Aquila Resources Inc.

DECEMBER 31, 2011
CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in United States Dollars, unless otherwise stated)
December 31, 2011

INDEX

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INDEPENDENT AUDITORS' REPORT

To the Shareholders of Aquila Resources Inc.

We have audited the accompanying consolidated financial statements of Aquila Resources Inc. and its subsidiaries, which comprise the consolidated balance sheet as at December 31, 2011, and the consolidated statements of comprehensive loss, changes in equity and cash flows for the year then ended and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Aquila Resources Inc. and its subsidiaries as at December 31, 2011, and the results of its operations and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Other Matter

The comparative information, which comprise the consolidated statements of financial position as at December 31, 2010 and January 1, 2010, the consolidated statement of comprehensive loss, consolidated statement of changes in equity, and consolidated statement of cash flows for the year ended December 31, 2010, and the summary of significant accounting policies and other explanatory information, including Note 18, which explains the transition from pre-changeover GAAP to IFRSs affected the entity's reported financial position, financial performance and cash flows, were audited by another auditor who expressed an unmodified opinion on March 27, 2012.

Collins Barrow Toronto LLP

Licensed Public Accountants
Chartered Accountants
March 27, 2012
Toronto, Ontario

EDMUND CACHIA & CO.
Chartered Accountants

INDEPENDENT AUDITORS' REPORT

To the Shareholders of Aquila Resources Inc.:

We have audited the comparative information of Aquila Resources Inc., which comprise the consolidated statements of financial position as at December 31, 2010 and January 1, 2010, the consolidated statement of comprehensive loss, consolidated statement of changes in shareholdersô equity, and consolidated statement of cash flows for the year ended December 31, 2010, and the summary of significant accounting policies and other explanatory information, including Note 18, which explains how the transition from pre-changeover Canadian generally accepted accounting principles to International Financial Reporting Standards affected the entityôs reported financial position, financial performance and cash flows.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of the consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of the consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on the comparative information in these accompanying consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditorôs judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entityôs preparation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entityôs internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained in our audits is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the comparative information in these accompanying consolidated financial statements present fairly, in all material respects, the consolidated financial position of Aquila Resources Inc. as at December 31, 2010 and January 1, 2010, and its financial performance and its cash flows for the year ended December 31, 2010, in accordance with International Financial Reporting Standards.

Other Matter

The consolidated statement of financial position as at December 31, 2011, the consolidated statement of comprehensive loss, consolidated statement of changes in shareholdersô equity, and consolidated statement of cash flows for the year ended December 31, 2011, and the summary of significant accounting policies and other explanatory information, are audited by another auditor who expressed an unmodified opinion on March 27, 2012.

Licensed Public Accountants
Chartered Accountants
March 27, 2012
Toronto, Ontario

Aquila Resources Inc.

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION
(Expressed in United States Dollars)

As at	Note	December 31, 2011	December 31, 2010 (Note 18)	January 1, 2010 (Note 18)
ASSETS				
Current				
Cash		$ 1,926,624	$ 950,662	$ 1,791,853
Accounts receivable		211,349	94,097	100,882
Prepaid expenses		29,887	33,817	35,891
		2,167,860	1,078,576	1,928,626
Security deposits	4(a)	166,111	134,528	119,464
Mineral property costs	4	30,347,560	28,237,272	27,505,401
Capital assets	5	868,617	796,484	816,047
		$ 33,550,148	$ 30,246,860	$ 30,369,538
LIABILITIES				
Current				
Accounts payable and accrued liabilities		$ 62,337	$ 173,359	$ 104,404
Advances for work to be performed	4(b)	250,000	210,811	-
		312,337	384,170	104,404
SHAREHOLDERS' EQUITY				
Share capital	6(a)	42,333,037	37,277,999	36,977,430
Contributed surplus		5,351,640	4,760,497	4,774,519
Warrants	7	199,778	-	-
Deficit		(14,646,644)	(12,175,806)	(11,486,815)
		33,237,811	29,862,690	30,265,134
		$ 33,550,148	$ 30,246,860	$ 30,369,538

Nature of operations (Note 1)
Commitments (Notes 4 and 9)
Subsequent event (Note 17)

Approved on behalf of the Board on March 27, 2012

'Edward J. Munden' Director

'Robin Dunbar' Director

Aquila Resources Inc.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS
(Expressed in United States Dollars)

	Note	For the Years Ended December 31, 2011	2010 (Note 18)
Expenses			
Depreciation		$ 18,420	$ 19,563
Consulting fees		97,183	54,851
Director's fees	8	31,270	32,222
Filing and regulatory fees		76,507	31,851
Foreign exchange (gain) loss		257,093	(68,146)
Interest and bank charges		4,186	3,759
Mineral property recovery, net of write-off		(12,735)	-
Management fees	8	65,137	100,853
Office, general and admin		151,470	87,338
Professional fees		251,448	68,441
Rent		22,895	13,981
Salaries and benefits		398,655	180,832
Share-based compensation	6(b)	1,012,186	63,404
Travel and promotion		103,706	106,697
		2,477,421	695,646
Interest and other income		6,583	6,655
Net loss and comprehensive loss for the year		$ 2,470,838	$ 688,991
Loss per common share			
Basic and fully diluted loss per share		$ (0.03)	$ (0.01)
Weighted average number of common shares outstanding		85,882,403	82,037,263

Aquila Resources Inc.

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
(Expressed in United States Dollars)

	Share Capital Shares	Share Capital Amount	Contributed Surplus	Warrants	Accumulated Deficit	Total
Balance January 1, 2010 (Note 18)	81,770,529	$ 36,977,430	$ 4,774,519	$ -	$ (11,486,815)	$ 30,265,134
Proceeds on exercise of options (Note 6(b))	886,182	223,143	-	-	-	223,143
Fair value of options exercised	-	77,426	(77,426)	-	-	-
Share-based compensation (Note 6(b))	-	-	63,404	-	-	63,404
Net loss	-	-	-	-	(688,991)	(688,991)
Balance, December 31, 2010 (Note 18)	82,656,711	$ 37,277,999	$ 4,760,497	$ -	$ (12,175,806)	$ 29,862,690
Proceeds on exercise of options (Note 6(b))	1,353,943	416,304	-	-	-	416,304
Fair value of options exercised	-	772,538	(772,538)	-	-	-
Share-based compensation (Note 6(b))	-	-	1,363,681	-	-	1,363,681
Private placement (Note 6(a)(i))	2,226,514	2,000,000	-	-	-	2,000,000
Private placement (Notes 6(a)(ii) and 7)	4,502,000	2,220,937	-	-	-	2,220,937
Share issue costs (Notes 6(a)(ii) and 7)	-	(354,741)	-	199,778	-	(154,963)
Net loss	-	-	-	-	(2,470,838)	(2,470,838)
Balance, December 31, 2011	90,739,168	$ 42,333,037	$ 5,351,640	$ 199,778	$ (14,646,644)	$33,237,811

Aquila Resources Inc.

CONSOLIDATED STATEMENTS OF CASH FLOWS
(Expressed in United States Dollars, unless otherwise stated)

	For the Years Ended December 31, 2011	2010
Cash flows from operating activities		
Net loss for the period	$ (2,470,838)	$ (688,991)
Adjustment for:		
Depreciation	18,420	19,563
Share-based compensation	1,012,186	63,404
Mineral properties write-off	114,038	-
	(1,326,194)	(606,024)
Changes in non-cash working capital (Note 10)	(216,738)	273,561
Cash flows used in operating activities	(1,542,932)	(332,463)
Cash flows from investing activities		
Increase in mineral properties	(8,440,839)	(5,127,347)
Mineral properties reimbursements	6,568,008	4,395,476
Additions to capital assets	(90,553)	-
Cash flows used in investing activities	(1,963,384)	(731,871)
Cash flows from financing activities		
Issuance of common shares, net of share issue costs	4,482,278	223,143
Cash flows provided from financing activities	4,482,278	223,143
Net increase (decrease) in cash	975,962	(841,191)
Cash and cash equivalents, beginning of period	950,662	1,791,853
Cash and cash equivalents, end of period	$ 1,926,624	$ 950,662

1. Nature of operations:

Aquila Resources Inc. (the "Company") was incorporated under the Business Corporations Act ("Canada") and is involved in the mineral exploration business. The Company's head office address is 65 Queen Street West, Suite 530, Toronto Canada, M5H 2M5.

The Company is listed on the Toronto Stock Exchange ("TSX") and 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.

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. Basis of Presentation:

These consolidated financial statements are the Company's first annual consolidated financial statements presented in accordance with International Financial Reporting Standards ("IFRS"). IFRS represents standards and interpretations approved by the International Accounting Standards Board ("IASB"), and are comprised of IFRSs, International Accounting Standards ("IASs"), and interpretations issued by the IFRS Interpretations Committee ("IFRICs") or the former Standing Interpretations Committee ("SICs").

An explanation of how the transition to IFRS with a transition date of January 1, 2010 has affected the reported financial position and financial performance of the Company is provided in Note 18. Note 18 includes reconciliations of the Company's consolidated balance sheets and consolidated statements of earnings and comprehensive income for comparative periods prepared in accordance with Canadian GAAP as previously reported to those prepared and reported in these consolidated financial statements in accordance with IFRS.

IFRS 1 - First-time Adoption of International Financial Reporting Standards ("IFRS 1") governs the first-time adoption of IFRS. IFRS 1 in general requires accounting policies under IFRS to be applied retrospectively to determine the opening balance sheet of the Company as of the transition date of January 1, 2010 ("Transition Date"), and allows certain exemptions which the Company has elected to apply as follows:

(i) On the Transition Date, the Company has elected not to retrospectively apply IFRS 2, Share-based Payment ("IFRS 2") to all share-based transactions at the date of transition. IFRS 2 will only be applied to equity instruments issued on or after, and that have not vested by the Transition Date.

(ii) The Company has elected not to retrospectively apply IFRS 3, Business Combinations, to any business combinations that occurred prior to the Transition Date.

3. Significant Accounting Policies:

The consolidated financial statements are expressed in US Dollars, except those amounts denoted CDN$ which are in Canadian Dollars.

The IASB continues to amend and add to current IFRS standards and interpretations with several projects underway. The significant accounting policies used in the preparation of these consolidated financial statements are as follows:

Translation of foreign currencies:

These consolidated financial statements are presented in US dollars, which is the functional and presentation currency of the Company. Foreign currency transactions are initially recorded in the functional currency at the transaction date exchange rate. At closing date, monetary assets and liabilities denominated in a foreign currency are translated into the functional currency at the closing date exchange rate, and non-monetary assets and liabilities at the historical rates. Exchange differences arising on the settlement of monetary items or on translating monetary items at rates different from those at which they were translated on initial recognition during the period are recognized in profit or loss.

Basis of measurement:

These consolidated financial statements have been prepared on a historical cost basis except items classified as FVTPL. In addition, these consolidated financial statements have been prepared using the accrual basis of accounting, except for cash flow information. All items were initially recorded at fair value.

Principles of consolidation:

These consolidated financial statements include the accounts of the Company and all of its subsidiaries. Subsidiaries are entities controlled by the Company. Control exists when the Company has the power to govern the financial and operating policies of an entity so as to obtain benefits from the entity's activities. Subsidiaries are included in the consolidated financial results of the Company from the effective date of acquisition up to the effective date of disposal or loss of control. The Company's principal subsidiary, Aquila Resources USA Inc., is located in Michigan USA. All inter-company balances and transactions have been eliminated.

Use of estimates:

The most significant estimates in these financial statements relate to mineral property costs, the recoverability of the carrying value of the mineral properties, the valuation of reclamation provisions, share-based compensation, income taxes and determination of the functional currency. Estimates are then based on historical experience and on various other assumptions that are believed to be reasonable under the circumstances. Actual results could be materially different from these estimates.

Impairment:

The carrying amounts of the Company's long-lived assets are reviewed at each reporting date to determine whether there is any indication of impairment. For the purpose of impairment testing, assets that cannot be tested individually are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups of assets (the group of assets so determined is referred to as a cash-generating unit, or "CGU").

3. Significant Accounting Policies: (Cont'd)

Impairment: (Cont'd)

An impairment exists when the carrying amount of the asset, or CGU, exceeds its recoverable amount. The impairment loss is the amount by which the carrying value exceeds the recoverable amount and such loss is recognized in the consolidated statement of comprehensive loss. The recoverable amount of an asset is the higher of its fair value less costs to sell and its value in use.

A previously recognized impairment loss is reversed if there has been a change in the estimates used to determine the asset's recoverable amount since the last impairment loss was recognized such that the recoverable amount has increased.

Deferred mineral property costs:

All costs incurred prior to obtaining the rights to explore a mineral property are expensed. Subsequent to obtaining the rights to explore its mineral properties the Company capitalizes all costs, net of any recoveries, during the evaluation and exploration and development stages. These costs will be amortized on the units-of-production basis over the estimated useful life of the properties following 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 are expensed as incurred.

The proceeds of options granted on a mining property are recorded as a reduction of the amounts recorded for mineral property costs and amounts exceeding cost are recorded as income.

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.

3. Significant Accounting Policies: (Cont'd)

Capital assets:

Capital assets consist of land and buildings, furniture fixtures and equipment which are initially recorded at cost. Depreciation is recorded using the following rates and methods:

Buildings	4%	Declining balance
Furniture, fixtures and equipment	20%	Declining balance

Depreciation on additions commences when assets are available for use.

Decommissioning, restoration and similar liabilities

The Company recognizes provision for statutory, contractual, constructive or legal obligations, including those associated with the reclamation of mineral properties and mineral assets under property, plant and equipment when those obligations result from the acquisition, construction, development or normal operation of the assets. Initially, a provision for decommissioning costs is recognized at the present value of management's best estimate of expenditure required to settle the present obligation at the balance sheet date. Upon initial recognition of the liability, the corresponding decommissioning cost is added to the carrying amount of the related asset and the cost is amortized as an expense over the economic life of the asset using either the unit-of-production method or the straight-line method, as appropriate. Following the initial recognition of the decommissioning costs, the carrying amount of the liability is increased for the passage of time and adjusted for changes to the current market-based discount rate, amount or timing of the underlying cash flows needed to settle the obligation.

The Company has no material decommissioning, restoration and similar liabilities as the disturbance to date is immaterial.

Revenue recognition:

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

Income taxes:

The Company accounts for and measures deferred tax assets and liabilities in accordance with the asset and liability method. Under this method, deferred tax assets and liabilities are recognized for the deferred tax consequences attributable to differences between the financial statement carrying amount of existing assets and liabilities and their respective tax bases. Deferred taxes are not recognized for the following temporary differences: the initial recognition of assets or liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable profit or loss, and differences relating to investments in subsidiaries and jointly controlled entities to the extent that it is probable that they will not reverse in the foreseeable future. Deferred 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 deferred 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. A deferred tax asset is recognized only to the extent that it is probable that future taxable profits will be available against which the asset can be utilized.

3. Significant Accounting Policies: (Cont'd)

Share-based compensation:

The Company has a stock option plan, which is described in Note 6(b). 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. The amount recognized as an expense is adjusted to reflect the actual number of share options for which the related services and non-market vesting conditions are met. Stock option compensation is recognized as an 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.

For equity-settled share-based payment transactions, the Company measures the goods or services received, and the corresponding increase in equity, directly, at the fair value of the goods or services received, unless that fair value cannot be estimated reliably, in which case, the Company measures their value, and the corresponding increase in equity, indirectly, by reference to the fair value of the equity instruments granted.

Basic and diluted loss per share:

The Company presents basic and diluted loss per share data for its common shares. Dilution is determined by adjusting the profit or loss attributable to common shareholders and the weighted average number of common shares outstanding for the effects of all dilutive potential common shares, which comprise convertible warrants and share options granted to directors, officers, employees, consultants and other service providers of the Company.

Financial instruments:

Assets or liabilities at fair value through profit or loss ("FVTPL")

Financial instruments classified as FVTPL assets or liabilities 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 cost 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 securities

Securities classified in the "Available-for-sale securities" category are non-derivative financial assets that are initially designated as available for sale or that are not classified in the "At fair value through profit or loss", "Held to maturity" or "Loans and receivables" categories. Available-for-sale securities can be sold further to or in view of fluctuations in interest rates, exchange rates, prices of equity instruments or changes in financing sources or terms, or to meet the liquidity needs of the Company.

Gains and losses resulting from changes in fair value, except for impairment losses and foreign exchange gains and losses, are recognized in the Consolidated Statements of Comprehensive Loss under "Net unrealized gains on available-for-sale securities" until the financial asset is derecognized. Premiums and discounts on the purchase of available-for-sale securities are amortized over the life of the security using the effective interest method and recognized in combined profit or loss.

3. Significant Accounting Policies: (Cont'd)

Classification of financial instruments:

The Company designates its cash and security deposits as FVTPL, 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 and advances for work to be performed are classified as other financial liabilities which are measured at amortized cost. Cash, accounts receivable, accounts payable and accrued liabilities and advances for work to be performed: due to the short-term nature of these instruments, their carrying value approximates their fair value. The fair value of the security deposits approximates its carrying value due to its interest rate approximating market rates.

Comprehensive income:

Comprehensive income, composed of net income and other comprehensive income, is defined as the change in shareholders' equity from transactions and other events from non-owner sources. Other comprehensive income ("OCI") includes unrealized gains and losses on available-for-sale securities, foreign currency translation adjustment and changes in the fair market value of derivatives designated as cash flow hedges, all net of related income taxes. The components of comprehensive income are disclosed in the statement of comprehensive income. Cumulative changes in other comprehensive income are included in accumulated other comprehensive income ("AOCI") which is presented as a category in shareholders' equity. As at December 31, 2011 and December 31, 2010 no other comprehensive income has been recognized.

Future accounting changes:

Certain pronouncements were issued by the IASB or the IFRIC that are mandatory for accounting periods after December 31, 2011 or later periods. Many are not applicable or do not have a significant impact to the Company and have been excluded below. The following have not yet been adopted and are being evaluated to determine their impact on the Company.

(i) IFRS 9 – Financial instruments ("IFRS 9") was issued by the IASB in October 2010 and will replace IAS 39 Financial Instruments: Recognition and Measurement ("IAS 39"). IFRS 9 uses a single approach to determine whether a financial asset is measured at amortized cost or fair value, replacing the multiple rules in IAS 39. The approach in IFRS 9 is based on how an entity manages its financial instruments in the context of its business model and the contractual cash flow characteristics of the financial assets. Most of the requirements in IAS 39 for classification and measurement of financial liabilities were carried forward unchanged to IFRS 9. The new standard also requires a single impairment method to be used, replacing the multiple impairment methods in IAS 39. IFRS 9 is effective for annual periods beginning on or after January 1, 2015.

(ii) IFRS 10 – Consolidated financial statements ("IFRS 10") was issued by the IASB in May 2011. IFRS 10 is a new standard which identifies the concept of control as the determining factor in assessing whether an entity should be included in the consolidated financial statements of the parent company. Control is comprised of three elements: power over an investee; exposure to variable returns from an investee; and the ability to use power to affect the reporting entity's returns. IFRS 10 is effective for annual periods beginning on or after January 1, 2013. Earlier adoption is permitted.

(iii) IFRS 11 – Joint arrangements ("IFRS 11") was issued by the IASB in May 2011. IFRS 11 is a new standard which focuses on classifying joint arrangements by their rights and obligations rather than their legal form. Entities are classified into two groups: parties having rights to the assets, and obligations for the liabilities, of an arrangement; and parties having rights to the net assets of an arrangement. Entities in the former case account for assets, liabilities, revenues and expenses in accordance with the arrangement,

3. Significant Accounting Policies: (Cont'd)

Future accounting changes: (Cont'd)

whereas entities in the latter case account for the arrangement using the equity method. IFRS 11 is effective for annual periods beginning on or after January 1, 2013. Earlier application is permitted.

(iv) IFRS 12 – Disclosure of interests in other entities ("IFRS 12") was issued by the IASB in May 2011. IFRS 12 is a new standard which provides disclosure requirements for entities reporting interests in other entities, including joint arrangements, special purpose vehicles, and off balance sheet vehicles. IFRS 12 is effective for annual periods beginning on or after January 1, 2013. Earlier application is permitted.

(v) IFRS 13 – Fair value measurement ("IFRS 13") was issued by the IASB in May 2011. IFRS 13 is a new standard which provides a precise definition of fair value and a single source of fair value measurement considerations for use across IFRSs. The key points of IFRS 13 are as follows:

- fair value is measured using the price in a principal market for the asset or liability, or in the absence of a principal market, the most advantageous market;
- financial assets and liabilities with offsetting positions in market risks or counter party credit risks can be measured on the basis of an entity's net risk exposure;
- disclosures regarding the fair value hierarchy has been moved from IFRS 7 to IFRS 13, and further guidance has been added to the determination of classes of assets and liabilities;
- a quantitative sensitivity analysis must be provided for financial instruments measured at fair value;
- a narrative must be provided discussing the sensitivity of fair value measurements categorized under Level 3 of the fair value hierarchy to significant unobservable inputs; and
- information must be provided on an entity's valuation processes for fair value measurements categorized under Level 3 of the fair value hierarchy.

IFRS 13 is effective for annual periods beginning on or after January 1, 2013. Earlier application is permitted.

(vi) IAS 1 – Presentation of financial statements ("IAS 1") was amended by the IASB in June 2011 in order to align the presentation of items in other comprehensive income with US GAAP standards. Items in other comprehensive income will be required to be presented in two categories: items that will be reclassified into profit or loss and those that will not be reclassified. The flexibility to present a statement of comprehensive income as one statement or two separate statements of profit and loss and other comprehensive income remains unchanged. The amendments to IAS 1 are effective for annual periods beginning on or after July 1, 2012.

(vii) IAS 27 – Consolidated and separate financial statements ("IAS 27") was amended by the IASB in May 2011. Consolidation requirements forming part of IAS 27 have been revised and are now contained in IFRS 10. The amendments to IAS 27 are effective for annual periods beginning on or after January 1, 2013. Earlier adoption is permitted.

(Expressed in United States Dollars, unless otherwise stated)

4. Mineral property costs:

Total accumulated deferred mineral property costs are detailed as follows:

Year ended December 31, 2011	Balance beginning of year	Acquisition	Exploration	Reimbursements	Re-allocations, Write-offs	Balance end of year
Back Forty Project	$27,651,097	$3,733,938	$1,610,664	$(5,505,452)	$85,352	27,575,599
Exploration						
Alliance	-	74,004	899,033	(1,062,556)	89,519	-
Michigan Gold	311,972	368,949	908,808	-	(84,653)	1,505,076
Reef	-	53,186	947,719	-	85,333	1,086,238
Other	274,203	76,000	120,033	-	(289,589)	180,647
	$28,237,272	$4,306,077	$4,486,257	$(6,568,008)	$(114,038)	$30,347,560

Year ended December 31, 2010	Balance beginning of year	Acquisition	Exploration	Reimbursements	Re-allocations, Write-offs	Balance end of year
Back Forty Project	$27,505,401	$2,308,414	$2,196,458	$(4,359,176)	$ -	$27,651,097
Exploration						
Alliance	-	-	36,300	(36,300)	-	-
Michigan Gold	-	31,162	280,810	-	-	311,972
Other	-	62,696	211,507	-	-	274,203
	$27,505,401	$2,402,272	$2,725,075	$(4,395,476)	$ -	$28,237,272

(a) Back Forty Project

The Back Forty Project controls approximately 7,600 (2010-9,300) acres of surface and mineral rights which are owned or held under lease or option by a 100% owned U.S. subsidiary and are subject to the HudBay Option and Joint Venture Agreement. 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. The entire project is subject to a 7% net distributable earnings royalty ("Net Profits after Payback") payable to a former joint venture partner.

4. Mineral property costs: (Cont'd)

(a) Back Forty Project (Cont'd)

HudBay Option and Joint Venture Agreement

On August 6, 2009, the Company signed a Subscription, Option and Joint Venture Agreement (the "Agreement") with HudBay Minerals Inc. ("HudBay"). Under the terms of the agreement, the following events came into effect:

i. HudBay subscribed for 12,141,051 common shares of the Company at $0.1827 per share for gross proceeds of CDN$2,218,170. These shares were subject to a four month hold period.

ii. While HudBay maintains at least a 10% ownership interest, HudBay has the right to nominate a director to the Company's Board of Directors and has pre-emptive rights to maintain its ownership interest. In addition, should HudBay choose to dispose of its equity interest in the Company, HudBay has agreed to do so in an orderly manner pursuant to the Agreement.

iii. HudBay has earned a 51% interest in the Back Forty Project (the "Project") by exceeding $10 million in aggregate expenditures on the Project over a 3 year period with a minimum of $3 million by the first anniversary, an additional US$3 million by the second anniversary, and an additional $4 million by the third anniversary (this obligation was fulfilled on August 31, 2010).

iv. Having earned its initial 51% interest, HudBay and the Company entered into a formal operating agreement reflective of their proportionate ownership interest in the Project on March 9, 2012 (see Note 17).

v. Having earned the initial 51% interest, HudBay has the option to increase its interest in the Project to 65% by funding and completing a feasibility study, funding and submitting a permitting application, and making outstanding specified option payments. A preliminary economic assessment is in progress.

vi. In the event a feasibility study is completed, permitting applications are submitted, HudBay elects to put the Project into production and issues a Development Notice, and permitting is obtained, the Company will have 90 days to arrange financing for its share of project costs. If the Company is unable to obtain financing, or elects not to do so, HudBay, by assuming the obligation to finance 100% of the development costs, will increase its ownership in the Project by a further 10% to a minimum of 75%. Pursuant to the Agreement, the Company's 25% share of the development costs would then be deducted from the Company's proportionate share from Net Proceeds of the Project.

vii. While HudBay retains the largest ownership interest in the Project, HudBay will be the manager and project operator. HudBay will also have exclusive marketing rights to sell production to HudBay or third parties on commercial terms.

(Expressed in United States Dollars, unless otherwise stated)

4. Mineral property costs: (Cont'd)

(a) Back Forty Project (Cont'd)

viii. If the feasibility study is not completed and all applications for permitting are not submitted on or before the fourth anniversary of the Agreement, the Company has the right to reacquire HudBay's 51% joint venture interest by reimbursing HudBay 50% of its total expenditures in respect of the Project incurred from the execution of the Agreement. If the Project is not brought into commercial production within four years from the grant of mining permits, the Company may reacquire HudBay's 65% joint venture interest by reimbursing HudBay 50% of its total Project expenditures incurred after execution of the Agreement. Notwithstanding the Company exercising the foregoing right, HudBay shall retain the marketing rights and the product rights as provided for in the Agreement. In addition, if the Company exercises its right after HudBay earns a 51% interest in the Project, then HudBay shall have its participating interest converted to a 1% NSR.

During 2009, in connection with securing the Agreement with HudBay, fees of $305,000 were paid to a consultant in cash, and 300,000 stock options were issued valued at CDN $60,600 using the Black Scholes option pricing model.

On August 31, 2010, pursuant to the Agreement, HudBay acquired a 51% interest in the Project. HudBay will act as operator of the joint venture with authority and discretion as to the exploration and potential development of the Project and will have exclusive rights to purchase and market the minerals produced from the property. Although called a joint venture in the Agreement, management has determined that a joint venture under applicable accounting standards does not exist. IAS 31 "Interest in Joint Ventures" requires the venturers to have joint control over the strategic financial and operating decisions of the venture for it to be considered a joint venture for accounting purposes. Under the Agreement the venturers do not have joint control.

At December 31, 2011 the Company maintained cash deposits in the amount of $166,111, pursuant to escrow agreements. The amounts are being held as security for the fulfillment of obligations in accordance with certain agreements pursuant to the Back Forty Project.

Future Back Forty Project commitments:

Estimated lease, option and property acquisition costs related to the Back Forty Project in each of the next five years, for which HudBay is materially liable throughout the duration of the agreement, are as follows:

2012	-	$1,575,741
2013	-	$2,244,581
2014	-	$1,527,195
2015	-	$1,557,852
2016	-	$148,509

(Expressed in United States Dollars, unless otherwise stated)

4. Mineral property costs: (Cont'd)

(b) Exploration Alliance

On October 15, 2010, the Company signed an Exploration Alliance agreement with HudBay. Under the agreement HudBay will fund exploration conducted by the Company (as Project Operator) in Michigan and other designated areas. HudBay made an initial payment to the Company of $250,000, which the Company used to identify exploration properties. The Company is obligated to present HudBay with a minimum of five exploration targets. Subject to an approval process under the agreement HudBay may fund any such target up to $2,000,000, following which the parties would form a 50/50 joint venture with respect to the target property. HudBay would then be able to increase its interest on each target to 65% by funding and completing a feasibility study and required mine permit applications.

During 2011 the Company presented five qualifying target properties to HudBay as required by the agreement. The Company and HudBay have agreed to proceed with four of them. HudBay has made a second payment to the Company of $250,000, which the Company is using to seek out another five target properties.

Future Exploration Alliance project costs:

Estimated lease and/or option costs related to the Exploration Alliance projects in each of the next five years are as follows:

2012	-	$106,912
2013	-	$127,862
2014	-	$140,862
2015	-	$18,412
2016	-	$22,823

(c) Michigan Gold

On October 21, 2010, the Company entered into an option agreement with Minerals Processing Corporation ("MPC"), a related party, to earn a 100% interest in certain surface and mineral rights located in Marquette County, Michigan. In order for the Company to earn a 100% interest in this property, the following commitments to MPC must be fulfilled by the Company:

Due Date	Cash payment		Share payment*	Exploration expenditures
October 21, 2010	$25,000	(Paid)	100,000	$ -
October 21, 2011	25,000	(Paid)	100,000	150,000
October 21, 2012	25,000		100,000	200,000
October 21, 2013	25,000		100,000	300,000
October 21, 2014	25,000		100,000	400,000
	$125,000		500,000	$ 1,050,000

* Instead of payment in stock, MPC may elect to receive $50,000 in lieu of 100,000 common shares of the Company. The minimum requirement for exploration expenditures for 2011 has been met by the Company. The October 21, 2010 and 2011 share payments have not been made; MPC has agreed to delay the due date to 2012 at Aquila's convenience and the option agreement is in good standing.

(Expressed in United States Dollars, unless otherwise stated)

4. Mineral property costs: (Cont'd)

(c) Michigan Gold (Cont'd)

In addition, to the above noted costs, in order to complete the 100% acquisition of the property, the Company must purchase the mineral and surface rights owned by MPC before the agreement expiry date of October 21, 2015. The property is comprised of: 332 acres of surface and mineral land, for which the purchase price is $1,300 per acre; 1,779 acres of mineral and mining rights only land, for which the purchase price is $1; and options to purchase 73 acres of surface overlying mineral and mining rights owned or leased, for which the purchase price is $1.

A net smelter royalty ranging from 1% to 4% is payable to MPC in the event of mineral production on the property.

MPC and the Company have common directors and officers.

Estimated lease and/or option costs related to the Michigan Gold Property are due in each of the next five years as follows:

2012	-	$57,560
2013	-	$58,760
2014	-	$61,760
2015	-	$62,960
2016	-	$70,120

(d) Reef

The Company entered into a series of agreements with private landholders in Marathon County Wisconsin for the optioning of surface and mineral rights. The agreements consist of mining leases and exploration agreements with an option to purchase. Currently there are a total of 729 acres under these agreements which have terms from 2 to 20 years up to 2031.

A net smelter royalty up to 2% is payable in the event of mineral production on the property.

Future Reef project costs:

Estimated lease and/or option costs related to the Reef Project in each of the next five years are as follows:

2012	-	$42,362
2013	-	$35,862
2014	-	$35,862
2015	-	$35,862
2016	-	$35,862

(Expressed in United States Dollars, unless otherwise stated)

4. Mineral property costs: (Cont'd)

(e) Other

The company has various other properties for which it owns exploration rights. Estimated related lease and/or option costs in each of the next five years are as follows:

2012	-	$90,000
2013	-	$12,000
2014	-	$14,000
2015	-	$16,000
2016	-	$ 9,000

5. Capital assets:

Cost	**Land**	**Buildings**	**Furniture and Fixtures**	**Total**
At January 1, 2010 and January 1, 2011	$ 405,880	$ 456,399	$ 32,808	$ 895,087
Additions	20,500	71,500	-	92,000
Disposals	-	-	(1,447)	(1,447)
December 31, 2011	$ 426,380	$ 527,899	$ 31,361	$ 985,640
Accumulated depreciation				
At January 1, 2010	$ -	$ (69,633)	$ (9,407)	$ (79,040)
Charge for the year	-	(15,000)	(4,563)	(19,563)
At January 1, 2011	-	(84,633)	(13,970)	(98,603)
Charge for the year	-	(14,871)	(3,549)	(18,420)
At December 31, 2011	$ -	$ (99,504)	$ (17,519)	$ (117,023)
Net book value				
December 31, 2011	**$ 426,380**	**$ 428,395**	**$ 13,842**	**$ 868,617**
December 31, 2010	$ 405,880	$ 371,766	$ 18,838	$ 796,484
January 1, 2010	$ 405,880	$ 386,766	$ 23,401	$ 816,407

6. Share capital:

(a) Common Shares

Authorized

The authorized capital stock of the Company consists of an unlimited number of common shares. Common share activity during the year was as follows:

i. In February 2011 the Company completed a non-brokered private placement of 2,226,514 common shares for proceeds of $2,000,000. The shares were purchased by HudBay.

(Expressed in United States Dollars, unless otherwise stated)

6. Share capital: (Cont'd)

ii. During December 2011, the Company completed a brokered private placement of 4,502,000 common shares for aggregate gross proceeds of $2,220,937 and incurred share issue costs of $354,741. Pursuant to the financing 515,140 broker warrants were issued.

(b) Stock-option and share-based compensation:

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 preceding the date the option is granted. The options are non-transferable.

As at December 31, 2011, common share stock options held by directors, officers, employees and consultants are as follows:

Number of options outstanding	CDN $ Exercise Price	Expiry Date	Number of options exercisable
1,200,000	2.15	February 8, 2012	1,200,000
1,292,000	0.15	March 2, 2014	1,292,000
791,250	0.25	November 10, 2014	791,250
1,645,000	0.90	February 2, 2016	1,645,000
4,928,250			4,928,250

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, 2011 have been valued at $1,363,681 (2010 - $63,404), of which $1,012,186 was expensed to loss, and $351,495 (2010 – Nil) was capitalized to the Mineral property exploration expenses. The following assumptions were used to value the options at the measurement date:

	2011	2010
Risk-free interest rate	**2.62%**	2.71%
Expected life	**5 years**	5 years
Price volatility (i)	**102%**	137%
Share price (CDN $)	**0.98**	0.25
Dividend yield	**Nil**	Nil

(i) The Company estimates the volatility of each stock option grant based on the Company's one year historical volatility prior to the grant.

(Expressed in United States Dollars, unless otherwise stated)

6. Share capital: (Cont'd)

(b) Stock-option and share-based compensation: (Cont'd)

A summary of the status of the Company's stock option plan as of December 31, 2011 and 2010, and changes during the periods are presented below:

	2011		2010	
	Options	Weighted average exercise Price (CDN $)	Options	Weighted average exercise Price (CDN $)
Balance outstanding January 1	**5,363,818**	**$ 0.70**	7,705,000	$ 0.73
Exercised	**(1,353,943)**	**0.30**	(886,182)	0.21
Expired	**(831,625)**	**0.86**	(1,455,000)	0.97
Granted	**1,750,000**	**0.90**	-	-
Balance outstanding December 31	**4,928,250**	**$ 0.90**	5,363,818	$ 0.70

7. Warrants:

As of December 31, 2011 there were 515,140 warrants issued and outstanding (December 31, 2010 – Nil) having a weighted average exercise price of CDN $0.51, and expiry dates between June 2012 and Oct 2014. The warrants were issued during the year in connection with the financing described in Note 6 (a)(ii) and issue costs in the amount of $15,656 were incurred. A grant date fair value of $215,434 was assigned to the warrants and reduced the share capital amount. The grant date fair value was determined using the Black-Sholes valuation model and the following assumptions – risk free interest rate 1.15%, expected life 3 years, price volatility 128.7%, share price $0.56 CDN, dividend yield nil. The Company estimated volatility based on the Company's one year historical volatility prior to the grant.

8. Related party transactions:

During the year ended December 31, 2011 management fees amounting to $65,137 (2010- $100,853) were charged by a company controlled by the CFO and a director of the Company.

During the year ended December 31, 2011 key management, and a related individual, received remuneration consisting of management fees and salaries. Total remuneration for the year amounted to $411,450 (2010-$327,800). There were no outstanding balances with these related parties at December 31, 2011 and December 31, 2010.

During the year a total of $466,993 (2010-$226,325) was billed to the Company by a geological consulting company of which the President and CEO and another director are major shareholders. The $446,993 was capitalized to the Mineral properties and is broken down as follows; $164,894 for lease and/or option payments, $199,733 for analytical services and sample preparation and analysis, $102,366 for other. As at December 31, 2011, accounts payable includes $Nil (December 31, 2010-$Nil; January 1, 2010 - $4,800) owing to this related party. All of the Michigan Gold properties, as described in Note 4, are optioned by this geological consulting company.

(Expressed in United States Dollars, unless otherwise stated)

8. Related party transactions: (Cont'd)

During the year, the Company was charged Directors' fees totaling $31,270 (2010- $32,222) by non-executive directors. Accounts payable includes $Nil (2010- $Nil) owing to these related parties.

During the year ended December 31, 2011 options were granted, with a Black Scholes value, to related parties as follows – key management and a related individual $701,322 (2010 - $Nil), Directors $467,548 (2010 - $Nil).

During the year, the Company was charged legal fees totaling $69,185 (2010-$38,503) by a law firm whose partner is an officer of the Company. As at December 31, 2011 accounts payable includes $Nil (2010-$Nil) due to this related party.

During the year rental expenditures in the amount of $14,400 (2010-$14,400) were charged by a Company with common directors. As of December 31, 2011, accounts payable includes $Nil (2010-$3,600) owing to this related party.

During the year exploration and evaluation expenditures in the amount of $6,568,008 (2010 - $4,395,476) were reimbursed by HudBay, a company that has an approximate 15.8% interest in the Company, and one member on its board of directors. The re-imbursement was pursuant to the terms of the HudBay Option and Joint Venture and the Exploration Alliance agreements described in Note 4. During the year HudBay purchased 2,226,514 common shares from the company as described in Note 6(a)i.

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.

9. Commitments:

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

2012	-	$64,200
2013	-	$32,000

10. Changes in non-cash working capital and other assets:

For the year ended December 31,	**2011**	2010
Accounts receivable	**$ (117,252)**	$ 6,785
Prepaid expenses	**3,930**	2,074
Security deposits	**(31,583)**	(15,064)
Accounts payable and accrued liabilities	**(111,022)**	68,955
Advance for work to be performed (i)	**39,189**	210,811
	$ (216,738)	$ 273,561

(i) The advance received in 2011 was $250,000 (2010 - $250,000).

11. Capital management:

The Company considers its capital to include all of the components of its 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 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, 2011.

12. 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, accounts receivable, and accounts payable and accrued liabilities and advance for work to be performed are comparable to their carrying value due to the relatively short period to maturity of these instruments. The fair value of the security deposits approximates carrying value due to its interest rate approximating market rates.

12. Financial instruments: (Cont'd)

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 cash and receivables included in current assets and security deposits. The Company has no material concentration of credit risk arising from operations. Cash and security deposits consists of bank deposits which have been invested with a Canadian Chartered Bank, from which management believes the risk of loss to be remote. 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, 2011, the Company had cash of $1,926,624 (December 31, 2010 - $950,662; January 1, 2010 - $1,791,853) to settle accounts payable and accrued liabilities of $62,337 (December 31, 2010 - $173,359; January 1, 2010 - $104,404). The ability of the Company to continue to pursue its exploration activities is dependent 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

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.

Sensitivity analysis

Based on management's knowledge and experience of the financial markets, the Company believes the following movements are "reasonably possible" over a three month period.

(a) The Corporation is exposed to foreign currency risk on fluctuations of financial instruments related to cash, accounts receivable, and accounts payable and accrued liabilities that are denominated predominantly in Canadian Dollars. Sensitivity to a plus or minus 10% change in the foreign exchange rate would affect net loss by approximately $167,000 (2010 - $20,000).

(Expressed in United States Dollars, unless otherwise stated)

12. Financial instruments: (Cont'd)

Sensitivity analysis (Cont'd)

(b) Commodity price risk could adversely affect the Company. In particular, the Company's future profitability and viability from mineral exploration depends upon the world market price of valuable minerals. Commodity prices have fluctuated significantly in recent years. There is no assurance that, even as commercial quantities of minerals may be produced in the future, a profitable market will exist for them.

As of December 31, 2011 the Company is not a producer of minerals. As a result, commodity price risk may affect the completion of future equity transactions such as equity offerings and the exercise of stock options. This may also affect the Company's liquidity and its ability to meet its ongoing obligations.

13. Income taxes:

(a) The Company's provision for income taxes differ from the amounts computed by applying the basic current rate of 28.25% (2010 – 27.4%) to the loss for the year before taxes, as shown in the following table:

		2011		2010
Statutory rate applied to loss for the year before income taxes	**$**	**(698,012)**	$	(198,455)
Increase (decrease) in taxes resulting from:				
Stock-based compensation cost		**285,943**		18,260
Capitalized stock options		**87,874**		-
Share issue costs		**(18,400)**		(124,305)
Change in rates and other items		**343,375**		919,616
Loss not tax-benefited		**(780)**		(615,116)
Deferred income tax (recovery)	**$**	**-**	$	-

(b) The tax effects of temporary differences that give rise to deferred income tax assets at December 31, 2011, December 31, 2010, and January 1, 2010 are as follows:

		December 31, 2011		December 31, 2010		January 1, 2010
Deferred tax assets:						
Non-capital losses carry forward	**$**	**5,338,724**	$	4,135,462	$	3,926,354
Mineral property		**(2,169,761)**		(1,015,931)		(491,932)
Capital assets		**(43,182)**		(92,298)		239
Share issue costs		**30,993**		129,861		337,549
		3,156,774		3,157,094		3,772,210
Tax benefit of losses not recognized		**(3,156,774)**		(3,157,094)		(3,772,210)
Net asset	**$**	**-**	$	-	$	-

(Expressed in United States Dollars, unless otherwise stated)

13. Income taxes: (Cont'd)

(c) The Company has non-capital losses of approximately $16,373,846 which expire through 2031. The benefit of these losses has not been recognized for financial statements purposes.

(d) During the year, the Company paid $ Nil (2010 - $Nil) in respect of income taxes.

14. 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:

		December 31, 2011	December 31, 2010	January 1, 2010
Canada	- current assets	**$ 1,765,704**	$ 896,299	$ 1,823,000
	- long term assets	**2,978,612**	2,988,791	2,989,000
Canada - total assets		**4,744,316**	3,885,090	4,812,000
United States	- current assets	**402,156**	182,277	105,626
	- long term assets	**28,403,676**	26,179,493	25,451,912
United States – total assets		**28,805,832**	26,361,770	25,557,538
Total assets		**$ 33,550,148**	$ 30,246,860	$ 30,369,538

The following table allocates net loss by segment:

Year ended December 31,	**2011**	2010
Canada	**$ (1,686,980)**	$ (422,285)
United States	**(783,858)**	(266,706)
Net loss	**$ (2,470,838)**	$ (688,991)

15. Supplemental cash flow information:

Non-cash activities were as follows:

	2011	2010
Fair value of options exercised reallocated from contributed surplus to share capital	**$ 772,538**	$ 77,426
Recovery of mineral property costs included in receivables	**$ -**	$ 62,012
Share based compensation capitalized to mineral properties	**$ 51,495**	$ -
Share issue costs – broker warrants	**$ 215,434**	$ -

16. Comparative Figures:

Certain comparative figures have been reclassified to conform to the current period's financial statement presentation.

17. Subsequent Event:

On March 9, 2012 the Company entered into an operating agreement with HudBay under which the Company transferred its interest in the Back Forty Project to a limited liability company. By entering into the agreement the Company has fulfilled its obligation under the HudBay Option and Joint Venture Agreement as described in Note 4 a) iv).

18. Transition to IFRS:

First-time adoption of IFRS:

The adoption of IFRS requires the application of IFRS 1, which provides guidance for an entity's initial adoption of IFRS on the first date at which IFRS was applied, which was January 1, 2010. IFRS 1 generally requires retrospective application of IFRS as effective at the end of its first annual IFRS reporting period. However, IFRS 1 also provides certain optional exemptions and mandatory exceptions to this retrospective treatment. The Company's elections have been disclosed in Note 2.

IFRS 1 does not permit changes to estimates that have been previously made. Accordingly, estimates used in the preparation of the Company's opening IFRS statements of financial position as at the Transition Date are consistent with those that were made under Canadian GAAP.

Changes to accounting policies:

The Company has changed certain accounting policies to be consistent with IFRS as is effective or available for adoption on December 31, 2011.

The following summarizes the results and adjustments to the Company's consolidated financial statements upon adoption of IFRS:

(a) Share-based payment

IFRS 2 requires each vesting tranche to be valued with unique assumptions, as if it were a separate grant, along with estimates on forfeitures based on historical trends experienced by the Company. Under IFRS, when a share-based payment award vests in installments over the vesting period (graded vesting), each installment is accounted for as a separate arrangement. Under prior Canadian GAAP, an entity can elect to treat the equity instruments as a pool and determine fair value using the average life of the instruments, and recognize the compensation cost on a straight-line basis, subject to at least the value of the vested portion of the award being recognized at each reporting date. Under IFRS, the Company uses an estimate of forfeitures based on historical trends experienced by the Company. Under prior Canadian GAAP no estimate was used, but rather actual forfeitures were accounted for as they occurred.

(b) Foreign currency translation

The Company and its subsidiaries determined their functional currency to be the US Dollar; under prior Canadian GAAP the Canadian Dollar was the functional currency. The exchange differences resulting from the change in functional currency were adjusted against deficit on the Transition Date.

There were no material adjustments to the previously reported statements of cash flows.

(Expressed in United States Dollars, unless otherwise stated)

18. Transition to IFRS: (Cont'd)

The January 1, 2010 Canadian GAAP statement of financial position is reconciled to IFRS as follows:

	Prior Canadian GAAP	Prior Canadian GAAP	IFRS Adjustment	Ref:	IFRS
	CDN$	**US $**	**US $**		**US $**
		(Note 18(b))			
Assets					
Current					
Cash	$ 1,866,125	$ 1,791,853	$ -		$ 1,791,853
Accounts receivable	105,063	100,882	-		100,882
Prepaid expenses	37,379	35,891	-		35,891
	2,008,567	1,928,626	-		1,928,626
Security deposits	124,415	119,464	-		119,464
Mineral property costs	30,120,135	27,505,401	-		27,505,401
Capital assets	976,180	816,407	-		816,047
	$ 33,229,297	$ 30,369,538	$ -		$ 30,369,538
Liabilities					
Current					
Accounts payable and accrued liabilities	$ 108,733	$ 104,404	$ -		$ 104,404
Shareholders' Equity					
Share capital	38,510,133	36,977,430	-		36,977,430
Contributed surplus	4,806,341	4,615,049	159,470	18(a)	4,774,519
Deficit	(10,195,910)	(11,327,345)	(159,470)	18(a)	(11,486,815)
	$ 33,229,297	$ 30,369,538	$ -		$ 30,369,538

(Expressed in United States Dollars, unless otherwise stated)

18. Transition to IFRS: (Cont'd)

The December 31, 2010 Canadian GAAP statement of financial position is reconciled to IFRS as follows:

	Prior Canadian GAAP	Prior Canadian GAAP	IFRS Adjustment	Ref:	IFRS
	CDN$	US $	US $		US $
		(Note 18(b))			
Assets					
Current					
Cash	$ 1,029,747	$ 950,662	$ -		$ 950,662
Accounts receivable	93,589	94,097	-		94,097
Prepaid expenses	33,636	33,817	-		33,817
	1,156,972	1,078,576	-		1,078,576
Security deposits	133,802	134,528	-		134,528
Mineral property costs	30,895,662	28,237,272	-		28,237,272
Capital assets	951,606	796,484	-		796,484
	$ 33,138,042	$ 30,246,860	$ -		$ 30,246,860
Liabilities					
Current					
Accounts payable and accrued liabilities	$ 384,952	$ 173,359	$ -		$ 173,359
Advance for work to be performed	219,549	210,811	-		210,811
Shareholders' Equity					
Share capital	38,819,709	37,277,999	-		37,277,999
Contributed surplus	4,882,017	4,729,027	31,470	18(a)	4,760,497
Deficit	(11,168,185)	(12,144,336)	(31,470)	18(a)	(12,175,806)
	$ 33,138,042	$ 30,246,860	$ -		$ 30,246,860

(Expressed in United States Dollars, unless otherwise stated)

18. Transition to IFRS: (Cont'd)

The Canadian GAAP statement of comprehensive loss for the year ended December 31, 2010 is reconciled to IFRS as follows:

	Prior Canadian GAAP	Prior Canadian GAAP	IFRS Adjustment	Ref:	IFRS
	CDN$	US $	US $		US $
		(Note 18(b))			
Expenses					
Depreciation	$ 25,306	$ 19,563	$ -		$ 19,563
Consulting fees	56,495	54,851	-		54,851
Directors' fees	33,188	32,222	-		32,222
Filing and regulatory fees	32,527	31,581	-		31,581
Foreign exchange loss (gain)	(9,489)	(68,146)	-		(68,146)
Interest and bank charges	3,872	3,759	-		3,759
Management fees	163,875	100,853	-		100,853
Office, general and administrative	95,168	87,338	-		87,338
Professional fees	70,492	68,441	-		68,441
Rent	14,400	13,981	-		13,981
Salaries and benefits	185,979	180,832	-		180,832
Share-based payment	197,137	191,402	(127,998)	18(a)	63,404
Travel and promotion	110,182	106,967	-		106,967
Loss before undernoted items	979,132	823,644	(127,998)		695,646
Interest income and other income	(6,857)	(6,655)	-		(6,655)
Net loss and comprehensive loss	$ 972,275	$ 816,989	$ (127,998)		$ 688,991
Basic and fully diluted loss per share	$ (0.01)	$ (0.01)	$ -		$ (0.01)
Weighted average number of shares	82,037,263	82,037,263	-		82,037,263