Prophecy

Coal Corp.

Condensed Interim Consolidated Financial Statements

Unaudited

For the three and six month period ended June 30, 2013

(Expressed in Canadian Dollars)

TABLE OF CONTENTS

Financial Statements

Consolidated Statements of Financial Position 4
Consolidated Statements of Operations and Comprehensive Loss 5
Consolidated Statements of Changes in Equity 6
Consolidated Statements of Cash Flows 1

Notes to Financial Statements

1. NATURE OF OPERATIONS AND GOING CONCERN 8
2. BASIS OF PRESENTATION 9
3. CHANGES IN ACCOUNTING STANDARDS 9
4. SEGMENTED INFORMATION 10
5. CASH AND CASH EQUIVALENTS 11
6. SHORT TERM INVESTMENTS 12
7. AVAILABLE FOR SALE INVESTMENTS 12
8. INVESTMENT IN ASSOCIATE 12
9. PROPERTY AND EQUIPMENT 15
10. MINERAL PROPERTIES 19
11. LOAN PAYABLE 21
12. SHARE CAPITAL 22
13. RELATED PARTY DISCLOSURES 27
14. KEY MANAGEMENT PERSONNEL COMPENSATION 28
15. KEY SUPPLEMENTAL CASH FLOW INFORMATION 29
16. EVENTS AFTER THE REPORTING DATE 29

NOTICE OF NO AUDITOR REVIEW OF CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

The accompanying unaudited condensed interim consolidated financial statements have been prepared by management and approved by the Audit Committee. The Company's independent auditors have not performed a review of these condensed interim consolidated financial statements in accordance with the standards established for a review of interim financial statements by an entity's auditors.

PROPHECY COAL CORP.
Condensed Interim Consolidated Statements of Financial Position
(Unaudited) (Expressed in Canadian Dollars)

	Notes	June 30 2013	December 31 2012
Assets			
Current assets			
Cash and cash equivalents	5	$ 377,244	$ 768,831
Restricted cash	5	3,500,000	-
Short term investments	6	489,316	5,107,500
Receivables		515,129	456,035
Amount due from associate		156,729	82,500
Prepaid expenses		1,488,008	1,443,282
Inventory		1,757,064	2,436,534
		8,283,491	10,294,682
Non-current assets			
Reclamation deposits		27,554	27,554
Available-for-sale-investments	7	1,053,723	628,188
Investment in associate	8	23,260,089	25,118,910
Property and equipment	9	11,058,891	12,929,342
Mineral properties	10	14,462,877	13,387,882
		$ 58,146,625	$ 62,386,558
Liabilities and Equity			
Current liabilities			
Accounts payable & accrued liabilities		$ 878,756	$ 766,209
Loan payable	11	9,656,023	9,392,170
		10,534,779	10,158,379
Non-current liabilities			
Provision for closure and reclamation		294,263	294,263
Deferred income tax		953,100	953,100
		11,782,141	11,405,742
Equity			
Share capital	12	147,509,578	145,796,591
Reserves		18,977,643	18,577,859
Accumulated other comprehensive gain	7	447,846	-
Deficit		(120,570,582)	(113,393,634)
Equity attributable to owners of the Company		46,364,484	50,980,816
Total Equity		46,364,484	50,980,816
		$ 58,146,625	$ 62,386,558

Approved on behalf of the Board:

"John Lee" — Director

"Greg Hall" — Director

Events After the Reporting Date (note 16)

PROPHECY COAL CORP.
Condensed Interim Consolidated Statements of Operations and Comprehensive loss
(Unaudited) (Expressed in Canadian Dollars)

	Notes	Three months ended June 30, 2013	Three months ended June 30, 2012	Six months ended June 30, 2013	Six months ended June 30, 2012
General and Administrative Expenses					
Advertising and promotion		$ 52,601	$ 519,251	$ 111,616	$ 1,238,854
Consulting and management fees		28,353	274,436	56,405	568,402
Depreciation		21,014	42,545	43,703	112,231
Director fees		50,498	70,758	96,251	139,908
Insurance		43,216	53,232	95,170	105,114
Office and administration		23,828	79,919	35,809	156,491
Professional fees		257,459	248,316	360,023	500,041
Salaries and benefits		124,225	372,941	324,461	506,714
Share-based payments	12	135,347	668,037	335,499	3,129,274
Stock exchange and shareholder services		22,831	49,268	69,457	158,090
Travel and accommodation		33,907	95,625	59,798	193,442
Loss Before Other Items and Deferred Income Tax Recovery		(793,281)	(2,474,328)	(1,588,194)	(6,808,561)
Other Items					
Costs in excess of impaired value		(712,457)	-	(2,765,560)	-
Foreign exchange gain (loss)		72,405	1,714,249	375,664	(42,059)
Interest expense		(632,649)	(1,089)	(1,247,743)	(57,600)
Interest income		4,313	17,156	24,410	37,031
Gain (loss) on sale of investments		19,545	(100,147)	19,545	(17,619)
Mineral property written off		-	(190,980)	-	(190,980)
Share of net loss of associate	8	(399,930)	-	(872,741)	-
Deemed disposal loss of associate	8	(1,122,329)	-	(1,122,329)	-
		(2,771,104)	1,439,188	(5,588,756)	(271,228)
Loss Before Deferred Income Tax Recovery		(3,564,385)	(1,035,139)	(7,176,950)	(7,079,789)
Deferred income tax recovery		-	(68,176)	-	53,285
Net Loss for Period		(3,564,385)	(1,103,315)	(7,176,950)	(7,026,503)
Fair value (loss) gain on available-for-sale investments	7	(333,639)	(2,114,759)	451,595	(1,241,772)
Unrealized loss on foreign exchange		-	(1,515,352)	-	(1,515,352)
Fair value loss on available-for-sale investments of an associate	7	-	-	(3,750)	-
Comprehensive Loss for Period		$ (3,898,023)	$ (4,733,426)	$ (6,729,104)	$ (9,783,627)
Net income (loss) for period attributable to:					
Owners of the Company		$ (3,564,385)	$ (289,024)	$ (7,176,950)	$ (4,802,593)
Non-controlling interest		-	(814,290)	-	(2,223,909)
		$ (3,564,385)	$ (1,103,314)	$ (7,176,950)	$ (7,026,502)
Comprehensive loss for period attributable to:					
Owners of the Company		$ (3,898,023)	$ (4,638,569)	$ (6,729,104)	$ (7,804,680)
Non-controlling interest		-	(94,856)	-	(1,978,946)
		$ (3,898,023)	$ (4,733,425)	$ (6,729,104)	$ (9,783,626)
Loss Per Common Share, basic and diluted		$ (0.02)	$ (0.00)	$ (0.03)	$ (0.03)
Weighted Average Number of Common Shares Outstanding		236,490,814	225,071,203	233,057,495	216,306,209

PROPHECY COAL CORP.
Condensed Interim Consolidated Statements of Changes in Equity
(Unaudited) (Expressed in Canadian Dollars)

	Note	Numbers of shares	Share Capital	Reserves	Accumulated Other Comprehensive Gain (Loss)	Deficit	Equity attributable to owners of the Company	Non-controlling Interest	Total
Balance, January 1, 2012		201,109,422	$ 134,492,080	$ 17,138,468	$ (1,842,782)	$ (53,375,529)	$ 96,412,237	$ 32,808,418	$ 129,220,655
Private placement, net of share issue costs		22,363,866	9,594,618	-			9,594,618	-	9,594,618
Options exercised		187,500	159,875	(113,000)	-	-	46,875	-	46,875
Warrants exercised		1,479,509	762,578	(7,233)	-	-	755,345	-	755,345
Share-based payments		-	-	316,538	-	-	316,538	2,689,946	3,006,484
Share bonus to personnel		-	(259,344)	259,344	-	-	-	-	-
Warrant modification		-	-	369,531			369,531	-	369,531
Common shares subscribed		-	-	-	-	-	1,350,000	-	1,350,000
Funding from non-controlling interest,									-
net of dilution		-	-	-	-	5,243,132	5,243,132	(1,473,380)	3,769,752
Loss for the period		-	-	-	-	(4,862,103)	(4,862,103)	(2,164,399)	(7,026,502)
Unrealized gain on available-for-sale-investments		-	-	-	(1,482,670)	15,966	(1,466,704)	224,932	(1,241,772)
Unrealized gain (loss) on foreign exchange		-	-	-	(1,515,352)	-	(1,515,352)	-	(1,515,352)
Balance, June 30, 2012		225,140,297	144,749,807	17,963,648	(4,840,804)	(52,978,534)	106,244,117	32,085,517	138,329,634
Balance, January 1, 2013		228,400,956	145,796,592	18,577,859	-	(113,393,632)	50,980,816	-	50,980,816
Private placement, net of share issue cost	16	12,525,428	1,432,986	-	-	-	1,432,986	-	1,432,986
Shares issued as financing fees	11	2,000,000	280,000	-	-	-	280,000	-	280,000
Share-based payments	12	-	-	387,114	-	-	387,114	-	387,114
Share bonus to personnel	12	-	-	12,670	-	-	12,670	-	12,670
Loss for the period		-	-	-	-	(7,176,950)	(7,176,950)	-	(7,176,950)
Fair value (loss) gain on available-for-sale-investments	7	-	-	-	451,596	-	451,596	-	451,596
Fair value loss on available-for-sale investments of an associate	8	-	-	-	(3,750)	-	(3,750)	-	(3,750)
Balance, June 30, 2013		242,926,384	$ 147,509,578	$ 18,977,643	$ 447,846	$ (120,570,582)	$ 46,364,484	$ -	$ 46,364,484

PROPHECY COAL CORP.
Condensed Interim Consolidated Statements of Cash Flows
(Unaudited) (Expressed in Canadian Dollars)

	Six Months Ended June 30, 2013	2012
Operating Activities		
Net loss for the period	$ (7,176,950)	$ (7,026,502)
Items not involving cash		
Depreciation	43,703	119,069
Share-based payments	335,499	3,129,274
Share of loss of an associate	872,741	-
Costs in excess of impaired value	2,765,560	-
Deferred income tax recovery	-	(53,285)
Interest income	(24,410)	-
	(3,183,860)	(3,831,444)
Changes in non-cash working capital		
Receivables	(133,323)	1,994,025
Prepaid expenses	(44,726)	(2,467,286)
Inventory	679,470	-
Accounts payable and accrued liabilities	(374,901)	1,108,200
Interest expense	1,247,743	-
Restricted cash	(3,500,000)	-
	(2,125,737)	634,939
Cash Used in Operating Activities	(5,309,597)	(3,196,504)
Investing Activities		
Acquisition of property and equipment	(548,970)	(7,123,918)
Mineral property expenditures	(931,759)	(8,840,101)
Investment in associate acquisition	(140,000)	-
(Purchase) sale of available-for-sale investments	44,717	2,838,983
Sale of Guaranteed Investment Certificate	4,618,184	-
Interest received from short term investment	24,410	-
Cash (Used in) Provided by Investing Activities	3,066,581	(13,125,036)
Financing Activities		
Interest paid	(703,891)	-
Deemed diposal loss of associate	1,122,331	-
Shares issued, net of share issuance costs	1,432,986	14,166,593
Cash Provided by Financing Activities	1,851,426	14,166,593
Net (Decrease) Increase in Cash	(391,587)	(2,154,947)
Cash and Cash Equivalents - beginning of period	768,831	3,480,050
Cash and Cash Equivalents - end of period	$ 377,244	$ 1,325,103

1. NATURE OF OPERATIONS AND GOING CONCERN

Prophecy Coal Corp. ("Prophecy Coal" or the "Company") is incorporated under the laws of the province of British Columbia, Canada and is engaged in exploring and developing coal properties and coal mine-mouth power projects in Mongolia. The Company maintains its head office at 2nd floor, 342 Water Street, Vancouver, B.C., Canada, V6B 1B6.

The business of mineral exploration involves a high degree of risk and there can be no assurance that the Company's current operations, including exploration programs, will result in profitable mining operations. The recoverability of the carrying value of mineral properties, and property and equipment interests and the Company's continued on going existence is dependent upon the preservation of its interest in the underlying properties, the discovery of economically recoverable reserves, the achievement of profitable operations, the ability of the Company to raise additional sources of funding, and/or, alternatively, upon the Company's ability to dispose of some or all of its interests on an advantageous basis.

It is indeterminate when and whether the Company can attain profitability and positive cash flow, obtain adequate additional financing, start and achieve profitable operations at the Ulaan Ovoo property, develop the Chandgana Power Plant project including coal feed, control costs of production, and achieve the required market price levels for coal.

The Company has incurred significant losses and negative cash flow from operations in recent years. The Company was in pre-commercial production at its Ulaan Ovoo coal property in Mongolia commencing in November 2010. In July 2012, the Company temporarily suspended pre-commercial production at Ulaan Ovoo due to soft market prices for coal and rising costs, and because at that time, Prophecy Coal had sufficient coal inventory to meet anticipated demand for the remainder of 2012 and into 2013. For the six month period ended June 30, 2013, the Company's net loss amounted to $7.2 million, including the expensing of Ulaan Ovoo property expenditures incurred in the six months period of 2013, classified as costs-in-excess of impaired value, amounting to $2.8 million. The carrying value of the Ulaan Ovoo property as at December 31, 2012 and June 30, 2013 remains unchanged at its impaired value of $2 million, while the overall cumulative deficit for the Company was $120.6 million, as at June 30, 2013.

At June 30, 2013, Prophecy Coal had approximately $0.4 million in cash and cash equivalents and $0.5 million in short term investments in the form of Guaranteed Investment Certificate ("GIC") with the Bank of Montreal. Working capital amounted to a deficit of $2.25 million at June 30, 2013 compared to working capital surplus of $0.1 million as at December 31, 2012.

Additional sources of funding, which may not be available at favourable terms, if at all, include: share equity and debt financings; dispositions of Prophecy Platinum Corp. common shares held as an investment in associate (Note 8); coal sales from stockpile inventory; rental of equipment; equity, debt or property level joint ventures with power project and coal property developers; and sale of interests in existing assets. In the event that the Company is not able to obtain adequate additional funding to continue as a going concern, material adjustment would be required to both the carrying value and classification of assets and liabilities on the balance sheet.

On February 7, 2013, the Company announced that it was undertaking a non-brokered private placement to raise gross proceeds of up to $8.4 million, of which as to this undertaking the Company closed a first tranche in April 2013 amounting to $0.6 million and a second tranche of $1.1 million in June 2013.

On July 15th, 2013 the Company signed an amended credit agreement with Waterton Global Value L.P. extending the maturity date from July 16, 2013 to October 31, 2013 for the remaining loan balance of $6.5 million (Note 11).

The board of directors has determined that the Company will be able to continue as a going concern for the foreseeable future and realize its assets and discharge its liabilities and commitments in the normal course of business, and therefore, these quarterly unaudited consolidated financial statements for the six month period ended June 30, 2013 have been prepared on a going concern basis and do not reflect any adjustments that maybe necessary if the Company is unable to continue as a going concern.

2. BASIS OF PRESENTATION

(a) Statement of compliance

These unaudited condensed interim consolidated financial statements have been prepared in accordance with IAS 34, Interim Financial Reporting.

The accounting policies applied in preparation of these unaudited condensed interim consolidated financial statements are consistent with those applied and disclosed in the Company's consolidated financial statements for the year ended December 31, 2012 (Note 6 of the annual consolidated financial statements), with the exception of certain new accounting standards issued by the International Accounting Standard Board ("IASB"), which were adopted and applicable from January 1, 2013. These adoptions did not have a significant impact on the Company's unaudited condensed interim consolidated financial statements.

The Company's management makes judgements in its process of applying the Company's accounting policies in the preparation of its unaudited condensed interim consolidated financial statements. In addition, the preparation of the financial data requires that the Company's management to make assumptions and estimates of effects for uncertain future events on the carrying amounts of the Company's assets and liabilities at the end of the reporting period and the reported amounts of revenues and expenses during the reporting period. Actual results may differ from those estimates as the estimation process is inherently uncertain. Estimates are reviewed on an ongoing basis based on historical experience and other factors that are considered to be relevant under the circumstances. Revisions to estimates and the resulting effects on the carrying amounts of the Company's assets and liabilities are accounted for prospectively. The critical judgements and estimates applied in the preparation of the Company's unaudited condensed interim consolidated financial statements are consistent with those applied and disclosed in Note 5 of the Company's consolidated financial statements for the year ended December 31, 2012.

(b) Approval of the financial statements

The condensed interim unaudited consolidated financial statements were approved and authorized for issue by the Audit Committee on August 8, 2013.

3. CHANGES IN ACCOUNTING STANDARDS

Accounting standards, which become effective in 2013 and 2015, are disclosed in Note 4 of the Company's consolidated financial statements for the year ended December 31, 2012. The Company anticipates that the most significant of these standards relate to the following:

(Unaudited) (Expressed in Canadian Dollars)

IFRS 10 – *Consolidated Financial Statements* ("IFRS 10"), IFRS 11 – *Joint Arrangements* ("IFRS 11"), IFRS 12 – *Disclosure of Interests in Other Entities* ("IFRS 12") and amendments to IAS 27 – *Separate Financial Statements* ("IAS 27") and IAS 28 – *Investments in Associates and Joint Ventures* ("IAS 28"), effective for annual periods beginning on or after January 1, 2013. The combination of these five new standards establishes control as the basis for consolidation and provides enhanced disclosure requirements for the Company's interests in other entities and the effects of those interests on the Company's consolidated financial statements.

The Company reviewed its investment in Prophecy Platinum at January 1, 2013 and has concluded that that the adoption of IFRS 10 did not result in any change to the investment in an associate balance. The Company does not anticipate the changes to IFRS 11 and the revised IAS 27 and IAS 28 to have a significant impact on the consolidated financial statements.

The requirement of IFRS 12 relates to disclosures only and is applicable for the first annual period after adoption. Accordingly, the Company will include additional disclosures about interests in other entities in its annual consolidated financial statements for the year ended December 31, 2013.

Fair value measurement

The Company adopted IFRS 13, Fair Value Measurement ("IFRS 13") with prospective application from January 1, 2013.

The adoption of IFRS 13 had immaterial effect on the Company's condensed interim consolidated financial statements for the six months ended June 30, 2013. The disclosure requirements of IFRS 13 will be incorporated in its annual consolidated financial statements for the year ended December 31, 2013.

4. SEGMENTED INFORMATION

The Company operates in one operating segment, being the acquisition, exploration and development of mineral properties. Geographic segmentation of Prophecy Coal's assets is as follows:

	June 30, 2013		
	Canada	Mongolia	Total
Reclamation deposits	$ 6,500	$ 21,054	$ 27,554
Property and equipment	236,209	10,822,681	11,058,891
Mineral properties	2,167,992	12,294,885	14,462,877
Investment in associate	23,260,089	-	23,260,089
	$ 25,670,792	$ 23,138,620	$ 48,809,411

	December 31, 2012		
	Canada	Mongolia	Total
Reclamation deposits	$ 6,500	$ 21,054	$ 27,554
Property and equipment	279,045	12,650,297	12,929,342
Mineral properties	2,159,765	11,228,117	13,387,882
Investment in associate	25,118,910	-	25,118,910
	$ 27,564,221	$ 23,899,467	$ 51,463,688

Prior to December 1, 2012, Prophecy Platinum's net assets and operations were consolidated into the financial statements of Prophecy Coal. On November 30, 2012, it was determined that Prophecy Coal's control changed to significant influence over Prophecy Platinum, and therefore, since December 1, 2012, the value of those amounts were reflected as an Investment in Associate using the equity accounting method (Note 8).

5. CASH AND CASH EQUIVALENTS

Cash and cash equivalents of Prophecy Coal are comprised of bank balances and short-term money market instruments with original maturities of six months or less. The carrying amounts of cash and cash equivalents approximate fair value. Prophecy Coal's cash and cash equivalents are denominated in the following currencies:

	June 30, 2013	December 31, 2012
Cash		
Denominated in Canadian dollars	$ 60,656	$ 269,246
Denominated in US dollars	8,092	58,484
Denominated in Mongolian tugriks	308,496	441,056
Cash equivalents		
Denominated in Canadian dollars	-	45
	$ 377,244	$ 768,831

Restricted Cash

In February 2013, the Company transferred $3,500,000 from short-term investment to restricted cash pursuant to Waterton Global Value L.P ("Waterton") loan waiver agreement (Note 11). Waterton agreed to waive the default, subject to the Company completing (completed) the following;

(a) setting aside $3.5 million in escrow, designated for the following purposes:

i) $1.5 million for the acquisition of the Mongolian Tugalgatai coal assets, and
ii) $2 million for the full repayment or a partial prepayment of the Waterton loan, due July 16, 2013 (Note 16).

6. SHORT TERM INVESTMENTS

		June 30, 2013		December 31, 2012
Short Term Investments				
Denominated in Canadian dollars	$	489,316	$	5,107,500
	$	489,316	$	5,107,500

The Company's short-term investments consist of a Bank of Montreal investment account containing $44,910 and a Guaranteed Investment Certificate ("GIC") of $444,406 earning annual interest at 1.65% and maturing on May 21, 2014, but which was redeemed for cash subsequent to June 30 2013.

7. AVAILABLE FOR SALE INVESTMENTS

At June 30 2013, the Company owned about 6.7% or 30,106,385 common shares of Victory Nickel Inc.'s issued and outstanding common shares, which were quoted on the Toronto Stock Exchange at $0.035 per share on June 30, 2013 for a total quoted amount of $1,053,723 (December 31, 2012 - $628,188, with a quoted price of $.02 per share), which represented a $451,595 other comprehensive gain for the 6 month period ended June 30, 2013. This gain less a $3,750 accumulated comprehensive loss (Note 8) resulting from Prophecy Platinum's marking-to-market the investment in Auriga Gold Corp. shares resulted in a net accumulated other comprehensive gain of $447,845 for the six month period ended June 30, 2013.

On June 28, 2013 Victory Nickel issued to the holders of its outstanding shares rights to subscribe for units of the corporation. One outstanding common share entitled the holder to one rights certificate. Four rights certificates plus the sum of $0.024 are required to subscribe for one unit. One unit entitles the subscriber to a common share and a warrant of Victory Nickel at an exercise price of $0.035 per warrant exercisable from July 31, 2014 to July 31, 2015. On July 30, 2013 these rights expired unexercised.

8. INVESTMENT IN ASSOCIATE

The investment in associate, Prophecy Platinum Corp. ("Prophecy Platinum"), is recorded at its carrying amount of $23,260,089 as at June 30, 2013 ($25,118,910 as at December 31, 2012). Prophecy Coal holds significant influence over Prophecy Platinum by way of its ownership of 28.79% as at June 30, 2013 (32.1% as at December 31, 2012) of the total issued and outstanding shares of Prophecy Platinum. Its investment was initially recognised on deconsolidation of Prophecy Platinum from the Company's financial statements as at November 30, 2012, whereon the Company's ownership was 32.6%. Thereafter, the Company has accounted for its share of Prophecy Platinum results under the equity accounting method as defined in IAS 28 – Investments in Associates and Joint Ventures and will continue to do so for as long as it retains significant influence over Prophecy Platinum.

(Unaudited) (Expressed in Canadian Dollars)

These unaudited condensed interim financial statements include the Company's share of Prophecy Platinum's six months ended June 30, 2013 net loss of $872,742, by way of reducing the Investment in Associate as follows:

		June 30, 2013		December 31, 2012
Investment in Associate				
Opening balance	$	25,118,910	$	-
Initial recognition		-		25,315,871
Share of net loss of associate		(872,742)		(196,961)
Acquisitions (Note 13)		140,000		-
Deemed disposal loss of associate		(1,122,329)		-
Fair value loss on available-for-sale investments of an associate		(3,750)		-
	$	23,260,089	$	25,118,910

On June 20, 2013, Prophecy Platinum completed a private placement that the Company did not participate in. As a result, the Company's ownership in Prophecy Platinum decreased. IAS 28 dictates that a reduction in the investor's ownership must be recorded as a deemed disposal. As such, for the six months ending June 30, 2013 a deemed disposal loss of $1,122,329 (December 31, 2012 - $NIL) was recorded.

At June 30, 2013, the Company held 22,216,788 Prophecy Platinum common shares, which as of that date were quoted on the Toronto Stock Venture Exchange at $0.57 per share for a total quoted amount of $12,663,569 (December 31, 2012 quoted at $1.01 per share for a total quoted amount of $22,233,937).

As described in Note 15 to the Company's annual consolidated financial statements for the year ended December 31, 2012, pursuant to the plan of arrangement and consolidation in share capital in the acquisition of Prophecy Platinum shares in June 2011, each option and warrant holder of Prophecy Coal as at June 9, 2011 will, upon the exercise of their Prophecy Coal options and warrants, ("June 9, 2011 Options and Warrants") receive 0.094758 of a Prophecy Platinum common share, in addition to one common share of Prophecy Coal for each whole option or warrant of Prophecy Coal held and exercised. At June 30, 2013 Prophecy Coal held, reserved in-trust, 3,267,934 (December 31, 2012 - 3,267,934) Prophecy Platinum shares contingent on exercise of these June 9, 2011 Options and Warrants. Any Prophecy Platinum shares held in-trust, but not delivered, due to the expiry of unexercised June 9, 2011 Options and Warrants, shall be returned to Prophecy Coal, of which none have been returned to date. Prophecy Platinum common shares held in-trust, for Prophecy Coal June 9, 2011 Options and warrants outstanding, are excluded from the calculation of Prophecy Coal's ownership percentage in Prophecy Platinum until they are returned, if any at all (subsequent to year end, 951,300 Prophecy Platinum shares were returned to the Company, see Note 16 d), to Prophecy Coal due to the expiry of unexercised June 9, 2011 Options and Warrants.

For the period from January 1, 2012 to November 30, 2012, the Company's consolidated financial statements include the consolidation of Prophecy Platinum as it had the power to control the financial performance and operating parameters of Prophecy Platinum.

On November 30, 2012, it was determined that Prophecy Coal's control changed to significant influence over Prophecy Platinum due to the culmination of a series of events including: the appointment of Prophecy Platinum's new senior executive management not common to both companies; election of a majority of the Board of Directors not common to both companies; a reduction in shared management and administrative functions between the companies; and the reduction of Prophecy Coal's equity ownership interest from 44.4%, as at the time of acquisition in June 2011, to 32.6% as at November 30, 2012.

The ownership interest in Prophecy Platinum during 2012 decreased from 40.8% to 32.1% as a consequence of: Prophecy Platinum's series of private share equity placements, to which Prophecy Coal did not participate; the issuance of Prophecy Platinum common shares upon the acquisition of Ursa Major Minerals Inc.; and the sale of 464,700 Prophecy Platinum common shares by Prophecy Coal. As at June 30 2013, the Company's ownership interest in Prophecy Platinum amounted to 28.79%.

(Unaudited) (Expressed in Canadian Dollars)

9. PROPERTY AND EQUIPMENT

There are no restrictions on title or any expenditure to construct property and equipment during the period. In addition, there are no contractual commitments to acquire property and equipment or receive any compensation from third parties for items of property and equipment that were impaired, lost, or given up which is included in earnings or loss.

						Ulaan Ovoo		
	Computer Equipment	Furniture & Equipment	Vehicles	Computer Software	Leasehold Improvements	Mining Equipment	Deferred Exploration	Total
Cost								
Balance, January 1, 2013	$ 176,192	$ 377,701	$ 786,946	$ 196,707	$ 172,818	$ 14,459,112	$ 2,000,000	$ 18,169,476
Additions								-
Assets acquired	2,621	-	363	187	-	-	5,125,172	5,128,343
Disposals	-	-	-	-	-	(59,445)	-	(59,445)
Sale of coal	-	-	-	-	-	-	(1,094,327)	(1,094,327)
Equipment rental revenue	-	-	-	-	-	-	(697,670)	(697,670)
Costs in excess of impaired value	-	-	-	-	-	-	(3,333,174)	(3,333,174)
Balance, June 30, 2013	$ 178,813	$ 377,701	$ 787,308	$ 196,894	$ 172,818	$ 14,399,667	$ 2,000,000	$ 18,113,203
Accumulated depreciation								
Balance, January 1, 2013	80,515	135,451	288,488	120,433	58,145	4,557,103	-	5,240,135
Depreciation for period	15,182	22,476	67,561	6,921	17,282	1,684,754	567,614	2,381,790
Costs in excess of impaired value	-	-	-	-	-	-	(567,614)	(567,614)
Balance, June 30, 2013	$ 95,697	$ 157,927	$ 356,049	$ 127,354	$ 75,427	$ 6,241,857	$ -	$ 7,054,311
Carrying amount								
At June 30, 2013	$ 83,115	$ 219,774	$ 431,260	$ 69,540	$ 97,391	$ 8,157,811	$ 2,000,000	$ 11,058,891

(Unaudited) (Expressed in Canadian Dollars)

	Computer Equipment	Furniture & Equipment	Vehicles	Computer Software	Leasehold Improvements	Ulaan Ovoo Mining Equipment	Ulaan Ovoo Deferred Exploration	Exploration Equipment	Total
Cost									
Balance, January 1, 2012	$ 144,445	$ 224,564	$ 772,111	$ 234,068	$ 172,818	$ 14,248,586	$ 38,338,876	$ 28,299	$ 54,163,767
Additions									
Assets acquired	33,319	153,137	14,835	21,726	-	210,526	15,705,544	330,590	16,469,678
Sale of coal	-	-	-	-	-	-	(2,325,623)	-	(2,325,623)
Disposals	-	-	-	-	-	-	-	-	-
Impairment	-	-	-	-	-	-	(49,718,797)	-	(49,718,797)
Deconsolidation of subsidiary	(1,572)	-	-	(59,087)	-	-	-	(358,889)	(419,548)
Balance, December 31, 2012	$ 176,192	$ 377,701	$ 786,946	$ 196,707	$ 172,818	$ 14,459,112	$ 2,000,000	$ -	$ 18,169,478
Accumulated amortization									
Balance, January 1, 2012	49,226	82,448	137,315	82,456	23,582	2,125,913	-	17,551	2,518,491
Amortization for the year	32,583	53,003	151,173	84,026	34,563	2,431,190	2,655,084	61,313	5,502,935
Impairment	-	-	-	-	-	-	(2,655,084)	-	(2,655,084)
Deconsolidation of subsidiary	(1,294)	-	-	(46,049)	-	-	-	(78,864)	(126,206)
Balance, December 31, 2012	$ 80,515	$ 135,451	$ 288,488	$ 120,433	$ 58,145	$ 4,557,103	$ -	$ -	$ 5,240,136
Carrying amounts									
At December 31, 2012	$ 95,678	$ 242,250	$ 498,459	$ 76,274	$ 114,673	$ 9,902,009	$ 2,000,000	$ -	$ 12,929,342

9. PROPERTY AND EQUIPMENT (Continued)

Prior to December 1, 2012, Prophecy Platinum's net assets and operations were consolidated into the financial statements of Prophecy Coal. On November 30, 2012, it was determined that Prophecy Coal's control changed to significant influence over Prophecy Platinum, and therefore, since December 1, 2012, the value of those amounts were reflected as an Investment in Associate using the equity accounting method (Note 8).

Ulaan Ovoo Property

In November 2005, Prophecy Coal entered into a letter of intent with Ochir LLC that set out the terms to acquire a 100% interest in the Ulaan Ovoo coal property. The Ulaan Ovoo property is located in Selenge province, Mongolia. It is held by Ochir LLC under a transferable, 55-year mining license with a 45-year option for extension granted by the Government of Mongolia. The purchase price for the 100% interest, together with all equipment, buildings, and other facilities assembled and constructed at the property, was US$9,600,000. Under the terms of the agreement, Ochir LLC retained a 2% net smelter return royalty ("NSR").

In November 2006, Prophecy Coal entered into an agreement with a private Mongolian corporation to purchase 100% title and interest in five mineral licenses including licenses that are contiguous and entirely surrounding the Ulaan Ovoo property. The aggregate purchase price for the licenses was US$400,000. Under the terms of the agreement the vendor retained a 2% NSR. A finder's fee of 58,500 common shares of Prophecy Coal was issued to a third party on the acquisition.

In March 2010, Prophecy Coal was granted an option to purchase a 2% NSR on the Ulaan Ovoo property from Dunview Services Ltd., a private British Virgin Islands company, with a cash payment of US$130,000 and issuance of 2,000,000 common shares of Prophecy Coal. In April 2010, Prophecy Coal exercised the option and a total of $1,570,000 was capitalized as acquisition costs of the property.

On November 9, 2010, Prophecy Coal received a mining permit from the Mongolian Ministry of Mineral Resources and Energy ("MMMRE") for the Ulaan Ovoo coal property. During the year ended December 31, 2010, Prophecy Coal had reached technical feasibility, commenced development, and achieved some pre-commercial production, and accordingly reclassified mineral property costs to Property and Equipment.

Costs in excess of impaired value and impairment write down of Ulaan Ovoo property

During the six months ending June 30, 2013, the Company incurred expenditures on the Ulaan Ovoo property, classified as costs in excess of impaired value, amounting to $2,765,560, which is reflected on the condensed interim consolidated statement of operations and comprehensive loss. As there were no benchmark or market changes from January 1, 2013 to June 30, 2013, the impaired value for Ulaan Ovoo within property and equipment, remains unchanged at a balance of $2,000,000 (see Note 9, table of property and equipment).

Pre-commercial operations for the period from commencement in November 2010 until the temporary shutdown in July 2012, to which shutdown is ongoing; along with project exploration and development costs were capitalized within the category Ulaan Ovoo deferred exploration costs within property and equipment. Modest coal sales revenue from an existing stockpile along with associated costs to deliver the coal occurred during the interim period, including the first six months of 2013, post shutdown, and have been recorded as deferred exploration, within property and equipment. The ending coal stockpile inventory value at June 30, 2013 was $1.8 million ($2.4 million at December 31, 2012). During the six months ending June 30, 2013, the Company rented out part of its equipment fleet for revenue proceeds of $697,670.

The determined impaired value of $2 million for the Ulaan Ovoo property on as at December 31, 2012, remains unchanged at June 30, 2013. The determination was based on pre-commercial operating results along with capital expenditures and the Ulaan Ovoo-Prefeasibility Study ("PFS") dated December 2010 prepared by the independent engineering firm, Wardrop, a Tetra Tech Company. The PFS determined a net present value for the project of US$71 million after capital expenditures of approximately US$70 million, assuming a base case price for coal at US$40 per tonne. Prophecy Coal expended about US$70 million in development and equipment costs but was unable to establish commercial production levels, faced higher input costs mainly due to fixed costs over lower production levels in addition to some higher unit input costs, and could not realize profitable coal sales prices. For 2011, which the PFS scheduled as a pre-commercial period, the PFS estimated coal sales of 250,000 tonnes with a gross value of $10 million, while in comparison, the Company in 2011 recorded coal sales of 132,000 tonnes for a gross value of $2.5 million. In 2012, the PFS projected coal sales rising to 1.1 million tonnes with a gross sales value of $45 million and thereafter at 2 million tonnes of annual coal production at a gross sales value of $80 million. For 2012, which was accounted for as a pre-commercial period, the Company recorded coal sales of 121,000 tonnes with a gross value of $2.3 million. Average coal prices realized for 2011, 2012 and most recently from 2013 coal shipments from the coal stockpile inventory, have averaged approximately US$20 per tonne, with only about 20% of the 2012 stockpile sales value above US$28 per tonne. The average lower sales volumes and prices is because of depressed local coal markets and the Company, due to border and export regulations, has been unable to ship coal across the Mongolian border into Russia where coal prices are significantly higher.

The Company continues to evaluate project operating optimization alternatives for the Ulaan Ovoo property, in addition to investigating potential strategic partner and joint venture arrangements, sale of part or whole of the project, and coal marketing arrangements both domestically and to other countries, potentially to access higher international coal market prices. However, Prophecy Coal is unable to determine with certainty, how long coal markets will remain depressed, and when, if at all, access to Russian coal markets will be opened, nor the extent of project changes and operational modifications that would be required to more fully realize, beyond its pre-commercial operating history, on the potential value of the existing NI 43-101 coal reserve estimates per the PFS and per the NI 43-101 coal resources as determined by the 2007 Behre Dolbear report. Based on longer term coal sales prices of $28 per tonne, unit costs approaching the PFS based on higher production levels, the Company determined a book recoverable amount for the Ulaan Ovoo property as at December 31, 2012, and unchanged as at June 30, 2013, at $2,000,000 and expensed, costs in excess of impaired value, of $2,765,560 ($3,333,174 credit to deferred exploration and a $567,614 charge to accumulated amortization) on its Ulaan Ovoo property for the six month period ended June 30, 2013.

(Unaudited) (Expressed in Canadian Dollars)

10. MINERAL PROPERTIES

	Chandgana Tal	Chandgana Khavtgai	Titan	Okeover, others	Total
Notes	17(a)	17(b)	17(c)	17(d)	17(e)
Balance, January 1, 2013	$ 8,624,130	$ 2,603,986	$ 750,628	$ 1,409,138	$ 13,387,882
2013 Additions:					
Acquisition cost	-	-	-	-	-
Deferred exploration costs:					
Licenses, leases, and power plant application	414,815	145,710	-	8,157	568,682
Geological core, engineering, and consulting	223,828	53,564	-	69	277,461
Camp and general	228,852	-	-	-	228,852
	867,495	199,274	-	8,226	1,074,995
Balance, June 30, 2013	**$ 9,491,625**	**$ 2,803,260**	**$ 750,628**	**$ 1,417,364**	**$ 14,462,877**

(Unaudited) (Expressed in Canadian Dollars)

	Chandgana Tal	Chandgana Khavtgai	Titan	Okeover, others	Ilch Khujirt	Lynn Lake	Wellgreen	Burwash
Notes	17(a)	17(b)	17(c)	17(d)	17(e)	17(f)	17(g)	17(h)
Balance, January 1, 2012	$ 4,752,701	$ 2,124,768	$ 738,649	$ 1,366,912	$ -	$ 32,760,807	$ 17,603,145	$ 1,883,050
2012 Additions:								
Acquisition cost	-	-	-	-	-	1,450,000	-	-
Deferred exploration costs:								
Application	2,493,956	-	11,979	14,056	-	28,474	3,987	-
Consulting	1,186,558	475,464	-	20,373	190,980	-	2,124,984	-
Drilling	-	-	-	-	-	-	3,945,131	-
Personnel	70,341	-	-	-	-	11,157	516,454	-
Recovery	-	-	-	-	-	(50,851)	-	-
Camp and general	120,574	3,754	-	7,797	-	11,291	1,839,816	16,744
Impairment					(190,980)			
	3,871,429	479,218	11,979	42,226	-	1,450,070	8,430,372	16,744
Deconsolidation of subsidiary	-	-	-	-	-	(34,210,877)	(26,033,517)	(1,899,794)
Balance, December 31, 2012	**$ 8,624,130**	**$ 2,603,986**	**$ 750,628**	**$ 1,409,138**	**$ -**	**$ -**	**$ -**	**$ -**

	Cerro Chato and others	Las Aguilas	Shakespeare	Baldwin and option	Shining Tree	Stumpy Bay Option	Fox Mountain	Total
Notes	17(i)	17(j)	17(k)	17(l)	17(m)	17(n)	17(o)	
Balance, January 1, 2012	$ 707,450	$ 231,999	$ -	$ -	$ -	$ -	$ -	$ 62,169,481
2012 Additions:								
Acquisition cost	-	198,255	5,989,350	477,114	442,873	318,811	109,373	8,985,776
Deferred exploration costs:								-
Licenses and leases	-	22,361	-	-	-	-	-	2,574,812
Consulting	40,256	-	-	-	-	-	-	4,038,615
Drilling	-	-	-	-	-	-	-	3,945,131
Personnel	-	-	-	-	-	-	-	597,952
Camp and general	-	8,228	-	-	-	-	-	(42,623)
Recovery	803	-	-	-	-	-	-	2,000,780
Impairment	-	(460,843)	-	-	-	-	-	(651,823)
	41,059	-	-	-	-	-	-	12,462,843
Deconsolidation of subsidiary	(748,509)	-	(5,989,350)	(477,114)	(442,873)	(318,811)	(109,373)	(70,230,218)
Balance, December 31, 2012	**$ -**	**$ -**	**$ -**	**$ -**	**$ -**	**$ -**	**$ -**	**$ 13,387,882**

(Unaudited) (Expressed in Canadian Dollars)

11. LOAN PAYABLE

The outstanding balance of the loan payable as at June 30, 2013 is summarized as follows:

		June 30, 2013		December 31, 2012
Loan payable	$	9,656,023	$	9,392,170
	$	9,656,023	$	9,392,170

On June 18, 2012, Prophecy Coal entered into a Sale and Purchase Agreement (the “Tugalgatai Agreement”) to acquire assets in Mongolia relating to certain Tugalgatai coal exploration property licenses from Tethys Mining LLC ("Tethys"), subject to approval from the Minerals Resource Authority of Mongolia to have such exploration licenses transferred to Prophecy Coal. The Tugalgatai licenses are contiguous to Prophecy Coal’s Chandgana licenses. The terms of the Agreement include a US$10 million upfront payment and an 8.5% royalty on future coal sales from both the Chandgana and Tugalgatai licenses. The royalty can be extinguished by paying Tethys US$20 million before 2021 or US$25 million from 2021 onwards.

Of the purchase price, US $10 million was deposited in escrow in July 2012, and classified as restricted cash. In October 2012 the funds, net of costs, amounting to US $9.9 million were returned to Prophecy Coal on termination of the Tugalgatai Agreement, which occurred due to the elapsing of the initial long stop date for approval of the licences transfer by the Minerals Resource Authority of Mongolia.

In order to purchase the Tethys property, in July 2012, Prophecy Coal arranged a secured debt facility of $10,000,000 (the “Loan”) with Waterton. The Loan has a one year term, due on July 16, 2013, and bears interest at 14% per annum payable monthly with an effective interest rate of 25%. In connection with the Loan, a structuring fee of 2.5% ($250,000) was paid to Waterton in cash and legal fees of $189,805 were paid. Pursuant to the terms of the Loan, Prophecy Coal issued (for a value of $600,000) 2,735,617 common shares of Prophecy Coal on closing of the Loan at July 16, 2012.

Upon entering into the secured debt facility, Prophecy Coal’s holding of 16.5 million Prophecy Platinum common shares, along with its holding of common shares in each of its Mongolian and Canadian subsidiaries were pledged as collateral against the Loan. Pursuant to the credit agreement dated July 16, 2012 (the “Credit Agreement”), the Loan funds will be used to complete the purchase of the Tugalgatai, Mongolia coal licenses and for general working capital.

As at December 31, 2012 and June 30, 2013, Prophecy Coal had outstanding $10,000,000 of the Loan, which is callable at the option of Waterton in the case of the termination of the Tugalgatai Agreement. Such termination occurred in October 2012 as the initial long stop date for approval of the licence transfers by Minerals Resource Authority of Mongolia had elapsed. Under the Credit Agreement, the expiry of the original purchase and sales agreement with Tethys constituted a default.

In February 2013, Waterton agreed to waive the default, subject to the Company completing (completed) the following;

(a) setting aside $3.5 million of the original $10 million loan in escrow for the following purposes:

i) $1.5 million for the acquisition of the Mongolian Tugalgatai coal assets, and

ii) $2 million for the full repayment or a partial prepayment of the Loan;

(b) issuing 2 million common shares to Waterton, which were issued March 15, 2013 at a value of $0.14 per share for a total of $280,000, as a financing fee pursuant to a February 2013 waiver agreement in relation to the $10 million loan.

(c) pledging additional security to Waterton in the form of 5,535,000 remaining free trading Prophecy Platinum common shares held by the Company.

At June 30, 2013 the Company had $3.5 million set aside in an escrow account, which may be used to decrease the loan payable amount of $10 million, due July 16, 2013, to a balance of $6.5 million (Note 1).

For the six month period ending June 30, 2013, the Company recorded an interest expense of $1,247,743 (of which $703,891 represents cash interest payments).

On July 15, 2013 the Waterton loan was reduced from $10 million to $6.5 million and the term extended to October 31, 2013 (Note 16b).

12. SHARE CAPITAL

(a) Authorized

The authorized share capital consists of an unlimited number of common shares without par value. There are no authorized preferred shares. At June 30, 2013, the Company had 242,926,384 (December 31, 2012 - 228,400,956) common shares issued and outstanding.

(b) Equity issuances

During the six month period ended June 30, 2013, Prophecy Coal had the following common share capital transactions:

(i) On January 24, 2013 the Board of Directors approved the grant of 2,197,500 bonus shares to employees, consultants and directors, subject to shareholder approval and subject to the following terms: 50% vest on shareholder approval and 50% vest on January 2, 2014. These bonus shares were approved by the TSX on March 7, 2013, subject to a shareholder vote, to which the shareholders approved the bonus share grant at the annual general meeting, on July 30, 2013 (Note 16). As of June 30, 2013 no bonus share expenses have been recorded or accrued, and will be recorded in the third quarter, whereon approval by the shareholders occurred.

(ii) On March 15, 2013, Prophecy Coal issued 2,000,000 shares to Waterton at a value of $0.14 per share, amounting to $280,000, as a financing fee pursuant to a waiver in relation to $10 million loan, (Note 11).

iii) On April 12, 2013, the Company closed the first tranche of a non-brokered private placement announced on February 7, 2013 (the “Private Placement”), issuing 4,382,571 the issuance of 4,382,571 units (each a “Unit”) of the Company, of which each Unit consists of one common share (a “Share”) and 0.75 common share purchase warrant (a “Warrant”), at a purchase price of $0.14 per Unit. Each whole Warrant is exercisable into one common share of Prophecy at a price of $0.18, expiring two years from the date of issue. Each Unit sold in the first tranche closing also included, subject to shareholder approval, which was obtained at the AGM on July 30, 2013 an adjustment warrant entitling the holder to acquire additional common shares of the Company in certain circumstances Finder's fees of 6% were paid in connection with a portion of the first tranche of the private placement.

(Unaudited) (Expressed in Canadian Dollars)

(iv) On June 6, 2013, the Company closed a second and final tranche of the Private Placement with the issuance of 8,142,857 units (each a "Unit") of the Company for aggregate consideration of $1,140,000. Each Unit consists of one common share and 0.75 of a common share purchase Warrant at a purchase price of $0.14 per Unit. Each whole Warrant is exercisable for one common share of Prophecy at a price of $0.18, expiring two years from the date of issue. Each Unit sold in the second tranche closing also included an adjustment warrant entitling the holder to acquire additional common shares of the Company in certain circumstances. A finder's fee of 6 percent was paid in respect of the NewMargin Prophecy Coal Limited portion of the second tranche of the Private Placement. The Company amended the Placement to include an additional warrant ("Adjustment Warrant") in each Unit sold in the final tranche. Each Adjustment Warrant may be exercised for no additional consideration for a period of 12 months following the closing of the final tranche of the private placement, for a fraction of a common share of Prophecy. The fraction will be calculated by first dividing the Unit subscription price of $0.14 by the market price (subject to a floor market price of $0.105) at the time of exercise, then subtracting one (1) from that resulting number to determine the fraction. Market price is defined as the 20 day moving average price for the Company's common shares. The Adjustment Warrants must be exercised in their entirety and may not be exercised in part, and the holder of Adjustment Warrants may not sell any securities of the Company within 20 days prior to exercise. Adjustment Warrants may also only be exercised to the extent that the holder continues to hold the shares and warrants comprising the Units of which the Adjustment Warrants formed part.

(c) Share purchase options

During the six months ended June 30, 2013, the Company granted 300,000 share options to a consultant, which under IFRS 2 is treated as employee options, at an exercise price of $0.14 with an expiry date of March 4, 2018.

The following is a summary of the changes in Prophecy Coal's share purchase options from January 1, 2013 to June 30, 2013:

	Number of Options	Weighted Average Exercise Price
Outstanding, January 1, 2013	32,485,550	$0.70
Granted	300,000	$0.14
Exercised	-	$0.00
Forfeited	(660,000)	$0.15
Cancelled	-	$0.00
Outstanding, June 30, 2013	32,125,550	$0.57
Options exercisable on June 30, 2013	23,568,883	$0.70

(Unaudited) (Expressed in Canadian Dollars)

Share-based payment expenses are amortized over the corresponding vesting periods. During the six months ended June 30, 2013 and the year ended December 31, 2012, the share-based payment expenses were calculated using the following weighted average assumptions:

	Six months ended June 30, 2013	Year ended December 31, 2012
Risk-free interest rate	1.41%	1.50%
Expected life of options in years	4.14 years	4.46 years
Expected volatility	92.2%	91.0%
Expected dividend yield	Nil	Nil
Expected forfeiture rate	12%	3%

The expected volatility used in the Black-Scholes option pricing model is based on the historical volatility of the Company's shares. The forfeiture rate in the period is greater than the historical due to a rationalization of the workforce.

For the six months ended June 30, 2013 and 2012, share-based payments were recorded as follows:

	Three Months Ended June 30, 2013	Three Months Ended June 30, 2012	Six Months Ended June 30, 2013	Six Months Ended June 30, 2012
Consolidated Statement of Operations				
Share based payments	$ 135,347	$ 407,781	$ 335,499	$ 673,747
Consolidated Statement of Financial Position				
Ulaan Ovoo exploration	18,229	(3,181)	50,542	12,321
Power Plant Project	4,783	-	13,743	-
	23,012	(3,181)	64,285	12,321
Total share-based payments	$ 158,359	$ 404,600	$ 399,784	$ 686,068

For the comparative three and six months ended June 30, 2012, Prophecy Platinum's share-based payments were consolidated into the statement of operations. On November 30, 2012, it was determined that Prophecy Coal's control changed to significant influence over Prophecy Platinum, and therefore, since December 1, 2012, the value of those amounts were reflected as an Investment in Associate using the equity accounting method (Note 8).

(Unaudited) (Expressed in Canadian Dollars)

As of June 30, 2013 and December 31, 2012, the following Prophecy Coal share options were outstanding:

June 30, 2013		December 31, 2012		Expiry	Exercisable	Unvested
Exercise Price	Options Outstanding	Exercise Price	Options Outstanding	Date	At June 30, 2013	At June 30, 2013
$0.14	1,500,000	$ 0.14	1,500,000	November 2, 2017	-	1,500,000
$0.14	300,000	$ -	-	March 4, 2018	-	300,000
$0.15	150,000	$ 0.15	150,000	November 5, 2017	-	150,000
$0.18	375,000	$ 0.18	375,000	September 24, 2017	-	375,000
$0.18	230,000	$ 0.18	230,000	August 16, 2017	-	230,000
$0.18	4,664,167	$ 0.18	5,044,167	August 22, 2017	-	4,664,167
$0.18	-	$ 0.18	100,000	September 20, 2017	-	-
$0.25	975,000	$ 0.25	975,000	October 29, 2014	975,000	-
$0.25	10,000	$ 0.25	10,000	June 1, 2017	5,000	5,000
$0.38	200,000	$ 0.38	200,000	November 30, 2014	200,000	-
$0.40	1,056,800	$ 0.40	1,056,800	January 23, 2014	1,056,800	-
$0.40	381,250	$ 0.40	381,250	January 29, 2015	381,250	-
$0.43	-	$ 0.43	80,000	January 9, 2017	-	-
$0.49	2,485,000	$ 0.49	2,555,000	March 22, 2017	1,242,500	1,242,500
$0.54	850,000	$ 0.54	850,000	September 21, 2015	850,000	-
$0.55	350,000	$ 0.55	350,000	March 11, 2015	350,000	-
$0.60	175,000	$ 0.60	175,000	July 17, 2014	175,000	-
$0.60	65,000	$ 0.60	65,000	September 21, 2014	65,000	-
$0.63	1,615,000	$ 0.63	1,615,000	June 13, 2016	1,615,000	-
$0.67	1,722,500	$ 0.67	1,722,500	May 10, 2015	1,722,500	-
$0.67	175,000	$ 0.67	175,000	October 15, 2015	175,000	-
$0.77	2,050,000	$ 0.77	2,050,000	December 24, 2015	2,050,000	-
$0.77	180,000	$ 0.77	210,000	August 30, 2016	90,000	90,000
$0.77	9,000,000	$ 0.77	9,000,000	December 10, 2015	9,000,000	-
$0.80	475,000	$ 0.80	475,000	April 30, 2015	475,000	-
$0.80	100,000	$ 0.80	100,000	September 23, 2015	100,000	-
$0.80	120,000	$ 0.80	120,000	January 4, 2016	120,000	-
$0.93	2,590,833	$ 0.93	2,590,833	December 24, 2015	2,590,833	-
$0.93	50,000	$ 0.93	50,000	January 6, 2016	50,000	-
$0.98	130,000	$ 0.98	130,000	February 14, 2016	130,000	-
$1.03	150,000	$ 1.03	150,000	March 24, 2015	150,000	-
	32,125,550		32,485,550		23,568,883	8,556,667

(Unaudited) (Expressed in Canadian Dollars)

(d) Share purchase warrants

The following is a summary of the changes in Prophecy Coal's warrants and adjustment warrants from January 1, 2013 to June 30, 2013:

	Number of Warrants	Weighted Average Exercise Price
Outstanding, January 1, 2013	10,339,926	$0.57
Issued warrants	9,394,072	$0.18
Expired	(6,508,415)	$0.80
Outstanding, June 30, 2013	13,225,583	$0.05

	Number of Adjustment Warrants	Weighted Average Exercise Price
Outstanding, January 1, 2013	-	-
Issued adjustment warrants	12,525,429	**
Expired	-	-
Outstanding, June 30, 2013	12,525,429	-

** Adjustment warrants, see Note 12 b (iv).

As at June 30, 2013 and December 31, 2012, the following Prophecy Coal warrants and adjustment were outstanding:

Exercise price	Number of Warrants At June 30, 2013	At December 31, 2012	Expiry date
$0.18	3,831,511	3,831,511	October 28, 2015
$0.18	-	551,968	March 31, 2013
$0.80	-	2,964,730	March 31, 2013
$0.80		337,750	April 21, 2013
$0.80	-	2,650,967	March 23, 2013
$0.18	3,286,929	-	April 11, 2015
$0.18	6,107,143	-	June 4, 2015
	13,225,583	10,339,926	

Exercise price	Number of Adjustment Warrants At June 30, 2013	At December 31, 2012	Expiry date
**	4,382,572	-	April 11, 2014
**	8,142,857	-	June 4, 2014
	12,525,429	-	

** Adjustment warrants, see Note 12 b (iv).

13. RELATED PARTY DISCLOSURES

Details of transactions between Prophecy Coal and other related parties are disclosed below.

Prophecy Coal had related party transactions with the following companies, related by way of directors and key management personnel:

(a) The Cantech Capital Corporation, a private company owned by Donald Gee, a former director of Prophecy Platinum, provided consulting and management services.

(b) The Elysian Enterprises Inc., a private company owned by David Patterson, a former director of Prophecy Platinum, provided consulting and management services.

(c) Energy Investment Capital, a private company owned by Jivko Savov, former Director of Prophecy Coal, provided consulting services to the Company.

(d) JWL Investment Corp., a private company owned by Joseph Li, former General Manager, Corporate Secretary and Director of Prophecy Coal and Prophecy Platinum, provided management services to the Company.

(e) Linx Partners Ltd., a private company controlled by John Lee, Director, Interim CEO and Executive Chairman of Prophecy Coal, and a Director and former Chairman and CEO of Prophecy Platinum, provides management and consulting services for Prophecy Coal and Director services to Prophecy Platinum.

(f) MaKevCo Consulting Inc., a private company 50% owned by Greg Hall, Director of Prophecy Coal and Prophecy Platinum, provides consulting and management services to the Company.

(g) The Energy Gateway Ltd., a private company owned by former Director Paul Venter, provided consulting and management services.

The Company's related party disclosure includes Prophecy Platinum's related party transactions during the six months ended June 30, 2012. Prior to December 1, 2012, Prophecy Platinum's net assets and operations were consolidated into the financial statements of Prophecy Coal. On November 30, 2012, it was determined that Prophecy Coal's control changed to significant influence over Prophecy Platinum, and therefore, since December 1, 2012, the value of those amounts were reflected as an Investment in Associate using the equity accounting method (Note 8).

On June 4, 2013, John Lee, the interim CEO, subscribed for 1,000,000 of the Company's common shares. In lieu of paying cash in the amount of $140,000 (1,000,000 shares at $0.14 per share), he transferred to the Company 202,989 shares of Prophecy Platinum (which were valued effective at $0.69 per share).

(Unaudited) (Expressed in Canadian Dollars)

A summary of related party expenses is as follows:

	Three months ended June 30,		Six months ended June 30,	
Related parties	2013	2012	2013	2012
Cantech Capital Corp. (a)	$ -	$ 2,500	$ -	$ 5,000
Directors and officers	79,271	94,527	166,227	172,860
Elysian Enterprises Inc. (b)	-	2,000	-	5,000
Energy Investment Capital (c)	-	-	-	26,239
JWL Investments Corp. (d)	-	42,000	-	84,000
Linx Partners Ltd. (e)	105,003	149,862	210,006	299,862
MaKevCo Consulting Inc. (f)	17,900	17,500	39,300	62,000
The Energy Gateway (g)	-	19,789	-	51,991
	$ 202,174	$ 328,179	$ 415,533	$ 706,952

A summary of the expenses by nature among the related parties is as follows:

	Three months ended June 30,		Six months ended June 30,	
Related parties	2013	2012	2013	2012
Consulting and management fees	$ 10,503	$ 232,362	$ 21,006	$ 502,284
Directors' fees	50,471	69,777	96,223	138,927
Mineral properties	73,500	9,895	147,000	25,996
Property and equipment	21,000	9,895	42,000	25,996
Salaries and benefits	46,700	6,250	109,304	13,750
	$ 202,174	$ 328,179	$ 415,533	$ 706,952

As at June 30, 2013, the amount included within accounts payable and accrued liabilities, which was due to related parties, consisted of amounts owing to directors for fees totalling $18,493 (December 31, 2012 – $53,334) and reimbursable expenses, and consulting fees for managing the mineral properties and power project.

Transactions with subsidiaries and associates

Transactions between the Company and its subsidiaries are eliminated on consolidation; therefore, they are not disclosed as related party transactions. Transactions between the Company and its associate, Prophecy Platinum, are disclosed as follows.

Prophecy Coal shares administrative assistance and office space, and previously shared management with Prophecy Platinum pursuant to a one year Service Agreement for 2012, consisting of fixed monthly fees of $40,000 subject to periodic adjustment. Prophecy Coal recovers costs for services rendered to Prophecy Platinum and expenses incurred on behalf of Prophecy Platinum. As at June 30, 2013 an estimated amount of $156,729 was due from Prophecy Platinum for shared office costs.

14. KEY MANAGEMENT PERSONNEL COMPENSATION

Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the Company, including directors of the Company.

(Unaudited) (Expressed in Canadian Dollars)

Key Management Personnel	Three months ended June 30, 2013	Three months ended June 30, 2012	Six months ended June 30, 2013	Six months ended June 30, 2012
Salaries and short term benefits	$ 153,432	$ 288,527	$ 323,008	$ 560,354
Share-based payments	84,843	16,905	204,407	116,666
	$ 238,275	$ 305,432	$ 527,415	$ 677,020

Included in the key management personnel compensation are John Lee's (Executive Chairman and interim CEO) compensation payments of $210,000, of which $189,000 was capitalized to the Ulaan Ovoo and Prophecy Power Generation projects for the period of January 1, 2013 – June 30, 2013.

15. KEY SUPPLEMENTAL CASH FLOW INFORMATION

	Six months ended June 30, 2013	Six months ended June 30, 2012
Supplementary information		
Interest paid	$ 703,891	$ 56,511
Non-Cash Financing and Investing Activities		
Shares issued as financing fees	$ 280,000	$ -
Capitalized depreciation of fixed assets	$ 2,381,790	$ 1,767,671
Property & equipment expenditures included in accounts payable	$ 339,300	$ 81,892
Mineral property expenditures included in accounts payable	$ 129,492	$ 1,544,766
Share-based payments capitalized in property and equipment	$ 50,542	$ 12,321
Share-based payments capitalized in mineral properties	$ 13,743	$ 234,419

16. EVENTS AFTER THE REPORTING DATE

The following events occurred subsequent to June 30, 2013:

a) Subsequent to June 30, 2013, the Company issued 358,542 common shares as a share bonus to personnel.

b) On July 15, 2013 the Company amended the Senior Secured Credit Agreement with Waterton Global Value, L.P. ("Waterton") (the "Amendment") originally entered into on July 16, 2012 as amended on February 1, 2013 by a Waiver Agreement (such credit agreement as amended by the waiver agreement and the Amendment, the "Amended Loan Agreement").

Prophecy Coal has agreed to and completed a partial pay down of the principal loan amount from $10 million to $6.5 million (the "Loan") from restricted cash-on-hand amounting to $3.5 million and extending the maturity date from July 16, 2013 to October 31, 2013. The Amended Loan Agreement facility is a non-revolving facility, and any repayment under the facility is not available for re-borrowing.

As consideration for entering into the Amendment, Prophecy Coal shall pay Waterton, in cash, a non-refundable restructuring fee (the "Restructuring Fee") in four (4) equal, consecutive, monthly installment payments (each, a "Restructuring Installment"). Each Restructuring Installment shall be in an amount equal to two percent (2%) of the outstanding principal of the Loan as of the date of the execution of the Amendment. The Restructuring Installments shall be due and payable on the following dates: the date of the execution of the Amendment; August 29, 2013; September 27, 2013; and October 31, 2013. No Restructuring Installment(s) will be due or payable following repayment, in full, by Prophecy Coal to Waterton, of all amounts owing under the Amended Loan Agreement. For example, if Prophecy Coal repays all amounts owing under the Amended Loan Agreement in full on September 15, 2013, then Prophecy will not have to pay Waterton the Restructuring Installments due and payable on September 27, 2013 or October 31, 2013.

As additional consideration, the Amendment also provides that each prepayment and repayment in full or in part of the principal amount outstanding under the Amended Loan Agreement must be increased as follows:

(i) if such payment is of the entire outstanding principal amount of the Loan, Prophecy Coal shall pay to Waterton an amount in cash equal to the quotient of the entire amount outstanding under the Loan and the applicable Discount Metric (as set out below); and
(ii) if such payment is a partial payment of the outstanding amount of the Loan, Prophecy Coal shall pay Waterton an amount in cash equal to the quotient of the partial payment amount and the applicable Discount Metric;
(iii) where "Discount Metric" means (i) 1.00 from the date of the Amendment up to and including August 16, 2013;(ii) 0.98 from August 17, 2013 up to and including August 31, 2013; (iii) 0.96 for the calendar month of September, 2013; and (iv) 0.94 for the calendar month of October, 2013.

c) Subsequent to June 30, 2013, the Company granted 500,000 stock options at price $0.13 per share for a period of five years to the Company's CFO.

d) Subsequent to June 30, 2013, 951,300 of Prophecy Platinum's reserved held in-trust shares were released back to the Company due to 9,230,749 Prophecy Coal warrants expiring and 808,514 Prophecy Coal options being cancelled or forfeited. As of August 13, 2013 the Company now owned 29.38% of Prophecy Platinum.

Management's Discussion and Analysis of Financial Condition and Results of Operations

For the three and six months ended June 30, 2013

(Expressed in Canadian Dollars)

CONTENTS

1. INTRODUCTION 4
2. QUARTER 2 HIGHLIGHTS AND SIGNIFICANT EVENTS 5
3. BUSINESS OVERVIEW 7
4. SUMMARY OF QUARTERLY RESULTS 8
5. DISCUSSION OF OPERATIONS 16
6. LIQUIDITY AND CAPITAL RESOURCES 21
7. ENVIRONMENT 24
8. RELATED PARTY DISCLOSURES 25
9. CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS 27
10. FINANCIAL INSTRUMENTS AND RELATED RISKS 29
11. RISKS AND UNCERTAINTIES 30
12. DISCLOSURE CONTROLS AND PROCEDURES 39
13. DISCLOSURE OF OUTSTANDING SHARE DATA 40
14. OFF-BALANCE SHEET ARRANGEMENT 42

This Interim Management's Discussion and Analysis ("**MD&A**") of Prophecy Coal Corp. and its subsidiaries ("**Prophecy Coal**", or the "**Company**") should be read in conjunction with the unaudited condensed interim consolidated financial statements of the Company and the notes thereto for the three and six months periods ended June 30, 2013 and with the audited consolidated financial statements of the Company and the notes thereto for the year ended December 31, 2012 ("**Audited Consolidated Financial Statements**"). The financial statements have been prepared in accordance with International Financial Reporting Standards ("**IFRS**") as issued by the International Accounting Standard Board ("**IASB**") and interpretations of the International Financial Reporting interpretations Committee ("**IFRIC**"). Additional information relating to the Company is available on the SEDAR website at www.sedar.com and the Company's website at www.prophecycoal.com.

Financial information is expressed in Canadian dollars, unless stated otherwise. This MD&A is current as of August 14, 2013. Readers are cautioned that this MD&A contains "forward-looking statements" and that actual events may vary from management's expectations. Readers are encouraged to read the cautionary note contained herein regarding such forward-looking statements. This MD&A was reviewed, approved and authorized for issue by the Company's Audit Committee on August 8, 2013.

Cautionary Note Regarding Forward-Looking Statements

Certain statements contained in this MD&A, including statements which may contain words such as "expects", "anticipates", "intends", "plans", "believes", "estimates", or similar expressions, and statements related to matters which are not historical facts, are forward-looking information within the meaning of applicable securities laws. Such forward-looking statements, which reflect management's expectations regarding Prophecy Coal's future growth, results of operations, performance, business prospects and opportunities, are based on certain factors and assumptions and involve known and unknown risks and uncertainties which may cause the actual results, performance, or achievements to be materially different from future results, performance, or achievements expressed or implied by such forward-looking statements. These estimates and assumptions are inherently subject to significant business, economic, competitive and other uncertainties and contingencies, many of which, with respect to future events, are subject to change and could cause actual results to differ materially from those expressed or implied in any forward-looking statements made by Prophecy.

In making the forward-looking statements in this MD&A, Prophecy Coal has made several assumptions that it believes are appropriate, including, but not limited to assumptions that: all required third party contractual, regulatory and governmental approvals will be obtained for the development, construction and production of Prophecy Coal's properties and the Chandgana Power Plant; there being no significant disruptions affecting operations, whether due to labour disruptions; currency exchange rates being approximately consistent with current levels; certain price assumptions for coal, prices for and availability of fuel, parts and equipment and other key supplies remain consistent with current levels; production forecasts meeting expectations, the accuracy of Prophecy Coal's current mineral resource estimates; labour and materials costs increasing on a basis consistent with Prophecy Coal's current expectations; and that any additional required financing will be available on reasonable terms. Prophecy Coal cannot assure you that any of these assumptions will prove to be correct.

In light of the risks and uncertainties inherent in all forward-looking statements, the inclusion or incorporation by reference of forward-looking statements in this MD&A should not be considered as a representation by Prophecy Coal or any other person that Prophecy Coal's objectives or plans will be achieved. Forward-looking statements in this MD&A include, without limitation, statements regarding the permitting, feasibility, plans for development and production of Prophecy Coal's Chandgana Power Plant, including finalizing of any power purchase agreement; the likelihood of securing project financing; estimated future coal production at the Ulaan Ovoo coal mineral property and the Chandgana coal mineral properties; and other information concerning possible or assumed future results of operations of Prophecy.

Numerous factors could cause Prophecy Coal's actual results to differ materially from those expressed or implied in the forward looking statements, including the following risks and uncertainties, which are discussed in greater detail under the heading "Risk Factors" in this MD&A: Prophecy's history of net losses and lack of foreseeable cash flow; exploration, development and production risks, including risks related to the development of Prophecy Coal's Ulaan Ovoo coal property; Prophecy Coal not having a history of profitable mineral production; the uncertainty of mineral resource and mineral reserve estimates; the capital and operating costs required to bring Prophecy Coal's projects into production and the resulting economic returns from its projects; foreign operations and political conditions, including the legal and political risks of operating in Mongolia, which is a developing jurisdiction; the availability and timeliness of various government approvals and licences; the feasibility, funding and development of the Chandgana Power Plant; title to the Prophecy Coal's mineral properties; environmental risks; the competitive nature of the mining business; lack of infrastructure; Prophecy Coal's reliance on key personnel; uninsured risks; commodity price fluctuations; reliance on contractors; Prophecy Coal's need for substantial additional funding and the risk of not securing such funding on reasonable terms or at all; foreign exchange risks; anti-corruption legislation; global financial conditions; the payment of dividends; and conflicts of interest.

These factors should be considered carefully, and readers should not place undue reliance on Prophecy Coal's forward-looking statements. Prophecy Coal believes that the expectations reflected in the forward-looking statements contained in this MD&A and the documents incorporated by reference herein are reasonable, but no assurance can be given that these expectations will prove to be correct. In addition, although Prophecy Coal has attempted to identify important factors that could cause actual actions, events or results to differ materially from those described in forward looking statements, there may be other factors that cause actions, events or results not to be as anticipated, estimated or intended. Prophecy Coal undertakes no obligation to release publicly any future revisions to forward-looking statements to reflect events or circumstances after the date of this MD&A or to reflect the occurrence of unanticipated events, except as expressly required by law.

1. INTRODUCTION

Prophecy Coal Corp. is a company incorporated under the laws of the province of British Columbia, Canada. Its focus is on the acquisition, exploration and development of coal properties and the development of its Chandgana Power Plant project in Mongolia.

General Corporate Information

At June 30, 2013 and August 14, 2013, Prophecy Coal had: (i) 230,400,956 and 243,184,926 common shares issued and outstanding, respectively; (ii) 32,515,550 and 32,625,550 share options for common shares outstanding, respectively; and (iii) 4,169,261 and 25,751,012 warrants for common shares outstanding, respectively.

Head office
2nd floor, 342 Water Street, Vancouver, BC, V6B 1B6
+1-604-569-3661
Registered office
Suite 1700, Park Place 666 Burrard St, Vancouver, BC V6C 2X8

Share Information
Common shares of Prophecy Coal are listed for trading on: (i) the TSX under the symbol "PCY", (ii) the OTC-QX under the symbol "PRPCF", and (iii) on the Frankfurt Stock Exchange under the symbol "1P2".

Transfer Agents and Registrars
Computershare Investor Services Inc.
3rd Floor, 510 Burrard Street
Vancouver, BC Canada
V6C 3B9
Tel: +1-604-661-9400

Investor Information
All financial reports, news releases and corporate information can be accessed on our web site at www.prophecycoal.com

Contact Information
Investors: Bekzod Kasimov
<bekzod@prophecycoal.com>
Media requests and queries:
+1.604.569.3690 Greg Hall
(Vancouver, Canada)
info@prophecycoal.com

(Expressed in Canadian Dollars)

Directors and Officers

As at the date of this MD&A, Prophecy Coal's directors and officers were as follows:

Directors	Officers
John Lee, Executive Chairman	John Lee, Interim Chief Executive Officer
Harald Batista	Jeffrey Mason, Chief Financial Officer
Chuluunbaatar Baz	
Michael Deats	
Greg Hall	

Audit Committee	*Compensation Committee*	*Corporate Governance Committee*
Greg Hall (Chair)	Greg Hall (Chair)	Greg Hall
Harald Batista	Harald Batista	Harald Batista
Michael Deats	Michael Deats	Michael Deats

Qualified Persons

Mr. Christopher Kravits, LPG, CPG, is a qualified person as defined under National Instrument 43-101 *Standards of Disclosure for Mineral Projects* ("**NI 43-101**"). Mr. Kravits is not considered independent of Prophecy Coal given the large extent that his professional time is dedicated solely to Prophecy Coal. Mr. Kravits has reviewed and approved the technical and scientific disclosure regarding the mineral properties of Prophecy Coal contained in this MD&A.

2. QUARTER 2 HIGHLIGHTS AND SIGNIFICANT EVENTS

- On February 7, 2013, the Company announced that it was undertaking a non-brokered private placement (the "**Placement**") of up to 60,000,000 units (each a "**Unit**") at a price of $0.14 per Unit to raise gross proceeds of up to $8.4 million. Each Unit consists of one common share (a "**Share**") of the Company and 0.75 of a share purchase warrant (a "**Warrant**"). Each whole Warrant entitles the holder to acquire an additional Share at a price of $0.18 per Share for a period of two years following closing.

  On April 12, 2013, the Company closed a first tranche of the Placement, issuing 4,382,571 Units for gross proceeds of $613,560 (the "**First Tranche Closing**"). Finder's fees of 6% were paid in connection with a portion of the first tranche of the private placement. The foregoing Shares and Warrants and any shares issued upon the exercise of the Warrants comprising the Units sold in the first tranche are subject to a four month resale hold period. Each Unit sold in the second tranche closing also included, upon shareholder approval, which was obtained on July 30 2013 at the Company's AGM, an adjustment warrant entitling the holder to acquire additional common shares of the Company in certain circumstances.

  On June 6, 2013, the Company closed a second and final tranche of the Placement with the issuance of 8,142,857 Units of the Company for aggregate consideration of $1,140,000. Each Unit consists of one common share and 0.75 of a common share purchase Warrant at a purchase price of $0.14 per Unit. Each whole Warrant is exercisable for one common share of Prophecy at a price of $0.18, expiring two years from the date of issue. Each Unit sold in the second tranche closing also included an adjustment warrant entitling the holder to acquire additional common shares of the Company in certain circumstances. A total of 12,525,428 Units were sold in the Placement, for aggregate gross proceeds of $1,753,560. The Company intends to use the proceeds of the Placement to advance the Chandgana power plant project and for general working capital purposes.

A finder's fee of 6 percent was paid in respect of the NewMargin Prophecy Coal Limited portion of the second tranche of the placement. All securities issued in connection to the Placement are subject to a 4 months and one day hold period from the date of security issuance.

- On May 17, 2013, the Company announced receipt of official correspondence from the Head of the Chandgana project working group (the "**Working Group**") designated by the Mongolian Ministry of Energy, outlining the terms of a tariff agreement reached by the Working Group and Prophecy Power Generation LLC ("**PPG**", wholly owned subsidiary of Prophecy), for the Chandgana coal mine mouth power plant project (the "**Chandgana Power Plant**").

Subsequent to quarter end

- On July 15, 2013 the Company amended the Senior Secured Credit Agreement with Waterton Global Value, L.P. ("**Waterton**") (the "**Amendment**") originally entered into on July 16, 2012 as amended on February 1, 2013 by a Waiver Agreement (such credit agreement as amended by the waiver agreement and the Amendment, the "**Amended Loan Agreement**").

  Prophecy Coal has agreed to and completed a partial pay down of the principal loan amount from $10 million to $6.5 million (the "**Loan**") from restricted cash-on-hand amounting to $3.5 million and extending the maturity date from July 16, 2013 to October 31, 2013. The Amended Loan Agreement facility is a non-revolving facility, and any repayment under the facility is not available for re-borrowing.

  As consideration for entering into the Amendment, Prophecy Coal is required to pay Waterton, in cash, a non-refundable restructuring fee (the "**Restructuring Fee**") in four equal, consecutive, monthly instalment payments (each, a "**Restructuring Instalment**"). Each Restructuring Instalment shall be in an amount equal to two percent (2%) of the outstanding principal of the Loan as of the date of the execution of the Amendment. The Restructuring Instalments are due and payable on the following dates: the date of the execution of the Amendment; August 29, 2013; September 27, 2013; and October 31, 2013. No Restructuring Instalment(s) will be due or payable following repayment, in full, by Prophecy Coal to Waterton, of all amounts owing under the Amended Loan Agreement. For example, if Prophecy Coal repays all amounts owing under the Amended Loan Agreement in full on September 15, 2013, then Prophecy will not have to pay Waterton the Restructuring Instalments due and payable on September 27, 2013 or October 31, 2013.

  As additional consideration, the Amendment also provides that each prepayment and repayment in full or in part of the principal amount outstanding under the Amended Loan Agreement must be increased as follows:

  (i) if such payment is of the entire outstanding principal amount of the Loan, Prophecy Coal shall pay to Waterton an amount in cash equal to the quotient of the entire amount outstanding under the Loan and the applicable Discount Metric (as set out below); and
  (ii) if such payment is a partial payment of the outstanding amount of the Loan, Prophecy Coal shall pay Waterton an amount in cash equal to the quotient of the partial payment amount and the applicable Discount Metric;
  (iii) where "Discount Metric" means (i) 1.00 from the date of the Amendment up to and including August 16, 2013;(ii) 0.98 from August 17, 2013 up to and including August 31, 2013; (iii) 0.96 for the calendar month of September, 2013; and (iv) 0.94 for the calendar month of October, 2013.

- The Company granted 500,000 stock options exercisable into common shares at a price of $0.13 per share, for a period of five years to the Company's CFO.

- Subsequent to June 30, 2013, 951,300 of Prophecy Platinum's reserved held in-trust shares were released back to the Company due to 9,230,749 Prophecy Coal warrants expiring and 808,514 Prophecy Coal options being cancelled or forfeited. As of August 6, 2013 the Company now owned 29.38% of Prophecy Platinum.

(Expressed in Canadian Dollars)

3. BUSINESS OVERVIEW

Prophecy Coal in its current form is primarily the product of an April 2010 business combination between Red Hill Energy Ltd. (at the time TSX.V - RH) and a company formed in 2006, Prophecy Resource Corp. ("**Old Prophecy Coal**"). Under that merger, Red Hill was the successor legal entity which is herein referred to as the "Corporation". Under that 2010 business combination Old Prophecy Coal was merged with a subsidiary of Red Hill.

Red Hill was incorporated on November 6, 1978 under the *Company Act* (British Columbia) under the name "Banbury Gold Mines Ltd." Banbury changed its name to "Enerwaste Minerals Corp." on December 17, 1993, Enerwaste changed its name to "Universal Gun-Loc Industries Ltd.". On April 24, 2002, Universal Gun-Loc changed its name to "UGL Enterprises Ltd." and to Red Hill Energy Inc on April 16, 2006. On May 10, 2005, the Corporation, as UGL, transitioned under the new (2004) *Business Corporations Act* (British Columbia) ("**BCBCA**") which is the corporate law statute which continues to govern the Corporation. On April 16, 2010, the Corporation (then Red Hill) changed its name to "Prophecy Resource Corp." in conjunction with the Red Hill merger. On June 13, 2011, the Corporation changed its name to "Prophecy Coal Corp. in connection with an asset spin-off to capitalize our controlled at that time, publicly traded Prophecy Platinum Corp. ("**Prophecy Platinum**") further described herein.

Prophecy Coal is a reporting issuer in the provinces of British Columbia, Alberta, and Ontario. The Company's common shares (the "Shares" or "Prophecy Coal Shares") are listed for trading on the Toronto Stock Exchange ("**TSX**" or the "Exchange") under the symbol "PCY". Prophecy Coal currently has six wholly-owned subsidiaries (the "**Subsidiaries**") and 29.38% publicly-traded associate company, Prophecy Platinum.

3.1 Investment in Associate

The investment in associate, Prophecy Platinum, is recorded at its carrying amount of $23,260,089 as at June 30, 2013 ($25,118,910 as at December 31, 2012). Prophecy Coal holds significant influence over Prophecy Platinum by way of its ownership of 28.79% as at June 30, 2013 (32.1% as at December 31, 2012) of the total issued and outstanding shares of Prophecy Platinum. Its investment was initially recognised on deconsolidation as at November 30, 2012 with ownership of 32.6%. Thereafter, the Company accounted for its share of Prophecy Platinum results under the equity accounting method and will continue to do so for as long as it retains significant influence over Prophecy Platinum (see Note 15 to the Audited Consolidated Financial Statements for the year ended December 31, 2012).

These unaudited condensed interim financial statements include the Company's share of Prophecy Platinum's six months ended June 30, 2013 net loss of $872,742, by way of reducing the Investment in Associate as follows:

		June 30, 2013		December 31, 2012
Investment in Associate				
Opening balance	$	25,118,910	$	-
Initial recognition		-		25,315,871
Share of net loss of associate		(872,742)		(196,961)
Acquisitions (Note 13)		140,000		-
Deemed disposal loss of associate		(1,122,329)		-
Fair value loss on available-for-sale investments of an associate		(3,750)		-
	$	23,260,089	$	25,118,910

On June 20, 2013, Prophecy Platinum completed a private placement that the Company did not participate in. As a result, the Company's ownership in Prophecy Platinum decreased. IAS 28 dictates that a reduction in the investor's ownership must be recorded as a deemed disposal. As such, for the six months ending June 30, 2013 a deemed disposal loss of $1,122,329 (December 31, 2012 - $NIL) was recorded.

At June 30, 2013, the Company held 22,216,788 Prophecy Platinum common shares, which as of that date were quoted on the Toronto Stock Venture Exchange at $0.57 per share for a total quoted amount of $12,663,569 (December 31, 2012 quoted at $1.01 per share for a total quoted amount of $22,233,937).

As described in Note 15 to the Company's Audited Consolidated Financial Statements for the year ended December 31, 2012, pursuant to the plan of arrangement and consolidation in share capital in the acquisition of Prophecy Platinum shares in June 2011, each option and warrant holder of Prophecy Coal as at June 9, 2011 will, upon the exercise of their Prophecy Coal options and warrants, ("**June 9, 2011 Options and Warrants**") receive 0.094758 of a Prophecy Platinum common share, in addition to one common share of Prophecy Coal for each whole option or warrant of Prophecy Coal held and exercised. At June 30, 2013 Prophecy Coal held in reserve 3,267,934 (December 31, 2012 - 3,267,934) Prophecy Platinum shares contingent on exercise of these June 9, 2011 Options and Warrants. Any Prophecy Platinum shares held in reserve but not delivered, due to the expiry of unexercised June 9, 2011 Options and Warrants, shall be returned to Prophecy Coal, of which none had been returned as at June 30, 2013. Prophecy Platinum common shares held in reserve for outstanding Prophecy Coal June 9, 2011 Options and Warrants are excluded from the calculation of Prophecy Coal's ownership percentage in Prophecy Platinum unless and until they are returned to Prophecy Coal due to the expiry of unexercised June 9, 2011 Options and Warrants.

Subsequent to June 30, 2013, 951,300 of Prophecy Platinum's reserved held in-trust shares were released back to the Company due to 9,230,749 Prophecy Coal warrants expiring and 808,514 Prophecy Coal options being cancelled or forfeited. As of August 6, 2013 the Company now owned 29.38% of Prophecy Platinum.

3.2 Mineral Properties

As of June 30, 2013, Prophecy Coal's primary mineral properties included: Ulaan Ovoo coal property (Mongolia) and the Chandgana Khavtgai and Chandgana Tal coal deposits (Mongolia), collectively known as the "Chandgana Coal Properties". The other properties of Prophecy Coal included the Okeover copper-molybdenum project (British Columbia, Canada), Kanichee property (Ontario, Canada), and the Titan iron-titanium project (Ontario, Canada).

Ulaan Ovoo Coal Property, Mongolia

Prophecy Coal (Red Hill at the time) entered into a letter of intent, dated November 24, 2005, as amended February 19, 2006, with Ochir LLC and a wholly owned subsidiary of Ochir LLC, both privately owned Mongolian companies, which set out the terms to acquire a 100% interest in the Ulaan Ovoo Property. The purchase price for the 100% interest, together with all equipment, buildings and other facilities, assembled and constructed at the Ulaan Ovoo property was US$9,600,000. The purchase price has been paid in full by Prophecy Coal. Ochir LLC retained a 2% royalty on production from the licenses, which was subsequently assigned to a third party.

On November 15, 2006, Prophecy Coal entered into an agreement with a private Mongolian company to purchase 100% of the title and interest in five mineral licenses including licenses that are contiguous and entirely surrounding the Ulaan Ovoo property. The aggregate purchase price for the licenses was US$400,000. Under the terms of the agreement the vendor retained a 2% net smelter return royalty on the five newly acquired licenses. On April 29, 2009, Prophecy Coal announced positive pre-feasibility study results for the Ulaan Ovoo property.

On March 11, 2010, Prophecy Coal entered into a royalty purchase agreement, dated for reference March 5, 2010, with Dunview Services Limited, a private British Virgin Islands company holding a 2% royalty on production from the licenses of the Ulaan Ovoo property, to acquire such royalty in full in exchange for US$130,000 and the issuance of 2,000,000 Prophecy Coal shares. This transaction was completed on April 30, 2010.

The Ulaan Ovoo site establishment commenced on July 13, 2010. In October 2010, Prophecy Coal provided 10,000 tonnes of coal as a trial run to power stations in Darkhan and Erdenet, Mongolia's second and third largest cities, respectively, after its capital, Ulaanbaatar. At the request of the Mongolian Ministry of Mineral Resources and Energy, Prophecy Coal commenced pre-commercial mining and trucked the first coal shipment to Sukhbaatar rail station, for transport to Darkhan power plant by rail.

On November 9, 2010, Prophecy Coal received the final permit to commence pre-commercial mining operations at the Ulaan Ovoo mine. On December 16, 2010, Prophecy Coal received an updated prefeasibility study (the "**PFS**") on the Ulaan Ovoo property. The focus of the Ulaan Ovoo PFS was for the development of low ash coal reserves in the form of a starter pit.

The estimated resources, reserves, coal quality, and other mine characteristics of the Ulaan Ovoo coal property were estimated by independent consultancies. The coal resources are presented in Table 1 and the coal reserves and mining characteristics for the starter pit area in Table 2.

Table 1. Coal resource detail of the Ulaan Ovoo property

Coal Resources (million tonnes)		
Measured	Indicated	Total
174.5	34.3	208.8

Resources are from the 2006 Behre Dolbear NI 43-101 report.

Table 2. Coal reserve detail of the starter pit area of the Ulaan Ovoo property

Coal Reserves (million tonnes)			Mining Period (years)	Strip Ratio (Bcm/t)	Coal Quality (arb)			
Proven	Probable	Total			Total Moisture (wt %)	Ash (wt %)	Gross Calorific Value (kcal/kg)	Total Sulfur (wt %)
20.7	0	20.7	10.7	1.8:1	21.7	11.3	5,040	Not det

Reserves, mining period, coal quality, and strip ratio are from the December 2010 Wardrop pre-feasibility report. This study was prepared for a starter pit and only considered a portion of the resource area north of the Zelter River. Coal reserves and qualities given in the above table are stated on a Run-of-Mine (ROM) basis and take into account mining loss and rock dilution at coal/rock interfaces. Strip ratio is the operating strip ratio. Proven reserves are of Low Ash (high grade) coal.

The Behre Dolbear & Company (USA), Inc. report ("**Scoping Study Ulaan-Ovoo Coal Deposit**") dated October 2006 was prepared by independent Qualified Person Mr. Gardar G. Dahl, Jr, P. Geo, a senior associate of Behre Dolbear & Company (USA), Inc. (the "**Behre Dolbear Report**"). The Wardrop report ("**Ulaan Ovoo Pre-Feasibility Study**") dated December 10, 2010 was prepared by John Sampson, B.Sc. (Hons) and Brian Saul P. Eng. who are independent Qualified Persons under NI 43-101. Both reports are available on www.sedar.com.

Operation Statistics:

The mine, which started operations in November 2010 through the mining contractor, Leighton Asia Limited and later, under Prophecy Coal's own management, has removed and stockpiled approximately 3.31 million bank cubic metres ("BCM") of topsoil and overburden (waste), and produced 451,231 tonnes of coal of all grades. In 2010 – 2011 Prophecy Coal acquired its two fleets of mining equipment for $14.7 million and secured a rail siding at Sukhbaatar with capacity of 40,000 tonnes. During 2011 and 2012, Prophecy Coal trucked 126,359 and 123,213 tonnes of coal from the mine to the rail siding, respectively. Prophecy Coal sold 133,895 tonnes of coal to both Mongolian and Russian companies during 2011 and 121,000 tonnes of coal to Mongolian companies during 2012.

In July 2012, the Company temporarily suspended pre-commercial production at Ulaan Ovoo due to soft market prices for coal and rising costs, and because at that time, Prophecy Coal had sufficient coal inventory to meet anticipated demand for the remainder of 2012 (the stockpile of coal was approximately 187,000 tonnes). Transport of inventory coal from existing coal stockpiles commenced during November 2012 and continued to July 1, 2013.

On December 31, 2012, the Company recorded a non-cash impairment write down of $47 million on the Ulaan Ovoo property, which was reflected on the consolidated statement of operations. The impairment charge reduced previously capitalized deferred exploration within property and equipment, to a balance of $2 million (Note 16 to the Audited Consolidated Financial Statements).

The determination of impaired value of $2 million for the Ulaan Ovoo property was based on pre-commercial operating results along with capital expenditures and the Ulaan Ovoo PFS. The PFS determined a net present value for the project of US$71 million after capital expenditures of approximately US$70 million, assuming a base case price for coal at US$40 per tonne. Prophecy Coal expended about US$70 million in development and equipment costs but was unable to establish commercial production levels, faced higher input costs mainly due to fixed costs over lower production levels in addition to some higher unit input costs, and could not realize profitable coal sales prices. For 2011, which the PFS scheduled as a pre-commercial period, the PFS estimated coal sales of 250,000 tonnes with a gross value of $10 million, while in comparison, the Company in 2011 recorded coal sales of 132,000 tonnes for a gross value of $2.5 million. In 2012, the PFS projected coal sales rising to 1.1 million tonnes with a gross sales value of $45 million and thereafter at 2 million tonnes of annual coal production at a gross sales value of $80 million. For 2012, which was accounted for as a pre-commercial period, the Company recorded coal sales of 121,000 tonnes with a gross value of $2.3 million. Average coal prices realized for 2011, 2012 and most recently from 2013 coal shipments from the coal stockpile inventory, have averaged approximately US$20 per tonne, with only about 20% of the 2012 stockpile sales value above US$28 per tonne. The average lower sales volumes and prices are because of depressed local coal markets and the Company, due to border and export regulations, has been unable to ship coal across the Mongolian border into Russia where coal prices are significantly higher.

During the first quarter ending March 31, 2013 the Company continued to ship coal from its stockpiles and leased a portion of its mining fleet while pursuing increased sales to its existing customers and new customers. The Company shipped approximately 40,000 tonnes of coal to local customers from the existing stockpiles and realized modest coal sales revenue along with associated costs to deliver the coal during this period. At the end of the first quarter the coal stockpile balance was approximately 92,000 tonnes. The Company leased a portion of the mining fleet and provided operators and technicians making for monthly revenues of approximately $102,000. Coal sales and lease of the equipment allowed the Company the flexibility to meet revenue targets.

During the second quarter ended June 30, 2013, the Company continued to supply coal from the existing coal stockpile, mined a small amount of coal, continued leasing equipment, increased efforts to develop new customers, continued assessment to re-start the mine, and continued building loyalty from its existing customer base. The Company shipped approximately 1,800 tonnes of coal to local customers in the second quarter. As of June 30, 2013 the coal stockpile balance was approximately 107,000 tonnes. The Company mined 22,217 tonnes of previously uncovered coal to avoid its inaccessibility, when water level rises during the spring thaw. The Company continued to lease part of its equipment fleet and supply operators and technicians with average monthly revenues of approximately $100,000. Additional technicians were hired to increase availability of the equipment. The sale of coal and lease of equipment allowed the Company revenues to offset ongoing costs. Inquiries from the State of Buryatia in the CIS and industrial customers in Mongolia led to several marketing trips for negotiations. The Company is in ongoing negotiations with several prospective customers, and is hopeful that sales contracts may be signed during the third quarter, 2013. If the Company is successful in entering into these contracts, it may result in an increase in coal production over previous years, along with increased revenue and profit margins. The Company has commenced preparations to potentially recommence operation of the mine, including reorganization of management, budgeting, some rehiring staff, repairs, and ordering of parts and supplies, and, in addition, it will take funds and time. Efforts continue with the local and national government and Buryiat and CIS states to open the Zeltura border crossing to allow coal exports.

During the second quarter 2013, the Company incurred expenditures on the Ulaan Ovoo property, classified as costs in excess of impaired value, amounting to $0.7 million, which is reflected on the condensed interim consolidated statement of operations and comprehensive loss. As there were no benchmark or market changes from April 1, 2013 to June 30, 2013, the impaired value for Ulaan Ovoo within property and equipment, remains unchanged at a balance of $2 million (Note 9 to the unaudited condensed interim consolidated financial statements).

Pre-commercial operations for the period from commencement in November 2010 until the temporary shutdown which commenced in July 2012, to which shutdown is ongoing; along with project exploration and development costs were capitalized within the category 'Ulaan Ovoo Deferred Exploration Costs within the 'Property and Equipment' heading. Modest coal sales revenue from an existing stockpile along with associated costs to deliver the coal occurred during the interim period, including the first six months of 2013, post shutdown, and have been recorded as deferred exploration, within Property and Equipment. The ending coal stockpile inventory value at June 30, 2013 was $1.76 million ($2.4 million at December 31, 2012).
2013 Outlook: The Company continues to work toward realizing the full value of the Ulaan Ovoo property. It continues to - evaluate operating alternatives (e.g. electrification, conveyance vs. haul), infrastructure improvement, and management changes, investigate the domestic and export coal market to access higher volume and margin customers and new uses for Ulaan Ovoo coal, and pursue financial arrangements including strategic partner and joint venture arrangements or sale of part or whole of the project. Though management believes the domestic and export thermal coal market appears to be improving, Prophecy is unable to determine whether improvement will materialize and if so, be sustainable, and when, if at all, access to Russian coal markets will be opened, nor the extent of project changes and operational modifications required the potential value of the coal resources.

Chandgana Coal Properties, Mongolia

The Chandgana properties consist of the Chandgana Tal ("**Tal**") and Khavtgai Uul ("**Khavtgai**") (formerly named Chandgana Khavtgai) properties which are within nine kilometres of each other in the Nyalga Coal Basin in east central Mongolia which is approximately 280 kilometres east of Ulaanbaatar. On November 22, 2006 Prophecy Coal (then Red Hill) entered into a letter agreement with a private Mongolian company that set out the terms to acquire a 100% interest in the Tal property. On August 7, 2007, Prophecy Coal (then Red Hill) entered into a letter agreement with another private Mongolian company that set out the terms to acquire a 100% interest in the Khavtgai property. Under the terms of the Chandgana Khavtgai agreement, Prophecy Coal paid a total of US$570,000. On February 8, 2011, Prophecy Coal received a full mining license from the Mineral Resources Authority of Mongolia for the Tal property. The license can be updated to allow mining of 3.5 million tonnes per year to meet the demand of the Chandgana power plant within 90 days.

During 2007 Prophecy Coal performed geologic mapping, drilling and geophysical surveys of the Tal and Khavtgai properties. During June, 2010, Prophecy Coal completed a 13 drill hole, 2,373 metre resource expansion drilling program on the Khavtgai property, including 1,070 metres of core drilling, and five lines of seismic geophysical survey for a total of 7.4 line kilometres. Prophecy completed a 15 drill hole program during June-July 2011 to better define the coal resource of the Tal licenses.

An NI 43-101 technical report ("**Technical Report on the Coal Resources of the Chandgana Tal Coal Project Khentii Aimag, Mongolia**") dated September 11, 2007 was prepared by independent Qualified Person Mr. Gardar G. Dahl, Jr, P. Geo, a senior associate of Behre Dolbear & Company (USA), Inc. (the "Behre Dolbear Report"). Prophecy Coal engaged Leighton Asia LLC to prepare a scoping level mine study for the Tal property which was completed during December 2011. Later a preliminary economic assessment ("PEA") was prepared by John T. Boyd Co. and received November 2012 for the Tal licenses. An updated NI 43-101 technical report on the Khavtgai property ("**Updated Technical Report on the Coal Resources of the Chandgana Khavtgai Coal Resource Area, Khentii Aimag, Mongolia**") dated September 28, 2010 was completed by Christopher Kravits, LPG, CPG of Kravits Geological Services LLC (the "Khavtgai Report"). The Khavtgai Report updates the previous independent technical report on the Khavtgai property prepared by Mr. Kravits dated January 9, 2008. All the reports are filed on www.sedar.com. The resource and mining characteristics of the Chandgana Coal Properties are summarized in the following table:

Table 3. Coal resource details of the Chandgana Properties

Property	Coal Resources (million tonnes)			Life of Mine (years)	Strip Ratio (Bcm/t)	Coal Quality (arb)			
	Measured	Indicated	Total			Total Moisture (wt %)	Ash (wt %)	Gross Calorific Value (kcal/kg)	Total Sulfur (wt %)
Khavtgai	509.3	538.8	1,048.1	Not det	2.2:1	36.5	10.1	3,636	0.6
Tal	124.4	0.0	124.4	35+	0.7:1	40.9	10.8	3,306	0.6
Total/Weighted Avg	633.7	538.8	1,172.5		2.0:1	37.0	10.2	3,601	0.6

Coal quality is for the in-place coal. Strip ratio is the point strip ratio for Khavtgai and operating strip ratio for Tal.

The Khavtgai coal resource area contains a significant coal resource. The coal seams are thick and the strip ratio is low such that surface mining methods appear best suited to recover the coal. The coal is of moderate grade and low rank and appears suitable for use as a thermal coal but the large size of the resource and moderate grade suggest the resource may also be suitable for use as a conversion feedstock.

During 1st quarter 2013, Prophecy Coal incurred total costs of $625,037 (1Q 2012 - $1,835,929) for Chandgana coal properties. For 2nd quarter 2013 Prophecy incurred costs of $14,000.

Chandgana Power Plant Project, Mongolia

The Chandgana Power Plant Project area is next to the Baganuur to Undurkhaan paved road and within 150 kilometres of the Central Mongolian Railroad. The paved road and railroad can facilitate the transportation of construction equipment, power plant components and mining equipment. The Power Plant Project is within 150 kilometres of the Bagaanuur interconnect to the central electricity transmission grid and 50 kilometres to the Undurhaan interconnect to the eastern electricity transmission grid.

On November 15, 2010, Prophecy Coal reported that a Detailed Environmental Impact Assessment ("**DEIA**") pertaining to the construction of the Power Plant Project has been approved by the Mongolian Ministry of Nature and the Environment. The DEIA was prepared by an independent Mongolian environmental consulting firm which considered social and labour issues, climate and environmental circumstances specific to the proposed power plant. According to the study, there are no major impediments to the Power Plant Project. On November 15, 2011, Prophecy Coal's wholly-owned Mongolian subsidiary East Energy Development LLC. (now renamed as Prophecy Power Generation LLC),("**Prophecy Power**") received a license certificate from the Mongolian Energy Regulatory Authority (the "ERA") to construct a 600 MW (150 MW x 4) power plant at Chandgana. An English translation of the license was filed on Sedar at www.sedar.com on December 14, 2011.

On May 28, 2012, Prophecy Coal reported that it entered into a Cooperation Covenant (the "**Covenant**") with the ERA to bring the 600 MW Chandgana Power Project online by 2016. The ERA is the agency which implements governmental policy in the power and energy sector of Mongolia. The Covenant provides for the coventees to support the construction and operation of the Chandgana 600 MW mine-mouth power plant and its ability to supply the electricity to the central and eastern power grids of Mongolia by 2016. The Covenant also addresses the basic rights and obligations of Prophecy Coal, as the seller and the National Electricity Transmission Grid Company of Mongolia ("**NETGCO**") as the purchaser of the electrical energy.

On August 7, 2012 Prophecy Coal reported that since East Energy Development LLC (now Prophecy Power Generation LLC) obtained the construction licence in November, 2011, Prophecy Coal has been in on-going discussions with the Mongolian government to finalize a Power Purchase Agreement ("**PPA**"). The proposed PPA details the terms under which Prophecy Power would supply power to NETGCO and once executed will enable Prophecy Coal to seek project financing and begin construction. Prophecy Coal has also had numerous discussions with the Ministry of Natural Resources and Energy (now Ministry of Energy) to discuss technical and commercial issues., Prophecy Power formally submitted its PPA proposal to NETGCO on September 6, 2012 the highlights of which include:

- A designated concrete-pour date of April 2013 (reset to October 31 , 2013) and 1st phase operational date of 1Q 2016 (subject to conditions including but not limited to financing availability)
- A long term power off-take contract to ensure 24/7, uninterrupted dispatch power supply to the Mongolian grid
- Capacity and energy charge components in the tariff to cover fixed and variable costs respectively.

Prophecy Power has also been in discussions with several private Mongolian companies regarding entering into bilateral power purchase agreements for mining projects (copper, molybdenum and iron ore) and an industrial development complex (cement manufacture and smelter) in Mongolia.

In addition, on September 3, 2012, Prophecy Power submitted a Tariff Application to the Energy Regulatory Commission ("ERC"). Prophecy received official notice outlining the terms of the tariff agreement on May 17, 2013. The tariff includes:

- An initial tariff for the first year of the Power Project plant operation; and
- A weighted average tariff for the remaining 24 years of power plant operation.

The tariff numbers are in-line with PPG's final proposal submission to the Working Group on February 2013.

Prophecy Power has since received preliminary feedback from both ERC and NETGCO regarding its submissions and expects a definitive reply in the coming months. Prophecy Coal will also seek to supply power from the Power Plant Project to parts of eastern and northern Mongolia, and the capital city of Ulaanbaatar.

On March 5, 2013, the Company announced that Prophecy Power has been granted 532.4 hectares of land to be used for siting the Company's proposed Chandgana power plant (the "**Land Use Rights**"). With the Land Use Rights in place, Prophecy Power has entered into a contract to Erchim Concern LLC to bring 4MW of temporary power to the Chandgana Power Plant site from a local 35kV power line. Separately, Prophecy Power has issued tenders for the construction of 250 housing units along with a water supply to the Chandgana power plant site.

Prophecy Power entered into a Memorandum of Cooperation with Murum soum where the power plant will be located wherein both parties will support each other in areas of mutual concern such as infrastructure, cultural issues, social issues, education, and health issues. As a result, a scholarship program was initiated during 2012 and continues for those interested in obtaining a university degree. Also, Prophecy Coal supports certain cultural and social events.

Coal supply agreement: On June 5, 2013 PPG and Chandgana Coal executed a Coal Supply Agreement (CSA). The CSA calls for Chandgana Coal LLC, another Prophecy Coal wholly-owned Mongolian subsidiary, to supply 3.6 million tonnes of coal per year to Prophecy Power for 25 years. The initial coal price is USD17.70 per tonne which is competitive with Mongolian domestic thermal coal prices and is subject to annual price adjustments through indexing using the US Consumer Price Index, Mongolian Wage Index and Mongolian Diesel Price Index. The coal is to be mined from Chandgana Coal's Chandgana Tal mining licenses located two kilometres to the south of the proposed power plant location.

Engineering, procurement and construction (EPC) of power plant: During December 2011, Prophecy Power began seeking EPC contractors. Six tenders were received by the submission deadline of May 1, 2012 in the first round. For the second round in July 2012, Prophecy Power requested more detailed tenders which resulted in the shortlisting of three EPC contractors based on completeness of the tenders, construction capability, equipment quality, time to deployment, and price.

During August 2012, Prophecy Power's technical team, led by VP Sharma, a consultant to Prophecy Coal, who has 30 years of experience with China Light and Power Group, met with those firms qualifying for the second round. The team discussed detailed owner technical specifications and requirements, Mongolian customs, transport and insurance, tax, permit, labor policies, and project timeline in order to facilitate preparation of final tenders. This resulted in three full and complete tenders that were received in late September 2012.

In order to begin construction of the Chandgana Power Plant, Prophecy Coal must obtain significant additional financing. Prophecy Coal, directly or through its subsidiary Prophecy Power, is actively considering its financing options, which includes equity and debt project financing and joint ventures with international power project developers.

(Expressed in Canadian Dollars)

Prophecy Coal's goal is to secure developer sponsorship during 2013. Prophecy Power is also in discussions with EPC contractors to obtain funding through an equity stake and/or advanced credit line to meet targeted commencement of construction in 2013.

2013 Outlook: Prophecy continues to pursue the remaining permits required to proceed with the development of the Chandgana Power Plant. Prophecy Power also continues to pursue the significant financing which will be required to advance the project. With the terms of the tariff agreement established the remaining milestone is approval of the PPA which Prophecy continues to pursue.

Titan Property, Ontario, Canada

Prophecy Coal has an 80% interest in the Titan iron-titanium property ("**Titan**") located in Ontario province, Canada. Prophecy Coal has done much exploration work including 22 line kilometres of line cutting covering over 2.7 square kilometres in 100 metre intervals that extended the current surveyed grid west and southwest of the Titan property. A ground magnetometer survey was completed during the summer of 2010, the results of which expanded the extent of the magnetic anomaly associated with the Titan deposit. This work successfully demonstrated that exploration is warranted outside the previously known limits. Modest assessment work is planned for 2013.

Kanichee Property, Ontario, Canada

Prophecy holds a 100% interest in the surface rights of Kanichee located in Streathy Township, 375 km north of Toronto, Ontario. Kanichee consists of 15 mineral claims covering 583 acres that include surface and underground mine workings. The property includes copper and nickel mineralization associated with two dykes. No assessment work is currently planned.

Okeover Property, British Columbia, Canada

The 60% interest of Okeover, a copper-molybdenum project in south-western British Columbia, Canada, 25 kilometres north of Powell River and 145 kilometres northwest of Vancouver, was acquired through the amalgamation between Red Hill and Prophecy Coal Holdings Inc. in April 2010. Exploration done so far suggests mineralization exists east, west and south of the known mineralized body. Modest assessment work is planned for 2013 to test the suggested mineralized areas.

4. SUMMARY OF QUARTERLY RESULTS

The following table summarizes selected financial information for the eight most recently completed quarters:

	2013		2012	
	Jun-30	Mar-31	Dec-31	Sep-30
Operating expense	(793,281)	(794,913)	$ (1,069,354)	$ (2,970,363)
Loss Before Other Items and Deferred Income Tax	(793,281)	(794,913)	(1,069,354)	(2,970,363)
Other items	(2,771,104)	(2,817,653)	(46,585,365)	(2,328,747)
Loss Before Deferred Income Tax	(3,564,385)	(3,612,566)	(47,654,718)	(5,299,110)
Deferred income tax recovery	-	-	(1,569,024)	160,247
Net Income (Loss) for Quarter	(3,564,385)	(3,612,566)	(49,223,742)	(5,138,863)
Fair value gain (loss) on available-for-sale investments	(333,639)	781,484	2,476,797	688,744
Comprehensive Income (Loss) for Quarter	(3,898,023)	(2,831,081)	(46,746,945)	(4,450,119)
Net Income (Loss) for Quarter Attributable to:				
Owners of the Company	(3,564,385)	(3,612,566)	(48,831,202)	(3,242,577)
Non-controlling interest	-	-	(879,254)	(1,409,573)
	(3,564,385)	(3,612,566)	(49,710,456)	(4,652,150)
Comprehensive Loss for Quarter Attributable to:				
Owners of the Company	(3,898,023)	(2,831,081)	(44,266,921)	(2,961,989)
Non-controlling interest	-	-	(804,911)	(1,647,892)
	$ (3,898,023)	$ (2,831,081)	$ (45,071,832)	$ (4,609,880)

(Expressed in Canadian Dollars)

Share Information				
Net Loss per share, basic and diluted attributable to:				
Owners of the Company	$ (0.02)	$ (0.02)	$ (0.22)	$ (0.01)
Non-controlling interest	(0.00)	(0.00)	(0.00)	(0.01)
Comprehensive Loss per share, basic and diluted attributable to:				
Owners of the Company	(0.02)	(0.01)	(0.21)	(0.01)
Non-controlling interest	(0.00)	(0.00)	(0.00)	$ (0.01)
Average number of common shares outstanding for quarter, basic and diluted	236,490,814	229,547,023	228,379,503	227,407,328

	2012		2011	
	Jun-30	Mar-31	Dec-31	Sep-30
Operating expense	$ (2,474,327)	$ (4,334,233)	$ (3,206,240)	$ (5,196,343)
Loss Before Other Items and Deferred Income Tax	(2,474,327)	(4,334,233)	(3,206,240)	(5,196,343)
Other items	1,439,189	(1,710,416)	2,199,362	494,235
Loss Before Deferred Income Tax	(1,035,138)	(6,044,649)	(1,006,878)	(4,702,107)
Deferred income tax recovery	(68,176)	121,461	448,687	-
Net Loss for Quarter	(1,103,314)	(5,923,188)	(558,191)	(4,702,107)
Fair value gain (loss) on available-for-sale investments	(2,114,759)	872,987	(240,610)	(808,025)
Comprehensive Income (Loss) for Quarter	(3,218,073)	(5,050,201)	(798,801)	(5,510,132)
Net Income (Loss) for Quarter Attributable to:				
Owners of the Company	(289,024)	(4,513,569)	567,571	(3,233,347)
Non-controlling interest	(814,290)	(1,409,619)	(1,125,761)	(1,468,760)
	(1,103,314)	(5,923,188)	(558,191)	(4,702,107)
Comprehensive Loss for Quarter Attributable to:				
Owners of the Company	(4,638,569)	(3,166,111)	425,073	(4,041,372)
Non-controlling interest	(94,856)	(1,884,090)	(1,223,872)	(1,468,760)
	$ (4,733,425)	$ (5,050,201)	$ (798,801)	$ (5,510,132)
Share Information				
Net Loss per share, basic and diluted attributable to owners of the Company				
Owners of the Company	$ (0.00)	$ (0.02)	$ 0.00	$ (0.02)
Non-controlling interest	(0.00)	(0.01)	(0.01)	(0.01)
Comprehensive Loss per share, basic and diluted attributable to owners of the Company				
Owners of the Company	(0.02)	(0.02)	0.00	(0.02)
Non-controlling interest	$ (0.00)	$ (0.01)	$ (0.01)	$ (0.01)
Average number of common shares outstanding for quarter, basic and diluted	225,071,203	199,587,605	195,035,960	195,008,886

Prior to December 1, 2012, Prophecy Platinum's results of operations were consolidated into the statement of operations and comprehensive loss while thereafter the proportional share of Prophecy Platinum's net loss was reflected in the Share of Loss of an Associate line item on the statements of operations and comprehensive loss (Note 15 to the Audited Consolidated Financial Statements).

The Company's quarterly general and administrative expenses remain relatively stable. Factors causing significant changes between the most recently completed eight quarters have primarily been items such as share-based payments expense, consulting and management fees, and advertising and promotion expense.

The increase in other items in the fourth fiscal quarter of 2012 was mainly due to an impairment loss of $47.1 million, an impairment loss on available-for-sale investments of $2.6 million, a deferred income tax expense of $1.4 million, offset by a gain on deconsolidation of Prophecy Platinum of $4.4 million.

(Expressed in Canadian Dollars)

The decrease in operating expenses in the first and second quarters of 2013 was mainly due to a decrease in salaries and benefits, advertising and promotion, and professional fees. For the three month period ended June 30, 2013, the Company recorded $0.7 million of costs in excess of impaired value on its Ulaan Ovoo property.

5. DISCUSSION OF OPERATIONS

Three Months Ended June 30, 2013 and 2012 (Q2 2013 and Q2 2012)

The information described below is accounted for in accordance with IFRS. The reader is encouraged to refer to Note 6 of Prophecy Coal's Audited Consolidated Financial Statements for the year ended December 31, 2012 for Prophecy Coal's IFRS accounting policies.

Prior to December 1, 2012, Prophecy Platinum's results of operations were consolidated into the statement of operations and comprehensive loss while thereafter the proportional share of Prophecy Platinum's net loss was reflected in the Share of Loss of an Associate line item on the statements of operations and comprehensive loss (Note 15 to the Audited Consolidated Financial Statements).

For the three months ended June 30, 2013, Prophecy Coal incurred a net loss of $3.5 million ($0.02 per share) compared to a $1.1 million net loss ($Nil per share) incurred for the three months ended June 30, 2012. The decrease by $2.4 million in net loss was mainly due to deconsolidation of Prophecy Platinum's results on November 30, 2012 and the deemed disposition loss on associate.

	Q2 2013	Q2 2012	Discussion
Advertising and promotion	$52,601	$519,251	Advertising and promotion expense decreased in Q2 2013 by $466,650, of which $287,200 was attributable to Prophecy Platinum no longer being consolidated as at November 30, 2012. The decrease was also due to a reduction of promotion carried out by the Company in Q2 2013.
Consulting and management fees	$28,353	$274,436	Consulting and management fees also include fees charged by officers of the Company and its subsidiaries. In Q2 2013, consulting and management fees decreased by $246,083, of which $110,600 were attributable to Prophecy Platinum no longer being consolidated as at November 30 2012.
Depreciation	$21,014	$42,545	Depreciation decreased by $21,531, as equipment was on standby.
Director fees	$50,498	$70,758	In Q2 2013, director fees decreased by $20,260, of which $10,500 was attributable to Prophecy Platinum no longer being consolidated as at November 30, 2012.
Insurance	$43,216	$53,232	There was no material change in insurance expense.
Office and	$23,828	$79,919	In Q2 2013, office and administration decreased by

(Expressed in Canadian Dollars)

administration			$56,091, of which 50% was attributable to Prophecy Platinum deconsolidated on November 30, 2012.
Professional fees	$257,459	$248,316	In Q2 2013, professional fees were approximately the same as in Q2 2012.
Salaries and benefits	$124,225	$372,941	The decrease in salaries and benefits by $248,716 was mainly due to decrease in number of employees.
Share-based payments	$135,347	$668,037	It is a non-cash expense and represents the estimated fair value of share options vested during the period. It is accounted for at fair value as determined by the Black-Scholes Option Pricing model and varies from period to period based on the number and valuation of the share options granted during the period, vesting provisions, and amortization schedule of the previously granted share options. In Q2 2013 share-based payment expense decreased by $532,690, of which $260,300 was attributable to Prophecy Platinum no longer being consolidated as at November 30, 2012. In Q2 2013, Prophecy Coal incurred $135,347 in share-based payment expense which is net of $23,012 that was capitalized to Ulaan Ovoo and PPA.
Stock exchange and shareholder services	$22,831	$49,268	In Q2 2013, stock exchange and shareholder services decreased by $26,437, of which $6,500 was attributable to Prophecy Platinum no longer being consolidated as at November 30, 2012.
Travel and accommodation	$33,907	$95,625	In Q2 2013, travel expense decreased by $61,718, of which $49,600 was attributable to Prophecy Platinum no longer being consolidated as at November 30, 2012.
Costs in excess of impaired value	$712,457	$Nil	The Company expensed Ulaan Ovoo property expenditures incurred in the quarter ending June 30, 2013, as costs in excess of impaired value.
Foreign exchange gain	$72,405	$198,897	The foreign exchange gain was due primarily to the translation of net monetary assets denominated in Mongolian tugrik to the Canadian dollar. The decrease in loss was due to fluctuations in the value of the Canadian dollar compared to the Mongolian tugrik and the United States dollar.
Interest expense	$632,649	$1,089	The increase in interest expense was mainly due to the interest charges at 25% effective interest rate

(Expressed in Canadian Dollars)

			on the $10 million Waterton loan, which was not outstanding in the comparable 2012 quarter.
Interest income	$4,313	$17,156	Interest income was earned on funds raised during the quarter and invested in short-term interest bearing accounts.
Loss (gain) on sale of investments	$(19,545)	$100,147	Minor gains loss of sales of investments
Mineral property written off	$Nil	$190,980	In Q2 2012 the Company terminated the Ilch Khujirt option as it is not a core asset to the Company. The Company recorded an impairment of $190,980 at June 30, 2012 for the full carrying amount of the property.
Share of loss of an associate	$399,930	$Nil	The Company's interest in Prophecy Platinum, commencing on December 1 2012, is reported using the equity accounting method. The share of loss of an associate amount represents the Company's ownership interest applied to the net loss of Prophecy Platinum for the three months ended June 30, 2013 (Note 9 to the condensed interim consolidated financial statements).
Deemed disposal Loss of associate	$1,122,329	$Nil	The Company's ownership percentage decreased in Prophecy Platinum as a result of a private placement by Prophecy Platinum that the Company did not participate in. As a result, a deemed disposition for a loss was recognized for the three months ended June 30, 2013.

Six Months Ended June 30, 2013 and 2012

The information described below is accounted for in accordance with IFRS. The reader is encouraged to refer to Note 6 of Prophecy Coal's Audited Consolidated Financial Statements for the year ended December 31, 2012 for Prophecy Coal's IFRS accounting policies.

Prior to December 1, 2012, Prophecy Platinum's results of operations were consolidated into the statement of operations and comprehensive loss while thereafter the proportional share of Prophecy Platinum's net loss was reflected in the Share of Loss of an Associate line item on the statements of operations and comprehensive loss (Note 15 to the Audited Consolidated Financial Statements).

For the six months ended June 30, 2013, Prophecy Coal incurred a net loss of $7.2 million ($0.03 per share) compared to a $7.0 million net loss ($0.03 per share) incurred for the six months ended June 30, 2012.

(Expressed in Canadian Dollars)

	June 30, 2013	June 30, 2012	Discussion
Advertising and promotion	$111,616	$1,238,854	Advertising and promotion expense decreased in the six months ended June 30, 2013 by $1,127,238 of which $613,700 was attributable to Prophecy Platinum no longer being consolidated as at November 30, 2012. The decrease was also due to a reduction of promotion carried out by the Company in 2013.
Consulting and management fees	$56,405	$568,402	Consulting and management fees also include fees charged by officers of the Company and its subsidiaries. In the six months ended June 30, 2013 consulting and management fees decreased by $511,997, of which $213,600 were attributable to Prophecy Platinum no longer being consolidated as at November 30 2012.
Depreciation	$43,703	$112,231	Depreciation decreased by $68,528.
Director fees	$96,251	$139,908	In the six months ended June 30, 2013, director fees decreased by $43,657, of which $22,000 was attributable to Prophecy Platinum no longer being consolidated as at November 30, 2012.
Insurance	$95,170	$105,114	There was no material change in insurance expense.
Office and administration	$35,809	$156,491	In the six months ended June 30, 2013, office and administration decreased by $120,682, of which 50% was attributable to Prophecy Platinum deconsolidated on November 30, 2012.
Professional fees	$360,023	$500,041	In the six months ended June 30, 2013, professional fees decreased by $140,018, $155,200 of which was attributable to Prophecy Platinum no longer being consolidated as at November 30, 2012. The decrease was also due to a reduction of legal expenses.
Salaries and benefits	$324,461	$506,714	The decrease in salaries and benefits by $182,253 was mainly due to decrease in number of employees.
Share-based payments	$335,499	$3,129,274	It is a non-cash expense and represents the estimated fair value of share options vested during the period. It is accounted for at fair value as determined by the Black-Scholes Option Pricing model and varies from period to period based on

(Expressed in Canadian Dollars)

			the number and valuation of the share options granted during the period, vesting provisions, and amortization schedule of the previously granted share options. In the six months ended June 30, 2013 share-based payment expense decreased by $2,793,775, of which $2,455,500 was attributable to Prophecy Platinum no longer being consolidated as at November 30, 2012. In the six months ended June 30, 2013, Prophecy Coal incurred $335,499 in share-based payment expense which is net of $64,285 that was capitalized to Ulaan Ovoo and PPA.
Stock exchange and shareholder services	$69,457	$158,090	In the six months ended June 30, 2013, stock exchange and shareholder services decreased by $88,633, of which $41,500 was attributable to Prophecy Platinum no longer being consolidated as at November 30, 2012.
Travel and accommodation	$59,798	$193,442	In the six months ended June 30, 2013, travel expense decreased by $133,644, of which $112,600 was attributable to Prophecy Platinum no longer being consolidated as at November 30, 2012.
Costs in excess of impaired value	$2,765,560	$Nil	The Company expensed Ulaan Ovoo property expenditures incurred in the quarter ending June 30, 2013, as costs in excess of impaired value.
Foreign exchange loss (gain)	$(375,664)	$1,557,411	The foreign exchange gain was due primarily to the translation of net monetary assets denominated in Mongolian tugrik to the Canadian dollar. The decrease in loss was due to fluctuations in the value of the Canadian dollar compared to the Mongolian tugrik and the United States dollar.
Interest expense	$1,247,743	$57,600	The increase in interest expense was mainly due to the interest charges at 25% effective interest rate on the $10 million Waterton loan, which was not outstanding in the comparable 2012 quarter.
Interest income	$24,410	$37,031	Interest income was earned on funds raised during the quarter and invested in short-term interest bearing accounts.
Loss (gain) on sale of investments	$(19,545)	$17,619	Minor gains loss of sales of investments

(Expressed in Canadian Dollars)

Mineral property written off	$Nil	$190,980	In the six months ended June 30, 2012 The Company terminated the Ilch Khujirt option as it is not a core asset to the Company. The Company recorded an impairment of $190,980 at June 30, 2012 for the full carrying amount of the property.
Share of loss of an associate	$872,741	$Nil	The Company's interest in Prophecy Platinum, starting December 1 2012, is reported using the equity accounting method. The share of loss of an associate amount represents the Company's ownership interest applied to the net loss of Prophecy Platinum for the six months ended June 30, 2013 (Note 9 to the condensed interim consolidated financial statements).
Deemed disposal Loss of associate	$1,122,329	$Nil	The Company's ownership percentage decreased in Prophecy Platinum as a result of a private placement by Prophecy Platinum that the Company did not participate in. As a result, a deemed disposition for a loss was recognized for the six months ended June 30, 2013.

6. LIQUIDITY AND CAPITAL RESOURCES

Prophecy Coal as at June 30, 2013 had a working capital deficiency, including restricted cash, of $2.25 million (December 31 2012: working capital surplus of $0.1 million) and will require additional sources of funding for ongoing operations, to continue to develop its Ulaan Ovoo coal property, and to potentially develop the Chandgana Power Plant project. Additional sources of funding, which may not be available at favourable terms, if at all, include: share equity and debt financings; dispositions of Prophecy Platinum Corp. common shares held as an investment in associate (Note 8 to the unaudited condensed interim consolidated financial statements); coal sales from stockpile inventory; equity, debt or property level joint ventures with power project and coal property developers; and sale of interests in existing assets.

The Company's exploration activities are subject to government legislation, policies and controls relating to prospecting, development, production, environmental protection, mining taxes and labour standards. In order for the Company to carry out its exploration activities, the Company is required to hold certain permits. There is no assurance that the Company's existing permits will be renewed or that new permits that have been applied for will be granted.

Major expenditures are required to locate and establish resources, ore reserves, to develop metallurgical processes and to construct mining and processing facilities at a particular site. The recoverability of valuations assigned to exploration and evaluation mineral properties are dependent upon discovery of economically recoverable reserves, the ability to obtain necessary financing to complete exploration, development and future profitable production or proceeds from disposition.

Management reviews the carrying value of the Company's interest in each property and where necessary, exploration and evaluation mineral properties are written down to their estimated recoverable amount or written off. Although management has made its best estimate of these factors, it is reasonably possible that certain events could adversely affect management's estimates of recoverable amounts and the need for, as well as, the amount of provision for impairment in the carrying value of exploration properties and related assets.

Many factors influence the Company's ability to raise funds, and there is no assurance that the Company will be successful in obtaining adequate financing and at favourable terms for these or other purposes including general working capital purposes. Prophecy Coal's unaudited condensed interim consolidated financial statements have been prepared on a going concern basis, which contemplates the realization of assets and settlement of liabilities in the normal course of business for the foreseeable future. Realization values may be substantially different from carrying values, as shown, and these unaudited condensed interim consolidated financial statements do not give effect to the adjustment that would be necessary to the carrying values and classifications of assets and liabilities should Prophecy Coal be unable to continue as a going concern.

6.1 Working Capital

As at November 30, 2012, the Company no longer consolidates the operating results of Prophecy Platinum in the Company's statements of operations and statements of cash flows. The statements of financial position line items as at December 31, 2012 and June 30, 2013 exclude the assets and liabilities of Prophecy Platinum, which are consolidated in prior quarters.

At June 30, 2013, Prophecy Coal had approximately $0.4 million, cash and cash equivalents and $0.5 million comprised of held private placement funds and short term investments in the form of Guaranteed Investment Certificates with the Bank of Montreal. The Company's working capital has decreased by $2.35 million since the year ended December 31, 2012 due to a decrease in current assets by $2 million (primarily relates to a decrease in short term investments and inventories) and increase in current liabilities by $0.4 million.

As at the date of this report, the Company's working capital deficit is approximately $2.9 million.

The Company raised $0.6 million in April 2013 and $1.1 million in June 2013 through a non-brokered private placement announced on February 7, 2013.

In July 2012, Prophecy Coal arranged the Loan of $10 million with Waterton. The Loan has a one year term, due July 16, 2013, and bears interest at 14% per annum payable monthly with an effective interest rate, when including fees, of 25%. In connection with the Loan, a structuring fee of 2.5% ($250,000) was paid to Waterton in cash and legal fees of $189,805 were paid. Pursuant to the terms of the Loan, Prophecy Coal issued for a value of $600,000, 2,735,617 common shares of Prophecy Coal on closing of the Loan at July 16, 2012 (Note 11 to the unaudited condensed interim consolidated financial statements).

Pursuant to the Tugalgatai Property Agreement, US $10 million was deposited in escrow in July 2012 and classified as restricted cash. During October 2012 the remaining funds, net of costs, amounting to US $9.9 million were returned to Prophecy Coal on termination of the Tugalgatai Agreement, which occurred in October 2012, due to the elapsing of the initial long stop date for approval of the licences transfer by the Minerals Resource Authority of Mongolia. Under the July 16, 2012 credit agreement between Prophecy Coal and Waterton, the expiry of the original purchase and sales agreement with Tethys constituted a default. Subsequent to the 2012 year end, in February 2013 Waterton agreed to waive the default, subject to certain conditions (see Notes 19 and 31 of the annual audited consolidated financial statements) one of which is the Company setting aside $1.5 million in escrow (completed) for the purchase of the Tugalgatai licenses. The full conditions which have been met are as follows:

(a) setting aside $3.5 million in escrow for the following purposes:

1) $1.5 million for the acquisition of the Mongolian coal assets and
2) $2 million for the full repayment or a partial prepayment of the 2012 Loan,

(b) issuing 2 million common shares to Waterton; and
(c) pledging additional security to Waterton in the form of 5,535,000 remaining free trading Prophecy Platinum common shares, (Notes 19 and 31 to the Audited Consolidated Financial Statements).

On July 15, 2013 the Company entered into the Amended Loan Agreement with Waterton pursuant to which Prophecy Coal has agreed to and completed the partial pay down of the principal loan amount from $10 million to $6.5 million from restricted cash-on-hand amounting to $3.5 million and extending the maturity date from July 16, 2013 to October 31, 2013. The Amended Loan Agreement facility is a non-revolving facility, and any repayment under the facility is not available for re-borrowing.

(Expressed in Canadian Dollars)

As consideration, Prophecy Coal shall pay Waterton, in cash, a non-refundable restructuring fee in 4 equal, consecutive, monthly instalment payments (each, a "**Restructuring Instalment**"). Each Restructuring Instalment shall be in an amount equal to two percent (2%) of the outstanding principal of the Loan as of the date of the execution of the Amendment. The Restructuring Instalments shall be due and payable on the following dates: the date of the execution of the Amendment (paid); August 29, 2013; September 27, 2013; and October 31, 2013. No Restructuring Instalment(s) will be due or payable following repayment, in full, by Prophecy to Waterton, of all amounts owing under the Amended Loan Agreement. For example, if Prophecy Coal repays all amounts owing under the Amended Loan Agreement in full on September 15, 2013, then Prophecy Coal will not have to pay Waterton the Restructuring Instalments due and payable on September 27, 2013 or October 31, 2013.

As additional consideration, each prepayment and repayment in full or in part of the principal amount outstanding under the Amended Loan Agreement must be increased as follows:

(iv) if such payment is of the entire outstanding principal amount of the Loan, Prophecy Coal shall pay to Waterton an amount in cash equal to the quotient of the entire amount outstanding under the Loan and the applicable Discount Metric (as set out below); and

(v) if such payment is a partial payment of the outstanding amount of the Loan, Prophecy Coal shall pay Waterton an amount in cash equal to the quotient of the partial payment amount and the applicable Discount Metric;

(vi) where "Discount Metric" means (i) 1.00 from the date of the Amendment up to and including August 16, 2013;(ii) 0.98 from August 17, 2013 up to and including August 31, 2013; (iii) 0.96 for the calendar month of September, 2013; and (iv) 0.94 for the calendar month of October, 2013.

Prophecy Coal had no long-term debt outstanding at June 30, 2013, other than provision for closure and reclamation of $0.3 million relating to its Ulaan Ovoo property. The Company has no capital lease obligations, operating leases (other than office leases) or any other long term obligations.

At the date of this MD&A Prophecy Coal holds for investment purposes 30 million common shares of Victory Nickel Inc. acquired in a reciprocal private placement and 22 million common shares of its 29% owned associate company, Prophecy Platinum, (TSXV:NKL) acquired in connection with the June 2011 spin out transaction (these common shares were pledged as collateral in connection with the Waterton loan). The aggregate market value of available for sale Prophecy Coal's marketable securities (including the 22 million pledged shares in Prophecy Platinum) is approximately $12.6 million. The market value of such shares is subject to fluctuation.

6.2 Cash Flow Highlights

		Six months ended June 30,	
		2013	2012
Cash used in operating activities	$	(5,309,597) $	(3,196,504)
Cash provided by (used in) investing activities		3,066,581	(13,125,036)
Cash provided by financing activities		1,851,426	14,166,593
Increase (decrease) in cash for period		(391,587)	(2,154,947)
Cash balance, beginning of period		768,831	3,480,050
Cash balance, end of period	$	377,244 $	1,325,103

6.3 Cash Flows for the six months ended June 30, 2013 and 2012

Operating activities: Cash used in operating activities was $5.3 million in the six months ended June 30, 2013 compared to cash used of $3.2 million in the same period of 2012. The increase in cash used in operating activities by $2.1 million was mainly due to the transfer of $3.5 million from Guaranteed Investment Certificate account to restricted cash (see Note 6.1) offset by a reduction in general and administration expenses of $2.5 million.

Investing activities: Cash generated from investing activities was $3.1 million (same period last year – cash used $13.1 million), of which $3.5 million was deposited to restricted cash as per Waterton waiver agreement, $0.55 million (same period last year $7.1 million) was related to the acquisition of property and equipment, $0.9 million (same period last year - $8.8 million) was used for exploration expenditures incurred at Prophecy Coal's mineral properties, $0.1 million (same period last year - $Nil) was spent on purchase of Prophecy Platinum shares. In the six months ended June 30 2013 $0.04 million (same period last year - $2.8 million) was received by Prophecy Coal (and by Prophecy Platinum in the same period last year) from sale of available-for-sale investments.

Financing activities: A total of $1.9 million cash was received from financing activities in the six months ended June 30, 2013 compared to $14.2 million received in the six months ended June 30, 2012. $1.4 million was received from a private placement compared to $14.2 million received from private placements in the same period of 2012. During six months ended June 30, 2013, the Company paid $0.7 million interest charges related to the Waterton loan.

6.4 Contractual Commitments

Prophecy Coal's commitments related to the Waterton loan are disclosed in Note 11 to the unaudited condensed interim consolidated financial statements and in section 6.1 Working Capital.

6.5 Capital Risk Management

Prophecy Coal considers its capital structure to consist of share capital, share options and warrants. Prophecy Coal manages its capital structure and makes adjustments to it, based on the funds available to Prophecy Coal, in order to support the acquisition and exploration of mineral properties. The Board of Directors does not establish quantitative returns on capital criteria for management.

The properties in which Prophecy Coal currently has an interest are in the exploration stage; as such, Prophecy Coal is dependent on external financing to fund its activities. In order to carry out the planned exploration and development and pay for administrative costs, Prophecy Coal will spend its existing working capital and raise additional amounts as needed.

Management reviews its capital management approach on an ongoing basis and believes that this approach, given the relative size of Prophecy Coal, is reasonable. There were no changes in Prophecy Coal's approach to capital management during the six months ended June 30, 2013. Neither Prophecy Coal nor its subsidiaries are subject to externally imposed capital requirements. Prophecy Coal's investment policy is to invest its surplus cash in highly liquid short-term interest-bearing investments with maturities of 90 days or less from the original date of acquisition, all held with major Canadian financial institutions.

7. ENVIRONMENT

Prophecy Coal is subject to the Environmental Protection Law of Mongolia (the "**EPL**") and has the following duties with respect to environmental protection:

- To comply with the EPL and the decision of the government, local self-governing organizations, local governors and Mongolian state inspectors;
- To comply with environmental standards, limits, legislation and procedures and to supervise their implementation with their organization;
- To keep records on toxic substances, adverse impacts, and waste discharged into the environment; and
- To report on measures taken to reduce or eliminate toxic chemicals, adverse impacts, and waste.

In addition to those duties imposed on them by the EPL, mining license holders are required to prepare an initial environment impact assessment analysis before the mine comes into production. The mining license holders must also annually develop and implement an environmental protection plan (including reclamation measures) in co-operation with the Ministry of Nature, Environment and Tourism which should take into account the results of the environmental impact assessment.

Prophecy Coal received approval of its detailed Environmental Impact Assessment and Environmental Protection Plan from the Mongolian Ministry of Nature and Environment for mining operations at its Ulaan Ovoo mine in 2010. Prophecy Coal has implemented a number of internal policies to embrace responsibility for the impact of its business activities on the environment. By conducting studies, carefully designing mine plans, implementing pollution control recommendations from internal and external sources, monitoring the effects of mining on mining areas and carefully designing mine closure plans, Prophecy Coal seeks to minimize the impact of our activities on the environment.

Prophecy Coal established an environmental policy in 2008. The environmental policy affirms Prophecy Coal's commitment to environmental protection. Prophecy Coal monitors its operations to ensure that it complies with all applicable environmental requirements, and takes actions to prevent and correct problems if needed.

Closure and reclamation liability results from the development, construction and ordinary operation of mining property, plant and equipment and from environmental regulations set by regulatory authorities. The liability includes costs related to removal and/or demolition of mine equipment, buildings and other infrastructure, removing contaminated soil, protection of abandoned pits and re-vegetation.

At June 30, 2013, Prophecy Coal had a provision for closure and reclamation liability of $294,263 (December 31, 2012 - $294,263). The fair value of the closure and reclamation liability is estimated using a present value technique and is based on existing laws, contracts or other policies and current technology and conditions (Note 20 of the Audited Consolidated Financial Statements).

8. RELATED PARTY DISCLOSURES

Details of transactions between Prophecy Coal and other related parties are disclosed below.

Prophecy Coal had related party transactions with the following companies, related by way of directors and key management personnel:

(a) Cantech Capital Corporation, a private company owned by Donald Gee, a former director of Prophecy Platinum, provided consulting and management services.

(b) Elysian Enterprises Inc., a private company owned by David Patterson, a former director of Prophecy Platinum, provided consulting and management services.

(c) Energy Investment Capital, a private company owned by Jivko Savov, former Director of Prophecy Coal, provided consulting services to the Company.

(d) JWL Investment Corp., a private company owned by Joseph Li, former General Manager, Corporate Secretary and Director of Prophecy Coal and Prophecy Platinum, provided management services to the Company.

(Expressed in Canadian Dollars)

(e) Linx Partners Ltd., a private company controlled by John Lee, Director, Interim CEO and Executive Chairman of Prophecy Coal, and a Director and former Chairman and CEO of Prophecy Platinum, provides management and consulting services for Prophecy Coal and Director services for Prophecy Platinum.

(f) MaKevCo Consulting Inc., a private company 50% owned by Greg Hall, Director of Prophecy Coal and Prophecy Platinum, provides consulting and management services to the Company.

(g) The Energy Gateway Ltd., a private company owned by former Director Paul Venter, provided consulting and management services.

The Company's related party disclosure includes Prophecy Platinum's related party transactions during the six months ended June 30, 2012. Prior to December 1, 2012, Prophecy Platinum's net assets and operations were consolidated into the financial statements of Prophecy Coal. On November 30, 2012, it was determined that Prophecy Coal's control changed to significant influence over Prophecy Platinum, and therefore, since December 1, 2012, the value of those amounts were reflected as an Investment in Associate using the equity accounting method (Note 8 to the condensed interim financial statements).

On June 4, 2013, John Lee, the interim CEO, subscribed for 1,000,000 of the Company's common shares. In lieu of paying cash in the amount of $140,000 (1,000,000 shares at $0.14 per share), he transferred to the Company 202,989 shares of Prophecy Platinum (which were valued effective at $0.69 per share).

A summary of related party general and administrative expenses is as follows:

Related parties	Three months ended June 30, 2013	Three months ended June 30, 2012	Six months ended June 30, 2013	Six months ended June 30, 2012
Cantech Capital Corp. (a)	$ -	$ 2,500	$ -	$ 5,000
Directors and officers	79,271	94,527	166,227	172,860
Elysian Enterprises Inc. (b)	-	2,000	-	5,000
Energy Investment Capital (c)	-	-	-	26,239
JWL Investments Corp. (d)	-	42,000	-	84,000
Linx Partners Ltd. (e)	105,003	149,862	210,006	299,862
MaKevCo Consulting Inc. (f)	17,900	17,500	39,300	62,000
The Energy Gateway (g)	-	19,789	-	51,991
	$ 202,174	$ 328,179	$ 415,533	$ 706,952

A summary of the expenses by nature among the related parties is as follows:

Related parties	Three months ended June 30, 2013	Three months ended June 30, 2012	Six months ended June 30, 2013	Six months ended June 30, 2012
Consulting and management fees	$ 10,503	$ 232,362	$ 21,006	$ 502,284
Directors' fees	50,471	69,777	96,223	138,927
Mineral properties	73,500	9,895	147,000	25,996
Property and equipment	21,000	9,895	42,000	25,996
Salaries and benefits	46,700	6,250	109,304	13,750
	$ 202,174	$ 328,179	$ 415,533	$ 706,952

As at June 30, 2013, the amount included within accounts payable and accrued liabilities, which was due to related parties, consisted of amounts owing to directors for fees totalling $18,493 (December 31, 2012 – $53,334) and reimbursable expenses, and consulting fees for managing the mineral properties and power project.

(Expressed in Canadian Dollars)

Transactions with subsidiaries and associates

Transactions between the Company and its subsidiaries are eliminated on consolidation; therefore, they are not disclosed as related party transactions. Prophecy Coal shares administrative assistance and office space, and previously shared management with Prophecy Platinum pursuant to a one year Service Agreement for 2012, consisting of fixed monthly fees of $40,000, subject to periodic review. Prophecy Coal recovers costs for services rendered to Prophecy Platinum and expenses incurred on behalf of Prophecy Platinum. As at June 30, 2013 an estimated amount of $156,729 was due from Prophecy Platinum for shared office costs.

Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the Company, including directors of the Company.

	Three months ended June 30,		Six months ended June 30,	
Key Management Personnel	2013	2012	2013	2012
Salaries and short term benefits	$ 153,432	$ 288,527	$ 323,008	$ 560,354
Share-based payments	84,843	16,905	204,407	116,666
	$ 238,275	$ 305,432	$ 527,415	$ 677,020

Included in the key management personnel compensation are John Lee's (interim CEO) compensation payments of $210,006, of which $189,005 was capitalized to the Ulaan Ovoo and Prophecy Power Generation projects for the period of January 1, 2013 – June 30, 2013.

9. CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS

Critical accounting estimates used in the preparation of the condensed interim consolidated financial statements include determining the carrying value of mineral properties exploration and evaluation projects and property and equipment, assessing the impairment of long-lived assets, determination of environmental obligation provision for closure and reclamation, determining deferred income taxes, and the valuation of share-based payments. These estimates involve considerable judgment and are, or could be, affected by significant factors that are out of Prophecy Coal's control.

Readers are encouraged to read the significant accounting policies and estimates as described in Prophecy Coal's Audited Consolidated Financial Statements for the year ended December 31, 2012 (Note 5 to the Audited Consolidated Financial Statements). Prophecy Coal's condensed interim consolidated financial statements have been prepared using the going concern assumption see Note 1 to the Company's condensed interim consolidated financial statements.

Significant accounting judgments and estimates

The preparation of financial statements in conformity with IFRS 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 revenues and expenses during the reporting period. Areas requiring the use of estimates include the rates of amortization for property and equipment, the useful life and recoverability of long-lived assets, the recoverability of accounts receivable, determination of environmental obligation provision for closure and reclamation, accounts payable and accrued liabilities, the assumptions used in the determination of the fair value of financial instruments and share-based payments, and the determination of the recoverability of deferred income tax assets. Prophecy Coal bases its estimates and assumptions on current and various other factors that it believes to be reasonable under the circumstances. Management believes the estimates are reasonable; however, actual results could differ from those estimates and could impact future results of operations and cash flows. The critical judgments and estimates applied in the preparation of the company's unaudited condensed interim financial statements are consistent with those applied and disclosed in Note 5 to the Audited Consolidated Financial Statements for the year ended December 31, 2012.

(Expressed in Canadian Dollars)

a) Same accounting policies as Audited Consolidated Financial Statements

The accounting policies applied in preparation of these unaudited condensed interim consolidated financial statements are consistent with those applied and disclosed in the Company's consolidated financial statements for the year ended December 31, 2012 (Note 6 to the Audited Consolidated Financial Statements).

New accounting standards

Accounting standards, which become effective in 2013 and 2015, are disclosed in Note 4 to the Company's Audited Consolidated Financial Statements. The Company anticipates that the most significant of these standards relate to the following:

IFRS 10 – *Consolidated Financial Statements* ("IFRS 10"), IFRS 11 – *Joint Arrangements* ("IFRS 11"), IFRS 12 – *Disclosure of Interests in Other Entities* ("IFRS 12") and amendments to IAS 27 – *Separate Financial Statements* ("IAS 27") and IAS 28 – *Investments in Associates and Joint Ventures* ("IAS 28"), effective for annual periods beginning on or after January 1, 2013. The combination of these five new standards establishes control as the basis for consolidation and provides enhanced disclosure requirements for the Company's interests in other entities and the effects of those interests on the Company's consolidated financial statements.

The Company reviewed its investment in Prophecy Platinum at January 1, 2013 and has concluded that that the adoption of IFRS 10 did not result in any change to the investment in an associate balance. The Company does not anticipate the changes to IFRS 11 and the revised IAS 27 and IAS 28 to have a significant impact on the consolidated financial statements.
The requirement of IFRS 12 relates to disclosures only and is applicable for the first annual period after adoption. Accordingly, the Company will include additional disclosures about interests in other entities in its annual consolidated financial statements for the year ended December 31, 2013.

Fair value measurement

The Company adopted IFRS 13, Fair Value Measurement ("IFRS 13") with prospective application from January 1, 2013.

The adoption of IFRS 13 had immaterial effect on the Company's consolidated financial statements for the six months ended June 30, 2013. The disclosure requirements of IFRS 13 will be incorporated in its annual consolidated financial statements for the year ended December 31, 2013.

b) Basis of consolidation

The unaudited condensed interim consolidated financial statements include the accounts of Prophecy Coal and its controlled subsidiaries. All material intercompany balances and transactions have been eliminated.

Details of Prophecy Coal's subsidiaries at the date of these MD&A:

	Principal Activity	Place of incorporation and operation	Ownership interest
0912603 B.C. Ltd.	Exploration/Development	Canada	100%
0912601 B.C. Ltd.	Exploration/Development	Canada	100%
Chandgana Coal LLC	Exploration/Development	Mongolia	100%
Prophecy Power Generation LLC	Exploration/Development	Mongolia	100%
Red Hill Mongolia LLC	Exploration/Development	Mongolia	100%
UGL Enterprises LLC	Inactive	Mongolia	100%

(Expressed in Canadian Dollars)

10. FINANCIAL INSTRUMENTS AND RELATED RISKS

The Board of Directors, through the Audit Committee is responsible for identifying the principal risks of Prophecy Coal and ensuring that risk management systems are implemented. Prophecy Coal manages its exposure to financial risks, including liquidity risk, foreign exchange rate risk, interest rate risk, and credit risk in accordance with its risk management framework. Prophecy Coal's Board of Directors reviews Prophecy Coal's policies on an ongoing basis.

10.1 Financial Instruments

Details of the significant accounting policies and methods adopted for financial instruments for each class of financial assets and financial liability are disclosed in Note 5 to the Audited Consolidated Financial Statements for the year ended December 31, 2012.

The following table sets forth Prophecy Coal's financial assets that are measured at fair value on a recurring basis by level within the fair value hierarchy. As at June 30, 2013, those financial assets and liabilities are classified in their entirety based on the level of input that is significant to the fair value measurement.

As at June 30, 2013	Level 1	Level 2	Level 3	Total
Financial assets				
Receivables	$ 515,129	$ -	$ -	$ 515,129
Due from related party	120,000	-	-	120,000
Available-for-sale investments	1,053,723	-	-	1,053,723
	$ 1,688,853	$ -	$ -	$ 1,688,853

As at December 31, 2012	Level 1	Level 2	Level 3	Total
Financial assets				
Receivables	$ 456,035	$ -	$ -	$ 456,035
Due from related party	82,500	-	-	82,500
Available-for-sale investments	628,188	-	-	628,188
	$ 1,166,723	$ -	$ -	$ 1,166,723

10.2 Related Risks

The Company's risk exposures and the impact on the Company's financial instruments are summarized below. There have been no changes in the risks, objectives, policies or procedures during the six months ended June 30, 2013.

Liquidity risk is the risk that an entity will be unable to meet its financial obligations as they fall due. The Company manages liquidity risk by preparing cash flow forecasts of upcoming cash requirements. At June 30, 2013, the Company had approximately $0.4 million in cash and cash equivalents (December 31, 2012 - $0.8 million) in order to meet short-term business requirements. At June 30, 2013, the Company had accounts payable and accrued liabilities of $0.9 million (December 31, 2012 - $0.8 million) which have contractual maturities of 90 days or less, and loan payable of $9.7 million (December 31, 2012 – 9.4 million) due on July 16, 2013.

Credit risk - Credit risk is the risk that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss. Prophecy Coal is exposed to credit risk primarily associated to cash and cash equivalents, receivables and deposits. Prophecy Coal manages credit risk, in respect of cash and cash equivalents, by purchasing highly liquid, short-term investment-grade securities held at a major Canadian financial institution. The carrying amount of assets included on the statements of financial position represents the maximum credit exposure. Concentration of credit risk exists with respect to Prophecy Coal's cash and cash equivalents, as substantially all amounts are held with a single Canadian financial institution.

Market risk - The significant market risks to which Prophecy Coal is exposed are interest rate risk, foreign currency risk, and commodity and equity price risk.

(a) Interest rate risk

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate due to changes in market interest rates. Prophecy Coal's cash equivalents primarily include highly liquid investments that earn interest at market rates that are fixed to maturity or at variable interest rates. Due to the short-term nature of these financial instruments, fluctuations in market rates do not have a significant impact on the fair values or future cash flows of the financial instruments as of June 30, 2013. Prophecy Coal manages interest rate risk by maintaining an investment policy that focuses primarily on preservation of capital and liquidity.

(b) Foreign currency risk

Prophecy Coal is exposed to foreign currency risk to the extent that monetary assets and liabilities held by Prophecy Coal are not denominated in Canadian dollars. Prophecy Coal has exploration and development projects in Mongolia and undertakes transactions in various foreign currencies. Prophecy Coal is therefore exposed to foreign currency risk arising from transactions denominated in a foreign currency and the translation of financial instruments denominated in US dollars and Mongolia tugrug into its reporting currency, the Canadian dollar.

Net exposures as at June 30, 2013, with other variables unchanged, a 1% strengthening (weakening) of the Canadian dollar against the Mongolian tugrug would not have a material impact on earnings with other variables unchanged. A 1% strengthening (weakening) of the US dollar against the Canadian dollar would not have a material impact on net loss. Prophecy Coal currently does not use any foreign exchange contracts to hedge this currency risk.

(c) Commodity and equity price risk

The Company holds investments in available-for-sale that fluctuate in value based on market prices. Based upon the Company's investment position as at June 30, 2013, a 10% increase (decrease) in the market price of the available-for-sale investments held would have resulted in an increase (decrease) to comprehensive income (loss) of approximately $45,200 (December 31, 2012 - $62,800). Commodity price risk is defined as the potential adverse impact on earnings and economic value due to commodity price movements and volatilities. The Company closely monitors commodity prices, individual equity movements and the stock market to determine the appropriate course of action to be taken by the Company. Fluctuations in value may be significant.

11. RISKS AND UNCERTAINTIES

Prophecy Coal is exposed to a number of risks and uncertainties that are common to other junior mineral exploration companies in the same business. The mining industry is capital intensive at all stages and is subjected to variations in commodity prices, market sentiment, exchange rates for currency, inflation and other risks. The Company currently has no other source of revenue other than interest on cash balances. The Company will rely mainly on equity financing to fund its exploration and development activities.

History of Net Losses; No Foreseeable Positive Cash Flow

The Company has not received any material revenue or net profit to date from the exploitation activities on its Ulaan Ovoo Property. Exploration and development of mineral properties requires large amounts of capital and usually results in accounting losses for many years before profitability is achieved, if ever. The Company has incurred losses and negative operating cash flow during its most recently completed financial year and for the current financial year to date. The Company believes that commercial mining activity is warranted on its Ulaan Ovoo Property but has not made this determination for any of its other properties. Even if the Company undertakes further development activity on its Ulaan Ovoo Property or any of its other properties, there is no certainty that the Company will produce revenue, operate profitably or provide a return on investment in the future.

The exploration of the Company's properties depends on the Company's ability to obtain additional required financing. There is no assurance that the Company will be successful in obtaining the required financing, which could cause it to postpone its exploration plans or result in the loss or substantial dilution of its interest in its properties.

Exploration, Development and Production Risks

The exploration for and development of minerals involves significant risks, which even a combination of careful evaluation, experience and knowledge may not eliminate. Few properties which are explored are ultimately developed into producing mines. There can be no guarantee that the estimates of quantities and qualities of minerals disclosed will be economically recoverable. With all mining operations there is uncertainty and, therefore, risk associated with operating parameters and costs resulting from the scaling up of extraction methods tested in pilot conditions. Mineral exploration is speculative in nature and there can be no assurance that any minerals discovered will result in an increase in the Company's resource base.

The Company's operations are subject to all of the hazards and risks normally encountered in the exploration, development and production of minerals. These include unusual and unexpected geological formations, rock falls, seismic activity; flooding and other conditions involved in the extraction of material, any of which could result in damage to, or destruction of, mines and other producing facilities, damage to life or property, environmental damage and possible legal liability. Although precautions to minimize risk will be taken, operations are subject to hazards that may result in environmental pollution, and consequent liability that could have a material adverse impact on the business, operations and financial performance of the Company.

Substantial expenditures are required to establish ore reserves through drilling, to develop metallurgical processes to extract the metal from the ore and, in the case of new properties, to develop the mining and processing facilities and infrastructure at any site chosen for mining. Although substantial benefits may be derived from the discovery of a major mineralized deposit, no assurance can be given that minerals will be discovered in sufficient quantities to justify commercial operations or that funds required for development can be obtained on a timely basis. The economics of developing coal, nickel and other mineral properties is affected by many factors including the cost of operations, variations in the grade of ore mined, fluctuations in metal markets, costs of processing equipment and such other factors as government regulations, including regulations relating to royalties, allowable production, importing and exporting of minerals and environmental protection. The remoteness and restrictions on access of properties in which Prophecy Coal will have has an interest will have an adverse effect on profitability as a result of higher infrastructure costs. There are also physical risks to the exploration personnel working in the terrain in which Prophecy Coal's properties are located, often in poor climate conditions.

The long-term commercial success of Prophecy Coal depends on its ability to find, acquire, develop and commercially produce coal. No assurance can be given that Prophecy Coal will be able to locate satisfactory properties for acquisition or participation. Moreover, if such acquisitions or participations are identified, Prophecy Coal may determine that current markets, terms of acquisition and participation or pricing conditions make such acquisitions or participations uneconomic.

No History of Profitable Mineral Production

The Company has no history of commercially producing metals from its mineral exploration properties and there can be no assurance that it will successfully establish mining operations or profitably produce coal or other base and precious metals.

None of the Company's properties, other than the Ulaan Ovoo Property, are currently under development. The future development of any properties found to be economically feasible will require the construction and operation of mines, processing plants and related infrastructure. As a result, the Company is subject to all of the risks associated with establishing new mining operations and business enterprises, including:

- the timing and cost of the construction of mining and processing facilities;

- the availability and costs of skilled labour and mining equipment;
- the availability and cost of appropriate smelting and/or refining arrangements;
- the need to obtain necessary environmental and other governmental approvals and permits and the timing of those approvals and permits; and
- the availability of funds to finance construction and development activities.

The costs, timing and complexities of mine construction and development are increased by the remote location of Prophecy Coal's mining properties. It is common in new mining operations to experience unexpected problems and delays during development, construction and mine start-up. In addition, delays in the commencement of mineral production often occur. Accordingly, there are no assurances that Prophecy Coal's activities will result in profitable mining operations or that Prophecy Coal will successfully establish mining operations or profitably produce coal or other metals at any of its properties.

Commencing Mine Development Activities without a Feasibility Study

The Company commenced mining development activities on the Ulaan Ovoo Property without having completed a feasibility study on the Ulaan Ovoo Property. There are certain risks and uncertainties associated with commencing production without a feasibility study. The deposit may lack all geological, engineering, legal, operating, economic, social, environmental, and other relevant factors which may be required to serve as a reasonable basis for a financial institution to finance the development of the deposit for mineral production. Additionally, the outcome of the feasibility study may not be positive or optimal for the production scale being initiated.

Mineral Resources and Reserves

Apart from Ulaan Ovoo, all of the properties in which the Company holds an interest are considered to be in the exploration or development stage only and do not contain a known body of commercial minerals. The figures for the Company's resources and reserves are estimates based on interpretation and assumptions and may yield less mineral production under actual conditions than is currently estimated. Unless otherwise indicated, mineralization figures presented in this AIF and in the Company's other filings with securities regulatory authorities, press releases and other public statements that may be made from time to time are based upon estimates made by the Company's personnel and independent geologists. These estimates are imprecise and depend upon geological interpretation and statistical inferences drawn from drilling and sampling analysis, which may prove to be unreliable. There can be no assurance that:

- these estimates will be accurate;
- resource or other mineralization figures will be accurate; or
- this mineralization could be mined or processed profitably.
-

Because the Company has not commenced production at any of its properties, other than Ulaan Ovoo, and has not defined or delineated any proven or probable reserves on any of its properties, other than Ulaan Ovoo, mineralization estimates for Prophecy Coal's properties may require adjustments or downward revisions based upon further exploration or development work or actual production experience. In addition, the grade of ore ultimately mined, if any, may differ from that indicated by drilling results. There can be no assurance that minerals recovered in small-scale tests will be duplicated in large-scale tests under on-site conditions or in production scale.

The resource and reserve estimates contained in this AIF and in the documents incorporated herein by reference have been determined and valued based on assumed future prices, cut-off grades and operating costs that may prove to be inaccurate. Extended declines in market prices for coal or other metals may render portions of Prophecy Coal's mineralization uneconomic and result in reduced reported mineralization. Any material reductions in estimates of mineralization, or of Prophecy Coal's ability to extract this mineralization, could have a material adverse effect on Prophecy Coal's results of operations or financial condition.

The Company has not established the presence of any proven and probable reserves at any of its mineral properties other than the Ulaan Ovoo Property. There can be no assurance that subsequent testing or future studies will establish proven and probable reserves at any of Prophecy Coal's properties. The failure to establish proven and probable reserves could restrict Prophecy Coal's ability to successfully implement its strategies for long-term growth.

Capital Costs, Operating Costs, Production and Economic Returns

Actual capital costs, operating costs, production and economic returns may differ significantly from those the Company has anticipated and there are no assurances that any future development activities will result in profitable mining operations. The capital costs required to take the Company's projects into production may be significantly higher than anticipated.

None of the Company's mineral properties, including the Ulaan Ovoo Property, have sufficient operating history upon which the Company can base estimates of future operating costs. Decisions about the development of these and other mineral properties will ultimately be based upon feasibility studies. Feasibility studies derive estimates of cash operating costs based upon, among other things:

- anticipated tonnage, grades and metallurgical characteristics of the ore to be mined and processed;
- anticipated recovery rates metals from the ore;
- cash operating costs of comparable facilities and equipment; and
- anticipated climatic conditions.

Cash operating costs, production and economic returns, and other estimates contained in studies or estimates prepared by or for the Company, including the Ulaan Ovoo pre-feasibility study or other feasibility studies, if prepared, may differ significantly from those anticipated by the Company's current studies and estimates, and there can be no assurance that Prophecy Coal's actual operating costs will not be higher than currently anticipated.

Foreign Operations and Political Conditions

The Company's current principal exploration properties are located in Mongolia and those of its 32.1% associate company, Prophecy Platinum, Canada. In Mongolia, its operations may be exposed to various levels of political, economic, and other risks and uncertainties. These risks and uncertainties include, but are not limited to political and bureaucratic corruption and uncertainty, terrorism; hostage taking; military repression; fluctuations in currency exchange rates; high rates of inflation; labour unrest; the risks of civil unrest; expropriation and nationalization; renegotiation or nullification of existing concessions, licenses, permits and contracts; illegal mining; changes in taxation policies; restrictions on foreign exchange and repatriation; and changing political conditions, currency controls, and governmental regulations that favour or require the awarding of contracts to local contractors, or require foreign contractors to employ citizens of, or purchase supplies from, a particular jurisdiction.

Future political and economic conditions may result in a government adopting different policies with respect to foreign development and ownership of mineral resources. Any changes in policy may result in changes in laws affecting ownership of assets, foreign investment, taxation, rates of exchange, resource sales, environmental protection, labour relations, price controls, repatriation of income, and return of capital which may affect both the ability of the Company to undertake exploration and development activities in respect of future properties in the manner currently contemplated, as well as its ability to continue to explore, develop, and operate those properties to which it has rights relating to exploration, development, and operations.

The Company's Ability to Carry On Business in Mongolian is Subject to Legal and Political Risk

Currently, the Company is materially dependent upon its foreign operations in Mongolia. Any changes in regulations or shifts in political attitudes in Mongolia are beyond the control of the Company and may adversely affect its business, financial condition and prospects. The Mongolian legal system shares several of the qualitative characteristics typically found in a developing country and many of its laws, particularly with respect to matters of taxation, are still evolving. A transaction or business structure that would likely be regarded under a more established legal system as appropriate and relatively straightforward might be regarded in Mongolia as outside the scope of existing Mongolian law, regulation or legal precedent. As the legal framework in Mongolia is in many instances based on recent political reforms or newly enacted legislation which may not be consistent with long-standing conventions and customs, certain business arrangements or structures and certain tax planning mechanisms may carry significant risks. In particular, when business objectives and practicalities dictate the use of arrangements and structures that, while not necessarily contrary to settled Mongolian law, are sufficiently novel within a Mongolian legal context, it is possible that such arrangements may be invalidated.

The legal system in Mongolia has inherent uncertainties that could limit the legal protections available to the Company, which include (i) inconsistencies between laws; (ii) limited judicial and administrative guidance on interpreting Mongolian legislation; (iii) substantial gaps in the regulatory structure due to delay or absence of implementing regulations; (iv) the lack of established interpretations of new principles of Mongolian legislation, particularly those relating to business, corporate and securities laws; (v) a lack of judicial independence from political, social and commercial forces; and (vi) bankruptcy procedures that are not well developed and are subject to abuse. The Mongolian judicial system has relative little experience in enforcing the laws and regulations that currently exist, leading to a degree of uncertainty as to the outcome of any litigation, it may be difficult to obtain swift and equitable enforcement, or to obtain enforcement of a judgment by a court of another jurisdiction.

In addition, while legislation has been enacted to protect private property against expropriation and nationalisation, due to the lack of experience in enforcing these provisions and political factors, these protections may not be enforced in the event of an attempted expropriation or nationalisation. Whether legitimate or not, expropriation or nationalisation of any of Prophecy Coal's assets, or portions thereof, potentially without adequate or any compensation, could materially and adversely affect its business and results of operations. In addition, there can be no assurance that neighbouring countries' political and economic policies in relation to Mongolia will not have adverse economic effects on Prophecy Coal's business, including its ability to transport and sell its product and access construction labour, supplies and materials.

Recent and future amendments to Mongolian laws could adversely affect the* Company*'s mining rights in the Ulaan Ovoo Project or its other projects, or make it more difficult to expensive to develop such projects and carry our mining.

The Government of Mongolia has, in the past, expressed its desire to foster, and has to date protected the development of, an enabling environment for foreign direct investment. However, there are political constituencies within Mongolia that have espoused ideas which would not be regarded by the international mining industry as conducive to foreign investment if they were to become law or official government policy. There can be no assurance that future political and economic conditions in Mongolia will not result in the Mongolian Government adopting different policies in relation to foreign development and ownership of mineral resources. Any such changes in government or policy may result in changes in laws affecting ownership of assets, environmental protection, labour relations, repatriation of income, return of capital, investment agreements, income tax laws, royalty regulation, government incentive and other areas, each of which may materially and adversely affect Prophecy Coal's ability to undertake exploration and development activities in the manner currently contemplated.

In 2006, the Mongolian Government enacted a new minerals law. The 2006 Minerals Law, which preserves, to a limited extent, some of the substance of the former minerals legislation of 1997 minerals legislation, was drafted with the assistance of legal experts in the area of mining legislation and was widely regarded as progressive, internally consistent and effective legislation. However, the 2006 Minerals Law contains new provisions that have increased the potential for political interference and weakened the rights and security of title holders of mineral tenures in Mongolia. Certain provisions of the 2006 Minerals Law are ambiguous and it is unclear how they will be interpreted and applied in practice. Examples of such provisions include those relating to the designation of a mineral deposit as a Mineral Deposit of Strategic Importance. The Mongolian Government could determine that any one or more of the Company's projects in Mongolia is a Mineral Deposit of Strategic Importance.

On July 16, 2009, Parliament enacted a new law (the "**Prohibition Law**") that prohibits minerals exploration and mining in areas such as headwaters of rivers and lakes, forest areas as defined in the Forest Law of Mongolia and areas adjacent to rivers and lakes as defined in the Law on Water of Mongolia. Pursuant to the Prohibition Law, the Mongolian government was instructed to define the boundaries of the areas in which exploration and mining would be prohibited. New exploration licenses and mining licenses overlapping the defined prohibited areas will not be granted —and previously granted licences that overlap the defined prohibited areas will be terminated within five months following the adoption of the law. The Prohibition Law provides that affected licence holders shall be compensated, but there are no specifics as to the way such compensation will be determined.

The Mineral Resources Authority of Mongolia ("**MRAM**") has prepared a draft list of licences that overlap with the prohibited areas described in the Prohibition Law. Six of the Company's exploration licenses included on MRAM's draft list of licenses may be included on the final list published by the Mongolian Government. This could potentially affect the status of those licenses. Specifically, on July 16, 2010, the Corporation received a notice from MRAM of the potential revocation of these licenses. However, on October 12, 2010, the Company received a further notice from MRAM invalidating its prior notice of potential revocation.

On November 18, 2010 the Mongolian Government announced its intention to initiate the revocation of licenses under the Prohibition Law on a staged basis, beginning with the revocation of 254 mineral licenses. None of the licenses held by the Company is on this list

Lastly, any restrictions imposed, or Mongolian Government charges levied or raised (including royalty fees), under Mongolian law for the export of coal could harm the Company n's competitiveness.

Permits and Licenses

The Company's activities are subject to government approvals, various laws governing prospecting, development, land resumptions, production taxes, labour standards and occupational health, mine safety, toxic substances and other matters, including issues affecting local native populations. Although the Company believes that its activities are currently carried out in accordance with all applicable rules and regulations, no assurance can be given that new rules and regulations will not be enacted or that existing rules and regulations will not be applied in a manner which could limit or curtail production or development. Amendments to current laws and regulations governing operations and activities of exploration and mining, or more stringent implementation thereof, could have a material adverse impact on the business, operations and financial performance of the Company. Further, the mining licenses and permits issued in respect of its projects may be subject to conditions which, if not satisfied, may lead to the revocation of such licenses. In the event of revocation, the value of the Company's investments in such projects may decline.

In Mongolia, the Company's exploration licences are subject to periodic renewal and may only be renewed a limited number of times for a limited period of time. While the Company anticipates that renewals will be issued as and when they are sought, there is no assurance that such renewals will be given as a matter of course and there is no assurance that new conditions will not be imposed in connection therewith. The Company's business objectives may also be impeded by the costs of holding and/or renewing the exploration licences in Mongolia. Licence fees for exploration licences increase substantially upon the passage of time from the original issuance of each individual exploration licence. The Company needs to assess continually the mineral potential of each exploration licence, particularly at the time of renewal, to determine if the costs of maintaining the exploration licences are justified by the exploration results to date, and may elect to let some of its exploration licences lapse. Furthermore, the Company will require mining licences and permits to mine in order to conduct mining operations in Mongolia. There can be no assurance, however, that such licences and permits will be obtained on terms favourable to it or at all for the Company n's future intended mining and/or exploration targets in Mongolia.

Chandgana Power Plant Project Challenges

Prophecy Coal has been in discussions with the Mongolian government to finalize the PPA that will enable Prophecy Coal to seek project financing and begin construction of a power plant at Chandgana. Prophecy Coal has also had discussions with the Mongolian Ministry to discuss technical and commercial issues relating to the Chandgana power plan. On September 6, 2012, Prophecy Power, formally submitted its PPA proposal to NETGCO. The proposed PPA details the terms under which Prophecy Power would be prepared to supply power to NETGCO.

In addition to entering into a PAA and obtaining all required licences and permits for the construction and operation of the Chandgana power plant, any power plant development would be subject to large financing requirements (in the magnitude of an estimated $800 million) as well as technical studies to confirm the technical and economic feasibility of a power plant supplied by Chandgana Tal coal to produce the power and secure a long-term power purchase contract for the proposed plant's electrical power output. There can be no assurance that such financing can be obtained on favourable terms or at all, that such technical studies will yield positive results. Prophecy Coal also does not have experience constructing or operating coal fired power plants or qualified personnel to do so, and will have to rely on contractors or potential partners to supply such expertise.

Title to Mineral Properties

Title to mineral properties, as well as the location of boundaries on the grounds may be disputed. Moreover, additional amounts may be required to be paid to surface right owners in connection with any mining development. At all of such properties where there are current or planned exploration activities, the Company believes that it has either contractual, statutory, or common law rights to make such use of the surface as is reasonably necessary in connection with those activities. Although the Corporation believes it has taken reasonable measures to ensure proper title to its properties, there is no guarantee that title to its properties will not be challenged or impaired. Successful challenges to the title of the Corporation's properties could impair the development of operations on those properties.

Environmental Risks

All phases of the mining business present environmental risks and hazards and are subject to environmental regulation pursuant to a variety of international conventions, and state and municipal laws and regulations. Environmental legislation provides for, among other things, restrictions and prohibitions on spills and releases or emissions of various substances produced in association with mining operations. The legislation also requires that wells and facility sites be operated, maintained, abandoned and reclaimed to the satisfaction of applicable regulatory authorities. Compliance with such legislation can require significant expenditures and a breach may result in the imposition of fines and penalties, some of which may be material. Environmental legislation is evolving in a manner expected to result in stricter standards and enforcement, larger fines and liability and potentially increased capital expenditures and operating costs. Environmental assessments of proposed projects carry a heightened degree of responsibility for companies and directors, officers and employees. The cost of compliance with changes in governmental regulations has a potential to reduce the profitability of operations.

Failure to comply with applicable laws, regulations, and permitting requirements may result in enforcement actions thereunder, including orders issued by regulatory or judicial authorities causing operations to cease or be curtailed, and may include corrective measures requiring capital expenditures, installation of additional equipment, or remedial actions. Parties engaged in mining operations may be required to compensate those suffering loss or damage by reason of the mining activities and may have civil or criminal fines or penalties imposed for violations of applicable laws or regulations and, in particular, environmental laws.

Amendments to current laws, regulations and permits governing operations and activities of mining companies, or more stringent implementation thereof, could have a material adverse impact on the Company and cause increases in capital expenditures, production costs or reduction in levels of production at producing properties, or require abandonment or delays in the development of new mining properties.

Competition

The mining industry in general is intensely competitive and there is no assurance that, even if commercial quantities of ore are discovered, a ready market will exist for the sale of same. Marketability of natural resources which may be discovered by Prophecy Coal will be affected by numerous factors beyond the control of Prophecy Coal, such as market fluctuations, the proximity and capacity of natural resource markets and processing equipment, government regulations including regulations relating to prices, royalties, land tenure, land use, importing and exporting of minerals and environmental protection. The exact effect of such factors cannot be predicted but they may result in Prophecy Coal not receiving an adequate return on its capital.

Lack of Infrastructure

The Company has projects located in extremely remote areas which currently lack basic infrastructure, including sources of electric power, water, housing, food and transport necessary to develop and operate a major mining project. While the Company has established the limited infrastructure necessary to conduct its exploration and development activities in Mongolia, substantially greater source of power, water, physical plant and transport infrastructure in the area will need to be established before the Company can conduct mining operations. Lack of availability of the means and inputs necessary to establish such infrastructure may adversely affect mining feasibility. Establishing such infrastructure will, in any event, require significant financing, identification of adequate sources of raw materials and supplies and necessary approvals from national and regional governments, none of which can be assured.

Key Personnel

The Company depends on a number of key personnel, including its directors and executive officers, the loss of any one of whom could have an adverse effect on the Company's operations. The Company has employment contracts with several key personnel and does not have key man life insurance.

The Company's ability to manage growth effectively will require it to continue to implement and improve management systems and to recruit and train new employees. The Company cannot assure that it will be successful in attracting and retaining skilled and experienced personnel.

Uninsured Risks

The Company's business is subject to a number of risks and hazards, including adverse environmental conditions, industrial accidents, labour disputes, unusual or unexpected geological conditions, ground or slope failures, cave-ins, changes in the regulatory environment and natural phenomena such as inclement weather conditions, floods and earthquakes. Such occurrences could result in damage to mineral properties or production facilities, personal injury or death, environmental damage to the Company's properties or the properties of others, delays in development or mining, monetary losses and possible legal liability.

Although the Company maintains insurance to protect against certain risks in amounts that it considers reasonable, its insurance will not cover all the potential risks associated with its operations. The Company may also be unable to maintain insurance to cover these risks at economically feasible premiums. Insurance coverage may not continue to be available or may not be adequate to cover any resulting liability. Moreover, insurance against risks such as environmental pollution or other hazards as a result of exploration and production is not generally available to the C Company or to other companies in the mining industry on acceptable terms. The Company may also become subject to liability for pollution or other hazards which may not be insured against or which the Company may elect not to insure against because of premium costs or other reasons. Losses from these events may cause the Company to incur significant costs that could have a material adverse effect upon its financial performance, results of operations and business outlook.

Fluctuating Market Prices

The Company's revenues, if any, are expected to be in large part derived from the mining and sale of coal and other minerals. The prices of those commodities has fluctuated widely, particularly in recent years, and are affected by numerous factors beyond the Company's control including international economic and political trends, expectations of inflation, currency exchange fluctuations, interest rates, global or regional consumption patterns, speculative activities and increased production due to new mine developments and improved mining and production methods.

The price of coal may have a significant influence on the market price of Prophecy Coal's shares and the value of Prophecy Coal's mineral properties. The effect of these factors on the price of coal, and therefore the viability of Prophecy Coal's exploration projects, cannot be accurately predicted. If silver and metals prices were to decline significantly or for an extended period of time, Prophecy Coal may be unable to continue operations, develop the properties or fulfill obligations under agreements with Prophecy Coal's joint venture partners or under its permits or licenses.

The Company will be Heavily Reliant Upon its Contractors

During the development of large scale projects, companies are often measured and evaluated by the behaviour and performance of their representatives, including in large part their contractors. The Company works hard to build in controls and mechanisms to choose and retain employees and contractors with similar values as the Company; however these controls may not always be effective. Sound judgment, safe work practices and ethical behaviour is expected from the Company's contractors both on and off-site. Any work disruptions, labour disputes, regulatory breach or irresponsible behaviour of the Company's contractors could reflect poorly on the Company and could lead to loss of social license, delays in production and schedule, unsafe work practices and accidents and reputational harm.

Additional Financing

The Company estimates that its current financial resources are sufficient to undertake presently planned exploration and development programs. Further exploration on and development and construction of the Company's mineral properties may require additional capital. One source of future funds presently available to the Company is through the sale of equity capital. There is no assurance that this source will continue to be available as required or at all. If it is available, future equity financings may result in substantial dilution to shareholders. Another alternative for the financing of further exploration would be the offering by the Company of an interest in its mineral properties to be earned by another party or parties carrying out further exploration or development thereof. There can be no assurance that the Company will be able to conclude any such agreements on favourable terms or at all.

Any failure of the Company to obtain the required financing on acceptable terms could have a material adverse effect on the Company's financial condition, results of operations and liquidity and may require the Company to cancel or postpone planned capital investments.

Foreign Exchange

In the past, Prophecy Coal has raised its equity and maintained its accounts in Canadian dollars. Foreign operations carried out in U.S. or local Mongolian currency could subject Prophecy Coal to foreign currency fluctuations that may materially and adversely affect Prophecy Coal's financial position.

The Company is Subject to Anti-Corruption Legislation

Prophecy Coal is subject to the Corruption of Foreign Public Officials Act (Canada) and other similar acts (collectively "Anti-Corruption Legislation"), which prohibit Prophecy Coal or any officer, director, employee or agent of Prophecy Coal or any stockholder of Prophecy Coal acting on its behalf from paying, offering to pay or authorizing the payment of anything of value to any foreign government official, government staff member, political party or political candidate in an attempt to obtain or retain business or to otherwise influence a person working in an office capacity. The Anti-Corruption Legislation also requires public companies to make and keep books and records that accurately and fairly reflect their transactions and to devise and maintain an adequate system of internal accounting controls. Prophecy Coal's international activities create the risk of unauthorized payments or offers of payments by its employees, consultants or agents, even though they may not always be subject to its control. The Company strictly prohibits these practices by its employees and agents. However, Prophecy Coal's existing safeguards and any future improvements may provide to be less than effective, and its employees, consultants and agents may engage in conduct for which Prophecy Coal may be held responsible. Any failure by Prophecy Coal to adopt appropriate compliance procedures and to ensure that its employees and agents comply with Anti-Corruption Legislation and applicable laws and regulations in foreign jurisdictions could result in substantial penalties or restrictions on its ability to conduct its business, which may have a material adverse impact of Prophecy Coal or its share price.

Recent Global Financial Conditions

Access to financing has been negatively impacted by many factors as a result of the global financial crisis. This may impact Prophecy Coal's ability to obtain debt or equity financing in the future on terms favourable to Prophecy Coal and Prophecy Coal's ability to attain strategic partnerships or enter into joint venture arrangements which may further negatively impact the timeline for commencement of commercial production. Additionally, global economic conditions may cause decreases in asset values that are deemed to be other than temporary, which may result in impairment losses. If such volatility and market turmoil continue, Prophecy Coal's business and financial condition could be adversely impacted.

Prophecy Coal Does Not Insure Against All Risks

Prophecy Coal's insurance will not cover all the potential risks associated with a mining company's operations. Prophecy Coal may also be unable to maintain insurance to cover these risks at economically feasible premiums. Insurance coverage may not continue to be available or may not be adequate to cover any resulting liability. Moreover, insurance against risks such as environmental pollution or other hazards as a result of exploration and production is not generally available to Prophecy Coal or to other companies in the mining industry on acceptable terms. Prophecy Coal might also become subject to liability for pollution or other hazards which may not be insured against or which Prophecy Coal may elect not to insure against because of premium costs or other reasons. Losses from these events may cause Prophecy Coal to incur significant costs that could have a material adverse effect upon its financial condition and results of operations.

Conflicts of Interest

Conflicts of interest may arise as a result of the directors, officers and promoters of the Company also holding positions as directors and/ or officers of other companies. Some of those persons who will be directors and officers of the Company have and will continue to be engaged in the identification and evaluation of assets and businesses and companies on their own behalf and on behalf of other companies, and situations may arise where the directors and officers will be in direct competition with Prophecy Coal. Such conflicts, if any, will be subject to the procedures and remedies under the *Business Corporations Act* (British Columbia).

Readers should carefully consider the risks and uncertainties described in the Company's Annual Information Form for the year ended December 31, 2012 (the "**AIF**") "Risk Factors" page 66. The AIF is available under the Company's profile at www.sedar.com.

12. DISCLOSURE CONTROLS AND PROCEDURES

Disclosure controls and procedures are designed to provide reasonable assurance that information required to be disclosed by Prophecy Coal in its annual filings, filings or other reports filed or submitted by it under securities legislation is recorded, processed, summarized and reported within the time periods specified in the securities legislation and include controls and procedures designed to ensure that information required to be disclosed by Prophecy Coal in its annual filings, filings or other reports filed or submitted under securities legislation is accumulated and communicated to Prophecy Coal's management, including its Interim Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

Management, including the Interim Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of the design and operation of Prophecy Coal's disclosure controls and procedures. As of June 30, 2013, the Interim Chief Executive Officer and Chief Financial Officer have each concluded that Prophecy Coal's disclosure controls and procedures, as defined in NI 52-109 are effective to achieve the purpose for which they have been designed except as follows: Prophecy Coal Corp. management identified two material weaknesses in internal controls regarding 2012 annual reporting, which have continued into 2013; being the consistent application of the Company's accounting policies and procedures during 2012 and for the six months ending June 30, 2013 by its wholly owned Mongolian subsidiaries and accounting for non-cash stock based compensation, both of which were communicated to the audit committee and the board of directors. To mitigate these issues the Company hired in 2012 an internal auditor to report to the audit committee, increased accounting personnel and time in these two areas, and expanded the review diligence, prior to the finalization of the 2012 year end and first quarter 2013 consolidated financial statements. The internal auditor resigned in Q2, 2013 and the position remains vacant at this time, subject to replacement based on direction from the audit committee. The audit committee and management continue to work on enhancing Company practices and internal controls, in addition to refinements to developing Whistle Blower and Code of Conduct policies.

Prophecy Coal's disclosure committee, is comprised of the Interim Chief Executive Officer and senior members of management and the audit chairman. The disclosure committee's responsibilities include determining whether information is material and ensuring the timely disclosure of material information in accordance with securities laws. The Board of Directors is responsible for reviewing the Company's disclosure policy, procedures and controls to ensure that it addresses the Company's principal business risks, and changes in operations or structure, and facilitates compliance with applicable legislative and regulatory reporting requirements and is working to refine and enhance existing disclosure policies.

Design of Internal Controls over Financial Reporting

Prophecy Coal's internal controls over financial reporting include policies and procedures that:

- pertain to the maintenance of records that, in reasonable detail accurately and fairly reflect the transactions, acquisition and disposition of assets and liabilities;

- provide reasonable assurance that transactions are recorded as necessary to permit preparation of the financial statements in accordance with IFRS and that receipts and expenditures are being made only in accordance with the authorization of management and directors of Prophecy Coal; and

- provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of assets, and incurrence of liabilities, that could have a material effect on the financial statements.

The Company's management is responsible for establishing and maintaining an adequate system of internal control over financial reporting. Any system of internal control over financial reporting, no matter how well designed, has inherent limitations. Therefore, even those systems determined to be effective can provide only reasonable assurance with respect to financial statement preparation and presentation and may not prevent or detect misstatements. Furthermore, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate. There has not been any change in the Company's internal control over financial reporting that occurred during the Company's first and second fiscal quarters of 2013 that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

13. DISCLOSURE OF OUTSTANDING SHARE DATA

As at the date of this MD&A, the following securities are outstanding:

13.1 Share Capital

Authorized – unlimited number of common shares without par value.

As at the date of this MD&A, common shares outstanding 243,184,926 with recorded value of $147,543,187.

Subsequent to June 30, 2013, the Company issued 358,542 common shares as a share bonus to personnel, and 100,000 common shares were returned to treasury.

13.2 Stock options

The Company adopted a rolling stock option plan (the "**2013 Plan**") approved by the shareholders at the annual meeting held on July 30, 2013. A significant amendment to the 2012 fixed stock option plan is that the 2013 Plan is a "rolling" stock option plan permitting the issuance of options exercisable for 20% of the Company's common shares issued and outstanding from time to time. The exercise price of options granted under the 2013 Plan is a price not less than the volume weighted average trading price of the Common Shares on the TSX during the last five trading days immediately preceding the date of grant during such five trading days. The provisions of the 2013 Plan dealing with the eligibility, grant and terms of options provide an allowable exercise period of options granted under the 2013 Plan of up to ten (10) years from the date the option is granted, subject to any accelerated termination. Options granted under the 2013 Plan will vest and become exercisable at 12.5% vested quarterly over two years, unless determined otherwise by the Board. For further information please refer to the Management Information Circular in the Company's Sedar profile at www.sedar.com.

On June 18, 2012, further to the voluntary forfeiture of share options held by certain directors, officers, employees and consultants with expiry dates on June 13, 2016, August 30, 2016, January 9, 2017, February 3, 2017, and March 22, 2017 at exercise prices ranging from $0.425 to $0.77, the Company granted 5,315,000 new share options to such individuals with an expiry date of June 18, 2017 at an exercise price of $0.28 per share subject to a two year vesting schedule whereby 50% of the options granted vest at the end of the each of the first and second years. The re-issuing of these options had been approved by shareholders at the annual meeting held on July 30, 2013.

On June 18, 2012, the Company amended the exercise price of 18,358,050 options that had previously been granted to directors, officers, employees and consultants with expiry dates ranging from January 23, 2014 to February 14, 2016 by reducing the exercise prices (which ranged from $0.38 to $0.93) to $0.28, subject to TSX (received) and shareholder approval. There were no changes to the expiry dates and vesting periods of these options. The re-pricing of these options had been approved by the shareholders at the annual meeting held on July 30, 2013.

Subsequent to June 30, 2013, the Company granted 500,000 stock options at price $0.13 per share for a period of five years to the Company's CFO.

As at the date of this MD&A, 32,625,550 stock options are outstanding, 23,568,883 are exercisable at prices ranging from $0.25 to $1.03 and which expire between 2014 and 2017.

13.3 Share Purchase Warrants

During the six months ended June 30, 2013, 6,508,415 warrants expired unexercised at a weighted average exercise price of $0.80.

On April 11, 2013, the Company issued 4,382,572 units, of which each unit consists of one share and 0.75 share purchase warrant at a purchase price of $0.14 per unit in the first tranche of the non-brokered private placement announced on February 7, 2013 and closed on April 12, 2013. Each warrant is exercisable into one common share of Prophecy Coal at a price of $0.18, expiring two years from the date of issue. The foregoing shares, warrants and any shares issued upon the exercise of the warrants are subject to a hold period which expires August 12, 2013.

On June 4, 2013, the Company issued 8,142,857 units, of which each unit consists of one share and 0.75 share purchase warrant at a purchase price of $0.14 per unit in the first tranche of the non-brokered private placement announced on February 7, 2013 and closed on April 12, 2013. Each whole warrant is exercisable for one common share of Prophecy at a price of $0.18, expiring two years from the date of issue. Each unit sold in the second tranche closing also included an adjustment warrant ("**Adjustment Warrant**") entitling the holder to acquire additional common shares of the Company in certain circumstances. Each Adjustment Warrant may be exercised for no additional consideration for a period of 12 months following the closing of the final tranche of the private placement, for a fraction of a common share of Prophecy Coal. The fraction will be calculated by first dividing the Unit subscription price of $0.14 by the market price (subject to a floor market price of $0.105) at the time of exercise, then subtracting one (1) from that resulting number to determine the fraction. Market price is defined as the 20 day moving average price for the Company's common shares. The Adjustment Warrants must be exercised in their entirety and may not be exercised in part, and the holder of Adjustment Warrants may not sell any securities of the Company within 20 days prior to exercise. Adjustment Warrants may also only be exercised to the extent that the holder continues to hold the shares and warrants comprising the Units of which the Adjustment Warrants formed part. The foregoing shares, warrants and any shares issued upon the exercise of the warrants are subject to a hold period which expires August 12, 2013.

As at the date of this MD&A, the following Prophecy Coal share purchase warrants and warrant adjustments are outstanding:

(Expressed in Canadian Dollars)

Exercise price	Number of Warrants		Expiry date
	At June 30, 2013	At December 31, 2012	
$0.18	3,831,511	3,831,511	October 28, 2015
$0.18	-	551,968	March 31, 2013
$0.80	-	2,964,730	March 31, 2013
$0.80		337,750	April 21, 2013
$0.80	-	2,650,967	March 23, 2013
$0.18	3,286,929	-	April 11, 2015
$0.18	6,107,143	-	June 4, 2015
	13,225,583	10,339,926	

Exercise price	Number of Adjustment Warrants		Expiry date
	At June 30, 2013	At December 31, 2012	
**	4,382,572	-	April 11, 2014
**	8,142,857	-	June 4, 2014
	12,525,429	-	

** These are the adjustment warrants, please refer to Note 12 b (iv) in the June 30, 2013 quarterly financial statements.

14. OFF-BALANCE SHEET ARRANGEMENT

During the six month ended June 30, 2013, Prophecy Coal was not a party to any off-balance-sheet arrangements that have, or are reasonably likely to have, a current or future effect on the results of operations, financial condition, revenues or expenses, liquidity, capital expenditures or capital resources of Prophecy Coal.