PROPHECY RESOURCE CORP.

FINANCIAL STATEMENTS

December 31, 2009
(Unaudited – prepared by management)

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 consolidated 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 consolidated 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 the standards established by the Canadian Institute of Chartered Accountants for a review of interim financial statements by an entity's auditor.

PROPHECY RESOURCE CORP.
INTERIM BALANCE SHEETS
AS AT DECEMBER 31, 2009
(Unaudited – prepared by management)

	December 31, 2009	September 30, 2009 (audited)
ASSETS		
Current		
Cash	$ 1,839,827	$ 8,776
Short-term investments (Note 3)	-	60,000
Receivables	3200	447
Prepaids	18,256	-
	1,861,283	69,223
Mineral property (Note 4)	1,176,614	150,750
Deferred exploration costs (Note 5)	1,021,535	1,019,869
Reclamation bond (Note 4)	6500	6,500
	$ 4,065,933	$ 1,246,342
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current		
Accounts payable and accrued liabilities	$ 47,371	$ 13,219
Due to related parties	40,000	-
	87,371	13,219
Future income taxes (Note 10)	46,329	46,329
	133,700	59,548
SHAREHOLDERS' EQUITY		
Share capital (Note 7)	4,201,412	1,388,802
Share purchase warrants	56,789	-
Contributed surplus (Note 7)	332,979	201,531
Deficit	(658,947)	(403,539)
	3,932,233	1,186,794
	$ 4,065,933	$ 1,246,342

Nature and continuance of operations (Note 1)
Commitment (Note 4)
Subsequent events (Note 13)

Approved on behalf of the Board:

"Stuart Rogers" Director ______________________ Director
Stuart Rogers John Lee

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

PROPHECY RESOURCE CORP.
INTERIM STATEMENTS OF LOSS, COMPREHENSIVE LOSS AND DEFICIT
(Unaudited – prepared by management)

	For the three months ended December 31, 2009	For the three months ended December 31, 2008
EXPENSES		
Investor relations – stock-based compensation (Note 8)	$ -	$ 3,940
Consulting	19,000	-
Consulting –stock based compensation	31,283	-
Management –stock based compensation	100,165	-
Office, rent and miscellaneous (Note 6)	5,335	4,702
Management fees (Note 6)	41,000	4,500
Professional fees	7,963	-
Shareholder communications	19,746	11,790
Transfer agent and filing fees	8,789	3,187
Travel	22,506	-
LOSS BEFORE OTHER ITEM	255,788	(28,119)
OTHER ITEM		
Interest income	380	3,206
LOSS BEFORE INCOME TAXES	(255,408)	(24,913)
	-	-
NET LOSS AND COMPREHENSIVE LOSS	(255,408)	(24,913)
DEFICIT, BEGINNING	(403,539)	(337,127)
DEFICIT, ENDING	$ (658,947)	$ (362,040)
LOSS PER COMMON SHARE - BASIC AND DILUTED	$ (0.02)	$ (0.01)
WEIGHTED AVERAGE NUMBER OF COMMON SHARES OUTSTANDING – BASIC AND DILUTED	11,274,243	11,100,000

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

PROPHECY RESOURCE CORP.
STATEMENTS OF CASH FLOWS
(Unaudited – prepared by management)

	For the three months ended December 31, 2009	For the three months ended December 31, 2008
CASH FLOWS FROM OPERATING ACTIVITIES		
Net loss	$ (255,408)	$ (24,193)
Items not involving cash:		
Stock based compensation	188,237	3,940
Changes in non-cash working capital items:		
Decrease in receivables	(2,753)	2,376
Decrease in prepaids	(18,256)	-
Increase (decrease) in accounts payable and accrued liabilities	74,152	(7,645)
Decrease in due to related parties	-	(5,308)
Net cash provided by (used in) operating activities	(14,028)	(31,550)
CASH FLOWS USED IN INVESTING ACTIVITIES		
Short-term investments redemptions	60,000	35,000
Acquisition of mineral property	(1,027,531)	(18,375)
Deferred exploration costs	-	-
Net cash provided by (used in) investing activities	(967,531)	16,625
CASH FLOWS FROM FINANCING ACTIVITIES		
Shares issued, net of share issuance costs	2,812,610	-
Net cash provided by financing activities	2,812,610	-
Decrease (Increase) in cash	(1,831,051)	(14,925)
Cash, beginning	8,776	17,787
Cash, ending	$ 1,839,827	$ 2,862

Supplemental disclosures with respect to cash flows (Note 9)

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

1. NATURE AND CONTINUANCE OF OPERATIONS

Prophecy Resource Corp. (the "Company") was incorporated under the Business Corporations Act (British Columbia) on February 9, 2006 and trades publicly on the TSX Venture Exchange ("TSX-V").

The Company is a mineral property exploration company and has not yet determined whether its mineral properties contain economically recoverable reserves. The recoverability of the amounts shown for mineral properties is dependent upon the confirmation of economically recoverable reserves, the ability of the Company to obtain necessary financing to successfully complete their development and upon future profitable production.

These financial statements have been prepared on a going concern basis which assumes that the Company will be able to realize its assets and discharge its liabilities in the normal course of business for the foreseeable future. The continuing operations of the Company are dependent upon its ability to raise adequate financing to develop its mineral properties, and to commence profitable operations in the future. To date the Company has not generated any significant revenues and is considered to be in the exploration stage.

Management is also aware that material uncertainties exist, related to current economic conditions, which could adversely affect the Company's ability to continue to finance its activities. Management's plan includes continuing to pursue additional sources of financing through equity offerings, seeking joint venture partners to fund exploration, monitoring exploration activity and reducing overhead costs. As a result of the implementation of this plan, management expects that the Company will have sufficient capital to fund operations and keep its mineral property in good standing for the upcoming fiscal year. Further discussion of liquidity risk has been disclosed in Notes 11 and 12.

These financial statements do not include any adjustments relating to the recoverability and classification of recorded asset amounts and classification of liabilities that might be necessary should the Company be unable to continue in existence.

2. SIGNIFICANT ACCOUNTING POLICIES

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

Use of estimates
The preparation of financial statements in conformity with Canadian GAAP requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amount of revenues and expenses during the period. Actual results could differ from these estimates. Significant areas requiring the use of management estimates relate to the determination of impairment of mineral property interests, expected tax rates for future income tax recoveries, the fair values of financial instruments, determining the fair value of stock-based payments and management's assessment of going concern. Where estimates have been used financial results as determined by actual events could differ from those estimates.

Government grants
Government assistance is recorded as either a reduction of the cost of the applicable assets or credited in the statement of loss as determined by the terms and conditions of the agreement under which the assistance is provided to the Company. Claims for tax credits are accrued upon the Company attaining reasonable assurance of collection from the Canadian tax authorities.

2. SIGNIFICANT ACCOUNTING POLICIES (cont'd…)

Mineral properties
The Company records its interests in mineral properties and areas of geological interest at cost. All direct and indirect costs relating to the acquisition 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 an 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. Mineral properties which are sold before that property reaches the production stage will have all revenues from the sale of the property credited against the cost of the property. Properties which have reached the production stage will have a gain or loss calculated based on the portion of that property sold.

The recorded cost of mineral exploration interests is based on cash paid, the value of share considerations and exploration and development costs incurred. The recorded amount may not reflect recoverable value as this will be dependent on the development program, the nature of the mineral deposit, commodity prices, adequate funding and the ability of the Company to bring its projects into production.

Management evaluates the carrying value of each mineral interest on a reporting period basis or as changes in events and circumstances warrant, and makes a determination based on exploration activity and results, estimated future cash flows and availability of funding as to whether capitalized costs are impaired. Mineral property interests, where future cash flows are not reasonably determinable, are evaluated for impairment based on management's intentions and determination of the extent to which future exploration programs are warranted and likely to be funded.

Ownership in mineral interests involves certain inherent risks due to the difficulties of determining and obtaining clear title to the claims as well as the potential for problems arising from the frequently ambiguous conveyancing history characteristic of many mineral interests.

Deferred exploration costs
The Company defers all exploration costs relating to mineral properties and areas of geological interest until the properties to which they relate are placed into production, sold, abandoned or management has determined there to be an impairment. These costs will be amortized on the basis of units produced in relation to the estimated reserves available on the related property following commencement of production or written-off to operations in the period related properties are abandoned.

Values
The amounts shown for mineral properties and deferred exploration costs represent costs incurred to date, net of impairments, and do not necessarily represent present or future values which are entirely dependent upon the economic recovery from production or from disposal.

Asset retirement obligations
The Company has adopted the Canadian Institute of Chartered Accountants ("CICA") Handbook section 3110, "Asset retirement obligations". This standard focuses on the recognition and measurement of liabilities related to obligations associated with the retirement of property, plant and equipment. Under this standard, these obligations are initially measured at fair value and subsequently adjusted for any changes resulting from the passage of time and revisions to either the timing or the amount of the original estimate of undiscounted cash flows. The asset retirement cost is to be capitalized to the related asset and amortized into earnings over time.

Mineral property related retirement obligations are capitalized as part of deferred exploration and development costs and amortized over the estimated useful lives of the corresponding mineral property.

At December 31, 2009 and 2008, management has determined that there are no material asset retirement obligations to the Company.

2. SIGNIFICANT ACCOUNTING POLICIES (cont'd…)

Impairment of long-lived assets

The Company follows the recommendations of the CICA Handbook section 3063, "Impairment of Long-Lived Assets". Section 3063 establishes standards for recognizing, measuring and disclosing impairment of long-lived assets held for use. The Company conducts its impairment test on long-lived assets when events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment is recognized when the carrying amount of an asset to be held and used exceeds the undiscounted future net cash flows expected from its use and disposal. If there is an impairment, the impairment amount is measured as the amount by which the carrying amount of the asset exceeds its fair value, calculated using discounted cash flows when quoted market prices are not available.

Financial instruments

The Company adopted the CICA Handbook Sections 3855, "Financial Instruments – Recognition and Measurement"; Section 3856, "Hedges"; Section 3862, "Financial Instruments – Disclosures" and Section 3863 "Financial Instruments Presentation". Section 3855 prescribes when a financial instrument is to be recognized on the balance sheet and at what amount. Under Section 3855, financial instruments must be classified into one of five categories: held-for-trading, held-to-maturity, loans and receivables, available-for-sale financial assets, or other financial liabilities. All financial instruments, including derivatives, are measured at the balance sheet date at fair value except for loans and receivables, held-to-maturity investments, and other financial liabilities which are measured at amortized cost. Section 3862 and Section 3863 replace Section 3861, "Disclosure and Presentation" and revise and enhance disclosure requirements while carrying forward presentation requirements.

The Company's financial instruments consist of cash, short-term investments, receivables, reclamation bond, accounts payable and due to related parties. Unless otherwise noted, it is management's opinion that the Company is not exposed to significant interest, currency, or credit risks arising from these financial instruments. The Company has made the following classifications for the financial instruments:

(i) Cash and short-term investments – held-for-trading; measured at fair value;
(ii) Receivables – loans and receivables; measured at amortized cost;
(iii) Reclamation bond – held to materiality; measured at amortized costs; and
(iv) Accounts payable and due to related parties – other financial liabilities; recorded at amortized cost.

Fair value estimates are made at the balance sheet date, based on relevant market information and other information about financial instruments, and approximate carrying values unless otherwise noted.

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

The Company does not use any hedging instruments.

Future income taxes

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

2. SIGNIFICANT ACCOUNTING POLICIES (cont'd…)

Stock-based compensation
The Company has adopted the accounting standards issued by the CICA Handbook Section 3870, "Stock-based compensation and other stock-based payments", which recommends the fair-value based method for measuring compensation costs. The Company determines the fair value of the stock-based compensation using the Black-Scholes option pricing model.

Comprehensive income
The Company adopted CICA Handbook Section 1530, "Comprehensive Income". Section 1530 establishes standards for the reporting and presenting of comprehensive income which is defined as the change in equity from transaction and other events from non-owner sources. Other comprehensive income refers to items recognized in comprehensive income that are excluded from net income (loss). At September 30, 2009 and 2008 the Company had no significant items that caused other comprehensive loss to be different than net loss.

Loss per share
The Company uses the treasury stock method to compute the dilutive effect of options, warrants and similar instruments. Under this method the dilutive effect on loss per share is recognized on the use of the proceeds that could be obtained upon exercise of options, warrants and similar instruments. It assumes that the proceeds would be used to purchase common shares at the average market price during the period. Basic and diluted loss per common share are calculated using the weighted-average number of common shares outstanding during the period. For the periods presented, dilutive loss per share is equal to basic loss per share.

Flow-through shares
The Company provides certain share subscribers with a flow-through component for tax incentives available on qualifying Canadian exploration expenditures. The Company renounces the qualifying expenditures upon the issuance of the respective flow-through common shares and accordingly is not entitled to the related taxable income deductions from such expenditures.

The Company has adopted the recommendation by the Emerging Issues Committee ("EIC") of the CICA relating to the recording of flow-through shares. EIC 146 stipulates that future income tax liabilities resulting from the renunciation of qualified resource expenditures by the Company from the issuance of flow-through shares are recorded as a reduction of share capital. Any corresponding realization of future income tax benefits resulting in the utilization of prior year losses available to the Company not previously recorded, whereby the Company did not previously meet the criteria for recognition, are reflected as part of the Company's operating results in the period the Company files the appropriate tax documents with the Canadian tax authorities.

Accounting changes
CICA Handbook Section 1506, "Accounting Changes," establishes criteria for changes in accounting policies, accounting treatment and disclosure regarding changes in accounting policies, estimates and corrections of errors. In particular, this section allows for voluntary changes in accounting policies only when they result in the financial statements providing reliable and more relevant information. This section requires changes in accounting policies to be applied retrospectively unless doing so is impracticable.

Capital disclosure
CICA Handbook Section 1535 "Capital Disclosure", specifies the disclosure of (i) an entity's objectives, policies and processes for managing capital; (ii) quantitative data about what the entity regards as a capital; (iii) whether the entity has not complied with any capital requirements; and (iv) if it has not complied, the consequences of such noncompliance. The Company has included disclosures recommended by this new section in Note 11 to these financial statements.

General standards for financial statement presentation
In June 2007, the CICA modified section 1400 "General Standards of Financial Statement Presentation" in order to require that management make an assessment of the Company's ability to continue as going concern over a period which is at least, but not limited to, twelve months from the balance sheet date. The Company has included this required disclosure in Note 1 to these financial statements.

2. SIGNIFICANT ACCOUNTING POLICIES (cont'd…)

Credit risk and the fair value of financial assets and financial liabilities
In January 2009, the CICA approved EIC 173, "Credit Risk and the Fair Value of Financial Assets and Liabilities". This guidance clarified that an entity's own credit risk and the credit risk of the counterparty should be taken into account in determining the fair value of financial assets and financial liabilities including derivative instruments. The implementation of the recommendations of this new section has not had a material impact on the Company's financial statements.

Mining exploration costs
In March 2009 the CICA approved EIC 174, "Mining Exploration Costs". The guidance clarified that an enterprise that has initially capitalized exploration costs has an obligation in the current and subsequent accounting periods to test such costs for recoverability whenever events or changes in circumstances indicate that its carrying amount may not be recoverable. The implementation of the recommendations of this new section has not had a material impact on the Company's financial statements.

Recent accounting pronouncements
In 2006, the Canadian Accounting Standards Board ("AcSB") published a strategic plan that will significantly affect financial reporting requirements for Canadian companies. The AcSB strategic plan outlines the convergence of Canadian generally accepted accounting principles with International Financial Reporting Standards ("IFRS") over an expected five year transitional period. In February 2008, the AcSB announced that 2011 is the changeover date for publicly-listed companies to use IFRS, replacing Canada's own generally accepted accounting principles. The date is for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2011. The transition date of January 1, 2011 will require the restatement for comparative purposes of amounts reported by the Company for the year ended September 30, 2010. The Company continues to monitor and assess the impact of Canadian GAAP and IFRS.

Other accounting pronouncements issued by the CICA with future affective dates are either not applicable or are not expected to be significant to the financial statements of the Company.

3. SHORT-TERM INVESTMENTS

Short-term investments consists of highly liquid Canadian dollar denominated guaranteed investment certificates with term to maturity of greater than ninety days but not more than one year. The counter-parties are financial institutions. At September 30, 2009, the instruments were yielding an annual interest rate of 1.70 %. The fair market value of the Company's short-term investment approximates its carrying value at the balance sheet dates.

4. MINERAL PROPERTY

	December 31, 2009	December 31, 2008
Okeover Property, British Columbia, Canada	$ 150,750	$ 107,375
Lynn Lake Project, Manitoba, Canada	1,025,864	-
	$ 1,176,614	$ 107,375

Title to mining properties involves certain inherent risks due to the difficulties of determining the validity of certain claims as well as the potential for problems arising from the frequently ambiguous conveyancing history characteristic of many mining properties. The Company has investigated title to its mineral property and to the best of its knowledge, title to its property is in good standing.

Okeover Property, British Columbia

On March 8, 2006 the Company acquired Goldrush Resources Ltd.'s ("Goldrush") option with Eastfield Resources Ltd. ("Eastfield") whereby Goldrush had the right to earn an interest in mineral exploration claims located north of Powell River in British Columbia (the "Okeover Property") from Eastfield.

4. MINERAL PROPERTY (cont'd...)

Subject to an underlying agreement, the Company paid $5,000 and issued 100,000 shares with a fair value of $12,000 to Goldrush to acquire the option during the year ended September 30, 2006. Pursuant to the underlying agreement, the Company paid the final $10,000 due to Goldrush during the year ended September 30, 2007. The Company also paid $27,000 to Eastfield for property payments. During the year ended September 30, 2009, the Company paid an additional $36,750 to Eastfield for property payments.

The Company can earn a 60% interest, subject to a 2.5% net smelter royalty, in the Okeover Property from Eastfield in exchange for cash and common shares as follows:

- $5,000 cash to be paid upon the acquisition of the option (paid); and
- $100,000 in exploration expenditures by September 30, 2006 (completed).

The Company also has the following optional commitments:

- $10,000 in cash or issuance of common shares by March 8, 2007 (issued common shares),
- $20,000 in cash or issuance of common shares by March 8, 2008 (paid),
- $25,000 in cash or issuance of common shares by March 8, 2009, (paid)
- $50,000 in cash or issuance of common shares by March 8, 2010; and
- Have completed $1,000,000 in cumulative exploration expenditures by March 8, 2010 (completed).

At September 30, 2009, the Ministry of Energy, Mines and Petroleum Resources of British Columbia holds a $6,500 (2008 - $6,500) reclamation bond from the Company to guarantee reclamation of the environment on the Okeover Property.

Lynn Lake Project, Manitoba

On October 20, 2009 the Company entered into an option agreement with Victory Nickel Inc. ("Victory") to acquire a 100% interest in the Lynn Lake Nickel-Copper Property (the "Lynn Lake Project") located in Manitoba, Canada. Prophecy has the right to earn and acquire a one hundred percent (100%) interest in the Properties by paying to Victory an aggregate of $4,000,000, by issuing to Victory 10% of Prophecy's outstanding common shares, calculated on an issued and outstanding basis after giving effect to such share issuance, and incurring an aggregate of $3,000,000 in Exploration Expenditures during the Option Period, as follows:

(a) (i) by paying $300,000 in cash to Victory by November 9, 2009 (paid);

(ii) by paying an additional $300,000 in cash to Victory by January 9, 2010 (paid);

(iii) by paying an additional $400,000 in cash to Victory by April 20, 2010;

(iv) by paying an additional $1,000,000 in cash to Victory by March 1, 2011;

(v) by paying an additional $1,000,000 in cash to Victory by March 1, 2012; and

(vi) by paying an additional $1,000,000 in cash to Victory by March 1, 2013.

(b) by issuing to Victory 10% of Prophecy's outstanding common shares after Prophecy completes a $1,500,000 equity financing which shall occur sixty (60) days from the date of this agreement calculated on an issued and outstanding basis after giving effect to such share issuance (for which 2,419,548 shares were issued to Victory on closing on December 31, 2009); and

(c) (i) by incurring Exploration Expenditures of $500,000 on or before November 1, 2010;

(ii) by incurring total Exploration Expenditures of $1,500,000 on or before November 1, 2011; and

(iii) by incurring total Exploration Expenditures of $3,000,000 on or before November 1, 2012.

5. DEFERRED EXPLORATION COSTS

The following exploration costs were incurred on the Okeover Property to December 31, 2009:

Balance as at September 30, 2007	$	498,315
Assay and drilling		323,793
Consulting		95,577
Field expenses		131,697
Road building		12,213
Property maintenance		2,957
		566,237
Government grant		(45,965)
		520,272
Balance as at September 30, 2008		1,018,587
Field expenses		1,282
Balance as at September 30, 2009 and December 31, 2009	$	1,019,869

During the three months ended December 31, 2009 the Company spent $1,666 on consulting at the Lynn Lake project.

6. RELATED PARTY TRANSACTIONS

The Company entered into the following transactions with related parties during the three months ended December 31, 2009:

a) Paid office rent of $4,500 (2008 - $4,500) to a company controlled by a director and officer of the Company;

b) Paid management fees of $1,000 (2008 – $3,000) to a director and officer of the Company; and

c) Paid management fees of $40,000 (2008 – Nil) to a company controlled by a Director and Officer.

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

At December 31, 2009 $40,000 (2008 - Nil) was owing to related parties. Amounts due to related parties are non-interest bearing, unsecured and have no fixed terms of repayment. The fair value of amounts due to related parties is not determinable as they have no specified repayment terms.

7. SHARE CAPITAL

	Number of Shares		Amount		Contributed Surplus		Total
Authorized							
Unlimited common shares without par value							
Issued							
Balance as at December 31, 2008	11,100,000		1,388,802		198,905		1,587,707
Stock-based compensation	-		-		2,626		2,626
Balance as at September 30, 2009	11,100,000	$	1,388,802	$	201,531	$	1,590,333
Private Placement at $0.05	7,000,000		350,000		-		350,000
Private Placement at $0.30	2,731,500		819,450		-		819,450
Private Placement (FT) at $0.35	3,129,282		1,095,249		-		1,095,249
Finder's warrants	-		(56,789)		56,789		-
Share issuance costs			(121,164		-		(121,164)
Property acquisition	2,419,548		725,864		-		725,864
Balance as at December 31, 2009	26,380,330	$	4,201,412	$	389,768	$	4,591,180

As at December 31, 2009, there are 457,500 (2008 – 1,372,500) common shares included in share capital being held in escrow subject to a three year escrow agreement pursuant to TSX-V policies.

2010

On December 31, 2009 the Company completed a non-brokered private placement of 7,000,000 units at a price of $0.05 per unit for gross proceeds of $350,000. Each unit consists of one common share of the Company and one half share purchase warrant, with each full warrant entitling the holder to purchase an additional share at an exercise price of $0.10 per share for a period of two years from the date of issue.

On December 31, 2009 the Company completed a non-brokered private placement of 2,731,500 units at a price of $0.30 per unit for gross proceeds of $819,450. Each unit consists of one common share of the Company and one half share purchase warrant, with each full warrant entitling the holder to purchase an additional share at an exercise price of $0.40 per share for a period of two years from the date of issue. In the event that the closing price of Prophecy's common shares on the TSX Venture Exchange is at least $0.60 for twenty consecutive trading days at any time following four months from the date of closing, the Company may reduce the remaining exercise period of the Warrants to not less than 30 days from the date of providing notice of such reduced exercise period. A finders fee of $37,560 was paid with respect to a portion of this placement

On December 31, 2009 the Company completed a non-brokered private placement of 3,129,282 flow-through units at a price of $0.35 per unit for gross proceeds of $1,095,249. Each unit consisted of one common share of the Company and one half share purchase warrant, with each full warrant exercisable into one additional non flow-through common share of the Company for a period of eighteen months from closing at an exercise price of $0.50 per share. In the event that the closing price of Prophecy's common shares on the TSX Venture Exchange is at least $0.70 for twenty consecutive trading days at any time following four months from the date of closing, the Company may reduce the remaining exercise period of the Warrants to not less than 30 days from the date of providing notice of such reduced exercise period. Finder's fees of $82,300 were paid on a portion of this placement along with the issuance of 217,142 finder's warrants, exercisable at $0.50 per share for a two year period, subject to the acceleration of exercise clause described above. The granting of these 217,142 finder's warrants resulted in stock-based compensation expense, calculated using the Black-Scholes option pricing model, of $56,789 which has been charged to share issuance costs. The Company has included the fair value of the warrants in share capital.

7. SHARE CAPITAL (cont'd…)

2010 (cont'd)

On December 31, 2009 the Company issued 2,419,548 common shares at a deemed value of $725,864 pursuant to the Lynn Lake Property agreement.

2009

There were no share capital transactions during the year ended September 30, 2009.

Flow-through shares

In accordance with accounting recommendations relating to the issuance of flow-through shares (Note 2), the Company reduced from flow-through share proceeds assigned to share capital and recognized as a future tax liability, the estimated tax effect of the timing difference resulting from renouncing exploration expenditures using currently enacted tax rates and laws.

Concurrently the Company recognized a future income tax recovery from the utilization of available tax losses of prior periods to offset the future tax liability recognized. The Company has not previously recognized tax benefits relating to losses of prior periods as the criteria for recognition had not been met.

8. STOCK OPTIONS AND WARRANTS

Stock options

The Company follows the policies of the TSX-V under which it would be authorized to grant options to executive officers and directors, employees and consultants enabling them to acquire up to 10% of the issued and outstanding common stock of the Company. Under the policies, the exercise price of each option equals the market price or a discounted price of the Company's stock as calculated on the date of grant. The options can be granted for a maximum term of five years.

The Company expenses the fair value of all stock-based compensation awards as determined using the Black-Scholes option pricing model. During the three months ended December 31, 2009 the Company granted 1,500,000 incentive stock options, exercisable at $0.25 per share for a five year period, to directors and consultants. Of these options, 200,000 vested immediately and had a fair value estimated at $47,136 that was charged to stock-based compensation during the period. The remaining 1,300,000 stock options had a vesting provision which allocated the amount of compensation to be recorded over a twelve month service period. The fair value of these options was estimated at $306,387 and vested over a one year period, resulting in a charge to stock-based compensation expense of $76,597(2008 - $Nil) during the period.

A further 200,000 options, exercisable at $0.38 per share for a five year period, were granted to a consultant during the three months ended December 31, 2009. The fair value of these stock options was estimated at $46,289 and the Company recognized $7,715 (2008 - $Nil) in compensation expense related to the options granted.

The weighted average fair value of the stock options granted during the three months ended December 31, 2009 was $0.24 (2008 - $0.08).

There were no stock options granted during the three months ended December 31, 2008.

The following assumptions were used for the Black-Scholes valuation of stock options granted during the three months ended December 31:

	2009	2008
Risk-free interest rate	2.79%-2.34%	-
Expected life	5 years	-
Annualized volatility	165%-167%	-
Dividend yield	0%	-

8. STOCK OPTIONS AND WARRANTS (cont'd…)

Stock options (cont'd...)

The following options were outstanding at December 31, 2009:

Number of Shares	Exercise Price	Expiry Date
450,000	$0.25	February 14, 2012
1,500,000	$0.25	October 29, 2014
200,000	$0.38	November 30, 2014

Stock option transactions are summarized as follows:

	Number of Options Outstanding	Number of Options Exercisable	Weighted Average Exercise Price
Balance, September 30, 2008	650,000	616,667	$ 0.25
Options expired	(200,000)	(166,667)	0.25
Balance, September 30, 2009	450,000	450,000	0.25
Options granted	1,700,000	387,500	0.27
Balance, December 30, 2009	2,150,000	650,000	0.26

The weighted average life remaining of the stock options outstanding and exercisable at December 31, 2009 is 3.39 years.

Warrants

There were 8,028,600 warrants outstanding at December 31, 2009.

The following assumptions were used for the Black-Scholes valuation of agent's warrants granted during the three month period ended December 31, 2009 (Note 7):

	2009
Risk-free interest rate	1.38%
Expected life	2 years
Annualized volatility	167%
Dividend yield	-

Warrant transactions and the number of warrants are summarized as follows:

	Number of Warrants	Weighted Average Exercise Price	Weighted Average Life Remaining (in years)
Balance, December 31, 2008	1,583,000	0.42	0.59
Expired	(1,583,000)	0.42	-
Balance, September 30, 2009	-	$ -	-
Issued	8,028,600	-	2.00
Balance, December 31, 2009	8,028,600	$ 0.29	2.00

9. SUPPLEMENTAL DISCLOSURE WITH RESPECT TO CASH FLOWS

		2009		2008
Cash paid during the year for interest	$	-	$	-
Cash paid during the year for income taxes	$	-	$	-

The significant non-cash transactions during the three months ended December 31, 2008 included:

a) Recording finder's warrants as share issuance costs at a fair value of $56,789 (Note 7).

b) Issuing 2,419,548 at a deemed value of $725,864 for acquisition of the Lynn Lake property.

10. INCOME TAXES

During the year ended September 30, 2008, the Company issued 1,450,000 flow-through units at a price of $0.35 per share for proceeds of $507,500 pursuant to a private placement (Note 9). The flow-through subscription agreements required the Company to renounce certain tax deductions for Canadian exploration expenditures incurred on the Company's mineral property to the flow-through participants. The Company filed the renunciation documentation for $507,500 of expenditures to the subscribers during 2008 which was effective December 31, 2007. Accordingly, $190,450, being the taxable benefit renounced, has been charged as a reduction to share capital (Note 9). Concurrent with the renunciation, the Company realized a future tax benefit. The realized tax benefit was recorded as a future income tax recovery during the year ended September 30, 2008, in accordance with CICA EIC-146.

As at September 30, 2008, the Company has satisfied its flow-through commitments and has fulfilled its commitment to expend the funds on qualifying exploration in accordance with the provisions of the Canadian Income Tax Act.

During the year ended September 30, 2008, the Company applied for a mining tax refund from the Government of British Columbia of $45,965 for exploration work incurred on the Okeover property. This refund was received by the Company during the year ended September 30, 2009.

11. 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.

The property in which the Company currently has an interest is in the exploration 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.

The Company is not subject to internally imposed capital requirements and there has been no change to the Company's approach to managing capital.

12. FINANCIAL INSTRUMENTS

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

Credit Risk
Credit risk is the risk that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss. The Company's primary exposure to credit risk is on its bank accounts and short-term investments, whose balance at December 31, 2009 were $1,839,827 and $Nil respectively. Bank accounts are held with a major bank in Canada. As all of the Company's cash is held by a Canadian bank and all the short-term investments are also held by the same Canadian bank, there is a concentration of credit risk with one bank in Canada. This risk is managed by using a major bank that is a high credit quality financial institution as determined by rating agencies. The Company's secondary exposure to credit risk is on its receivables and reclamation bond. This risk is minimal as receivables consist primarily of refundable government sales taxes and the reclamation bond is held with government authorities.

Currency Risk
The Company operates in Canada and is therefore not exposed to foreign exchange risk arising from transactions denominated in a foreign currency.

Interest Rate Risk
Interest rate risk is the risk that an investment's value will change due to a change in the level of interest rates. The Company's exposure to interest rate risk relates to its ability to maintain the current rate of interest on its short-term investment.

Liquidity and Funding Risks
Liquidity risk arises through the excess of financial obligations over available financial assets due at any point in time. The Company's objective in managing liquidity risk is to maintain sufficient readily available reserves in order to meet its liquidity requirements at any point in time. Funding risk is the risk that market conditions will impact the Company's ability to raise capital through equity markets under acceptable terms and conditions. Under current market conditions, both liquidity and funding risks are assessed as high.

Industry Risk
The Company is engaged primarily in the mineral exploration field and manages related industry risk issues directly. The Company is potentially at risk for environmental reclamation and fluctuations in commodity based market prices associated with resource property interests. Management is of the opinion that the Company addresses environmental risk and compliance in accordance with industry standards and specific project environmental requirements.

13. SUBSEQUENT EVENTS

Subsequent to December 31, 2009, the Company entered into the following transactions:

a) The Company entered into an agreement with VMS Ventures Inc. (TSX-V: VMS) whereby Prophecy has been granted the option to earn a 100% interest in the Lynn Gabbros property in Manitoba near the Company's Lynn Lake Nickel-Copper project. In order to acquire a 100% interest in the Lynn Gabbros property, subject to a 3% NSR, Prophecy issued 750,000 of its common shares to VMS Ventures and agree to reimburse VMS Ventures up to $100,000 to satisfy certain work obligations to be performed by VMS Ventures prior to the transfer of title by June 1, 2010. A finder's fee of $24,000 was paid with respect to this acquisition.

b) Prophecy closed the second and final tranche of a private placement announced December 9, 2009 of 2,761,936 units to raise a total of $828,580. Each unit consists of one share and one half-warrant, with each full warrant exercisable to purchase an additional share of the Company at $0.40 until January 25, 2012. Finder's fees totaling $28,120 cash were paid in respect to a portion of this placement.

13. SUBSEQUENT EVENTS (cont'd…)

c) Prophecy Resource Corp. received TSX Venture Exchange approval for an option agreement with Randsburg International Gold Corp. (TSX.V: RGZ), whereby Prophecy can earn an 80-per-cent interest in the Titan vanadium-titanium-iron project located in Ontario, Canada. Under the agreement, Prophecy shall have the right to acquire an 80-per-cent interest in the Titan project by paying Randsburg an aggregate of $500,000 and incurring $200,000 in exploration expenditures by Dec. 31, 2010.

d) On January 20, 2010 entered into a letter agreement Red Hill Energy Inc. (TSX.V: RH) (the "LOA") in respect of a friendly transaction to combine the companies through an all share transaction (the "Proposed Transaction"). The combined company is hereinafter referred to as "new Prophecy". Per the LOA, Red Hill shareholders will receive 0.92 of a new Prophecy common share for each Red Hill common share held which represents a 26.8% premium to the shareholders of Red Hill as at the close of market on January 20, 2010. All outstanding Red Hill options and warrants will be exchanged for options and warrants of new Prophecy on similar terms. The parties have agreed to enter into a definitive agreement by February 28, 2010 and complete the Proposed Transaction by May 15, 2010. Completion of the Proposed Transaction is conditional upon both the Red Hill and Prophecy Shareholders having approved the Proposed Transaction, completion of legal and financial due diligence by each of the parties, receipt of all necessary regulatory approvals, including the approval of the TSX Venture Exchange (the "Exchange") and certain other customary conditions.

e) The Company agreed to grant 750,000 stock options to directors and consultants at an exercise price of $0.40 for a period of 5 years.

PROPHECY RESOURCE CORP.

MANAGEMENT'S DISCUSSION AND ANALYSIS
OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS
For the three months ended December 31, 2009

The following discussion and analysis should be read in conjunction with the Interim Financial Statements for Prophecy Resource Corp (the "Company") and related notes for the three months ended December 31, 2009. All dollar amounts included therein and in the following management discussion and analysis ("MDA") are stated in Canadian funds. This discussion is based on information available as at March 1, 2010.

This discussion contains forward-looking statements that involve risks and uncertainties. Such information, although considered reasonable by the Company's management at the time of preparation, may prove to be inaccurate and actual results may differ materially from those anticipated in the statements made.

The Company was incorporated under the *Business Corporations Act* (British Columbia) on February 9, 2006 under the name "Prophecy Resource Corp." Prophecy is focused on the acquisition of base and precious metal exploration properties primarily in Canada. The Company has no subsidiaries.

Overview

On March 8, 2006 the Company entered into an option with Eastfield Resources Ltd. (TSX.V: ETF) whereby Prophecy has the right to earn a 60% interest in the Okeover Copper-Molybdenum property from Eastfield by spending $1,000,000 on exploration of the Okeover Property (completed) and by making cash payments totalling $110,000, of which all but $50,000 has been paid. Upon the Company earning its 60% interest in the Okeover property, the Company and Eastfield intend to form a joint venture for the further exploration and development of the Okeover property, with Prophecy becoming the operator. Notwithstanding the final option payment of $50,000 due in March 2010, the companies have agreed, by nature of the $1,000,000 exploration commitment having been completed, to begin sharing ongoing exploration costs at Okeover on a pro rata basis.

In October, 2009 the Company entered into an Option Agreement with Victory Nickel Inc. (TSX.T: NI) whereby Prophecy has the right to acquire a 100% interest in the Lynn Lake Nickel-Copper Project located in Manitoba, Canada. This transaction was accepted for filing by the TSX Venture Exchange and closed on December 31, 2009.

The Okeover Copper-Molybdenum Property

The following represents information summarized from a technical report (the "Okeover Property Report") dated October 5, 2006 entitled "Technical Report on the OK Copper Property", prepared by N.C. Carter, Ph.D. P. Eng. pursuant to the provisions of National Instrument 43-101 ("NI 43-101").

N.C. Carter is a "qualified person" within the meaning of NI 43-101. N.C. Carter is independent of the Company applying all of the tests in section 1.5 of NI 43-101 and has not had prior involvement with the Okeover Property that is the subject of the Okeover Property Report.

The Okeover Property (copper-molybdenum) consists of eleven contiguous legacy and cell mineral claims located in the Vancouver Mining Division of south western British Columbia, 25 kilometres north of Powell River and 145 kilometres northwest of Vancouver. Collectively, the claims cover an area of approximately 5,882 hectares between latitudes $49^0$59.5' and $50^0$04.6' North and longitudes $124^0$37.0' and $124^0$41.2'

All claims are registered in the name of Eastfield and are subject to a March 4, 2003 option agreement with Robert Edward Mickle of Likely, B.C. whereby Eastfield has the right to earn a 100% interest in the property subject to a 2.5% net smelter royalty interest which may be purchased from the vendor for $2 million on commencement of commercial production.

Copper and molybdenum mineralization was discovered in creek bottoms in the central part of the Okeover Property in 1965. Between 1966 and 1977, seven companies carried out a number of geological, geochemical and geophysical surveys, mechanical trenching and more than 14,000 metres of drilling. Companies working on the property included Noranda Exploration Company Ltd., Asarco Exploration Company of Canada Limited, Falconbridge Nickel Mines Ltd., Duval International Corporation, Granite Mountain Mines Ltd., Sierra Empire and Western Mines Ltd.

Drilling completed between 1966 and 1977 consisted of 13,831.5 metres of diamond drilling in 82 holes and 12 vertical percussion holes totalling 732 metres. Average diamond drill hole length was 169 metres and the deepest hole drilled was 363 metres in length. Vertical percussion holes were drilled to 61 metres depths.

2008 Exploration Program

On May 22, 2008 Prophecy initiated a six hole (1,449 metre) diamond drilling program at Okeover. The predominant thrust of this program was to significantly expand the known mineral resource at the North Lake Zone, which is one of eight known areas of significant copper-molybdenum mineralization on the Okeover project. Five of the six holes were completed as step outs to the south and west sides of the existing resource area at North Lake, with drill results being announced July 28, 2008.

Highlights of the 2008 drill program include Hole OK-08-03, which intersected 45.5 metres grading 0.33% copper and 0.003% molybdenum, including 12 metres grading 0.41% copper and 0.001% molybdenum. Hole OK-08-03 was drilled 90 metres to the south of the nearest hole in the current North Lake resource area and creates an open southern edge for future expansion of the resource area in this direction.

At Okeover, the objectives of the recent program were achieved and expanded the mineralized area of the North Lake Zone (calculated in 2006 by N.C. Carter, Ph.D., P. Eng to contain 86.8 million tonnes grading 0.31% copper and 0.014% MoS_2) a substantial distance to the south.

A summary of the drill results from the 2008 exploration programs is as follows:

Hole	Intercept (m)	From (m)	To (m)	Cu %	Mo %
Ok-08-01 Including	57.0 42.0	113.0 122.0	170.0 164.0	0.30 0.33	0.003 0.003
Ok-08-02 And	26.3 16.5	72.5 107.3	98.8 123.8	0.26 0.33	0.002 0.003
Ok-08-03 Including Including	198.5 45.5 12.0	39.5 39.5 73.0	238.0 85.0 85.0	0.16 0.33 0.41	0.001 0.003 0.001
Ok-08-04	2.2	98.2	98.0	0.21	0.004
Ok-08-05	46.4	2.1	48.5	0.10	0.001

Hole OK-08-06, drilled three kilometres further to the south, returned only anomalous values, with individual three metres sample intervals returning values to 0.28% Cu and 0.029% Mo.

With this drill program complete, Prophecy has spent over $1,000,000 in exploration at Okeover and satisfied its work commitment to earn a 60% interest from Eastfield Resources Ltd. (TSX.V: ETF).

Prophecy believes that well situated copper porphyry projects with access to the Asian Rim will continue to be valuable and can be expected to be in higher demand once the current western world recession abates.

The Company has begun permitting for a further drill program to be conducted at Okeover during 2010, to be funded on a pro-rata basis by Prophecy and Eastfield in accordance with their respective percentage interests.

Agreement to acquire Lynn Lake Nickel project in Manitoba

On October 21, 2009 the Company entered into an Option Agreement with Victory Nickel Inc. (TSX.T: NI) whereby Prophecy has the right to acquire a 100% interest in the Lynn Lake Nickel-Copper Project located in Manitoba, Canada. This transaction was accepted for filing by the TSX Venture Exchange and closed on December 31, 2009.

The Lynn Lake Project is located in the historic mining town of Lynn Lake in northern Manitoba, about 320 kilometres by road access northwest of the Thompson mining camp. The property is the former Sherritt Gordon Mines Limited mine site known as the Lynn Lake A mine and Farley mine, comprised of 30 mineral leases covering an area of 590 hectares. The property was operated by Sherritt Gordon from 1953 to 1976 for a total of 24 years, with reported production of 22.2 million tons at an average grade of 1.023% nickel and 0.535% copper.

Under the agreement, Prophecy shall have the right to acquire a 100% interest in the Lynn Lake project by paying Victory an aggregate of $4,000,000 over a four year period (of which $600,000 has been paid) and incurring an aggregate of $3,000,000 in Exploration Expenditures over a three year period.

As part of the agreement, Prophecy also agreed to issue to Victory 10% of Prophecy's outstanding shares on closing (for which 2,419,548 shares were issued to Victory on closing on December 31, 2009) and grant Victory the right to participate in future equity financings on a pro rata basis so that Victory may maintain its 10% interest in Prophecy.

In February 2010 Prophecy announced the results of an updated independent mineral resource estimate on the Lynn Lake Nickel-Copper property completed by Wardrop Engineering Inc on January 28, 2010 and prepared in accordance with National Instrument 43-101 ("NI 43-101") Standards of Disclosure for Mineral Projects. The property is estimated to contain a **Measured and Indicated resource of 22.9 million tons at 0.57% nickel and 0.3% copper**, together with an **Inferred resource of 8.1 million tons at 0.51% nickel and 0.28% copper**. The estimate uses a 0.4% Nickel equivalent (NiEQ%) cutoff. The results are summarized in the following Table:

Mineral Resource Estimate for Lynn Lake (at a cut-off of 0.4% NiEQ%)					
Resource Category	Tons	Ni Grade	Cu Grade	Ni Contained	Cu Contained
	(millions)	(%)	(%)	lbs	lbs
Measured & Indicated	22.9	0.57	0.30	263,028,299	136,133,440
Inferred	8.1	0.51	0.28	81,559,227	45,614,959

The current estimate updates previous estimates produced by Wardrop in October 2005 and 2007, using ordinary kriging methodology, and includes mineralisation from the N, O and G zones. It has been calculated from an extensive database of 3,709 drill holes with an aggregate length of 399,088 meters (1,309,345 feet). NiEQ% was calculated using a Nickel price of $7.22/lb and a Copper price of $2/lb. Metal recoveries were assumed to be 100% for both Nickel and Copper, as metal recovery options such as bio-leach are being investigated with results pending.

The current estimate does not include mineralisation from the Disco zone discovery made in 2008 which includes intercepts of 47 meters of 0.7% nickel and 18 meters of 1.5% nickel, located 1.5km away from the outlined resource. Wardrop determined that there is not enough drill information to generate an inferred resource for the Disco Zone at this time.

The mineral resource estimate model was completed by Todd McCracken, P. Geo, Principal Geologist with Wardrop Engineering Inc. and a Qualified Person as defined by NI 43-101.

<u>Appointment of Directors and Advisors</u>

In October, 2009, concurrent with the announcement of the Lynn Lake option agreement, Mr. John Lee, CFA, was appointed as a Director of the Company. Mr. Lee was subsequently appointed Chairman and Chief Executive Officer of Company on November 30, 2009 following the resignation of James Brown as President.

On November 30, 2009 Prophecy also announced the appointment of Mr. Greg Hall and Dr. George Gale as Special Advisors of the company.

Mr. Greg Hall is a financial market professional with over 25 years of experience. Currently a director of Silvercorp Metals Inc (NYSE: SVM, TSX: SVM), he was part of the team that helped build Silvercorp into China's largest primary silver producer and the lowest cost silver producer among its industry peers.

Mr. Hall has previously held senior positions at Haywood Securities Inc., Canaccord Capital Corporation, and Leede Financial Markets and will be guiding Prophecy's corporate strategy and financing activities.

In January 2010, Mr. Hall was appointed as a Director of the Company to fill the vacancy created by the resignation of James Brown as a Director.

Dr. George Gale has been a mineral deposit geologist for more than 40 years. Currently VP Exploration and a director of VMS Ventures Inc. (TSX-V: VMS), he led the exploration activities that resulted in their discovery of the high-grade Manitoba Reed Lake VMS deposit in 2007.

Dr. Gale was the head of the Mineral Deposits Section of the Manitoba Geological Survey from 1977 to 1999. He will advise Prophecy's exploration activities based on his extensive geological expertise in Manitoba.

John Lee states "Mr. Hall and Dr. Gale will have an immediate impact in shaping the future of Prophecy. The recent $192 million acquisition of Canadian Royalties Inc. by China's Jilin Jien Nickel Industry Co. Ltd has set a positive tone for Prophecy, which is in the process of acquiring the former Lynn Lake nickel mine in Manitoba, one of the significant undeveloped NI 43-101 compliant nickel resources in Canada. We are thrilled with the addition of those two veterans to our team and we will work tirelessly to duplicate their previous success within Prophecy."

On January 5, 2010 Prophecy announced the appointment of Harald Batista as a Special Advisor to the Chairman.

Mr. Batista is an accomplished entrepreneur with over 2 decades of sales and marketing experience. He holds an MBA degree from Santa Clara University in California and is a member of the prominent Batista family in Brazil that includes Eliezer Batista, the founder of Vale do Rio Doce Company (now Vale Inco) and Eike Batista, the founder of EBX Group. EBX Group focuses on investment opportunities in infrastructure and natural resources, sectors in which Brazil presents important competitive differentials. These investments are focused on MMX (mining), MPX (energy), LLX (logistics), OGX (oil and gas) and OSX (oil services). MMX, OGX, MPX and LLX are listed on Brazil's Novo Mercado - at the São Paulo Stock Exchange (BOVESPA). The combined market capitalization of EBX Group companies exceeds US $150 billion.

John Lee, Chairman of Prophecy states: "Harald brings a wealth of marketing and international networking experience to Prophecy. As the company continues to execute the strategy of acquiring advanced global mineral assets, we look to Harald to help us develop international marketing exposure and potential partnerships with the world's largest natural resource firms."

Private Placements of $2,264,699 completed

On December 31, 2009 Prophecy closed private placements announced on October 21, 2009, December 9, 2009, December 14, 2009 and December 23, 2009 totaling 12,860,782 shares and 6,430,391 warrants to raise a total of $2,264,699. Of this total, $1,095,249 was by way of flow-through subscriptions and $1,169,450 by way of non flow-through subscriptions. Proceeds from the private placements were applied to acquisition costs and exploration of the Lynn Lake Project and for working capital.

All of the shares, warrants and any shares issued upon exercise of the warrants comprising the units issued pursuant to the private placements are subject to a hold period and may not be traded until May 1, 2010.

Private Placement of $828,580 completed

In January 2010 Prophecy closed the second and final tranche of a private placement announced December 9, 2009 of 2,761,936 units to raise a total of $828,580. Each unit consists of one share and one half-warrant, with each full warrant exercisable to purchase an additional share of the Company at $0.40 until January 25, 2012. Finder's fees totaling $28,120 were paid in respect to a portion of this placement.

All of the shares, warrants and any shares issued upon exercise of the warrants issued pursuant to the private placement are subject to a hold period and may not be traded until May 26, 2010.

Acquisition of Lynn Lake Lake Gabbros; VMS Ventures Inc. Private Placement

On January 12, 2010 Prophecy announced it had entered into an agreement with VMS Ventures Inc. (TSX.V:VMS) to consolidate the Lynn Lake Nickel District. Under the agreement, in order to acquire a 100% interest in the Lynn Gabbros property near Prophecy's Lynn Lake nickel-copper project (subject to a 3% NSR), Prophecy will issue 750,000 of its common shares to VMS Ventures and reimburse VMS Ventures up to $100,000 to satisfy certain work obligations to be performed by VMS Ventures prior to the transfer of title by June 1, 2010. Separately, VMS Ventures Inc also agreed to make a strategic investment in Prophecy totalling $300,000 by subscribing to one million units under the same terms as our private placement announced December 9, 2009; this amount was included in the private placement totalling $828,580 that closed January 25, 2010, as more fully described above. On a partially diluted basis, VMS Ventures would own approximately 8% of Prophecy.

On January 25, 2010 Prophecy received TSX Venture Exchange approval on January 25, 2010 and issued 750,000 shares in its capital stock to VMS to close the transaction. Prophecy paid a finder's fee of $24,000 in connection with this acquisition.

Rick Mark, Chairman and CEO of VMS Ventures states: "Prophecy's commitment to exploring and developing the Lynn Lake Mine and surrounding area has impressed our Board. We believe the opportunity to own a significant percentage of the complete Lynn Lake play through our option agreement and investment will produce benefits to VMS shareholders in the near and longer term. We have worked with John Lee in the past and feel Prophecy has the best chance to make the Lynn Lake mine and the surrounding properties a business success."

John Lee, Chairman of Prophecy states: "Lynn Lake fits perfectly with our business strategy of acquiring advanced mineral assets to provide Prophecy investors financial leverage on rising metal prices. Prophecy is very pleased to acquire and consolidate this premier Lynn Lake Nickel Camp, where we intend to conduct an extensive exploration program in 2010."

Acquisition of 80% Interest in Titan Vanadium-Titanium-Iron Project In Ontario

In January, 2010 Prophecy entered into an option agreement with Randsburg International Gold Corp. (TSX-V: RGZ) whereby Prophecy can earn an 80-per-cent interest in the Titan vanadium-titanium-iron project located in Ontario, Canada.

The Titan project is located in Eastern Ontario, approximately 120 kilometres east-northeast of Sudbury, straddling the boundary between Angus and Flett townships, with access to excellent infrastructure. The Titan property consists of 1,052 contiguous hectares (2,600 acres) comprising 17 patented claims and three mining claims.

Magnetite, ilmenite, titanium dioxide and vanadium mineralization at Titan occurs in a southeast-plunging body in gabbro to leucotroctolite in the northeastern corner of the Fall Lake complex. The Titan deposit is located at the northern end of an aeromagnetic anomaly that is approximately 1,200 by 800 metres in area.

A total of 4,898 assay intervals is recorded from 38 core holes drilled by Randsburg on the property. Drilling highlights reported by Randsburg included **142 metres of 0.27 per cent vanadium** (0.48 per cent vanadium pentoxide) from hole RA-5-21 and **174 metres of 0.26 per cent vanadium** (0.46 per cent vanadium pentoxide) from hole RA-5-10. The mineralization started from surface to an open vertical depth of 500 metres. The complete horizontal and vertical extent of the deposit is still to be determined. Information on the geology at Titan and assay results reported by Randsburg are available on the Prophecy website.

A technical report dated Feb. 12, 2007, prepared by Mines Development Associates for Randsburg, calculated a National Instrument 43-101-compliant inferred resource for the Titan project. This technical report can be accessed under Randsburg's filings at www.sedar.com.

Under the agreement, Prophecy shall have the right to acquire an 80-per-cent interest in the Titan project by paying Randsburg an aggregate of $500,000 and incurring $200,000 in exploration expenditures by Dec. 31, 2010. This transaction was accepted for filing by the TSX Venture Exchange and completed on January 22, 2010.

John Lee, chairman of Prophecy, states: "Vanadium and lithium car batteries are the green wave of the future. We are fortunate to acquire one of the few vanadium deposits available anywhere in the world. Titan fits perfectly with our business strategy of acquiring advanced mineral assets to provide Prophecy investors financial leverage on rising metal prices. We intend to explore and expand the Titan vanadium resource in 2010."

Proposed Business Combination with Red Hill Energy Inc.

Prophecy and Red Hill Energy Ltd. (TSX.V: RH) announced on January 21, 2010 that their respective Boards of Directors had unanimously approved a letter agreement dated January 20, 2009 (“LOA”) in respect of a friendly transaction to combine the companies through an all share transaction.

Red Hill controls 100% interests in two key Mongolian coal districts, Ulaan Ovoo and Chandgana. Combined, Red Hill has 504.5 million tons of Measured, 524 million tons of Indicated and 475.9 million tons of inferred thermal coal in Mongolia.

The Ulaan Ovoo Coal Project

The Ulaan Ovoo coal project is 100% owned by Red Hill. The project is located within 10 km of the Russian border, northern Mongolia and is 120km (75 miles) east of the Central Mongolian Railroad which links the project to the vast coal markets of Russia and Asia. The project contains 174.5 million tons Measured, 34.3 million tons Indicated and 35.9 million tons of Inferred thermal coal. The coal is of excellent low ash and sulfur quality at 5,204 KCAL/KG LB- which is highly desired regionally. The average seam thickness of the resource is 53.9 metres with a stripping ratio of 2.0:1 on the first 140 million tons. The Mongolian government has granted the project a fully transferable 30 year mining license that can be extended by an additional 40 years. The project has met Mongolian environmental approvals as per the Mongolian Ministry of Nature and the Environment which approved a Detailed Environmental Impact Assessment (DEIA) and Environmental Protection Plan (EPP) specifically for Ulaan Ovoo, an important pre-condition prior to production. The central Russian transmission grid reaches within 25 kilometres to the north of the project. Several economic studies including a Scoping Study conducted by Behre Dolbear (USA) Ltd. of Denver, CO USA and a recently completed Pre-Feasibility Study conducted by Minarco-MineConsult of Sydney, Australia demonstrate the economic potentials of the project. These reports are available at www.sedar.com

The Chandgana Tal and Chandgana Khavtai Coal Projects

The Chandgana Tal and Chandgana Khavtai coal projects are both 100% owned by Red Hill. The projects share the same Nyalga Basin coal seam and are both contiguous to Vale's (formerly CVRD) largest Mongolian coal project. The Chandgana projects contain a combined total of 819.7 million tons Measured and Indicated and 440 million tons of Inferred thermal coal. (Specifically: Chandgana Tal, 141. 3 million tons Measured, and Chandgana Khavtgai, 188.7 Measured, 489.7 Indicated and 440 Inferred) Both projects have extremely low stripping ratios, 0.53:1 in the case of Chandgana Tal and 2.1:1 in the case of Chandgana Khavtgai with respective average coal seam thicknesses of 40 and 45.4 metres. The Nyalga Coal Basin is within 160 km's (100 miles) of the Central Mongolian Railroad, offering the project a direct link to China, Russia as well as other Asian destinations. Both the Chandgana's coal qualities are of desirable low ash, low sulfur content with KCAL/KG LB averaging up to 4,358. Additional information is available at www.redhillenergy.com and at www.sedar.com.

Financial Terms of the Transaction

Per the LOA, Red Hill shareholders will receive 0.92 of a new Prophecy common share for each Red Hill common share held which represents a 26.8% premium to the shareholders of Red Hill as at the close of market on January 20, 2010. All outstanding Red Hill options and warrants will be exchanged for options and warrants of new Prophecy on similar terms.

Highlights of the Proposed Transaction

- The combined company will have control over NI-43-101 compliant Measured and Indicated mineral resources of 232 million pounds of nickel, 1 billion tonnes of coal and 116 million pounds of copper as well as inferred resources of 500 million tones of coal and 593 million pounds of copper. New Prophecy will also hold properties with significant exposure to vanadium and titanium. The company offers diversified financial leverage to rising commodity prices.
- Positive synergy in the combined management with expertise in geology, engineering, marketing, and M&A.
- Broader appeal to international and institutional investors with multiple advanced assets, greater stock liquidity and the benefits of exposure to a broader range of commodities.
- Enhanced market capitalization and capacity to evaluate and acquire other advanced stage and pre-production stage resource opportunities internationally.

Arnold Armstrong, Chairman and Chief Executive Officer of Red Hill Energy stated: "Prophecy has demonstrated its vision of creating a quality company focused on acquiring advanced mineral assets internationally. We are particularly impressed with Prophecy's speed of conducting business and its ability to bring quality projects and investors together under one name. I am confident that Red Hill shareholders will reap the rewards by owning the majority of the new Prophecy."

John Lee, Chairman and Chief Executive Officer of Prophecy Resource stated: "I joined Prophecy in October with the goal of amassing advanced assets, management talent, and investors world wide. Our Lynn Lake Nickel project and the newly acquired coal assets provide cornerstones from which Prophecy can now build its legacy. Mr. Armstrong is a highly regarded businessman and I look forward to working with him in his position with new Prophecy in taking our venture to the next level".

It is contemplated that the Proposed Transaction will be a business combination of Prophecy and Red Hill by way of a plan of arrangement and will be structured in a way that will result in the financial terms of the Proposed Transaction being met. The parties have agreed to enter into a definitive agreement by March 3, 2010 and complete the Proposed Transaction by May 15, 2010.

As a result of the Proposed Transaction, all existing warrants, options and other rights to acquire common shares of Red Hill will be deemed to represent comparable securities of Prophecy adjusted on the same share exchange ratio basis. The agreed share exchange ratio is based upon an assessment of the recent trading activity and assets of both Red Hill and Prophecy.

Completion of the Proposed Transaction is conditional upon:

1. Both the Red Hill shareholders and Prophecy Shareholders having approved the Proposed Transaction;
2. Completion of legal and financial due diligence by each of the parties;
3. Receipt of all necessary regulatory approvals, including the approval of the TSX Venture Exchange;
4. Certain other customary conditions.

The LOA includes a commitment by both parties to not conduct negotiations or solicit alternative transactions. In certain circumstances, if the Proposed Transaction is terminated by either party, a breakup fee of $500,000 is payable by the terminating party. On or before the date of execution of the Definitive Agreement, the directors and officers of both Red Hill and Prophecy shall have entered into a share lock-up agreement to vote in favour of the Proposed Transaction;

Upon completion of the Proposed Transaction the current Chairman and CEO of Prophecy, Mr. John Lee, will remain the Chairman & CEO of the combined company which will retain the name "Prophecy Resource Corp." The board of directors of new Prophecy will consist of four nominees from Red Hill and three nominees from Prophecy.

Pursuant to the LOA, Red Hill has the right, prior to closing of the Proposed Transaction, to transfer to a newly formed subsidiary ("NewCo") the following: (i) $1,000,000 cash, and (ii) all of Red Hill's non-Mongolian assets, namely, the Red Lithium Property near Clayton Valley, Nevada and Thor Rare Earth Property in Nevada, and distribute securities of NewCo to shareholders of Red Hill as of a to-be-determined record date by way of spinoff or similar mechanism. Red Hill is reviewing the merits of this proposed spinoff and will update its shareholders in a later news release.

If the Proposed Transaction is completed, and based upon the current issued capital of each company including the private placement to be conducted by Red Hill as described below, new Prophecy will have approximately 85,400,000 common shares issued and outstanding, of which Red Hill shareholders will own approximately 65% and current Prophecy shareholders will own approximately 35%.

Options Granted

On October 29, 2009 the Company agreed to grant incentive stock options to directors and consultants on 1,500,000 common shares at an exercise price of $0.25 per share for a period of five years. A further 200,000 options exercisable at $0.38 for a five year period were granted on November 30, 2009. All of these options are subject to vesting over a two year period.

On January 25, 2010 the Company agreed to grant incentive stock options to consultants on 750,000 common shares at an exercise price of $0.40 per share for a period of five years. All of these options are subject to vesting over a two year period, and are subject to shareholder approval.

Going concern issue

The Company is in the exploration stage and has no revenue or income from operations. The Company has limited capital resources and has to rely upon the sale of equity and/or debt securities for cash required for exploration and development purposes, for acquisitions and to fund the administration of the Company. Since the Company does not expect to generate any revenues from operations in the near future, it must continue to rely upon the sales of its equity or debt securities or joint venture agreements to raise capital. It follows that there can be no assurance that financing, whether debt or equity, will be available to the Company in the amount required by the Company at any particular time or for any period and that such financing can be obtained on terms satisfactory to the Company.

The Company's financial statements have been prepared on a going concern basis which assumes that the Company will be able to realize its assets and discharge its liabilities in the normal course of business for the foreseeable future. The continuing operations of the Company are dependent upon its ability to obtain the necessary financing to meet its ongoing commitments and further its mineral exploration programs.

The Company may encounter difficulty sourcing future financing in light of the recent economic downturn. The current financial equity market conditions and the inhospitable funding environment make it difficult to raise capital through the private placements of shares. The junior resource industry has been severely affected by the world economic situation as it is considered speculative and high-risk in nature, making it even more difficult to fund. While the Company is using its best efforts to achieve its business plans by examining various financing alternatives, there is no assurance that the Company will be successful with any financing ventures.

Management's Discussion and Analysis

The following discussion and analysis is based on the Company's results of operations and financial position and should be read in conjunction with the interim financial statements for the period ended December 31, 2009.

The Company holds an option to earn a 60% interest in eleven contiguous mineral claims in British Columbia totaling approximately 3,950 hectares called the Okeover Property. During the period under review, the Company entered into an agreement to acquire a 100% interest in the Lynn Lake Nickel-Copper Project in Manitoba. The Company is a resource development company focused on the acquisition and exploration of mineral properties and therefore has no regular cash flow from operations. The level of operations has been determined by the availability of capital resources. To date, private placements have provided the main source of funding.

Results of Operations

Operating expenses for the three months ended December 31, 2009 totaled $232,790 as compared to $28,119 during the same period a year prior. The significant expenditures were as follows:

During the three months ended December 31, 2009 the Company incurred $5,336 for office, rent and expenses, which was increased from the $4,702 incurred during the same period a year prior.

During the three months ended December 31, 2009 the Company incurred stock-based compensation expense, a non-cash expense, of $104,149 for options granted to directors, officers and consultants that vested during the period. This compares to stock-based compensation expense of $3,940 incurred during the three months ended December 31, 2008 for options granted to investor relations consultants in 2007 that vested during the period.

The Company incurred consulting fees of $9,000 during the three months ended December 31, 2010 for web site development and preparation of promotional materials. There was no comparable expense during the same period a year prior.

The Company spent $8,789 for transfer agent and filing fees during the three months ended December 31, 2009. This was increased from the $3,187 incurred for transfer agent and filing fees during the same period a year prior when the Company was less active and did not raise any money through private placements or undertake any acquisitions.

During the three months ended December 31, 2009 the Company incurred $19,746 for shareholder communications expenses, which included web site maintenance, consulting, news release dissemination and advertising. This compares to $11,790 incurred during the same period a year prior when the Company elected to conserve cash during the difficult market conditions prevalent during the fourth quarter of calendar 2008.

Management fees of $41,000 incurred during the three months ended December 31, 2009 were increased from the $4,500 paid during the comparable period a year due to a change in management staff and their level of compensation during the current period to enable the Company to undertake and complete the acquisitions and financings announced during the period and in January 2010.

During the three months ended December 31, 2009 professional fees were increased to $12,964 from the $nil incurred during the same period a year prior due to an increase in legal and accounting fees during the current period commensurate with the increased level of business activity .

Travel expenses increased to $31,806 during the three months ended December 31, 2009 due to increased travel by management for property review, attendance at trade shows and fund raising efforts. This compares to travel expenditures of $nil during the comparable period a year prior.

During the three months ended December 31, 2009 the Company earned interest income of $380 on short-term investments and cash on hand. This is reduced from the $3,206 earned during the same period a year prior primarily due to a reduction in the Company's cash balances.

As a result of the foregoing, the Company incurred a net loss after income taxes for the three months ended December 31, 2009 of $232,410 as compared to a loss of $24,913 for the comparable period a year prior.

Summary of Quarterly Results

	Q1-10	Q4-09	Q3-09	Q2-09	Q1-09	Q4-08	Q3-08	Q2-08
Revenue	Nil	Nil	Nil	Nil	Nil	Nil	Nil	Nil
Net Income (Loss) ($)	(232,410)	18,993	(11,701)	(48,791)	(24,913)	(33,717)	(31,219)	34,391
Per Share (Loss) ($)	(0.02)	(0.00)	(0.01)	(0.01)	(0.01)	(0.01)	(0.01)	0.01

The Company recorded income for the second quarter of fiscal 2008 of $34,391 primarily due to recording a future income tax recovery of $92,380 during the period as a result of the issuance of 2,200,000 flow-through shares during the prior calendar year. This served to offset the loss for the period of $57,989 that would have been recorded otherwise, with the increase from the $44,781 incurred during the first quarter of 2008 the result of additional professional fees incurred during the second quarter for preparation of the Company's audited financial statements for the prior fiscal year.

As there was no future income tax recovery in the third quarter of fiscal 2008, the Company incurred a loss of $31,219 for the period. When compared to prior fiscal periods, this reduced loss was primarily as a result of reductions in expenditures for professional fees and transfer agent and filing fees, offset by additional expenditures for consultants providing shareholder communications services. The loss for the fourth quarter of fiscal 2008 was relatively unchanged at $33,717.

The loss during the first quarter of fiscal 2009 was reduced to $24,913 from the $33,717 incurred during the fourth quarter of fiscal 2008 primarily due to a reduction in professional fees and expenditures on shareholder relations during the current period.

During the second quarter of fiscal 2009 the loss increased to $48,791 as a result of additional professional fees and Part XII.6 tax paid to the Government of Canada during the period on funds raised by the Company through flow-through share offerings during prior years.

The loss for the third quarter of fiscal 2009 was reduced to $11,701 due to the elimination of expenditures on professional fees and Part XII.6 during the quarter.

The Company recorded income for the fourth quarter of fiscal 2009 of $18,993 primarily due to recording a future income tax recovery of $39,421 during the period, which offset the loss of $20,428 that would have been recorded otherwise, an increase over the third quarter of fiscal 2009 as a result of accounting fees accrued during the period for the completion of the year end audited financial statements for fiscal 2009.

For the first quarter of fiscal 2010, the company recorded a loss of $232,410 primarily due to an increase in stock-based compensation expense of $104,149, a non-cash expense, as well as significant increases in management and professional fees and travel expenses.

Liquidity and Capital Resources

Prophecy is in the development stage and therefore has no regular cash flow. As at December 31, 2009, the Company had working capital of $1,759,612, inclusive of cash and short-term investments on hand of $1,839,827. This compares to working capital of $56,004 at September 30, 2009, inclusive of cash on hand and short term investments of $68,776.

At December 31, 2009 the Company had current assets of $1,856,283, total assets of $4,070,932 and total liabilities of $96,671. The Company has no long-term debt other than a liability for future income taxes of $46,329. There are no known trends in the Company's liquidity or capital resources.

The principal assets of the Company are its mineral exploration properties, amounting to $2,208,149, and cash amounting to $1,839,827, as at December 31, 2009.

The increase in cash during the period ended December 31, 2009 of $1,831,051 was primarily due to cash provided by share issuances.

The decrease in cash during the three months ended December 31, 2008 of $14,925 was primarily due to cash used by operations of $31,550 and cash used for property exploration and acquisition expenditures of $18,375, offset by cash received from short-term investment redemptions of $35,000.

The Company had sufficient funds on hand at December 31, 2009 to fund its operating expenses for the balance of the current fiscal year as well as conduct exploration on its properties. On December 31, 2009 the Company closed private placements totalling 12,860,782 shares and 6,430,391 warrants to raise a total of $2,264,699. Of this total, $1,095,249 was by way of flow-through subscriptions and $1,169,450 by way of non flow-through subscriptions. Subsequent to the period the Company closed the second and final tranche of a private placement announced December 9, 2009 of 2,761,936 units to raise a further $828,580. This will provide the Company with sufficient funding to satisfy it's obligations on the Lynn Lake Nickel project and working capital for at least the next six months, at which time the Company will be required to raise additional capital. Although the company has been successful in the past in obtaining financing through the sale of equity securities, there can be no assurance that the Company will be able to obtain adequate financing in the future or that the terms of such financing will be favorable. Failure to obtain such additional financing could result in the delay or indefinite postponement of further exploration and development of the Companies properties.

Cash flow to date has not satisfied the Company's operational requirements. The development of the Company may in the future depend on the Company's ability to obtain additional financings. In the past, the Company has relied on the sale of equity securities to meet its cash requirements. Future developments, in excess of funds on hand, will depend on the Company's ability to obtain financing through joint venturing of projects, debt financing, equity financing or other means.

There can be no assurances that the Company will be successful in obtaining any such financing or in joint venturing its property.

Off Balance Sheet Arrangements

The Company has no off Balance Sheet arrangements.

Changes in Accounting Policies

Adoption of New Accounting Standards and Accounting Pronouncements

Effective January 1, 2008, the Company adopted the following new accounting standards that were issued by the Canadian Institute of Chartered Accountants. These accounting policy changes were adopted on a prospective basis with no restatement of prior period financial statements:

(i) Financial Instrument Disclosures and Presentation

CICA Handbook Sections 3862 *"Financial Instruments – Disclosures"* and Section 3863*"Financial Instruments – Presentation"* replace Section 3861 *"Financial Instruments – Disclosure and Presentation"*. The new standards carry forward the presentation requirements for financial instruments and enhance the disclosure requirements by placing increased emphasis on disclosures about the nature and extent of risks arising from financial instruments and how the entity manages those risks.

(ii) Capital Disclosures

CICA Handbook Section 1535 requires the company to disclose (a) its objectives, policies and processes for managing capital; (b) quantitative data about what the entity regards as capital; (c) whether the entity has complied with any capital requirements; and (d) if it has not complied, the consequences of such noncompliance.

(iv) Going Concern

CICA Handbook Section 1400 - General Standards of Financial Statements. The new standard requires management to make an assessment of the Company's ability to continue as a going concern, and to disclose any material uncertainties related to events or conditions that may cast significant doubt upon the entity's ability to continue as a going concern.

New Accounting Pronouncements Effective in Future Periods

CICA Handbook Section 3064 - Goodwill and other intangibles assets. This new section replaces Section 3062, Goodwill and other intangible assets and Section 3450, Research and development costs. It establishes standards for the recognition, measurement, presentation and disclosure of goodwill subsequent to its initial recognition and of intangible assets by profit-oriented enterprises. Standards concerning goodwill are unchanged from the standards included in the previous Section 3062. The new Section will be applicable to financial statements relating to fiscal years beginning on or after October 1, 2008. Management does not expect the adoption of this new standard to have a material impact on the financial statements of the Company or its business. The Company adopted the new standards for its fiscal year beginning October 1, 2009.

International Financial Reporting Standards (IFRS)

In 2006, the Accounting Standards Board ("AcSB") published a new strategic plan that will significantly affect financial reporting requirements for Canadian companies. The AcSB strategic plan outlines the convergence of Canadian GAAP with IFRS over an expected five year transitional period. In February 2008, the AcSB announced that 2011 is the changeover date for publicly-listed companies to use IFRS, replacing Canada's own GAAP. The date is for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2011. The transitional date of January 1, 2011 will require the restatement for comparative purposes of amounts reported by the Company for the year ended September 30, 2010.

Management plans for conversion include internal training, external consulting on complex issues and Board and Audit Committee oversight. The Company continues to monitor and assess the impact of convergence of Canadian GAAP and IFRS. Management has attended briefing seminars on the transition to IFRS, and we are awaiting the release of various exposure drafts and reports which will more clearly define the accounting standards for the mining exploration industry.

Risk, Uncertainties and Outlook

The business of mineral deposit exploration and extraction involves a high degree of risk. Few properties that are explored ultimately become producing mines. At present, none of the Company's properties has a known commercial ore deposit. Operations, the status of mineral property rights and the recoverability of amounts shown for mineral properties can be affected by changing economic, regulatory and political situations. Other risks facing the Company include competition for mineral properties, environmental and insurance risks, fluctuations in metal prices, fluctuations in exchange rates, share price volatility and uncertainty of additional financing.

Related Party Transactions

During the three months ended December 31, 2009, $4,500 (2008- $4,500) was paid to a private company wholly-owned by Stuart Rogers, a director and Chief Financial Officer of the Company, for office rent and administration services provided to the Company.

During this same period, $40,000 (2008- $Nil) was paid to a private company wholly-owned by John Lee, the President and a director of the Company, for management services provided.

During the three months ended December 31, 2009, $1,000 (2008- $3,000) was paid to James Brown, the former President of the Company, for management services provided to the Company.

These amounts were incurred in the ordinary course of business.

Contingencies

The Company is aware of no contingencies or pending legal proceedings as of March 1, 2010.

Equity Securities Issued and Outstanding

The Company had 29,892,266 common shares issued and outstanding as of March 1, 2010. In addition, there were 2,900,000 incentive stock options and 8,028,600 warrants outstanding as of March 1, 2010.

Disclaimer

The information provided in this document is not intended to be a comprehensive review of all matters concerning the Company. It should be read in conjunction with all other disclosure documents provided by the Company, which can be accessed at www.sedar.com. No securities commission or regulatory authority has reviewed the accuracy or adequacy of the information presented herein.

Certain statements contained in this document constitute "forward-looking statements". Such forward-looking statements involve known and unknown risks, uncertainties and other factors which may cause the actual results, performance, or achievements of the Company to be materially different from any future results, performance, or achievements expressly stated or implied by such forward-looking statements. Such factors include, among others, the following: mineral exploration and development costs and results, fluctuation in the prices of commodities for which the Company is exploring, competition, uninsured risks, recoverability of resources discovered, capitalization requirements, commercial viability, environmental risks and obligations, and the requirement for obtaining permits and licenses for the Company's operations in the jurisdictions in which it operates.