as the effect would be anti-dilutive.



**Translation of foreign currencies:**

Monetary assets and liabilities denominated in foreign currencies are translated into Canadian dollars at exchange rates prevailing at the balance sheet date. Non-monetary assets and liabilities are translated into Canadian dollars at approximate exchange rates prevailing at the transaction date. Revenue and expenses are translated at average exchange rates prevailing during the year. The resulting gains and losses are included in loss for the year.

**Property option agreements:**

From time to time, the Company may acquire or dispose of properties pursuant to the terms of option agreements. Due to the fact that options are typically exercisable entirely at the discretion of the optionee, the amounts payable or receivable are not recorded. Option payments are recorded as resource property costs or recoveries when the payments are made or received.

**Mineral property pre-acquisition costs:**

The Company capitalizes pre-acquisition costs investigating potential property acquisition. However, if the Company determines that a specific property acquisition will not be concluded, the costs associated with the specific property are charged to operations in the current period.

**Financial assets and liabilities:***Assets or liabilities held-for-trading*

Financial instruments classified as assets or liabilities held for trading are reported at fair value at each balance sheet date, and any change in fair value is recognized in net income (loss) in the period which the change occurs.

*Held-to-maturity investments, loans and receivables and other financial liabilities*

Financial instruments classified as loans and receivables, held-to-maturity investments and other financial liabilities are carried at amortized costs using the effective interest method. Interest income or expenses is included in net income (loss) over the expected life of the instrument.

*Available-for-sale*

Financial instruments classified as available for sale are recorded at fair value at each balance sheet date and any change in fair value is recognized in other comprehensive income in the period in which these changes occur. Securities classified as available for sale and with no quoted market price in an active market are carried at cost. Available-for-sale securities are written down to fair value (impairment recognized in loss) when it is necessary to reflect an other-than-temporary impairment. Upon derecognition, any accrued gains or losses in accumulated other comprehensive income are then recognized in net income (loss).

**Classification of financial instruments:**

The Company designates its cash and cash equivalents as held-for-trading, which is measured at fair value. Accounts receivable are classified as loans and receivables, which are measured at amortized cost. Accounts payable and accrued liabilities are classified as other financial liabilities which are measured at amortized cost. Due to the short-term nature of these instruments, their carrying value approximates their fair value.

**Cumulative information for exploration stage companies:**

The Company has adopted CICA Handbook Accounting Guideline #11 with respect to financial statement presentation for exploration stage companies. Accordingly, the statements of loss and cash flows have been altered to include a column outlining the cumulative revenues, expenses and cash flows from the date of commencement of exploration stage activities being January 16, 2004 to the fiscal year end date of the consolidated financial statements.

**Change in accounting policies:**

Effective January 1, 2008, the Company adopted the following accounting policies as recommended by the CICA handbook:

Section 3855 - Financial Instruments - Recognition and Measurement: Section 3855 requires that all financial assets, except those classified as held-to-maturity, and derivative financial instruments, must be measured at fair value. All financial liabilities must be measured at fair value when they are classified as held-for-trading; otherwise, they are measured at cost. Investments classified as available-for-sale are reported at fair market value based on quoted market prices with unrealized gains or losses excluded from earnings and reported as other comprehensive income or loss.

Section 1530 - Comprehensive Income: This standard introduces new rules for the reporting and display of comprehensive income. Comprehensive income represents a change in shareholders' equity (net assets) of an enterprise during a reporting period from transactions and other events and circumstances from non-owner sources. It includes all changes in equity during a period except those resulting from investments by owners and distributions to owners. These items include holding gains and losses on certain investments, gains and losses on certain derivative instruments, and foreign currency gains and losses related to self-sustaining foreign operations.

Transition adjustment to opening balance: The adoption of Sections 1530 and 3855 did not impact the opening equity and losses of the Company.

The Company adopted the revised CICA Handbook Section 1506, Accounting Changes, which requires that: (a) a voluntary change in accounting principals can be made if, and only if, the changes result in more reliable and relevant information, (b) changes in accounting policies are accompanied with disclosures of prior period amounts and justification for the change and (c) for changes in estimates, the nature and amount of the change should be disclosed. The Company has not made any voluntary change in accounting principles since the adoption of the revised standard.

Capital Disclosures – Section 1535 specifies the disclosure of (i) an entity's objectives, policies and processes for managing capital; (ii) quantitative data about what the entity regards as capital; (iii) whether the entity has complied with any capital requirements; and (iv) if it has not complied, the consequences of such noncompliance. The Company has included disclosures recommended by the new Handbook section in note 13 to these consolidated financial statements.

Financial instruments – Sections 3862 and 3863 replace Section 3861, Financial Instruments – Disclosure and Presentation, revising and enhancing its disclosure requirements, and carrying forward unchanged its presentation requirements. These new sections place increased emphasis on disclosures about the nature and extent of risks arising from financial instruments and how the entity manages those risks. The Company has included disclosures recommended by the new section in note 14 to these consolidated financial statements.

**Future accounting changes:***Amendments to Section 1400 – Going Concern*

Section 1400, "General Standards of Financial Statement Presentation", was amended to include requirements to assess and disclose an entity's ability to continue as a going-concern. When financial statements are not prepared on a going concern basis, that fact shall be disclosed together with the basis on which the financial statements are prepared and the reason why the company is not considered a going-concern. The new requirements are effective for the Company for interim and annual financial statements beginning January 1, 2009. The Company is currently evaluating the impact of this new standard.

Section 3064 - Goodwill and Intangible Assets replacing Section 3450, Research and Development Costs. The new standard, which the Company will adopt in fiscal 2009, establishes guidelines for the recognition, measurement, presentation and disclosure of research and development costs. Management is in the process of assessing the impact of this new standard and the impact on the Company's consolidated financial statements has not yet been determined.

Section 1601 Consolidated Financial Statements. This new Section will be applicable to financial statements relating to the Company's interim and fiscal year beginning on or after January 1, 2011. Early adoption is permitted. This section establishes standards for the preparation of consolidated financial statements. The Company has not yet determined the impact of the adoption of this new section on the consolidated financial statements.

*International Financial Reporting Standards ("IFRS")*

In January 2006, the CICA's Accounting Standards Board ("AcSB") formally adopted the strategy of replacing Canadian GAAP with IFRS for Canadian enterprises with public accountability. The current conversion timetable calls for financial reporting under IFRS for accounting periods commencing on or after January 1, 2011. On February 13, 2008, the AcSB confirmed that the use of IFRS will be required in 2011 for publicly accountable profit-oriented enterprises. For these entities, IFRS will be required for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2011.

The Company is currently assessing the impact of IFRS on its financial statements.

**3. Mineral property costs and commitments:**

Total accumulated deferred mineral property costs are detailed as follows:

	Balance beginning of year	Acquisition	Exploration	Recoveries	Write-down	Balance end of year
<b>2008</b>						
<b>Michigan, USA</b>						
Back Forty Project	\$ 18,136,287	\$ 2,062,381	\$ 8,054,102	\$ -	\$ -	\$ 28,252,770
<b>2007</b>						
<b>Michigan, USA</b>						
Back Forty Project	\$ 8,512,443	\$ 2,117,244	\$ 7,506,600	\$ -	\$ -	\$ 18,136,287
<b>Honduras</b>						
Cedros Property	768,774	-	-	-	(768,774)	-
	\$ 9,281,217	\$ 2,117,244	\$ 7,506,600	\$ -	\$ (768,774)	\$ 18,136,287

**Michigan, USA**

*Back Forty Project*

The Back Forty Project controls approximately 9,600 acres of surface and mineral rights which are owned or held under lease or option by a 100% owned U.S. subsidiary. Some lands are subject to net smelter royalties varying from 1% to 3.5%, with certain lands subject to a 2% - 7% state royalty, which under state law can be renegotiated. Annual option and property acquisition costs for 2008 were \$2,062,381 (2007-\$2,117,244). The entire project is subject to a 7% net distributable earnings royalty ("Net Profits after Payback") payable to a former joint venture partner.

*MRT Property*

On August 3, 2006, the Company entered into an option agreement to acquire a 100% interest in approximately 50 acres of surface and mineral rights in Lake Township, Menominee County, Michigan (the "MRT property"). The aggregate price payable of US\$11,700,000 is due in annual installments on the anniversary date over a nine year option period as follows: US\$1,333,333 on August 3, 2006, US\$1,333,333 on August 3, 2007 and August 3, 2008, US\$250,000 on each of the 3rd and 4th anniversaries, and US\$1,440,000 on each of the 5th through 9th anniversaries. During 2008 and 2007, the Company made annual cash option payments of US\$1,333,333 to maintain its interest in the property.

The Company maintains a cash deposit in the amount of \$116,540 (US \$100,000), pursuant to an escrow agreement. The amount is being held as security for the fulfillment of obligations in accordance with the above noted option agreement. During the year, the deposit accrued interest of \$8,120 (2007-\$4,435).

#### *Metallic mineral leases*

On December 7, 2006, 27 state metallic mineral leases were assigned to the Company from a Company of which the President and CEO and another Director are major shareholders.

In order to retain its interest in these state leases, the Company must make annual lease payments over the next four years as follows:

2009 - US\$37,304; 2010 - US\$37,304; 2011 - US\$37,304; 2012 - US\$45,599

#### *Purchase of Property under Option*

During the year the Company purchased three parcels of private land held under option. The property ownership consist of surface and mineral rights. Aggregate consideration for the three properties was US \$617,500.

The Company purchased a property, held under option by a geological consulting company of which the President, CEO and another Director are major shareholders for \$586,421, including costs. The Company had made a \$50,000 option payment on this property in 2006.

On October 7, 2006, the Company entered into an option agreement to acquire a 100% interest in 181 acres of surface and mineral rights in Lake Township, Menominee County, Michigan. In order to earn a 100% interest in the project area from the option, the Company entered into a three-year option agreement, for an aggregate price payable of US \$2,300,000 payable: US \$300,000 in year one, of which US \$50,000 has been paid, US \$1,000,000 in year two, and US \$1,000,000 in year three.

During the year, the Company terminated the option. No further commitments and encumbrances remain.

#### **Future Commitments**

Estimated lease, option and property acquisition costs related to the Back-Forty Project in each of the next four fiscal years are as follows:

2009 - US\$396,323; 2010 - US\$1,142,323; 2011 - US\$1,557,323; 2012 - US\$1,565,619

See Note 9 for additional mineral property commitment detail that is included in the above figures.

#### **Honduras**

##### *Cedros Property*

During the year, the Company ended its contractual obligation to acquire the Cedros Property. An agreement to acquire title to the Cedros Property had been entered into in 2005. Subject to the satisfactory transfer of title, 1,000,000 common shares had been held in escrow pending transfer. In December 2008, the Company entered into a settlement agreement with First Point Minerals Corp. (the parent of the Honduran company which holds title to the Honduras property interest) that was to transfer the rights to the Property. Under the terms of agreement, the Company cancelled 500,000 of the shares held in escrow and released the balance of the shares to First Point Minerals Corp. The Company has no further rights or obligations with respect to the Cedros Property. In 2007, the Property was fully written down. First Point Minerals Corp. and the Company have one common director.

**4. Capital assets:**

	2008			2007
	Cost	Accumulated depreciation	Net book value	Net book value
Land	\$ 503,962	\$ -	\$ 503,962	\$ 482,253
Buildings	528,838	47,346	481,492	292,750
Furniture, fixtures and equipment	29,583	3,482	26,101	1,002
	<b>\$ 1,062,383</b>	<b>\$ 50,828</b>	<b>\$ 1,011,555</b>	<b>\$ 776,005</b>

During the year, depreciation amounting to \$11,710 (2007 - \$10,249) was capitalized to mineral property costs.

**5. Share capital:**

a) Authorized  
Unlimited number of common shares

b) Issued  
Common shares

	Number of Common	
	Shares	Amount
Issued at December 31, 2005	16,321,170	\$ 4,923,871
Financing fees	34,312	5,902
Pre RTO Aquila shareholders	16,355,482	4,929,773
Shares issued to JML shareholders for net assets	9,109,286	122,724
Conversion of JML preference shares	1,274,377	-
Broker shares	525,435	121,754
Issued for cash to 2079537 Ontario Ltd. shareholders	10,599,500	2,119,900
Subscription receipts	1,230,000	246,000
Issue of common shares on exercise of warrants for settlement of debt	520,000	87,056
Private placement	15,515,151	25,599,999
Issued for cash / on exercise of options	633,833	190,150
Issued for cash / on exercise of warrants	13,550,247	4,198,442
Fair value of options exercised	-	329,307
Share issue costs	-	(2,362,563)
Issued at December 31, 2006	69,313,311	35,582,542
Issued for cash / on exercise of options	796,167	452,600
Fair value of options exercised	-	428,647
Issue costs	-	(2,078)
Issued at December 31, 2007	70,109,478	\$ 36,461,711
Cedros Property settlement (Note 3)	(500,000)	(175,000)
Issued at December 31, 2008	69,609,478	\$ 36,286,711

## c) Warrants:

The following summarizes the warrants that were outstanding during the year:

	Number of Warrants	
	2008	2007
Balance, beginning of the year	8,843,635	8,843,635
Warrants expired during the year	(8,843,635)	-
Balance, end of the year	-	8,843,635

On December 15, 2008, 8,843,635 warrants with an exercise price of \$2.15 expired.

As at December 31, 2007, 8,843,635 warrants expiring on December 15, 2008, with an exercise price of \$2.15, were outstanding. Each warrant entitled the holder to purchase the above stated number of common shares on or before the expiry date.

## d) Stock-option plan:

The Company maintains a Stock Option Plan (the "Plan") for the benefit of directors, officers, employees, consultants and other service providers of the Company and its subsidiaries in order to assist the Company in attracting, retaining, and motivating such persons by providing them with the opportunity, through stock options to acquire an increased proprietary interest in the Company. Under the Plan, options are non-assignable and may be granted for a term not exceeding five years. The number of common shares that may be reserved for issuance to any one person must not exceed 5% of the outstanding common shares. The exercise price of an option may not be lower than the closing price of the common shares on the TSX, subject to applicable discounts, on the business day immediately proceeding the date the option is granted. The options are non-transferable.

The fair value of each option was estimated on the date of grant. Under Black-Scholes the options vested during the year ended December 31, 2008 have been valued at \$462,600 (2007 - \$2,306,307), and expensed to loss, using the following assumptions at the measurement date:

	2008	2007
Risk-free interest rate	3.26%	4.12%
Expected life	5 years	4.3 years
Price volatility	115%	115%
Dividend yield	Nil	Nil

A summary of the status of the Company's stock option plan as of December 31, 2008 and 2007, and changes during the years are presented below:

	2008		2007	
	Options	Weighted average exercise price	Options	Weighted average exercise price
Outstanding at beginning of the year	4,550,000	1.17	3,646,167	\$ 0.65
Exercised	-	-	(796,167)	0.37
Expired	(420,000)	1.29	-	-
Granted	700,000	0.90	1,700,000	2.04
Outstanding at end of the year	4,830,000	1.13	4,550,000	\$ 1.17

The following summarizes information on the stock options outstanding at December 31, 2008:

Weighted average exercise price	\$ 1.13
Options outstanding as at December 31, 2008	4,830,000
Remaining contractual life	3.23 years
Options exercisable as at December 31, 2008	4,760,000

See note 17 for additional stock option information.

e) Escrowed shares

As at December 31, 2008, there were no shares held in escrow. Of the Company's issued share capital, 13,808,669 common shares were held in escrow pursuant to an escrow agreement as at December 31, 2006.

During 2007, these shares were released subsequent to the Company listing on the TSX.

During the year, 1,000,000 common shares that were held in escrow relating to the Cedros Property were released.

**6. Contributed surplus:**

	2008	2007
Balance, beginning of the year	\$ 3,826,573	\$ 1,894,913
Stock-based compensation cost	462,600	2,360,307
Fair value of stock options exercised	-	(428,647)
Shares cancelled (Note 3)	175,000	-
Balance, end of the year	\$ 4,464,173	\$ 3,826,573

**7. Related party transactions:**

For the year ended December 31, 2008 management fees amounting to \$71,875 (2007 - \$95,000) were charged by a company controlled by the CFO and a director of the Company. As at December 31, 2008 accounts payable includes \$3,281 (2007-\$27,852) owing to this related party.

During 2008 and 2007 the President and CEO, and related individuals received remuneration consisting of management fees and salaries. Total remuneration for 2008 was \$414,416 (2007-\$308,202). Accounts payable includes \$Nil (2007-\$50,000) owing to these related parties at December 31, 2008.

A total of US \$729,853 (2007 - US \$2,050,818) was charged in the operations at the Back Forty Project by a geological consulting company of which the President and CEO and another director are major shareholders. A management fee calculated on a percentage of wages payable was included in the amount charged by the geological consulting company to the Company. As at December 31, 2008 accounts payable includes \$12,400 (2007-\$327,596) owing to this related party.

During the year, the Company was charged Directors' fees totaling \$91,607 (2007 - \$85,250) by non-executive directors. Accounts payable includes \$Nil (2007- \$20,000) owing to these related parties.

During the year, the Company was charged legal fees totaling \$50,985 (2007-\$72,330) by a law firm whose partner is an officer of the Company. As at December 31, 2008 accounts payable includes \$2,954 (2007-\$1,360) due to this related party.

Rental expenditures in the amount of \$22,352 (2007-\$22,384) were charged by a Company with common directors.

See notes 3 and 17 for additional related party information.

Management believes these transactions are in the normal course of business and are measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties.

**8. Funds held in trust:**

In accordance with certain covenants under the terms of the Company's agency agreement related to its December 2006 private placement, \$300,000 was held in trust for the benefit of the Company. During 2007 the amount held in trust was released to the Company in full.

**9. Commitments:**

Future minimum warehouse lease payments under a non-cancellable lease are as follows:

2009	US \$	48,000
2010	US \$	48,000
2011	US \$	48,000
2012	US \$	48,000
2013	US \$	32,000

**10. Income taxes:**

(a) The Company's provision for income taxes differ from the amounts computed by applying the basic current rates to loss for the year before taxes, as shown in the following table:

	2008	2007
Statutory rate applied to loss for the year before income taxes	\$ (228,417)	\$ (1,748,223)
Increase (decrease) in taxes resulting from:		
Stock-based compensation cost	152,658	852,543
Write down of mineral property	-	277,681
Amortization of exploration costs	(407,807)	-
Share issue costs	(179,020)	63,210
Other items	(22,045)	722
Loss not tax-benefited	684,631	554,067
Future income tax (recovery)	\$ -	\$ -

(b) The tax effects of temporary differences that give rise to future income tax assets at December 31, 2008 and 2007 are as follows:

	2008	2007
Future tax assets:		
Non-capital losses carry forward	\$ 3,126,010	\$ 1,705,602
Mineral property	105,464	755,081
Capital assets	195	3,921
Share issue costs	527,841	1,033,257
	3,759,510	3,497,861
Less: valuation allowance	(3,759,510)	(3,497,861)
Net asset	\$ -	\$ -

(c) The Company has non-capital losses of approximately \$9,472,759 which expire through 2028. The benefit of these losses has not been recognized for financial statements purposes.

(d) During the year, the Company paid \$ nil (2007- \$nil) in respect of income taxes.



**11. Comparative figures:**

Certain comparative figures have been reclassified to conform to the current year's presentation. These reclassifications did not affect the prior year's net losses.

**12. Changes in non-cash operating working capital:**

	2008	2007
Accounts receivable	\$ 13,471	\$ 3,138
Funds held in trust	-	300,000
Prepaid expenses	6,070	4,421
Accounts payable and accrued liabilities	(707,757)	313,067
	<b>\$ (688,216)</b>	<b>\$ 620,626</b>

**13. Capital management:**

The Company considers its capital to include components of shareholders' equity.

The Company's objectives in managing its capital are: to maintain adequate levels of funding to support its expenditures arising from the Company's investments; to safeguard the Company's ability to continue as a going concern in order to pursue the exploration of its properties; to maintain a flexible capital structure for its projects for the benefit of its stakeholders; to maintain corporate and administrative functions necessary to support the Company's operations and corporate functions; and to seek out and acquire new projects of merit.

The Company manages its capital structure and makes adjustments to it, based on the funds available to the Company in order to support the acquisition, exploration and development of mineral properties. The Board of Directors does not establish quantitative return on capital criteria for management, but rather relies on the expertise of the Company's management to sustain future development of the business.

The properties in which the Company currently has an interest are in the exploration stage; as such the Company is dependent on external financing to fund its activities. In order to carry out the planned exploration and pay for administrative costs, the Company will spend its existing working capital and raise additional amounts as needed. The Company will continue to assess new properties and seek to acquire an interest in additional properties if it feels there is sufficient geologic or economic potential and if it has adequate financial resources to do so.

The Company's investment policy is to invest excess cash in low risk, highly liquid, short-term interest bearing investments, selected with regards to the expected timing of upcoming expenditures.

The Company expects its current capital resources will be sufficient to carry out its exploration plans, operation plans and operations through its current operating period.

Management reviews its capital management approach on an ongoing basis and believes that this approach, given the relative size of the Company, is reasonable.

There were no changes in the Company's approach to capital management during the year ended December 31, 2008.

#### 14. Financial instruments:

##### *Fair value*

The Company has determined the estimated fair value of its financial instruments based on estimates and assumptions. The actual results may differ from those estimates and the use of different assumptions or methodologies may have a material effect on the estimated fair value amounts.

The fair value of cash and cash equivalents, accounts receivable and accounts payable and accrued liabilities are comparable to their carrying value due to the relatively short period to maturity of these instruments.

The Company's risk exposures and the impact on the Company's financial instruments are summarized below:

##### *Credit risk*

The Company's credit risk is primarily attributable to short-term investments and receivables included in current assets. The Company has no material concentration of credit risk arising from operations. Cash and cash equivalents consist of bank deposits and money market funds holding Banker's Acceptances, which have been invested with or purchased from a company controlled by a Canadian Chartered bank, from which management believes the risk of loss to be remote. Other credit risk primarily consists of GST receivable. Management believes that the credit risk concentration with respect to receivables is remote.

##### *Liquidity risk*

The Company's approach to managing liquidity risk is to ensure that it will have sufficient liquidity to meet liabilities when due. As at December 31, 2008, the Company had cash and cash equivalents of \$2,138,518 (December 31, 2007- \$13,416,459) to settle accounts payable and accrued liabilities of \$211,632 (December 31, 2007- \$919,386). The ability of the Company to continue to pursue its exploration activities is dependant on its ability to secure additional equity or other financing. All of the Company's financial liabilities have contractual maturities of less than 30 days and are subject to normal trade terms.

##### *Market risk*

###### (a) Interest rate risk

The Company has cash and cash equivalents bearing fixed interest rates and no interest bearing debt. The Company's current policy is to invest excess cash in investment-grade short-term deposit certificates issued by its banking institutions. The Company periodically monitors the investments it makes and is satisfied with the credit ratings of its banks.

###### (b) Foreign currency risk

The Company is exposed to currency risk arising from fluctuations in foreign exchange rates. The Company raises funds from equity financing primarily in Canadian dollars and pays for a significant amount of expenditures relating to its mineral property interests in U.S. dollars.

###### (c) Commodity price risk

The Company is exposed to price risk with respect to commodity prices. Changes in commodity prices will impact the economics of development of the Company's mineral properties. The Company closely monitors commodity prices to determine the appropriate course of action to be taken by the Company.

##### *Sensitivity analysis*

As at December 31, 2008, the carrying value amounts of the Company's financial instruments approximates their fair value.

At December 31, 2008, the Company is exposed to currency risk through the following financial assets and liabilities denominated in U.S. dollars:

	2008	2007
Cash and cash equivalents	\$ 494,951	\$ 5,529,152
Accounts payable and accrued liabilities	(56,197)	(490,202)
	<b>\$ 438,754</b>	<b>\$ 5,038,950</b>

Based on the above net exposures as at December 31, 2008, and assuming that all other variables remain constant, a 10% depreciation or appreciation of the Canadian dollar against the U.S. dollar would result in an increase or decrease of approximately \$43,875 (2007-\$503,895) in the Company's net loss.

Price risk is remote since the Company is currently not a revenue producing entity.

*Limitations of sensitivity analysis*

The above analysis demonstrates the effect of a change in foreign currency rates in isolation. In reality, there is a correlation between two factors. Additionally, the financial position of the Company may vary at the time that a change in either of these factors occurs, causing the impact on the Company's results to differ from that shown above.

**15. Supplemental cash flow information:**

Non-cash activities were as follows:

	2008	2007
Fair value of options exercised	\$ -	\$ 428,647
Depreciation capitalized to resource properties	\$ 11,710	\$ 10,249
Cancellation of escrowed shares	\$ 175,000	\$ -

**16. Segmented information:**

The Company operates in a single reportable operating segment, the exploration and development of mineral properties. Segmented geographic information is as follows:

The following table allocates assets by segment:

As at December 31	2008	2007
Canada	\$ 5,111,299	\$ 14,521,313
United States	26,524,545	18,051,862
Total assets	<b>\$ 31,635,844</b>	<b>\$ 32,573,175</b>

The following table allocates net loss by segment:

Year ended December 31	2008	2007
Canada	\$ (638,110)	\$ (3,826,357)
United States	(54,064)	(244,909)
Honduras	-	(768,774)
Net loss	<b>\$ (692,174)</b>	<b>\$ (4,840,040)</b>

**17. Subsequent events:**

Subsequent to year end, the Company granted 1,850,000 stock options, exercisable at \$0.15 for a period of five years to management, employees, and directors of the Company. In addition, the Company has reserved 300,000 options, exercisable at \$0.30 to a third party consultant. The issuance of the options is contingent on the consultant successfully sourcing non-equity financing for the Company.