



## **TALON METALS CORP.**

### **Condensed Consolidated Interim Financial Statements**

**September 30, 2017 and 2016**

*(Expressed in Canadian dollars)*

These unaudited Condensed Consolidated Interim Financial Statements of Talon Metals Corp. (the "Company") have not been reviewed by the auditors of the Company. This notice is being provided in accordance with Section 4.3(3)(a) of National Instrument 51-102 (Continuous Disclosure Obligations).

**Talon Metals Corp.**  
**Condensed Consolidated Interim Balance Sheets**

*(Expressed in Canadian dollars)*

*(Unaudited)*

	<i>Notes</i>	<b>September 30, 2017</b>	<b>December 31, 2016</b>
<b>Assets</b>			
<b>Current assets</b>			
Cash and cash equivalents		\$ 1,255,772	\$ 676,542
Prepayments		64,693	22,948
Accounts and other receivables		1,514	9,909
Deferred financing costs		-	114,766
		<u>1,321,979</u>	<u>824,165</u>
<b>Non-current assets</b>			
Equipment and software		23,936	34,153
Resource properties and deferred expenditures	4	<u>38,378,189</u>	<u>37,052,077</u>
		<u>\$ 39,724,104</u>	<u>\$ 37,910,395</u>
<b>Liabilities</b>			
<b>Current liabilities</b>			
Accounts payable and accrued liabilities	12	\$ 187,162	\$ 278,579
Contingencies	13	<u>254,937</u>	<u>266,841</u>
		442,099	545,420
<b>Long-term liabilities</b>			
Unsecured convertible loan	5	<u>24,451,752</u>	<u>18,620,651</u>
		<u>\$ 24,893,851</u>	<u>\$ 19,166,071</u>
<b>Shareholders' equity</b>			
Share capital	6a	\$ 80,182,410	\$ 80,182,410
Warrants	6b	903,521	539,793
Contributed surplus		16,241,559	16,178,464
Deficit		<u>(82,497,237)</u>	<u>(78,156,343)</u>
		<u>14,830,253</u>	<u>18,744,324</u>
		<u>\$ 39,724,104</u>	<u>\$ 37,910,395</u>

**Nature of Operations and Going Concern - Note 1**  
**Subsequent Event - Note 16**

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

Approved by the audit committee of the board of directors on November 10, 2017

Signed:

*"Gregory S. Kinross"*

*"David E. Singer"*

**Talon Metals Corp.****Condensed Consolidated Interim Statements of Loss and Comprehensive Loss***(Expressed in Canadian dollars)**(Unaudited)*

		Three months ended September 30, 2017	Three months ended September 30, 2016	Nine months ended September 30, 2017	Nine months ended September 30, 2016
<b>Revenue</b>					
Interest income		\$ 1,535	\$ 472	\$ 3,301	\$ 1,070
<b>Expenses</b>					
Salaries, benefits, consulting and Brazil administration	12	98,873	113,432	290,191	495,734
Professional fees		21,288	24,452	79,684	61,737
Office and general		10,439	19,828	36,444	73,543
Insurance		18,530	15,695	68,157	47,160
Travel		(1,089)	4,393	-	13,577
Listing, filing and shareholder communications		7,426	6,196	49,995	60,716
Stock option compensation	7	-	-	-	43,596
Depreciation of equipment and software		4,149	(6,464)	10,217	16,660
Loss on investments		-	-	-	1,150,044
Impairment loss on resource properties	4	74	-	4,543	30,661
Refund of deposit		-	-	(7,911)	-
Loss (gain) on revaluation of unsecured convertible loan	5	533,966	(273,724)	3,775,176	(1,511,713)
Foreign currency translation loss (gain)		51,501	(16,090)	37,699	(296,051)
		<u>745,157</u>	<u>(112,282)</u>	<u>4,344,195</u>	<u>185,664</u>
<b>Net income (loss) and comprehensive income (loss)</b>		<u>\$ (743,622)</u>	<u>\$ 112,754</u>	<u>\$ (4,340,894)</u>	<u>\$ (184,594)</u>
<b>Basic and diluted net income (loss) per share</b>	8	<u>\$ (0.01)</u>	<u>\$ 0.00</u>	<u>\$ (0.03)</u>	<u>\$ (0.00)</u>
Weighted average shares outstanding - basic and diluted		<u>129,645,201</u>	<u>129,645,201</u>	<u>129,645,201</u>	<u>129,356,021</u>

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

**Talon Metals Corp.**

**Condensed Consolidated Interim Statements of Changes in Equity**

(Expressed in Canadian dollars)

(Unaudited)

	Notes	Common shares		Warrants	Contributed surplus	Deficit	Shareholders' equity
		Number	Amount				
Balance at January 1, 2017		129,645,201	\$ 80,182,410	\$ 539,793	\$ 16,178,464	\$ (78,156,343)	\$ 18,744,324
Warrants issued	6b	-	-	426,823	-	-	426,823
Warrants expired	8b	-	-	(63,095)	63,095	-	-
Stock option compensation payments	7	-	-	-	-	-	-
Net income (loss)		-	-	-	-	(4,340,894)	(4,340,894)
<b>Balance at September 30, 2017</b>	<b>6a</b>	<b>129,645,201</b>	<b>\$ 80,182,410</b>	<b>\$ 903,521</b>	<b>\$ 16,241,559</b>	<b>\$ (82,497,237)</b>	<b>\$ 14,830,253</b>
Balance at January 1, 2016		128,809,937	\$ 80,107,904	\$ 602,100	\$ 16,070,178	\$ (76,790,865)	\$ 19,989,317
Shares issued	8a	835,264	74,506	-	-	-	74,506
Warrants issued	8b	-	-	2,383	-	-	2,383
Stock option compensation payments	7	-	-	-	43,596	-	43,596
Net income (loss)		-	-	-	-	(184,594)	(184,594)
<b>Balance at September 30, 2016</b>	<b>6a</b>	<b>129,645,201</b>	<b>\$ 80,182,410</b>	<b>\$ 604,483</b>	<b>\$ 16,113,774</b>	<b>\$ (76,975,459)</b>	<b>\$ 19,925,208</b>

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

**Talon Metals Corp.**  
**Condensed Consolidated Interim Statements of Cash Flows**

*(Expressed in Canadian dollars)*

*(Unaudited)*

	<b>Nine months ended September 30, 2017</b>	<b>Nine months ended September 30, 2016</b>
<b>Cash flows from operating activities</b>		
Net loss	\$ (4,340,894)	\$ (184,594)
<b>Non-cash adjustments:</b>		
Stock option compensation	-	43,596
Loss (gain) on revaluation of unsecured convertible loan	3,775,176	(1,511,713)
Warrants issued for consulting services	-	2,383
Decrease in contingencies due to foreign exchange translation	(11,904)	-
Loss on investments	-	1,150,044
Impairment loss on resource properties	4,543	30,661
Depreciation of equipment and software	10,217	16,660
	<u>(562,862)</u>	<u>(452,963)</u>
<b>Working capital adjustments:</b>		
(Increase) decrease in prepayments	(41,745)	(11,698)
Decrease (increase) in accounts and other receivables	8,395	19,980
Decrease in accounts payables and accrued liabilities	(91,417)	(227,467)
<b>Net cash flows used in operating activities</b>	<u>(687,629)</u>	<u>(672,148)</u>
<b>Cash flows from investing activities</b>		
Disposition (Acquisition) of equipment and software	-	31,885
Proceeds on sale of investments	-	578,470
Acquisition of resource properties and deferred expenditures	(1,330,655)	(21,776,796)
Restricted cash invested in resource properties and deferred expenditures	-	20,760,000
<b>Net cash flows used in investing activities</b>	<u>(1,330,655)</u>	<u>(406,441)</u>
<b>Cash flows from financing activities</b>		
Proceeds from issuance of shares, net of costs	-	74,506
Proceeds from issuance of warrants, net of costs	426,823	-
Proceeds from unsecured convertible loan, net of costs	2,055,925	-
Decrease in deferred financing costs	114,766	-
<b>Net cash flows provided by financing activities</b>	<u>2,597,514</u>	<u>74,506</u>
<b>Net increase (decrease) in cash and cash equivalents</b>	<u>579,230</u>	<u>(1,004,083)</u>
Cash and cash equivalents, beginning of the year	676,542	2,014,013
<b>Cash and cash equivalents, end of the year</b>	<u>\$ 1,255,772</u>	<u>\$ 1,009,930</u>

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

# Talon Metals Corp.

## Notes to the Condensed Consolidated Interim Financial Statements For the three and nine months ended September 30, 2017 and 2016 (Expressed in Canadian dollars)

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### 1. NATURE OF OPERATIONS AND GOING CONCERN

Talon Metals Corp. (“Talon” or the “Company”) is a mineral exploration company focused on the exploration and development of the Tamarack nickel-copper-PGE project (the “Tamarack Project”) in Minnesota, USA (which is comprised of the Tamarack North Project and the Tamarack South Project). The Company currently holds an 18.45% interest in the Tamarack Project, which was earned pursuant to an Exploration and Option Agreement (the “Tamarack Earn-in Agreement”) (as amended) that the Company is a party to with Kennecott Exploration Company (“Kennecott”), a subsidiary of the Rio Tinto Group. The Company’s interest in the Tamarack Project is held through its indirect Delaware, USA subsidiary, Talon Nickel (USA) LLC (“Talon Nickel”). The Company also holds a 100% interest in the Trairão iron project (the “Trairão Project”) in Brazil which is held through its indirect Brazilian subsidiary, Talon Ferrous Mineração Ltda.

The Company’s head office address is Craigmuir Chambers, P.O. Box 71, Road Town, Tortola, British Virgin Islands.

A subsidiary is an entity that is controlled by the Company. In assessing control, potential voting rights that are presently exercisable or convertible, are taken into account in the assessment of whether control exists. Subsidiaries are fully consolidated from the date on which control is transferred to the Company. They are deconsolidated from the date on which control ceases.

All intercompany accounts and transactions have been eliminated.

The Company has not earned any revenue to date from its operations. The Company, and its partner Kennecott, are in the process of exploring the Tamarack Project and the Company has not yet determined whether the Tamarack Project contains ore reserves that are economically recoverable. The recoverability of the Company’s property carrying value and of the related deferred exploration expenditures depends on the Company’s ability to maintain an interest in the Tamarack Project, discover economically recoverable reserves and on the Company’s ability to obtain necessary financing to complete the development and to establish profitable production in the future, or the receipt of sufficient proceeds on disposal of its interest in the Tamarack Project.

As at September 30, 2017, the Company had working capital of \$0.9 million (December 31, 2016 – \$0.3 million) and Shareholders’ equity of \$16.3 million (December 31, 2016 – \$18.7 million). Working capital is defined as current assets less current liabilities.

These condensed consolidated interim financial statements have been prepared on a going concern basis which contemplates that the Company will continue in operations for the foreseeable future and will be able to realize its assets and discharge its liabilities in the normal course of business. The Company’s ability to continue as a going concern is dependent on its ability to sell non-core assets, cut costs and/or raise financing. There can be no assurance that the Company will be successful in selling non-core assets, cutting sufficient costs and/or, in compliance with the RCF Loan Agreement (note 5), raising financing to meet the Company’s commitments.

These circumstances cast significant doubt on the Company’s ability to continue as a going concern and ultimately on the appropriateness of the use of accounting principles applicable to a going concern.

Please see note 10(b) “Liquidity Risk” for more information in this regard.

These condensed consolidated interim financial statements do not give effect to any adjustments that would be necessary to the carrying values and classifications of assets and liabilities should the Company be unable to continue as a going concern.

# Talon Metals Corp.

## Notes to the Condensed Consolidated Interim Financial Statements For the three and nine months ended September 30, 2017 and 2016 (Expressed in Canadian dollars)

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### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

#### Statement of compliance

These condensed consolidated interim financial statements have been prepared in accordance with International Financial Reporting Standards (“IFRS”), interpretations as issued by the International Accounting Standards Board (“IASB”) and in particular International Accounting Standard (“IAS”) 34 (Interim Financial Reporting) as issued by the IASB.

These condensed consolidated interim financial statements were approved by the Audit Committee of the Board of Directors of the Company on November 10, 2017.

#### Basis of preparation

These condensed consolidated interim financial statements are presented in Canadian dollars. The condensed consolidated interim financial statements are prepared on the historical cost basis, except for portfolio investments and financial instruments that are measured at fair value.

#### Foreign currencies

##### *Functional and presentation currency*

The Canadian dollar is the functional currency and reporting currency of the Company and of all its subsidiaries.

The condensed consolidated interim financial statements are presented in Canadian dollars. Monetary items are translated into Canadian dollars at the rate of exchange in effect at the end of the reporting period. Revenues and expenses are translated into Canadian dollars at the rates of exchange prevailing when the underlying transactions occurred.

Foreign exchange gains and losses resulting from the settlement of foreign currency transactions and from the translation of monetary assets and liabilities denominated in foreign currencies are recognized in the condensed consolidated interim statements of loss and comprehensive loss.

#### Cash and cash equivalents

Cash and cash equivalents consist of cash deposits in banks, certificates of deposit, money market funds and short-term investments with remaining maturities of three months or less at the time of acquisition. At September 30, 2017 and December 31, 2016, the Company held both cash and cash equivalents.

#### Equipment

Equipment is carried at cost, less accumulated depreciation and accumulated impairment losses. The cost of an item of equipment consists of the purchase price, any costs directly attributable to bringing the asset to the location and condition necessary for its intended use and an initial estimate of the costs of dismantling and removing the item and restoring the site on which it is located. An item of equipment is derecognized upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on disposal of the asset, determined as the difference between the net disposal proceeds and the carrying amount of the asset, is recognized in the condensed consolidated interim statements of loss and comprehensive loss. Where an item of equipment comprises major components with different useful lives, the components are accounted for as separate items of equipment. Expenditures incurred to replace a component of an item of equipment that is accounted for separately, including major inspection and overhaul expenditures are capitalized.

# Talon Metals Corp.

## Notes to the Condensed Consolidated Interim Financial Statements For the three and nine months ended September 30, 2017 and 2016 (Expressed in Canadian dollars)

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The Company provides for depreciation of its equipment and software at the following annual rates:

Office and equipment	10% to 33% straight-line basis
Software	33% straight-line basis

### Resource properties and deferred exploration and evaluation costs

Interests in mineral exploration properties are recorded at cost. Exploration and development expenditures, including an allocation of salaries, benefits and consulting fees, other than those of a general nature, relating to mineral properties in which an interest is retained are deferred and carried as an asset until the results of the projects are known. If the project is unsuccessful or if exploration has ceased because continuation is not economically feasible, the cost of the property and the related exploration expenditures are written off or written down to the net recoverable amount of the deferred exploration expense.

The cost of mineral properties includes the cash consideration paid and the fair value of shares issued on the acquisition of properties. Properties acquired under option agreements, whereby option payments are made at the discretion of the Company, are recorded in the condensed consolidated interim financial statements at the time payments are made. The proceeds from options granted on properties are credited to the cost of the related property.

The amounts shown for mineral properties and deferred exploration costs represents cost to date less accumulated impairment, and do not necessarily represent present or future values as they are entirely dependent upon the economic recovery of future reserves.

The Company does not accrue the estimated future costs of maintaining its mineral properties in good standing.

### Impairment of non-financial assets

At the end of each reporting period, the carrying amounts of the Company's non-financial assets are reviewed to determine whether there is any indication that those assets have suffered an impairment loss. Where such an indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment, if any. The recoverable amount is the higher of fair value less costs to sell and value in use. Fair value is determined as the amount that would be obtained from the sale of the asset in an arm's length transaction between knowledgeable and willing parties. In order to determine fair value, the Company considers multiple valuation approaches, including the income, market and cost approaches. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. If the recoverable amount of an asset is estimated to be less than its carrying amount, the carrying amount of the asset is reduced to its recoverable amount and the impairment loss is recognized in the condensed consolidated interim statements of loss and comprehensive loss for the period.

Where an impairment loss subsequently reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognized for the asset in prior years. A reversal of an impairment loss is recognized immediately in the condensed consolidated interim statements of loss and comprehensive loss.



# Talon Metals Corp.

## Notes to the Condensed Consolidated Interim Financial Statements For the three and nine months ended September 30, 2017 and 2016 (Expressed in Canadian dollars)

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### Asset retirement obligations

A provision is recognized on the consolidated balance sheets when the Company has a present legal or constructive obligation as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability. The Company's asset retirement obligations arise from its obligations to undertake site reclamation and remediation in connection with its resource properties. The estimated costs of reclamation are based on current regulatory requirements and the estimated reclamation costs at the date of purchase. Future changes to those regulations and standards, as well as changes resulting from operations may result in actual reclamation costs differing from the estimate.

### Deferred taxes

The Company uses the asset and liability method of accounting for income taxes, under which deferred tax assets and liabilities are recognized for the estimated future income tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using income tax rates in effect for the period in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in income tax rates or laws is recognized as part of the provision for income taxes in the period the changes are considered substantively enacted.

Deferred tax benefits attributable to these differences, if any, are recognized to the extent that the realization of such benefits is probable.

### Financial assets and liabilities

Financial instruments are measured on initial recognition at fair value, plus, in the case of financial instruments other than those classified as "fair value through profit and loss", directly attributable transaction costs. Measurement of financial assets in subsequent periods depends on whether the financial instrument has been classified as "fair value through profit and loss", "available-for-sale", "held-to-maturity", or "loans and receivables" as defined by IAS 39, *Financial Instruments: Recognition and Measurement* ("IAS 39"). Measurement of financial liabilities subsequent to initial recognition depends on whether they are classified as fair value through profit and loss or "other financial liabilities".

Financial assets and financial liabilities at fair value through profit and loss include financial assets and financial liabilities that are held-for-trading or designated upon initial recognition as fair value through profit and loss. These financial instruments are measured at fair value with changes in fair values recognized in the condensed consolidated interim statements of loss and comprehensive loss. Financial assets classified as available-for-sale are measured at fair value, with changes in fair values recognized in other comprehensive income ("OCI"), except when there is objective evidence that the asset is impaired, at which point the cumulative loss that had been previously recognized in OCI is recognized in profit or loss. Financial assets classified as held-to-maturity and loans and receivables are measured subsequent to initial recognition at amortized cost using the effective interest method. Financial liabilities, other than financial liabilities classified as fair value through profit and loss, are measured in subsequent periods at amortized cost using the effective interest method.

The Company has classified its financial instruments as follows:

Cash and cash equivalents	-	Fair value through profit and loss
Restricted cash	-	Fair value through profit and loss
Accounts and other receivables	-	Loans and receivables
Accounts payable and accrued liabilities	-	Other liabilities
Contingencies	-	Other liabilities
Unsecured convertible loan	-	Fair value through profit and loss

# Talon Metals Corp.

## Notes to the Condensed Consolidated Interim Financial Statements For the three and nine months ended September 30, 2017 and 2016 (Expressed in Canadian dollars)

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Financial instruments recorded at fair value on the consolidated balance sheets are classified using a fair value hierarchy that reflects the significance of the inputs used in making the measurements. The fair value hierarchy has the following levels:

- Level 1 - valuation based on quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2 - valuation techniques based on inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and
- Level 3 - valuation techniques using inputs for the asset or liability that are not based on observable market data (unobservable inputs).

Cash and cash equivalents and restricted cash have been measured using Level 1 inputs. The convertible loan has been measured using both Level 1 and Level 3 inputs.

### Unsecured convertible loan

In December 2015, the Company issued an unsecured convertible loan (note 5) which was subsequently increased in January 2017. The Company has designated the unsecured convertible loan at fair value through profit and loss. The Company has used estimates in determining the fair value of the unsecured convertible loan. Inputs used in the models employed in the valuation of the convertible loan as a hybrid financial instrument require subjective assumptions, including the expected price volatility, the price of the Company's shares and credit yield-to-maturity of the Company. Changes in these assumptions and the selected valuation model can materially affect the fair value estimate. The valuation methods and the underlying assumptions used in the re-measurement of the unsecured convertible loan are disclosed in Note 5.

### Stock option compensation

The Company's shareholder-approved stock option plan allows employees, directors and consultants of the Company to acquire shares of the Company. The fair value of options granted is recognized as an employee or consultant expense with a corresponding increase in equity. An individual is classified as an employee when the individual is an employee for legal or tax purposes (direct employee) or provides services similar to those performed by a direct employee, and includes directors and most consultants of the Company. The fair value is measured at grant date and each tranche is recognized over the period during which the options vest. The fair value of the options granted is measured using the Black-Scholes option pricing model taking into account the terms and conditions upon which the options were granted.

### Loss per share

Basic loss per common share is calculated by dividing the loss attributed to shareholders for the period by the weighted average number of common shares outstanding in the period. Diluted loss per common share is calculated by adjusting the weighted average number of common shares outstanding to assume conversion of all dilutive potential common shares.

### Segment reporting

A segment is a component of the Company that is distinguishable by economic activity (business segment), or by its geographical location (geographical segment), which is subject to risks and rewards that are different from those of other segments. The Company operates in one business segment, namely, mineral exploration and geographically in the USA and Brazil. Substantially all working capital and investments are held at head office and substantially all equipment held at head office or Brazil. The segmentation of resource properties and deferred expenditures by mineral property, and hence country, are presented in

# Talon Metals Corp.

## Notes to the Condensed Consolidated Interim Financial Statements For the three and nine months ended September 30, 2017 and 2016 (Expressed in Canadian dollars)

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note 4.

### Changes in accounting policies

There were no material changes in accounting policies for the nine months ended September 30, 2017 compared to 2016.

### Future accounting policies

IFRS 9 Financial Instruments: This standard replaces the current IAS 39 Financial Instruments Recognition and Measurement. The standard introduces new requirements for classifying and measuring financial assets and liabilities. The effective date of IFRS 9 is January 1, 2018. The Company intends to adopt the standard on its effective date and has not yet evaluated the impact on the condensed consolidated interim financial statements.

### Reclassification

Certain amounts in the condensed consolidated interim financial statements from the prior year may have been reclassified to conform to the current year's presentation.

## 3. SIGNIFICANT ACCOUNTING JUDGMENTS AND ESTIMATES

The preparation of these condensed consolidated interim financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the condensed consolidated interim financial statements and reported amounts of expenses during the reporting period. Actual outcomes could differ from these estimates. The condensed consolidated interim financial statements include estimates which, by their nature, are uncertain. The impacts of such estimates are pervasive throughout the condensed consolidated interim financial statements, and may require accounting adjustments based on future occurrences. Revisions to accounting estimates are recognized in the period in which the estimate is revised and also in future periods when the revision affects both current and future periods.

Significant assumptions about the future and other sources of estimation uncertainty that management has made at the end of each reporting period and for the periods then ended, that could result in a material adjustment to the carrying amounts of assets and liabilities, in the event that actual results differ from assumptions made, relate to, but are not limited to, the valuation of resource properties and the valuation of the unsecured convertible loan.

The uncertainty in regards to the valuation of resource properties arises as a result of estimates and judgments such as forecasts of metal prices, operating costs, capital costs and income taxes among numerous other valuation inputs, discount rates, comparability of the Company's properties to those of other market participants and the selection of market-participant assumptions used to determine recoverable value.

The uncertainty in regards to the valuation of the unsecured convertible loan arises a result of certain key inputs such as expected volatility, the price of the Company's shares, the yield-to-maturity or discount rate on the loan portion and the selected valuation methodology.

# Talon Metals Corp.

## Notes to the Condensed Consolidated Interim Financial Statements For the three and nine months ended September 30, 2017 and 2016 (Expressed in Canadian dollars)

### 4. RESOURCE PROPERTIES AND DEFERRED EXPENDITURES

The properties on which the Company's subsidiaries carry out exploration activities or hold an interest in an exploration project are located in the USA (the Tamarack Project) and Brazil (the Trairão Project). Details of the change for the year ended December 31, 2016 and the period ended September 30, 2017, are as follows:

	December 31, 2015	Additions	Write- downs	December 31, 2016	Additions	Write- downs	September 30, 2017
Tamarack Project	\$ 15,226,360	21,825,717	-	37,052,077	1,326,112	-	38,378,189
Trairao Project	-	16,596	(16,596)	-	4,543	(4,543)	-
Total	\$ 15,226,360	21,842,313	(16,596)	37,052,077	1,330,655	(4,543)	38,378,189

Although the Company believes it has taken reasonable measures to ensure proper title to its mineral properties and those which it has an interest in, there is no guarantee that title to any of these mineral properties will not be challenged or impaired. Third parties may have valid claims underlying portions of the Company's interests, including prior unregistered liens, agreements, transfers or claims, including native land claims, and title may be affected by, among other things, undetected defects. In addition, the Company or Kennecott (in respect of the Tamarack Project) may be unable to operate their properties as permitted or to enforce their rights with respect to its properties. In order to help mitigate this risk, Talon purchased title insurance in July 2014 over certain lands that form part of the Tamarack North Project. Talon further expanded the area covered by the title insurance policy in October 2014. In regards to the Trairão Project, the material licenses have reached the end of their validity and the Company has submitted a final exploration report to the Departamento Nacional de Produção Mineral ("DNPM") in respect of these licenses. In 2013, the Company was granted a suspension of the DNPM's review and approval of the final exploration report (called 'sobrestamento') which lasted for a period of three years. Prior to the expiry of the three year period, the Company submitted another request for sobrestamento and the Company is awaiting a decision by the DNPM on such request.

#### (a) Tamarack Project

On June 25, 2014, Talon's wholly owned indirect subsidiary, Talon Nickel, entered into the Tamarack Earn-in Agreement with Kennecott, pursuant to which Talon Nickel received the right to acquire an interest in the Tamarack Project.

Pursuant to the original terms of the Tamarack Earn-in Agreement, Talon Nickel had the right to acquire a 30% interest in the Tamarack Project over a three year period by making US\$7.5 million in installment payments to Kennecott, and incurring US\$30 million in exploration expenditures (the "Tamarack Earn-in Conditions"). In addition, Talon Nickel had agreed to make certain land option payments on behalf of Kennecott, which were payable over the Earn-in Period (and, when payable, are included as part of the Tamarack Earn-in Conditions).

On March 26, 2015, Kennecott and Talon amended the Tamarack Earn-in Agreement to defer the second year option payment in the amount of \$2.5 million from June 25, 2015 to December 21, 2015 (the "Deferred Option Payment") and delay further cash calls from being made by Kennecott until October 1, 2015. The Deferred Option Payment was recognized as a liability on June 25, 2015 and subsequently extinguished on December 29, 2015 as part of the Debt Settlement Agreement (note 5). The extinguishment was applied against the resource properties and deferred expenditures balance, which was where the Deferred Option Payment had been previously capitalized.

On November 25, 2015, Kennecott and Talon Nickel entered into a further agreement to amend the Tamarack Earn-in Agreement, to provide, among other things:

## Talon Metals Corp.

### Notes to the Condensed Consolidated Interim Financial Statements For the three and nine months ended September 30, 2017 and 2016 (Expressed in Canadian dollars)

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- that upon receipt by Kennecott from Talon of US\$15 million (which is in addition to previous amounts paid to Kennecott of US\$10.52 million), Talon will earn an 18.45% interest in the Tamarack Project and Talon will have no further funding requirements to earn its interest in the Tamarack Project;
- once Kennecott has spent the funds advanced by Talon on exploration activities in respect of the Tamarack Project, subject to certain self-funding rights by Kennecott during the earn-in period, Kennecott will have 180 days to elect whether to: (a) proceed with a 81.55/18.45 joint venture on the Tamarack Project, with Kennecott owning an 81.55% participating interest, and Talon owning an 18.45% participating interest (the "Tamarack Joint Venture"); or (b) grant Talon the right to purchase Kennecott's interest in the Tamarack Project for a total purchase price of US\$114 million (the "Purchase Option"). In the event Kennecott grants Talon the Purchase Option, and Talon elects to proceed with the Purchase Option, Talon will have up to 18 months to close the transaction, provided it makes an upfront non-refundable payment of US\$14 million; and
- until Kennecott makes its decision as to whether to grant the Company the Tamarack Purchase Option, the Company is responsible for certain costs to keep the Tamarack Project in good standing based on its 18.45% interest. If the Company fails to make any of such payments, its interest in the Tamarack Project will be diluted in accordance with the Tamarack Earn-in Agreement.

On January 4, 2016, Talon Nickel made the US\$15 million payment to Kennecott to earn an 18.45% interest in the Tamarack Project. There are no further amounts required to be paid to earn the 18.45% interest

The total amount paid to Kennecott to earn the 18.45% interest was US\$25.52 million.

On December 16, 2016, Talon Nickel and Kennecott entered into a further agreement to amend the Tamarack Earn-in Agreement pursuant to which Talon Nickel and Kennecott agreed to co-fund a 2016/2017 winter exploration program at the Tamarack Project in the approximate amount of US\$3,500,000, with Talon Nickel funding its proportionate share of 18.45% thereof. In addition, Talon Nickel and Kennecott agreed that Kennecott may elect at any time up to and including September 25, 2017 to grant Talon Nickel the Purchase Option or proceed with the Tamarack Joint Venture in respect of the Tamarack Project. On the same date, Talon entered into an amendment to the RCF Loan (defined below) as explained in Note 5.

During Q1 2017, the Company paid approximately US\$604,349 to Kennecott pursuant to the Tamarack Earn-in Third Amending Agreement.

On September 25, 2017, Talon Nickel received notification from Kennecott that it had decided to grant Talon Nickel the Tamarack Purchase Option on the terms of the Tamarack Earn-in Agreement (as amended). Pursuant to the Tamarack Earn-in Agreement, Talon Nickel had until November 6, 2017 to advise Kennecott as to whether or not it would exercise the Tamarack Purchase Option. Effective November 1, 2017, Kennecott agreed to grant Talon Nickel an extension until December 31, 2017 to make its election as to whether it would exercise the Tamarack Purchase Option. In return for the granting of such extension by Kennecott, Talon Nickel agreed to grant Kennecott a 0.5% NSR in the event Talon Nickel exercises the Tamarack Purchase Option.

#### **(b) Trairão Project**

On September 29, 2010, Talon announced that it had acquired 100% of the rights to the Trairão Project and the Inajá South Project in Pará State, Brazil, through concluding two separate agreements with Codelco do Brasil Mineração Ltda. ("Codelco") and Barrick International (Barbados) Corp. ("Barrick Barbados").

Under the agreement with Codelco, Talon paid Codelco a nominal purchase price and will pay a royalty of US\$0.7005 per tonne of iron mined and sold.

Under the agreement with Barrick Barbados, Talon paid Barrick Barbados a nominal purchase price and is obliged to pay certain production related royalties, at varying levels in respect of specific metals. In the case

# Talon Metals Corp.

## Notes to the Condensed Consolidated Interim Financial Statements For the three and nine months ended September 30, 2017 and 2016 (Expressed in Canadian dollars)

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of the Trairão Project, the royalty payable is US\$0.2995 per tonne of iron mined and sold. However, Talon has the right to buy back this royalty for US\$599,000 during the 12 month period following the start of commercial production.

On December 31, 2015, the Company determined that the carrying value of the property would not be recoverable and wrote off the carrying value of the property in full. The determination was made taking into consideration the deterioration in projected future iron ore prices, the closing of a local off-taker, the poor and declining condition of roads with little prospect of improvement and current poor general market conditions. The fair value measurement falls within a Level 3 estimate under IFRS.

### 5. UNSECURED CONVERTIBLE LOAN (RCF Loan)

On November 25, 2015, the Company entered into definitive agreements with Resource Capital Fund VI L.P. ("RCF") whereby RCF agreed to provide US\$15 million to the Company (the "RCF Financing") to be used to earn an 18.45% interest in the Tamarack Project. After receipt by the Company of the US\$15 million, the entire amount was transferred to Kennecott on January 4, 2016.

The RCF Financing was subject to certain closing conditions, including, the receipt of shareholder approval. The Company held a special meeting of its shareholders on December 29, 2015 where shareholders approved, among other things, the RCF Financing. The material terms of the RCF Financing are as follows:

- RCF provided the Company with US\$15 million, as follows: (a) US\$1 million via a private placement subscription for 11,540,833 common shares in the capital of the Company at a subscription price of C\$0.12 per common share (the "RCF Private Placement"), and (b) US\$14 million via an unsecured convertible loan (the "Unsecured Convertible Loan" or "RCF Loan", and the agreement governing the RCF Loan, the "RCF Loan Agreement"). The RCF Loan matures on the maturity date (the "Maturity Date") being the earlier of: (i) November 25, 2018; and (ii) the date upon which RCF elects to accelerate the due date upon the occurrence of certain events, including an event of default.
- The RCF Loan bears interest at the rate of 12% per annum. All interest accrues and become payable on the Maturity Date. The Company may only prepay the RCF Loan (including accrued interest), in full or in part, with the prior approval of RCF.
- Under the terms of the RCF Loan, RCF may elect to convert all or part of the principal amount of the RCF Loan (including all capitalized interest) into common shares of the Company at any time at a conversion price of \$0.156 per common share (the "Conversion Price"), representing a 30% premium to the RCF Subscription Price. Interest that has not been capitalized is to be converted at a price equal to the volume weighted average trading price for the five trading days prior to the conversion. Any amount being converted pursuant to RCF's conversion right will be converted from United States dollars into Canadian dollars based on the currency exchange rate as reported by Bloomberg as of 5:00 p.m. (EST) on the first business day preceding the conversion date.
- For as long as the RCF Loan Agreement is in effect or while RCF and its affiliates, on a partially diluted basis, hold common shares of the Company equal to or exceeding 10% of all common shares issued and outstanding, RCF has the right to participate in any equity or debt financings of the Company (other than certain exempt issuances) at the same price and on the same terms, on a pro rata basis, such that RCF may maintain its percentage interest in common shares of the Company on a partially diluted basis, assuming the full exercise of all rights under the RCF Loan to receive common shares, including all rights of conversion.
- At all times, (a) while any obligation remains outstanding under the RCF Loan Agreement, or (b) RCF and its affiliates, on a partially diluted basis, hold common shares of the Company equal to or exceeding

## Talon Metals Corp.

### Notes to the Condensed Consolidated Interim Financial Statements For the three and nine months ended September 30, 2017 and 2016 (Expressed in Canadian dollars)

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10% of all common shares of the Company issued and outstanding, RCF will have the right to nominate one individual to serve on the Company's board of directors.

- A number of events constitute an event of default under the RCF Loan Agreement, including certain material adverse changes, the delisting of the Common Shares from the TSX, the abandonment or termination of a material portion of the Tamarack Project or a change of control of the Company. Upon an event of default, the principal and interest will become due and payable and interest will accrue at the default interest rate of 17% per annum.
- The Company must adhere, within five percent (5%), to an agreed overhead budget.
- Up to June 30, 2017, the Company was not permitted to issue common shares or other securities convertible into common shares of the Company for consideration less than the Conversion Price.

The Unsecured Convertible Loan is denominated in US dollars and convertible into common shares based on the principal and interest balance translated to Canadian dollars. Management determined that the Unsecured Convertible Loan represents a combined instrument that contains an embedded derivative, being the conversion option. As a result of the foreign exchange impact on the conversion factor, the conversion option does not meet the fixed for fixed criteria and therefore represents a derivative liability. In accordance with IAS 39, the Company has designated the entire Unsecured Convertible Loan at fair value through profit or loss. The Unsecured Convertible Loan was initially recorded at fair value and re-valued at period end with changes in fair value being recorded through profit and loss.

The total expenses associated with the RCF Financing totalled \$635,996 and were allocated as follows on December 29, 2015:

Common shares	\$	42,400
Unsecured convertible loan		593,596
	\$	<u>635,996</u>

#### Increase to RCF Loan

On December 16, 2016, the Company entered into an amending agreement (the "RCF Loan First Amending Agreement") with RCF to amend the RCF Loan Agreement. Pursuant to the terms of the RCF Loan First Amending Agreement, RCF agreed to increase the principal amount of the RCF Loan by US\$2,000,000 (from US\$14,000,000 to US\$16,000,000) to be provided, subject to certain closing conditions, including the receipt of shareholder approval, in a second advance on substantially the same terms as the RCF Loan.

Pursuant to the RCF Loan First Amending Agreement, as consideration for RCF's agreement to increase the amount of the RCF Loan, the Company agreed to issue to RCF 15,000,000 common share purchase warrants (the "RCF Warrants"), each RCF Warrant exercisable for one common share in the Company at an exercise price of C\$0.11 up to January 18, 2021.

The effectiveness of the RCF Loan First Amending Agreement and the issuance of the RCF Warrants were subject to the approval of the shareholders of the Company. On January 18, 2017, at a special meeting of shareholders, the shareholders of the Company approved the RCF Loan First Amending Agreement and the issuance of the RCF Warrants.

The total expenses associated with the increase to the RCF Loan totalled \$137,052 and were allocated as follows on January 18, 2017:

Increase to RCF Loan	\$	113,491
RCF Warrants		23,561
	\$	<u>137,052</u>

# Talon Metals Corp.

## Notes to the Condensed Consolidated Interim Financial Statements For the three and nine months ended September 30, 2017 and 2016 (Expressed in Canadian dollars)

### Fair value determination

The fair value of the Unsecured Convertible Loan, including the increase thereto, has been determined using a combination of the Black-Scholes option pricing model for the equity conversion portion and the discounted cash flow method for the loan portion. The following assumptions were used to determine the fair value of the Unsecured Convertible Loan at September 30, 2017 and December 31, 2016:

	<b>Sept 30, 2017</b>	<b>Dec 31, 2016</b>
Risk-free interest rate	1.78%	0.73%
Expected volatility	60%	60%
Talon share price	\$ 0.115	\$ 0.070
Expected dividend yield	0%	0%
Effective interest rate on bifurcated loan portion	24.01%	24.01%
Actual interest rate	12.00%	12.00%
Period end foreign CAD/USD foreign exchange rate	1.2480	1.3427

Sensitivity analysis: As at September 30, 2017, the value of the Unsecured Convertible Loan, including the increase thereto, assuming different share prices (given share price is the most critical input variable) as at the end of the current reporting period is as follows:

Valuation date share price	<b>\$ 0.100</b>	<b>\$ 0.115</b>	<b>\$ 0.130</b>	<b>\$ 0.156</b>
Fair value of Unsecured Convertible Loan				
In US dollars millions	\$ 18.83	19.59	20.51	22.40
In Canadian dollars millions	\$ 23.49	24.45	25.60	27.96

A continuity schedule reconciling the change in fair value of the Unsecured Convertible Loan follows:

	<b>Nine months ended September 30, 2017</b>		<b>Year ended December 31, 2016</b>	
	<b>USD</b>	<b>CAD</b>	<b>USD</b>	<b>CAD</b>
Fair value - beginning of year	\$ 13,868,065	\$ 18,620,651	\$ 14,008,646	\$ 19,387,966
Increase in principal	2,000,000	2,619,800	-	-
Less: Allocation to RCF Warrants	(343,831)	(450,385)	-	-
Expenses allocated to loan portion	(86,641)	(113,491)	-	-
Interest expense	1,634,808	2,136,294	1,758,295	2,417,380
Fair value adjustment	2,520,349	1,638,882	(1,898,876)	(3,184,695)
Increase (decrease)	5,724,685	5,831,101	(140,581)	(767,315)
Fair value - end of year	<b>\$ 19,592,750</b>	<b>\$ 24,451,752</b>	<b>\$ 13,868,065</b>	<b>\$ 18,620,651</b>

As at September 30, 2017, the principal plus accrued interest of the Unsecured Convertible Loan was US\$19.40 million or \$24.21 million (December 31, 2016 - US\$15.77 million or \$21.17 million).



# Talon Metals Corp.

## Notes to the Condensed Consolidated Interim Financial Statements For the three and nine months ended September 30, 2017 and 2016 (Expressed in Canadian dollars)

### 6. SHARE CAPITAL AND OTHER EQUITY

#### (a) Authorized, issued and outstanding common shares

Authorized – 100,000,000,000 common shares, no par value.

Issued and outstanding – 129,645,201 at December 31, 2016 and September 30, 2017.

During 2016, the Company issued 835,264 shares valued at \$74,506 to settle legal expenses incurred by RCF in connection with the RCF Financing (Note 5).

#### (b) Warrants

Warrant transactions for the period ended September 30, 2017 and the year ended December 31, 2016 are as follows:

	Nine months ended September 30, 2017			Year ended December 31, 2016		
	Number of warrants	Exercise price	Fair value	Number of warrants	Exercise price	Fair value
Outstanding – beginning of the year	10,794,391	\$ 0.42	\$ 539,793	11,513,052	\$ 0.42	\$ 602,100
Issued	15,000,000	0.11	426,823	166,666	0.13	2,383
Expired	(1,000,000)	0.30	(24,095)	-	-	-
Expired	(250,000)	0.37	(33,552)	-	-	-
Expired	(1,000,000)	0.65	(5,448)	(885,327)	0.32	(64,690)
Outstanding – end of the period or year	23,544,391	\$ 0.22	\$ 903,521	10,794,391	\$ 0.42	\$ 539,793

In 2016, in connection with the termination of an employee, the Company issued 166,666 warrants at an exercise price of \$0.13, which vested immediately and expire on April 30, 2018. The fair value was determined using the Black-Scholes model using the following estimates: risk-free interest rate – 0.62%, expected life – 1.93 years, expected volatility – 60% and dividend yield – 0%.

In 2017, in connection with the increase to the RCF Loan, the Company issued 15,000,000 warrants to RCF at an exercise price of C\$0.11, which vested immediately and expire on January 18, 2021. The fair value was determined using the Black-Scholes model using the following estimates: risk-free interest rate – 0.96%, expected life – 4 years, expected volatility – 60% and dividend yield – 0%. The fair value determined for these warrants was \$450,385, however expenses relating to the increase to the RCF Loan of \$23,561 were allocated to the warrants, for a net increase in the warrant balance of \$426,823.

As at September 30, 2017 and December 31, 2016, warrants outstanding were as follows:

September 30, 2017			December 31, 2016		
Number of warrants	Exercise price	Expiration date	Number of warrants	Exercise price	Expiration date
-	\$ -		250,000	\$ 0.37	August 21, 2017
7,377,725	0.45	November 6, 2017	7,377,725	0.45	November 6, 2017
1,000,000	0.156	November 25, 2018	1,000,000	0.30	April 1, 2017
166,666	0.13	April 30, 2018	1,000,000	0.65	April 1, 2017
15,000,000	0.11	January 18, 2021	1,000,000	0.156	November 25, 2018
-	-		166,666	0.13	April 30, 2018
23,544,391	\$ 0.22		10,794,391	\$ 0.42	

# Talon Metals Corp.

## Notes to the Condensed Consolidated Interim Financial Statements For the three and nine months ended September 30, 2017 and 2016 (Expressed in Canadian dollars)

### 7. STOCK OPTION COMPENSATION – EMPLOYEE SHARE OPTION PLAN

The Company has adopted a stock option plan (the "Plan") for its directors, officers, employees and consultants to acquire common shares of the Company. The exercise price of each option is determined by the board of directors of Talon but, in any event, is not lower than the closing market price on the TSX on the trading day immediately preceding the date the option is granted. The terms and conditions of the options are determined by the board of directors of the Company pursuant to the rules of the Plan. All options are granted for a term not exceeding ten years from the grant date. The total number of options that can be granted is limited to 12.5% of the issued and outstanding share capital of the Company.

A summary of the change in options outstanding during the period ended September 30, 2017 and the year ended December 31, 2016 is as follows:

	Nine months ended September 30, 2017		Year ended December 31, 2016	
	Number of stock options	Exercise price	Number of stock options	Exercise price
Outstanding – beginning of the year	11,319,350	\$ 0.17	12,179,350	\$ 0.33
Granted	-	-	300,000	0.156
Expired	-	-	(255,000)	1.58
Expired	-	-	(20,000)	2.12
Expired	-	-	(825,000)	1.95
Cancelled	-	-	(45,000)	0.20
Cancelled	-	-	(15,000)	1.95
Outstanding – end of the period	11,319,350	\$ 0.17	11,319,350	\$ 0.17

2,233,733 of the 11,319,350 options outstanding have been issued outside of the Plan. No options were exercised during the period ended September 30, 2017 and the year ended December 31, 2016.

As at September 30, 2017, the Company had the following stock options outstanding:

Date of grant	Number of options	Exercise price	Exercisable	Exercise price	Expiry date
January 31, 2012	1,966,267	0.156	1,966,267	0.156	November 25, 2020
January 31, 2012	833,733	0.156	833,733	0.156	November 25, 2020
April 4, 2012	1,033,940	0.156	1,033,940	0.156	November 25, 2020
April 25, 2012	376,060	0.156	376,060	0.156	November 25, 2020
June 15, 2012	400,000	0.156	400,000	0.156	November 25, 2020
February 20, 2013	200,000	0.30	200,000	0.30	February 20, 2018
February 20, 2013	100,000	0.156	100,000	0.156	November 25, 2020
February 28, 2013	100,000	0.156	100,000	0.156	November 25, 2020
March 20, 2013	1,000,000	0.30	-	0.30	March 20, 2018
August 1, 2013	350,000	0.156	350,000	0.156	November 24, 2020
October 1, 2013	500,000	0.156	500,000	0.156	November 25, 2020
May 28, 2014	300,000	0.156	300,000	0.156	November 25, 2020
July 2, 2014	1,795,000	0.156	1,795,000	0.156	November 25, 2020
May 28, 2015	64,350	0.20	64,350	0.20	May 28, 2020
May 28, 2015	2,000,000	0.156	2,000,000	0.156	November 25, 2020
April 12, 2016	300,000	0.156	300,000	0.156	April 12, 2021
Total / weighted average	11,319,350	\$ 0.172	10,319,350	\$ 0.159	

# Talon Metals Corp.

## Notes to the Condensed Consolidated Interim Financial Statements For the three and nine months ended September 30, 2017 and 2016 (Expressed in Canadian dollars)

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A stock option compensation expense of nil for the nine months ended September 30, 2017 (2016 – \$43,596) was recognized in the condensed consolidated interim statements of loss and comprehensive loss.

### Options Granted in 2016

In April 2016, 300,000 options were issued to a director of the Company with a contractual life of 5 years, an exercise price of \$0.156 and vesting on the date of grant.

The fair value of the options granted was determined using the Black-Scholes option pricing model, using the following range of assumptions:

	<u>2017</u>	<u>2016</u>
Risk-free interest rate	N/A	0.72%
Expected life	N/A	5 years
Expected volatility	N/A	60%
Expected dividend yield	N/A	Nil

## 8. NET INCOME OR LOSS PER SHARE

### (a) Basic

Basic net income or net loss per share has been calculated using the weighted average number of common shares outstanding during the period.

### (b) Diluted

Diluted net income per share is equal to basic net income per share because there are no in-the-money options, warrants or other convertible securities that could dilute earnings. Diluted net loss per share has not been presented as it is anti-dilutive.

## 9. FINANCIAL INSTRUMENTS

The Company's financial instruments include cash and cash equivalents, accounts and other receivables, accounts payable, accrued liabilities and the Unsecured Convertible Loan.

The Company has classified its financial assets and liabilities carried at fair value through profit and loss into the following levels (as discussed in Note 2) as follows:

	<u>Sept 30, 2017</u>	<u>Dec 31, 2016</u>
Level 1		
Cash and cash equivalents	\$ 1,255,772	\$ 676,542
Level 3		
Unsecured Convertible Loan	\$ 24,451,752	\$ 18,620,651

## 10. FINANCIAL RISK MANAGEMENT

### (a) Credit risk management

Certain of the Company's financial assets are exposed to a degree of credit risk. The Company endeavors to mitigate credit risk by holding its cash and cash equivalents as cash deposits, short-term government treasury bills, money market funds and guaranteed investment certificates ("GICs") with major commercial banks.

# Talon Metals Corp.

## Notes to the Condensed Consolidated Interim Financial Statements For the three and nine months ended September 30, 2017 and 2016 (Expressed in Canadian dollars)

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Credit risk relating to accounts receivable arises from the possibility that any counterparty to an instrument fails to perform. The Company does not feel there is significant counterparty risk that could have an impact on the fair value of cash and cash equivalents and receivables.

### **(b) Liquidity risk**

The Company has in place a planning and budgeting process to help determine the funds required to support the Company's normal operating requirements on an ongoing basis and its capital, development and exploration expenditures.

On January 18, 2017, at a special meeting of shareholders, the shareholders of the Company approved the RCF Loan First Amending Agreement and the Company received US\$2 million as an increase to the principal amount of the RCF Loan.

As of September 30, 2017, the Company had a cash and cash equivalents balance of \$1.3 million, (December 31, 2016 – \$0.7 million) to settle current liabilities of \$0.4 million (December 31, 2016 - \$0.5 million).

In order to meet future working capital requirements, the Company may need to sell non-core assets, cut costs and/or raise additional capital (as permitted pursuant to the RCF Loan Agreement). There can be no assurance that the Company will be successful in selling non-core assets, cutting sufficient costs and/or, in compliance with the RCF Loan Agreement (note 5), raising financing to meet the Company's future working capital requirements.

### **(c) Market risk**

Market risk is the risk that changes in market prices including foreign exchange rates and interest rates will affect the Company's income or the value of its financial instruments. The Company records its investments using the closing price at the end of the reporting period. As at September 30, 2017 and December 31, 2016, the Company held no investments other than cash and cash equivalents which management considers to not be materially susceptible to market risks.

### **(d) Foreign exchange risk**

The Company is exposed to movements in the United States dollar and, to a lesser extent, the Brazilian real. Payments made to Kennecott pursuant to the Tamarack Earn-in Conditions were made in United States dollars and any future payments pursuant to the Tamarack Earn-in Agreement (as amended) and the Purchase Option or Tamarack Joint Venture will be in United States dollars. Transfers made to the Brazilian subsidiaries of the Company are made in United States or Canadian dollars and subsequently converted in Brazil to Brazilian reals. In addition, the Unsecured Convertible Loan is denominated in United States dollars.

Talon is exposed to movements in the United States dollar as a result of the Unsecured Convertible Loan, which at September 30, 2017 had a fair value of \$24.5 million.

At September 30, 2017, the Company had net monetary liabilities in foreign currencies, as follows (Canadian dollar equivalent):

United States dollars	\$(23.54 million)
Brazilian real	\$ (0.23 million)

If foreign exchange rates had changed by 5% on the last day of the period with all other facts/assumptions held constant, there would be a change in the net loss of the Company for the period ended September 30, 2017 of approximately \$1.2 million.

# Talon Metals Corp.

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### (e) Interest rate risk

Interest rate risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The Company is exposed to interest rate risk in regards to its interest income on Treasury Bills and other short-term notes contained within money market funds.

The risk of investing cash equivalents into fixed interest rate investments is mitigated by the short terms in which these investments mature. The investments are typically short-term investments with a term of less than ninety days.

As of September 30, 2017, the Company had interest bearing debt of \$24.4 million (December 31, 2016 – \$18.6 million) pursuant to the Unsecured Convertible Loan. Interest rate risk on the Company's debt is mitigated by the fixed interest rate of 12% and relatively short term to maturity of approximately 1.2 years (December 31, 2016 – 1.9 years) of the loan.

## 11. CAPITAL RISK MANAGEMENT

Capital is comprised of equity which at September 30, 2017 was \$16.2 million (December 31, 2016 – \$18.7 million). The Company manages its capital structure and attempts to make adjustments to it, in order to have the funds available to support its exploration, development and/or operating activities.

The Company's objective when managing capital is to safeguard its ability to continue as a going concern in order to pursue the exploration of its mineral properties and maximize shareholders' returns. The Company satisfies its capital requirements through careful management of its cash resources and by utilizing short-term loans or equity issues, as necessary, based on the prevalent economic conditions of both the industry and the capital markets and the underlying risk characteristics of the related assets. As at September 30, 2017 and December 31, 2016, the Company had the Unsecured Convertible Loan (note 5).

In accordance with the RCF Loan Agreement, up to June 30, 2017, the Company could not issue common shares or other securities convertible into common shares of the Company for consideration less than the Conversion Price. During 2016 and 2015, the Company was compliant with this requirement. In January 2017, pursuant to the RCF Loan First Amending Agreement, the Company issued the RCF Warrants at a price below the Conversion Price.

Management reviews its capital management approach on an ongoing basis. There were no changes in the Company's approach to capital management during the period ended September 30, 2017 and the year ended December 31, 2016. The Company is not subject to externally imposed capital requirements.

For further discussion related to Capital Risk Management, see note 10(b) "Liquidity Risk".

## 12. RELATED PARTY TRANSACTIONS AND BALANCES

Related parties include directors and officers of the Company, close family members and enterprises which are controlled by these individuals as well as certain persons performing similar functions.

The Company previously entered into a services agreement with a company owned by a director of Talon (Luis Azevedo) (the "Brazil Agreement") pursuant to which the company provides Talon with certain accounting, legal and general administrative functions in Brazil for a monthly service fee of US\$5,000. The Brazil Agreement was terminated on December 31, 2015. For 2016, Talon renegotiated for an expanded bundle of services to be provided by the company owned by Mr. Azevedo in exchange for a reduced fee of \$40,000 for the entire year (the "2016 Brazil Agreement"). For 2017, fees for the bundle of services were set at \$43,000 for the entire year (the "2017 Brazil Agreement").

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Under the 2016 Brazil Agreement, \$40,000 was paid in 2016 and under the 2017 Brazil Agreement, \$43,000 was paid in 2017.

Accounts payable and accrued liabilities at September 30, 2017 include \$3,152 payable to a company controlled by a director of the Company (Luis Azevedo) for services rendered in connection with a royalty previously held by the Company (December 31, 2016 - \$5,145 payable to a company controlled by a director of the Company (Luis Azevedo) to refund him for the payment of such amount on the Company's behalf).

The remuneration of directors and officers of the Company for the three and nine months ended September 30, 2017 and 2016 was as follows:

	Three months ended Sept 30,		Nine months ended Sept 30,	
	2017	2016	2017	2016
Cash compensation	\$ 164,250	\$ 225,917	\$ 501,333	\$ 743,000
Stock option compensation	-	-	-	43,194
Aggregate compensation	\$ 164,250	\$ 225,917	\$ 501,333	\$ 786,194

Cash compensation is recorded on the condensed consolidated interim statements of loss and comprehensive loss in "Salaries, benefits, consulting and Brazil administration" and on the condensed consolidated interim balance sheets in "Resource properties and deferred expenditures". The amount of cash compensation that was capitalized to Resource properties and deferred expenditures for the nine months ended September 30, 2017 was \$338,950 (2016 - \$386,910) and for the three months ended September 30, 2017 was \$97,400 (2016 - \$124,930).

In April 2016, 300,000 options were issued to a director of the Company with a contractual life of 5 years, an exercise price of \$0.156 and vesting on the date of grant.

### 13. CONTINGENCIES

In the normal course of business, the Company may be involved in legal proceedings, claims and assessments. Such matters are subject to many uncertainties, and outcomes are not predictable with assurance. Legal fees for such matters are expensed as incurred and the Company accrues for adverse outcomes as they become probable and estimable.

The Company has been named a defendant in three legal actions in Brazil, including two labour lawsuits involving two former employees (the Company has appealed one of the rulings) and a lawsuit related to the termination of a mineral assignment agreement. Legal counsel is of the opinion that some amount of loss is probable and thus a liability of \$254,937 (December 31, 2016 - \$266,841) has been recognized. The change from December 31, 2016 to September 30, 2017 was the result of foreign currency translation from Brazilian real to Canadian dollars.

### 14. INCOME TAXES

Deferred tax assets have not been recognized in respect of deductible temporary differences of \$18,800,000 (December 31, 2016 - \$19,500,000) which arises from non-capital losses and may be used to offset up to 30% of the Company's taxable income in Brazil in each future tax period. The non-capital losses of \$18,800,000 (December 31, 2016 - \$19,500,000) may be carried forward indefinitely.

### 15. GEOGRAPHIC INFORMATION

Interest income is earned in Canadian dollars. The Company's equipment and mineral properties are

## **Talon Metals Corp.**

### **Notes to the Condensed Consolidated Interim Financial Statements For the three and nine months ended September 30, 2017 and 2016 (Expressed in Canadian dollars)**

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located in Canada, the USA and Brazil.

#### **16. SUBSEQUENT EVENT**

On September 25, 2017, Talon Nickel received notification from Kennecott that it had decided to grant Talon Nickel the Tamarack Purchase Option on the terms of the Tamarack Earn-in Agreement (as amended). Pursuant to the Tamarack Earn-in Agreement, Talon Nickel had until November 6, 2017 to advise Kennecott as to whether or not it would exercise the Tamarack Purchase Option. Effective November 1, 2017, Kennecott agreed to grant Talon Nickel an extension until December 31, 2017 to make its election as to whether it would exercise the Tamarack Purchase Option. In return for the granting of such extension by Kennecott, Talon Nickel agreed to grant Kennecott a 0.5% NSR in the event Talon Nickel exercises the Tamarack Purchase Option.