X-Terra Resources Corporation

(an exploration stage company)

Consolidated Financial Statements

December 31, 2009 and 2008

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April 30, 2010

Auditors' Report

To the Shareholders of
X-Terra Resources Corporation
(an exploration stage company)

We have audited the consolidated balance sheets of **X-Terra Resources Corporation** as at December 31, 2009 and 2008 and the consolidated statements of operations and deficit, comprehensive income 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, 2009 and 2008 and the results of its operations and its comprehensive income, deficit and cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

PricewaterhouseCoopers LLP[1]

[1] Chartered accountant auditor permit No. 14707

X-Terra Resources Corporation

(an exploration stage company)

Consolidated Balance Sheets

As at December 31, 2009 and 2008

	2009 $	2008 $
Assets		
Current assets		
Cash and cash equivalents (note 4)	2,609,361	4,296,385
Marketable securities (note 5)	1,008,570	-
Investments (note 6)	2,050,000	851,716
Accounts receivable (note 7)	179,525	78,721
Prepaid insurance	5,743	6,628
	5,853,199	5,233,450
Property, plant and equipment (note 8)	9,588	13,255
Mining and oil and gas properties (note 9)	996,655	988,074
Deferred exploration expenses (note 10)	492,336	377,451
	7,351,778	6,612,230
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities	35,482	49,258
Part XII.6 taxes payable	-	9,922
	35,482	59,180
Shareholders' Equity		
Share capital (note 11)	25,440,232	26,191,429
Warrants and brokers' options (note 11)	1,736,775	1,814,247
Contributed surplus (note 13)	2,070,212	1,153,105
Deficit	(22,772,724)	(22,625,731)
Accumulated other comprehensive income	841,801	20,000
	7,316,296	6,553,050
	7,351,778	6,612,230

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

Approved by the Board of Directors

Martin Dallaire (signed) Director
Martin Dallaire

Sylvain Champagne (signed) Director
Sylvain Champagne

X-Terra Resources Corporation

(an exploration stage company)

Consolidated Statements of Operations and Deficit

For the years ended December 31, 2009 and 2008

	2009 $	2008 $
Administrative expenses		
Insurance	8,133	14,921
Professional fees	44,492	93,214
General administrative expenses	285,606	343,124
Shareholders' communication	8,187	9,523
Transfer agent and regulatory fees	19,553	27,580
Stock-based compensation (note 12)	69,020	256,520
Amortization of property, plant and equipment	3,667	2,137
	438,658	747,019
Other expenses (income)		
Interest income	(28,480)	(76,555)
Extension of warrants (note 11)	60,198	-
Gain on sale of mining and oil and gas properties (note 9)	-	(835,766)
Unrealized loss (gain) on investments held for trading (note 6)	(198,284)	12,090
Transaction costs on investment held for trading	5,718	-
	(160,848)	(900,231)
Income (loss) before income taxes	(277,810)	153,212
Future income tax recovery (note 16)	130,817	-
Net income (loss) for the year	(146,993)	153,212
Deficit – Beginning of year	(22,625,731)	(22,778,943)
Deficit – End of year	(22,772,724)	(22,625,731)
Basic and diluted net income (loss) per share	(0.01)	0.02
Weighted average number of shares outstanding		
Basic	11,725,116	9,344,727
Diluted	11,725,116	9,344,727

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

X-Terra Resources Corporation

(an exploration stage company)

Consolidated Statements of Comprehensive Income

For the years ended December 31, 2009 and 2008

	2009 $	2008 $
Net income (loss) for the year	(146,993)	153,212
Other comprehensive income		
Unrealized gain on available-for-sale investments, net of related income taxes of $130,817 (2008 – nil) (note 6)	841,801	20,000
Comprehensive income for the year	694,808	173,212

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

X-Terra Resources Corporation

(an exploration stage company)

Consolidated Statements of Cash Flows

For the years ended December 31, 2009 and 2008

	2009 $	2008 $
Cash flows from		
Operating activities		
Net income (loss) for the year	(146,993)	153,212
Adjustments for		
Stock-based compensation (note 12)	69,020	256,520
Amortization of property, plant and equipment (note 8)	3,667	2,137
Extension of warrants	60,198	-
Gain on sale of mining and oil and gas properties (note 9)	-	(835,766)
Unrealized loss (gain) on investments held for trading (note 6)	(198,284)	12,090
Transaction costs on held-for-trading investments	5,718	-
Future income tax recovery	(130,817)	-
	(337,491)	(411,807)
Changes in non-cash operating working capital items (note 14)	(45,485)	(88,024)
	(382,976)	(499,831)
Financing activities		
Issuance of common shares and warrants and brokers' options	-	5,350,199
Share issue expenses	-	(571,325)
Purchase of shares under normal course issuer bid	(93,880)	(116,110)
	(93,880)	4,662,764
Investing activities		
Net acquisition of investments	(1,008,570)	-
Acquisition of property, plant and equipment	-	(15,392)
Acquisition of mining and oil and gas properties	(8,581)	(20,250)
Deferred exploration expenses	(193,017)	(303,262)
	(1,210,168)	(338,904)
Increase (decrease) in cash and cash equivalents during the year	(1,687,024)	3,824,029
Cash and cash equivalents – Beginning of year (note 4)	4,296,385	472,356
Cash and cash equivalents – End of year (note 4)	2,609,361	4,296,385

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

1 Nature of operations

X-Terra Resources Corporation (the "Company"), an exploration stage company, is in the business of acquiring, exploring and developing mining and oil and gas properties. It has interests in properties at the exploration stage located in Canada.

The Company is in the process of exploring its mining and oil and gas property interests and has not yet determined whether they contain mineral deposits that are economically recoverable. The Company will periodically have to find additional funds to continue its exploration activities, and while it has been successful in doing so in the past, there can be no assurance it will be able to do so in the future.

Until it is determined that properties contain mineral reserves or resources that can be economically mined, they are classified as exploration properties. The recoverability of deferred exploration expenses is dependent on the discovery of economically recoverable reserves and resources; securing and maintaining title and beneficial interest in the properties; the ability to obtain necessary financing to continue the exploration and development of its properties; and future profitable production or proceeds from the disposal of properties.

At the annual and special meeting of shareholders held on August 27, 2008 in Rouyn-Noranda, Quebec, shareholders approved a special resolution authorizing the continuance of the Company under the Canada Business Corporations Act. On September 4, 2008, the Company obtained a Certificate and Articles of Continuance under the Act, rendering the continuance effective.

As at December 31, 2009, the Company holds the Lindsay, Cool Lake, Rimouski, Rimouski North and Shawinigan properties and has cash and cash equivalents totalling $2,609,361 (2008 – $4,296,385) and working capital of $5,817,717 (2008 – $5,174,270).

2 New accounting policies

Accounting standards newly adopted

Effective January 1, 2009, the Company adopted an amendment to an accounting standard related to financial instruments, one new accounting standard related to goodwill and intangible assets and two new abstracts related to credit risk and the fair value of financial assets and financial liabilities and mining exploration costs that were issued by the Canadian Institute of Chartered Accountants ("CICA"). The CICA amendment, new standard and abstracts are as follows:

a) Section 3862, "Financial Instruments – Disclosures"

On January 1, 2009, the Company adopted an amendment to Section 3862 which establishes additional disclosure requirements regarding the level in the fair value hierarchy in which fair value measurements are categorized for financial assets and financial liabilities measured in the consolidated balance sheet.

b) Section 3064, “Goodwill and Intangible Assets”

In February 2008, the CICA issued Section 3064, which replaces Section 3062, “Goodwill and Other Intangible Assets”. This new Section provides guidance on the recognition, measurement, presentation and disclosure of goodwill and intangible assets. This new Section specifically excludes mining activities related to prospecting, acquisition of mineral rights, exploration, drilling and mineral development from being considered as intangible assets, as existing Section 3061, “Property, Plant and Equipment”, contains standards for the measurement, presentation and disclosure of mining properties. Adoption of this standard did not have any effect on the Company’s consolidated financial statements.

c) EIC-173, “Credit Risk and the Fair Value of Financial Assets and Financial Liabilities”

In January 2009, the CICA issued EIC-173, which provides guidance on how to take into account the credit risk of an entity and counterparty when determining the fair value of financial assets and financial liabilities, including derivative instruments. This Abstract applies to interim and annual financial statements relating to fiscal years beginning on or after January 1, 2009. Adoption of this Abstract did not have any effect on the Company’s consolidated financial statements.

d) EIC-174, “Mining Exploration Costs”

In March 2009, the CICA issued EIC-174, which provides guidance on the accounting and impairment review of exploration costs. This Abstract applies to interim and annual financial statements relating to fiscal years beginning on or after January 1, 2009. Adoption of this Abstract did not have any effect on the Company’s consolidated financial statements.

New accounting standards not yet adopted

e) Section 1601, “Consolidated Financial Statements”, and Section 1602, “Non-controlling Interests”

In January 2009, the CICA issued sections 1601 and 1602, which together replace Section 1600, “Consolidated Financial Statements”. Section 1601 establishes standards for the preparation of consolidated financial statements. Section 1602 establishes standards for accounting for a non-controlling interest in a subsidiary in consolidated financial statements subsequent to a business combination. It is equivalent to the corresponding provisions of International Accounting Standard 27 (Revised), “Consolidated and Separate Financial Statements”. The sections apply to interim and annual consolidated financial statements relating to fiscal years beginning on or after January 1, 2011. The Company is evaluating the impact of the adoption of these new sections on its consolidated financial statements.

f) Section 1582, "Business Combinations"

In January 2009, the CICA issued Handbook Section 1582, which replaces Section 1581 of the same title. Section 1582 establishes standards for accounting for a business combination and provides the Canadian equivalent to International Financial Reporting Standard 3 (Revised), "Business Combinations". The Section applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after January 1, 2011. Earlier application is permitted. The Company is evaluating the impact of the adoption of this new Section on the consolidated financial statements.

3 Significant accounting policies

Basis of accounting

These consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP"). The Canadian dollar is the functional and reporting currency used to measure the Company's operations.

Basis of consolidation

These consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries, Minera Reina Isabel, S.A. de C.V. ("Minera Reina") and Minera Tatemas, S.A. de C.V. ("Minera Tatemas"), which are currently inactive. All intercompany transactions and balances have been eliminated.

Use of estimates

The preparation of financial statements in conformity with Canadian GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Significant areas where management judgment is applied are assumptions and estimates relating to the useful life of assets for amortization purposes and for evaluation of their net recoverable amount, the valuation of mining and oil and gas properties and deferred exploration expenses, valuation allowances for future income taxes and the valuation of stock-based compensation and warrants and brokers' options. Actual results could differ from those estimates and such differences could be material.

Cash and cash equivalents

Cash and cash equivalents include cash on hand, bank balances and highly liquid short-term investments with original maturities of three months or less.

Investments

Investments consist of investments in shares and in warrants of a public company.

Investments that are shares of a public company are classified as available-for-sale investments. Warrants held by the Company are classified as investments held for trading. Transactions are recorded on the settlement date, and investments are recognized at fair value. Unrealized gains and losses are recorded, net of income taxes if any, in comprehensive income in the case of available-for-sale investments or in net income for investments held for trading. When available-for-sale investments are disposed of or impaired, these gains or losses are reclassified to net income (loss).

Property, plant and equipment

Property, plant and equipment are recorded at cost. Amortization is calculated to amortize the cost of the property, plant and equipment less their residual values over their estimated useful lives using the following method and rates:

	Method	Rate
Computer equipment/software	Declining balance	30%
Office furniture	Declining balance	20%

Amortization of property, plant and equipment related to exploration and development activities is capitalized to mining and oil and gas properties and deferred exploration expenses and are recognized in the consolidated statement of operations through amortization of mining and oil and gas properties when they are put into production. For those which are not related to exploration and development activities, amortization expense is recognized in the consolidated statement of operations.

Mining and oil and gas properties and deferred exploration expenses

Mining and oil and gas properties and deferred exploration expenses include rights in mining and oil and gas properties and deferred exploration costs and are recorded at acquisition cost less option payments received and other recoveries or at their fair value in the case of a devaluation caused by an impairment in value.

Exploration costs are deferred until the economic viability of the project has been established, at which time costs are added to mining properties. Costs are written off when properties are abandoned or when cost recovery is uncertain. Management has defined uncertainty as either there being no financial resources available from the Company or its joint venture partners for development of a mining or oil and gas property or results from exploration work not warranting further investment.

Proceeds from the sale of exploration properties are applied in reduction of related carrying costs, and any excess is recorded as a gain in the consolidated statement of operations. In the case of a partial sale, if carrying costs exceed the proceeds, only the losses are recorded.

Although management takes steps to verify title to mining and oil and gas properties in which the Company may have 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 unregistered prior agreements and be in non-compliance with regulatory requirements.

Mining and oil and gas property option agreements

Option payments are made at the discretion of the optionee and, accordingly, are accounted for when received. Option payments received are treated as a reduction of the carrying value of the related mining or oil and gas property and as deferred costs until the Company's costs are recovered. Option payments received in excess of costs incurred are credited to income.

Refundable tax credits for mining exploration expenses and mining duties

The Company is entitled to a refundable tax credit of 35% on qualified mining exploration expenses incurred in the province of Quebec. Furthermore, the Company is entitled to a refund of mining duties of 12% on qualified mining exploration expenses net of the refundable tax credit. Both credits are accounted for against the exploration expenses incurred.

Impairment of long-lived assets

Long-lived assets are reviewed for impairment upon the occurrence of events or changes in circumstances indicating that the carrying value of the assets may not be recoverable, as identified by comparing their net book value to the estimated undiscounted future cash flows generated by their use and eventual disposal. Impairment is measured as the excess of the carrying value over the fair value, determined principally by discounting the estimated net future cash flows expected to be generated from the use and eventual disposal of the related asset. In the event that the Company has insufficient information about its exploration properties to estimate future cash flows to test the recoverability of the capitalized costs, the Company will test for impairment by comparing the fair value to the carrying amount, without first performing a test for recoverability.

The amount shown as mining and oil and gas properties and deferred exploration expenses represents costs to date and does not necessarily reflect present or future values. Changes in future conditions could require material writedowns of the carrying amounts of the mining and oil and gas properties and deferred exploration expenses.

Income taxes

The Company provides for income taxes using the liability method of tax allocation. Under this method, future income tax assets and liabilities are determined based on deductible or taxable temporary differences between the accounting values and tax values of assets and liabilities using enacted or substantively enacted income tax rates expected to be in effect for the year in which the differences are expected to reverse. The Company establishes a valuation allowance against future income tax assets if, based on available information, it is more likely than not that some or all of the income tax assets will not be realized.

Flow-through shares

The Company finances a portion of its exploration expenses through the issuance of flow-through common shares. Under the terms of the flow-through share agreements, the resource expense deductions for income tax purposes are renounced to investors in accordance with the appropriate income tax legislation. The Company recognizes future income tax liability and reduces shareholders' equity when the expenses are renounced and when the renunciation forms are filed with the tax authorities.

Foreign currency transactions and integrated foreign subsidiaries

The financial statements of integrated foreign operations and transactions denominated in currencies other than the functional currency are translated into the functional currency using the temporal method. Under this method, monetary assets and liabilities in foreign currencies are translated into the functional currency at the exchange rates in effect at the balance sheet date. Non-monetary assets and liabilities are translated at historical rates, unless such assets and liabilities are carried at market value, in which case, they are translated at the exchange rate in effect at the balance sheet date. Income and expenses denominated in foreign currencies are translated at the rate of exchange prevailing on each transaction date. Gains and losses on translation are included in the consolidated statement of operations.

Income (loss) per share

The calculation of income (loss) per share is based on the weighted average number of shares outstanding for the year. Basic income (loss) per share is calculated by dividing the net income (loss) for the year by the weighted average number of common shares outstanding during the year. The computation of diluted income (loss) per share assumes the conversion, exercise or contingent issuance of securities only when such conversion, exercise or issuance would have a dilutive effect on income (loss) per share. The treasury stock method is used to determine the dilutive effect of the warrants, brokers' options and stock options. When the Company reports a loss, the diluted net loss per common share is equal to the basic net loss per common share because of the anti-dilutive effect of the outstanding warrants, brokers' options and stock options.

Share, warrant and brokers' option issue expenses

Share, warrant and brokers' option issue expenses are recorded as a decrease in share capital and warrants and brokers' options on the consolidated balance sheet in the year in which they are incurred.

Stock-based compensation

The Company applies the fair value method to account for options granted to its directors, officers, employees and consultants. Any consideration paid on exercise of stock options is credited to share capital. The stock compensation cost is stated as per the periods of option acquisition. Contributed surplus resulting from stock-based compensation is transferred to share capital when the options are exercised.

Financial instruments – Recognition and measurement

All financial instruments are required to be measured at fair value on initial recognition, except for certain related party transactions. Measurement in subsequent periods depends on whether the financial instrument has been classified as held for trading, available for sale, held to maturity, loans and receivables, or other liabilities.

- Financial assets and financial liabilities classified as held for trading are required to be measured at fair value, with changes in fair value recognized in net income (loss).
- Financial assets classified as held to maturity, loans and receivables, and financial liabilities (other than those held for trading) are required to be measured at amortized cost using the effective interest method.
- Available-for-sale financial assets are required to be measured at fair value, with unrealized gains and losses recognized in other comprehensive income. Fair value is based on the quoted market price at the reporting date. If there is a permanent decline in the fair value of the investment, the cumulative loss recognized in accumulated other comprehensive income is reclassified to net income (loss). An other than temporary decline in fair value is evidenced by significant and prolonged decline in fair value and adverse indications in the market and economic environment. Investments in equity instruments classified as available for sale that do not have a quoted market price in an active market are measured at cost.

The Company has adopted the following financial instrument classifications:

Financial instrument	**Classification**
Cash and cash equivalents	Held for trading
Money market funds	Held for trading
Interest income receivable	Loans and receivables
Marketable securities (bonds)	Held for trading
Investments (common shares of a public company)	Available for sale
Investments (warrants of a public company)	Held for trading
Accounts payable and accrued liabilities	Other liabilities

4 Cash and cash equivalents

	2009 **$**	**2008** **$**
Cash on hand and bank balances	608,168	796,385
Money market fund	2,001,193	-
Guaranteed investment certificates, bearing interest at a rate of 3.14%, matured in January 2009	-	3,500,000
	2,609,361	4,296,385

5 Marketable securities

	2009		**2008**	
Held for trading	**Carrying value $**	**Fair value $**	**Carrying value $**	**Fair value $**
Bonds				
Companies	499,925	499,925	-	-
Financial institutions	508,645	508,645	-	-
Total	1,008,570	1,008,570	-	-

a) Allocation of bonds by maturity date

	2009		
	3 years $	**5 years $**	**Total $**
Carrying value	508,645	499,925	1,008,570
Fair value	508,645	499,925	1,008,570

As at December 31, 2008, the Company had no investments in bonds.

b) Interest rate

The bonds bear interest at fixed rates ranging from 3.27% to 4.90%.

6 Investments

	2009		2008	
Investments available for sale	**Carrying value $**	**Fair value $**	**Carrying value $**	**Fair value $**
Common shares of public companies*	1,760,000	1,760,000	760,000	760,000
Investments held for trading				
Warrants of public companies*	290,000	290,000	91,716	91,716
	2,050,000	2,050,000	851,716	851,716

* These investments are the result of a transaction completed on October 28, 2008 between the Company and Brownstone Ventures Inc. ("Brownstone") to which the Company sold a 50% interest in exploration licences in exchange for 2,000,000 common shares and 2,000,000 common share purchase warrants. Each purchase warrant entitles the Company to purchase one common share of Brownstone at a price of $2 until October 28, 2010. The exploration licences sold are related to the Rimouski, Rimouski North and Shawinigan mining and oil and gas properties (note 9).

The fair value of warrants is determined through the use of Black-Scholes pricing models as they are not traded on any public stock exchange.

For the year ended December 31, 2009, the Company recognized an unrealized gain of $952,618 (2008 – $20,000) on common shares of a public company designated as available for sale in other comprehensive income and a $198,284 unrealized gain (2008 – loss of $12,090) on warrants of a public company classified as held for trading was included in net income (loss) for the year. Transaction costs of $47,382 and $5,718 have been recorded for available-for-sale investment in common shares and held-for-trading investment in warrants respectively.

7 Accounts receivable

	2009 $	**2008 $**
Refundable tax credits and mining duties	85,962	-
Sales taxes	9,695	55,838
Receivable from a partner	67,718	-
Advance for shale gas permits	16,150	-
Interest income receivable	-	22,883
	179,525	78,721

8 Property, plant and equipment

			2009
	Cost $	**Accumulated amortization** $	**Net** $
Computer equipment/software	11,952	4,841	7,111
Office furniture	3,440	963	2,477
	15,392	5,804	9,588

			2008
	Cost $	**Accumulated amortization** $	**Net** $
Computer equipment/software	11,952	1,793	10,159
Office furniture	3,440	344	3,096
	15,392	2,137	13,255

All property, plant and equipment are located in Canada.

9 Mining and oil and gas properties

Property	Number of claims/ permits	Undivided interest %	Balance – December 31, 2008 $	Net additions $	Balance – December 31, 2009 $
Lindsay[1]	25	100	977,863	581	978,444
Cool Lake	40	100	2,172	-	2,172
Rimouski[2]	2	50	2,010	1,994	4,004
Rimouski North[2]	3	50	2,643	2,629	5,272
Shawinigan[2]	3	50	3,386	3,377	6,763
			988,074	8,581	996,655

All mining and oil and gas properties are located in Canada.

(1) The Lindsay property comprises the former Villedieu and Lindsay properties, which have been combined because they are contiguous.

(2) On October 28, 2008, the Company entered into an agreement with Brownstone whereby Brownstone acquired a 50% interest in the exploration licences of the Rimouski, Rimouski North and Shawinigan properties in exchange for the issuance to the Company of 2,000,000 common shares valued at $740,000 and 2,000,000 common share purchase warrants valued at $103,806, for a total of $843,806. The gain on sale of mining and oil and gas properties of $835,766 was calculated net of the book value of the assets sold of $8,040. Pursuant to an operating agreement to be entered into by the Company and Brownstone, Brownstone will be the operator of an exploration program for the territories covered by the licences.

10 Deferred exploration expenses

Property	Undivided interest %	Balance – December 31, 2008 $	Additions $	Refundable tax credits and mining duties $	Balance – December 31, 2009 $
Lindsay (note 9[1])	100	346,865	119,395	(51,101)	415,159
Cool Lake	100	29,993	8,564	(3,665)	34,892
Rimouski (note 9[2])	50	593	24,197	(10,356)	14,434
Rimouski North (note 9[2])	50	-	27,708	(11,859)	15,849
Shawinigan (note 9[2])	50	-	20,983	(8,981)	12,002
		377,451	200,847	(85,962)	492,336

	2009 $	2008 $
Deferred exploration expenses		
Accommodations	14,000	23,832
Maps, printing and drafting	1,500	350
Consulting	-	-
Assay and geochemical analyses	2,177	8,135
Geology	106,298	217,757
Geophysics	71,409	62,966
Project management fees	5,463	16,981
	200,847	330,021
Deductions		
Refundable tax credits and mining duties	(85,962)	-
Increase in deferred exploration expenses	114,885	330,021
Balance – Beginning of year	377,451	47,430
Balance – End of year	492,336	377,451

11 Share capital and warrants and brokers' options

Capital management

The Company defines its capital as shareholders' equity. Its capital management objectives are to:

- have sufficient capital to be able to complete the Company's mining and oil and gas property exploration and mining development plan in order to ensure the growth of its activities; and
- have sufficient cash to fund exploration expenses, investing activities and working capital requirements.

Share capital

Authorized
Unlimited common shares without par value

Issued
Changes in the Company's share capital are as follows:

	Number of shares	Amount $
Balance – December 31, 2007	6,776,671	23,195,520
Private placement(1)	5,000,000	2,990,947
Purchased and cancelled(2)	(241,500)	(532,430)
Exercise of warrants(3)	377,999	390,251
Exercise of brokers' options(3)	27,999	27,213
Exercise of options (note 12)	62,400	119,928
Balance – December 31, 2008	12,003,569	26,191,429
Cancelled(2)	(50,000)	(97,205)
Purchased and cancelled(2)	(320,500)	(698,992)
Finder's fee(4)	150,000	45,000
Balance – December 31, 2009	11,783,069	25,440,232

Warrants and brokers' options

The following table details the changes in the Company's warrants and brokers' options:

			2009
	Number of warrants	**Number of brokers' options**	**Amount $**
Balance – Beginning of year	6,209,999	400,000	1,814,247
Finder's fee(4)	150,000	-	8,100
Extension of warrants(5)	-	-	60,198
Expired	(559,999)	-	(145,770)
Balance – End of year	5,800,000	400,000	1,736,775

			2008
	Number of warrants	**Number of brokers' options**	**Amount $**
Balance – Beginning of year	1,587,998	27,999	511,185
Private placement[1]	5,000,000	400,000	1,437,728
Exercised[3]	(377,999)	(27,999)	(134,666)
Balance – End of year	6,209,999	400,000	1,814,247

(1) On July 11, 2008, the Company completed a private placement of 5,000,000 units at a deemed price of $1 per unit for cash consideration of $5,000,000. Each unit consists of one common share and one common share purchase warrant. Each purchase warrant entitles the holder to purchase one common share at a price of $1.50 until July 11, 2010. From the total compensation received, $1,415,000 was assigned to warrants and $3,585,000 to share capital according to their estimated fair values.

Share issue expenses of $828,526 were incurred, of which $234,473 has been allocated to warrants and $594,053 to share capital. These share issue expenses include a fair value of $257,200 for 400,000 brokers' options, entitling the brokers to purchase 400,000 units at a price of $1 per unit until July 11, 2010. Each unit consists of one common share and one common share purchase warrant. Each purchase warrant entitles the holder to purchase one common share at a price of $1.50 until July 11, 2010.

The fair value of the brokers' options was estimated using a binomial pricing model based on the following assumptions: dividend yield of nil, volatility of 100%, risk-free interest rate of 3.18% and an expected life of two years. As a result, the fair value of the brokers' options was estimated at $257,200.

(2) For the year ended December 31, 2009, the Company purchased 320,500 (2008 – 241,500) of its own shares for cancellation for a cash consideration of $93,880 (2008 – $116,110), in connection with its normal course issuer bid. During 2009, 50,000 of the shares repurchased in 2008 were cancelled. Share capital has been reduced by the average issue price per share before buy-back of $2.18 (2008 – $2.16) totalling $796,197 (2008 – $532,430), of which $702,317 (2008 – $416,320) has been charged to contributed surplus.

(3) In 2008, 377,999 warrants and 27,999 brokers' options were exercised for cash consideration of $265,999 and $16,799 respectively, and a fair value of $124,252 and $10,414 respectively from these warrants and brokers' options has been reclassified on the balance sheet from warrants and brokers' options to share capital. No warrants and brokers' options have been exercised in 2009.

(4) On February 10, 2009, the Company issued 150,000 units to PowerOne Capital Markets Limited. Each unit consists of one common share and one common share purchase warrant representing transaction costs (note 6). Each purchase warrant entitles the holder to purchase one common share at a price of $1.50 until February 10, 2011. A value of $53,100 was assigned to the issuance of the units. Of this amount, $45,000 was assigned to the common shares and $8,100 to the warrants.

(5) On May 19, 2009, the Company extended the life of 650,000 existing warrants entitling the holder to acquire one common share at a price of $0.70 until May 28, 2010. These warrants have been valued at $60,198 using the Black Scholes pricing model with the following assumptions: risk free interest rate of 1.73%, average expected volatility of 106% and no amount of expected dividend per share.

Information relating to warrants and brokers' options outstanding as at December 31, 2009 is as follows:

Expiry date	**Number of warrants outstanding**	**Number of broker's options outstanding**	**Exercise price $**
May 2010	650,000	-	0.70
July 2010	-	400,000	1.00
July 2010	5,000,000	-	1.50
February 2011	150,000	-	1.50
	5,800,000	400,000	

Except for the brokers' options, the warrants, when granted, are accounted for at their fair value determined by the Black-Scholes pricing model, based on the vesting period and on the following weighted average assumptions:

	2009	**2008**
Average dividend per share	Nil	Nil
Volatility	110%	100%
Risk-free interest rate	1.18%	3.18%
Weighted average expected life	2 years	2 years
Weighted average fair value of warrants granted	$0.054	$0.280

Normal course issuer bid

The Company has instituted a normal course issuer bid through the facilities of the TSX Venture Exchange. Under the normal course issuer bid, which is effective from September 15, 2008 to September 14, 2009, the Company may repurchase for cancellation a maximum of 612,250 common shares over a 12-month period, representing approximately 5% of the "public float" of the Company's shares outstanding as at September 3, 2008. Purchases of common shares under the normal course issuer bid have been made at market prices and otherwise in accordance with the policies of the TSX Venture Exchange. The Company did not purchase any common shares during the 12 months preceding the normal course issuer bid.

The normal course issuer bid has been instituted because the Company considers the repurchase of common shares at certain market prices to be beneficial to the Company. The normal course issuer bid is being conducted through Desjardins Securities Inc. To the best of the Company's knowledge, no director or senior officer of the Company or their associates or affiliates currently intends to sell shares of the Company during the normal course issuer bid.

12 Stock options

In 2002, the Company adopted a stock option plan (the "Option Plan"), as amended, authorizing the granting of stock options to qualified optionees to purchase a total maximum of 10% of the number of outstanding issued common shares of the Company at any time. This is referred to as a "rolling plan". Under the Option Plan, the term of stock options granted may not exceed five years following the date of grant.

The Company applies the fair value method of accounting for stock options, and accordingly the fair value of the vested portion of stock options granted in 2009 of $69,020 (2008 – $256,520) has been included in administrative expenses.

The following table summarizes information relating to the share purchase options for the year ended December 31, 2009:

	Options outstanding	**Weighted average exercise price $**
Balance – December 31, 2008	822,500	1.49
Granted	290,000	0.50
Cancelled	(117,500)	1.53
Balance – December 31, 2009	995,000	1.20

Information relating to options outstanding and exercisable as at December 31, 2009 is as follows:

Exercise price $	Options outstanding	Weighted average remaining contracted life (years)	Options exercisable	Weighted average remaining contracted life (years)
1.10	60,000	2.45	60,000	2.45
1.90	375,000	3.42	375,000	3.42
1.00	270,000	3.66	270,000	3.66
0.50	290,000	4.50	290,000	4.50
	995,000	3.74	995,000	3.74

The options, when granted, are accounted for at their fair value determined by the Black-Scholes option pricing model based on the vesting period and on the following weighted average assumptions:

	2009	2008
Average dividend per share	Nil	Nil
Volatility	100%	98%
Risk-free interest rate	2.34%	3.17%
Weighted average expected life	5 years	5 years
Weighted average fair value of options granted	$0.238	$0.240

13 Contributed surplus

The following are the changes in the Company’s contributed surplus:

	2009 $	2008 $
Balance – Beginning of year	1,153,105	532,794
Stock-based compensation	69,020	256,520
Options exercised	-	(52,529)
Warrants expired	145,770	-
Shares cancelled	97,205	-
Shares purchased and cancelled	605,112	416,320
Balance – End of year	2,070,212	1,153,105

14 Cash flow information

The changes in non-cash operating working capital items are as follows:

	2009 $	2008 $
Increase in accounts receivable	(14,842)	(63,093)
Decrease (increase) in prepaid insurance	885	(6,628)
Decrease in restricted cash	-	500
Decrease in accounts payable and accrued liabilities	(21,606)	(28,725)
Increase (decrease) in Part XII.6 taxes payable	(9,922)	9,922
	(45,485)	(88,024)

For the year ended December 31, 2009, the Company's investments in deferred exploration expenses amounted to $200,847 (2008 – $330,021), of which $193,017 (2008 – $303,262) has been paid. Also, the Company accrued refundable tax credits and mining duties of $85,962 (2008 – nil).

15 Related party transactions

Related party transactions occurred in the normal course of business and were recorded at the exchange values, which is the consideration determined and agreed to by the related parties. Unless indicated otherwise, the following transactions are included in general administrative expenses:

	2009 $	2008 $
Leasing contract*	24,000	24,000
Management consulting fees charged by a company controlled by a director of the Company	72,000	54,000
Administrative service fees charged by a company controlled by a director of the Company	143,520	81,225
Administrative service fees charged by a company controlled by a director of the Company (included in share issue expenses as a reduction of share capital)	-	13,680
Consulting fees charged by a company controlled by two directors of the Company	-	50,000
Consulting fees charged by a company controlled by a director of the Company	-	8,000
	239,520	230,905

* The Company has entered into a lease for an office in Rouyn-Noranda with a company controlled by directors and officers of the Company.

16 Income taxes

A reconciliation of the combined Canadian federal and provincial income taxes at statutory rate and the Company's effective income tax expense are as follows:

	2009 $	2008 $
Income taxes at statutory rate	(85,843)	(47,343)
Non-deductible expense	6,195	80,470
Taxable capital gain on warrants	22,521	-
Effect of tax rate changes on future income taxes	246,331	98,430
Loss carryforwards expired	81,408	70,870
Other	(40,531)	-
Change in valuation allowance	(360,898)	(202,427)
Future income tax recovery	(130,817)	-

The components of future income tax assets are as follows:

	2009 $	2008 $
Resource assets	176,347	169,129
Non-capital loss carryforwards	386,491	349,212
Capital losses	1,539,187	1,788,089
Unrealized gain	(156,717)	(1,236)
Financing fees	147,160	148,172
	2,092,468	2,453,366
Less: Valuation allowance	(2,092,468)	(2,453,366)
Future income tax recovery	-	-

As at December 31, 2009, the Company has accumulated non-capital losses for income tax purposes amounting to approximately $1,437,000. These losses will expire as follows:

		$
Years ending December 31,	2010	46,000
	2014	65,000
	2015	85,000
	2026	91,000
	2027	348,000
	2028	349,000
	2029	453,000

The Company's balance of capital losses amounts to approximately $11,500,000 and can be carried forward indefinitely to be used against future capital gains.

The unamortized balance for tax purposes of share and warrant issue expenses amounting to approximately $547,000 is deductible over the next four years.

17 Financial instruments

The Company is exposed to various financial risks resulting from both its operations and its investment activities. The Company's management manages its financial risks. The Company does not enter into financial instrument agreements including derivative financial instruments for speculative purposes. The Company's main financial risk exposure and its financial risk management policies are as follows.

Interest rate risk

Interest rate risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate as a result of changes in market interest rates. Cash equivalents bear interest at fixed rates.

Other current financial assets and financial liabilities are not exposed to interest rate risk because they are non-interest bearing.

The Company does not use derivative financial instruments to mitigate its exposure to interest rate risk.

Credit risk

Credit risk is the risk that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss. The Company is subject to concentrations of credit risk through its cash and cash equivalents and accounts receivable. The Company reduces its credit risk by maintaining part of its cash and cash equivalents in financial instruments guaranteed by and held with a Canadian chartered bank. Investments in debt securities are made in quality corporate instruments with high credit ratings; therefore, the Company considers the risk of non-performance for investments in debt securities remote.

It is management's opinion that the Company is not exposed to significant credit risk.

Currency risk

It is management's opinion that the Company is not exposed to significant foreign exchange risk. As at December 31, 2009, all financial assets and financial liabilities are denominated in Canadian dollars, as are all its activities.

Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet the obligations associated with its financial liabilities. As at December 31, 2009, the Company had enough funds available to satisfy its obligations under accounts payable and accrued liabilities. All of the Company's financial liabilities have contractual maturities of less than three months and are subject to normal trade terms.

In the past few years, the Company has financed its liquidity needs primarily by issuing equity securities. As the Company has currently incurred operating losses, additional capital will be required to continue exploration activities on its properties (note 1).

Market risk

i) Fair value

The fair value of financial instruments is summarized as follows:

	2009		2008	
	Carrying value $	**Fair value $**	**Carrying value $**	**Fair value $**
Financial assets				
Held for trading				
Cash and cash equivalents	2,609,361	2,609,361	4,296,385	4,296,385
Marketable securities	1,008,570	1,008,570	-	-
Investments	290,000	290,000	91,716	91,716
Available for sale				
Investments	1,760,000	1,760,000	760,000	760,000
Loans and receivables				
Interest income receivable	-	-	22,883	22,883
Financial liabilities				
Other liabilities				
Accounts payable and accrued liabilities	35,482	35,482	49,258	49,258

Fair value estimates are made at the balance sheet date, based on relevant market information and other information about financial instruments.

ii) Fair value hierarchy

The following table summarizes the fair value hierarchy under which the Company's financial instruments are valued.

Level 1 includes unadjusted quoted prices in active markets for identical assets or liabilities. Level 2 includes inputs other than quoted prices included in Level 1 that are observable for the assets or liability, either directly or indirectly; and Level 3 includes inputs for the asset or liability that are not based on observable market data. For those fair value measurements included in Level 3 of the fair value hierarchy, a reconciliation from the opening balances to the closing balances has been provided.

				Assets measured at fair value As at December 31, 2009
	Level 1 $	**Level 2 $**	**Level 3 $**	**Total $**
Held for trading				
Cash on hand and bank balances	608,168	-	-	608,168
Money market funds	2,001,193	-	-	2,001,193
Marketable securities	-	1,008,570	-	1,008,570
Investments in warrants	-	-	290,000	290,000
	2,609,361	1,008,570	290,000	3,907,931
Available for sale				
Investments in common shares	1,760,000	-	-	1,760,000

	Reconciliation of long-term investments measured at fair value based on Level 3 inputs As at December 31, 2009
	$
Balance – beginning of year	91,716
Change in fair value	198,284
Balance – end of year	290,000