

**Consolidated Financial Statements of**

**NEMI NORTHERN ENERGY & MINING INC.**

**For the period ended December 31, 2009**

**(Expressed in Canadian Dollars)**

# **NEMI NORTHERN ENERGY & MINING INC.**

## **NOTICE OF NO AUDITOR REVIEW OF INTERIM FINANCIAL STATEMENTS**

Under National Instrument 51-102, Part 4, subsection 4.3(3) (a), if an auditor has not performed a review of the interim financial statements, they must be accompanied by a notice indicating that the financial statements have not been reviewed by an auditor.

The accompanying unaudited interim financial statements of the Company have been prepared by and are the responsibility of the Company's management.

The Company's independent auditor has not performed a review of these financial statements in accordance with standards established by the Canadian Institute of Chartered Accountants for a review of interim financial statements by an entity's auditor.

# NEMI NORTHERN ENERGY & MINING INC.

## Consolidated Balance Sheets

(Prepared without audit)

(incorporated in Alberta)

(Expressed in Canadian dollars)

	As at December 31, 2009	As at September 30, 2009
<b>ASSETS</b>		
<b>CURRENT</b>		
Cash and cash equivalents	\$ 14,500,992	\$ 17,974,011
Marketable securities (Note 3)	680,250	659,843
Accounts receivable	4,549	1,130,971
Taxes recoverable	6,166	1,890
Prepaid expenses and other	43,418	55,266
	<b>15,235,375</b>	<b>19,821,981</b>
INVESTMENT IN PEACE RIVER COAL LP (Note 4)	49,632,982	46,116,103
PLANT AND EQUIPMENT (Note 5)	25,118	26,644
<b>Total Assets</b>	<b>\$ 64,893,475</b>	<b>\$ 65,964,728</b>
<b>LIABILITIES</b>		
<b>CURRENT</b>		
Accounts payable and accrued liabilities	\$ 397,332	\$ 699,037
CONVERTIBLE DEBENTURES (Note 6)	10,473,379	10,292,424
<b>Total Liabilities</b>	<b>10,870,711</b>	<b>10,991,461</b>
<b>SHAREHOLDERS' EQUITY (Note 7)</b>		
SHARE CAPITAL	52,232,779	54,188,712
CONTRIBUTED SURPLUS	9,781,550	8,587,935
WARRANTS	35,289	35,289
EQUITY PORTION OF CONVERTIBLE DEBENTURES (Note 6)	1,862,731	1,862,731
DEFICIT	(9,889,585)	(9,701,400)
<b>Total Shareholders' Equity</b>	<b>54,022,764</b>	<b>54,973,267</b>
<b>Total Liabilities and Shareholders' Equity</b>	<b>\$ 64,893,475</b>	<b>\$ 65,964,728</b>

NATURE OF OPERATIONS (Note 1)

COMMITMENTS (Note 12)

ON BEHALF OF THE BOARD

(signed) "Michael Cooney"

(signed) "Lyle Stein"

**NEMI NORTHERN ENERGY & MINING INC.**  
**Consolidated Statements of Operations,**  
**Comprehensive Earnings and Deficit**  
**(Prepared without audit)**  
**(Expressed in Canadian dollars)**

	For the three months ended	
	December 31, 2009	December 31, 2008
<b>EXPENSES</b>		
Advertising and public relations	\$ 625	\$ 4,753
Amortization	1,525	1,968
Consulting	19,500	19,500
Directors' fees	54,000	27,000
Insurance	10,236	6,500
Office and sundry	2,266	13,866
Office rent	11,600	13,978
Professional fees	11,615	389,000
Regulatory fees	4,180	11,123
Stock-based compensation	8,000	-
Stock transfer fees	1,233	1,462
Telecommunications	7,187	6,880
Travel and accommodation	2,081	28,690
Wages and benefits	2,832	94,628
Workers compensation fees	643	983
Loss before other income (expenses)	(137,523)	(620,331)
Break fee settlement	-	(1,000,000)
Foreign exchange gain	(636)	9,554
Interest on current debt and bank charges	(928)	(2,468)
Interest on convertible debentures	(420,911)	(420,911)
Interest and other income	15,406	93,062
Increase in value of marketable securities (Note 3)	20,407	-
Share of income (loss) of Peace River Coal LP (Note 4)	336,000	(120,000)
<b>NET EARNINGS (LOSS) AND COMPREHENSIVE</b>		
EARNINGS (LOSS) FOR THE PERIOD	(188,185)	(2,061,094)
DEFICIT, BEGINNING OF THE PERIOD	(9,701,400)	(5,500,509)
DEFICIT, END OF THE PERIOD	\$ (9,889,585)	\$ (7,561,603)
<b>Earnings (loss) per share (Basic and diluted)</b>		
	\$ (0.00)	\$ (0.04)
<b>Weighted average number of shares outstanding</b>		
	56,475,475	57,869,745

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

# NEMI NORTHERN ENERGY & MINING INC.

## Consolidated Statements of Cash Flows

(Prepared without audit)

(Expressed in Canadian dollars)

	For the three months ended	
	December 31, 2009	December 31, 2008
CASH FLOWS FROM		
OPERATING ACTIVITIES		
Net earnings (loss) and comprehensive earnings (loss) for the period	\$ (188,185)	\$ (2,061,094)
Items not affecting cash:		
Amortization	1,525	1,968
Share of (income) loss of Peace River Coal LP	336,000	120,000
Increase in value of marketable securities	(20,407)	-
Accretion of debenture and deferred financing costs	180,955	180,955
Stock-based compensation	8,000	-
	(354,112)	(1,758,171)
Net changes in non-cash working capital items		
Accounts receivable	1,126,422	(761)
Taxes recoverable	(4,276)	(1,796)
Prepaid expenses and other	11,848	20,822
Accounts payable and accrued liabilities	(301,706)	(375,244)
Net cash used in operating activities	478,176	(2,115,150)
FINANCING ACTIVITIES		
Repurchased capital stock	(770,316)	-
Net cash provided by financing activities	(770,316)	-
INVESTING ACTIVITIES		
Capital investment in Peace River Coal	(6,794,480)	(5,306,834)
Capital distribution in Peace River Coal	3,613,601	18,862,003
Net cash provided by (used in) investing activities	(3,180,879)	13,555,169
INCREASE IN CASH	(3,473,019)	11,440,019
CASH AND EQUIVALENTS - BEGINNING OF THE PERIOD	17,974,011	10,681,935
CASH AND EQUIVALENTS - END OF THE PERIOD	\$ 14,500,992	\$ 22,121,954
Cash interest expense paid	\$ 479,912	\$ 484,427

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

# NEMI NORTHERN ENERGY & MINING INC.

## Notes to Consolidated Financial Statements

December 31, 2009

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(Expressed in Canadian dollars)

### 1. NATURE OF OPERATIONS

NEMI Northern Energy & Mining Inc. ("NEMI" or the "Company") was incorporated under the Business Corporations Act of Alberta and extra-provincially registered under the Company Act of British Columbia.

On November 29, 2006, the Company concluded an agreement with Hillsborough Resources Limited ("Hillsborough") and Anglo Coal Canada Limited ("Anglo"), indirectly a wholly-owned subsidiary of Anglo American plc, wherein the north-eastern British Columbia metallurgical coal assets of the Company, Hillsborough and Anglo have been consolidated into a new entity, Peace River Coal Limited Partnership ("PRC" or "Peace River Coal LP") which was initially owned 60% by Anglo, 20% by Hillsborough, and 20% by NEMI. The assets transferred to PRC by the Company include the Trend Mine and related facilities, and NEMI's 50% interest in the Belcourt Saxon Coal Limited Partnership ("Belcourt Saxon Coal LP").

The Company's principal asset is the interest it holds in PRC, which currently stands at 12.2%.

Significant risk factors affecting the development of PRC's properties include the determination of coal resource to support mine operations; the successful execution of mine plans; the long term strength of metallurgical coal markets; and the ability to secure permits should commercial production from properties be demonstrated to be feasible. It is expected that the capital requirements to develop the various properties now held within PRC over the coming years will be significant. Accordingly, the Company's investment in PRC is subject to financing and dilution risk.

### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

These interim financial statements have been prepared by the Company in accordance with Canadian generally accepted accounting principles, using the same accounting policies and methods as per the annual financial statements for the year ended September 30, 2009. These interim financial statements should be read in conjunction with the most recent annual financial statements of the Company.

#### *Convergence with International Financial (IFRS)*

In 2006, Canada's Accounting Standards Board ratified a strategic plan that will result in Canadian GAAP, as used by public companies, being evolved and converged with International Financial Reporting Standards (IFRS) over a transitional period to be completed by 2011. The Company will be required to report using the converged standards effective for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2011. Canadian GAAP will be converged with IFRS through a combination of two methods: as joint-convergence of the United States' Financial Accounting Standards Board and the International Accounting Standards Board are agreed upon, they will be adopted by Canada's Accounting Standards Board and may be introduced in Canada before the complete changeover to IFRS. Also, the United States' Financial Accounting Standards Board and the International Accounting Standards Board have completed a joint-project on business combinations and non-controlling interests. As the International Accounting Standards Board currently, and expectantly, has projects underway that should result in new pronouncements that continue to evolve IFRS, and as this Canadian convergence initiative is in an early stage as of the date of these consolidated financial statements, it is premature to currently assess the impact of the Canadian initiative on the Company. The transition will require the restatement for comparative purposes of amounts reported by the Company for the year ended September 30, 2011. While the Company has begun assessing the adoption of IFRS, the financial reporting impact of the transition to IFRS cannot be reasonably estimated at this time.

# NEMI NORTHERN ENERGY & MINING INC.

## Notes to Consolidated Financial Statements

December 31, 2009

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(Expressed in Canadian dollars)

### 3. MARKETABLE SECURITIES

During the year ended September 30, 2009 the Company acquired 1,360,500 common shares of Hillsborough Resources Limited ("Hillsborough") for a purchase price of \$392,842 representing an average price of \$0.29 per share.

During the quarter ended December 31, 2009, Hillsborough completed a statutory arrangement (the "Arrangement") whereby Vitol Anker International B.V. ("Vitol") acquired all the shares of Hillsborough at a price of \$0.50 per share. As permitted by the terms of the Arrangement, NEMI has filed a notice of dissent and is currently evaluating Vitol's offer to pay in accordance with the dissent process.

As there is no longer a market price for the Hillsborough shares, NEMI is carrying the shares at a value of \$0.50 per share, representing Vitol's most recent offer to pay which was received January 11, 2009. The carrying value of the shares at December 31, 2009 was \$680,250, resulting in a gain of \$20,407 included in Net Earnings (Loss) and Comprehensive Earnings (Loss) for the quarter then ended.

The price NEMI eventually receives may be more or less than \$0.50, based on the outcome of the dissent process.

### 4. INVESTMENT IN PEACE RIVER COAL LP

PRC was formed pursuant to and is governed by a Limited Partnership Agreement made as of October 16, 2006, and amended as of November 24, 2006. Under the terms of the Limited Partnership Agreement, the partners are not obliged to fully participate in any of the partnership's programs and budgets, but they are subject to dilution provisions should they elect not to fully participate.

The Company accounts for its interest in PRC under the equity method. Upon formation, the book value of PRC was \$173 million and the partnership accounts of Anglo, the Company and Hillsborough were credited with the amounts of \$103.8 million (60%), \$34.6 million (20%) and \$34.6 million (20%), respectively, being the fair values of contributed property interests as determined by a formal valuation process and as agreed by the parties. In addition, the Company received as consideration a free cash carry in PRC to December 31, 2007 to a maximum of \$18 million.

In May 2007, PRC delivered its 2007 Program and Budget, including capital expenditures and working capital to fund net operating losses through the pre-commercial operation phase, for expenditures amounting to \$53 million, of which the Company's 20% share was \$10.6 million and was funded by the free cash carry. Hillsborough elected not to participate in either the 2007 Program and Budget or its share of NEMI's carry, and as a result, its interest in the partnership was diluted to 14.1%.

PRC subsequently approved a 2007 Supplemental Program and Budget for expenditures amounting to \$25 million, of which the Company's 20% share was \$5 million and was also funded by the free cash carry. For the 2007 Programs and Budgets, the Company used \$15.6 million of its \$18 million free cash carry. PRC audited partners' equity was \$236 million as at December 31, 2007.

# NEMI NORTHERN ENERGY & MINING INC.

## Notes to Consolidated Financial Statements

December 31, 2009

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(Expressed in Canadian dollars)

### 4. INVESTMENT IN PEACE RIVER COAL LP (Continued)

The 2008 Program and Budget called for expenditures amounting to \$198 million, of which the Company's 20% share was \$39.6 million. In December 2007, the Company elected to participate in the 2008 Program and Budget in the amount of \$5 million, and as a result the Company's interest in PRC was diluted, on a provisional basis, to approximately 12% (the "Provisional Interest"). Under the terms of the Limited Partnership Agreement, a final recalculation of each partner's PRC interest is made at the end of each budgetary period to reflect the actual debits, credits, and contributions made during that period.

During the calendar year ended December 31, 2008, PRC approved Supplemental Programs and Budgets for the Trend Transition Project and existing operations for aggregate expenditures amounting to \$101 million, of which the Company's share was \$12.1 million based on its Provisional Interest. The Company elected to fully fund its share of these Supplemental Programs and Budgets. For the calendar year ended December 31, 2008, the partners of PRC were presented with aggregate Programs and Budgets totaling \$299 million, of which the Company elected to fund \$17.1 million. Actual cash calls in respect of those Programs and Budgets totaled \$289 million, with the Company funding \$15.9 million. At year end, PRC recalculated the Company's and Hillsborough's partnership interest resulting in the Company's partnership interest being reduced to 12.0% and the Company receiving a rectifying cash distribution of \$16 million in November 2008. PRC audited partners' equity was \$359 million as at December 31, 2008.

PRC's 2009 Program and Budget called for expenditures amounting to \$225 million, of which the Company's pro rata share was \$27 million. In December 2008, the Company elected to fully fund its share of the 2009 Program and Budget. With the 2009 Program and Budget, PRC began making periodic cash distributions as revenue is received, typically making a cash call and a cash distribution monthly. During the calendar year 2009, PRC made \$170.6 million in cash calls in respect of the 2009 Program and Budget, of which the Company's share was \$20.7 million. In addition to funding these cash calls, the Company also paid \$0.5 million to fund shortfalls created by Hillsborough's failure to fund its proportion of the January 2009 cash call. As a result of these payments and the penalty imposed on Hillsborough for failing to fund its cash call, the Company's interest in PRC increased to 12.184%, Anglo's interest increased to 74.825%, and Hillsborough's interest decreased to 12.991%. In calendar 2009, PRC made cash distributions of \$134.3 million, of which the Company received \$16.3 million. PRC audited partners' equity was \$396 million as at December 31, 2009.

In September 2009, the Company settled its disputes with Anglo, Hillsborough, and Peace River Coal Inc. regarding its unused 2007 carried interest in PRC and interest on its share of the rectifying distribution. The parties agreed that PRC would pay NEMI \$1.1 million and that the parties would release each other from any claims in respect of the Programs and Budgets for any year up to and including December 2008. In addition, Anglo waived its right as the Limited Partner having the largest limited partnership interest under the parties' Limited Partnership Agreement to require NEMI's limited partnership interest to be converted into a net proceeds royalty interest if it is reduced to 10%, but only for so long as such interest was greater than 8%.

PRC's 2010 Program and Budget calls for expenditures amounting to \$152.3 million, of which the Company's pro rata share is \$18.6 million. In December 2009, the Company elected to fully fund its share of the 2010 Program and Budget.



**NEMI NORTHERN ENERGY & MINING INC.**  
**Notes to Consolidated Financial Statements**  
**December 31, 2009**

(Expressed in Canadian dollars)

**4. INVESTMENT IN PEACE RIVER COAL LP (Continued)**

The Company's net investment in PRC is as follows:

	<b>As at December 31, 2009</b>	<b>As at September 30, 2009</b>
Balance – beginning of year	\$46,116,103	\$46,708,040
Capital contributions paid during the quarter/year	6,794,480	19,668,190
Capital distribution allocated during the quarter/year	(3,613,601)	(20,545,127)
	<u>46,296,982</u>	<u>45,831,103</u>
Share of income for the quarter/year	336,000	285,000
	<u>49,632,982</u>	<u>46,116,103</u>

**5. PLANT AND EQUIPMENT**

	<b>December 31, 2009</b>		
	<b>Cost</b>	<b>Accumulated Depreciation</b>	<b>Net Book Value</b>
Equipment	\$ 28,104	\$ 14,439	\$ 13,665
Leasehold improvements	16,744	5,291	11,453
	<u>\$ 44,848</u>	<u>\$ 19,730</u>	<u>\$ 25,118</u>
	<b>September 30, 2009</b>		
	<b>Cost</b>	<b>Accumulated Depreciation</b>	<b>Net Book Value</b>
Equipment	\$ 28,104	\$ 13,516	\$ 14,588
Leasehold improvements	16,744	4,688	12,056
	<u>\$ 44,848</u>	<u>\$ 18,204</u>	<u>\$ 26,644</u>

**NEMI NORTHERN ENERGY & MINING INC.**  
**Notes to Consolidated Financial Statements**  
**December 31, 2009**

(Expressed in Canadian dollars)

**6. CONVERTIBLE DEBENTURES**

	Liability Component	Equity Component
Debenture	\$ 10,895,484	\$ 2,017,116
Deferred financing costs	(422,105)	(154,385)
	<u>\$ 10,473,379</u>	<u>\$ 1,862,731</u>

The Company issued a total of \$12,724,000 in 8% Convertible Debentures, on March 12 and April 1, 2008, for cash. The Debentures are unsecured and bear interest at a rate of 8% per annum, payable semi-annually in arrears, on June 30th and December 31st each year commencing June 30th, 2008. The Debentures mature on March 12, 2013 and are convertible into common shares of the Company at any time up until maturity at a conversion price of \$0.90 per share. After March 12, 2010, the Company has the right, under certain circumstances, to redeem the debentures in whole or in part. In addition, the Company has the right to repay the principal amount of the Debentures in common shares at a price equal to 95% of the weighted average trading price of the Company's shares on the Toronto Stock Exchange for the 20 trading day period ending 5 trading days prior to the date fixed for redemption or at maturity.

The Company paid a cash commission of \$763,440 and issued 100,000 non-transferable agent's warrants to the Agent as consideration for arranging the financing. Each warrant entitles the Agent to acquire one common share of the Company at a price of \$0.90 per share at any time until March 12, 2010.

As the convertible debentures were considered to be compound financial instruments, the liability and equity components are presented separately as determined on the measurement date. The Company valued the separate components of the convertible debenture using the proportionate method. The liability component was valued using the current market rate for comparable instruments at the time of issuance, which was estimated to be 17%.

The proceeds from the issue of the convertible debenture have been allocated based upon the fair value of the liability component with the residual allocated to the equity component:

Proceeds	\$12,724,000
Less equity component	(2,146,116)
Amount recorded as liability component	10,577,884
Accretion of liability component	953,400
Conversion of debentures to common shares	(635,800)
	<u>\$10,895,484</u>

Interest expense on the convertible debenture for the current period is comprised of:

Interest on convertible debenture	\$239,956
Accretion of convertible debenture	133,654
Accretion of deferred finance costs	47,301
<b>Debenture interest</b>	<u>\$420,911</u>

# NEMI NORTHERN ENERGY & MINING INC.

## Notes to Consolidated Financial Statements

December 31, 2009

(Expressed in Canadian dollars)

### 7. SHAREHOLDERS' EQUITY

(a) *Authorized:*

Unlimited number of Class A no par value voting common shares  
Unlimited number of Class B no par value non-voting common shares  
Unlimited number of Class C no par value non-voting common shares  
Unlimited number of Class D no par value non-voting, non-cumulative redeemable  
and retractable preferred shares

(b) *Issued and fully paid:*

Class A shares	December 31, 2009		September 30, 2009	
	Number of Shares	Amount	Number of Shares	Amount
Beginning of the year	56,882,355	\$ 54,188,712	57,869,745	\$ 54,981,872
Shares repurchased and cancelled	(1,692,500)	(1,752,995)	(721,500)	(685,495)
Shares repurchased for cancellation	(213,597)	(202,938)	(265,890)	(107,665)
End of the period	<u>54,976,258</u>	<u>\$ 52,232,779</u>	<u>56,882,355</u>	<u>\$ 54,188,712</u>

During the year ended September 30, 2009, the Company repurchased 987,390 common shares for \$378,328 for cancellation. 721,500 common shares purchased for \$270,663 were cancelled during the period and share capital has been reduced by \$685,495, based upon the average share issuance price, with the difference of \$414,832 recorded as contributed surplus. During the quarter ended December 31, 2009, the Company repurchased 1,906,097 common shares for \$770,317 for cancellation. 1,692,500 shares were cancelled during the period and 213,597 shares were cancelled subsequent to December 31, 2009, with share capital reduced by \$1,955,933 (based upon the average share issuance price) and the difference of \$1,185,615 recorded as contributed surplus.

(c) *Stock options:*

The Company has adopted a rolling 10% stock option plan ("Plan") which provides that the directors of the Company may grant options to purchase Class A shares of the Company to directors, officers, employees and service providers of the Company, with the number of options being limited to 10% of the issued Class A shares of the Company at the time of granting of options.

The Company's stock options outstanding as at December 31 and September 30, 2009 and the changes for the periods then ended are as follows:

	Quarter Ended Dec. 31, 2009	Weighted average exercise price	Year Ended Sept. 30, 2009	Weighted average exercise price
Beginning of the period	400,000	\$ 0.59	1,400,000	\$ 0.90
Options granted	-	-	250,000	0.41
Options expired/cancelled	-	-	(1,250,000)	0.90
End of the period	<u>400,000</u>	<u>\$ 0.59</u>	<u>400,000</u>	<u>\$ 0.59</u>
Options exercisable	<u>233,333</u>	<u>\$ 0.73</u>	<u>233,333</u>	<u>\$ 0.73</u>

# NEMI NORTHERN ENERGY & MINING INC.

## Notes to Consolidated Financial Statements

December 31, 2009

(Expressed in Canadian dollars)

### 7. SHAREHOLDERS' EQUITY (continued)

During the year ended September 30, 2009, the Company granted options to acquire 250,000 common shares of the Company at a price of \$0.41 per share exercisable at any time until May 27, 2014. Options to acquire 83,333 common shares vested immediately with further tranches of 83,333 vesting on May 28, 2010 and 2011. The fair value of the options was determined to be \$67,000 using the Black Scholes model with the following assumptions: risk-free interest rate – 0.50%; expected life - 2 years; expected volatility - 127%; and expected dividends – nil. Stock compensation expense for the year ended September 30, 2009 was \$11,000 with the remaining \$56,000 expense to be recognized at \$8,000 per quarter over the balance of the vesting period.

During the year ended September 30, 2009, the Company cancelled options to acquire 1,250,000 common shares of the Company at a price of \$0.90

During the year ended September 30, 2008, the Company granted options to acquire 1,400,000 shares of the Company at a price of \$0.90 per share exercisable at any time until April 1, 2013. The fair value of the options was determined to be \$504,000 using the Black Scholes model with the following assumptions: risk-free interest rate – 2.64%; expected life - 2 years; expected volatility - 100%; and expected dividends - nil.

(c) *Stock options (continued):*

Options to acquire Class A shares at September 30, 2009 are as follows:

<u>Number Outstanding</u>	<u>Exercise Price</u>	<u>Expiry Date</u>
150,000	\$0.90	April 1, 2013
250,000	0.41	May 27, 2014

The outstanding options have a weighted average remaining contractual life of 3.73 years.

(d) *Warrants:*

The Company's share purchase warrants and broker warrants outstanding as at December 31 and September 30, 2009 and the changes for the periods then ended are as follows:

	<u>Quarter Ended Dec. 31, 2009</u>	<u>Weighted average exercise price</u>	<u>Year Ended Sept. 30, 2009</u>	<u>Weighted average exercise price</u>
Beginning of the year	100,000	\$ 0.90	100,000	\$ 0.90
Broker warrants issued	-	-	-	-
Expired during the year	-	\$ -	-	\$ -
End of the year	<u>100,000</u>	<u>\$ 0.90</u>	<u>100,000</u>	<u>\$ 0.90</u>

The Company granted 100,000 non-transferable agent's warrants in connection with the closing of the Debenture financing. Each warrant entitles the agent to acquire one common share of the Company at a price of \$0.90 per share at any time until March 12, 2010. The fair value of the warrants was determined to be \$35,289 using the Black Scholes model with the following assumptions: risk-free interest rate – 4.67%; expected life - 2 years; expected volatility - 141%; and expected dividends - nil.

# NEMI NORTHERN ENERGY & MINING INC.

## Notes to Consolidated Financial Statements

### December 31, 2009

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(Expressed in Canadian dollars)

#### 7. SHAREHOLDERS' EQUITY (continued)

(c) *Contributed surplus:*

The changes in contributed surplus are as follows:

	<u>Dec. 31, 2009</u>	<u>Sept. 30, 2009</u>
Contributed surplus – beginning of year	\$ 8,587,935	\$ 8,154,103
Stock-based compensation	8,000	19,000
Shares cancelled	<u>1,185,615</u>	<u>414,832</u>
Contributed surplus – end of year	<u>\$ 9,781,550</u>	<u>\$ 8,587,935</u>

#### 8. AVIVA CORPORATION

In October 2008, the Company and Aviva Corporation (“Aviva”) entered into a merger implementation agreement to combine the businesses of the two companies (the “Merger”). The Merger was expected to be completed by way of an Aviva scheme of arrangement in Australia, with the Company issuing 0.59 shares for each Aviva share held at completion. Upon closing, it was expected that the existing shareholders of the Company would hold approximately 45% and the former shareholders of Aviva would hold approximately 55% of the share capital of the merged group. The completion of the Merger was subject to the approval of the shareholders of both companies, regulatory authorities in Canada and Australia, and the Australian Courts.

In December 2008, Aviva cancelled the transaction, citing a material adverse change in the affairs of the Company caused by the Company’s interest in PRC being diluted to 12%. Consequently, the Company paid a break fee of \$1 million to Aviva. The Company incurred \$324,000 in due diligence costs to September 30, 2008 and a further \$360,000 in costs during the six months ended March 31, 2009 associated with the Merger.

#### 9. RELATED PARTY TRANSACTIONS

- a) During the three months ended December 31, 2009, consulting fees of \$19,500 (2008 - \$19,500) were charged in respect of services rendered by a company with a common officer.
- b) The Trend Property was acquired in an agreement with and carries a 1% royalty interest (the "Trend Royalty") payable to a former officer of the Company. During the year ended September 30, 2006, the former President and CEO of the Company acquired approximately half of this royalty interest in a private transaction from the former officer of the Company for consideration of \$nil. The Trend property was transferred to and the Trend Royalty was assumed by PRC on November 29, 2006. There were no royalties paid or payable to the former President and CEO of the Company by NEMI during the three months ended December 31, 2008 and 2009, however, PRC paid royalties of US\$993,000 and US\$1,143,000 during the years ended September 30, 2008 and 2009, respectively on account of the Trend Royalty.

# NEMI NORTHERN ENERGY & MINING INC.

## Notes to Consolidated Financial Statements

December 31, 2009

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(Expressed in Canadian dollars)

### 10. SEGMENTED INFORMATION

The Company operates in one segment – the acquisition, exploration and development of coal properties, and subsequent production. During the periods ended December 31, 2009 and 2008 and as at December 31, 2009, all the operations and assets were in Canada.

### 11. FINANCIAL INSTRUMENTS AND CAPITAL DISCLOSURES

The Company's financial instruments consist of cash and cash equivalents, marketable securities, amounts receivable, investments, accounts payable and accrued liabilities. For cash and current receivables and accounts payable and accrued liabilities, carrying value is considered to be a reasonable approximation of fair value due to the short-term nature of these instruments. The fair value of other financial assets represents the market value of quoted investments.

Cash and marketable securities are designated as held for trading and therefore carried at fair value, with the unrealized gain or loss recorded on the statement of operations.

The Company's financial instruments are exposed to a number of financial and market risks, including credit, liquidity, foreign exchange, interest rate and price risks. The Company may, or may not, establish from time to time active policies to manage these risks. The Company does not currently have in place any active hedging or derivative trading policies to manage these risks since the Company's management does not believe that the current size, scale and pattern of its operations would warrant such hedging activities.

#### (a) Credit risk

Credit risk is the risk that a counterparty to a financial instrument will not discharge its obligations, resulting in a financial loss to the Company. The Company has procedures in place to minimize its exposure to credit risk. Company management evaluate credit risk on an ongoing basis, including evaluation of counterparty credit rating, monitoring activities related to trade and other receivables and counterparty concentrations measured by amount and percentage.

The primary sources of credit risk for the Company arise from the following financial assets: (1) cash and cash equivalents held with major Canadian financial institutions; (2) marketable securities; and (3) amounts receivable. The Company has not had any credit losses in the past, nor does it expect to have any credit losses in the future. At December 31, the Company has no financial assets that are past due or impaired due to credit risk defaults.

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**11. FINANCIAL INSTRUMENTS AND CAPITAL DISCLOSURES (continued)**

The Company's maximum exposure to credit risk at the reporting date is as follows:

	<b>December 31, 2009</b>	September 30, 2009
Cash and cash equivalents	\$ 14,500,992	\$ 17,974,011
Marketable securities	680,250	659,843
Accounts receivable	4,549	1,130,971
	<b>\$ 15,185,791</b>	<b>\$ 19,764,825</b>

(b) Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its obligations with respect to financial liabilities as they fall due. The Company's financial liabilities are comprised of accounts and interest payable and accrued liabilities. The Company frequently assesses its liquidity position by reviewing the timing of amounts due and the Company's current cash flow position to meet its obligations. The Company manages its liquidity risk by maintaining sufficient cash and cash equivalents and short-term investment balances to meet its anticipated operational needs.

The Company's financial liabilities, consisting of accounts and interest payable and accrued liabilities, arose as a result of corporate expenses and interest on the convertible debentures. Payment terms on these liabilities are typically 30 to 60 days from receipt of invoice and do not generally bear interest. Interest on the convertible debentures is paid semi-annually on June 30<sup>th</sup> and December 31<sup>st</sup>.

The following table summarizes the remaining contractual maturities of the Company's financial liabilities:

	<b>December 31, 2009</b>	September 30, 2009
Accounts payable and accrued liabilities	\$ 397,332	\$ 699,037
	<b>\$ 397,332</b>	<b>\$ 699,037</b>

Typical repayment terms for the Company do not exceed 90 days.

(c) Market risk

Market risk is the risk that the fair value for assets classified as held-for-trading and available-for-sale or future cash flows for assets or liabilities considered to be held-to maturity, other financial liabilities, and loans or receivables of a financial instrument will fluctuate because of changes in market conditions. The Company evaluates market risk on an ongoing basis. The Company's exposure to interest rate risk is limited as its convertible debentures carry a fixed rate of interest and the Company has sufficient funds available for their repayment.

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### 11. FINANCIAL INSTRUMENTS AND CAPITAL DISCLOSURES (continued)

#### (d) Foreign exchange risk

The Company operates in Canada only and has minimal transactions in foreign currencies.

#### (e) Capital disclosure

The Company's objectives when managing its capital are to maintain a flexible structure in order to optimize the cost of capital at an acceptable level of risk, balancing the interests of both equity and debt holders while allowing for development of the business.

The Company considers shareholders' equity, long term debt or debentures and short term borrowing to be components, from time to time, of capital under management.

The current activities of the Company are limited, however, the Company may issue new shares or incur debt, as required, in order to meet the objectives above. The Company monitors its capital based upon debt to equity and working capital ratios.

The components of capital and key ratios as of December 31 and September 30, 2009 are as follows:

	<u>Dec. 31, 2009</u>	<u>Sept. 30, 2009</u>
Long-term debt	\$ 10,473,379	\$ 10,292,424
Shareholders' equity	<u>\$ 54,022,764</u>	<u>\$ 54,973,267</u>
Debt to equity	0.19 : 1	0.19 : 1
Current assets	\$ 15,235,375	\$ 19,821,981
Current liabilities	<u>\$ 397,332</u>	<u>\$ 699,037</u>
Working Capital ratio	38 : 1	28 : 1

The Company believes these ratios are within reasonable limits in light of its current business activities and objectives and there have not been any significant changes in the Company's objectives from the previous period.



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#### 12. CONTINGENCIES AND COMMITMENTS

- a) On May 12, 2009, Patrick Devlin ("Devlin"), commenced an action in the Supreme Court of British Columbia against the Company alleging that the Company wrongfully dismissed Devlin from his employment with Company, or alternatively, that the Company's actions constituted a constructive dismissal of Devlin or a repudiation of a contract of employment between the Company and Devlin. Devlin is claiming liquidated damages in the amount of \$800,000, or alternatively, damages for wrongful or constructive dismissal and/or breach of contract, special damages, interest and special costs. The Company disputes the allegations made in the action and will take all steps available to it to fully protect its interests and those of its shareholders.

Out of an abundance of caution the Company has reserved \$300,000 with respect to Devlin's claim for wrongful dismissal. The Company continues to deny liability and will defend all claims for the benefit of all shareholders.

- b) The Company is committed under the terms of an office lease agreement for previous premises for the following estimated annual rent and operating costs:

year ending September 30, 2010	\$244,000
year ending September 30, 2011	\$123,000

The Company has sublet this office space at its cost to PRC.

- c) During the year ended September 30, 2008, the Company entered into an office lease agreement for its current premises for the following estimated annual rent and operating costs:

year ending September 30, 2010	\$56,000
year ending September 30, 2011	\$58,000
year ending September 30, 2012	\$58,000
year ending September 30, 2013	\$53,000