

TALMORA DIAMOND INC.
(A Development Stage Company)

FINANCIAL STATEMENTS

DECEMBER 31, 2008 AND 2007

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AUDITORS' REPORT

To the Shareholders of
Talmora Diamond Inc.
(A Development Stage Company)

We have audited the balance sheets of Talmora Diamond Inc. as at December 31, 2008 and 2007 and the statements of operations, comprehensive loss and deficit and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

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

McGOVERN, HURLEY, CUNNINGHAM, LLP

A handwritten signature in black ink that reads 'McGovern, Hurley, Cunningham LLP'.

**Chartered Accountants
Licensed Public Accountants**

TORONTO, Canada
April 10, 2009, except for Note 13,
which is as at April 18, 2009

BALANCE SHEETS
AS AT December 31

	2008 \$	2007 \$
ASSETS		
CURRENT		
Cash and cash equivalents (Note 4)	38,606	336,423
Short-term investment (Note 5)	30,000	-
Sundry receivables	<u>13,585</u>	<u>35,079</u>
	82,191	371,502
DEFERRED MINERAL EXPLORATION COSTS (Notes 6 and 9)	998,677	874,447
FUTURE INCOME TAX ASSET (Note 8(b))	<u>-</u>	<u>15,000</u>
	<u>1,080,868</u>	<u>1,260,949</u>
LIABILITIES		
CURRENT		
Accounts payable and accrued liabilities (Note 9)	<u>29,351</u>	<u>46,909</u>
SHAREHOLDERS' EQUITY		
CAPITAL STOCK (Note 7(b))	1,175,274	1,225,724
WARRANTS (Note 7(c))	71,200	184,250
CONTRIBUTED SURPLUS (Note 7(e))	225,650	91,875
(DEFICIT)	<u>(420,607)</u>	<u>(287,809)</u>
	<u>1,051,517</u>	<u>1,214,040</u>
	<u>1,080,868</u>	<u>1,260,949</u>

GOING CONCERN (Note 1)

COMMITMENTS AND CONTINGENCIES (Notes 6 and 10)

APPROVED ON BEHALF OF THE BOARD:

Signed "Raymond Davies", Director

Signed "Richard Hogarth", Director

**STATEMENTS OF OPERATIONS, COMPREHENSIVE LOSS AND DEFICIT
FOR THE YEARS ENDED DECEMBER 31,**

	2008 \$	2007 \$
EXPENSES		
Administration (Note 9)	122,984	103,083
Stock-based compensation (Note 7(d))	29,725	91,875
Professional fees	25,788	65,467
Bank charges	<u>174</u>	<u>1,228</u>
Loss before the under-noted	178,671	261,653
Interest income	<u>(1,423)</u>	<u>(11,119)</u>
Net loss before income taxes	177,248	250,534
Income tax (recovery) (Note 8(a))	<u>(44,450)</u>	<u>(27,450)</u>
NET LOSS AND COMPREHENSIVE LOSS FOR THE YEAR	132,798	223,084
Deficit, beginning of year	<u>287,809</u>	<u>64,725</u>
Deficit, end of year	<u><u>420,607</u></u>	<u><u>287,809</u></u>
NET LOSS PER SHARE – basic and diluted	<u>0.006</u>	<u>0.013</u>
WEIGHTED AVERAGE NUMBER OF SHARES OUTSTANDING – basic and diluted	<u>21,774,935</u>	<u>17,026,912</u>

STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31

	2008 \$	2007 \$
CASH FLOWS FROM OPERATING ACTIVITIES		
Net (loss) for the year	(132,798)	(223,084)
Changes not involving cash		
Income tax (recovery)	(44,450)	(27,450)
Stock-based compensation	29,725	91,875
Changes in non-cash working capital balances:		
Decrease (increase) in sundry receivables	21,494	(26,988)
Increase (decrease) in accounts payable and accrued liabilities	<u>1,664</u>	<u>(1,384)</u>
Cash flows from operating activities	<u>(124,365)</u>	<u>(187,031)</u>
CASH FLOWS FROM FINANCING ACTIVITIES		
Private placements, net of costs	<u>(6,475)</u>	<u>538,000</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Cash acquired in reverse take-over, net of costs (Note 3)	-	59,633
Short-term investment	(30,000)	153,646
Deferred mineral exploration costs, net of recoveries	<u>(136,977)</u>	<u>(651,688)</u>
Cash flows from investing activities	<u>(166,977)</u>	<u>(438,409)</u>
(Decrease) in cash and cash equivalents	(297,817)	(87,440)
Cash and cash equivalents, beginning of year	<u>336,423</u>	<u>423,863</u>
Cash and cash equivalents, end of year	<u><u>38,606</u></u>	<u><u>336,423</u></u>
SUPPLEMENTAL INFORMATION		
Interest paid	-	-
Income taxes paid	-	-
Change in accrued exploration expenditures	(12,747)	11,311
Change in accrued share issue costs	(6,475)	6,475
Common shares issued in reverse take-over (Note 3)	-	138,218

1. NATURE OF OPERATIONS AND GOING CONCERN

Canadian Diamind Limited and Talmora Resources Inc. amalgamated on January 23, 2007 to continue as Talmora Diamond Inc. (the "Company"). In accordance with EIC-10 "Reverse Takeover Accounting" of the Canadian Institute of Chartered Accountants ("CICA") Handbook, the substance of the transaction was a capital transaction and was accounted for as a reverse takeover ("RTO"), since Canadian Diamind Limited was identified as the acquirer (see Note 3).

The Company is a development stage company as defined by CICA Accounting Guideline 11 "Enterprises in the Development Stage" and currently has interests in exploration and development properties in Canada. Substantially all of the Company's efforts are devoted to financing and developing these properties. There has been no determination whether the Company's interests in mineral properties contain mineral reserves, which are economically recoverable

Although the Company has taken steps to verify title to the properties on which it is conducting exploration and 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 unregistered prior agreements and non-compliance with regulatory requirements.

The business of exploring for minerals involves a high degree of risk and there can be no assurance that current exploration programs will result in profitable mining operations. The recoverability of the carrying value of exploration properties and the Company's continued existence is dependent upon the preservation of its interest in the underlying properties, the discovery of economically recoverable reserves, the achievement of profitable operations, or the ability of the Company to raise alternative 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.

As at December 31, 2008, the Company had cash, cash equivalents and short-term investments totaling \$68,606 and working capital of \$52,840. Management of the Company believes that it has sufficient funds to pay its ongoing administrative expenses and to meet its liabilities for the ensuing year as they fall due. However, over the longer term, the Company's ability to continue operations and fund its exploration property expenditures is dependent on management's ability to secure additional financing. Management is actively pursuing such additional sources of financing, 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. Because of this uncertainty there is some doubt about the ability of the Company to continue as a going concern. These financial statements do not include the adjustments that would be necessary should the Company be unable to continue as a going concern. Such adjustments could be material.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting policies of the Company are in accordance with Canadian generally accepted accounting principles and their basis of application is consistent with that of the previous year, except as disclosed below. Outlined below are those policies considered particularly significant:

Cash and Cash Equivalents

Cash and cash equivalents include cash on hand and balances with banks net of bank overdrafts, cashable guaranteed investment certificates, and highly liquid temporary investments with original maturities of less than ninety days.

Short-Term Investments

Short-term investments comprise highly liquid Canadian dollar investments with original terms to maturity of greater than ninety days but not more than one year.

Deferred Mineral Exploration Costs

The cost of mineral properties and related exploration expenditures are deferred until the properties to which they relate are placed into production, sold or allowed to lapse. These costs will be amortized over the estimated useful life of the properties following commencement of production or written off if the properties are sold or allowed to lapse. The Company does not accrue future costs to keep the properties in good standing. Administrative expenditures are charged to operations as incurred.

The Company reviews its mineral properties to determine if events or changes in circumstances have transpired which indicate that the carrying value of its assets may not be recoverable. 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. An impairment loss is recognized when the carrying amount of the mineral properties is not recoverable and exceeds its fair value. 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.

Asset Retirement Obligations

The Company follows the CICA accounting standard on "Asset retirement obligations". Under the standard the Company is required to record a liability for the estimated future costs associated with legal obligations relating to the reclamation and closure of its mineral exploration properties. This amount is initially recorded at its discounted present value with subsequent annual recognition of an accretion amount on the discounted liability. An equivalent amount is recorded as an increase to exploration properties and deferred exploration expenditures and is amortized over the useful life of the property. Management is not aware of any asset retirement obligations as at December 31, 2008 and 2007.

Flow-Through Financing

The Company has financed a portion of its exploration activities through the issue of flow-through shares, which transfer the tax deductibility of exploration expenditures to the investor. Proceeds received on the issue of such shares have been credited to capital stock and the related exploration costs have been charged to deferred mineral exploration costs.

Resource expenditure deductions for income tax purposes related to exploration and development activities funded by flow-through share arrangements are renounced to investors in accordance with income tax legislation. When these expenditures are renounced, temporary taxable differences created by the renunciation will reduce share capital.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Income Taxes

The Company follows the asset and liability method of accounting for income taxes. Under this method, future income tax assets and liabilities are determined based on differences between the financial statement carrying values and the income tax bases of assets and liabilities, and are measured using the substantively enacted income tax rates and laws that are expected to be in effect when the temporary differences are expected to reverse. The effect on future income tax assets and liabilities of a change in income tax rates is recognized in the period that includes the date of enactment or substantive enactment of the change. When the future realization of income tax assets does not meet the test of being more likely than not to occur, a valuation allowance in the amount of the potential future benefit is taken and no net asset is recognized.

Stock-Based Compensation

The Company records compensation cost based on the fair value method of accounting for stock-based compensation. The fair value of stock options is determined using the Black-Scholes option pricing model. The fair value of the options is recognized over the vesting period as compensation expense and contributed surplus. When options are exercised, the proceeds received, together with any related amount in contributed surplus, will be credited to capital stock.

Loss Per Share

Basic loss per share is calculated using the weighted average number of common shares outstanding. Diluted loss per share is calculated using the treasury stock method. In order to determine diluted loss per share, the treasury stock method assumes that any proceeds from the exercise of dilutive stock options and warrants would be used to repurchase common shares at the average market price during the period, with the incremental number of shares being included in the denominator of the diluted loss per share calculation. The diluted loss per share calculation excludes any potential conversion of options and warrants that would increase earnings per share or decrease loss per share.

Use of Estimates

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make certain 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 related reported amounts of revenue and expense during the period. Significant estimates include the valuation of the deferred mineral exploration costs, stock-based compensation, warrants and future tax assets and liabilities. Actual results could differ from estimates. Management believes that the estimates are reasonable.

New Accounting Pronouncements:

Capital Disclosures

In December 2006, the CICA issued Section 1535, "Capital Disclosures", which establishes guidelines for the disclosure of information on an entity's capital and how it is managed. Effective January 1, 2008, this enhanced disclosure enables users to evaluate the entity's objectives, policies and processes for managing capital. The Company has included this disclosure in Note 11 to the financial statements.

Financial Instruments - Disclosure and Presentation

In December 2006, the CICA issued Section 3862, "Financial Instruments - Disclosure", and Section 3863, "Financial Instruments - Presentation" to replace the existing Section 3861 "Financial Instruments - Disclosure and Presentation". Section 3862 requires enhanced disclosure on the nature and extent of financial instrument risks and how an entity manages those risks. Section 3863 carries forward the existing presentation requirements and provides additional guidance for the classification of financial instruments. These sections are effective January 1, 2008. The Company has included this disclosure in Note 12 to the financial statements.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

New Accounting Pronouncements: (Continued)

Mining Exploration Costs

On March 27, 2009, the AcSB issued EIC-174 "Mining Exploration Costs". In this EIC the Committee provided additional guidance for an enterprise that has initially capitalized exploration costs and has an obligation in the current and subsequent accounting periods to test such costs for recoverability whenever events or changes in circumstances indicate that its carrying amount may not be recoverable. The EIC should be applied to financial statements issued after March 27, 2009. The Company has adopted EIC-174 in these financial statements.

Future Accounting Pronouncements:

International Financial Reporting Standards ("IFRS")

In January 2006, the CICA Accounting Standards Board ("ACSB") adopted a strategic plan for the direction of accounting standards in Canada. As part of that plan, accounting standards in Canada for public companies are expected to converge with IFRS by 2011. The Company continues to monitor and assess the impact of the convergence of Canadian GAAP and IFRS.

Credit Risk and the Fair Value of Financial Assets and Financial Liabilities

In January 2009, the CICA approved EIC 173 Credit Risk and the Fair Value of Financial Assets and Financial Liabilities. This guidance clarified that an entity's own credit risk and the credit risk of the counterparty should be taken into account in determining the fair value of financial assets and financial liabilities including derivative instruments. This guidance is applicable to fiscal periods ending on or after January 12, 2009. The Company is continually evaluating its counterparties and their credit risks.

3. AMALGAMATION

Effective January 23, 2007, pursuant to a letter of intent dated June 30, 2005 and a definitive amalgamation agreement dated July 31, 2006, Canadian Diamind Limited amalgamated with Talmora Resources Inc., a junior capital pool company formed under the rules of the Alberta Stock Exchange, and continued under the name Talmora Diamond Inc.. Talmora Resources Inc. was de-listed from the TSX Venture Exchange on July 3, 2001 for failure to complete listing requirements. Pursuant to the amalgamation agreement, shares of the Company were issued on the basis of one post-amalgamation share for each pre-amalgamation share of Talmora Resources Inc. and one post-amalgamation share for every five pre-amalgamation shares of Canadian Diamind Limited. Holders of common share purchase warrants in the capital of Canadian Diamind Limited received 3,250,000 common share purchase warrants in the capital of the Company. Each whole warrant of the Company entitled the holder to acquire one share of the Company for \$0.16 until June 30, 2008.

Immediately after amalgamation, former shareholders of Canadian Diamind Limited held 68.6% of the common shares of the amalgamated company and Canadian Diamind Limited was deemed the acquirer for accounting purposes. The substance of the transaction was a capital transaction and was accounted for as a reverse takeover in accordance with EIC-10 "Reverse Takeover Accounting" of the CICA Handbook.

This transaction is a "related party transaction" for the purposes of Ontario Securities Commission Rule 61-501 as the President who is also a director of Talmora Resources Inc. and a director of Canadian Diamind Limited, owns 14.4% and 10.9% of the issued and outstanding shares of Talmora Resources Inc. and Canadian Diamind Limited, respectively. The transaction is exempt from the related party valuation and minority security holder approval requirements of the OSC Rule on the basis that no securities of Talmora Resources Inc. were listed or quoted on any specified markets.

3. AMALGAMATION (Continued)

Based on the audited December 31, 2006 balance sheet of Talmora Resources Inc., the net assets at estimated fair market value that were combined with Canadian Diamind Limited were as follows:

Cash	\$ 87,899
Amounts receivable	5,655
Deferred transaction costs	57,168
Current liabilities	(15,571)
Future tax assets	<u>62,700</u>
Net assets acquired	<u>\$ 197,851</u>

Additional related transaction costs of \$28,266 were recorded as a share issue cost during the year ended December 31, 2007.

4. CASH AND CASH EQUIVALENTS

	2008	2007
	\$	\$
Cash and cash equivalents are composed of		
Cash	32,772	311,423
Guaranteed Investment Certificates, bearing interest at 2.5% (2007 - 3.4%)	<u>5,834</u>	<u>25,000</u>
	<u>38,606</u>	<u>336,423</u>

5. SHORT-TERM INVESTMENT

As at December 31, 2008, the Company had short-term investments of \$30,000 bearing interest at 2.75% with a maturity date of June 8, 2009.

6. DEFERRED MINERAL EXPLORATION COSTS

In 2003, the Company acquired the Horton River property, consisting of three prospecting permits in the Horton River area in the Inuvialuit settlement region of the Northwest Territories. The property is 120 kilometers south of Paulatuk, a village located on the Arctic coast, about 400 kilometers east of Inuvik. These permits lapsed on January 31, 2008 and during the year ended December 31, 2008 the Company staked 50 claims within the same area covered by these expired permits. These claims are in good standing until October 2012 or later.

In 2007, the Company acquired a further nine prospecting permits adjoining the Horton River property of which six permits in the Sahtu Settlement Region are valid until January 31, 2011, and the remaining three permits in the Inuvialuit Settlement Region are valid until January 31, 2012. Two of the six Sahtu permits are in good standing to 2011. Future cash deposits of \$57,947 or work of equal value are required by January 31, 2010 on four of the six Sahtu permits to maintain them in good standing to 2011 and future cash deposits of \$85,993 or work of equal value are required by January 31, 2011 on the three Inuvialuit permits to maintain them in good standing to 2012.

In 2008, the Company acquired four new prospecting permits, which are valid until January 31, 2012. Future cash deposits of \$28,974 or work of equal value are required by January 31, 2010 and further cash deposits of \$57,947 or work of equal value are required by January 31, 2011 to maintain these permits in good standing to 2012.

Claims can be staked within the permits at any time so long as the permits are in good standing. All the Company's permits and claims are located on Crown Land straddling the boundary between the Inuvialuit and Sahtu Settlement Regions of the Northwest Territories.

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6. DEFERRED MINERAL EXPLORATION COSTS (Continued)

On February 28, 2008, the Sahtu Secretariat Inc. and a number of other applicants (collectively, the "Applicants") in the Sahtu Settlement Region applied for a judicial review of the decision of the Supervising Mining Recorder to issue 60 prospecting permits within the Sahtu Settlement Region on February 1, 2008. Four of the permits were those issued to Talmora. The Applicants claim that they were insufficiently consulted and accommodated by the Supervising Mining Recorder before the permits were issued. The Minister of Indian Affairs and Northern Development and the Supervising Mining Recorder intend to oppose the application. This application does not affect the adjoining nine permits and 50 claims held by Talmora.

HORTON RIVER, NWT	<u>\$</u>
<u>Acquisition costs:</u>	
Balance, December 31, 2006	22,000
Staking	<u>63,952</u>
Balance, December 31, 2007 and 2008	<u>85,952</u>
<u>Exploration expenditures</u>	
Balance, December 31, 2006	189,448
Permits and legal	15,491
Consulting	1,175
Geophysical airborne survey	330,017
Summer exploration program	<u>252,364</u>
Balance, December 31, 2007	788,495
Supplies and freight	2,167
Sample sorting, analyses	67,148
Field office support	48,139
Exploration	<u>6,776</u>
Balance, December 31, 2008	<u>912,725</u>
Total Balance, December 31, 2008	<u>998,677</u>

7. CAPITAL STOCK

a) Authorized

Unlimited number of common shares

b) Issued

	Common Shares #	Amount \$
Balance, December 31, 2006	11,252,830	710,932
Common shares issued in reverse take-over (Note 3)	5,142,105	197,851
Common shares issued for cash (i)	170,000	17,000
Flow-through common shares issued for cash (i)	1,130,000	113,000
Warrant valuation (i)	-	(21,000)
Common shares issues for cash (ii)	3,160,000	316,000
Flow-through common shares issued for cash (ii)	920,000	92,000
Warrant valuation (ii)	-	(59,200)
Share issue costs	-	(72,309)
Renunciation of flow-through expenditures (iv)	<u>-</u>	<u>(68,550)</u>
Balance, December 31, 2007	21,774,935	1,225,724
Renunciation of flow-through expenditures (iv)	<u>-</u>	<u>(50,450)</u>
Balance, December 31, 2008	<u>21,774,935</u>	<u>1,175,274</u>

(i) In April 2007, the Company closed a private placement financing for 170,000 non-flow-through units and 1,130,000 flow-through units at a price of \$0.10 per unit for total gross proceeds of \$130,000. Each unit consisted of one common share and one-half of one common share purchase warrant. Each whole common share purchase warrant will be exercisable at \$0.16 per common share until April 18, 2009.

The grant date fair value of the warrants of \$21,000 was estimated using the Black-Scholes option pricing model with the following assumptions: expected dividend yield of 0%; expected volatility of 100%; risk free interest rate of 4.1%; and expected life of two years.

(ii) On December 28, 2007, the Company closed another private placement financing for 3,160,000 non-flow-through units and 920,000 flow-through units at a price of \$0.10 per unit for total gross proceeds of \$408,000. Each unit consists of one common share and one-half of one common share purchase warrant. Each whole common share purchase warrant will be exercisable at \$0.20 per common share until December 28, 2009.

The grant date fair value of the warrants of \$59,200 was estimated using the Black-Scholes option pricing model with the following assumptions: expected dividend yield of 0%; expected volatility of 100%; risk free interest rate of 4.1%; and expected life of two years.

(iii) On June 12, 2007, shareholders of the Company entered into an escrow agreement relating to 5,654,935 common shares of the Company and 525,000 common share purchase warrants. As at December 31, 2008, 2,544,720 common shares and 78,750 warrants were held in escrow of which 1/3 of the remaining escrowed securities were released on January 26, 2009, 1/2 of the remaining escrowed securities will be released July 26, 2009 and the remaining escrowed securities will be released January 26, 2010.

(iv) During the year ended December 31, 2008, the Company renounced flow-through expenditures in the amount of \$205,000 (2007 - \$370,000) with respect to flow-through financings that occurred during the year ended December 31, 2007 (2007 - year ended December 31, 2006), creating a future income tax liability of \$59,450 (2007 - \$120,250), of which \$50,450 (2007 - \$68,550) was allocated as a cost of issuing the flow-through shares and \$9,000 (2007 - \$51,700) was allocated as a cost of issuing warrants.

Continued...

7. CAPITAL STOCK (Continued)

c) Warrants

A summary of changes in warrants is as follows:

	Warrants	Weighted Average Exercise Price	Value
	#	\$	\$
Balance, December 31, 2006	3,250,000	0.160	155,750
Issued (Note 7(b)(i))	650,000	0.160	21,000
Issued (Note 7(b)(ii))	2,040,000	0.200	59,200
Renunciation of flow-through expenditures (Note 7(b)(iv))	<u>-</u>	-	<u>(51,700)</u>
Balance, December 31, 2007	5,940,000	0.174	184,250
Expired	(3,250,000)	0.160	(104,050)
Renunciation of flow-through expenditures (Note 7(b)(iv))	<u>-</u>	-	<u>(9,000)</u>
Balance, December 31, 2008	<u>2,690,000</u>	0.19	<u>71,200</u>

As at December 31, 2008, the following warrants were issued and outstanding:

<u>Number of warrants</u>	<u>Exercise Price</u>	<u>Value</u>	<u>Expiry date</u>
#	\$	\$	
650,000	0.16	18,640	April 18, 2009
<u>2,040,000</u>	0.20	<u>52,560</u>	December 28, 2009
<u>2,690,000</u>	0.19	<u>71,200</u>	

d) Options

The Company has a stock option plan under which officers, directors, employees, and consultants are eligible to receive stock options. The aggregate number of shares to be issued upon exercise of all options granted under the plan may not exceed 10% of the outstanding shares of the Company. Options granted under the plan generally have a term of five years and vest at terms to be determined by the directors at the time of grant. The exercise price of each option is fixed by the board of directors but shall not be less than the price permitted by any stock exchange on which the Company's common shares may be listed which is generally the trading price of the Company's stock at or about the grant date of the options.

A summary of changes in stock options is as follows:

	Options	Weighted Average Exercise Price
	#	\$
Balance, December 31, 2006	-	
Issued	<u>1,600,000</u>	0.10
Balance, December 31, 2007 and 2008	<u>1,600,000</u>	0.10

The weighted average grant date fair value of the options issued during the year ended December 31, 2007 was \$0.076. The fair value of the options was estimated using the Black-Scholes option pricing model with the following assumptions: expected dividend yield of 0%; expected volatility of 100%; risk free interest rate of 4.1%; and expected life of five years.

Continued...

7. CAPITAL STOCK (Continued)

d) Options (continued)

As at December 31, 2008, the following options were issued and outstanding:

<u>Options Granted</u>	<u>Options Vested</u>	<u>Exercise Price</u>	<u>Expiry date</u>
#	\$	\$	
<u>1,600,000</u>	<u>1,600,000</u>	0.10	April 25, 2012

e) Contributed Surplus

	Amount
	\$
Balance, December 31, 2006	-
Employee stock based compensation	69,768
Non-employee stock based compensation	<u>22,107</u>
Balance, December 31, 2007	91,875
Employee stock based compensation	22,572
Non-employee stock based compensation	7,153
Expiration of warrants (Note 7(c))	<u>104,050</u>
Balance, December 31, 2008	<u>225,650</u>

8. INCOME TAXES

a) Provision for Income Taxes

Major items causing the Company's income tax rate to differ from the federal statutory rate of approximately 34% (2007 – 36.1%) are as follows.

	<u>2008</u>	<u>2007</u>
	\$	\$
(Loss) before taxes:	<u>(177,248)</u>	<u>(250,534)</u>
Expected income tax (benefit)	(59,400)	(90,200)
Adjustments to benefit resulting from:		
Stock-based compensation	10,000	33,000
Expiry of losses	6,300	16,200
Other	(8,850)	-
Change in expected tax rate	6,600	13,550
Change in valuation allowance	<u>900</u>	<u>-</u>
Income tax (recovery)	<u>(44,450)</u>	<u>(27,450)</u>

Continued...

8. INCOME TAXES (Continued)

b) Future Tax Balances

The tax effects of temporary differences that give rise to future income tax assets and liabilities are as follows:

	<u>2008</u>	<u>2007</u>
	\$	\$
Future income tax assets (liabilities):		
Mineral exploration properties	(62,800)	(56,000)
Non-capital loss carry-forwards	41,500	47,000
Share issue and transaction costs	<u>22,200</u>	<u>24,000</u>
	900	15,000
Valuation allowance	<u>(900)</u>	<u>-</u>
Future income tax asset	<u><u>-</u></u>	<u><u>15,000</u></u>

c) Tax Loss Carry-Forwards

As at December 31, 2008, the Company had approximately \$59,700, \$86,000 and \$636,000 of foreign exploration, Canadian development and Canadian exploration expenditures respectively, which under certain circumstances, may be utilized to reduce taxable income of future years.

As at December 31, 2008, the Company had available for deduction against future taxable income, non-capital losses of approximately \$143,000 which expire as follows:

2009	\$ 42,000
2010	27,000
2013	30,000
2025	38,000
2028	<u>6,000</u>
	<u>\$ 143,000</u>

9. RELATED PARTY TRANSACTIONS

During the year ended December 31, 2008, administration expenses of \$92,466 (2007 - \$84,450) were charged by four officers of the Company of which \$16,986 (2007 - \$Nil) was for out-of-pocket expenses and \$75,480 (2007 - \$84,450) was charged for services provided by four officers, one of whom is also a director of the Company.

During the year ended December 31, 2008, an amount of \$57,083 (2007 - \$134,577) was charged to deferred mineral exploration costs for services provided by a director and officer of the Company and two officers of the Company. Of this amount, \$Nil (2007 - \$107,322) represents reimbursements of out-of-pocket expenses at cost.

During the year ended December 31, 2008, deferred mineral exploration costs of \$Nil (2007 - \$9,600) were paid to a corporation of which a director and officer of the Company holds a significant interest.

During the year ended December 31, 2008, deferred mineral exploration costs of \$Nil (2007 - \$21,012) were charged for services provided by an officer of the Company. Included in accounts payable and accrued liabilities at December 31, 2008 was \$Nil (2007 - \$6,274) due to this corporation. This amount is unsecured, non-interest bearing with no fixed terms of repayment.

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

Continued...

9. RELATED PARTY TRANSACTIONS (Continued)

During the year ended December 31, 2007, directors and officers of the Company and a spouse of an officer subscribed for 40,000 non-flow-through units and 330,000 flow-through units for gross proceeds of \$37,000 pursuant to the private placement described in Note 7(b)(i).

During the year ended December 31, 2007, directors and officers of the Company and a spouse of an officer subscribed for 500,000 non-flow-through units and 400,000 flow-through units for gross proceeds of \$100,000 pursuant to the private placement described in Note 7(b)(ii). A spouse of an officer of the Company charged a finder's fee of \$3,450 with respect to this financing which was included in accounts payable as at December 31, 2007. This amount is unsecured, non-interest bearing with no fixed terms of repayment.

See also Note 3.

10. CONTINGENCIES

Environmental Contingencies

The Company's exploration activities are subject to various federal and provincial laws and regulations governing the protection of the environment. These laws and regulations are continually changing and generally becoming more restrictive. The Company conducts its operations so as to protect public health and the environment and believes its operations are materially in compliance with all applicable laws and regulations. The Company has made, and expects to make in the future, expenditures to comply with such laws and regulations.

Sahtu Settlement Region

See also Note 6 with respect to four claims located in the Sahtu Settlement Region, which are currently subject to dispute.

11. CAPITAL MANAGEMENT

The Company considers its capital structure to consist of capital stock, warrants and contributed surplus. 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 and development stage; as such the Company is dependent on external financing to fund its activities. In order to carry out the planned exploration and development, 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.

Management reviews its capital management approach on an ongoing basis and believes that this approach, given the relative size of the Company, is reasonable. There were no changes in the Company's approach to capital management during the year ended December 31, 2008.

12. FINANCIAL RISK FACTORS

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 equivalents and sundry receivables. The Company has no significant concentration of credit risk arising from operations. Cash equivalents consist of guaranteed investment certificates, which have been invested with reputable financial institutions, from which management believes the risk of loss to be remote. Financial instruments included in sundry receivable consist of goods and services tax due from the Federal Government of Canada and receivables from unrelated companies. Management believes that the credit risk concentration with respect to these financial instruments included in cash equivalents and sundry receivable is remote.

Liquidity Risk

The Company's approach to managing liquidity risk is to ensure that it will have sufficient liquidity to meet liabilities when due. As at December 31, 2008, the Company had a cash and cash equivalents balance of \$38,606 (2007 - \$336,423) and short-term investments of \$30,000 (2007 - \$Nil) to settle current liabilities of \$29,351 (2007 - \$46,909).

Market Risk

(a) Interest Rate Risk

The Company has cash equivalent balances subject to fluctuations in the prime rate. The Company's current policy is to invest excess cash in investment-grade short-term deposit certificates issued by its banking institutions. The Company periodically monitors the investments it makes and is satisfied with the credit ratings of its banks. Currently, the Company does not hedge against interest rate risk.

(b) Foreign Currency Risk

The Company's functional currency is the Canadian dollar and major purchases are transacted in Canadian dollars. Management believes the foreign exchange risk derived from currency conversions is negligible and therefore does not hedge its foreign exchange risk. The Company does not hold balances in foreign currencies to give rise to exposure to foreign exchange risk.

(c) Price Risk

The Company is exposed to price risk with respect to diamond prices. The Company closely monitors diamond prices to determine the appropriate course of action to be taken by the Company. As the Company's mineral properties are in the exploration stage and do not contain any mineral resources or mineral reserves, the Company does not hedge against price risk.

(d) Title Risk

See Note 6.

Sensitivity Analysis

The Company has designated its cash and cash equivalents and short-term investments as held-for-trading, measured at fair value. Financial instruments included in sundry receivables are classified as receivables, which are measured at amortized cost. Accounts payable and accrued liabilities are classified as other financial liabilities, which are measured at amortized cost.

As at December 31, 2008, the carrying and fair value amounts of the Company's financial instruments are approximately the same. The Company does not anticipate any material fluctuations as a result of changes in interest or foreign currency rates.

Continued...

13. SUBSEQUENT EVENTS

Subsequent to December 31, 2008, 650,000 warrants exercisable at \$0.16 per share expired, unexercised.

See Note 7(b)(iii).