

**CANADA COAL INC.**

**CONSOLIDATED FINANCIAL STATEMENTS  
FOR THE YEARS ENDED SEPTEMBER 30, 2013 AND 2012  
(EXPRESSED IN CANADIAN DOLLARS)**

## INDEPENDENT AUDITOR'S REPORT

To the Shareholders of Canada Coal Inc.

We have audited the accompanying consolidated financial statements of Canada Coal Inc. and its subsidiaries, which comprise the consolidated statements of financial position as at September 30, 2013 and 2012, and the consolidated statements of loss and comprehensive loss, consolidated statements of cash flows and consolidated statements of changes in equity for the years then ended, and a summary of significant accounting policies and other explanatory information.

### Management's Responsibility for the Consolidated Financial Statements

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

### Auditor's Responsibility

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

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

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

### Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Canada Coal Inc. and its subsidiaries as at September 30, 2013 and 2012, and their financial performance and cash flows for the years then ended in accordance with International Financial Reporting Standards.

McGOVERN, HURLEY, CUNNINGHAM, LLP



Chartered Accountants  
Licensed Public Accountants

TORONTO, Canada  
January 23, 2014

**CANADA COAL INC.**  
**CONSOLIDATED STATEMENTS OF FINANCIAL POSITION**  
**(EXPRESSED IN CANADIAN DOLLARS)**  
**AS AT**

	September 30, 2013	September 30, 2012
<b>ASSETS</b>		
<b>Current</b>		
Cash and cash equivalents (Note 7)	\$ 1,883,776	\$ 3,187,279
Receivables (Note 8)	76,712	86,574
Prepaid expenses (Note 9)	37,261	6,576
Total Current Assets	1,997,749	3,280,429
<b>Equipment</b> (Note 10)	20,785	29,677
<b>Investment</b> (Note 11)	41,250	-
<b>Exploration and evaluation expenditures</b> (Note 12)	4,680,131	4,341,679
Total Assets	\$ 6,739,915	\$ 7,651,785
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
<b>Current</b>		
Accounts payable and accrued liabilities (Note 13)	\$ 51,295	\$ 259,601
<b>Deferred tax liability</b> (Note 17)	119,000	348,000
Total Liabilities	170,295	607,601
<b>Shareholders' equity</b>		
Capital stock (Note 15)	7,596,420	7,596,420
Reserves	3,013,402	3,114,516
Deficit	(4,040,202)	(3,666,752)
Total Shareholders' Equity	6,569,620	7,044,184
Total Liabilities and Shareholders' Equity	\$ 6,739,915	\$ 7,651,785

**Nature and continuance of operations** (Note 1)  
**Commitments and contingencies** (Notes 12 and 19)

**On behalf of the Board:**

\_\_\_\_\_, Director

\_\_\_\_\_, Director

**See accompanying notes to the consolidated financial statements.**

**CANADA COAL INC.**  
**CONSOLIDATED STATEMENTS OF LOSS AND COMPREHENSIVE LOSS**  
**(EXPRESSED IN CANADIAN DOLLARS)**  
**FOR THE YEARS ENDED**

	September 30, 2013	September 30, 2012
<b>EXPENSES</b>		
Management fees (Note 13)	\$ 252,000	\$ 339,000
Consulting fees	113,931	45,625
Office, rent, and miscellaneous (Note 13)	54,551	61,508
Professional fees (Notes 13)	63,122	210,123
Shareholder communications and promotion	26,980	23,848
Share-based compensation (Note 15)	6,049	746,779
Property investigation costs	41,100	-
Transfer agent and filing fees	24,278	73,545
Travel and accommodation	28,658	33,413
<b>Loss before write offs, investment income and reverse take-over costs</b>	<b>610,669</b>	<b>1,533,841</b>
<b>OTHER ITEMS</b>		
Investment income	(29,353)	(67,284)
Share of losses of equity associate (Note 11)	8,750	-
Write off of exploration and evaluation expenditures (Note 12)	119,548	-
Reverse take-over transaction costs (Note 14)	-	1,187,770
<b>Net loss before income taxes</b>	<b>709,614</b>	<b>2,654,327</b>
Deferred income tax (recovery) expense (Note 17)	(239,642)	610,000
<b>Net loss and comprehensive loss for the year</b>	<b>\$ 469,972</b>	<b>\$ 3,264,327</b>
<b>Basic and diluted net loss per common share</b>	<b>\$ 0.01</b>	<b>\$ 0.08</b>
<b>Weighted average number of common shares outstanding – basic and diluted</b>	<b>43,449,750</b>	<b>39,038,101</b>

See accompanying notes to the consolidated financial statements.

**CANADA COAL INC.**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**(EXPRESSED IN CANADIAN DOLLARS)**  
**FOR THE YEARS ENDED**

	September 30, 2013	September 30, 2012
<b>CASH FLOW FROM OPERATING ACTIVITIES</b>		
Net loss for the year	\$ (469,972)	\$ (3,264,327)
Items not affecting cash:		
Deferred income tax (recovery) expense	(239,642)	610,000
Share of losses of equity associate	8,750	-
Write off of exploration and evaluation expenditures	119,548	-
Reverse take-over transaction cost	-	1,187,770
Share-based compensation	6,049	746,779
	<u>(575,267)</u>	<u>(719,778)</u>
Change in non-cash working capital items:		
Decrease in receivables	73,417	6,544
(Increase) in prepaid expenses	(7,250)	(6,576)
(Decrease) increase in accounts payable and accrued liabilities	(28,193)	13,484
	<u>(537,293)</u>	<u>(706,326)</u>
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Proceeds from private placements	-	4,349,127
Share issue costs	-	(383,810)
Net cash flows from financing activities	<u>-</u>	<u>3,965,317</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Exploration and evaluation expenditures	(716,210)	(3,432,274)
Purchase of equipment	-	(32,641)
Purchase of investment (Note 11)	(50,000)	-
Net cash acquired in reverse acquisition (Note 14)	-	318,633
Net cash flows used by investing activities	<u>(766,210)</u>	<u>(3,146,282)</u>
<b>(Decrease) increase in cash and cash equivalents</b>	<b>(1,303,503)</b>	<b>112,709</b>
<b>Cash and cash equivalents, beginning of year</b>	<b>3,187,279</b>	<b>3,074,570</b>
<b>Cash and cash equivalents, end of year</b>	<b>\$ 1,883,776</b>	<b>\$ 3,187,279</b>
<b>Comprised of:</b>		
Cash	13,182	183,947
Short term money market investments	1,870,594	3,003,332

Supplemental disclosure with respect to cash flows (Note 16)

See accompanying notes to the consolidated financial statements.

**CANADA COAL INC.**  
**CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY**  
**(EXPRESSED IN CANADIAN DOLLARS)**  
**FOR THE YEARS ENDED**

	Number of Shares	Capital Stock	Reserves Equity Settled Share- Based Payments Reserve	Warrant Reserve	Deficit	Total
<b>Balance, September 30, 2011</b>	31,500,000	\$ 2,871,329	\$ 193,165	\$ 1,308,060	\$ (509,356)	\$ 3,863,198
Share-based compensation	-	-	746,779	-	-	746,779
Issued pursuant to private placement	8,600,000	3,546,843	-	753,157	-	4,300,000
Acquisition of Mercury Capital Limited	3,349,750	1,373,398	138,769	6,048	-	1,518,215
Additional contribution for seed shares	-	49,127	-	-	-	49,127
Expiry of options	-	-	(106,931)	-	106,931	-
Issue costs-cash	-	(355,350)	-	(75,458)	-	(430,808)
Issue costs-non cash	-	(90,667)	-	90,667	-	-
Deferred income tax recovery on share issue costs	-	201,740	-	60,260	-	262,000
Net loss and comprehensive loss for the year	-	-	-	-	(3,264,327)	(2,654,327)
<b>Balance, September 30, 2012</b>	43,449,750	7,596,420	971,782	2,142,734	(3,666,752)	7,044,184
Share-based compensation	-	-	6,049	-	-	6,049
Expiry of options	-	-	(37,640)	-	37,640	-
Expiry of warrants	-	-	-	(69,523)	69,523	-
Tax effect of warrant expiry	-	-	-	-	(10,641)	(10,641)
Net loss and comprehensive loss for the year	-	-	-	-	(469,972)	(469,972)
<b>Balance, September 30, 2013</b>	43,449,750	7,596,420	940,191	2,073,211	(4,040,202)	6,569,620

See accompanying notes to consolidated financial statements.

**CANADA COAL INC.**  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(EXPRESSED IN CANADIAN DOLLARS)  
FOR THE YEARS ENDED SEPTEMBER 30, 2013 AND 2012

**1. NATURE AND CONTINUANCE OF OPERATIONS**

Canada Coal Inc. (hereafter the "Company" or "Canada Coal") was incorporated on August 26, 2010 under the Business Corporation Act (Ontario) under the name Pacific Coal Corp. On April 12, 2011, the Company changed its name to Canada Coal Inc. The Company's principal business is the acquisition and exploration of coal properties in Nunavut, Canada. The Company is at the early stages of exploration on its projects and as such, to date, has not generated significant revenues from its operations.

The Company's head office is located at 181 Bay Street, Suite 1800, Toronto, Ontario, M5J 2T9.

These consolidated financial statements were approved by the Board of Directors on January 23, 2014.

The Company is in the process of exploring its properties and has not yet determined whether the properties contain reserves that are economically recoverable. The recoverability of the amounts shown for exploration and evaluation expenditures are dependent upon the existence of economically recoverable reserves, the ability of the Company to obtain necessary financing to complete the development of those reserves, the achievement of profitable production, 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 of exploration and evaluation expenditures.

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 Company's assets may also be subject to increases in taxes and royalties, renegotiation of contracts, currency exchange fluctuations and restrictions, and political uncertainty.

On November 4, 2011, the Company entered into an agreement with Mercury Capital Limited ("Mercury Capital") in respect to a combination to be effected by way of an amalgamation of the parties (Note 14). Under the terms of the agreement, holders of common shares and other securities such as options and warrants of Canada Coal and Mercury Capital, received common shares and other securities of the resulting issuer on a one-for-one basis. The amalgamation constituted a qualifying transaction for Mercury Capital as defined in Policy 2.4 of the Exchange's Corporate Finance Manual.

Canada Coal Inc. was the resulting issuer from the amalgamation and upon completion of the amalgamation, was considered a Tier I mining issuer. Conditional approval for the transaction was received January 23, 2012 from the TSX Venture Exchange and shareholder approval was obtained on February 21, 2012. The amalgamation was effective February 23, 2012 and the Company began trading on the TSX Venture Exchange on February 29, 2012.

These consolidated financial statements have been prepared with the assumption that the Company will continue in operation for the foreseeable future and will be able to realize its assets and discharge its liabilities in the normal course of operations. As at September 30, 2013, the Company had working capital of \$1,946,454 and an accumulated deficit of \$4,040,202 compared with working capital of \$3,020,828 and an accumulated deficit of \$3,666,752 as at September 30, 2012. The continuing operations of the Company are dependent upon its ability to continue to raise adequate financing and to commence profitable operations in the future. Management believes it will be successful in raising the necessary funding to continue operations in the normal course of operations. These consolidated 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. STATEMENT OF COMPLIANCE**

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS"), as issued by the International Accounting Standards Board ("IASB"), and its interpretations.

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**CANADA COAL INC.**  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(EXPRESSED IN CANADIAN DOLLARS)  
FOR THE YEARS ENDED SEPTEMBER 30, 2013 AND 2012

**3. BASIS OF PRESENTATION**

These consolidated financial statements have been prepared on a historical cost basis except for financial instruments classified as held-for-trading, which are stated at their fair value. In addition, these consolidated financial statements have been prepared using the accrual basis of accounting, except for cash flow information.

**4. SIGNIFICANT ACCOUNTING POLICIES**

The accounting policies set out below have been applied consistently to all periods presented in these consolidated financial statements.

**Principles of consolidation**

These consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries, Canadian Sovereign Coal Corp., a company incorporated under the laws of British Columbia, and 5200 Nunavut Ltd., a company incorporated under the laws of Nunavut. Significant inter-company balances and transactions have been eliminated upon consolidation. All references to the Company should be treated as references to Canada Coal Inc. and its subsidiaries.

Subsidiaries are entities over which the Company has control, where control is defined as the power to govern financial and operating policies of an entity so as to obtain benefit from its activities. Generally, the Company has a shareholding of more than one half of the voting rights in its subsidiaries. The effects of potential voting rights that are currently exercisable are considered when assessing whether control exists. Subsidiaries are fully consolidated from the date control is transferred to the Company, and are de-consolidated from the date control ceases.

**Cash and cash equivalents**

Cash and cash equivalents include balances with banks and short-term money market investments with original maturities of 90 days or less which are readily convertible into a known amount of cash. The Company's cash and cash equivalents are invested with major financial institutions in business accounts and are available on demand by the Company.

**Financial instruments**

Financial assets and financial liabilities that are purchased and incurred with the intention of generating profits in the near term are classified as held-for-trading. These instruments are measured at fair value with subsequent changes in fair value recognized in the statement of loss and comprehensive loss. As at September 30, 2013 and 2012, the Company's cash equivalents are classified as held-for-trading.

Financial assets that have a fixed maturity date and fixed or determinable payments, where the Company intends and has the ability to hold the financial asset to maturity are classified as held-to-maturity and are measured at amortized cost using the effective interest rate method. Any gains and losses arising from the sale of held to maturity financial assets are recognized in the statement of loss and comprehensive loss. As at September 30, 2013 and 2012, the Company has no held-to-maturity financial assets.

Items classified as loans and receivables are measured at amortized cost using the effective interest method. Any gains or losses on the realization of loans and receivables are recognized in the statement of loss and comprehensive loss. The Company's cash and receivables are classified as loans and receivables. The estimated fair values of these financial instruments approximate their carrying values because of the limited terms of these instruments.

Available-for-sale assets are those financial assets that are not classified as held-for-trading, held-to-maturity or loans or receivables, and are carried at fair value. Any gains or losses arising from the change in fair value are recorded as other comprehensive income. Available-for-sale investments are written down to fair value through operations whenever it is necessary to reflect other than temporary impairment. Cumulative gains and losses arising upon the sale of the instrument are included in operations. Regular way purchases and sales of financial assets are accounted for at the trade date. As at September 30, 2013 and 2012, the Company has no available-for-sale assets.

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**CANADA COAL INC.**  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(EXPRESSED IN CANADIAN DOLLARS)  
FOR THE YEARS ENDED SEPTEMBER 30, 2013 AND 2012

**4. SIGNIFICANT ACCOUNTING POLICIES (Continued)**

**Financial instruments (Continued)**

Financial liabilities that are not classified as held-to-maturity are classified as other financial liabilities, and are carried at amortized cost using the effective interest method. Any gains or losses arising from the realization of other financial liabilities are recognized in the statement of loss and comprehensive loss. The Company has classified accounts payable and accrued liabilities as other financial liabilities, which are carried at amortized cost. Due to their short-term natures, the fair values of these financial instruments approximate their carrying values, and are not subject to significant credit or interest rate risk.

The Company classifies its fair value measurements using a fair value hierarchy that reflects the significance of the inputs used in making the measurements. The fair value hierarchy has the following levels: (a) quoted prices (unadjusted) in active markets for identical assets or liabilities (Level 1); (b) inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (i.e., as prices) or indirectly (i.e., derived from prices) (Level 2); and (c) inputs for the asset or liability that are not based on observable market data (unobservable inputs) (Level 3). At September 30, 2013 and September 30, 2012, the Company's financial instruments that were carried at fair value, consisted of cash equivalents which have been classified as Level 2 within the fair value hierarchy.

**Impairment of financial assets**

Financial assets are assessed for indicators of impairment at the end of each reporting period. Financial assets are impaired when there is objective evidence that the estimated future cash flows of the assets have been negatively impacted. The amount of the loss is measured as the difference between the asset's carrying amount and the present value of the estimated future cash flows discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced by the amount of the impairment and the loss is recognized in the statement of loss and comprehensive loss.

If in a subsequent period, the amount of impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized, the previously recognized impairment loss is reversed to the extent that the carrying value of the asset does not exceed what the amortized cost would have been had the impairment not been recognized. Any subsequent reversal of an impairment loss is recognized in the statement of loss and comprehensive loss.

If an available-for-sale asset is impaired, an amount comprising the difference between its cost and its current fair value, less any impairment previously recognized in profit or loss, is transferred from equity to profit or loss. Reversals in respect of equity instruments classified as available-for-sale are not recognized in the statement of loss and comprehensive loss.

**Impairment of non financial assets**

At each date of the statement of financial position, the Company reviews the carrying amounts of its non-financial assets to determine whether there is an indication that those assets have suffered an impairment loss. If such an indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss. The recoverable amount is the higher of the fair value less costs to sell and the value in use. If the recoverable amount is less than the carrying amount of the asset, the carrying amount is reduced to the recoverable amount and the impairment loss is recognized in the statement of loss and comprehensive loss.

**Investments**

Investments in associates are accounted for using the equity method based on the Company's ability to exercise significant influence over the operating and financial policies of the investee. Investments of this nature are recorded at original cost and adjusted periodically to recognize the Company's proportionate share of the associate's net income or losses after the date of investment, additional contributions made and dividends received. Investments are written down when there has been a significant or prolonged decline in fair value.

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**CANADA COAL INC.**  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(EXPRESSED IN CANADIAN DOLLARS)  
FOR THE YEARS ENDED SEPTEMBER 30, 2013 AND 2012

**4. SIGNIFICANT ACCOUNTING POLICIES (Continued)**

**Equipment**

Equipment is stated at cost less accumulated amortization and accumulated impairment losses. The cost of an item of equipment consists of the purchase price, any costs directly attributable to bringing the asset to the location and condition necessary for its intended use and an initial estimate of the costs of dismantling and removing the item and restoring the site on which it is located.

The Company's amortization is recorded as an addition to exploration and evaluation expenditures and amortizes cost less estimated residual values on a straight line method over the estimated useful life of the asset. The estimated useful life of assets is as follows:

Equipment	5 years
Vehicles	2 years

An item of equipment is derecognized upon disposal, when held for sale or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on disposal of the asset, determined as the difference between the net disposal proceeds and the carrying amount of the asset, is recognized in the statement of loss and comprehensive loss.

The Company conducts an assessment of the residual balances, useful lives and amortization methods being used for equipment at each reporting date and any changes arising from the assessment are applied by the Company prospectively.

**Foreign currency translation**

The Canadian dollar is the functional and reporting currency of the Company and its subsidiaries. All monetary assets and liabilities are translated at the rate of exchange at the financial reporting date and non-monetary assets and liabilities are translated at historical exchange rates, unless such items are carried at market, in which case they are translated at the exchange rates in effect on the statement of financial position date. Income and expenses are translated at the rates approximating those at the transaction dates. Gains and losses arising from translation of foreign currency monetary assets and liabilities are recognized in the statement of loss and comprehensive loss.

**Exploration and evaluation expenditures**

All of the Company's property interests are in the exploration and evaluation phase. The Company records its interests in properties and areas of geological interest at cost. Expenditures incurred prior to obtaining the legal right to explore are expensed. All direct and indirect costs relating to the acquisition and exploration of these interests are capitalized on the basis of specific claim blocks or areas of geological interest until the properties to which they relate are placed into production, sold or management has determined there to be impairment. These costs will be amortized on the basis of units produced in relation to the proven reserves available on the related property following commencement of production. The Company classifies the costs between exploration and evaluation expenditures and equipment based on the nature of the costs incurred.

The cost of property interests includes any cash consideration paid and the fair market value of shares issued, if any, on the acquisition of property interests. Acquisition costs of properties acquired under option agreements, whereby payments are made at the sole discretion of the Company, are recorded in the accounts when the payments are made. The recorded amounts of property claim acquisition costs and their related exploration and evaluation costs represent actual expenditures incurred and are not intended to reflect present or future values.

The Company reviews capitalized costs on its properties on a periodic basis and when events or changes in circumstances indicate that its carrying amount may not be recoverable. The Company will recognize an impairment in value based upon current exploration results and upon management's assessment of the future probability of revenues from the property or from the sale of the property.

Continued...

**CANADA COAL INC.**  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(EXPRESSED IN CANADIAN DOLLARS)  
FOR THE YEARS ENDED SEPTEMBER 30, 2013 AND 2012

**4. SIGNIFICANT ACCOUNTING POLICIES (Continued)**

**Restoration, rehabilitation and environmental obligations**

A legal or constructive obligation to incur restoration, rehabilitation and environmental costs may arise when environmental disturbance is caused by the exploration, development or ongoing production of a property interest. Such costs arising from the decommissioning of plant and other site preparation work, discounted to their net present value, are provided for and capitalized to the carrying amount of the asset, as soon as the obligation to incur such costs arises. Discount rates using a pre-tax rate that reflects the time value of money are used to calculate the net present value. These costs are charged against profit or loss over the economic life of the related asset, through amortization using the unit-of-production method. Changes to the current market based discount rate, amount or timing of the underlying cash flows needed to settle the obligation impact the carrying value of the asset and liability. The related liability is adjusted each period for the unwinding of the discount rate. The Company had no significant restoration, rehabilitation and environmental obligations as at September 30, 2013 and September 30, 2012.

**Provisions**

Provisions are recorded when a present legal or constructive obligation exists as a result of past events where it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate of the amount of the obligation can be made. The amount recognized as a provision is the best estimate of the consideration required to settle the present obligation at the statement of financial position date, taking into account the risks and uncertainties surrounding the obligation. Where a provision is measured using the cash flows estimated to settle the present obligation, its carrying amount is the present value of those cash flows.

A provision for onerous contracts is recognized when the expected benefits to be derived by the Company from a contract are lower than the unavoidable cost of meeting its obligations under the contract.

The Company had no material provisions at September 30, 2013 and September 30, 2012.

**Share-based payment transactions**

In situations where equity instruments are issued to non-employees and some or all of the goods or services received by the entity as consideration cannot be specifically identified, they are measured at fair value of the share-based payment. Otherwise, share-based payments are measured at the fair value of goods or services received.

The fair value of stock options granted to employees is recognized as an expense over the vesting period with a corresponding increase in the equity settled share-based payments reserve account. An individual is classified as an employee when the individual is an employee for legal or tax purposes (direct employee) or provides services similar to those performed by a direct employee, including directors of the Company.

The fair value is measured at the grant date and recognized over the period during which the options vest. The fair value of the options granted is measured using the Black-Scholes option-pricing model, taking into account the terms and conditions upon which the options were granted. At each financial position reporting date, the amount recognized as an expense is adjusted to reflect the actual number of stock options that are expected to vest.

Where the terms of an equity-settled award are modified, the minimum expense recognized is the expense as if the terms had not been modified. An additional expense is recognized for any modification which increases the total fair value of the share-based payment arrangement, or is otherwise beneficial to the employee as measured at the date of modification.

Unexercised expired stock options are transferred to deficit.

Continued...

**CANADA COAL INC.**  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
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**4. SIGNIFICANT ACCOUNTING POLICIES (Continued)**

**Warrants**

Warrants are recognized at fair value on the date of grant and are measured using the Black-Scholes option pricing model. Incremental costs directly attributable to the issue of new warrants are shown in equity as a deduction, net of tax, from the proceeds. Unexercised expired warrants are transferred to deficit.

**Flow-through shares**

The Company has financed a portion of its exploration activities through the issue of flow-through shares, which offer a tax incentive to Canadian investors by transferring the tax deductibility of exploration expenditures from the Company to the investor.

The Company has adopted a policy whereby flow-through proceeds are allocated between the offering of the common shares and the sale of tax benefits when the common shares are offered. The allocation is made based on the difference between the quoted price of the common shares and the amount the investor pays for the flow-through shares. A liability is recognized for the premium paid by the investors. Upon renunciation of the flow through expenditures for Canadian income tax purposes, the liability component is derecognized and a deferred income tax liability is recognized for the taxable temporary difference created at the Company's applicable tax rate which is expected to apply in the year the deferred income tax liability will be settled. Any difference between the amount of the liability component derecognized and deferred income tax liability recognized is recorded in profit and loss.

Resource expenditure deductions for income tax purposes related to exploration and evaluation activities funded by flow-through share arrangements are renounced to investors in accordance with income tax legislation.

**Income taxes**

Income tax on the profit or loss for the periods presented comprises current and deferred tax. Income tax is recognized in profit or loss except to the extent that it relates to items recognized directly in equity, in which case it is recognized in equity.

Current tax expense is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at period end, adjusted for amendments to tax payable with regards to previous years.

Deferred tax is provided using the liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The amount of deferred tax provided is based on the expected manner of realization or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted at the financial position reporting date. A deferred tax asset is recognized only to the extent that it is probable that future taxable profits will be available against which the asset can be utilized. Deferred tax assets are reviewed at each reporting date and to the extent that the Company does not consider it probable that a future tax asset will be recovered, it is not recognized.

**Loss per share**

The basic loss per share is computed by dividing the net loss by the weighted average number of common shares outstanding during the period. The diluted loss per share reflects the potential dilution of common share equivalents, such as outstanding stock options and share purchase warrants, in the weighted average number of common shares outstanding during the period, if dilutive. The proceeds upon the exercise of the options and warrants are used to purchase common shares at the average market price during the period. During the years ended September 30, 2013 and 2012, all the outstanding stock options and warrants were anti-dilutive.

**Comprehensive loss**

Other comprehensive loss represents the change in net equity for the period that arises from unrealized gains and losses on available-for-sale financial instruments. Amounts included in other comprehensive loss are shown net of tax. Cumulative changes in other comprehensive loss are presented separately in the consolidated statement of changes in equity. The Company has no financial assets classified as available for sale, and accordingly, net loss is equivalent to comprehensive loss.

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**CANADA COAL INC.**  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
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**4. SIGNIFICANT ACCOUNTING POLICIES (Continued)**

**Use of estimates**

The preparation of these consolidated financial statements requires management to make estimates and assumptions that affect the reported amount of the assets and liabilities and the disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amount of revenues and expenses during the year. The impact of these estimates are pervasive throughout the financial statements and may require accounting adjustments based on future occurrences. Revisions to accounting estimates are recognized in the period in which the estimate is revised and future periods if the revision affects both current and future periods. Estimates are based on historical experience, current and future economic conditions and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Significant estimates made by the Company include factors affecting the recoverability of exploration and evaluation expenditures, valuation of restoration, rehabilitation and environmental obligations, inputs used for share-based payment transactions, inputs used for valuation of warrants and valuation of deferred tax assets and liabilities. Actual results could differ from those estimates.

The areas which require management to make significant judgments, estimates and assumptions in determining carrying values include, but are not limited to:

**Assets' carrying values and impairment charges**

In the determination of carrying values and impairment charges, management looks at the higher of recoverable amount or fair value less costs to sell in the case of assets and at objective evidence, significant or prolonged decline of fair value on financial assets indicating impairment. These determinations and their individual assumptions require that management make a decision based on the best available information at each reporting period.

**Capitalization of exploration and evaluation expenditures**

Management has determined that exploration and evaluation expenditures incurred during the year have future economic benefits and are economically recoverable. In making this judgment, management has assessed various sources of information including but not limited to the geologic and metallurgic information, proximity of operating facilities, operating management expertise and existing permits.

**Impairment of exploration and evaluation expenditures**

While assessing whether any indications of impairment exist for exploration and evaluation expenditures, consideration is given to both external and internal sources of information. Information the Company considers includes changes in the market, economic and legal environment in which the Company operates that are not within its control that could affect the recoverable amount of exploration and evaluation expenditures. Internal sources of information include the manner in which exploration and evaluation expenditures are being used or are expected to be used and indications of expected economic performance of the expenditures. Estimates include but are not limited to estimates of the discounted future after-tax cash flows expected to be derived from the Company's mining properties, costs to sell the properties and the appropriate discount rate. Reductions in metal price forecasts, increases in estimated future costs of production, increases in estimated future capital costs, reductions in the amount of recoverable mineral reserves and mineral resources and/or adverse current economics can result in a write-down of the carrying amounts of the Company's exploration and evaluation expenditures.

**Estimation of decommissioning and restoration costs and the timing of expenditure**

The cost estimates are updated annually to reflect known developments, (e.g. revisions to cost estimates and to the estimated lives of operations), and are subject to review at regular intervals. Decommissioning, restoration and similar liabilities are estimated based on the Company's interpretation of current regulatory requirements, constructive obligations and are measured at fair value. Fair value is determined based on the net present value of estimated future cash expenditures for the settlement of decommissioning, restoration or similar liabilities that may occur upon decommissioning of the mine. Such estimates are subject to change based on changes in laws and regulations and negotiations with regulatory authorities.

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**4. SIGNIFICANT ACCOUNTING POLICIES (Continued)**

**Use of estimates (Continued)**

Income taxes and recoverability of potential deferred tax assets

In assessing the probability of realizing income tax assets recognized, management makes estimates related to expectations of future taxable income, applicable tax planning opportunities, expected timing of reversals of existing temporary differences and the likelihood that tax positions taken will be sustained upon examination by applicable tax authorities. In making its assessments, management gives additional weight to positive and negative evidence that can be objectively verified. Estimates of future taxable income are based on forecasted cash flows from operations and the application of existing tax laws in each jurisdiction. Where applicable tax laws and regulations are either unclear or subject to ongoing varying interpretations, it is reasonably possible that changes in these estimates can occur that materially affect the amounts of income tax assets recognized. Also, future changes in tax laws could limit the Company from realizing the tax benefits from the deferred tax assets. The Company reassesses unrecognized income tax assets at each reporting period.

**Share-based payments**

Management determines costs for share-based payments using market-based valuation techniques. The fair value of the market-based and performance-based share awards are determined at the date of grant using generally accepted valuation techniques. Assumptions are made and judgment used in applying valuation techniques. These assumptions and judgments include estimating the future volatility of the stock price, expected dividend yield, future employee turnover rates and future employee stock option exercise behaviors and corporate performance. Such judgments and assumptions are inherently uncertain. Changes in these assumptions affect the fair value estimates.

**New accounting changes**

IAS 1 – Presentation of Financial Statements (“IAS 1”) was amended by the IASB in June 2011 in order to align the presentation of items in other comprehensive income with US GAAP standards. Items in other comprehensive income will be required to be presented in two categories: items that will be reclassified into profit or loss and those that will not be reclassified. The flexibility to present a statement of comprehensive income as one statement or two separate statements of profit and loss and other comprehensive income remains unchanged. At October 1, 2012, the Company adopted this standard and there was no material impact on the Company’s consolidated financial statements.

**Future accounting changes**

Certain new standards, interpretations and amendments to existing standards have been issued by the IASB or IFRIC that are mandatory for accounting periods beginning on or after October 1, 2013 or later periods.

IFRS 9 Financial Instruments: Classification and Measurement (“IFRS 9”), effective for annual periods beginning on or after January 1, 2015, with early adoption permitted, introduces new requirements for the classification and measurement of financial instruments. Management anticipates that this standard will be adopted in the Company’s consolidated financial statements for the period beginning October 1, 2015, and has not yet considered the potential impact of the adoption of IFRS 9.

IFRS 10 Consolidated Financial Statements (“IFRS 10”) provides a single model to be applied in the control analysis for all investees, including entities that currently are special purpose entities in the scope of SIC 12. In addition, the consolidation procedures are carried forward substantially unmodified from IAS 27 Consolidated and Separate Financial Statements. The Company intends to adopt IFRS 10 in its financial statements for the annual period beginning on October 1, 2013. The Company has not yet determined the impact of IFRS 10 on its consolidated financial statements.

IFRS 11 Joint Arrangements (“IFRS 11”) replaces the guidance in IAS 31 Interests in Joint Ventures. Under IFRS 11, joint arrangements are classified as either joint operations or joint ventures. IFRS 11 essentially carves out of previous jointly controlled entities, those arrangements which although structured through a separate vehicle, such separation is ineffective and the parties to the arrangement have rights to the assets and obligations for the liabilities and are accounted for as joint operations in a fashion consistent with jointly controlled assets/operations under IAS 31. In addition, under IFRS 11 joint ventures are stripped of the free choice of equity accounting or proportionate consolidation; these entities must now use the equity method.

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**4. SIGNIFICANT ACCOUNTING POLICIES (Continued)**

**Future accounting changes (Continued)**

Upon application of IFRS 11, entities which had previously accounted for joint ventures using proportionate consolidation shall collapse the proportionately consolidated net asset value (including any allocation of goodwill) into a single investment balance at the beginning of the earliest period presented. The investment's opening balance is tested for impairment in accordance with IAS 28 Investments in Associates and IAS 36 Impairment of Assets. Any impairment losses are recognized as an adjustment to opening retained earnings at the beginning of the earliest period presented. The Company intends to adopt IFRS 11 in its financial statements for the annual period beginning on October 1, 2013. The Company has not yet determined the impact of IFRS 11 on its consolidated financial statements.

IFRS 12 Disclosure of Interests in Other Entities ("IFRS 12") sets out the disclosure requirements for entities reporting under IFRS 10 and IFRS 11, and effective for years beginning on or after October 1, 2013, replaces the disclosure requirements currently found in IAS 28 Investments in Associates ("IAS 28"). The objective of IFRS 12 is to require the disclosure of information that enables users of financial statements to evaluate: (a) the nature of, and risks associated with, its interests in other entities; and (b) the effects of those interests on its financial position, financial performance and cash flows. The Company is currently evaluating the impact the introduction of IFRS 12 will have on its consolidated financial statements.

IFRS 13 Fair Value Measurement ("IFRS 13") converges IFRS and US GAAP on how to measure fair value and the related fair value disclosures. The new standard creates a single source of guidance for fair value measurements, where fair value is required or permitted under IFRS, by not changing how fair value is used but how it is measured. The focus will be on an exit price. IFRS 13 is effective for annual periods beginning on or after January 1, 2013, with early adoption permitted. The Company has not yet determined the impact of IFRS 13 on its consolidated financial statements.

IAS 28 Investments in Associates and Joint Ventures ("IAS 28") was issued by the IASB in May 2011 and supersedes IAS 28 Investments in Associates and prescribes the accounting for investments in associates and sets out the requirements for the application of the equity method when accounting for investments in associates and joint ventures. IAS 28 defines significant influence as the power to participate in the financial and operating policy decisions of the investee but is not control or joint control of those policies. IAS 28 also provides guidance on how the equity method of accounting is to be applied and also prescribes how investments in associates and joint ventures should be tested for impairment. The amendments to IAS 28 are effective for annual periods beginning on or after January 1, 2013. The Company is currently assessing the impact of this standard on its consolidated financial statements.

IAS 32 Financial Instruments: Presentation ("IAS 32") was amended by the IASB in December 2011 to clarify certain aspects of the requirements on offsetting. The amendments focus on the criterion that an entity currently has a legally enforceable right to set off the recognized amounts and the criterion that an entity intends either to settle on a net basis, or to realize the asset and settle the liability simultaneously. The amendments to IAS 32 are effective for annual periods beginning on or after January 1, 2014. Earlier adoption is permitted. The Company is currently assessing the impact of this standard on its consolidated financial statements.

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**5. CAPITAL MANAGEMENT**

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. Management considers the Company's capital structure to primarily consist of the components of shareholder's equity.

The properties in which the Company currently has an interest are in the exploration and evaluation stage; as such the Company is dependent on external financing to fund its activities. In order to carry out the planned exploration and pay for administrative costs, the Company will spend its existing working capital and raise additional amounts as needed. The Company will continue to assess new properties and seek to acquire an interest in additional properties if it feels there is sufficient geologic or economic potential and if it has adequate financial resources to do so.

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 significant changes in the Company's approach to capital management during the years ended September 30, 2013 and 2012. Neither the Company nor its subsidiaries are subject to externally imposed capital requirements.

**6. FINANCIAL RISK FACTORS**

There have been no changes in the risks, objectives, policies and procedures from the previous period. 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 receivables. The receivables primarily relate to sales tax and a refund of licence deposits due from the Federal Government of Canada. The Company has no significant concentration of credit risk arising from operations. Management believes that the credit risk concentration with respect to its receivables is remote.

**Liquidity risk**

The Company's approach to managing liquidity risk is to ensure that it will have sufficient liquidity to meet liabilities when due. All of the Company's financial liabilities have contractual maturities of less than 30 days and are subject to normal trade terms. The Company has sufficient cash to meet its current short and mid-term funding requirements however it will require further cash to fund its 2014 planned work program.

**Market risk**

**(a) Interest rate risk**

The Company has cash balances and no interest-bearing debt therefore, interest rate risk is minimal.

**(b) Foreign currency risk**

The majority of the Company's administrative expenditures are transacted in Canadian dollars. The Company funds certain expenses in the United States on a cash call basis using US dollar currency converted from its Canadian dollar bank accounts held in Canada. Management does not hedge its foreign exchange risk. A 1% change in foreign exchange rates between the Canadian and US dollar at September 30, 2013 would not have a significant impact on the Company's financial statements.

**(c) Price risk**

The Company is exposed to price risk with respect to commodity prices. The Company closely monitors commodity prices to determine the appropriate course of action to be taken by the Company.

**(d) Sensitivity analysis**

Based on management's knowledge and experience of the financial markets, the Company does not expect material movements in the underlying market risk variables over the next three-month period.

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**7. CASH AND CASH EQUIVALENTS**

The Company's short term money market instruments accrued interest between 1.25% to 1.35% (2012: 1.25% to 1.35%) per annum during the year and are redeemable at any time without penalty.

**8. RECEIVABLES**

The receivables balance is comprised of the following items:

	September 30, 2013	September 30, 2012
Sales tax due from Federal Government	\$ 13,157	\$ 85,114
License fees	63,555	-
Other	-	1,460
<b>Total</b>	<b>\$ 76,712</b>	<b>\$ 86,574</b>

**9. PREPAID EXPENSES**

The prepaid expense balance is comprised of the following items:

	September 30, 2013	September 30, 2012
Consulting	\$ 23,435	\$ -
Insurance	6,576	6,576
Promotion	7,250	-
<b>Total</b>	<b>\$ 37,261</b>	<b>\$ 6,576</b>

**10. EQUIPMENT**

	Equipment	Vehicles	Total
<b>Cost</b>			
Balance September 30, 2011	\$ -	\$ -	\$ -
Acquisitions	14,945	17,696	32,641
Balance September 30, 2012 and 2013	14,945	17,696	32,641
<b>Accumulated amortization</b>			
Balance, September 30, 2011	\$ -	\$ -	\$ -
Amortization	996	1,968	2,964
Balance, September 30, 2012	996	1,968	2,964
Amortization	2,988	5,904	8,892
Balance, September 30, 2013	3,984	7,872	11,856
<b>Carrying Value</b>			
At September 30, 2012	\$ 13,949	\$ 15,728	\$ 29,677
At September 30, 2013	\$ 10,961	\$ 9,824	\$ 20,785

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**11. INVESTMENT**

In October 2012, the Company acquired a 25% interest in Nord Iron Mines ("Nord Iron"), a private company. The Company exercises significant influence over Nord Iron and accordingly accounts for its investment on an equity method basis. Nord Iron acquired mineral interests in certain claims; however, title ownership is currently being litigated. During the period ended September 30, 2013, the Company has recorded an equity loss of \$8,750 with respect to its investment in Nord Iron. (Note 13)

**12. EXPLORATION AND EVALUATION EXPENDITURES**

On September 15, 2010, the Company entered into an agreement with Weststar Resources Corp. ("Weststar") to purchase the outstanding capital of Weststar's wholly-owned subsidiary, Canadian Sovereign Coal Corp. ("CSCC"). CSCC's only assets were an 80% interest in nine coal exploration licences and eight coal exploration licence applications located in Ellesmere Island, Nunavut. Weststar's 80% interest in the claims was acquired pursuant to a Letter of Intent dated March 18, 2009 between Hunter Exploration Group ("Hunter") and Weststar.

On September 20, 2010, the Company, Weststar and Hunter entered into an agreement whereby Weststar was released from any obligations or commitments under the original Letter of Intent dated March 18, 2009 and a 100% interest in the coal licences and licence applications was transferred to CSCC. As consideration for the September 15, 2010 and September 20, 2010 agreements, in December 2010, the Company issued 500,000 common shares valued at \$50 to Weststar and 1,000,000 common shares valued at \$100 to Hunter. In addition, commencing on December 1, 2013, the Company is obligated to pay \$50,000 representing annual advance royalty payments in connection with the licences. Hunter retained a 2% royalty on the licenses of which 1% can be purchased by the Company for \$1,000,000.

On April 12, 2011, the Company entered into an agreement to purchase all of the issued and outstanding capital of 5200 Nunavut Ltd. ("5200") from arm's length third party vendors. The only assets held by 5200 were interests in seven coal exploration licences located in Nunavut. As consideration for the acquisition, the Company paid \$15,700 and issued 1,000,000 shares valued at \$140,000.

During fiscal 2011, the Company also applied for 51 coal exploration licences which have been granted. In August 2012, the Company applied for an additional 11 coal exploration licences. The licences for these applications were granted in April 2013. In May 2013, the Company applied for two coal exploration licences near Pond Inlet on Baffin Island.

In June 2013, seven of the licence blocks held by the Company expired. The Company submitted applications to reacquire the area covered by the expired licences.

On July 26, 2013, twenty coal licences located in Axel Heiberg expired. The acquisition and maintenance fee costs related to those claims have been written off accordingly.

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**12. EXPLORATION AND EVALUATION EXPENDITURES (Continued)**

During the years ended September 30, 2013 and September 30, 2012, expenditures incurred on mineral claims were as follows:

	September 30, 2013	September 30, 2012
Acquisition costs:		
Balance, beginning of the year	\$ 280,022	\$ 265,829
Additions during the year	10,877	14,193
Write offs during the year	(39,849)	-
Acquisitions, end of year	<u>251,050</u>	<u>280,022</u>
Deferred exploration costs:		
Balance, beginning of the year	4,061,657	528,907
Geologists and consultants	359,238	1,087,822
Permitting	1,910	14,550
Community consultation	7,318	47,745
Assays	-	43,338
Field supplies	-	36,860
Equipment rental (recovery)	(905)	58,117
Transportation	-	1,239,694
Fuel	-	181,904
License, maintenance fees	-	260,037
Travel, meals and accommodation	65,392	528,900
Amortization	8,892	2,964
Administrative and other expenses	5,278	30,819
	<u>4,508,780</u>	<u>4,061,657</u>
Write offs during the year	(79,699)	-
Deferred exploration, end of year	<u>4,429,081</u>	<u>4,061,657</u>
Total exploration and evaluation expenditures, end of year	<u>\$ 4,680,131</u>	<u>\$ 4,341,679</u>

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**13. RELATED PARTY TRANSACTIONS**

Related parties include the Board of Directors, Executive Officers and any companies owned or controlled by them or any companies where they are also a director or officer.

*Trading Transactions*

The Company entered into the following transactions with related parties

	Nature of transactions	Notes	Year ended September 30, 2013	Year ended September 30, 2012
West Oak Capital	Management fees	a	\$ 96,000	\$ 108,000
Abraham Jonker	Management fees	b	\$ 96,000	\$ 162,000
Olga Nikitovic	Management fees	c	\$ 60,000	\$ 69,000
Aird & Berlis	Legal fees	d	\$ 16,355	\$ 177,358
Evolving Gold	Rent	e	\$ 18,000	\$ 12,000

a) West Oak Capital Partners Inc. ("West Oak") is owned by R. B. Duncan, the Company's CEO until February 23, 2012 at which time Mr. Duncan became the Executive Chairman of the Board. The fees paid to West Oak are included in management fees.

b) Abraham Jonker became CEO of the Company on February 23, 2012. His fees are included in management fees. The 2012 fees included a \$90,000 signing bonus.

c) Olga Nikitovic is the CFO of the Company. The fees paid relate to financial management and accounting services and are classified as management fees.

d) Tom Fenton, Director and Corporate Secretary for the Company is a partner with Aird & Berlis LLP. Fees relate to legal services. General corporate legal fees of \$16,355 (2012: \$137,525) are reflected as professional fees, fees related to the private placements of \$Nil (2012: \$39,833) are reflected as share issue costs. Legal fees included in accounts payable at September 30, 2013 are \$559 (2012: \$1,875).

e) The Company shares office space with Evolving Gold Corp. ("Evolving Gold") and accordingly pays rent of \$1,500 per month to Evolving Gold. The Company and Evolving Gold share one common officer and two common directors. The costs are included in office, rent and miscellaneous expense.

f) The Company acquired a 25% interest in Nord Iron through the acquisition of 4,000,000 shares valued at \$50,000. Officers and directors of the Company are shareholders of Nord Iron. (Note 11)

*Compensation of key management personnel*

	Notes	Year ended September 30, 2013	Year ended September 30, 2012
Salaries	a	\$ 252,000	\$ 339,000
Share-based payments	b	\$ 6,049	\$ 746,779
<b>Total</b>		<b>\$ 258,049</b>	<b>\$ 1,085,779</b>

a) The Company does not pay any directors' fees nor does the Company pay any health or post employment benefits. The salaries include the fees for the Executive Chairman, CEO and CFO included in trading transactions above.

b) Share-based payments are the fair value of options granted to key management and directors.

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**14. REVERSE ACQUISITION**

Mercury Capital and the Company signed a definitive agreement (“Agreement”) dated November 4, 2011. Under the terms of the Agreement, holders of common shares and other securities such as options and warrants of Canada Coal and Mercury Capital, each received common shares and other securities of the resulting issuer on a one for one basis. The amalgamation constituted a qualifying transaction for Mercury Capital as defined in Policy 2.4 of the Exchange's Corporate Finance Manual. The resulting issuer was named Canada Coal Inc. The amalgamation was completed on February 23, 2012.

As a result of the transaction, the former shareholders of the original Canada Coal owned 92% of the outstanding shares of the amalgamated entity. In accordance with IFRS 3, Business Combinations, the substance of the transaction is a reverse acquisition of a non-operating company. The transaction does not constitute a business combination as Mercury Capital did not meet the definition of a business under that standard. As a result, the transaction is accounted for as a capital transaction with the original Canada Coal being identified as the acquirer and the equity consideration being measured at fair value. The resulting financial statements are presented as a continuance of the original Canada Coal.

IFRS 2 applies to transactions where an entity grants equity instruments and cannot identify specifically some or all of the goods or service received in return. Because Canada Coal issued shares with a value in excess of the assets received, IFRS 2 would indicate that the difference is recognized in comprehensive loss as a reverse takeover transaction cost. The amount recognized as a reverse transaction cost is the difference between the fair value of the consideration paid and the net identifiable assets of Mercury Capital acquired by Canada Coal and included in the consolidated statement of loss and comprehensive loss.

The transaction recognizes the acquisition of all of the shares of Mercury Capital by Canada Coal. The fair value of Canada Coal's shares based on the value from the private placement described in 15(b) is \$0.41 per share (price of the unit less fair value of warrants). The fair value of the options and warrants issued as consideration was determined using the Black Scholes option pricing model. The fair value of the shares issued was \$1,373,398, and the fair value of options and warrants issued was \$138,769 and \$6,048, respectively.

Based on Mercury Capital's statement of financial position at the time of the reverse takeover, the net assets at fair value that were acquired by Canada Coal were \$330,445 and the resulting reverse acquisition cost charged to the statements of loss and comprehensive loss was as follows:

Consideration		
Shares (Note 15(d))		\$1,373,398
Options		138,769
Warrants		6,048
		<u>\$1,518,215</u>
Identifiable assets acquired		
Cash		\$318,633
Other receivables		17,812
Account payable and accrued liabilities		(6,000)
Unidentifiable assets acquired		
Reverse takeover transaction cost		1,187,770
Total net identifiable assets and reverse takeover transaction cost		<u>\$1,518,215</u>

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**15. CAPITAL STOCK, STOCK OPTIONS AND WARRANTS**

**Capital Stock**

The Company has authorized an unlimited number of common shares without par value. As at September 30, 2013, the Company had 43,449,750 common shares outstanding (2012: 43,449,750) and 4,275,000 common shares held in escrow (2012: 7,125,000).

For the year ended September 30, 2013, the Company entered into the following capital stock transactions:

- a) In July 2013, 200,000 stock options were granted to a director. The stock options have an exercise price of \$0.20 and have a life of five years. The options had a grant date fair value of \$6,049 determined using the Black-Scholes option pricing model.

For the year ended September 30, 2012, the Company entered into the following capital stock transactions:

- b) On November 4, 2011, the Company closed a private placement in which it issued 6,500,000 flow-through units and 2,100,000 subscription receipts for units at \$0.50 per unit for gross proceeds of \$4,300,000.

Each flow through unit consisted of one common share and one half of one common share purchase warrant. Each whole warrant is exercisable at \$0.80 for three years from the date of closing. \$585,000 of the flow-through proceeds has been allocated to warrants.

The proceeds from the issuance of subscription receipts were held in escrow until the amalgamation was complete. The 2,100,000 subscription units were issued for gross proceeds of \$1,050,000 of which \$168,157 has been allocated to warrants. In February 2012, each holder of a subscription unit received one common share and one half of one common share purchase warrant exercisable at \$0.80 for three years from the date of closing.

Finders' fees of \$301,000 cash were paid and 602,000 broker warrants valued at \$110,570 were issued. The broker warrants are exercisable at \$0.80 for a period of three years and were valued using the Black-Scholes pricing model. \$19,903 of the value of these broker warrants were allocated to the warrants issued in the private placement. Total cash issue costs were \$430,808 of which \$75,443 were allocated to warrants issued in the private placement.

- c) In November 2011, 2,100,000 stock options were granted to directors. The stock options have an exercise price of \$0.50 and have a life of five years. The options had a grant date fair value of \$746,779 determined using the Black-Scholes option pricing model.
- d) The seed shareholders contributed an additional \$49,127 for their shares to comply with founder share limits set by the Exchange.
- e) On February 23, 2012, the Company issued 3,349,750 shares valued at \$1,373,398, 419,950 options valued at \$138,769 and 25,000 warrants valued at \$6,048 for the acquisition of the net assets of Mercury Capital. (Note 14)

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**15. CAPITAL STOCK, STOCK OPTIONS AND WARRANTS (Continued)**

**Share purchase warrants**

At September 30, 2013, warrants were outstanding enabling holders to acquire shares as follows:

Expiry Date	Exercise Price \$	Warrants Outstanding and Exercisable	
		Number of Warrants Outstanding	Weighted average remaining contractual life (years)
March 1, 2014	0.30	21,500,000	0.42
November 4, 2014	0.80	4,902,000	1.09
		26,402,000	0.54

The following is a summary of the warrant transactions for the years ended September 30, 2013 and 2012.

	Year ended September 30, 2013		Year ended September 30, 2012	
	Number Of Warrants	Weighted Average Exercise Price \$	Number Of Warrants	Weighted Average Exercise Price \$
Balance, beginning of the year	28,027,000	0.38	23,100,000	0.29
Warrants issued pursuant to private placements	-	-	4,300,000	0.80
Warrants issued to brokers pursuant to private placements	-	-	602,000	0.80
Warrants issued pursuant to acquisition of Mercury Capital (Note 14)	-	-	25,000	0.20
Warrants expired	(1,625,000)	0.20	-	-
Balance, end of year	26,402,000	0.39	28,027,000	0.38

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**15. CAPITAL STOCK, STOCK OPTIONS AND WARRANTS (Continued)**

The following weighted average assumptions were used for the Black-Scholes valuation of warrants issued for the years ended September 30, 2013 and 2012.

	Year ended September 30, 2013	Year ended September 30, 2012
Risk-free interest rate	-	1.10%
Expected life of warrants	-	2.92 years
Expected annualized volatility	-	92.5%
Expected dividend rate	-	0.00%

**Stock options**

The Company may grant stock options pursuant to a stock option plan (the "Plan") which was established in accordance with the policies of the TSX Venture Exchange. The Board of Directors administers the Plan, pursuant to which the Board may grant from time to time incentive stock options up to an aggregate maximum of 10% of the issued and outstanding shares of the Company to directors, officers, employees, consultants or advisors. The options can be granted for a maximum of 10 years.

As at September 30, 2013, the following incentive stock options were outstanding:

Expiry Date	Exercise Price \$	Options Outstanding and Exercisable	
		Number of Options Outstanding and Exercisable	Weighted average remaining contractual life (years)
February 21, 2016	0.20	1,000,000	2.40
June 21, 2016	0.20	100,000	2.73
August 1, 2016	0.20	500,000	2.83
November 1, 2016	0.50	200,000	4.08
November 4, 2016	0.50	1,600,000	3.09
July 2, 2018	0.20	200,000	4.76
January 28, 2021	0.20	259,975	7.33
		<u>3,859,975</u>	<u>3.29</u>

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**15. CAPITAL STOCK, STOCK OPTIONS AND WARRANTS (Continued)**

**Stock options (Continued)**

The following is a summary of the stock option transactions for the years ended September 30, 2013 and 2012.

	Year ended September 30, 2013		Year ended September 30, 2012	
	Number Of Options	Weighted Average Exercise Price \$	Number Of Options	Weighted Average Exercise Price \$
Balance, beginning of the year	3,819,950	0.34	1,600,000	0.20
Options granted	200,000	0.20	2,100,000	0.50
Options issued pursuant to acquisition of Mercury Capital (Note 14)	-	-	419,950	0.20
Options expired	(159,975)	0.20	(300,000)	0.20
Balance, end of year	3,859,975	0.34	3,819,950	0.34

The following weighted average assumptions were used for the Black-Scholes valuation of options granted for the years ended September 30, 2013 and 2012.

	Year ended September 30, 2013	Year ended September 30, 2012
Risk-free interest rate	1.77%	1.45%
Expected life of options	5.0 years	5.2 years
Expected annualized volatility	108.64%	131.80%
Expected dividend rate	0.00%	0.00%

**Share-based compensation**

The Company granted 200,000 options during the year ended September 30, 2013 (2012: 2,100,000). The options vested immediately upon grant. Total share-based compensation for the year ended September 30, 2013 was \$6,049 (2012: \$746,779) and has been expensed with a corresponding amount being recorded in the equity settled share-based payments reserve.

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**16. SUPPLEMENTAL DISCLOSURE WITH RESPECT TO CASH FLOWS**

Significant non-cash financing and investing transactions for the year ended September 30, 2013 consisted of:

- a) Decrease in accrued exploration and evaluation expenditures of \$180,112.
- b) Increase in prepaid exploration and evaluation expenditures of \$23,435.
- c) Increase in receivables related to exploration and evaluation expenditures of \$63,555.
- d) Amortization in exploration and evaluation expenditures of \$8,892.

Significant non-cash financing and investing transactions for the year ended September 30, 2012 consisted of:

- a) The issuance of warrants for services valued at \$110,570.
- b) Increase in accrued exploration and evaluation expenditures of \$111,705.
- c) Decrease in accrued prepaid transaction costs of \$11,672.
- d) Issued 3,349,750 shares valued at \$1,373,398, 419,950 options valued at \$138,769 and 25,000 warrants valued at \$6,048 to Mercury Capital for the acquisition of net assets of Mercury Capital.
- e) Amortization in exploration and evaluation expenditures of \$2,964.

**17. INCOME TAXES**

A reconciliation of income taxes at the statutory rate of 27% (2012: 27%) with the reported taxes is as follows:

	2013	2012
	\$	\$
Net loss before income taxes	(709,614)	(2,654,327)
Expected income tax (recovery)	(191,000)	(722,000)
Share-based compensation	2,000	203,000
Tax assets acquired on acquisition of Mercury Capital	-	(60,000)
Flow-through renunciation	-	861,000
RTO transaction costs not recognized	-	323,000
Other	(50,642)	5,000
Deferred income tax (recovery) expense	(239,642)	610,000

The significant components of the Company's deferred income tax assets and liabilities are as follows:

	2013	2012
	\$	\$
Deferred income tax assets (liabilities)		
Mineral properties and exploration expenditures	(385,000)	(610,000)
Share issue costs	133,000	186,000
Non capital loss carryforwards	126,000	76,000
Other temporary differences	7,000	-
Net deferred tax liability	(119,000)	(348,000)

As at September 30, 2013, the Company had approximately \$135,000 of Canadian development expenditures and \$2,949,000 of Canadian exploration expenditures which, under certain circumstances, may be used to reduce taxable income of future years. The Company has share issue costs deductible in future years of approximately \$496,000. The Company has non-capital losses of approximately \$472,000 available for deduction against future taxable income and expiring between the years 2029 and 2033.

Continued...

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**18. SEGMENTED INFORMATION**

The Company primarily operates in one reportable operating segment, being the acquisition and exploration of mineral properties in Canada. As the operations comprise in a single reporting segment, amounts disclosed in the consolidated financial statements also represent segment amounts.

**19. COMMITMENTS AND CONTINGENCIES**

The Company's exploration and evaluation 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.

The Company entered into certain management contracts which contain clauses requiring additional payments of up to \$480,000 to be made upon the occurrence of certain events such as a change of control. As a trigger event has not taken place, the contingent payments have not been reflected in these consolidated financial statements.

**20. SUBSEQUENT EVENT**

Subsequent to September 30, 2013, the Company granted 200,000 options exercisable at \$0.20 per share for five years to a director of the Company.