

Audited Financial Statements of

KARNALYTE RESOURCES INC.

Years ended December 31, 2010 and 2009

MANAGEMENT’S REPORT TO THE SHAREHOLDERS

The accompanying financial statements are the responsibility of management.

The financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles. Other financial information appearing throughout the report is presented on a basis consistent with the financial statements.

Karnalyte Resources Inc. has established procedures and systems of internal control designed to provide reasonable assurance that assets are safeguarded and that reliable financial information is produced in a timely manner.

The Audit Committee of the Board of Directors has reviewed these financial statements with management and the independent auditors and reports its findings to the Board of Directors before such statements are approved by the Board.

The financial statements have been audited by KPMG LLP, the independent auditors, in accordance with Canadian generally accepted auditing standards on behalf of the shareholders. KPMG LLP have full and free access to the Audit Committee. The Audit Committee is responsible for determining their reappointment and the setting of their fees.

March 8, 2011

“signed”

Robin Phinney

Director and Chief Executive Officer

“signed”

Ron Love

Director and Chief Financial Officer

INDEPENDENT AUDITORS' REPORT

To the Shareholders of Karnalyte Resources Inc.

We have audited the accompanying consolidated financial statements of Karnalyte Resources Inc. (the "Company"), which comprise the balance sheets as at December 31, 2010 and 2009, the statements of loss, comprehensive loss and deficit and cash flows for the years then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the Company's preparation and fair presentation of the 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 Company'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 financial statements.

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

Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2010 and 2009, and of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

"signed KPMG LLP"

Chartered Accountants

Calgary, Canada

March 8, 2011

KARNALYTE RESOURCES INC.

BALANCE SHEETS

As at	ASSETS	
	December 31,	December 31,
	<u>2010</u>	<u>2009</u>
Current assets		
Cash	\$ 59,000,457	\$ 2,490,823
Restricted cash (note 3)	125,000	-
Investments (note 4)	-	6,147,759
Accounts receivable	43,276	279,283
Prepaid expenses	312,865	216,949
	<hr/> 59,481,598	<hr/> 9,134,814
Mineral property and deferred exploration and development costs (note 7)	10,572,459	6,791,804
Capital assets (note 6)	459,376	396,938
Intangible assets (note 5)	97,026	75,215
	<hr/>	<hr/>
TOTAL ASSETS	\$ 70,610,459	\$ 16,398,771

LIABILITIES		
Current liabilities		
Accounts payable and accrued liabilities	\$ 2,288,123	\$ 680,795
Current portion of capital lease liability (note 6)	6,904	-
	<hr/> 2,295,027	<hr/> 680,795
Capital lease liability (note 6)	6,904	-
Asset retirement obligations (note 8)	37,129	-
	<hr/>	<hr/>
Total liabilities	2,339,060	680,795

SHAREHOLDERS' EQUITY		
Share capital (note 10(b))	71,705,231	18,331,857
Warrants and rights (note 10(d))	1,273,605	293,494
Contributed surplus (note 10(f))	306,978	6,161
Deficit	(5,014,415)	(2,913,536)
	<hr/> 68,271,399	<hr/> 15,717,976
	<hr/>	<hr/>
LIABILITIES AND SHAREHOLDERS' EQUITY	\$ 70,610,459	\$ 16,398,771

Nature of operations and basis of presentation (note 1)
Commitments (note 13)
Subsequent events (notes 13 and 16)
See accompanying notes to the financial statements.

Approved on behalf of the Board:

"signed"

Ian Brown, Director

"signed"

Mark Wayne, Director

KARNALYTE RESOURCES INC.

STATEMENTS OF LOSS, COMPREHENSIVE LOSS AND DEFICIT

For the Years Ended December 31,

	<u>2010</u>	<u>2009</u>
Expenses		
General and administrative	\$ 2,840,196	\$ 1,805,852
Depreciation and accretion	52,371	20,618
Loss on investments (note 4)	277	4,844
Loss on foreign exchange	3,076	32,747
Stock-based compensation (note 10(e))	318,672	-
Interest and other income	(38,750)	(48,729)
	<hr/>	<hr/>
Loss before income taxes	(3,175,842)	(1,815,332)
Income taxes		
Future income tax reduction (note 9)	1,074,963	-
	<hr/>	<hr/>
Net and comprehensive loss	\$ (2,100,879)	\$ (1,815,332)
Deficit, beginning of year	(2,913,536)	(1,098,204)
Deficit, end of year	<u>\$ (5,014,415)</u>	<u>\$ (2,913,536)</u>
Loss per share (note 10(g))		
Basic and diluted	<u>\$ (0.16)</u>	<u>\$ (0.17)</u>

See accompanying notes to the financial statements.

KARNALYTE RESOURCES INC.

STATEMENTS OF CASH FLOWS

For the years ended December 31,

	<u>2010</u>	<u>2009</u>
Cash Flows from (used in) Operating Activities		
Net loss	\$ (2,100,879)	\$ (1,815,332)
Items not involving cash:		
Depreciation and accretion	52,371	20,618
Stock-based compensation	318,672	-
Loss on temporary investments	277	13,305
Loss on foreign exchange	3,076	16,884
Future income tax reduction	(1,074,963)	-
<u>Change in non-cash working capital (note 13)</u>	<u>233,405</u>	<u>(101,798)</u>
	<u>(2,568,041)</u>	<u>(1,866,323)</u>
Cash Flows from (used in) Investing Activities		
Increase in restricted cash	(125,000)	-
Decrease (increase) in temporary investments	6,147,482	(4,050,009)
Additions to intangible assets	(35,524)	(64,511)
Additions to capital assets	(85,979)	(129,718)
Additions to mineral property	(3,744,835)	(5,324,994)
<u>Change in non-cash working capital (note 13)</u>	<u>981,241</u>	<u>270,511</u>
	<u>3,137,385</u>	<u>(9,298,721)</u>
Cash Flows from (used in) Financing Activities		
Issuance of common shares	60,380,600	14,627,850
Share issue costs	(4,970,007)	(1,121,956)
<u>Change in non-cash working capital (note 13)</u>	<u>532,773</u>	<u>-</u>
	<u>55,943,366</u>	<u>13,505,894</u>
Effect of foreign exchange on cash	(3,076)	(16,884)
Change in cash and cash equivalents	56,509,634	2,323,966
Cash and cash equivalents, beginning of year	2,490,823	166,857
<u>Cash and cash equivalents, end of year</u>	<u>\$ 59,000,457</u>	<u>\$ 2,490,823</u>

See accompanying notes to the financial statements.

KARNALYTE RESOURCES INC.

Notes to Financial Statements

Years ended December 31, 2010 and 2009

1. **Nature of operations and basis of presentation**

Nature of operations

Karnalyte Resources Inc. (the “Company” or “Karnalyte”) is an exploration and development stage company. The business of Karnalyte consists of the exploration and development of its property and planned construction of a potash mine. The property is situated in Saskatchewan, south of Wynyard and contains a dominant zone of potash and magnesium minerals. The recoverability of amounts shown for mineral properties and deferred exploration and development costs is dependent upon the discovery of economically recoverable reserves, the ability of the Company to obtain necessary financing to develop the property and upon future profitable production or the sale thereof.

The Company has sufficient cash to meet its short-term corporate costs and existing current capital plans and has sufficient funds to finance exploration and development and ongoing corporate functions. There is no certainty, however, that the Company will be able to raise additional funds to obtain the necessary capital to move forward to the production stage.

Basis of presentation

These financial statements have been prepared by management in accordance with accounting principles generally accepted in Canada. The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reported period. Actual results may differ from these estimates. Certain amounts have been reclassified to conform with current period presentation.

2. **Significant accounting policies**

All amounts are presented in Canadian dollars. The Company’s significant accounting policies are as follows:

a) Mineral property and deferred exploration and development costs

The amount shown for mineral properties and deferred exploration and pre-development costs includes the direct costs of acquiring, maintaining, exploring and developing properties and the costs of acquiring directly related equipment. All other costs, including administrative overhead, are expensed as incurred.

Management reviews the carrying amounts of its mineral property and deferred exploration and development costs with internal and external mining professionals, at least annually. A decision to abandon, reduce or expand activity is based upon many factors including general and specific assessments of exploration and development results, anticipated future mineral prices, anticipated costs of developing and operating a producing mine and the general likelihood that the Company will continue exploration and development on the properties.

If the mineral property is abandoned or it is determined that its carrying amount cannot be supported by future production or sales, the related costs will be charged against operations in the year of abandonment or determination of impairment of value. The amounts recorded as mineral properties and deferred exploration and development costs represent unamortized costs to date and do not necessarily reflect present or future values.

KARNALYTE RESOURCES INC.

Notes to Financial Statements

Years ended December 31, 2010 and 2009

Once commercial production begins, the accumulated costs of mineral properties will be amortized to operations on a unit of production basis over the shorter of estimated reserves or useful life as determined by the Company's independent geological and engineering consultant.

b) Use of estimates

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying disclosures. Although these estimates are based on management's best knowledge of current events and actions the Company may undertake in the future, actual results may differ from these estimates. Significant areas requiring the use of management estimates include the determination of impairment of mining assets and equipment and deferred exploration and development costs, asset retirement obligations, future income taxes and stock-based compensation. These estimates are reviewed periodically and, as adjustments become necessary, they are reported in earnings in the periods in which they become known.

c) Asset retirement obligations

The Company recognizes the fair value of asset retirement obligations in the period in which it is incurred when a reasonable estimate of the fair value can be made. The fair value of the estimated asset retirement obligations is recorded as a liability, with a corresponding increase in the carrying amount of the related asset. The capitalized amount is depleted on the unit-of-production method over the shorter of estimated reserves or useful life. The liability amount is increased each reporting period due to the passage of time and the amount of accretion is expensed to income in the period. Actual costs incurred upon the settlement of the asset retirement obligations are charged against the liability to the extent recorded. Any difference between actual costs incurred and the liability recorded is recognized as a gain or loss in earnings in the period the costs are incurred.

d) Income taxes

The Company uses the asset and liability method of accounting for income taxes. Under the asset and liability method, future tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective income tax basis. Future tax assets and liabilities are measured using enacted or substantively enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on future tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the date of enactment or substantive enactment. A valuation allowance is recorded against any future assets if it is more likely than not that the asset will not be realized.

e) Stock-based compensation

The Company has a stock-based compensation plan for directors and consultants as described in Note 10. The Company uses the fair value method of accounting for stock options granted. The fair value of stock options is measured at grant date with the fair value of the options being expensed over the vesting period. In determining the fair value of the stock options granted, the Black-Scholes model is used and assumptions regarding interest rates, volatility of the Company's stock and expected life of the options are made. The Company does not incorporate a forfeiture rate for stock options that will not vest, but rather accounts for actual forfeitures as they occur.

KARNALYTE RESOURCES INC.

Notes to Financial Statements

Years ended December 31, 2010 and 2009

f) Cash and cash equivalents

Cash and cash equivalents consist of cash in bank accounts as well as investments with original maturity dates of three months or less.

g) Financial Instruments

The Company's financial instruments consist of cash and cash equivalents, restricted cash, investments, accounts receivable and accounts payable and accrued liabilities.

All financial instruments are measured at fair value on initial recognition except in specific circumstances. Changes in fair value in subsequent periods depend on whether the financial instrument has been classified as: "held for trading", "held to maturity", "loans and receivables", "available for sale" or "other financial liabilities". "Held for trading" financial assets and financial liabilities are measured at fair value with changes in fair value recognized in earnings. "Available for sale" financial assets are measured at fair value, with changes in fair value recognized in other comprehensive income. "Held to maturity" financial assets and "loans and receivables" and "other financial liabilities" are measured at amortized cost. The Company has classified its cash and cash equivalents, restricted cash and its investments as "held for trading", its accounts receivables as "loans and receivables" and its accounts payable and accrued liabilities as "other financial liabilities".

h) Capital disclosures

Capital disclosures specifies the disclosures of information that enable users of an entity's financial statements to evaluate its objectives, policies and processes for managing capital such as qualitative information about its objectives, policies and processes for managing capital, summary quantitative data about what the entity manages as capital, whether it has complied with any capital requirements and, if it has not complied, the consequences of non-compliance.

i) Depreciation

Capital and intangible assets are recorded at cost. The Company depreciates the costs of its capital and intangible assets over their estimated useful lives using the following rates and methods:

Buildings	25 years	Straight-line method
Furniture & Equipment	5 years	Straight-line method
Leasehold Improvements	5 years	Straight-line method
Patents	20 years	Straight-line method
Computer Software	1 year	Straight-line method

Depreciation starts in the month following completion of the capital spending on a project or the month following the time when an asset is substantially complete and is available for use.

j) Comprehensive income

Comprehensive income includes unrealized gains and losses, such as changes in currency translation adjustments relating to self-sustaining foreign operations, unrealized gains or losses on available-for-sale investments and the effective portion of gains or losses on derivatives designated as cash flow hedges. For the periods presented, comprehensive loss is the same as net loss.

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Notes to Financial Statements

Years ended December 31, 2010 and 2009

k) Per share amounts

Basic earnings per share is calculated by dividing net income by the weighted average number of common shares outstanding during the period. The treasury stock method is used to calculate diluted per share amounts whereby proceeds from the exercise of in-the-money stock options and unrecognized future stock-based compensation expense are assumed to be used to purchase common shares of the Company at the average market price during the period. Diluted per share amounts reflect the potential dilution that could occur if stock options to purchase common shares were exercised and converted to common shares.

l) Flow-through shares

Periodically, the Company may finance a portion of its exploration and development activities through the issuance of flow-through shares. Under the terms of the flow-through shares issues, the tax attributes of the related expenditures are renounced to subscribers. Share capital is reduced and the future tax liability is increased by the tax effected amount of the renounced tax deductions at the time of renouncement, which is when the related documentation is filed with the appropriate governmental agency and there is reasonable certainty that the expenditures will be incurred.

3. Restricted Cash

The Company was required to submit a \$125,000 irrevocable letter of credit to Saskatchewan Ministry of Environment towards any future environmental damage that could potentially be caused by the operation of its pilot plant near Wynyard, Saskatchewan. The Company believes that the limited operation of this plant will not produce any environmental issues but the letter of credit represented a condition precedent to operating the pilot facility. The letter of credit has been provided by the Company's bank on behalf of the Company and is secured by interest-bearing deposits that are not available to the Company for general use. Funds are invested in a Guaranteed Investment Certificate which is redeemable on the 15th day of each month and is due for renewal in 2013.

4. Investments

The investments held have been classified as "held for trading" for valuation purposes. The securities were measured at fair value with changes in fair value recognized in earnings. The investment instruments were all purchased with the intention of trading prior to the maturity date as they can be redeemed at any time.

During the year ended on December 31, 2010 the Company held Government of Canada Treasury Bills which bore interest at a weighted average rate of 1.04%. As at December 31, 2010 the Company had nil (December 31, 2009 - \$6,147,759) outstanding.

5. Intangible Assets

The Company capitalizes intangible assets and amortizes them over the life of the asset. Intangible assets are recorded at cost and are depreciated over their estimated useful lives using the straight-line method of depreciation.

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As at	December 31, 2010			December 31, 2009		
	Cost	Accumulated Depreciation	Net Book Value	Cost	Accumulated Depreciation	Net Book Value
Process patent	62,017	5,589	56,428	40,621	2,877	37,744
Computer software	56,448	15,850	40,598	42,320	4,849	37,471
Balance, end of year	\$ 118,465	\$ 21,439	\$ 97,026	\$ 82,941	\$ 7,726	\$ 75,215

6. Capital assets

Capital assets are recorded at cost and are depreciated over their estimated useful lives using the straight-line method of depreciation.

As at	December 31, 2010			December 31, 2009		
	Cost	Accumulated Depreciation	Net Book Value	Cost	Accumulated Depreciation	Net Book Value
Building	\$ 259,462	\$ 21,142	\$ 238,320	\$ 250,362	\$ 10,763	\$ 239,599
Land	124,656	-	124,656	124,656	-	124,656
Leasehold improvements	63,516	19,503	44,013	28,998	6,799	22,199
Equipment under capital lease	20,712	8,054	12,658	-	-	-
Furniture & equipment	46,976	7,247	39,729	11,519	1,035	10,484
Balance, end of year	\$ 515,322	\$ 55,946	\$ 459,376	\$ 415,535	\$ 18,597	\$ 396,938

7. Mineral property and deferred exploration and pre-development costs

No depletion or depreciation has been recorded during the period. Details of total mineral properties and deferred exploration and pre-development costs are as follows:

As at	December 31, 2010	December 31, 2009
Acquisition costs		
Surface land	\$ 751,750	\$ 331,750
Permits	130,906	79,582
Exploration		
Geophysics	3,282,474	2,926,175
Drilling	5,354,843	3,076,277
Engineering	794,871	193,755
Environmental	257,615	184,265
Balance, end of year	\$ 10,572,459	\$ 6,791,804

8. Asset Retirement Obligations

	December 31, 2010
Balance, beginning of year	\$ -
Obligations incurred	35,820
Accretion	1,309
Balance, end of year	\$ 37,129

KARNALYTE RESOURCES INC.

Notes to Financial Statements

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The Company's asset retirement obligations are based on the Company's net ownership in wells and facilities. Management estimates the costs to abandon and reclaim the wells and the facilities and the estimated time period during which these costs will be incurred in the future. The majority of these costs are expected to be incurred over the next 30 years. The undiscounted amount of estimated costs required to settle the retirement obligations at December 31, 2010 is \$148,000 (December 31, 2009 – \$nil). The estimated costs have been inflated at 2 percent and discounted at a credit-adjusted risk free rate of 10 percent for 2010.

9. **Income taxes**

The provision for income taxes in the statements of loss and deficit reflects an effective tax rate which differs from the expected statutory tax rate. Differences are as follows:

Year Ended December 31,	2010	2009
Loss before tax	\$ (3,175,842)	\$ (1,815,332)
Statutory Rate	28.00%	29.00%
Expected recovery at statutory rate	(889,236)	(526,446)
Non-deductible expenses	3,781	1,970
Stock-based compensation	89,228	-
Rate reductions	26,206	72,534
Change in valuation allowance	(304,942)	451,942
Provision for income taxes	\$ (1,074,963)	\$ -

The Company did not consider it more likely than not that it would be able to realize a future tax benefit on continuing operations and as a result, a valuation allowance is provided against the future tax assets. Significant components of future income tax assets (liabilities) are as follows:

As at	December 31, 2010	December 31, 2009
Mineral property, capital and intangible assets	\$ (1,082,730)	\$ 6,581
Share issue costs	1,166,060	230,039
Non-capital losses	1,781,761	776,635
Asset retirement obligations	9,282	-
Valuation allowance	(1,874,373)	(1,013,255)
	\$ -	\$ -

The Company has Canadian non-capital losses, for which no benefit has been recognized in the financial statements of approximately \$7,100,000, which commence expiry in 2026.

10. **Share Capital**

a) *Authorized:*

Unlimited voting common shares; and

Unlimited preferred shares for which none have been issued.

KARNALYTE RESOURCES INC.

Notes to Financial Statements

Years ended December 31, 2010 and 2009

b) Issued and outstanding:

	Number	Amount
Balance, December 31, 2008	9,738,400	\$ 5,112,363
Common shares issued for cash	2,037,600	10,188,000
Flow-through shares issue for cash	747,800	4,299,850
Amount ascribed to flow-through warrants	-	(22,434)
Exercised options	140,000	140,000
Share issuance costs	-	(1,331,888)
Stock-based compensation on exercise	-	7,094
Amount ascribed to rights on common shares	-	(61,128)
Balance, December 31, 2009	12,663,800	\$ 18,331,857
Issuance of common shares	6,975,000	59,985,000
Share issuance costs	-	(6,033,680)
Exercised options	176,400	395,600
Stock-based compensation on exercise of options	-	17,855
Exercise of warrants and rights	278,540	83,562
Tax effect of flow-through share renunciation	-	(1,074,963)
Balance, December 31, 2010	20,093,740	\$ 71,705,231

c) Flow-through shares

In August, 2009, the Company issued 747,800 flow-through common shares at a price of \$5.75 per share for total gross proceeds of \$4,299,850. As of December 31, 2009, the Company had incurred all of the eligible expenditures required under the flow-through share agreements.

d) Warrants and rights:

	Number	Amount
Balance, December 31, 2008	-	\$ -
Flow-through warrants	747,800	22,434
Broker warrants	167,124	209,932
Rights on common shares	2,037,600	61,128
Balance, December 31, 2009	2,952,524	\$ 293,494
Exercise of flow-through warrants	(747,800)	(22,434)
Exercise of rights on common shares	(2,037,600)	(61,128)
Broker warrants	418,500	1,063,673
Balance, December 31, 2010	585,624	\$ 1,273,605

Each flow-through warrant and right on common shares shall entitle the holder to receive a liquidity penalty which will entitle them to receive, for no additional consideration; (a) a liquidity penalty of one common share for every 10 common shares subscribed for pursuant to the offering, in the event that a liquidity event is not completed by November 12, 2010; (b) an additional Liquidity Penalty of 0.5 of a common share for every 10 common shares subscribed for pursuant to the offering in the event a liquidity event is not completed by or April 12, 2011; and (c) a further liquidity penalty of 0.1 of a common share for every 10 common shares subscribed for pursuant to the offering for every month commencing after April 12, 2011 in which a liquidity

KARNALYTE RESOURCES INC.

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Years ended December 31, 2010 and 2009

event is not completed. As at November 12, 2010, no liquidity event had occurred. As a result, 278,540 common shares were issued in fulfillment of the liquidity penalty of 1 common share for each 10 flow-through warrants and rights outstanding. Upon completion of the initial public offering on December 14, 2010, the terms of the flow-through warrants and rights have been fulfilled and are no longer outstanding.

The fair value of the broker warrants granted pursuant to the private placement and initial public offering were estimated on the date of the issue of the Agent warrants using the Black-Scholes pricing model. The fair value of the warrants was calculated to be \$209,932 (\$1.27 per warrant) for the private placement and \$1,063,673 (\$2.54 per warrant) for the initial public offering using the following fair value and weighted average assumptions:

	<u>2010</u>	<u>2009</u>
Expected life (years)	1.50	2.25
Risk-free interest rate (%)	1.60	2.00
Expected volatility (%)	60%	40%
Expected divided yield (%)	-	-
Grant date share price (\$/share)	8.60	5.00

e) Options

The Company has a stock option plan under which directors, officers, and non-employees of the Company are eligible to receive stock options. The aggregate number of common shares to be issued upon the exercise of all stock options granted under the plan shall not exceed 10% of the issued common shares of the Company at the time of granting of the options. Options granted under the plan generally have a term of two years but may not exceed five years and vest at terms to be determined by the directors at the time of grant. The exercise price of each option shall be determined by the directors at the time of grant but shall not be less than the price permitted by the policies of the stock exchange on which the Company's common shares are then listed.

Prior to the initial public offering, there were 1,300,000 (2009 – nil) options granted to directors, officers and employees of the Company. The fair value of these options granted was estimated on the date of grant using the Black-Scholes option-pricing model. These options vested immediately. Following the completion of the initial public offering an additional 528,000 options were granted to directors, officers and employees. These options vest over two years and have a life of 5 years. The fair value of these options were also calculated using the Black-Scholes options pricing model. All options granted throughout the year carried the following fair value and weighted average assumptions:

	<u>2010</u>	<u>2009</u>
Expected life (years)	2.97	-
Risk-free interest rate (%)	1.77	-
Expected volatility (%)	17%	-
Expected divided yield (%)	-	-
Fair value of options granted (\$/option)	1.35	-

The options granted prior to the initial public offering were calculated using the minimum value method for volatility (0%). Following the initial public offering, the fair value of the options was calculated using

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Years ended December 31, 2010 and 2009

estimated volatility based on a review of peer company volatilities (60%). The table above represents a weighted average of both methods of calculation.

A summary of the status of the Company's stock option plan is as follows:

	Options	Weighted Average Exercise Price
Balance, December 31, 2008	261,600	\$ 1.00
Exercised options	(140,000)	1.00
Balance, December 31, 2009	121,600	\$ 1.00
Options granted	1,828,000	6.04
Exercised options	(176,400)	2.24
Balance, December 31, 2010	1,773,200	\$6.07

The following table summarizes shares outstanding and exercisable under the plan at December 31, 2010:

Options outstanding and exercisable					
Exercise price	Number outstanding at period end	Weighted average remaining contractual life	Weighted average exercise price	Number exercisable at period end	Weighted average exercise price
\$5.00	1,245,200	1.59 years	\$5.00	1,245,200	\$5.00
\$8.60	528,000	4.97 years	\$8.60	-	-
	1,773,200	2.59 years	\$6.07	1,245,200	\$5.00

f) Contributed surplus

A reconciliation of contributed surplus is as follows:

	Amount
Balance, December 31, 2008	\$ 13,255
Transfer to share capital	(7,094)
Balance, December 31, 2009	\$ 6,161
Stock-based compensation expense	318,672
Transfer to share capital	(17,855)
Balance, December 31, 2010	\$ 306,978

g) Per share amounts

Basic and diluted loss per share is calculated using the weighted average number of shares outstanding during the year of 13,089,492 (2009 - 10,871,663). Excluded from the calculation were 1,773,200 (2009 - 121,600) options, and 585,624 (2009 - 2,952,524) broker warrants, flow-through warrants and rights as their effect would have been anti-dilutive.

11. Related party transactions

During the year ended December 31, 2010, the Company incurred \$23,883 (2009 - \$25,783) in costs from a law firm in which a director of the Company is a partner. The Company also incurred \$46,698 (2009 - \$nil) in costs paid to directors.

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The Company did not incur consulting fees for management services for the year ended December 31, 2010. However in the prior year, non-independent directors were working under contract arrangements resulting in \$562,744 fees for the year ended December 31, 2009.

These transactions are in the normal course of operations and have been recorded at exchange amount within general and administrative expenses.

12. **Supplemental cash flow information**

Changes in non-cash working capital are as follows:

	2010	2009
Accounts receivable	\$ 236,007	\$ (183,087)
Prepaid expenses	(95,916)	(152,147)
Accounts payable and accrued liabilities	1,607,328	503,947
	<hr/> \$ 1,747,419	<hr/> \$ 168,713
Relating to:		
Operating activities	\$ 233,405	\$ (101,798)
Investing activities	981,241	270,511
Financing activities	532,773	-
	<hr/> \$ 1,747,419	<hr/> \$ 168,713

13. **Commitments**

The Company is required to pay annual rent of \$0.50 per acre on its permit held for a term of five years. The permit contains 68,301 acres. The total consideration paid out in yearly rental fees on the permit property is \$34,150. The rental for any extension of the term of the permit is \$10,000 for the first extension period, \$20,000 for the second extension and \$40,000 for the third extension period. For its permit, the Company is required to expend \$40,000 in each of the second and third years of the term, and \$80,000 in the fourth and fifth years of the term on work for the purpose of exploring for, developing or mining subsurface minerals. To date, the Company has met and expects to meet all of these related commitments.

The Company is required to pay an annual lease of \$2.00 per acre (16,825 acres) on any area held under lease for a term of twenty-one years. The Company is required to expend not less than \$3,000,000 for work during the first three years of the term of the lease. In the case of any deficiency in the amount of expenditures to be incurred pursuant to this requirement, the lessee may upon application obtain twelve month extensions of time for making the required expenditures with a maximum of three such extensions, provided that for each twelve month extension the lease holder incurs a cash deposit equivalent to three per cent of the difference between \$3,000,000 and the amount of accumulated expenditures made prior to the date of application. Upon application, the lessee may, after the third extension, obtain further extensions of time for making the expenditures required to be made by a deposit of \$90,000 for each twelve month extension or portion thereof. If a lease is surrendered by the lessee or cancelled by the minister, the requirement of expenditures to be made is terminated. If the lessee incurs the expenditures and furnishes proof thereof in accordance with "The Subsurface Mineral Regulations, 1960", the deposit will be refunded to the lessee.

The Company has entered into contracts for various technical, geological, environmental, engineering and consulting services. The total committed costs for the year ended December 31, 2010 were \$384,298 (2009 -

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\$2,794,000). Subsequent to the year end the Company entered into a contract with a third party to complete a feasibility study. The total amount of the contract is approximately \$6.4 million and the work is expected to be complete by December 31, 2011.

The Company secured computer equipment by entering a capital lease on January 1, 2010. The lease carries a term of 36 months with an implicit interest rate of 13%. The present value of the minimum lease payments was \$20,712.

The Company has also signed a lease agreement for the building space that was being used for management offices. The lease is paid on a monthly basis of \$18,325 and will expire on April 30, 2013.

The following table outlines the Company's lease obligations at December 31, 2010:

	Total	Less than 1 year	1-3 years	4-5 years	More than 5 years
Mineral lease	\$ 786,678	\$ 70,990	\$ 109,988	\$ 67,300	\$ 538,400
Operating lease	513,100	219,900	293,200	-	-
Capital lease	13,808	6,904	6,904	-	-
Total	\$ 1,313,586	\$ 297,794	\$ 410,092	\$ 67,300	\$ 538,400

14. **Financial instruments and risk management**

a) Fair value of financial assets and liabilities

Section 3862, Financial Instruments – Disclosures requires an explanation about how fair value is determined for assets and liabilities measured in the financial statements at fair value and establishes a hierarchy for which these assets and liabilities must be grouped, based on significant levels of input as follows:

Level 1: observable inputs such as quoted prices in active markets;

Level 2: inputs, other than the quoted market prices in active markets, which are observable, either directly and/or indirectly; and

Level 3: unobservable inputs for the asset or liability in which little or no market data exists therefore requiring an entity to develop its own assumptions.

As at December 31, 2010 and 2009, the only financial assets measured at fair value on the Company's balance sheet were the investments which have been valued using level 2 inputs.

b) Risk Management

The Company has exposure to the following risks:

- i) Credit risk
- ii) Liquidity risk
- iii) Foreign exchange risk
- iv) Interest rate risk
- v) Commodity price risk

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This note presents information about the Company's exposure to each of the above risks, the Company's objectives, policies and processes for measuring and managing risk, and the Company's management of capital. Further quantitative disclosures are included throughout these financial statements.

The Board of Directors has overall responsibility for the establishment and oversight of the Company's risk management framework. These risks are discussed with Management and to the extent the Board determines that the risks are of such a nature that they need to be mitigated, procedures are put in place. To date, no specific risk management tools have been put in place to mitigate these risks.

i) Credit risk

Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its obligation.

Cash consists of bank balances and short-term deposits that are redeemable at any time at the option of the Company. Investments consisted of treasury bills with a weighted average interest rate 1.04 percent. The Company manages the credit exposure related to short-term investments and cash by depositing only with large banks within a particular region which management believes the risk of loss to be remote.

Accounts receivable primarily relate to GST and interest receivable from the Government of Canada, the credit risk of which is considered very low.

The carrying amounts of cash, restricted cash, investments and accounts receivable represents the maximum credit exposure. The Company does not have an allowance for doubtful accounts as at December 31, 2010 (2009 - nil) and considers none of its receivables to be past due.

ii) Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its obligations as they come due. Due to the fact that the Company has no operations that generate cash flow to meet such obligations, and it is an exploration and development Company, the Company requires external financing to ensure all of its obligations are met on a timely basis. To date the Company has been successful in raising the funds necessary to meet its obligations and fund its capital program.

The Company will need to obtain a substantial amount of funding in order to continue mine development and achieve commercial production. It is the intent of the Company to raise these funds through debt and equity financing.

iii) Foreign exchange risk

Currently the Company does not have any material receivables or payables in foreign currencies on their statements and therefore does not face material risk in relation to foreign exchange. As of December 31, 2010 there was a cash balance of \$46,083 (2009 - \$74,155) in the US account. A change in the foreign exchange rate of \$0.01 would have an insignificant effect on the Company's reported loss for 2010.

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iv) Interest rate risk

The Company does not have significant interest-bearing borrowings or lendings, other than its investments, for which general rate fluctuations apply. A change in the interest rate by 1% would have an insignificant effect on the Company's reported loss for 2010.

v) Commodity price risk

The future profitability of the Company and the recoverability of deferred project development costs are directly related to the market prices of the products it will sell in the future. Those products include magnesium and potash.

15. Capital management

The Company's policy is to maintain a strong capital base so as not to expose the Company to excess risk and to maintain investor confidence. The Company considers shareholders' equity to be capital. Due to the fact that the Company does not have cash flow from operations to service debt financing, the Company's capital programs have been funded through equity financing. The Company does not have any externally imposed capital requirements. During the periods ended December 31, 2010 and 2009, there have been no changes to the way the Company manages its capital.

16. Subsequent event

Subsequent to year end on January 13, 2011 the Company issued 470,000 shares at a price of \$8.60 for a total of \$4,042,000 as a result of the overallotment option being filled following the initial public offering. The share issue costs related to the overallotment totaled \$242,520 for a total net proceeds on the issuance of \$3,799,480.

Subsequent to year end on March 7, 2011 a syndicate member for the initial public offering exercised 33,502 broker warrants at a price of \$8.60 for a total of \$288,117.