

**KATANGA MINING LIMITED**

**CONSOLIDATED FINANCIAL STATEMENTS**  
**FOR THE YEARS ENDED DECEMBER 31, 2010 and 2009**

# KATANGA MINING LIMITED

## CONSOLIDATED FINANCIAL STATEMENTS FOR THE YEARS ENDED DECEMBER 31, 2010 and 2009

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## **KATANGA MINING LIMITED**

### **Management's Responsibility for Financial Reporting**

The accompanying consolidated financial statements of Katanga Mining Limited were prepared by management in accordance with Canadian generally accepted accounting principles. Management acknowledges responsibility for the preparation and presentation of the consolidated financial statements, including responsibility for significant accounting judgments and estimates and the choice of accounting principles and methods that are appropriate to the Company's circumstances. The significant accounting policies of the Company are summarized in note 2 to the consolidated financial statements.

Management has established a system of internal control over the financial reporting process, which is designed to provide reasonable assurance that relevant and reliable information is produced.

The Board of Directors is responsible for reviewing and approving the consolidated financial statements, the accompanying Management's Discussion and Analysis and for ensuring that management fulfills its financial reporting responsibilities. An Audit Committee which is comprised of a majority of independent non-executive directors assists the Board of Directors in fulfilling this responsibility. The Audit Committee meets with management as well as with the independent auditors to review the internal controls over the financial reporting process, the consolidated financial statements and the auditors' report. The Audit Committee reports its findings to the Board of Directors for its consideration in approving the consolidated financial statements for issuance to the shareholders.

Management recognizes its responsibility for conducting the Company's affairs in compliance with established financial standards, and applicable laws and regulations, and for maintaining proper standards of conduct for its activities.

Signed by

John Ross  
Chief Executive Officer

Nick Brodie  
Chief Financial Officer

February 10, 2011

# Independent Auditors' Report

## To the Shareholders of Katanga Mining Limited

We have audited the accompanying consolidated financial statements of Katanga Mining Limited and its subsidiaries, which comprise the consolidated balance sheet as at December 31, 2010, consolidated statements of income (loss) and comprehensive income (loss), changes in shareholders' equity, and cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

### *Management's responsibility for the consolidated financial statements*

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

### *Auditor's responsibility*

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

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

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

### *Opinion*

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Katanga Mining Limited and its subsidiaries as at December 31, 2010, and their financial performance and cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

### *Other Matters*

The financial statements of Katanga Mining Limited for the year ended December 31, 2009, were audited by another auditor who expressed an unmodified opinion on those statements on February 5, 2010.

*Signed by Deloitte & Touche LLP*

Chartered Accountants  
Licensed Public Accountants  
Toronto, Canada

February 10, 2011

# KATANGA MINING LIMITED

## CONSOLIDATED STATEMENTS OF INCOME (LOSS) AND COMPREHENSIVE INCOME (LOSS)

(Expressed in thousands of U.S. dollars, except per share amounts)

<b>For the years ended December 31,</b>	<b>Note</b>	<b>2010</b>	<b>2009</b>
		<b>\$</b>	<b>\$</b>
Sales revenue	14	535,946	285,549
Cost of sales		(290,297)	(245,590)
Royalties and transportation costs		(75,473)	(46,849)
Depreciation and amortization		(59,477)	(28,101)
		<b>110,699</b>	<b>(34,991)</b>
<b>Other income (expenses)</b>			
General and administrative		(8,159)	(16,740)
Restructuring income (expenses), net	15	14,374	(14,015)
Debenture interest		(18,782)	(17,214)
Interest income		244	1,670
Foreign exchange loss and other expenses	16	(9,406)	(23,726)
<b>Income (loss) before income taxes</b>		<b>88,970</b>	<b>(105,016)</b>
Recovery of (provision for) income taxes	19	176,006	(2,984)
<b>Net and comprehensive income (loss)</b>		<b>264,976</b>	<b>(108,000)</b>
Basic and diluted income (loss) per common share		<b>\$0.14</b>	<b>\$(0.09)</b>
Weighted average number of common shares outstanding		<b>1,907,380,413</b>	<b>1,156,333,506</b>

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

**KATANGA MINING LIMITED**  
**CONSOLIDATED BALANCE SHEETS**

(Expressed in thousands of U.S. dollars)

<b>As at December 31,</b>	<b>Note</b>	<b>2010</b> <b>\$</b>	<b>2009</b> <b>\$</b>
<b>ASSETS</b>			
<b>Current</b>			
Cash and cash equivalents		29,987	77,243
Restricted cash	5	11,658	11,455
Accounts receivable		100,291	58,379
Inventories	6	108,159	92,434
Prepaid expenses and other current assets		39,133	28,180
		<b>289,228</b>	<b>267,691</b>
<b>Non-current</b>			
Property, plant and equipment, net	7	1,636,430	1,481,904
Restricted cash	5	-	2,000
Other non-current assets		5,430	-
Future income tax assets	19	13,070	56
		<b>1,944,158</b>	<b>1,751,651</b>
<b>LIABILITIES</b>			
<b>Current</b>			
Accounts payable and accrued liabilities	8	167,285	122,204
Unearned revenue	14	48,906	14,600
		<b>216,191</b>	<b>136,804</b>
<b>Non-current</b>			
Debentures payable	9	120,358	112,929
Other long-term liabilities	10	54,172	56,291
Asset retirement obligations	12	10,653	4,964
Restricted stock units	13	68	47
Future income tax liabilities	19	-	163,630
		<b>401,442</b>	<b>474,665</b>
<b>SHAREHOLDERS' EQUITY</b>			
Capital stock	11	190,750	190,750
Warrants	11	5,809	5,809
Contributed surplus		2,540,777	2,540,023
Deficit		(1,194,620)	(1,459,596)
		<b>1,542,716</b>	<b>1,276,986</b>
		<b>1,944,158</b>	<b>1,751,651</b>

Guarantees - Note 5  
 Commitments and contingencies – Note 18

Signed by:  
 Hugh Stoyell (Non-executive Chairman)

Signed by:  
 Robert G. Wardell (Non-executive Director)

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

# KATANGA MINING LIMITED

## CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

(Expressed in thousands of U.S. dollars)

Years ended December 31, 2010 and 2009

	Number of shares	Capital stock \$	Warrants \$	Contributed surplus \$	Equity component of convertible debt \$	Deficit \$	Total \$
<b>Balance at January 1, 2009</b>	<b>206,320,802</b>	<b>20,644</b>	<b>5,809</b>	<b>2,174,787</b>	<b>2,716</b>	<b>(1,351,596)</b>	<b>852,360</b>
Options vested during the year	-	-	-	5,246	-	-	5,246
Performance awards vested during the year	-	-	-	61	-	-	61
Equity component of refinanced convertible debt	-	-	-	-	5,065	-	5,065
Shares issued on conversion of convertible debt	971,023,329	97,102	-	173,133	-	-	270,235
Reclassification of equity component of convertible debt	-	-	-	7,781	(7,781)	-	-
Shares issued in rights offering	718,036,282	71,804	-	173,432	-	-	245,236
Shares issued on acquisition of Kamoto Operating Limited	12,000,000	1,200	-	5,583	-	-	6,783
Net loss for the year	-	-	-	-	-	(108,000)	(108,000)
<b>Balance at December 31, 2009</b>	<b>1,907,380,413</b>	<b>190,750</b>	<b>5,809</b>	<b>2,540,023</b>	<b>-</b>	<b>(1,459,596)</b>	<b>1,276,986</b>
Options vested during the year	-	-	-	754	-	-	754
Net income for the year	-	-	-	-	-	264,976	264,976
<b>Balance at December 31, 2010</b>	<b>1,907,380,413</b>	<b>190,750</b>	<b>5,809</b>	<b>2,540,777</b>	<b>-</b>	<b>(1,194,620)</b>	<b>1,542,716</b>

The accompanying notes constitute an integral part of these consolidated financial statements

# KATANGA MINING LIMITED

## CONSOLIDATED STATEMENTS OF CASH FLOWS

(Expressed in thousands of U.S. dollars)

For the years ended December 31,	Note	2010 \$	2009 \$
<b>Cash flows from operating activities</b>			
Net income (loss) for the year		264,976	(108,000)
Add (deduct):			
Depreciation and amortization		59,477	28,101
Non-cash restructuring (income) expenses	15	(14,374)	1,411
Stock-based compensation		574	2,664
Debenture interest		1,960	1,834
Unrealized foreign exchange loss		5,889	16,931
Convertible debt accretion		-	6,197
Asset retirement obligation accretion		634	295
Loss on disposal of property, plant and equipment		1,326	-
Net derivative gain		-	(48)
Future income taxes		(176,644)	655
Changes in non-cash working capital:			
Increase in accounts receivable		(39,412)	(58,379)
Increase in prepaid expenses and other current assets		(18,313)	(651)
Increase in inventories		(11,194)	(25,171)
Increase (decrease) in accounts payable and accrued liabilities		57,420	(45,980)
Increase in unearned revenue		34,306	559
		<b>166,625</b>	<b>(179,582)</b>
<b>Cash flows from investing activities</b>			
Additions to property, plant and equipment		(218,486)	(118,084)
Proceeds from disposal of property, plant and equipment		3,312	-
Restricted cash		1,797	(2,830)
		<b>(213,377)</b>	<b>(120,914)</b>
<b>Cash flows from financing activities</b>			
Proceeds from convertible debt		-	100,000
Proceeds from rights offering, net of issue costs and repayment of bridge facility		-	245,226
		-	<b>345,226</b>
<b>(Decrease) increase in cash and cash equivalents</b>		<b>(46,752)</b>	<b>44,730</b>
Cash and cash equivalents, beginning of year		77,243	31,824
Effect of exchange rate changes on cash held in foreign currencies		(504)	689
<b>Cash and cash equivalents, end of year</b>		<b>29,987</b>	<b>77,243</b>
<b>Supplementary cash flow information</b>			
Interest paid		16,822	15,380
Income taxes paid		439	1,833
<b>Non-cash investing and financing activities</b>			
Additions to property, plant and equipment financed by long-term liabilities		2,451	56,291
Shares issued on conversion of convertible debt		-	270,235
<b>Cash and cash equivalents are comprised of the following:</b>			
Cash		29,987	61,219
Cash on short-term deposit (less than three months)		-	16,024

The accompanying notes constitute an integral part of these consolidated financial statements

# KATANGA MINING LIMITED

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in thousands of U.S. dollars, except per share amounts and as otherwise stated)

Years Ended December 31, 2010 and 2009

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### 1. DESCRIPTION OF BUSINESS

Katanga Mining Limited ("Katanga" or the "Company") is incorporated under the laws of Bermuda.

Katanga, through Kamoto Copper Company SARL ("KCC"), is engaged in copper and cobalt mining and related activities in the Democratic Republic of Congo ("DRC"). KCC is engaged in the exploration, mining, refurbishment, rehabilitation and operation of the Kamoto / Mashamba East mining complex, the KOV copper and cobalt mine, various oxide open pit resources, the Kamoto Concentrator and the Lulu Metallurgical Plant (collectively, the "Project"), in the DRC.

### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

#### Basis of presentation

The consolidated financial statements have been prepared by management of the Company in accordance with Canadian generally accepted accounting principles ("Canadian GAAP"). The consolidated financial statements consolidate the assets, liabilities and results of all entities in which the Company holds a controlling financial interest and accordingly include the Company's wholly-owned subsidiaries and its 75% interest in KCC. These consolidated financial statements reflect all normal and recurring adjustments which are, in the opinion of management, necessary for a fair presentation of the respective years presented. The effects of all transactions between controlled entities are eliminated.

#### Foreign Currency translation

The functional currency of the Company is the U.S. dollar. The Company's foreign operations are classified as integrated for foreign currency translation purposes. Monetary assets and liabilities denominated in foreign currencies are translated at the exchange rates in effect at the balance sheet date. Non-monetary items are translated at historical rates. Revenues and expenses are translated at the average exchange rate during the year with the exception of depreciation and amortization which is translated at the historical rate recorded for property, plant and equipment. Exchange gains and losses arising on the translation of monetary assets and liabilities are included in the statements of income (loss) and comprehensive income (loss) for the year.

#### Income (loss) per common share

Basic income (loss) per common share is computed by dividing the income (loss) for the year by the weighted average number of common shares outstanding during the year, including contingently issuable shares which are included when the conditions necessary for issuance have been met. Diluted income (loss) per share is calculated in a similar manner, except that the weighted average number of common shares outstanding is increased to include potentially issuable common shares from the assumed exercise of common share purchase options, warrants and on the conversion of debt, if dilutive. The number of additional shares included in the calculation is based on the treasury stock method for options, warrants and the conversion of debt.

Currently, the effect of potential issuances of shares under options, warrants and the conversion of debt would be anti-dilutive and accordingly basic and diluted income (loss) per common share are the same.

# KATANGA MINING LIMITED

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in thousands of U.S. dollars, except per share amounts and as otherwise stated)

Years Ended December 31, 2010 and 2009

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### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

#### Use of estimates

The preparation of the consolidated financial statements in conformity with Canadian GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements and reported amounts of revenue and expenses during the year.

Significant areas where management's judgment is applied include, but are not limited to:

- ... The carrying value of mineral properties and inventories and impairment charges related thereto
- ... Estimation of mineral prices, recoverable reserves and operating and capital costs
- ... Estimation of asset retirement obligations
- ... Estimation of future income taxes
- ... Fair value estimates for stock options, warrants and restricted stock units
- ... Estimation of the value of the work carried out on terminated contracts for the deferred SX/EW plant
- ... Estimated useful lives of depreciable assets

While management believes that its estimates and assumptions are reasonable, actual results could vary significantly from these estimates. In particular, although management has used its best estimates in the determination of the termination and settlement of construction services contracts for the SX/EW plant, actual liabilities will only be confirmed once they are settled. In 2010, the settlement process resulted in a net gain of approximately \$11,546 relative to the respective recorded accruals.

#### Revenue recognition

Revenues are recognized when title, risk and rewards pass to the customer, typically when goods have been delivered to a contractually agreed location. Sales agreements are generally recognized at a provisional price with final prices being determined at a specified future date based on market prices. Changes between the price recorded upon initial recognition of revenue and the final price due to fluctuations in commodity prices result in an embedded derivative. This embedded derivative is recorded at fair value, with changes in fair value recorded in revenue and accounts receivable (see Note 14).

Lease payments are payable to Gécamines, (2.5%) and royalties to the DRC treasury, (2%) based on net sales receipts. Net sales receipts are defined as gross revenues less permitted deductions (costs related to the transportation, sale, insurance and storage and all applicable taxes). Lease payments and royalties are included within royalties and transportation costs in the consolidated statement of income (loss) and comprehensive income (loss).

As at December 31, 2010, the Company recognized an unearned revenue balance of \$48,906 (December 31, 2009 - \$14,600) due to advance payments received on future sales and contractual obligations to invoice upon shipment of goods from the mine site. Sales revenue is not recognized until title and ownership has transferred. The unearned revenue balance is presented net of the cost of the related inventory shipped from the mine site.

# KATANGA MINING LIMITED

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in thousands of U.S. dollars, except per share amounts and as otherwise stated)

Years Ended December 31, 2010 and 2009

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### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

#### **Income taxes**

Income taxes are calculated using the asset and liability method of tax accounting. Under this method, current income taxes are recognized for the estimated income taxes payable for the current year. Future income tax assets and liabilities are determined based on differences between the financial reporting and tax bases of assets and liabilities and on unclaimed losses carried forward and are measured using the substantively enacted tax rates that will be in effect when the differences are expected to reverse or losses are expected to be utilized. Future income tax assets are recognized to the extent that the likelihood of recovering future income tax assets is considered more likely than not (see Note 19).

#### **Cash and cash equivalents**

Cash and cash equivalents include cash on hand, balances with banks and short-term deposits with original maturities of three months or less.

#### **Inventories**

Inventories include inventory of supplies, which consists of raw materials and consumables, and product inventories.

Inventory of supplies is valued at the lower of cost and net realizable value on a first-in first-out ("FIFO") basis. Cost includes all costs incurred in the normal course of business in bringing each supply to its present location and condition.

Product inventories include ore in stockpiles, work in progress and finished product (which comprises copper cathode, copper concentrate and cobalt metal). Product inventory is measured at the lower of cost and net realizable value. Cost is calculated as a weighted average cost, including materials, direct labor, other direct costs, production overheads and depreciation and amortization of property, plant and equipment directly involved in the mining and production processes.

#### **Property, plant and equipment**

Property, plant and equipment are recorded at cost less accumulated depreciation and amortization less any accumulated impairment write downs.

Depreciation and amortization are charged to the consolidated statements of income (loss) and comprehensive income (loss) over the estimated useful lives of the assets on a units-of-production or straight line basis as appropriate.

#### **Overburden removal costs**

The costs of removing overburden material to access mineral reserve deposits, referred to as "stripping costs", are accounted for as variable production costs to be included in the cost of inventory produced, unless the overburden removal activity can be shown to be a betterment of the mineral property, in which case these costs are capitalized. Betterment occurs when the overburden removal activity provides access to additional mineral deposit reserves that will be produced in future periods which would not have otherwise been accessible in the absence of the stripping activity. These deferred costs are included in mineral interests and are amortized using the units-of-production basis or straight-line method to cost of sales over the life of the mineral deposit reserves.

# KATANGA MINING LIMITED

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in thousands of U.S. dollars, except per share amounts and as otherwise stated)

Years Ended December 31, 2010 and 2009

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### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

#### Mineral interests

All direct costs relating to the mineral interests that meet the generally accepted criteria for deferral are capitalized as incurred. These criteria include having a clearly defined process with identifiable associated costs, establishment of technical feasibility, an intention to process and sell the recovered minerals to a clearly defined market, and adequate resources exist or are expected to be available to complete the project to commercial production.

Carrying values of mineral interests as reported on the consolidated balance sheet do not necessarily reflect the actual present or future value. Recovery of carrying values is dependent upon the future commercial success of operations.

Upon establishment of commercial production, carrying values of mineral interests are amortized over the estimated life of the mines, using the units-of-production method, based upon the current estimated recoverable reserves and resources.

#### Other property, plant, equipment and amortization

Other property, plant and equipment is depreciated using the following rates and methods:

Plant and equipment	3 – 7 years	Straight-line
Computer equipment	3 years	Straight-line
Computer software	1 – 3 years	Straight-line
Furniture and fixtures	3 – 10 years	Straight-line
Land and Buildings	10 years	Straight-line
Vehicles	2 – 7 years	Straight-line
Leasehold improvements	-	Over term of underlying lease

#### Impairment of long-lived assets

Property, plant and equipment and mineral properties are reviewed for possible impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. When events or changes in circumstances suggest possible impairment, estimated future net cash flows for a mine or development project are calculated using estimated future prices, mineral resources and operating and capital costs on an undiscounted basis. When estimated future undiscounted cash flows are less than the carrying value, the asset is considered impaired. Reductions in carrying value are recorded to the extent the carrying value exceeds the fair value of the assets.

The Company's estimates of mineral prices, recoverable reserves and operating and capital costs are subject to certain risks and uncertainties that may affect the recoverability of mineral property costs. Although the Company has made its best estimate of these factors, it is possible that changes could occur that could further affect management's estimate of the recoverable amount.

# KATANGA MINING LIMITED

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in thousands of U.S. dollars, except per share amounts and as otherwise stated)

Years Ended December 31, 2010 and 2009

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### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

#### Financial instruments

Management determines the classification of financial assets and financial liabilities at initial recognition and, except in very limited circumstances, the classification is not changed subsequent to initial recognition. The classification depends on the purpose for which the financial instruments were acquired or entered into, their characteristics and/or management's intent. Transaction costs with respect to instruments not classified as held-for-trading are recognized as an adjustment to the cost of the underlying instruments and amortized using the effective interest method.

Financial instruments are classified in the following categories:

#### Held-for-trading

Financial assets or financial liabilities acquired or incurred principally for the purpose of selling or repurchasing in the near future are classified as held-for-trading. Financial instruments included in this category are initially recognized at fair value and transaction costs are taken directly to the consolidated statements of income (loss) and comprehensive income (loss) along with gains and losses arising from changes in fair value. The Company's classification of held-for-trading financial instruments includes cash, cash equivalents and restricted cash.

#### Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments. Loans and receivables are initially recognized at fair value and are subsequently measured at amortized cost, using the effective interest method. Transaction costs with respect to instruments not classified as held-for-trading are recognized as an adjustment to the cost of the underlying instrument and amortized using the effective interest method. The Company's classification of loans and receivables includes accounts receivable.

#### Held-to-maturity

This category is for fixed maturity financial assets with fixed or determinable payments that the Company has the positive intention and ability to hold to maturity. Financial assets classified as held-to-maturity are measured at amortized cost.

#### Other liabilities

All of the other liabilities are initially recognized at fair value and are subsequently measured at amortized cost using the effective interest method. Interest expense on long-term debt (other than debenture interest which is separately disclosed) is recorded in foreign exchange loss and other expenses in the consolidated statements of income (loss) and comprehensive income (loss) unless it relates specifically to a development project and is capitalized to property, plant, and equipment. The Company's classification of other liabilities includes accounts payable and accrued liabilities, debentures payable and other long-term liabilities.

# KATANGA MINING LIMITED

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in thousands of U.S. dollars, except per share amounts and as otherwise stated)

Years Ended December 31, 2010 and 2009

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### 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

#### Financial instruments (continued)

##### Derivative instruments

Derivative instruments, including embedded derivatives, are recorded at fair value unless exempted from derivative treatment as normal purchase and sale. All changes in their fair value are recorded in the consolidated statements of income (loss) and comprehensive income (loss). The Company's derivative instruments include receivables from provisionally priced copper sales and restricted stock units.

All financial instruments are required to be measured at fair value on initial recognition, except for certain related party transactions. Fair value measurement for financial instruments and liquidity risk disclosures require a three-level hierarchy that reflects the significance of the inputs used in making the fair value measurements. Fair value of assets and liabilities included in Level 1 are determined by reference to quoted prices in active markets for identical assets and liabilities. Assets and liabilities in Level 2 include valuations using inputs other than the quoted prices for which all significant inputs are based on observable market data, either directly or indirectly. Level 3 valuations are based on inputs that are not based on observable market data. See Note 4 for additional disclosures regarding the hierarchy.

##### Asset retirement obligations

The fair value of liabilities for asset retirement obligations is recognized in the period in which they are incurred. The fair value is determined based on the estimated future cash flows required to settle the liability discounted at a credit adjusted discount rate. The liability is adjusted for changes in the expected amounts and timing of cash flows and accreted over time to its present value, (accretion charge is included in the consolidated statements of income (loss) and comprehensive income (loss) within cost of sales). The associated asset retirement costs are capitalized as part of the carrying amount of property, plant and equipment and amortized over the expected useful life of the asset.

##### Stock-based compensation

The Company recognizes the fair value of stock-based compensation over the vesting period of the options and restricted stock units. The fair value of the options granted is calculated using the Black-Scholes option pricing model that takes into account the exercise price, expected life of the option, expected volatility of the underlying shares, expected dividend yield, and the risk-free interest rate for the term of the option.

The fair value of the restricted stock units is based on the market value of the underlying stock at the date of grant and is revalued based on the market value at the balance sheet date.

##### Future changes in accounting policies

##### *International Financial Reporting Standards ("IFRS")*

In 2008, the Canadian Accounting Standards Board confirmed that publicly-listed companies will be required to adopt IFRS for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2011. The Company expects its first consolidated financial statements presented in accordance with IFRS to be for the three month period ending March 31, 2011, which includes presentation of its comparative results for fiscal 2010 under IFRS; as well as reconciliation to Canadian GAAP for the comparative quarter and as at the January 1, 2010 transaction date. Although IFRS uses a conceptual framework similar to Canadian GAAP, there are significant differences in recognition, measurement and disclosure.

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

# KATANGA MINING LIMITED

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in thousands of U.S. dollars, except per share amounts and as otherwise stated)

Years Ended December 31, 2010 and 2009

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### 3. CAPITAL DISCLOSURES

The Company includes as capital its common shares and has no externally imposed capital requirements. The Company's objective when managing capital is to safeguard its accumulated capital in order to provide an adequate return to shareholders by maintaining a sufficient level of funds to support continued production and development. There have been no changes in the Company's definition of capital or in its objectives when managing capital during the year ended December 31, 2010.

The Company manages its capital structure and makes adjustments to it, based on the level of funds available to the Company to manage its operations. In order to maintain or adjust the capital structure, the Company expects that it will be able to obtain long-term debt, equipment-based financing and/or project-based financing sufficient to maintain and expand its operations. There are no assurances that these initiatives will be successful. In order to achieve these objectives, the Company invests its unexpended cash in highly liquid, highly rated financial instruments. The Company is currently in compliance with all capital requirements including requirements relating to its long-term debt.

### 4. FINANCIAL RISK MANAGEMENT

The Company's risk exposures and their impact on the Company's consolidated financial position are summarized below:

#### Credit risk

The Company's credit risk is primarily attributable to short-term deposits and trade receivables from copper, cobalt and concentrate sales. The Company has a concentration of credit risk with all sales to two customers, which is closely monitored by management.

The majority of the Company's cash is on deposit with banks or money market participants with a Standard & Poors rating of A or greater in line with the Company's treasury policy. The Company does not own any asset-backed commercial paper.

#### Market risk

##### (a) Interest rate risk

The Company has cash balances and debenture notes. The debenture notes have a fixed interest rate of 14.0%. Thus, the Company is exposed to interest rate risk. The Company does not use derivative instruments to reduce its exposure to interest rate risk.

##### (b) Foreign currency risk

Foreign currency risk is the risk that a variation in exchange rates between the U.S. dollar and the Canadian dollar or other foreign currencies will affect the Companies operating and financial results. The Company does not use derivative instruments to reduce its exposure to foreign currency risk.

The Company's functional currency is the U.S. dollar. Sales are transacted in U.S. dollars and the majority of major purchases are transacted in U.S. dollars and South African rand. The Company maintains the majority of its cash and cash equivalents in U.S. dollars but it does hold balances in South African rand, British pounds, Canadian dollars, Swiss franc and Euros (for future expenditures which will be denominated in these currencies). It also maintains small balances in the local currency of the DRC, Congolese francs. If the U.S. dollar moved by plus or minus 1% relative to these currencies at December 31, 2010, the unrealized foreign exchange gain or loss would move by approximately \$66.

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

# KATANGA MINING LIMITED

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in thousands of U.S. dollars, except per share amounts and as otherwise stated)

Years Ended December 31, 2010 and 2009

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### 4. FINANCIAL RISK MANAGEMENT (continued)

The debentures payable are denominated in Canadian dollars and as such the Company is exposed to unrealized foreign exchange gains or losses which will be realized upon maturity of the debentures on November 20, 2013. A plus or minus 1% movement in the Canadian dollar exchange rate at December, 31 2010 would affect the consolidated statements of income (loss) and comprehensive income (loss) by approximately \$1,242.

#### Commodity risk

The Company sells copper, cobalt and concentrate at prevailing market prices. Under certain revenue contracts, final pricing adjustments are made after delivery to customers. The Company is therefore exposed to changes in commodity prices of copper and cobalt both in respect of future sales and previous sales which remain open to final pricing.

The Company has not used any commodity price derivatives in this or the prior years. There is currently no intention to hedge future copper and cobalt sales.

As at December 31, 2010, the Company had 980 tonnes of copper and 190 tonnes of cobalt sales for which final commodity prices had yet to be determined. These were valued at the end of the year at an average commodity price of \$9,665 per tonne for copper and \$38,665 per tonne for cobalt (amounts in whole numbers). A 1% plus or minus movement in the copper and cobalt price at December 31, 2010 would result in a \$167 change to revenue and trade receivables.

#### Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they become due. It is anticipated that the Company's existing cash balances, cash flows from future operations and existing credit facilities will be sufficient to fund the operations, Phase III and Phase IV capital and reclamation programs planned for the next twelve months (see note 18).

#### Mineral property risks

The Company's operations in the DRC are exposed to various levels of political risk and uncertainties, including political and economic instability, government regulations relating to exploration and mining, military repression and civil disorder, all or any of which may have a material adverse impact on the Company's activities or may result in impairment or loss of part or all of the Company's assets.

#### Financial instruments fair value

At December 31, 2010 and 2009, the Company's financial instruments consisted of cash and cash equivalents, restricted cash, accounts receivable, accounts payable and accrued liabilities, non-hedged embedded derivative financial instruments, debentures payable and other long-term liabilities. With respect to all of these financial instruments with the exception of the publicly-traded debentures, the Company estimates that the fair value of these financial instruments approximates the carrying values at December 31, 2010 and 2009, respectively. The publicly-traded debentures were trading at a premium to their carrying value, as at December 31, 2010 (fair value - \$128,551), and at a discount, as at December 31, 2009 (fair value - \$109,474).

# KATANGA MINING LIMITED

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in thousands of U.S. dollars, except per share amounts and as otherwise stated)

Years Ended December 31, 2010 and 2009

### 4. FINANCIAL RISK MANAGEMENT (continued)

The Company values instruments carried at fair value using quoted market prices, where available. Quoted market prices represent a Level 1 valuation. When quoted market prices are not available, the Company maximizes the use of observable inputs within valuation models. When all significant inputs are observable, the valuation is classified as Level 2. Valuations that require the significant use of unobservable inputs are considered Level 3.

The following table outlines financial assets and liabilities measured at fair value in the consolidated financial statements and the level of the inputs used to determine those fair values in the context of the hierarchy as defined above as at December 31, 2010 and 2009:

	Hierarchy level	December 31, 2010 \$	December 31, 2009 \$
Held for trading:			
Cash and cash equivalents	1	29,987	77,243
Restricted cash	1	11,658	13,455
		41,645	90,698
Loans and receivables			
Receivables from provisionally priced copper sales <sup>(1)</sup>	2	9,469	9,213
Other liabilities			
RSUs <sup>(2)</sup>	1	68	47

<sup>(1)</sup> Open provisionally priced copper sales which retain an exposure to future changes in commodity prices are marked-to-market based on London Metal Exchange ("LME") forward prices for copper offset by the contractual discount to the LME price. As such, these receivables are classified within Level 2 of the fair value hierarchy.

<sup>(2)</sup> Outstanding restricted stock units ("RSUs") are marked-to-market based on the Company's share price on the Toronto Stock Exchange at the reporting date. As such, these payables are classified within Level 1 of the fair value hierarchy.

# KATANGA MINING LIMITED

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in thousands of U.S. dollars, except per share amounts and as otherwise stated)

Years Ended December 31, 2010 and 2009

### 5. RESTRICTED CASH

	As at December 31, 2010 \$	As at December 31, 2009 \$
Guarantees <sup>(1)</sup>	3,000	5,000
Debenture interest <sup>(2)</sup>	8,658	8,455
<b>Total restricted cash</b>	<b>11,658</b>	<b>13,455</b>

<sup>(1)</sup> The Company has entered into a guarantee as required by a capital asset procurement contract. This guarantee matures on April 30, 2011.

<sup>(2)</sup> Semi-annual debenture interest held in trust before payment to debenture-holders after December 31, 2010 and 2009, respectively.

### 6. INVENTORIES

	As at December 31, 2010 \$	As at December 31, 2009 \$
Ore in stockpiles	30,349	24,260
Work in progress	7,670	6,359
Finished product	9,747	20,785
Product inventories	47,766	51,404
Consumables	60,393	41,030
<b>Total inventories</b>	<b>108,159</b>	<b>92,434</b>

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

# KATANGA MINING LIMITED

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in thousands of U.S. dollars, except per share amounts and as otherwise stated)

Years Ended December 31, 2010 and 2009

### 7. PROPERTY, PLANT AND EQUIPMENT, NET

	Cost \$	Accumulated amortization and depreciation \$	Carrying amount \$
<b>As at December 31, 2010</b>			
<b>Mineral interests <sup>(1)</sup></b>			
Capitalized development expenditures	131,303	-	131,303
Assets subject to amortization	1,114,330	27,788	1,086,542
<b>Total</b>	<b>1,245,633</b>	<b>27,788</b>	<b>1,217,845</b>
<b>Other property, plant and equipment</b>			
Plant and equipment	417,813	68,740	349,073
Computer equipment and software	8,195	4,798	3,397
Furniture and fixtures	2,790	2,110	680
Land and buildings	26,211	3,105	23,106
Vehicles	38,163	15,499	22,664
Closure and restoration costs	7,093	798	6,295
Leasehold improvements	10,274	2,786	7,488
Assets under construction	5,882	-	5,882
<b>Total</b>	<b>516,421</b>	<b>97,836</b>	<b>418,585</b>
<b>Total property, plant and equipment</b>	<b>1,762,054</b>	<b>125,624</b>	<b>1,636,430</b>
<b>As at December 31, 2009</b>			
<b>Mineral interests <sup>(1)</sup></b>			
Capitalized development expenditures	956,930	-	956,930
Assets subject to amortization	120,811	8,917	111,894
<b>Total</b>	<b>1,077,741</b>	<b>8,917</b>	<b>1,068,824</b>
<b>Other property, plant and equipment</b>			
Plant and equipment	361,158	29,310	331,848
Computer equipment and software	6,880	3,350	3,530
Furniture and fixtures	2,613	1,471	1,142
Land and buildings	24,136	1,425	22,711
Vehicles	37,565	13,000	24,565
Closure and restoration costs	2,039	81	1,958
Leasehold improvements	10,194	1,395	8,799
Assets under construction	18,527	-	18,527
<b>Total</b>	<b>463,112</b>	<b>50,032</b>	<b>413,080</b>
<b>Total property, plant and equipment</b>	<b>1,540,853</b>	<b>58,949</b>	<b>1,481,904</b>

<sup>(1)</sup> In July 2010, the KOV pit commenced commercial production and accordingly the costs related to the KOV pit were reclassified as assets subject to amortization.

# KATANGA MINING LIMITED

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in thousands of U.S. dollars, except per share amounts and as otherwise stated)

Years Ended December 31, 2010 and 2009

### 8. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

	As at December 31, 2010 \$	As at December 31, 2009 \$
Trade payables and accruals	138,479	81,274
Other accruals <sup>(1)</sup>	28,806	40,930
<b>Total accounts payable and accrued liabilities</b>	<b>167,285</b>	<b>122,204</b>

<sup>(1)</sup> During the year ended December 31, 2008, the Company indicated its intention to defer expansion plans relating to the development of a SX/EW plant. The Company recorded an accrual based on legal obligations incurred relating to work carried out on terminated contracts at the time of termination. The balances outstanding at December 31, 2010 and 2009 represent the respective remaining estimated amounts to be settled (see Note 15).

### 9. DEBENTURES PAYABLE

On November 20, 2006, the Company closed a debenture offering of 115,000 units ("Units") for an aggregate of Canadian \$115,000,000. Each Unit consists of a Canadian \$1,000 unsecured subordinated note ("Notes") and 40 common share purchase warrants ("Warrants"). Each Warrant entitles the holder to purchase 1.28 common shares of the Company anytime within five years from the closing date at Canadian \$8.50 per Warrant. The Notes bear interest at the rate of 14% per annum, payable semi-annually in arrears in equal instalments on January 1 and July 1 of each year. The Company may redeem the Notes, in whole or in part, at any time after November 20, 2009. The Notes mature on November 20, 2013.

The debentures payable balance is comprised of the following as at December 31, 2010 and 2009:

	Year ended	
	December 31, 2010 \$	December 31, 2009 \$
Debenture payable, beginning of the year	112,929	94,520
Changes during the year:		
Accretion	1,540	1,540
Foreign exchange translation loss <sup>(1)</sup>	5,889	16,869
<b>Debentures payable, end of the year</b>	<b>120,358</b>	<b>112,929</b>

<sup>(1)</sup> The foreign exchange translation loss is unrealized and represents the revaluation of the Canadian dollar denominated debentures to U.S. dollars. The foreign exchange translation amount will change in accordance with the relative movement of the Canadian dollar to the U.S. dollar. The foreign exchange translation gain or loss is expected to be realized upon maturity of the debentures on November 20, 2013.

During the year ended December 31, 2010, \$16,822 of interest was paid on the debentures (year ended December 31, 2009 - \$15,380).

# KATANGA MINING LIMITED

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in thousands of U.S. dollars, except per share amounts and as otherwise stated)

Years Ended December 31, 2010 and 2009

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### 10. OTHER LONG-TERM LIABILITIES

Pursuant to the terms of the new Joint Venture Agreement, a “pas de porte” (“entry premium”) obligation is payable to La Générale des Carrières et des Mines (“Gécamines”) for access to the Project. The total amount of \$140,000 is payable in instalments on an agreed upon schedule until 2016. Of the \$140,000, \$30,000 has already been paid and \$24,500 has been deducted from the payable representing Gécamines’ outstanding share capital contribution to KCC. The net present value of the outstanding payments has been recognized in these consolidated financial statements and capitalized to mineral interests. This amount is being amortized over the life of the mines using the units-of-production method. The expected cash flows are discounted at the Company’s estimated cost of capital of 14% per annum.

### 11. CAPITAL STOCK AND CONTRIBUTED SURPLUS

#### (a) AUTHORIZED

1,000 common shares, par value \$12.00 each  
5,000,000,000 common shares, par value \$0.10 each

On January 12, 2009, the authorized share capital of the Company was increased from 300,000,000 to 5,000,000,000 common shares with a par value of \$0.10 each.

#### (b) WARRANTS

The following table reflects the continuity of warrants during the year ended December 31, 2010:

Expiry date	Exercise price <sup>(1)</sup>	Outstanding December 31, 2009	Issued during the year	Exercised / expired during the year	Outstanding December 31, 2010
November 20, 2011	\$8.50	3,966,400	-	-	3,966,400

<sup>(1)</sup> Denominated in Canadian Dollars

# KATANGA MINING LIMITED

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in thousands of U.S. dollars, except per share amounts and as otherwise stated)

Years Ended December 31, 2010 and 2009

### 11. CAPITAL STOCK AND CONTRIBUTED SURPLUS (continued)

#### (c) STOCK OPTIONS

The Company maintains a stock option plan, pursuant to which securities of the Company may be issued as compensation. Eligible participants are those persons designated from time to time by the Compensation Committee of the Board of Directors (the Committee) from among the directors, executive officers and key employees of the Company or its subsidiaries who occupy responsible managerial or professional positions and who have the capacity to contribute to the success of the Company.

Options may be granted in respect of authorized but unissued shares, provided that the aggregate number of shares reserved for issuance under the option plan, together with all other security based compensation arrangements established or maintained by the Company, shall not exceed 10% of the issued and outstanding shares (190,737,941 shares). The remaining number of options which may be issued under the stock option plan is 179,674,029 as at December 31, 2010. Options are issued and vest on such terms as the Committee determines.

The following table reflects the continuity of stock options during the years presented:

	Number of stock options	Weighted Exercise Price per Share <sup>(1)</sup>
Outstanding at January 1, 2009	5,515,686	\$11.95
Forfeited during the year	(1,065,000)	\$10.92
Outstanding at December 31, 2009	4,450,686	\$12.20
Granted during the year	6,613,226	\$ 1.07
Outstanding at December 31, 2010	<b>11,063,912</b>	<b>\$ 5.55</b>

<sup>(1)</sup> Denominated in Canadian dollars.

# KATANGA MINING LIMITED

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in thousands of U.S. dollars, except per share amounts and as otherwise stated)

Years Ended December 31, 2010 and 2009

### 11. CAPITAL STOCK AND CONTRIBUTED SURPLUS (continued)

#### (c) STOCK OPTIONS (continued)

During the year ended December 31, 2010, 6,613,226 stock options were granted pursuant to the Company's stock option plan with an average exercise price of Canadian \$1.07 (year ended December 31, 2009, no options granted). The values assigned to these options were calculated using the Black-Scholes valuation model with the following assumptions: dividend yield 0%, risk free rate of return 0.78% and expected maturity of 3 years. The weighted average grant date fair value of each option was Canadian \$0.65 and the total fair value assigned was Canadian \$4,274. The options vest on August 10, 2013.

The following table summarizes the stock options outstanding at December 31, 2010:

Exercise Price per Share <sup>(1)</sup>	Expiry Date	Exercisable Options	Outstanding unvested Options <sup>(2)</sup>	Total
\$4.10	January 17, 2011	30,000	-	30,000
\$7.40	April 18, 2011	783,333	-	783,333
\$6.15	July 6, 2011	200,000	-	200,000
\$6.00	July 9, 2011	185,000	-	185,000
\$7.30	December 17, 2011	400,000	-	400,000
\$12.81	April 1, 2012	25,000	-	25,000
\$15.97	May 6, 2012	25,000	-	25,000
\$16.29	May 9, 2012	100,000	-	100,000
\$18.09	July 1, 2012	50,000	-	50,000
\$14.61	December 5, 2012	1,100,000	-	1,100,000
\$14.77	January 24, 2013	500,000	-	500,000
\$16.10	July 16, 2016	702,376	-	702,376
\$16.10	September 24, 2016	97,056	-	97,056
\$16.10	January 8, 2017	71,763	-	71,763
\$16.10	March 28, 2017	31,158	-	31,158
\$13.59	April 28, 2013	33,333	16,667	50,000
\$13.25	April 30, 2013	33,333	16,667	50,000
\$10.50	August 14, 2013	33,333	16,667	50,000
\$1.07	August 11, 2020	-	6,613,226	6,613,226
		<b>4,400,685</b>	<b>6,663,227</b>	<b>11,063,912</b>

<sup>(1)</sup> Denominated in Canadian dollars.

<sup>(2)</sup> The aggregate fair value of these unvested options not yet charged to operations is \$3,461.

The weighted average exercise price of the exercisable options is Canadian \$12.19 and the outstanding unvested options is Canadian \$1.16.

The Company recorded a compensation expense of \$530 for the year ended December 31, 2010 (\$2,645 for the year ended December 31, 2009) with respect to the vesting of options in the corresponding years.

#### (d) DILUTED EARNINGS PER SHARE

Total stock options of 11,063,912 (2009 – 4,985,686) and warrants of 3,966,400 (2009 – 3,966,400) were anti-dilutive and accordingly were excluded from the computation of diluted earnings per share because the exercise prices exceeded the average market value of the common shares for the year ended December 31, 2010, of Canadian \$1.04 (2009 – Canadian \$0.40) per share.

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

# KATANGA MINING LIMITED

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in thousands of U.S. dollars, except per share amounts and as otherwise stated)

Years Ended December 31, 2010 and 2009

### 12. ASSET RETIREMENT OBLIGATIONS (“AROs”)

AROs arise from the acquisition, development, construction and normal operation of mining property, plant and equipment due to government controls and regulations that protect the environment on the closure and reclamation of mining properties. The following table details the items that affect the AROs:

	As at December 31, 2010 \$	As at December 31, 2009 \$
Asset retirement obligations, beginning of the year	4,964	4,674
Accretion	634	417
Revision to estimate	5,055	(127)
<b>Asset retirement obligations, end of the year</b>	<b>10,653</b>	<b>4,964</b>

As at December 31, 2010, the Company reassessed its AROs due to the completion of a new Environmental Impact Study and Environmental Management Plan for the Project. This resulted in a \$5,055 increase in the ARO.

As at December 31, 2009, the Company reassessed its AROs due to the transfer of the KZC concentrator to Gécamines as agreed in the new Joint Venture Agreement. This resulted in a \$127 reduction in the ARO.

The Company has estimated that it will require approximately \$110,000 in cash flows to settle these obligations over the next 1 to 32 years. A credit adjusted discount rate of 14% was applied to expected future cash flows to determine the carrying value of the AROs.

### 13. RESTRICTED STOCK UNITS (“RSUs”)

The following table reflects the continuity of RSUs during the years presented:

	December 31, 2010		December 31, 2009	
	Number of RSUs	\$	Number of RSUs	\$
Restricted stock units, beginning of the year	70,531	47	324,634	66
Vested	(22,762)	(22)	(205,436)	(85)
Forfeited	-	-	(48,667)	(20)
Effect of changes in the Company's share price	-	40	-	39
Effect of changes in foreign exchange rates	-	3	-	47
<b>Restricted stock units, end of the year</b>	<b>47,769</b>	<b>68</b>	<b>70,531</b>	<b>47</b>

The Company recorded a compensation expense of \$44 for the year ended December 31, 2010 (\$19 for the year ended December 31, 2009) with respect to the vesting of RSUs in the corresponding years.

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

# KATANGA MINING LIMITED

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in thousands of U.S. dollars, except per share amounts and as otherwise stated)

Years Ended December 31, 2010 and 2009

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### 14. SALES REVENUE

	Year ended	
	December 31, 2010	December 31, 2009
	\$	\$
Copper	381,027	208,175
Cobalt	126,686	70,935
Copper concentrate	28,233	6,439
<b>Sales</b>	<b>535,946</b>	<b>285,549</b>

Copper, cobalt and concentrate sales are made under various sales agreements. Sales are made at a provisional price in the month of shipment with final pricing based on average copper and cobalt prices at a specified period as stated in the relevant sales agreement. At each reporting date, open provisionally priced copper sales which retain an exposure to future changes in commodity prices are marked-to-market based on London Metal Exchange ('LME') forward prices for copper offset by the contractual discount to the LME price, with adjustments being recorded in sales revenue in the consolidated statements of income (loss) and comprehensive income (loss) and accounts receivable on the consolidated balance sheet. The mark-to-market gain for the year ended December 31, 2010, was \$256 (December 31, 2009, \$9,213) with a corresponding increase in accounts receivable at December 31, 2010 and at December 31, 2009, respectively.

As at December 31, 2010, the Company recognized an unearned revenue balance of \$48,906 on copper and cobalt shipments (December 31, 2009 - \$14,600) due to advance payments received as a result of contractual rights to invoice upon shipment of goods from the mine site. Sales revenue is not recognized in the consolidated statements of income (loss) and comprehensive income (loss) until title and ownership has transferred. The unearned revenue balance is presented net of the cost of the related inventory shipped from the mine site.

# KATANGA MINING LIMITED

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in thousands of U.S. dollars, except per share amounts and as otherwise stated)

Years Ended December 31, 2010 and 2009

### 15. RESTRUCTURING INCOME (EXPENSES)

The following represent amounts recorded as part of the restructuring of the Company's operations, which the Company was required to complete in order to comply with the new Joint Venture Agreement in addition to the implementation of a new mine plan and the reduction of the Company's non-core overheads.

	Year ended	
	December 31, 2010	December 31, 2009
	\$	\$
Gain (loss) on return of assets to Gécamines <sup>(1)</sup>	2,828	(7,015)
Termination of Kamoto Operating Limited operating agreement <sup>(2)</sup>	-	(6,784)
Office closure costs <sup>(3)</sup>	-	(4,748)
Net gain on termination and settlement of construction services contracts for SX/EW plant <sup>(4)</sup>	11,546	9,114
Employee termination costs <sup>(5)</sup>	-	(4,582)
	<b>14,374</b>	<b>(14,015)</b>

(1) As part of the merger of the KCC and DRC Copper and Cobalt Project SARL ("DCP") joint ventures, the KZC concentrator at Kolwezi was returned to Gécamines resulting in an estimated loss of \$7,015 in the year ended December 31, 2009. The gain recognized in the year ended December 31, 2010 resulted from revisions to those estimates.

(2) As part of the merger of the KCC and DCP Joint Ventures, the operating agreement with Kamoto Operating Limited was terminated. The expenses related thereto were \$6,784.

(3) Office closure costs represent remaining lease costs and employee termination costs related to the closure of the UK corporate services office (the corporate services office has now relocated to Switzerland) and costs related to the relocation of the South African office.

(4) The net gain on settlement in the years ended December 31, 2010 and 2009 represents the gains, net of losses incurred on contracts settled in 2010 and 2009, relative to the respective recorded accruals.

(5) Employee termination costs represent costs incurred to terminate employees in the DRC as a result of the deferral of the SX/EW plant expansion and the closure of the UK office.

### 16. FOREIGN EXCHANGE LOSS AND OTHER EXPENSES

	Year ended	
	December 31, 2010	December 31, 2009
	\$	\$
Foreign exchange loss	6,393	16,242
Net derivative gain	-	(48)
Interest expense	3,013	1,335
Convertible debt accretion	-	6,197
	<b>9,406</b>	<b>23,726</b>

The accompanying notes constitute an integral part of these consolidated financial statements

# KATANGA MINING LIMITED

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in thousands of U.S. dollars, except per share amounts and as otherwise stated)

Years Ended December 31, 2010 and 2009

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### 17. RELATED PARTY TRANSACTIONS

Related parties and related party transactions not otherwise disclosed in these consolidated financial statements include:

#### Related Parties

**La Générale des Carrières et des Mines (“Gécamines”)** a state owned and operated mining enterprise of the DRC, has a 25% minority interest in KCC. KCC is required to make royalty and lease payments to Gécamines pursuant to the Joint Venture Agreement between Katanga, Gécamines and KCC.

**Glencore International AG (“Glencore”)** is the Company's majority shareholder and is represented on the Board of Directors of the Company. In November 2007, Glencore entered into a 100% off-take agreement for concentrate sales with the Company and commencing January 1, 2009, pursuant to additional off-take agreements, all copper and cobalt metal produced are sold to Glencore on market terms. During the year ended December 31, 2009, Glencore also provided funding to the Company in the form of convertible debt and a non-convertible bridge loan facility. The off-take agreements were entered into before Glencore was a related party of the Company.

**Xstrata Queensland Ltd (“Xstrata”)** is a subsidiary of Xstrata plc and at December 31, 2010, Glencore owned 34.08% of Xstrata plc's issued share capital. During 2009 and 2010, Xstrata provided mining equipment and services to the Company.

**Mopani Copper Mine Plc (“Mopani”)** is a copper and cobalt producer located in Zambia. Mopani is a 73% owned subsidiary of Glencore. During 2009 and 2010, Mopani supplied sulphuric acid and other consumables to the Company, and purchased concentrate from the Company. On August 4, 2010, the Company's Board of Directors approved entering into three contracts with Mopani providing for the purchase by Mopani of oxide concentrate from, and sale by Mopani of starter sheets and lead to, the Company in the ordinary course of business and on arm's length commercial terms. After reviewing the terms of the proposed three contracts, the Company's independent Directors, who are also members of its Corporate Governance and Nominations Committee unanimously recommended the Board of Directors approve entering into the three contracts with Mopani.

**Mutanda ya Mukonkota Mining SPRL (“Mutanda”)** is a copper and cobalt producer located in the DRC. Mutanda is a 40% owned investment of Glencore. There is an agreement in place for employees to use charter flights operated by either company with associated costs invoiced. Additionally, during the year ended December 31, 2010, Mutanda supplied medical services to the Company and during the year ended December 31, 2009, Mutanda supplied cranes to the Company and the Company supplied vehicles and furniture to Mutanda.

**Enterprise Generale Malta Forrest SPRL (“EGMF”)** a company owned by George Forrest and which has Malta Forrest as a Director, both of whom had a beneficial interest in the Company, was involved in contracts for the sourcing and provision of goods and services (including construction and other resources), mining of one of the open pit ore bodies, civil work and the construction of a tailings dam. These contracts were entered into while EGMF was a related party. EGMF ceased being a related party on June 10, 2009.

**Bateman Engineering N.V (“Bateman”)** a company in the BSG Resources group who through Oakey Investment Holdings, was a related party as a result of owning a beneficial interest in the Company, and was engaged in the engineering and procurement contracts for the Project. These contracts were entered into while Bateman was a related party. Bateman ceased being a related party on June 2, 2009.

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

# KATANGA MINING LIMITED

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in thousands of U.S. dollars, except per share amounts and as otherwise stated)

Years Ended December 31, 2010 and 2009

### 17. RELATED PARTY TRANSACTIONS (continued)

#### Transactions

All transactions, other than the financing transactions with the Company's parent company, Glencore, were in the normal course of business and recorded at exchange amounts. The following table provides the total amount of the transactions entered into with these related parties:

	Year ended December 31, 2010 \$	Year ended December 31, 2009 \$
<b>Purchases from related parties</b>		
Gécamines	12,523	5,153
Xstrata	2,896	7,861
Glencore	33,169	21,836
Mopani	9,749	7,151
Mutanda	6	464
<b>Purchases from former related parties</b>		
EGMF	-	28,829
Bateman	-	4,617
<b>Sales to related parties</b>		
Mutanda	380	440
Mopani	28,233	-
Glencore <sup>(1)</sup>	507,713	284,626
<b>Sales to former related parties</b>		
EGMF	-	3,808
	As at December 31, 2010 \$	As at December 31, 2009 \$
<b>Amounts owed to related parties</b>		
Gécamines	9,939	-
Glencore	3,800	178
Mopani	1,387	-
Xstrata	-	1,915
<b>Amounts owed by related parties</b>		
Gécamines	3,035	806
Mopani	12,387	5,190
Mutanda	80	24
Glencore	74,235	44,774

<sup>(1)</sup> Glencore and the Company have signed an off-take agreement whereby, commencing January 1, 2009, all copper and cobalt metal produced is sold to Glencore based on market terms.

# KATANGA MINING LIMITED

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in thousands of U.S. dollars, except per share amounts and as otherwise stated)

Years Ended December 31, 2010 and 2009

### 18. COMMITMENTS AND CONTINGENCES

The following table summarizes the Company's contractual and other obligations as at December 31, 2010.

<b>Payments due by period</b>	<b>Total</b>	<b>Less than</b>	<b>1-3</b>	<b>4-5</b>	<b>After 5</b>
	<b>\$</b>	<b>1 year</b>	<b>years</b>	<b>years</b>	<b>years</b>
	<b>\$</b>	<b>\$</b>	<b>\$</b>	<b>\$</b>	<b>\$</b>
Capital expenditure commitments <sup>(1)</sup>	33,107	33,107	-	-	-
Debentures payable <sup>(2)</sup>	175,363	17,478	157,885	-	-
Other long-term liabilities <sup>(3)</sup>	85,500	10,000	30,000	30,000	15,500
Gécamines lease <sup>(4)</sup>	25,200	1,800	5,400	3,600	14,400
	<b>319,170</b>	<b>62,385</b>	<b>193,285</b>	<b>33,600</b>	<b>29,900</b>

(1) The capital expenditure commitments relate to Phase III of the Project. Phase III commenced in 2009 and is expected to increase production to 150,000 tonnes per annum of copper production by the end of the second quarter of 2011. It is expected that Phase III will be funded from existing cash balances and cash generated by operations.

(2) The total payable includes all interest costs to the date of repayment.

(3) A "pas de porte" ("entry premium") obligation is payable to Gécamines for access to the Project. The total amount of \$140,000 is payable in installments on an agreed schedule until 2016. Of the \$140,000, \$30,000 has already been paid and \$24,500 has been deducted from these payables representing Gécamines' outstanding share capital contribution to KCC (see Note 10).

(4) Pursuant to the terms of the New Joint Venture Agreement, all installations and infrastructures within the perimeter of the KCC concession are being rented for an annual lease payment to Gécamines of \$1,800.

The Company and its subsidiaries are also subject to routine legal proceedings and tax audits. The Company does not believe that the outcome of any of these matters, individually or in aggregate, would have a material adverse effect on its consolidated earnings, cash flow or financial position.

Guarantees are disclosed in Note 5.

# KATANGA MINING LIMITED

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in thousands of U.S. dollars, except per share amounts and as otherwise stated)

Years Ended December 31, 2010 and 2009

### 19. INCOME TAXES

The following table reconciles the expected income tax recovery (provision) at the statutory income tax rates to the amounts recognized in the consolidated statements of income (loss) and comprehensive income (loss):

	Year ended	
	December 31, 2010	December 31, 2009
	\$	\$
Income (loss) before income taxes	88,970	(105,016)
Expected income tax (expense) recovery at Canadian statutory rates	(25,801)	30,455
Effect of difference in foreign tax rates	62,312	36,362
Permanent differences	(10,859)	(10,455)
Temporary differences and current year losses not recognized	(48,487)	(57,441)
Temporary differences and prior years losses not previously recognized	198,841	-
Adjustment in respect of prior years	-	(1,905)
Recovery of (provision for) income taxes	<b>176,006</b>	<b>(2,984)</b>

The components of the recovery of (provision for) income taxes comprise:

	Year ended	
	December 31, 2010	December 31, 2009
	\$	\$
Current tax provision		
Canada	-	-
Foreign	(638)	(2,329)
Future tax recovery (provision)		
Canada	-	-
Foreign <sup>(1)</sup>	176,644	(655)
	<b>176,006</b>	<b>(2,984)</b>

<sup>(1)</sup> The Company released \$160,789 of its future income tax valuation allowance as at December 31, 2010 based on its taxable income projections and its ability to utilize its net operating loss carry forwards and other tax assets relating to KCC. The Company will continue to evaluate whether the remaining valuation allowance of \$37,160 is required in a future reporting periods.

# KATANGA MINING LIMITED

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in thousands of U.S. dollars, except per share amounts and as otherwise stated)

Years Ended December 31, 2010 and 2009

### 19. INCOME TAXES (continued)

The following table reflects the future income tax asset and liability amounts at December 31, 2010 and December 31, 2009:

	As at December 31, 2010 \$	As at December 31, 2009 \$
<b>Future income tax assets</b>		
Property, plant and equipment, net	168	180
Non-capital losses carried forward	331,111	280,739
Other	22,053	16,574
	353,332	297,493
Less: valuation allowance	(37,160)	(197,949)
Total future income tax assets	316,172	99,544
<b>Future income tax liabilities</b>		
Property, plant and equipment, net	(23,463)	(191,468)
Exploration and development	(279,639)	(71,650)
Total future tax liabilities	(303,102)	(263,118)
<b>Future income tax assets (liabilities) - net</b>	<b>13,070</b>	<b>(163,574)</b>

The future income tax assets of \$316,172 primarily represent tax losses in the DRC, to the extent they offset deferred tax liabilities arising in the same company.

The Company has recorded a valuation allowance in respect of non-capital losses and other tax assets in the amount of \$37,160 as at December 31, 2010 (December 31, 2009 - \$197,949) as it is not considered to be more likely than not that the benefit associated with these losses and other tax assets will be realized prior to their expiry.

Gross non-capital losses carried forward of \$41,676 expired on the exchange of the convertible facility on June 2, 2009. In addition, gross non-capital losses carried forward of \$52,319 in DCP expired on the merger with KCC.

The following table reflects the expiry of the Company's gross non-capital losses available for future use:

	As at December 31, 2010 \$	As at December 31, 2009 \$
2013	106,444	106,444
2014	403,871	403,871
2029	8,894	8,894
2030	21,554	-
Do not expire	568,208	418,166
<b>Total gross non-capital losses</b>	<b>1,108,971</b>	<b>937,375</b>

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

# KATANGA MINING LIMITED

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in thousands of U.S. dollars, except per share amounts and as otherwise stated)

Years Ended December 31, 2010 and 2009

### 20. SEGMENTED INFORMATION

The Company has two reportable segments being Corporate and its operations in the DRC. The operations segment mainly comprises the mining, processing and selling of commodity copper and cobalt. The Corporate segment comprises the management of cash and cash equivalents, logistics and general corporate activities.

	Corporate \$	Operations in DRC \$	Total \$
<b>As at December 31, 2010</b>			
Total assets	45,298	1,898,860	<b>1,944,158</b>
<b>As at December 31, 2009</b>			
Total assets	95,909	1,655,742	<b>1,751,651</b>
<b>Year ended December 31, 2010</b>			
Sales revenue	-	535,946	<b>535,946</b>
Depreciation and amortization	(5,216)	(54,261)	<b>(59,477)</b>
Interest income	138	106	<b>244</b>
Debenture interest	(18,782)	-	<b>(18,782)</b>
Recovery of income taxes	-	176,006	<b>176,006</b>
Net (loss) income	(39,507)	304,483	<b>264,976</b>
Additions to property, plant and equipment	308	218,178	<b>218,486</b>
<b>Year ended December 31, 2009</b>			
Sales revenue	-	285,549	<b>285,549</b>
Depreciation and amortization	(678)	(27,423)	<b>(28,101)</b>
Interest income	1,028	642	<b>1,670</b>
Debenture interest	(17,214)	-	<b>(17,214)</b>
Provision for income taxes	(802)	(2,182)	<b>(2,984)</b>
Net loss	(53,419)	(54,581)	<b>(108,000)</b>
Additions to property, plant and equipment	124	117,960	<b>118,084</b>

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