

PALLADON VENTURES LTD.  
UNAUDITED INTERIM CONSOLIDATED FINANCIAL STATEMENTS  
THREE AND NINE MONTHS ENDED NOVEMBER 30, 2009

PALLADON VENTURES LTD.

*Notice of No Auditor Review of Interim Consolidated Financial Statements*

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

"John W. Cutler"  
Chief Executive Officer

January 13, 2010

PALLADON VENTURES LTD.  
INTERIM CONSOLIDATED BALANCE SHEETS  
November 30, 2009 and February 28, 2009

	Unaudited	
	November 30, 2009	February 28, 2009
Cash	\$475,341	\$8,014,594
GST recoverable	3,077	47,352
Amounts receivable	-	59,219
Marketable securities	49,500	27,000
Total Current Assets	527,918	8,148,165
Property and equipment - Notes 4 and 13	4,201,867	5,176,266
Reclamation bond - Note 5	919,581	1,020,483
Mineral properties and related equipment - Schedule 1 and Note 6	31,270,440	28,182,884
Total Assets	36,919,806	42,527,798
Accounts payable and accrued liabilities	134,453	716,058
Due to related parties - Note 12	649,234	649,234
Loans payable - Notes 8 and 15	41,568,184	45,393,441
Total Current Liabilities	42,351,871	46,758,733
Total Liabilities	42,351,871	46,758,733
Share capital - Note 11	95,730,142	95,730,142
Contributed surplus - Note 11	3,071,383	3,071,383
Deficit	(104,233,590)	(103,032,460)
Total Shareholders' Equity (Deficiency)	(5,432,065)	(4,230,935)
Total Liabilities and Shareholders' Equity (Deficiency)	\$36,919,806	\$42,527,798

Nature of Operations and Ability to Continue as a Going Concern - Notes 2 and 15

Commitments - Notes 13 and 15

Subsequent Events - Note 15

APPROVED BY THE DIRECTORS:

*"John W. Cutler"*

\_\_\_\_\_  
John W. Cutler

*"Leonard J. Sojka"*

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Leonard J. Sojka

SEE ACCOMPANYING NOTES

PALLADON VENTURES LTD.

INTERIM CONSOLIDATED STATEMENTS OF OPERATIONS AND DEFICIT

For the three and nine months ended November 30, 2009 and 2008

	Unaudited		Unaudited	
	Three Months Ended		Nine Months Ended	
	November 30, 2009	November 30, 2008	November 30, 2009	November 30, 2008
General and Administrative Expenses:				
Amortization	\$227,034	\$431,275	\$786,531	\$476,361
Consulting - Note 12	89,951	263,472	340,668	324,382
Interest on loans payable	1,264,376	1,071,050	4,198,934	2,048,753
Office and administration	81,637	179,086	646,812	332,376
Professional fees	100,403	85,768	337,827	302,931
Rent	50,913	44,508	139,356	106,310
Salaries and benefits - Note 12	202,622	245,070	953,826	734,325
Shareholder communications	9,341	17,032	23,891	65,909
Telephone	2,135	4,303	7,112	11,014
Transfer agent and filing fees	3,964	29,540	19,160	52,969
Travel and promotion	22,388	41,428	104,113	87,642
Loss before other and non-controlling interest	(2,054,764)	(2,412,532)	(7,558,230)	(4,542,973)
Other:				
Unrealized gain (loss) on marketable securities	-	(87,750)	22,500	(121,500)
Write-off other assets	-	-	(187,734)	(10)
Other income	107	-	58,798	-
Gain (loss) on foreign exchange	1,074,354	(3,519,120)	6,463,537	(6,546,425)
Loss before non-controlling interest	(980,303)	(6,019,402)	(1,201,130)	(11,210,908)
Non-controlling interest - Note 7	-	-	-	292,231
Net loss for the period	(980,303)	(6,019,402)	(1,201,130)	(10,918,677)
Deficit, beginning of the period	(103,253,286)	(93,761,622)	(103,032,460)	(28,378,922)
Acquisition of non-controlling interest - Note 7	-	-	-	(60,483,425)
Deficit, end of the period	(\$104,233,590)	(\$99,781,024)	(\$104,233,590)	(\$99,781,024)
Basic and diluted loss per share	(\$0.01)	(\$0.04)	(\$0.01)	(\$0.08)
Weighted average number of shares outstanding	168,964,132	168,964,132	168,964,132	129,929,533

SEE ACCOMPANYING NOTES

**PALLADON VENTURES LTD.**  
**INTERIM CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**For the three and nine months ended November 30, 2009 and 2008**

	Unaudited		Unaudited	
	Three Months Ended		Nine Months Ended	
	November 30, 2009	November 30, 2008	November 30, 2009	November 30, 2008
<b>Operating Activities:</b>				
Net loss for the period, before non-controlling interest	(\$980,303)	(\$6,019,402)	(\$1,201,130)	(\$11,210,908)
Items not involving cash:				
Amortization	227,034	431,275	786,531	476,361
Unrealized (gain) loss on marketable securities	-	87,750	(22,500)	121,500
Unrealized foreign exchange (gain) loss	(1,106,320)	6,930,550	(7,999,109)	9,309,078
Accrued interest	1,264,376	-	3,646,387	-
Write-off of other assets	-	-	187,734	10
	<u>(\$95,213)</u>	<u>1,430,173</u>	<u>(4,602,088)</u>	<u>(1,303,958)</u>
<b>Changes in non-cash working capital items:</b>				
Amounts receivable	-	-	59,219	13,232
GST recoverable	44,275	-	44,275	422
Accounts payable and accrued liabilities	(94,140)	50,034	(581,605)	(664,167)
	<u>(49,865)</u>	<u>50,034</u>	<u>(478,111)</u>	<u>(650,514)</u>
Cash (used in) provided from operating activities	<u>(645,078)</u>	<u>1,480,207</u>	<u>(5,080,198)</u>	<u>(1,954,472)</u>
<b>Investing activities:</b>				
Acquisition of Palladon Iron Corporation	-	-	-	(38,826,000)
Acquisition of equipment	-	(5,193,772)	-	(6,111,900)
Reclamation bonds	-	-	(76,841)	(164,314)
Mineral property costs, net of recoveries	(337,776)	1,608,235	(3,007,713)	(907,769)
Cash (used in) provided from investing activities	<u>(337,776)</u>	<u>(3,585,538)</u>	<u>(3,084,555)</u>	<u>(46,009,982)</u>
<b>Financing activities:</b>				
Advances (to) from related parties	-	-	-	(233,780)
Issuance of shares for cash, net of share issuance cost:	-	-	-	59,980,239
Loans repaid	(206,780)	-	(206,780)	(551,058)
Cash (used in) provided from financing activities	<u>(206,780)</u>	<u>-</u>	<u>(206,780)</u>	<u>59,195,400</u>
Foreign exchange loss (gain) on cash held in US\$	(23,589)	-	832,280	-
Increase (decrease) in cash during the period	(1,213,223)	(2,105,331)	(7,539,253)	11,230,946
Cash, beginning of the period	1,688,564	14,156,657	8,014,594	820,381
Cash, end of the period	<u>\$475,341</u>	<u>\$12,051,327</u>	<u>\$475,341</u>	<u>\$12,051,327</u>
<b>Supplemental disclosure of cash flow information:</b>				
Cash paid for interest	-	\$132,522	\$499,123	\$536,665

PALLADON VENTURES LTD.  
 INTERIM CONSOLIDATED SCHEDULE OF MINERAL PROPERTIES AND RELATED EQUIPMENT  
 For the nine months ended November 30, 2009

Schedule 1

	Unaudited Iron Mountain Project, Utah, USA							Power Line	Total Iron Mountain	Total
	Other Properties	Mineral Property	Equipment Under Construction				Plant			
			Ball Mill	Rail Line	Transformer	Substation				
Beginning balance - February 28, 2009	\$894,672	\$19,745,924	\$1,503,034	\$3,915,094	-	-	\$1,146,588	\$977,572	\$27,288,212	\$28,182,884
Acquisition and Construction Costs	-	102,926	36,735	-	-	-	-	-	139,662	139,662
Exploration expenditures / (recovered):										
Field costs & claim fees & misc.	-	10,279	-	-	-	-	-	-	10,279	10,279
Consulting	-	1,228,113	-	(4,223)	-	-	1,224	-	1,225,114	1,225,114
Iron ore	-	227,428	-	-	-	-	-	-	227,428	227,428
Pre-stripping	-	1,758,392	-	-	-	-	-	-	1,758,392	1,758,392
Security and site maintenance	-	107,934	-	-	-	-	-	-	107,934	107,934
Less ore sales, net of costs	-	(247,961)	-	-	-	-	-	-	(247,961)	(247,961)
Subtotal	-	3,084,187	-	(4,223)	-	-	1,224	-	3,081,187	3,081,187
Amortization of advances	-	(133,294)	-	-	-	-	-	-	(133,294)	(133,294)
Ending balance - November 30, 2009	\$894,672	\$22,799,744	\$1,539,769	\$3,910,870	-	-	\$1,147,812	\$977,572	\$30,375,768	\$31,270,440

PALLADON VENTURES LTD.  
CONSOLIDATED SCHEDULE OF MINERAL PROPERTIES AND RELATED EQUIPMENT  
For the fiscal year ended February 28, 2009

Schedule 1

	Iron Mountain Project, Utah, USA							Power Line	Total Iron Mountain	Total
	Other Properties	Mineral Property	Equipment Under Construction				Plant			
			Ball Mill	Rail Line	Transformer	Substation				
Beginning balance - February 29, 2008	\$894,682	\$14,129,278	\$1,467,175	\$2,495,036	\$944,559	\$2,546,271	\$1,040,371	\$510,715	\$23,133,405	\$24,028,087
Acquisition and Construction Costs	-	1,271,34	35,859	1,399,25	38,387	174,85	-	951,58	3,871,29	3,871,29
Exploration expenditures / (recovered):										
Field costs & claim fees & misc.	-	-	-	2,568	-	-	-	-	2,568	2,56
Consulting	-	87,143	-	18,232	-	-	106,21	-	211,59	211,59
Iron ore	-	749,30	-	-	-	-	-	-	749,30	749,30
Pre-stripping	-	2,020,24	-	-	-	-	-	-	2,020,24	2,020,24
Security and site maintenance	-	232,04	-	-	-	-	-	-	232,04	232,04
Less ore sales, net of cost	-	(200,456)	-	-	-	-	-	-	(200,456)	(200,456)
Subtotal	-	2,888,26	-	20,800	-	-	106,21	-	3,015,28	3,015,28
Write-offs	(10)	-	-	-	-	-	-	-	-	(10)
Assets placed in service	-	-	-	-	(982,946)	(2,721,128)	-	(484,729)	(4,188,803)	(4,188,803)
Advances	-	1,457,03	-	-	-	-	-	-	1,457,03	1,457,03
Ending balance - February 28, 2009	\$894,672	\$19,745,924	\$1,503,034	\$3,915,094	-	-	\$1,146,588	\$977,572	\$27,288,212	\$28,182,884

**PALLADON VENTURES LTD.**  
NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS  
(Unaudited)  
November 30, 2009

Note 1 **Interim Financial Statements**

While the information presented in these interim consolidated financial statements is unaudited, it includes all adjustments which are, in the opinion of management, necessary to present fairly the financial position, results of operations and cash flows for the interim period presented. These interim consolidated financial statements follow the same accounting policies and methods of their application as the Company's February 28, 2009 consolidated financial statements, so it is suggested that these interim consolidated financial statements be read in conjunction with the audited annual financial statements.

Certain comparative figures for the periods have been reclassified to conform to the current period's presentation.

Note 2 **Nature of Operations and Ability to Continue as a Going Concern**

Palladon Ventures Ltd. ("Palladon" or the "Company") was incorporated on August 25, 1980 under the Company Act of British Columbia. The Company is publicly listed on the TSX Venture Exchange (the "Exchange") and on the Frankfurt exchange.

Palladon is a development stage company focused on mining iron ore from its wholly-owned Iron Mountain Project located in southwest Utah. The Company is in the process of exploring Iron Mountain, and has not yet determined whether the property contains reserves that are economically recoverable. The recoverability of amounts shown for mineral properties and deferred exploration costs is dependent upon the discovery of economically recoverable reserves and confirmation of the Company's interest in the underlying mineral properties, the ability of the Company to obtain necessary financing to complete the development of the properties, and upon future profitable production or proceeds from the disposition thereof.

The financial statements have been prepared in accordance with generally accepted accounting principles applicable to a going concern, which assumes that the Company will be able to meet its obligations and continue its operations for the next fiscal year. Realization values may be substantially different from carrying values as shown, and these financial statements do not give effect to adjustments that would be necessary to the carrying values and classification of assets and liabilities should the Company be unable to continue as a going concern.

At November 30, 2009, the Company had a working capital deficit of \$41.8 million, has not yet achieved profitable operations, has a deficit of \$104.2 million since inception, and expects to incur further losses in the development of its business, all of which cast substantial doubt about the Company's ability to continue as a going concern. This working capital deficit includes loans payable of \$41.6 million (Note 8). The Company's ability to continue as a going concern is dependent upon its ability to generate and maintain future profitable operations and to obtain the necessary financing to meet its obligations and repay its liabilities arising from normal business operations when they come due.

Note 3      **Significant Accounting Policies**

The financial statements of the Company have been prepared in accordance with generally accepted accounting principles in Canada and are stated in Canadian dollars. Because a precise determination of many assets and liabilities is dependent on future events, the preparation of financial statements for a period necessarily involves the use of estimates that have been made using careful judgment. Actual results may differ from these estimates. The financial statements have, in management's opinion, been properly prepared within reasonable limits of materiality and within the framework of the significant accounting policies summarized below:

a)    **Principles of Consolidation**

These financial statements include the accounts of the Company and its U.S. subsidiaries Palladon Iron Corporation ("PIC") and PIC Railroad Inc. ("PICR"). PIC was incorporated as a wholly-owned subsidiary in Utah on April 6, 2005 and holds the Iron Mountain mineral properties. During the year ended February 28, 2006, the Company sold 50% of its interest in PIC and at February 29, 2008 held 44% (2007:44%) of its issued shares. During the quarter ended August 31, 2008 the Company purchased the 56% of PIC that it did not own, thereby establishing 100% ownership (Note 7). PICR was incorporated during the year ended February 28, 2007 as a wholly-owned subsidiary of PIC.

b)    **Equipment and Amortization**

Equipment is recorded at cost. The Company provides for amortization using the following rates:

Building	10% declining balance
Mining equipment – long lived	20% declining balance
Mining equipment	30% declining balance
Office furniture and equipment	30% declining balance

Additions are amortized at one-half the normal rate during the year of acquisition. Plant and equipment under construction is not amortized until construction is complete and the assets are available for use.

c)    **Mineral Properties**

The Company defers the cost of acquiring, maintaining its interest, exploring and developing its mineral properties until such time as the property is placed into production, abandoned, sold or considered to be impaired in value. When operational, mineral property will be amortized on a unit of production basis. Proceeds received on the sale of interests in mineral properties and incidental sales are credited to the carrying value of the mineral properties, with any excess included in operations. Write-downs due to impairment in value are charged to operations.

The Company is in the process of exploring and developing its mineral properties and has not yet determined the amount of reserves available. Management reviews the carrying value of mineral properties on a periodic basis and will recognize impairment in value based upon current exploration results, the prospect of further work being carried out by the Company, the assessment of future probability of profitable revenues from the property or from the sale of the property. Amounts shown for properties represent costs incurred net of write-downs and recoveries, and are not intended to represent present or future values.

d) Basic and Diluted Gain (Loss) Per Share

Basic gain (loss) per share is computed by dividing the gain (loss) for the period by the weighted average number of common shares outstanding during the period. Diluted gain (loss) per share reflects the dilution that could occur if potentially dilutive securities were exercised or converted to common stock. The dilutive effect of options and warrants and their equivalent is computed by application of the treasury stock method. Common equivalent shares (consisting of shares issuable on the exercise of common stock options and warrants) totalling 22,211,739 as of November 30, 2009 (February 28, 2009: 33,341,819) were not included in the computation of diluted gain (loss) per share because the effect was anti-dilutive.

e) Income Taxes

The Company uses the asset and liability method of accounting for income taxes. Under this method, current income taxes are recognized for the estimated income taxes payable for the current period. Future income tax assets and liabilities are recognized for temporary differences between the tax and accounting basis of assets and liabilities as well as for the benefit of losses available to be carried forward to future years for tax purposes only if it is more likely-than-not that they can be realized.

f) Foreign Currency Translation

Monetary items denominated in a foreign currency are translated into Canadian dollars at exchange rates prevailing at the balance sheet date and non-monetary items are translated at exchange rates prevailing when the assets were acquired or obligations incurred. Foreign currency denominated revenue and expense items are translated at exchange rates prevailing at the transaction date. Gains or losses arising from the translations are included in operations.

g) Stock-based Compensation

The Company accounts for all grants of options to employees, non-employees and directors in accordance with the fair value method for accounting for stock-based compensation. Compensation expense for employees is generally amortized using the straight line method over the period from the grant date to the date the options vest. Compensation expense for non-employees is recognized immediately for past services and pro-rata for future services over the service provision period. Compensation for non-employees is re-measured at each balance sheet date until the earlier of vesting date or the date of completion of the service. Upon exercise of share purchase options, the

consideration paid by the option holder, together with the amount previously recognized in contributed surplus, is recorded as an increase to share capital.

h) Asset Retirement Obligations

The fair value of obligations associated with the retirement of tangible long-lived assets is recorded in the period the asset is put into use, with a corresponding increase to the carrying amount of the related asset. The obligations recognized are statutory, contractual or legal obligations. The liability is accreted over time for changes in the fair value of the liability through charges to accretion, which is included in depletion, depreciation and accretion expense. The costs capitalized to the related assets are amortized in a manner consistent with the depletion and depreciation of the related asset. At November 30, 2009 and February 28, 2009, the Company did not have any asset retirement obligations.

i) Impairment of Long-lived Assets

Canadian generally accepted accounting principles require that long-lived assets and intangibles to be held and used by the Company be reviewed for possible impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. If changes in circumstances indicate that the carrying amount of an asset that an entity expects to hold and use may not be recoverable, future cash flows expected to result from the use of the asset and its disposition must be estimated. If the undiscounted value of the future cash flows is less than the carrying amount of the asset, impairment is recognized. Except as provided, management believes there has been no impairment of the Company's long-term assets at November 30, 2009.

j) Comprehensive Income

Comprehensive income includes both net gain (loss) and other comprehensive income ("OCI"). OCI is the change in shareholders' equity from non-owner sources which is not included in the calculation of net gain (loss) until realized. Cumulative changes in OCI are included in Accumulated Other Comprehensive Income ("AOCI"), which is presented as a new category of shareholders' equity on the balance sheet. The Company had no OCI transactions during the quarter ended November 30, 2009 or the year ended February 28, 2009, and neither opening nor closing balances for AOCI.

k) Financial Instruments Recognition, Measurement, Disclosure and Presentation

All financial instruments are classified into one of these five categories: held-for-trading, held-to-maturity investments, loans and receivables, available-for-sale financial assets or other financial liabilities. All financial instruments and derivatives are measured on the trade date at fair value upon initial recognition. Subsequent measurement depends on the initial classification of the instrument. Held-for-trading financial assets are measured at fair value, with changes in fair value recognized in net earnings (loss). Available-for-sale financial instruments are measured at fair value, with changes in fair value recorded in OCI until the instrument is derecognized or impaired. Loans and receivables, held-to-maturity investments and other financial liabilities are measured at amortized cost. All derivative instruments, including embedded derivatives, are recorded in the

Palladon Ventures Ltd.  
Notes to the Interim Consolidated Financial Statements  
(Unaudited)  
November 30, 2009

balance sheet at fair value unless they qualify for the normal sales and purchases exemption. Changes in the fair value of derivatives that are not exempt are recorded in the statement of operations. Transaction costs on the acquisition of financial assets and liabilities that are classified as other than held-for-trading are expensed.

The Company has made the following designations of its financial instruments: cash and marketable securities as held-for trading; amounts receivable as loans and receivables; accounts payable and accrued liabilities, loans payable and due to related parties as other financial liabilities. At November 30, 2009 and February 28, 2009, the Company had neither available-for-sale nor held-to-maturity financial instruments.

1) Newly Adopted Accounting Pronouncements

Going-concern

In June 2007, the Canadian Institute of Chartered Accountants (“CICA”) amended Handbook section 1400, “General Standards of Financial Statement Presentation,” which requires management to make an assessment of the Company’s ability to continue as a going-concern. When financial statements are not prepared on a going-concern basis, that fact shall be disclosed together with the basis on which the financial statements are prepared and the reason why the Company is not considered a going-concern. Effective March 1, 2008, the Company adopted this standard and the adoption had no impact on the Company’s financial position or results of operations.

Capital Disclosures

In December 2006, the CICA issued Section 1535 “Capital Disclosures,” which specifies the disclosure of information that enables users of an entity’s financial statements to evaluate its objectives, policies and processes for managing capital, summary quantitative data about what the entity manages as capital, whether it has complied with any capital requirements and, if it has not complied, the consequences of non-compliance. The mandatory effective date is for annual interim financial statements for years beginning on or after October 1, 2007. Effective March 1, 2008, the Company adopted this standard and the related disclosures are included in Note 9.

Financial Instruments Disclosures and Financial Instruments Presentation

Sections 3862 and 3863 replace Section 3861, “Financial Instruments Disclosure and Presentation,” and establish standards for presentation of financial and non-financial derivatives and specify information that should be disclosed about them. These new sections place increased emphasis on disclosure about the nature and extent of risk arising from financial instruments and how the entity manages those risks. The effective date is for annual and interim financial statements for years beginning on or after October 1, 2007. Effective March 1, 2008, the Company adopted these standards (see Note 10).

Business Combinations, Consolidated Financial Statements, and Non-controlling Interests

In January 2009, the CICA issued Handbook Sections 1582 – *Business Combinations* (“Section 1582”), 1601 – *Consolidated Financial Statements* (“Section 1601”) and 1602 – *Non-controlling Interests* (“Section 1602”) which replaces CICA Handbook Section 1581 – *Business Combinations* and 1600 – *Consolidated Financial Statements*. Section 1582 establishes standards for the accounting for business combinations that is equivalent to the business combination accounting standard under International Financial Reporting Standards (“IFRS”). Section 1582 is applicable for the Company’s business combinations with acquisition dates on or after January 1, 2011. Early adoption of this Section is permitted. Section 1601 together with Section 1602 establishes standards for the preparation of consolidated financial statements. Section 1601 is applicable for the Company’s interim and annual consolidated financial statements for its fiscal year beginning January 1, 2011. Early adoption of this section is permitted. If the Company chooses to early adopt any of these Sections, the other two sections must also be adopted at the same time.

During the year ended February 28, 2009, the Company early adopted Handbook Section 1601, Consolidations, Handbook Section 1602, Non-controlling Interests, and Handbook Section 1582, Business Combinations. These sections replace the former CICA Handbook Section 1581, “Business Combinations” and Section 1600, “Consolidated Financial Statements” and establish a new section for accounting for a non-controlling interest in a subsidiary. CICA Handbook Section 1582 establishes standards for the accounting for a business combination, and states that all assets and liabilities of an acquired business will be recorded at fair value. Obligations for contingent consideration and contingencies will also be recorded at fair value at the acquisition date. Acquisition-related costs will be expensed as incurred and restructuring charges will be expensed in the periods after the acquisition date.

CICA Handbook Section 1602 establishes standards for accounting for a non-controlling interest in a subsidiary in the preparation of consolidated financial statements subsequent to a business combination. This standard states that changes in a parent’s ownership interest in a subsidiary that do not result in a loss of control are accounted for as equity transactions.

The new Sections 1582, 1601 and 1602 have been applied effective March 1, 2008, and except for presentation of the non-controlling interest, no restatement of the comparative periods was required. Under the new policy the non-controlling interest is presented as a component of shareholders’ equity.

#### m) Future Accounting Pronouncements

##### Goodwill and Intangible Assets

The CICA issued new Handbook Section 3064, “Goodwill and Intangible Assets”, which will replace Section 3062, “Goodwill and Other Intangible Assets”. The new standard establishes revised standards for the recognition, measurement, presentation and disclosure of goodwill and intangible assets. The new standard also provides guidance for the treatment of preproduction and start-up costs and requires that these costs be expensed as incurred. The new standard applies to annual and interim financial statements relating to fiscal years beginning on or after October 1, 2008. The Company is currently assessing the impact of these new accounting standards. The Company believes they will not have any significant impact on its consolidated financial statements.

International Financial Reporting Standards ("IFRS")

In 2006, the Canadian 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 transition date of January 1, 2011 will require the restatement for comparative purposes of amounts reported by the Company for the year ended February 28, 2011. The Company has begun an internal diagnostic review to understand, identify and assess the overall effort required to produce financial information under IFRS, however, at this time, the financial reporting impact of the transition to IFRS cannot be reasonably estimated.

Note 4 **Property and Equipment**

	Declining Balance Rate	November 30, 2009		
		Cost	Accumulated	
			Amortization	Net
Land	-	\$164,313	-	\$164,313
Building	10%	219,878	\$34,223	185,655
Mining equipment - long lived	20%	4,188,803	1,020,891	3,167,912
Mining equipment - other	30%	583,899	195,067	388,831
Office furniture and equipment	30%	484,626	189,471	295,155
Total		<u>\$5,641,519</u>	<u>\$1,439,652</u>	<u>\$4,201,867</u>

	Declining Balance Rate	February 28, 2009		
		Cost	Accumulated	
			Amortization	Net
Land	-	\$164,313	-	\$164,313
Building	10%	219,878	\$17,778	202,101
Mining equipment - long lived	20%	4,188,803	452,230	3,736,573
Mining equipment - other	30%	850,191	153,022	697,169
Office furniture and equipment	30%	489,683	113,573	376,110
Total		<u>\$5,912,869</u>	<u>\$736,603</u>	<u>\$5,176,266</u>

Note 5 **Reclamation Deposits**

The Company has an insurance policy of US\$1,299,100 as security for possible future reclamation work on the Iron Mountain property, for which the Company has deposited US\$650,000 as collateral with the insurer. Additional security deposits of US\$55,666 were paid during the nine months ended November 30, 2009. At November 30, 2009, total security deposits held by third parties were \$919,581 (US\$865,895) (February 28, 2009 \$1,020,483 (US\$809,907)).

Note 6 **Mineral Properties**

Title to mineral 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 mineral properties. The Company has investigated title to all of its mineral properties and, to the best of its knowledge, title to all of its properties is in good standing.

**Iron Mountain**

During the year ended February 28, 2006, the Company completed the purchase of the Iron Mountain properties, including Comstock / Mountain Lion and Rex properties located in Utah, US. The purchase price of the property was US\$10 million, of which \$50,000 was paid on signing, with \$1.3 million as a credit at closing for the amount of the reclamation bond obligation assumed by the Company (Note 5), and \$8.65 million paid in cash at closing. Prior to entering into the purchase agreement, the Company and Western Utah Copper Company (WUCC) entered into a Joint Venture Agreement, which provided that the Company shall have a 65% interest in the property, and WUCC shall have a 35% interest. Concurrently with the acquisition, the parties negotiated the buyout of WUCC's interest for US\$3.5 million plus the forgiveness of approximately US\$1.5 million in loans and accrued interest receivable previously made by the Company to WUCC. The Iron Mountain properties are held by the Company's subsidiary, Palladon Iron Corp.

During the nine months ended November 30, 2009, and the year ended February 28, 2009, incidental sales of iron ore were realized and credited against the carrying cost of the properties. During the year ended February 28, 2009, the Company engaged a contract mine operator (Note 13d) to commence mining activities, based on a contract to sell iron ore (Note 13a). All mining activity at the site was stopped in June 2009, and the Company negotiated termination of standby charges by the contract mine operator. No iron ore was shipped with respect to the contract to sell iron ore, and on September 15, 2009, the Company announced termination of the contract (Notes 13 and 15).

Note 7 **Acquisition of Non-controlling Interest**

During the year ended February 28, 2009, the Company achieved 100% ownership of PIC by purchasing the non-controlling interest for consideration of US\$65,000,000, of which US\$40,000,000 was paid on closing of a private placement (Notes 11 and 14), and US\$25,000,000 was deferred until June 26, 2009 plus interest accrued at 11.6% per annum. In conjunction with the purchase agreement, the terms of the already outstanding loan payable to Luxor were amended to

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revise the due date to be the same June 26, 2009 date as for the deferred purchase consideration. Both loans were extended on the June 26, 2009 due date (Note 8).

In accordance with the adoption of Handbook Section 1602, Non-controlling Interests, changes in a parent's ownership in a subsidiary that do not result in a loss of control are accounted for as equity transactions. In connection with the acquisition, \$60,483,425 was charged to deficit as follows:

Purchase price	\$64,499,500
Less: non-controlling interest at date of purchase	<u>(4,016,075)</u>
Excess to deficit	<u>\$60,483,425</u>

Note 8 **Loans Payable**

	<u>November 30, 2009</u>	<u>February 28, 2009</u>
Term Loan of US\$9,722,151 (February 28, 2009: US\$9,064,074) due December 4, 2009, with interest at 12.5% per annum, compounded quarterly	\$10,324,925	\$11,420,734
Deferred Loan of US\$29,419,265 (February 28, 2009: US\$26,962,466) due December 4, 2009, with interest at 12.5% per annum, compounded quarterly	<u>31,243,259</u>	<u>33,972,707</u>
	41,568,184	45,393,441
Less current portion	<u>(\$41,568,184)</u>	<u>(\$45,393,441)</u>
	<u>-</u>	<u>-</u>

Both the Term Loan and the Deferred Loan are owed to Luxor Capital Partners, LP ("Luxor").

On the June 26, 2009 due date, Palladon negotiated an extension of the Luxor loans' maturity date to October 15, 2009. The interest rate on both loans was increased to 12.5%, compounded quarterly, from 9.25% on the Term Loan and from 11.6% on the Deferred Loan. The Company also paid additional interest of US\$500,000, which was added to the Term Loan. Both Luxor loans are collateralized by a promissory note, a general security agreement, the shares of PIC and a mortgage on the Murdock Railway Property.

On October 15, 2009, the Company announced a standstill agreement with Luxor that extended the October 15, 2009 due date to December 4, 2009. In connection with the standstill agreement, the Company repaid \$200,000 of the Luxor loan amount outstanding.

On December 4, 2009, Palladon announced that effective immediately the Company and Luxor entered into a letter of agreement (the "Letter Agreement"), subject to TSX Venture Exchange approval, to the extension agreement dated June 26, 2009, and to the standstill agreement dated October 15, 2009. The Letter Agreement grants Palladon an irrevocable option (the "Payment

Option") to acquire from Luxor the entirety of its outstanding loans including interest (the "Loan Amount"), by paying US\$30 million on or before March 31, 2010.

In the event that the Company does not exercise the Payment Option on or before March 31, 2010, Luxor has agreed to reduce the outstanding Loan Amount to US\$25 million, in exchange for transfer and assignment by the Company of 50% of the equity of PIC to Luxor (the "Luxor Equity"), subject to terms and conditions to be set out in a definitive agreement. Such terms include, but are not limited to, Luxor having control the PIC board of directors.

The US\$25 million Loan Amount will then accrue interest at the three-month LIBOR rate plus 500 basis points, with a 3% LIBOR floor resulting in a minimum rate of 8%, and such interest will be due and payable quarterly in arrears at the end of each calendar quarter. At Palladon's option, all or any portion of the interest due on any interest payment date may be paid by adding such interest to the principal amount, with such unpaid interest accruing interest from such Interest Payment Date at the foregoing rate and being treated for all purposes as principal. The loan shall mature 3 years from the expiry of the Payment Option.

Furthermore, in the event that Palladon does not exercise the Payment Option on or before March 31, 2010, it shall have a three-year option to purchase 50% of the Luxor Equity for US\$18.75 million.

Note 9 **Management of Capital**

The Company manages and adjusts its capital structure based on available funds in order to support its operations and the acquisition and exploration of mineral properties. The Company's primary objectives in managing capital are:

- Safeguard the entity's ability to continue as a going concern
- Maintain an optimal capital base in order to support the capital requirements of its operations, including growth opportunities and maintaining investor confidence.

The capital of the Company consists of shareholders' equity. The Board of Directors does not establish quantitative return on capital for management, but rather relies on the expertise of the Company's management to sustain future development of the business. The Company is not subject to any externally imposed capital requirements, other than as described in the subsequent paragraph. The Company relies on capital markets to support continued growth.

Palladon has limited flexibility with respect to managing its capital structure. As discussed in Note 8 above and in Note 15, the Company needs to raise funding to finance the repayment of its debt outstanding by March 31, 2010, or 50% of PIC will be transferred to Luxor in exchange for reduction of the debt. Furthermore, the Company also needs to raise capital to continue to fund day to day operations and to further the development of the Iron Mountain Project.

Note 10 **Financial Instruments**

The Company's financial instruments consist of cash, amounts receivable, marketable securities, accounts payable, accrued liabilities, due to related parties and loans payable. 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.

a) Credit Risk

Credit risk is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation. The Company's cash and receivables are exposed to credit risk. The Company reduces its credit risk on cash by placing these instruments with institutions of high credit worthiness. As of the end of the period the Company is not exposed to any significant credit risk.

b) Liquidity Risk

The Company's exposure to liquidity risk is dependent on purchasing commitments and obligations, and the raising of funds to meet commitments and sustain operations. The Company is a development stage company and is reliant on external fundraising to support its operations. The Company manages liquidity risk by continuously monitoring actual and projected cash flows. The Board of Directors reviews and approves the Company's operating and capital budgets, as well as any material transactions not in the ordinary course of business. The majority of the Company's accounts payable and accrued liabilities have maturities of less than three months.

The Company is specifically exposed to cash repayments of the Luxor loans, which were extended to December 4, 2009, and were then renegotiated pursuant to the Letter of Agreement (Notes 8 and 15). Given these circumstances and the uncertainty that the Company can raise additional financing, commence profitable operations and further refinance or extend the loans, the Company could lose all of its interest in the Iron Mountain properties and related equipment.

c) Market Risk – Interest Rate and Foreign Exchange

The Company's activities are conducted in U.S. dollars within the United States. Financial results are translated into Canadian dollars for financial reporting purposes.

Note 11 **Share Capital**

Shares Authorized: Unlimited common shares without par value.

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<u>Shares Issued</u> :		Number	Share	Contributed
		of Shares	Capital	Surplu
Balance, February 29, 2008		76,417,46	\$35,691,02	\$3,166,38
Exercise of warrants, at	\$0.50	3,126,000	1,563,00	-
Exercise of warrants, at	\$0.70	773,61	541,52	-
Exercise of options, at	\$0.40	300,00	120,00	-
Exercise of options, at	\$0.50	100,00	50,000	-
Transfer from contributed surplus to share capital on exercise of stock options		-	95,000	(95,000)
Private placement, at	\$0.70	87,375,16	61,162,61	-
Agent shares - non-cash	\$0.70	871,88	610,32	-
Less share issue		-	(4,103,353)	-
Balance, February 28, 2009		168,964,13	95,730,14	3,071,383
		-	-	-
Balance, November 30, 2009		168,964,13	\$95,730,14	\$3,071,38

During the year ended February 28, 2009, pursuant to a non-brokered private placement, the Company issued 87,375,169 units at \$0.70 per unit for total proceeds of \$61,162,618. Each unit consisted of one share and 1/4 of one share purchase warrant. Each whole warrant entitles the holder to purchase one additional common share at \$1.00 per share for eighteen months. In conjunction with the placement the Company paid a sales commission consisting of \$3,493,033 in cash plus 871,885 units. The Company uses the residual method to allocate the transaction date market price to shares sold, which resulted in no allocation of value to the warrants. The agent's warrants included in the units were thus valued at \$nil.

Commitments:

a) Share Purchase Options:

The Company may grant share purchase options to directors, officers or employees to acquire shares of the Company. Unless noted otherwise, the share purchase options vest when granted. Share purchase option activity for the nine months ended November 30, 2009 and year ended February 28, 2009 is summarized as follows:

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	Nine months ended November 30, 2009		Year ended February 28, 2009	
	Number of Shares	Weighted Average Exercise Price	Number of Shares	Weighted Average Exercise Price
Balance, beginning of period	1,030,00	\$0.55	2,835,00	\$0.51
Cancelled	(880,000)	0.58	(1,405,000)	0.51
Exercised	-	-	(400,000)	0.43
Balance, end of period	150,00	\$0.40	1,030,00	\$0.55

As of November 30, 2009, there were 150,000 share purchase options outstanding, each of which entitles the holder to purchase one common share at \$0.40 until expiration on October 31, 2012.

b) Share Purchase Warrants:

Each warrant entitles the holder to purchase one common share. Activity for the quarter ended November 30, 2009 and year ended February 28, 2009 is as follows:

	Warrants	Weighte Average
Outstanding February 29, 2008	26,156,93	\$0.62
Issued	22,061,73	1.00
Exercise	(3,899,613)	0.54
Expired	(12,007,238)	0.74
Outstanding February 28, 2009	32,311,81	0.84
Expired	(10,250,080)	0.50
Outstanding November 30, 2009	22,061,73	\$1.00

On May 10, 2009, 10,250,080 warrants at an exercise price of \$0.50 per share expired unexercised.

As of November 30, 2009, there were 22,061,739 warrants outstanding. Each warrant entitles the holder to purchase one common share at an exercise price of \$1.00. These warrants expired unexercised on December 26, 2009.

Note 12 Related Party Transactions

The Company incurred the following transactions with related parties consisting of current and/or former directors of the Company or private companies controlled by them:

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	Three months ended		Nine months ended	
	November 30,		November 30,	
	2009	2008	2009	2008
Consulting fees	\$20,769	-	\$142,651	\$7,586
Directors' fees	40,002	-	112,138	-
Salaries and benefits	46,669	\$82,706	256,701	272,605
Total	\$107,439	\$82,706	\$511,490	\$280,191

During the three and nine months ended November 30, 2009, the Company paid consulting fees to a director – a former CPA with major accounting firm experience – as follows:

- To reconstitute the financial reporting and accounting function,
- To amend and restate three prior interim period financial statements and the related Management's Discussion and Analysis,
- To close the books and prepare financial statements for the annual audit and to work with the outside audit firm to complete the annual audit for the period ended February 28, 2009, and
- To perform the job responsibilities of the Chief Financial Officer function, including preparing the quarterly financial statements and related Management's Discussion and Analysis.

Monthly directors' fees were paid for services rendered. Salaries and benefits for the nine month period ended November 30, 2009 include salary and final payments to the prior CEO and CFO.

Balance sheet amounts due to related parties are owing to former directors and to an affiliate of a former director, and are unsecured, non-interest bearing and due on demand.

Note 13 **Commitments**

- a) During the year ended February 28, 2009, PIC entered into a contract for a term expiring March 31, 2013, to supply 2,000,000 metric tonnes of iron ore during each twelve month period. Under the contract terms, the iron ore was to be delivered freight on board ("FOB") to the Port of Long Beach, California for US\$70 per metric tonne until March 31, 2009, and thereafter subject to adjustment based on the World Benchmark Price for iron ore.

No iron ore was shipped pursuant to this contract. On September 15, 2009, the Company announced that its wholly owned subsidiary, Palladon Iron Corporation ("PIC"), had notified the buyer – China Kingdom International (Australia) PTY LTD, / CKI Minerals & Metals ("CKI") – of the termination of the Sales Agreement for the Purchase of Iron Ore dated March 31, 2008, between PIC as seller and CKI as buyer, subject to the dispute resolution mechanisms as set out in that agreement. When the Agreement was negotiated and entered into, both parties understood that the iron ore would be delivered to CKI at the Port of Long Beach. This understanding is set forth in the Agreement. At that time, both parties knew that PIC had

not yet entered into a signed agreement for the storage of the iron ore at the Port of Long Beach, and both parties knew that the performance of the Agreement would be dependent upon PIC successfully obtaining such a signed storage agreement. Subsequent to the signing of the Agreement, and despite its best efforts, PIC was unable to secure a signed agreement for a storage facility at the Port of Long Beach. This made it commercially impracticable or impossible for either party to perform its obligations under the Agreement.

On January 4, 2010, more than four months after PIC notified CKI that the Agreement was terminated, CKI first notified PIC that it did not agree with PIC's assertion that the Agreement was terminated.

On January 8, 2010 Palladon announced that PIC submitted a Request for Arbitration with respect to the termination of the Sales Agreement for the Purchase of Iron Ore (the "Agreement") dated March 31, 2008, between PIC as seller and CKI as buyer.

Pursuant to the Agreement, all disputes between the parties are to be resolved by arbitration in Salt Lake City, Utah, under the Rules of Arbitration of the International Chamber of Commerce. Accordingly, PIC has submitted a request for arbitration to the International Chamber of Commerce, seeking a determination of the issue of whether the Agreement is terminated due to the commercial impracticability or impossibility of either party to perform its obligations under the Agreement.

- b) The Company has entered into a five-year lease ending April 30, 2014 for office premises located in Salt Lake City, Utah. First year rent is US\$9,888 per month, increasing annually thereafter at an inflation factor, to \$11,129 per month in the final year.
- c) The Company has entered into an agreement to supply, if requested, a minimum of 12,000 tons of iron ore per year over a four-year term ending December 31, 2011.
- d) PIC entered into a contract dated June 1, 2008, with an independent mining contractor whereby the contractor agreed to mine and process iron ore at the Iron Mountain Project until May 31, 2013. Under the contract terms, PIC agreed to a fixed rate per ton for the amount of ore mined and loaded, and rental rates for use of equipment provided by the contractor, subject to a minimum standby fee of US\$500,000 per month. The rates are subject to a 2% annual increase after the first year.

During the quarter ended November 30, 2009, the contractor agreed to waive any future standby charges under the contract in exchange for retention of unused advances in the amount of US\$1.0 million (CDN\$1.3 million), plus the transfer from PIC to the contractor of a piece of mining equipment with a net book value of US\$190 thousand (CDN\$186 thousand), plus a royalty on future production.

Investing and financing activities that do not have a direct impact on current cash flows are excluded from the cash flow statements.

During the year ended February 28, 2009, the following transactions were excluded from the statement of cash flows:

- a) The Company issued 871,885 units valued at \$610,320 as partial payment of a sales commission related to a private equity placement (Note 11).
- b) The Company, in relation to the purchase of the remaining non-controlling interest (Note 7), issued a note payable in the amount of \$25,673,500 (US\$25,000,000).

Note 15 **Subsequent Events**

Subsequent to November 30, 2009:

- a) On December 4, 2009, Palladon announced that effective immediately the Company and Luxor entered into a letter of agreement (the "Letter Agreement"), subject to TSX Venture Exchange approval, to the extension agreement dated June 26, 2009, and to the standstill agreement dated October 15, 2009. The Letter Agreement grants Palladon an irrevocable option (the "Payment Option") to acquire from Luxor the entirety of its outstanding loans including interest (the "Loan Amount"), by paying US\$30 million on or before March 31, 2010 (Note 8).

In the event that the Company does not exercise the Payment Option on or before March 31, 2010, Luxor has agreed to reduce the outstanding Loan Amount to US\$25 million, in exchange for transfer and assignment by the Company of 50% of the equity of PIC to Luxor (the "Luxor Equity"), subject to terms and conditions to be set out in a definitive agreement. Such terms include, but are not limited to, Luxor having control the PIC board of directors.

The US\$25 million Loan Amount will then accrue interest at the three-month LIBOR rate plus 500 basis points, with a 3% LIBOR floor resulting in a minimum rate of 8%, and such interest will be due and payable quarterly in arrears at the end of each calendar quarter. At Palladon's option, all or any portion of the interest due on any interest payment date may be paid by adding such interest to the principal amount, with such unpaid interest accruing interest from such Interest Payment Date at the foregoing rate and being treated for all purposes as principal. The loan shall mature 3 years from the expiry of the Payment Option.

Furthermore, in the event that Palladon does not exercise the Payment Option on or before March 31, 2010, it shall have a three-year option to purchase 50% of the Luxor Equity for US\$18.75 million.

- b) On December 26, 2009, warrants for 22,061,739 shares expired.
- c) On January 8, 2010, Palladon Iron Corporation filed a Request for Arbitration with the Secretariat of the International Court of Arbitration, Re: *Palladon Iron Corporation ("PIC")*

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*(Seller) vs. China Kingdom International (Australia) PTY Ltd. and CKI Minerals & Metals Co., Ltd. ("CKI") (Buyer), seeking a determination that the "Sales Agreement for the Purchase of Iron Ore" is terminated due to the commercial impracticability or impossibility of either party to perform its obligations under the Agreement (Note 13).*