# Ona Power Corp.

## Financial Statements

## September 30, 2011

## INDEPENDENT AUDITOR'S REPORT

To the Shareholders of Ona Power Corp.:

We have audited the accompanying financial statements of Ona Power Corp. which comprises of the balance sheets as at September 30, 2011 and 2010, and the statements of loss, comprehensive loss and deficit and cash flows for the years then ended, and a summary of significant accounting policies and other explanatory information.

**Management's Responsibility for the Financial Statements**

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Canadian generally accepted accounting principles, and for such internal controls as management determines is necessary to enable the preparation of 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 these 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 financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the 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 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 controls. 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 financial statements.

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

**Opinion**

In our opinion, these financial statements present fairly, in all material respects, the financial position of Ona Power Corp. as at September 30, 2011 and 2010 and the results of its operations and its cash flows for the years then ended, in accordance with Canadian generally accepted accounting principles.

**Emphasis of Matter**

We draw attention to Note 1 to the financial statements, which describe certain conditions that give rise to substantial doubt about the entity's ability to continue as a going concern. The financial statements do not include any adjustments that might result from the outcome of this uncertainty. Our opinion is not qualified in respect of this matter.

/s/DMCL

DALE MATHESON CARR-HILTON LABONTE LLP
CHARTERED ACCOUNTANTS

Vancouver, Canada
January 25, 2012

**ONA POWER CORP.**
Balance Sheets
As at September 30, 2011 and 2010

| | | 2011 | | 2010 |
|---|---|---|---|---|
| **ASSETS** | | | | |
| **Current assets** | | | | |
| Cash and cash equivalents | $ | 114,391 | $ | 199,549 |
| Receivables | | 4,048 | | - |
| | | 118,439 | | 199,549 |
| **Equipment** (Note 3) | | - | | 1,043 |
| | $ | 118,439 | $ | 200,592 |
| **LIABILITIES** | | | | |
| **Current liabilities** | | | | |
| Accounts payable and accrued liabilities | $ | 14,907 | $ | 270,255 |
| Amount due to related party (Note 7) | | 20,000 | | 2,423 |
| | | 34,907 | | 272,678 |
| **SHAREHOLDERS' EQUITY (DEFICIT)** | | | | |
| **Share capital** (Note 4) | | 22,809,240 | | 22,581,024 |
| **Contributed surplus** (Note 4) | | 6,372,363 | | 6,165,546 |
| **Deficit** | | (29,098,071) | | (28,818,656) |
| | | 83,532 | | (72,086) |
| | $ | 118,439 | $ | 200,592 |

Going concern (Note 1)
Commitment (Note 10)

***Approved by the Board:***

*"Lucky Janda"*
Lucky Janda, Director

*"Rana Vig"*
Rana Vig, Director

*See accompanying notes to the financial statements*

**ONA POWER CORP.**
Statements of Loss, Comprehensive Loss and Deficit
For the years ended September 30, 2011 and 2010

| | | 2011 | | 2010 |
|---|---|---|---|---|
| **Expenses** | | | | |
| Amortization | $ | 1,043 | $ | 2,055 |
| Consulting and management fees (Note 7) | | 35,000 | | 104,387 |
| Impairment of exploration assets (Note 6) | | 169,713 | | - |
| Office and general | | 880 | | 23,065 |
| Occupancy and administration (Note 7) | | 25,000 | | 55,000 |
| Professional fees | | 22,247 | | 90,085 |
| Stock-based compensation (Note 4) | | 35,033 | | - |
| Transfer agent and filing fees | | 14,145 | | 18,774 |
| Travel | | 3,030 | | 4,781 |
| **Loss before other items** | $ | (306,091) | $ | (298,147) |
| **Other item** | | | | |
| Gain on debt settlement (Note 8) | | 26,676 | | - |
| **Loss from continuing operations** | | (279,415) | | (298,147) |
| **Discontinued operations** (Note 5) | | | | |
| Loss from discontinued operations, net of taxes | | - | | (1,579,448) |
| Loss from disposition of YPPC | | - | | (4,592,112) |
| | | - | | (6,171,560) |
| **Net loss and comprehensive loss** | | (279,415) | | (6,469,707) |
| Deficit, beginning | | (28,818,656) | | (22,348,949) |
| **Deficit, ending** | $ | (29,098,071) | $ | (28,818,656) |
| Basic and diluted loss per common share, from continuing operations | $ | (0.01) | $ | (0.26) |
| Basic and diluted loss per common share from discontinued operations | | - | | (0.08) |
| Weighted average number of common shares outstanding – basic and diluted | | 48,111,294 | | 18,985,450 |

*See accompanying notes to the financial statements*

**ONA POWER CORP**
Statements of Cash Flows
For the years ended September 30, 2011 and 2010

| | 2011 | 2010 |
|---|---|---|
| **Operating Activities** | | |
| Net loss from continuing operations | $ (279,415) | $ (298,147) |
| Non cash items | | |
| Gain on debt settlement | (26,676) | - |
| Amortization | 1,043 | 2,055 |
| Stock-based compensation | 35,033 | - |
| Impairment of exploration assets | 169,714 | - |
| Changes in non-cash working capital items | | |
| Receivables | (4,048) | 8,777 |
| Accounts payable & accrued liabilities | (228,672) | 330,241 |
| Used in continuing operations | (333,021) | 42,926 |
| Used in discontinued operations | - | (526,829) |
| | (333,021) | (483,903) |
| **Investing Activities** | | |
| Disposition of discontinued operations | - | (7,199) |
| Investing activities - discontinued operations | - | (56,239) |
| Exploration properties | (169,714) | - |
| | (169,714) | (63,438) |
| **Financing Activities** | | |
| Due to related parties | 17,577 | 2,423 |
| Net proceeds from share issuance and exercise of options | - | 1,584,001 |
| Repayment of loans and convertible debentures | - | (1,500,000) |
| Common shares issued for cash | 400,000 | - |
| Financing activities – discontinued operations | - | 102,923 |
| | 417,577 | 189,347 |
| Effect of exchange rate changes | - | (1,113) |
| **Change in cash during the year** | $ (85,158) | $ (357,994) |
| Cash, beginning | 199,549 | 558,656 |
| Cash, ending | $ 114,391 | $ 199,549 |
| Represented by | | |
| Cash – continuing operations | $ 114,391 | $ 199,549 |
| Cash – discontinuing operations | - | - |
| | $ 114,391 | $ 199,549 |
| **Supplementary cash flow information** | | |
| Cash paid for interest | $ - | $ 661,916 |
| Cash paid for income taxes | $ - | $ - |

*See accompanying notes to the financial statements*

## 1. NATURE OF OPERATIONS

Ona Power Corp. (the "Company") was incorporated under the Business Corporation Act of Alberta on August 31, 1998 and was continued to British Columbia on January 30, 2006. The Company's shares are publicly traded on the Frankfurt Exchange and Canadian National Stock Exchange.

The Company's principal business was the acquisition and development of power generation in China. On August 31, 2010, the Company entered into an agreement to dispose of its 60% ownership in its operating subsidiary, Yongxing Power Plant Corporation ("YPPC") (Note 5). The Company's current principal business activity is resource property exploration and development. On February 18, 2011, the Company acquired interests in two oil wells located in Tennessee, USA (Note 6).

**Going concern**
These financial statements have been prepared on a going concern basis which assumes that the Company will be able to realize its assets and discharge its liabilities in the normal course of business for the foreseeable future. The continuing operations of the Company are dependent upon its ability to raise adequate financing to develop its resource properties, and to commence profitable operations in the future. To date, the Company has not generated any revenue and is considered to be in the exploration stage. Management's plan includes continuing to pursue additional sources of financing through equity offerings, seeking joint venture partners to fund exploration, monitoring exploration activity and reducing overhead costs. As a result of its plans, management expects that the Company will have sufficient capital to fund operations. The financial statements do not include any adjustments relating to the recoverability and classification of recorded asset amounts and classification of liabilities that might be necessary should the Company be unable to continue in existence.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

**Basis of presentation**
These financial statements have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP") and are presented in Canadian dollars.

**Basis of consolidation**
These consolidated financial statements include the accounts of the Company and its wholly-owned subsidiary ("YPPC") up to date of disposition in fiscal 2010. All intercompany balances and transactions have been eliminated on consolidation.

**Use of Estimates**
The preparation of financial statements in conformity with 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. Actual results could differ from those estimates. Significant areas requiring the use of management estimates relate to determining the expected tax rates for future income taxes, the carrying value of resource properties, stock based transactions, asset retirement obligations and management's assumptions and estimates for going concern considerations.

**Loss per Share**
The Company uses the treasury stock method for the computation and disclosure of loss per share. The treasury stock method is used to determine the dilutive effect of stock options and other dilutive instruments which assume that proceeds received from in-the-money stock options are used to repurchase common shares at the prevailing market rate.

Basic and diluted net loss per share have been calculated using the weighted average number of shares outstanding during the period. Diluted loss per share figures are equal to those of basic loss per share for each period since the effects of the stock options and other dilutive instruments have been excluded as they are anti-dilutive.

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES** (continued)

**Financial Instruments**

The Company follows the Canadian Institute of Chartered Accountants ("CICA") Handbook Section 3855, Financial Instruments – Recognition and Measurement. Section 3855 prescribes when a financial instrument is to be recognized on the balance sheet and at what amount. Under Section 3855, financial instruments must be classified into one of five categories: held-for-trading, held-to-maturity, loans and receivable, available-for-sale financial assets, or other financial liabilities. All financial instruments, including derivatives, are measured at the balance sheet date at fair value except for loans and receivables, held-to-maturity investments, and other financial liabilities which are measured at amortized cost.

The Company's financial instruments consist of cash and cash equivalents, receivables, accounts payable and amounts due to a related party. Cash and cash equivalents are measured at face value, representing fair value, and are classified as held-for-trading. Receivables, which are measured at amortized cost, are classified as loans and receivables. Accounts payable and amounts due to a related party are measured at amortized cost and classified as other financial liabilities. The fair value of these financial instruments approximates their carrying values, unless otherwise noted.

The Company has determined that it does not have derivatives or embedded derivatives.

The CICA Handbook Section 3862, Financial Instruments – Disclosure, requires an entity to classify fair value measurements in accordance with an established hierarchy that prioritizes the inputs in valuation techniques used to measure fair value. The levels and inputs which may be used to measure fair value are as follows:

1. Level 1 – fair values are based on quoted prices (unadjusted) in active markets for identical assets or liabilities;
2. Level 2 – fair values are based on inputs other than quoted prices included in level 1 that are observable for the asset or liability, either directly (as prices) or indirectly (derived from prices); or
3. Level 3 – applies to assets and liabilities for inputs that are not based on observable market data, which are unobservable inputs.

Financial instruments classified as level 1 include cash and cash equivalents and accounts payable.

**Income Taxes**

Future income taxes are recorded using the asset and liability method whereby future tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of assets and liabilities and their respective tax bases. Future tax assets and liabilities are measured using the enacted or substantively enacted tax rates expected to apply when the asset is realized or the liability settled. The effect on future tax assets and liabilities of a change in tax rates is recognized in income in the period that substantive enactment or enactment occurs. To the extent that the Company does not consider it more likely than not that a future tax asset will be recovered, it provides a valuation allowance against the excess.

**Stock-based Compensation**

The Company grants options to purchase shares to employees or directors. The fair value of the options on the date of the grant is recognized as a compensation expense, with a corresponding increase in contributed surplus, over the period during which the related options vest. When options to purchase shares are granted to non-employees in return for goods or services, the fair value of the options granted is recognized as an expense, with a corresponding increase in contributed surplus, in the period in which the goods or services are received or are expected to be received. The consideration received on the exercise of share options is credited to share capital. When options are exercised, previously recorded compensation is transferred from contributed surplus to share capital to fully reflect the consideration for the shares issued.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

**Cash and equivalents**
Cash and cash equivalents consist of cash on deposit and short-term, highly liquid interest bearing investments that are readily convertible into known amounts of cash.

Cash and cash equivalents consist of:

| | September 30, 2011 | | September 30, 2010 | |
|---|---|---|---|---|
| Cash | $ | 13,424 | $ | 199,549 |
| Guaranteed investment certificates | | 100,967 | | - |
| Cash and cash equivalents | $ | 114,391 | $ | 199,549 |

**Resource Property Interests**

Full cost method
The Company follows the full cost method of accounting for oil and gas properties whereby all costs related to the exploration and development of oil and gas properties are capitalized in separate geographical cost centres. Costs of investigating properties not acquired are expensed to operations during the year. Gains or losses are not recognized upon disposition of oil and gas properties unless crediting the proceeds against accumulated costs would result in a change in the rate of depletion of 20% or more.

Capitalized costs will be depleted on the unit of production method based on estimated proven oil and gas reserves as determined by the Company and substantiated by independent professional engineers. Oil and gas reserves are converted to a common unit of measure on an energy equivalent basis of six thousand cubic feet (“mcf”) of gas to one barrel of oil. Costs of acquiring and evaluating unproven properties are excluded from depletion calculations until it is determined whether or not proven reserves are attributable to the properties or impairment occurs.

Ceiling test
The Company places a limit on the carrying value of oil and gas properties which may be depleted against revenues of future periods (the “ceiling test”). The carrying value is assessed to be recoverable when the sum of the undiscounted cash flows expected from the production of proved reserves, the lower of cost and fair value of unproved properties and the cost of major development projects exceeds the carrying value. When the carrying value is not assessed to be recoverable, an impairment loss is recognized to the extent that the carrying value of assets exceeds the sum of the discounted cash flows expected from the production of proved and probable reserves, the lower of cost and fair value of unproved properties and the cost of major development projects. The cash flows are estimated using expected future product prices and costs and are discounted using a risk-free interest rate. To date the Company’s properties are all classified as unproven.

**Asset retirement obligations**
The Company follows the CICA Handbook Section 3110, Asset Retirement Obligations. Section 3110 establishes standards for the recognition, measurement and disclosure of liabilities for asset retirement obligations and the associated asset retirement costs. The standard applies to potential statutory, regulatory, or civil obligations associated with the retirement of long-lived tangible assets that arise from the acquisition, construction, development or normal operation of such assets. The standard requires that a liability for an asset retirement obligation be recognized in the period in which it is identifiable and when a reasonable estimate of the fair value of the liability can be made. Furthermore, a corresponding asset retirement cost should be recognized by increasing the carrying amount of the related long-lived asset. The asset retirement cost will be allocated over the remaining life of the asset. Management has reviewed the Company's determinable or likely future obligations and retirement costs of long lived assets and has concluded that the Company does not have any asset retirement obligations.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

**Impairment of long-lived Assets**
Long-lived assets are reviewed for impairment losses whenever events or changes in circumstances indicate that the carrying amount may not be recoverable from the future undiscounted net cash flows expected to be generated by the asset. If the asset is not fully recoverable, an impairment loss would be recognized in that period for the difference between the carrying value of the asset and its estimated fair value based on discounted net future cash flows or quoted market prices.

**Foreign Currency Translation**
The financial statements are presented in Canadian dollars. Foreign denominated monetary assets and liabilities are translated to their Canadian dollar equivalents using foreign exchange rates which prevailed at the balance sheet date. Non-monetary items are translated at historical exchange rates. Revenue and expenses are translated at average rates of exchange during the year. Exchange gains or losses arising on foreign currency translation are included in the determination of operating results for the year.

**Equipment**
Equipment is recorded at cost and amortization is calculated on the declining balance basis at an annual rate of 30%.

**Recent Accounting Pronouncements**

International Financial Reporting Standards ("IFRS")

The Canadian Accounting Standards Board will require all public companies to use IFRS for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2011. Companies will be required to provide IFRS comparative information for the previous fiscal year. The transition from Canadian GAAP to IFRS will be applicable for the Company for the first quarters of fiscal year ending September 30, 2012 when the Company will prepare both the current and comparative financial information using IFRS. The Company has begun assessing the adoption of IFRS for 2011, the financial reporting impact of the transition to IFRS and initial adoption alternatives have not been determined.

Business Combination, Consolidated Financial Statements and Non-controlling interest

For interim and annual financial statements relating to fiscal years commencing on or after January 1, 2011, the Company will be required to adopt new CICA Section 1582 "Business Combinations", Section 1601 "Consolidated Financial Statements" and Section 1602 "Non-Controlling Interests". Section 1582 replaces existing Section 1581 "Business Combinations", and Sections 1601 and 1602 together replace Section 1600 "Consolidated Financial Statements". The adoption of Sections 1582 and collectively, 1601 and 1602 provides the Canadian equivalent to IFRS 3 "Business Combinations" and International Accounting Standard ("IAS") 27 "Consolidated and Separate Financial Statements" respectively. Management does not consider that the adoption of these standards will have a significant impact on the Company's financial statements.

## 3. EQUIPMENT

| | September 30, 2011 | | | September 30, 2010 | | |
|---|---|---|---|---|---|---|
| | Cost | Accumulated Amortization | Net Book Value | Cost | Accumulated Amortization | Net Book Value |
| Equipment | $ 10,812 | $ 10,812 | $ - | $ 10,812 | $ 9,769 | $ 1,043 |

## 4. SHARE CAPITAL

**Authorized**
Unlimited number of common shares without par value
Unlimited number of Class A Preferred Shares

**Issued**
Common shares

| | Number of Shares | | Amount |
|---|---|---|---|
| **Balance, September 30, 2009** | 18,792,573 | $ | 21,771,680 |
| Private placement | 23,466,666 | | 809,344 |
| **Balance, September 30, 2010** | 42,259,239 | | 22,581,024 |
| Private placement | 8,000,000 | | 228,216 |
| **Balance, September 30, 2011** | **50,259,239** | **$** | **22,809,240** |

In January 2011, the Company completed a private placement for gross proceeds of $400,000 and issued 8,000,000 units. Each unit consisted of one common share and one warrant of the Company. Each warrant entitles the holder to purchase a common share of the Company at $0.05 for a period of five years. The Company allocated $228,216 to common shares and $171,784 to the value of the warrants.

| Expiry Date | Exercise Price | Balance: September 30, 2010 | Issued | Expired | Balance: September 30, 2011 |
|---|---|---|---|---|---|
| March 10, 2011 | $ 2.50 | 3,506,553 | - | (3,506,553) | - |
| March 10, 2011 | $ 3.75 | 761,051 | - | (761,051) | - |
| August 11, 2011 | $ 0.20 | 10,333,300 | - | (10,333,300) | - |
| August 13, 2011 | $ 0.40 | 1,000,000 | - | (1,000,000) | - |
| September 27, 2012 | $ 0.075 | 23,466,666 | - | - | 23,466,666 |
| January 7, 2011 | $ 0.05 | - | 8,000,000 | - | 8,000,000 |
| Total | | 39,067,570 | 8,000,000 | 15,600,904 | 31,466,666 |

On September 30, 2011 the weighted average exercise price and the weighted average remaining life of the outstanding warrants are $0.07 and 1.83 years respectively (2010 - $0.41, 1.5 years).

The Company completed a non-brokered private placement on September 28, 2010 by issuing 23,466,666 units at a price of $0.075 per unit for proceeds of $1,760,000. Each unit consists of one common share and one common share purchase warrant. Each warrant entitles the holder to purchase one common share at $0.075 for a two-year period ending September 27, 2012. A finder's fee of $175,999 was paid.

The Company allocated $809,344 to common shares and $774,657 to the value of warrants. The fair value of the warrants was calculated using the Black-Scholes option pricing model and the following assumptions:

| | Year ended September 30, 2011 | Year ended September 30, 2010 |
|---|---|---|
| Risk-free interest rate | 2.53% | 1.45% |
| Expected volatility | 100% | 285% |
| Expected life | 5 years | 2 years |
| Dividend yield | 0% | 0% |

**Stock Options**

On March 1, 2011, 725,000 stock options were granted to various consultants, directors, and officers with an exercise price of $0.10 per share and exercisable for five years. The fair value of the options at the date of grant was $35,033.

| Expiry Date | Exercise Price | Balance: September 30, 2010 | Issued | Expired | Balance: September 30, 2011 |
|---|---|---|---|---|---|
| March 1, 2016 | $ 0.10 | - | 725,000 | - | 725,000 |

On September 30, 2011, the weighted average exercise price and weighted average remaining life of the Company's outstanding stock options are $0.10 and 4.42 years respectively.

The Black-Scholes option pricing model was used using the following assumptions:

| | |
|---|---|
| Risk-free interest rate | 2.6% |
| Expected volatility | 100% |
| Expected life | 5 years |
| Dividend yield | 0% |

| Contributed surplus | September 30, 2011 | September 30, 2010 |
|---|---|---|
| Opening balance, beginning | $ 6,165,546 | $ 5,390,889 |
| Stock options granted | 35,033 | - |
| Warrants | 171,784 | 774,657 |
| Closing balance, end of year. | $ 6,372,363 | $ 6,165,546 |

## 5. DISCONTINUED OPERATIONS

During the year ended September 30, 2010, Foothill Enterprise Ltd. ("Foothill") issued a notice of default to the Company requesting an immediate repayment of principal and accrued interest on convertible debentures totaling approximately $6,700,000. The Company did not have the liquidity and financial resources to meet the repayment demand. The Company reached an agreement with Foothill to fully settle the convertible debentures by assigning its 60% interest in YPPC and outstanding loans receivable to Foothill.

In the event of a successful sale of YPPC, Foothill will pay the Company the proceeds of the sale minus the amount of the convertible debentures plus accrued interest as at July 31, 2010 less the $1,500,000 cash payment paid and an administrative fee of $100,000.

## 6. RESOURCE PROPERTIES

On February 18, 2011, the Company entered into an agreement to purchase interests in two oil wells located in Tennessee, USA. The Company paid US$135,000 (CDN$134,772) in acquisition costs and incurred $34,941 in exploration activity costs during the year ended September 30, 2011.

Management has determined that both wells are not commercially viable and both interests have been fully impaired as at September 30, 2011.

## 7. RELATED PARTY TRANSACTIONS

During the year ended September 30, 2011, management and consulting fees of $35,000 (2010 – $104,387) and rent of $25,000 (2010 - $55,000) were charged by companies with a common director of the Company. Amounts due to a related party non-interest bearing, due on demand, and are unsecured.

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

## 8. DEBT SETTLEMENT

During the year ended September 30, 2010, the Company settled outstanding debt of $26,676 (2010 - $Nil) with their debtors and recognized a gain on the settlement of the same amount.

## 9. CAPITAL MANAGEMENT

The Company manages its capital, consisting of share and working capital, in a manner consistent with the risk characteristic of the assets it holds. All sources of financing are analyzed by management and approved by the board of directors.

The Company's objectives when managing capital are to safeguard the Company's ability to continue as a going concern.

The Company is meeting its objective of managing capital through preparing short-term and long-term cash flow analysis to ensure an adequate amount of liquidity. The Company is not subject to any externally imposed capital restrictions.

## 10. COMMITMENTS

As at September 30, 2011, the Company has a consulting agreement with a related party. The Company a monthly consulting fee of $5,000 on an ongoing basis until the agreement is terminated.

## 11. INCOME TAXES

The Company is subject to Canadian federal and provincial income taxes at an approximate rate of 28.50% (2010 – 28.88%). The reconciliation of the recovery for income taxes at the Canadian statutory rate compared to the Company's income tax expense as reported is as follows:

| | | 2011 | | 2010 |
|---|---|---|---|---|
| Loss from continued operations | $ | (279,415) | $ | (298,147) |
| Statutory tax rate | | 26.97% | | 28.88% |
| Expected income tax recovery at the statutory rate | | (75,358) | | (86,090) |
| Non-deductible items and other permanent | | 9,448 | | (2,205,583) |
| Expiration of non-capital losses | | - | | 63,342 |
| Effect of change in tax rates | | 4,814 | | 299,039 |
| Change in valuation allowance | | 61,096 | | 1,929,292 |
| **Total income tax recovery** | **$** | **-** | **$** | **-** |

Future income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Significant components of the Company's deferred assets and liabilities as of September 30, 2011 and 2010 are as follows:

| | 2011 | 2010 |
|---|---|---|
| **Future income tax assets** | | |
| Future income tax assets: | | |
| Non-capital losses carry-forward | $ 1,203,148 | $ 1,184,742 |
| Capital loss carry-forward | 1,855,342 | 1,855,342 |
| Mineral properties | 126,622 | 84,193 |
| Cumulative eligible capital | 66,786 | 66,786 |
| Equipment | 261 | - |
| Others | 106,154 | 106,154 |
| Total future income tax assets | 3,358,313 | 3,297,217 |
| Less: Valuation allowance | (3,358,313) | (3,297,217) |
| **Net future income tax assets** | **$ -** | **$ -** |

The Company has non-capital losses of approximately $4,812,594 which are available to reduce future taxable income in Canada and which expire between 2014 and 2031. The Company has not recognized any future benefit for these tax losses and resource and other available deductions, as it is not considered likely that they will be utilized. The expiration of these losses will occur as follows:

| Year | Amount |
|---|---|
| 2014 | $ 178,006 |
| 2015 | 145,848 |
| 2026 | 610,913 |
| 2027 | 677,234 |
| 2028 | 1,352,301 |
| 2029 | 1,203,313 |
| 2030 | 571,354 |
| 2031 | 73,625 |
| **Total** | $ 4,812,594 |

Tax declarations, together with other legal compliance areas (as examples, customs and currency control matters) are subject to review and investigation by a number of authorities, who are enabled by law to impose extremely severe fines, penalties and interest charges. The risk remains that the relevant authorities could take differing positions with regard to interpretive issues and the effect could be significant. The fact that a year has been reviewed does not close that year, or any tax declaration applicable to that year, from further review.

## 12. FINANCIAL INSTRUMENTS

*Financial Risk Management*
The Company is exposed in varying degrees to a variety of financial instrument related risks.

*Liquidity risk*
Liquidity risk arises through the excess of financial obligations over available financial assets due at any point in time. The Company's objective in managing liquidity risk is to maintain sufficient readily available reserves in order to meet its liquidity requirements.

*Interest rate risk*
Interest rate risk refers to the risk that fair values of future cash flows of a financial instrument will fluctuate due to changes in market interest rates. The Company is not exposed to significant 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's primary exposure to credit risk is on its cash and cash equivalents. Cash and cash equivalents are held with the same financial institution giving rise to a concentration of credit risk. This risk is managed by using a major Canadian bank that is a high credit quality financial institution as determined by ratings agencies. The Company's secondary exposure to credit risk is on its receivables. This risk is minimal as receivables consist primarily of refundable government sales taxes

*Currency risk*
Currency risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates. The Company is exposed to foreign currency fluctuations as certain expenditures incurred are denominated in US dollars. A significant change in the currency rates between the Canadian dollar relative to the US dollar could have an effect on the Company's results of operations, financial position and/or cash flows. The Company has not hedged its exposure to currency fluctuations.