



**PROPHECY COAL CORP.
(HEREIN "PROPHECY COAL" OR THE "COMPANY")**

**ANNUAL INFORMATION FORM
FOR THE FINANCIAL YEAR ENDED DECEMBER 31, 2013**

March 28, 2014

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1. GENERAL

1.1 Forward Looking Statements

This Annual Information Form (“AIF”) contains forward-looking statements within the meaning of applicable Canadian securities legislation concerning anticipated developments in the Company’s continuing and future operations in Mongolia, the adequacy of the Company’s financial resources and financial projections. Such forward-looking statements include but are not limited to 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. See in particular, portions of Part 3.1 – *Three Year Corporate Development History – Summary of Two Principal Mineral Projects* and Part 4 – *Description of the Business*.

Forward-looking statements in this document are frequently identified by words such as “expects”, “anticipates”, “intends”, “believes”, “estimates”, “potentially” or similar expressions, or statements that events, conditions or results “will”, “may”, “would”, “could”, “should” occur or are “to be” achieved, and statements related to matters which are not historical facts. Information concerning management’s expectations regarding Prophecy Coal’s future growth, results of operations, performance, business prospects and opportunities may also be deemed to be forward-looking statements, as such information constitutes predictions based on certain factors, estimates and assumptions subject to significant business, economic, competitive and other uncertainties and contingencies, and involve known and unknown risks which may cause the actual results, performance, or achievements to be different from future results, performance, or achievements contained in such forward-looking statements made by Prophecy Coal.

In making the forward-looking statements in this AIF, 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 or other causes; 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 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.

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 Part 6 – *Risk Factors* in this AIF: 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; commencing mine development without a feasibility study; 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 country and being subject to its local laws; the availability and timeliness of various government approvals and licences; the feasibility, funding and development of the Chandgana Power Plant; protecting title to 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 risk;

anti-corruption legislation; recent global financial conditions; the payment of dividends; and conflicts of interest.

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 AIF should not be considered as a representation by Prophecy Coal or any other person that Prophecy Coal's objectives or plans will be achieved.

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 AIF 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 publicly update any future revisions to forward-looking statements to reflect events or circumstances after the date of this AIF or to reflect the occurrence of unanticipated events, except as expressly required by law.

The information in this AIF is for the fiscal year ended December 31, 2013 but is current as of March 28, 2014 unless otherwise stated or clear from the context.

1.2 Accounting Principles

All financial information in this AIF is prepared in accordance with International Financial Reporting Standards, as issued by the International Accounting Standards Board.

1.3 Currency

Unless otherwise indicated all references to "dollar" or "\$" are to Canadian dollars and all references to "US dollars" or "US \$" are to United States of America dollars.

	Year ended December 31		
	<u>2013</u>	<u>2012</u>	<u>2011</u>
High	\$1.01663	\$1.0418	\$1.0604
Low	0.9336	0.9710	0.9449
Average ⁽¹⁾	0.9711	0.9996	0.9891
Closing	0.9015	0.9949	1.0170

Note:

(1) *Calculated as average of the daily noon rates for each period.*

On March 28, 2014, the Bank of Canada noon mid-market rate of exchange was US \$0.9038 dollars to \$1.00.

1.4 Documents Incorporated by Reference

The following documents are incorporated by reference into this AIF:

- (a) "Ulaan Ovoo – Pre-Feasibility Study" dated December 10, 2010, prepared by John Sampson, B.Sc. (Hons) and Brian Saul P. Eng. of Wardrop Engineering Inc. ("**Wardrop**") (the "**Ulaan Ovoo Technical Report**" or "**Ulaan Ovoo PFS**"), who is an independent Qualified Person under National Instrument 43-101 – *Standard of Disclosure for Mineral Properties* ("**NI 43-101**");
- (b) "Updated Technical Report on the Coal Resources of the Chandgana Khavtgai Coal Resource Area, Khentii Aimag, Mongolia" dated September 28, 2010, prepared by Christopher M. Kravits, CPG, LPG of Kravits Geological Services, LLC (the "**Chandgana Technical Report**"), who was

at the time an independent Qualified Person under NI 43-101 but has since become non-independent by virtue of the fact that the Company has become his primary client;

- (c) Senior Secured Credit Agreement dated July 16, 2012 between Prophecy Coal Corp. and Waterton Global Value, L.P. ("**Waterton**");
- (d) Material Change Report dated February 25, 2013, disclosing the initiation of a non-brokered private placement and current number of units subscribed for thereunder;
- (e) Material Change Report dated March 1, 2013 disclosing the waiver of default under the Senior Secured Credit Agreement due to the expiry of the original purchase and sales agreement with Tethys Mining LLC ("**Tethys**");
- (f) Material Change Report dated March 11, 2013 disclosing the grant of land use rights to Prophecy's 100%-owned subsidiary Prophecy Power Generation LLC ("**Prophecy Power**") for the Company's proposed Chandgana Power Plant;
- (g) Material Change Report dated May 17, 2013 disclosing the entering into of a 25-year Tariff Agreement for the Chandgana Power Plant project;
- (h) Coal Supply Agreement dated June 5, 2013 between Chandgana Coal LLC ("**Chandgana Coal**") and Prophecy Power (the "**CSA**");
- (i) Material Change Report dated June 5, 2013 disclosing the entering into of the CSA;
- (j) Material Change Report dated June 7, 2013 disclosing the closing of the final tranche of the non-brokered private placement;
- (k) Material Change Report dated June 24, 2013 disclosing an update on the Ulaan Ovoo mine;
- (l) First Amendment to the Senior Secured Credit Agreement dated July 15, 2013 between Prophecy Coal and Waterton (the "**Extending Agreement**");
- (m) Material Change Report dated July 15, 2013 disclosing the entering into of the Extending Agreement;
- (n) Material Change Report dated October 17, 2013 disclosing the acceptance of an offer to purchase shares in Wellgreen Platinum Ltd. (formerly Prophecy Platinum Corp.) ("**Wellgreen Platinum**");
- (o) Material Change Report dated October 24, 2013 disclosing the acceptance of an offer to purchase additional shares in Wellgreen; and
- (p) "Technical Report Coal Resources and Preliminary Economic Assessment - Coal Mine Component, Chandgana Tal Coal Project, Khentii Province, Mongolia" (the "**PEA**") dated November 30, 2012 and prepared by John T. Boyd Co. (USA). The lead Qualified Person for the report is Thaddeus J. Sobek, who is an independent Qualified Person under NI 43-101. A subsequent update to the PEA was prepared and submitted to regulators. However, as of the date of this AIF, it has not yet been finalized for filing.

The Ulaan Ovoo Technical Report, the Chandgana Technical Report, and the PEA are available for review under the SEDAR profile of Prophecy Coal at www.SEDAR.com.

2. CORPORATE STRUCTURE

2.1 Name, Address and Incorporation

Prophecy Coal Corp. (“**Prophecy Coal**” or the “**Company**”) 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**”). Under that merger Red Hill was the successor legal entity which is herein referred to as the “Company”. Under that 2010 business combination Old Prophecy was merged with a subsidiary of Red Hill and then Red Hill’s name was changed to Prophecy Resource Corp. and, in 2011, to Prophecy Coal Corp. Red Hill was incorporated on November 6, 1978 under the *Corporations 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 Company, as UGL, transitioned under the new (2004) *Business Corporations Act* (British Columbia) (“**BCBCA**”) which is the corporate law statute which continues to govern the Company. On April 16, 2010, the Company (then Red Hill) changed its name to “Prophecy Resource Corp.” in conjunction with the Red Hill merger. On June 13, 2011, the Company changed its name to “Prophecy Coal Corp.” in connection with an asset spin-off to capitalize the Company’s controlled, at that time, affiliate (initially approximately 44% controlled), publicly traded Wellgreen Platinum.

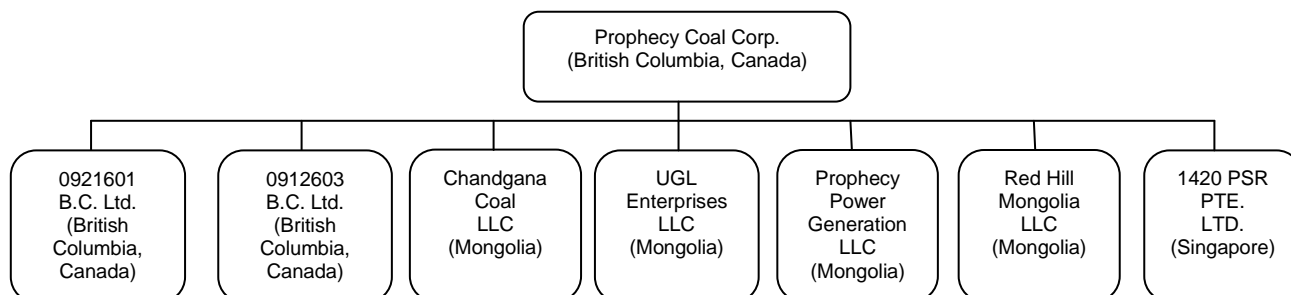
Prophecy Coal is a reporting issuer in the provinces of British Columbia, Alberta, and Ontario. The Company’s common shares (the “**Shares**” or “**Prophecy Shares**”) are listed for trading on: (i) the Toronto Stock Exchange under the symbol “PCY”, (ii) the OTC-QX under the symbol “PRPCF”, and (iii) on the Frankfurt Stock Exchange under the symbol “1P2”.

Prophecy Coal’s head and registered offices are located at 342 Water Street, 2nd Floor, Vancouver, BC, V6B 1B6. The Company’s website is www.prophecycoal.com.

2.2 Inter-corporate Relationships

Prophecy Coal currently has seven wholly-owned subsidiaries (the “**Subsidiaries**”). Subsequent to the year, the Company incorporated a subsidiary in Singapore to act as a holding company to facilitate coal sales to Russian customers.

The following diagram describes the inter-corporate relationships among Prophecy Coal and its 100%-owned Subsidiaries as of the date of this AIF.



3. GENERAL DEVELOPMENT OF THE BUSINESS

Prophecy Coal is an exploration and development stage company engaged in the acquisition, exploration and development of coal properties and the development of its Chandgana Power Plant project in Mongolia. As of the date of this AIF, the Company holds the following interests in its material mineral projects:

- a 100% interest in mining licenses for the Ulaan Ovoo property in Mongolia (the “**Ulaan Ovoo Property**”), which is on care and maintenance since July 2012; and
- a 100% interest in the licenses for the Chandgana properties in Mongolia (the “**Chandgana Properties**”) for which technical and economic studies are underway and a conditional permit or “energy license” to build a 600 MW mine-mouth power plant has been issued and land has been granted by the Mongolian government.

3.1 Three Year Corporate Development History

During 2006-2009, the Company’s business was being pursued through two different public corporations which were merged in April 2010. One of the Company’s two predecessors, Red Hill Energy Inc., was primarily pursuing development of the Ulaan Ovoo and Chandgana coal deposits in Mongolia. For financial statement purposes, Red Hill carried its mineral properties at approximately \$16 million, showed share capital and paid-in surplus of some \$38 million and had a cumulative deficit of about \$22 million. Ulaan Ovoo had been the subject of a pre-feasibility report and represented the majority of Red Hill’s property accounts, at \$12.6 million. The Company’s other predecessor, Old Prophecy, was formed in 2006 and was pursuing nickel projects in three Provinces of Canada. Old Prophecy’s principal mineral project was the Lynn Lake (Manitoba) project, described in Part 5 hereof, which is now held by Wellgreen Platinum and carried at approximately \$33 million. Old Prophecy carried its mineral interests at approximately \$2 million and had about \$2 million in working capital. The Red Hill/Old Prophecy merger is described in detail in a management Information Circular filed on the Company’s www.SEDAR.com continuous disclosure profile dated March 15, 2010.

2011-2013 Asset Spin-Off Transactions, and Cessation of Control and Significant Influence over Wellgreen Platinum

The Company’s current corporate structure is the result of two corporate mergers and two corporate spin-off transactions over 2010-2011. (Merger in this instance means the combining of two or more corporations and their businesses and spin-off means the division of business assets and their transfer to a different corporation). One merger and one spin-off were completed in April 2010, a second merger was completed in September 2010 and a second spin-off was completed in June 2011.

June 2011 Asset Spin-Off to Wellgreen Platinum Ltd.

On June 13, 2011, the Company completed a court approved plan of arrangement under the BCBCA with Pacific Coast Nickel Corp. (for simplicity, herein given its subsequent name change, referred to as “Wellgreen Platinum” and such arrangement is herein the “**Wellgreen Platinum Arrangement**”). As part of the Wellgreen Platinum Arrangement, the Company transferred the assets comprising the Lynn Lake project and the Wellgreen Property to a newly incorporated subsidiary (“**Spinco**”). Wellgreen Platinum then acquired all of the shares of Spinco in exchange for the issuance of 450,000,000 common shares in the capital of Wellgreen Platinum (the “**Wellgreen Platinum Shares**”), of which 225,000,000 Wellgreen Platinum Shares were retained by the Company and 225,000,000 Wellgreen Platinum Shares were distributed or reserved for distribution on a *pro rata* basis to holders of Prophecy Shares, on a fully diluted basis.

Immediately prior to the completion of the Wellgreen Platinum Arrangement there were 189,973,664 Prophecy Coal Shares and 47,345,588 Prophecy Coal convertible securities issued and outstanding. Following the completion of the Wellgreen Platinum Arrangement, Wellgreen Platinum consolidated its share capital on a ten old for one basis (the “**Consolidation**”) and changed its name to “Prophecy Platinum Corp.”, on December 19, 2013 Prophecy Platinum changed its name to “Wellgreen Platinum Ltd.” As a result of the Consolidation and the Wellgreen Platinum Arrangement, each Prophecy Coal Shareholder received 0.094758 of a post-Consolidation Wellgreen Platinum Share for each Prophecy Coal Share held as of June 13, 2011. Each option holder and warrant holder of Prophecy Coal will, upon the exercise of their Prophecy Coal options and warrants, as the case may be, receive 0.094758 of a post-Consolidation Wellgreen Platinum Share, in addition to one common share of Prophecy Coal for each whole option or warrant of Prophecy Coal held, Prophecy Coal reserved 44,176,425 (4,417,642 post

consolidation) Wellgreen Platinum Shares (the “**Reserved Shares**”) if these options and warrants are exercised. As a result of the completion of the Wellgreen Platinum Arrangement and the Consolidation, Prophecy Coal held 22,500,000 Wellgreen Platinum Shares representing 44.4% of the outstanding capital of Wellgreen Platinum and the Company changed its name to “Prophecy Coal Corp.” The spin-off is described in detail in a management Information Circular of the Prophecy Coal at www.SEDAR.com dated May 5, 2011.

November 30 2012 Change from Control to Significant Influence over Wellgreen Platinum Ltd.

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

Cessation of Significant Influence over Wellgreen Platinum Ltd.

Prophecy Coal’s ownership interest in Wellgreen Platinum during 2013 decreased to 4.12% (excluding reserved Wellgreen Platinum shares) or 7% (including reserved Wellgreen Platinum shares) as a consequence of: (i) Wellgreen Platinum’s series of private equity placements, to which Prophecy Coal did not participate; and (ii) the sale of 19.84 million Wellgreen Platinum Shares held by Prophecy Coal. Therefore, the Company ceased to have significant influence over Wellgreen Platinum and Prophecy Coal is also no longer classified as an insider of Wellgreen Platinum.

As of December 31, 2013 the Company held 3,327,261 of Wellgreen Platinum’s issued and outstanding common shares. The closing price on December 31, 2013 as quoted on the Toronto Stock Venture Exchange was \$0.69 per share for a total value based on quoted amount of \$2,295,810.

Pursuant to the Wellgreen Platinum Arrangement and Consolidation described in Note 13 “Available-For-Sale Investments”, to the annual audited consolidated financial statements, 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 Wellgreen Platinum Share, in addition to one Prophecy Coal Share for each whole option or warrant of Prophecy Coal held and exercised. As of December 31, 2013 Prophecy Coal held, reserved in-trust, 2,316,634 (December 31, 2012 - 3,267,934) Wellgreen Platinum Shares contingent on the exercise of these June 9, 2011 Options and Warrants. Upon the expiry of any unexercised June 9, 2011 Options and Warrants, the related Wellgreen Platinum Shares held in-trust, shall be returned to Prophecy Coal, of which 2,475,181 have been returned to-date.

Summary of Two Principal Mineral Projects

1. Ulaan Ovoo Property – Thermal Coal Resource

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, that 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 the Company. Ochir LLC retained a 2% royalty on production from licenses, which was subsequently assigned to a third party.

On November 15, 2006, the Company 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, the Company 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.

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, behind its capital Ulaanbaatar. At the request of the Mongolian Ministry of Mineral Resources and Energy, Prophecy Coal commenced mining and trucked the first coal shipment to Sukhbaatar rail station, ready to be transported to Darkhan power plant by rail.

On November 9, 2010, Prophecy Coal received the final permit to commence mining operations at the Ulaan Ovoo Property and an official mine opening ceremony was held on November 20, 2010. On December 16, 2010, Prophecy Coal received the Ulaan Ovoo PFS, an updated prefeasibility study on the Ulaan Ovoo Property which is incorporated by reference into this AIF. The focus of the Ulaan Ovoo PFS was for the development of low ash coal reserves in the form of a starter pit.

In 2011, the Company spent \$32.6 million on preparing the Ulaan Ovoo Property for commercial production through development of infrastructure (\$2.7 million), purchase of mining and mobile equipment (\$16.4 million), transportation (\$2.7 million), mine development (\$9.3 million), and general working capital (\$1.6 million).

In 2012, the Company spent additional \$15.7 million for the Ulaan Ovoo Property. However, 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). A remaining coal stockpile as at October 2012 of 159,000 tonnes was used to supply coal sales during the period November 1 2012 to November 2013.

Since November 2010, the Company has removed and stockpiled approximately 3.6 million bank cubic metres of topsoil, overburden and waste and produced nearly 531,000 tonnes of thermal coal of different grades from the Ulaan Ovoo Property. Of this, the Company sold 403,234 tonnes for average proceeds of \$20.00 per tonne in 2011, \$18.6 per tonne in 2012 and \$29.00 per tonne in 2013. Mining recommenced October 23, 2013 as announced in the news release dated November 4, 2013, immediately after the Company's initial dewatering program. All required mining, safety, and transportation staff were re-hired. All of the Company's leased-out mining and transportation equipment were recalled and arrived back on site including a fleet of 3 operating mining excavators, 5 dump trucks, tipper trucks and other ancillary equipment. The Company continues to evaluate operating alternatives (e.g. electrification, conveyance vs. haul), infrastructure improvement, and further management changes.

During 2013 the Company produced approximately 89,000 tonnes of coal. As of December 31, 2013, the coal stockpile balance was approximately 119,900 tonnes with a value of approximately \$1.76 million.

The Company sold approximately 125,000 tonnes of coal during 2013 with total sales revenue of approximately of \$3,250,000. In addition, the Company earned approximately \$1,340,000 in revenue from leasing and renting out its idle equipment and staff while mining operations were suspended during the year.

Since resuming operations, the Company has estimated its average cash cost per tonne, including transportation & administration expenses, at approximately US \$29.50 per tonne and has experienced domestic average sales prices of approximately US \$36 per tonne for coal with GCV greater than 5,000

kcal/kg. On the other hand, average sales prices for coal with GCV less than 5,000 kcal/kg was \$20.50 per tonne. However, approximately over 60% of the Company's sales in 2013 consisted of sales of coal with GCV greater than 5,000 kcal/kg. Furthermore, domestic market prices for coal with GCV greater than 5,000 kcal/kg range from \$30 to \$50 per tonne, dependant on quantity and point of delivery. In addition, the Company's neighbouring market in the Russian regions realize sales prices for coal with GCV of 4500 kcal/kg to 5,000 kcal/kg ranging from 1800 to 2200 Roubles per tonne (US \$50 to US \$60 per tonne), dependant on point of delivery.

From the resumption of mining to the first quarter of 2014 the company has added some staff, acquired mining and pumping equipment and improved the management of the mine. This has enhanced mining capacity, made for production of new coal products, and improved the efficiency of the operation.

Impairment Write Down of Ulaan Ovoo Property

On December 31, 2012, the Company recorded a non-cash impairment write down of \$47,063,173 on the Ulaan Ovoo Property, which is reflected on the consolidated statement of operations. The impairment charge reduces previously capitalized deferred exploration within property and equipment, to a balance of \$2 million.

The impairment test was based on pre-commercial operating results along with capital expenditures and the 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 about 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 2012 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.

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 at \$2 million and recorded a \$47,063,713 non-cash impairment write-down.

The determined impaired value of \$2 million for the Ulaan Ovoo property as at December 31, 2012, remains unchanged at December 31, 2013. As there were no benchmark or market changes from October 1, 2013 to December 31, 2013, the impaired value for Ulaan Ovoo within property and equipment, remains unchanged at a balance of \$2 million. The costs in excess of impaired value, of \$2.36 million were expensed for the year ended December 31, 2013.

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 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 Wardrop PFS and per the NI 43-101 coal resources as determined by the 2007 Behre Dolbear report.

2. Chandgana Coal Properties

The Chandgana properties consist of the Chandgana Tal and Khavtgai Uul (formerly named Chandgana Khavtgai) properties. 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 Chandgana Tal properties. 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 property known as Chandgana Khavtgai. The Chandgana Properties consist of exploration and mining licenses, located in the Nyalga coal basin, approximately 280 km east of Ulaan Bataar, and are nine kilometres apart. Under the terms of the Chandgana Khavtgai agreement, Prophecy Coal paid a total of US \$570,000.

In June, 2010, Prophecy Coal completed a 13 drill hole, 2,373 metre resource expansion drilling program on the Khavtgai Uul Property, including 1,070 metres of core drilling, and five lines of seismic geophysical survey for a total of 7.4 line km.

Prophecy Coal received a Detailed Environmental Impact Assessment (“**DEIA**”) pertaining to the construction of a pit-mouth 600MW coal fired power plant on the Chandgana Tal property, which DEIA has been approved by the Mongolian Ministry of Nature and the Environment. The DEIA was prepared for Prophecy Coal by an independent Mongolian environmental consulting firm. The DEIA considers social and labour issues, climate and environmental circumstances representative of the proposed power plant. The approved study concluded that there are no major impediments to the project and provided recommendations on best practices for conservation of the environment and the community.

In February 2011, Prophecy Coal received the full mining license from the Mineral Resources Authority of Mongolia for the Chandgana Tal property. On November 21, 2011, the Company’s wholly-owned Mongolian subsidiary, Prophecy Power (former East Energy Development LLC), received a construction license from the Mongolian Energy Regulatory Authority (“**MEA**”) to construct a 600 MW power plant at Chandgana Tal. In May 2012, the Company entered into a Cooperation Covenant (the “**Covenant**”) agreement with the MEA to bring the Chandgana power project online by 2016. Prophecy Coal engaged Leighton Asia LLC to prepare a scoping level mine study for the Chandgana Tal property which was completed in December 2011. A preliminary economic assessment was later prepared by John T. Boyd Co. and received November 2012 for the Chandgana Tal licenses. The preliminary economic assessment has since been revised by John T. Boyd Co. and currently being finalized for filing. Prophecy Coal has also received a mining permit to mine coal on the licenses and can receive approval of a modification to mine up to 3.5 million tonnes per year within approximately 90 days.

In March 2013, Prophecy Power was granted 532.4 hectares of land to be used for siting the Company’s proposed Chandgana power plant (the “**Land Use Rights**”). A news release issued by Prophecy Coal on March 5, 2013 provides further information and can be found on the Company’s www.SEDAR.com continuous disclosure profile.

Prophecy Coal has been in on-going discussions with the Mongolian government to finalize a Power Purchase Agreement (“**PPA**”) that will enable Prophecy Coal to seek project financing and begin construction. Prophecy Coal has also had discussions with the Ministry of Natural Resources and Energy (“**NETGCO**”) (now Ministry of Energy) to discuss technical and commercial issues. 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 May 2013 the Company received official correspondence from the NETGCO outlining the terms of a tariff agreement, as described above in the PPA, reached between the NETGCO and Prophecy Power. A news release issued by Prophecy Coal on May 17, 2013 provides further information and can be found on the Company’s www.SEDAR.com continuous disclosure profile.

On June 5, 2013 Prophecy Power and Chandgana Coal executed a 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 US \$17.70 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.

In July 2013, the Company applied for a concession with the Ministry of Economic Development (MOED) for the power project. After extensive document submissions and discussions, the Mongolian Cabinet approved Chandgana Power Plant project as a concession project in January 2014. Subject to negotiations, a concession project may be entitled to stable tax rates, favorable VAT and customs duties, as well as other forms of government subsidies, endorsement and support; all of which can enhance bankability and lead to better financing options for the project. While the Company is pleased with the overall progress and appreciated support from various Mongolian authorities, it cannot offer certainty or a definitive time frame to conclude the Concession Agreement with MOED, or the Power Purchase Agreement with the Ministry of Energy.

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 plant's electrical power output.

Recent Financings

On March 8, 2012, the Company closed a non-brokered private placement, previously announced on March 1, 2012, of 22,363,866 Shares at a price of \$0.45 per Share for gross proceeds of \$10,063,740. Finder's fees of 6% of the proceeds, payable in cash, were paid on certain arm's-length portions of the placement. All Shares issued were subject to a hold period that expired on July 9, 2012. Proceeds of the placement were applied to technical work at the Chandgana Property, operations at the Ulaan Ovoo Property and for general corporate purposes.

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 units (each a "**Unit**") of the Company, of which each Unit consisted of one common share (a "**Share**") and 0.75 common share purchase warrant (a "**Warrant**"), at a purchase price of \$0.14 per Unit for aggregate consideration of \$613,560. Each whole Warrant is exercisable into one common share of Prophecy at a price of \$0.18, expiring two years from the date of issuance. Each Unit sold in the first tranche also included, subject to shareholder approval, which was obtained at the AGM on July 30, 2013, an adjustment warrant ("**Adjustment Warrant**") entitling the holder to acquire additional common shares of the Company. Finder's fees of 6% were paid in connection with a portion of the first tranche of the private placement.

On June 6, 2013, the Company closed a second and final tranche of the Private Placement with the issuance of 8,142,857 Units of the Company for aggregate consideration of \$1,140,000. Each whole Warrant is exercisable for one common share of Prophecy at a price of \$0.18, expiring two years from the date of issuance. Each Unit sold in the second tranche also included an Adjustment Warrant entitling the holder to acquire additional common shares of the Company. Finder's fees of 6% were also paid on the second tranche of the Private Placement.

The Company amended the first and second tranches of the Private Placement to include an additional Adjustment Warrant in each Unit sold in the Private Placement. Each Adjustment Warrant were exercisable 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 in the capital of Prophecy Coal. The fraction was to 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 were to be exercised in their entirety and not in part, and the holder of Adjustment Warrants could not sell any securities of the Company within 20 days prior to the exercise. Adjustment Warrants could also only be exercised to the extent that the holder continued to hold the Shares and Warrants comprising the Units of which the Adjustment Warrants were attached. A total of 12,525,420 Adjustment Warrants were issued and subsequently exercised resulting in the Company issuing 4,175,143 common shares on October 4, 2013.

Secured Credit Facility

In July 2012, Prophecy Coal arranged a Loan of \$10 million debt facility (the "**Loan**") with Waterton. The Loan had a one year term, due July 16, 2013, and bore interest at 14% per annum payable monthly with an effective interest rate of 24%. 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 17 to the annual audited consolidated financial statements).

On June 18, 2012, Prophecy Coal entered into a Sale and Purchase Agreement to acquire assets in Mongolia relating to certain Tugalgatai coal exploration property licenses from 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 included 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, \$10,189,400 was deposited in escrow in the period and included in restricted cash on the balance sheet. During October 2012, the funds, net of costs, amounting to US \$9.9 million was 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.

On November 5, 2012 the Sale and Purchase Agreement to acquire assets in Mongolia relating to certain Tugalgatai coal exploration property licenses from Tethys was terminated.

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.

In February 2013 Waterton agreed to waive the default, subject to certain conditions which have been met and were as follows: a) setting aside \$3.5 million in escrow, 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 Wellgreen Platinum common shares.

On July 15, 2013 the Company entered into the Extending Agreement. Prophecy Coal agreed to and completed a partial pay down of the principal loan amount from \$10 million to \$6.5 million (the "**Loan**") from cash in escrow (see (a) above) amounting to \$3.5 million and extending the maturity date from July 16, 2013 to October 31, 2013. As consideration for entering into the Amendment, the Company paid Waterton \$390,000 restructuring fees.

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

- (i) if such payment is of the entire outstanding principal amount of the Loan, the Company 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);
- (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 (the Company paid \$250,000 on July 12, 2013); and

- (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.

In November, 2013, the Company repaid the remaining balance of Waterton Loan, plus applicable fees and interest totalling \$7,039,005 pursuant to the Amended Loan Agreement and has been provided with a release/discharge of security interests, charges, and pledges.

Line of Credit Facilities

In August 2012, Prophecy Coal's wholly-owned Mongolian subsidiary, Red Hill Mongolia LLC ("**Red Hill**"), arranged a line of credit for US \$500,000 with the Khan Bank. The line of credit has a one year term, with the option of extending it, and bears interest at 14.4% per annum and a commitment rate of 2% per annum payable monthly. A structuring fee of 0.5% was paid in cash. The funds will be used for working capital and general and administrative expenses. The line of credit facility is collateralized by certain equipment. As at December 31, 2012, Red Hill had fully repaid the loan and nil amounts were drawn as of December 31, 2013.

In October 2013, Red Hill arranged a line of credit for US \$1,500,000 with the Trade and Development Bank of Mongolia. The line of credit has a 1.5 year term, with the option of extension, and bears interest at 15% per annum and a commitment rate of 2% per annum payable monthly. The funds were used for working capital and general and administrative expenses. The loan facility is collateralized by certain equipment and mineral and exploration licences. As at December 31, 2013, Red Hill had drawn down US \$1.5 million of the line of credit. Pursuant the LOC agreement, Red Hill shall pay a fixed amount of US \$125,000 monthly against the principal starting May 2014.

3.2 Significant Acquisitions

Any significant acquisitions in 2013, 2012, and 2011 are described in section 3.1 above.

4. DESCRIPTION OF THE BUSINESS

4.1 General

Prophecy Coal is engaged in exploring and developing coal properties and coal mine-mouth power projects in Mongolia. The Company holds a 100% interest in mining licenses in the Ulaan Ovoo Property and Chandgana Property in Mongolia, which have been estimated to host some 1.4 billion tons of measured and indicated high grade subbituminous B rank (ASTM) coal resources.

Market and Marketing

Prophecy's principal product is subbituminous B rank (ASTM) thermal coal from the Ulaan Ovoo deposit which is currently being developed and is in the pre-commercial production stage. The low calorific value of subbituminous coal results in a much lower price than for anthracite or coking coal. Subbituminous coal is usually not shipped long distances as the cost of doing so is prohibitive vis-à-vis its sales value. Its best use is in local thermal applications including making steam for electrical power generation.

Fresh coal deliveries from Ulan Ovoo started in November 2013 and over the course of the third quarter, the Company entered into binding coal sales contracts with a number of local buyers which involve the sale of approximately 10,000 tonnes of coal from the mine. The Company was also able to obtain binding contracts for coal sales delivered to Mongolian customers through Mongolia's Sukhbaatar rail station ("**Sukhbaatar**") totalling approximately 360,000 tonnes of coal. The buyers include cement plants, a metallurgical plant, a heat plant, chemical plants, a railway company and coal traders. The off-take quantities and variety of customers reflect the Company's significant efforts to drive higher margin sales while satisfying government power plant needs.

Competitive Conditions

The mineral exploration and mining industry is generally competitive in all phases of exploration, development and production. Prophecy Coal competes with other mining companies, some of which have greater financial resources and technical facilities, for the acquisition of mineral interests for exploration and development projects.

International coal pricing is generally established in US dollars and the competitive positioning between producers can be significantly affected by fluctuations in exchange rates. The competitiveness of coal producers is significantly determined by the quality of the deposit, production costs and transportation costs relative to other producers. Such costs are largely influenced by the location and nature of coal deposits, mining and processing costs, transportation and port costs, currency exchange rates, operating and management skills, and differing taxation systems between countries.

Components

All of the raw materials Prophecy Coal requires to carry on its business are available through normal supply or business contracting channels.

Mining Cycles

The mining business is subject to mineral price cycles. Since Prophecy Coal's mining and exploration business is substantially in the development stage, Prophecy Coal is not currently directly affected by changes in commodity demand and prices. Prophecy Coal's ability to fund ongoing exploration is affected by the availability of financing which is, in turn, affected by prices of commodities, the strength of the economy and other general economic factors.

Economic Dependence

Prophecy Coal's business is not substantially dependent on any one contract such as a property option agreement or a contract to sell the major part of its output. It is not expected that Prophecy Coal's business will be affected in the current financial year by the renegotiation or termination of contracts or sub-contracts although it continues to seek Mongolian export related approvals in connection with its Ulaan Ovoo production in order to sell output into the higher priced Russian market.

Environmental Conditions

All aspects of Prophecy Coal's field operations are subject to environmental regulations and generally require approval by appropriate regulatory authorities prior to commencement and continuous monitoring. Any failure to comply could result in fines and penalties. Should any projects advance to the production stage, in addition to Ulan Ovoo, more time and money would be involved in satisfying environmental protection requirements.

Employees

As of December 31, 2013, Prophecy Coal had approximately two employees and two contractors or consultants in Canada and 226 employees and 22 contractors or consultants in Mongolia. Prophecy Coal utilizes consultants and contractors to carry on many of its activities. As Prophecy Coal expands its activities, it is probable that it will hire additional employees and engage additional contractors.

Foreign Operations

Prophecy Coal currently holds an interest in certain exploration stage and development stage mineral resource properties located in Mongolia and, as such, Prophecy Coal's business is exposed to various degrees of political, economic and other risks and uncertainties inherent in any developing economy. Prophecy Coal's operations and investments may be affected by local political and economic

developments, including expropriation, nationalization, invalidation of government orders, permits or agreements pertaining to property rights, political unrest, labour disputes, limitations on repatriation of earnings, limitations on mineral exports, limitations on foreign ownership, inability to obtain or delays in obtaining necessary mining permits, opposition to mining from local, environmental or other non-governmental organizations, government participation, royalties, duties, rates of exchange, high rates of inflation, price controls, exchange controls, currency fluctuations, alleged political and bureaucratic corruption, taxation and changes in laws, regulations or policies as well as by laws and policies of Canada affecting foreign trade, investment and taxation of repatriated earnings, if any.

Bankruptcy and Similar Procedures

There are no bankruptcies, receiverships or similar proceedings against Prophecy Coal, nor is Prophecy Coal aware of any such pending or threatened proceedings. There has not been any voluntary bankruptcy, receivership or similar proceedings by Prophecy Coal during its last three financial years.

Reorganization

Other than the two mergers and two spin-offs described in section 3.1 above, Prophecy Coal has not completed any reorganizations in the last three financial years.

Social or Environmental Policies

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. Prophecy Coal's management, with the assistance of its contractors and advisors, ensures its ongoing compliance with local environmental and other laws in the jurisdictions in which it does business.

Prophecy Coal is committed to continually improving the lives of those who work for, partner with and host Prophecy Coal in their communities. Prophecy Coal's goal is to work with community stakeholders to make positive contributions to local economic development. Prophecy Coal places a priority on hiring local workers and assisting in supporting local community development projects, where it can. In Mongolia, Prophecy Coal sponsors a children's charity.

5. MINERAL PROJECTS

The information in this section of this AIF has been extracted fully or where appropriate in part, from the Ulaan Ovoo Technical Report and the Chandgana Technical Report, as applicable. New information is provided where appropriate. Portions of the following excerpts are based on the assumptions, qualifications and procedures set forth in the respective technical reports which are not fully described herein. For a complete description of assumptions, qualifications and procedures associated with the information contained in each technical report, reference should be made to the full text of each technical report available under Prophecy Coal's, or Wellgreen Platinum's, profile, as applicable, on www.SEDAR.com.

5.1 Ulaan Ovoo Property

Property Location, Ownership

The Ulaan Ovoo Property is located in the territory of Tushig soum (sub province) of Selenge aimag (province) in Northern Mongolia. It is 8 kilometres west of the central village of Tushig soum and 17 km away from Mongolian-Russian border port of Zelter.

Figure 1 Location of Ulaan Ovoo Coal Project

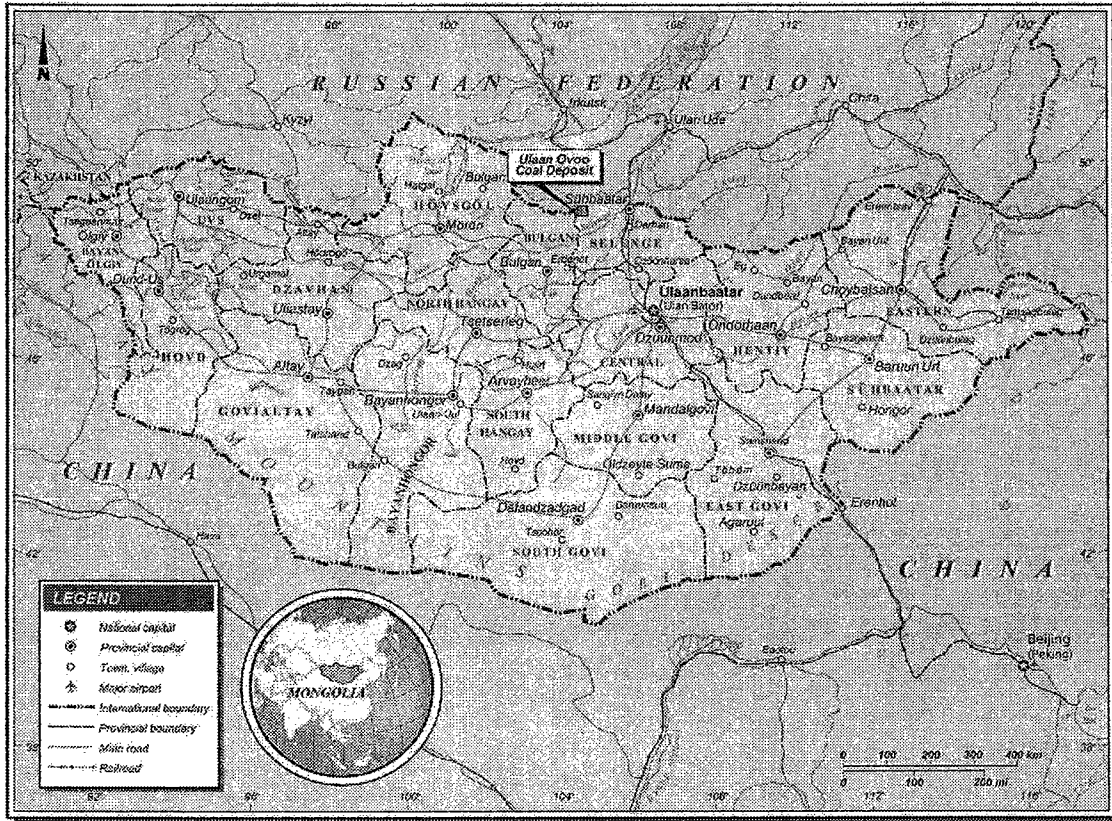


Figure courtesy of Minarco MineConsult

The Ulaan Ovoo Property is situated in the Zelter River valley, which runs between the Zed and Buteel Mountain Ranges in Northern Mongolia. The river flows from southwest to northeast and exits northward into Russia at the Zheltura Border Crossing, 17 km northeast of the project area. Geographically, the district is included in a region having medium-sized mountains, the highest altitude being 1,800 metres. The south half of the deposit underlies the flood plain of the Zelter River and the north half lies on the southern flank of a low hill to the north and above the flood plain. Surface elevations at the project site range from 764 m to 820 m above sea level.

The deposit area covers an area of approximately 790 hectares. Red Hill, which is owned and controlled by Prophecy Coal, holds the Ulaan Ovoo Property under mining licenses MV-1231, which covers an area of 214 ha and mining license MV-14657 with an area of 355 ha. The licences are for a term of 30 years with a 40-year extension option. In November 2006 Red Hill purchased 100% of the title and interest in six exploration licences - 6830, 6831, 6832, 6834, 6837 and 12170 - contiguous to or near MV-1231 and MV-14657.

Accessibility, Climate, Local Resources, Infrastructure and Physiography

Property Access

The Ulaan Ovoo Property is accessible via paved highway, maintained double lane dirt road and then unmaintained road; or by railway followed by unmaintained road. The various means of access are:

- Access by road from Ulaanbaatar (427 km) - Proceed northward from Ulaanbaatar via Altanbulag-Ulaanbaatar highway A0401 to the central village of Shaamar soum (sub-province) (300 km). Then, via a maintained dirt road, which connects Shaamar, Zuunburen, Tsagaannuur

and Tushig soums (119 km). This segment of the trip includes crossings of the Orkhon, Selenge and Zelter Rivers by concrete bridges. The last segment of the trip is via a maintained dirt road from the central village of Tushig soum, to the deposit (8 km);

- Access by railway (498 km) - The Trans-Mongolian railroad runs to Shaamar Soum station from Ulaanbaatar (384 km) from where a maintained dirt road leads to the deposit area as described above (114 km);
- Access by road from Russia (162 km) - Access to the project is via a 120 km concrete road from Galuutnuur village to Petropavlovsk village, then another 25 km on maintained dirt road to the border village of Zheltura port, then another 17 km on dirt road to the project site; and
- Access to market – the Ulaan Ovoo Property is 137 km from year-round Naushki border port and 12 km from Zeltura border port which Prophecy Coal is in process of reopening.

Climate

The Ulaan Ovoo Property has a sharply continental climate with predominately hot summers and cold winters. The area is hot and relatively rainy in summer, with highest temperatures of 35° to 40 degrees Celsius (°C) in June and July and cold in the winter, with lowest temperatures in the range of minus (-) 35° to -40°C in December and January. Annual precipitation fluctuates between 100 millimetres (mm) and 500 mm and most (60% to 70%) of it falls as rain in August. Maximum snow depths may reach up to 2m where drifted but averages 10 centimetres (cm) to 20 cm where not drifted. Wind usually blows from northwest to southeast with an average speed of 14 kilometres per hour (km/h) to 24 km/h.

Local Resources & Regional Infrastructure

The Ulaan Ovoo Property is located within the territory of Tushig soum (sub-province) of Selenge aimag (province) and the nearest settlement to the deposit is the soum's central village, also called Tushig, located approximately 7 km to the southeast of the project area. The soum borders the state of Buryatia of Russia to the north, Bugat soum of Bulgan aimag to the west and Tsagaannuur soum of Selenge aimag to the east and south. Tushig soum has a territory of 276 square kilometres (km²) and a population of 7,500.

Physiography

The Ulaan Ovoo Property is situated in the Zelter River valley, which runs between the Zed and Buteel Mountain Ranges in Northern Mongolia. The river flows from southwest to northeast and exits northward into Russia at the Zheltura Border Crossing, 17 km northeast of the project area. Geographically, the district is included in a region having medium-sized mountains, the highest altitude being 1,800 m. The south half of the deposit underlies the flood plain of the Zelter River and the north half lies on the southern flank of a low hill to the north of and topographically above the flood plain. Surface elevations at the project site range from 764 m to 820 m above sea level.

Mountainous parts of the region have taiga-like forests of conifer and deciduous trees. The southern aspects of the hills in the area tend to be relatively treeless. Braided stream deposits covered with a mixture of small trees and bushes form the Zelter River valley flood plain. The north half of the coal deposit area is treeless and the south half is covered by willows and birch. Fertile soil is up to 4 m thick at the flood plain of the river valley and 20 cm to 30 cm on the adjacent hillsides.

History

Under the Mining law of Mongolia approved in 1994, Erdenet, a Mongolian-Russian state-owned joint venture, was granted Mining License Number (No) 166 for the Ulaan Ovoo Property in Tushig soum, Selenge aimag, on 2nd November 1995, by the Ministry of Energy, Geology and Mining, for a term of 10 years.

After the enactment of the new Minerals Law of Mongolia in July 1997, the Director of the office of Geological and Mining Cadastre granted a revised mining licence certificate No 1231A to the Ulaan Ovoo Property to Erdenet, the Mongolian-Russian joint venture.

Under a decision No. 880 (2002) the director of the Office of Geological and Mining Cadastre and with accordance to Minerals law of Mongolia, the Mining Licence No. 1231A was then transferred to a Mongolian-Chinese joint venture company called Mongolia Mid Asia International (MMAI) on 14th December 2002.

MMAI was restructured into a 100% Mongolian-owned company in 2005. The State Registration Office registered the company and the mining licence of the Ulaan Ovoo Property was renewed and granted to the newly restructured MMAI in compliance with the Minerals Law of Mongolia on 5th June 2005, for a term of 55 years.

Exploration Licence No. 5895X, covering an area adjacent to the licence No. 1231A, was granted by the director of the Office of Geological and Mining Cadastre to MMAI to be an additional portion of Ulaan-Ovoo Property on 6th June 2003.

An option to purchase these properties was entered into between UGL Enterprises LLC, a fully-owned Mongolian subsidiary company of Red Hill, and Ochir LLC, the parent company of Mongolian MMAI, in November 2005.

In November 2005, Red Hill purchased both licences and in November 2006, purchased the 6 exploration licence areas surrounding the deposit.

History of Geological Exploration Work

The first official geological survey work was undertaken by the Russians in 1974-1975. The fact that the Ulaan Ovoo Property had coal was known before this survey because a ravine adjacent to the deposit had been traditionally called the 'coaly ravine'. This study recommended further coal exploration work and drilling.

Between 1979 and 1982, the Russians conducted geological mapping studies in the Selenge and Bulgan aimags. This work integrated stratigraphic, magmatic and regional tectonic data around the Ulaan Ovoo Property and resulted in the first 1:200,000-scale geological map of the area. The exploration work included mapping, trenching and drilling undertaken in 1979.

In-fill drilling and coring was conducted in 1993 through to 1995.

In April 2006, a programme to confirm previous exploration was undertaken by Red Hill. The previous drilling was conducted under the Russian system and there was some question as to whether or not the drilling adequately portrayed the deposit. In all, 11 holes were drilled under the aegis of this new programme.

History of Production

At the request of the authorities of Tushig and Tsagaannuur soums, a small open pit in the sooty (weathered) coal was exploited starting 1998. The open pit or strip mine was 70 m long and 30 m to 35 m wide. The highwall was 5.3 m to 5.6 m high and the average mining output was 1,500 to 2,000 tonnes per year. The mining was extremely simple as the sooty coal was loaded by hand shovel onto the consumer's truck and hauled from the site.

The combined consumption of the two soum centres was 1,500 t/a to 2,000 t/a, judging by the extent of exploitation. At the beginning of October 2005, the current licence holder, MMAI, signed a contract with the local authority providing that the payment for the coal mined be credited to an environmental protection fund in an account created by the Governor of the Tushig soum. In accordance with the

Mineral Law of Mongolia, MMAI prepared a mine plan. Red Hill has paid the Mongolian Government the corresponding mining licence fees since 2006.

In August 2008, approximately 25,000 t of partially oxidised coal were removed from the open pit to a maximum depth of 15 m, as part of the preparation work required to take a bulk sample. The coal was separated from the overburden and stockpiled south of the pit for easy access. The now much larger pit has been closed to vehicle access and local consumers will have enough stockpiled coal to supply them for several years.

Geology

The Ulaan Ovoo Property is in the Orkhon-Selenge coal district and the Zelter coal basin and is the middle deposit of a series of five coal deposits that trend northeast to southwest and parallel the Zelter River. It is part of the Sharyn Gol formation which is composed of continentally derived tuffaceous-sandstone, tuffaceous-conglomerate, conglomerate, sandstone, siltstone, mudstone and coal.

Sediments in the Sharyn Gol formation are thought to be about 500 m thick and are subdivided into:

- Upper Member: 130 m of shale with ash grey colour, medium-grained grey sandstone and a low hydrocarbon content oil shale;
- Middle Member: 170 m of shale, conglomerate, coal and carbonaceous coal; and
- Lower Member: 200 m of tuffaceous conglomerate and sandstone, andesite basalt, schist and conglomerate.

The northeast outcrop of the coal has burned at the north end of the deposit forming red clinker material. A hill is formed over this more resistant clinker. The Mongolian language words for this red hill are Ulaan Ovoo. It is thought that the coal was set on fire by lightning or some other natural cause.

The structure at the site consists of a gentle to moderate-dipping basin or syncline within the fault blocks. The syncline is 1.5 km wide and 2 km long.

There are high angle normal faults on the east, south and west sides. The fault on the east side trends roughly North (N) 10 degrees (°) West (W) and the downthrown side is the coal-bearing west side; the fault on the south side is also a high angle normal fault trending N 70° East (E) with the downthrown side being to the north and the west fault is a normal fault trending N 10° W with the downthrown side being the east side.

A high angle reverse fault trends northwest-southeast through the centre of the deposit and divides it into north and south (S) blocks. Throw on the fault is 10 m - 20 m and the downthrown side is the north. A moderate (20° - 30°), southward dipping coal subcrop on the north side of the deposit. Igneous activity is evidenced by the 137 m of horizontally-bedded basalt. Eleven holes were drilled by Red Hill in 2006.

Exploration

During 2006 Red Hill conducted an exploration drill programme which undertook the drilling of 11 drill holes from surface identifying the presence and delineation of the coal seams present at the site. This exploration programme formed the basis of the Behre Dolbear report supported by non-compliant data gathered during the period from the early 1970's up to 1992. This data was collected by a Russian entity in control of the project at that time.

In April 2010 the Company merged with Red Hill as described in section 3.1 and therefore assumed control of the permits and licences under the auspices of Red Hill. During 2010 Red Hill drilled one drill hole to obtain samples for grade control and marketing efforts. During 2011 Red Hill drilled nine drill holes to obtain grade control information and rock mechanics data.

Mineralization

The Ulaan Ovoo Property, which is part of the 520 m thick Sharyn Gol Formation, has two main coal seams that contain five sub-units of coal.

Mod Coal Seam (formerly Coal Seam 1): This seam is the lower of the two main coal sequences. It merges with the upper and thicker Gol Coal Seam in the north-eastern part of the area and splits to the southwest. It is well developed in the western part of the syncline. Its thickness ranges from 2.0 m to 7.5 m and thins in the south-western part of the deposit. The seam contains up to three partings with thicknesses of 0.56 m to 0.77 m. In the area where it is best developed, the Mod Coal seam is separated from the Gol Coal Seam by a sandstone parting which may exceed 30 m in thickness.

Gol Coal Seam (formerly Coal Seam II): This is the uppermost of the two main coal seams. Because of limited drilling south of the Central fault, it had previously only been clearly defined in the northern half of the syncline. It has relatively consistent thickness in the northern half of the deposit, ranging from 29.8 m to 63.9 m. In the west, the Gol Seam splits into two major sub-seams and its aggregate thickness diminishes where it splits. Further to the west sub-seam the lower split further subdivides into two smaller sub-seams. The Gol seam may contain as many as 11 partings. These partings consist mainly of clayey rocks and coal-bearing mudstone with a thickness of 0.15 m to 1.0 m. With proper design, the thickest of these partings can be removed during the mining process. Consequently, the partings will not represent a serious diminution of coal quality if properly handled.

Several thin coal beds are encountered to the west of the syncline, in the lower part of the middle member of the Sharyn Gol formation (J2-3 chg). Their thickness ranges between 0.9 m and 2.0 m. The extent of these thin seams is not known at this time, but they do not add materially to the coal resource base of the deposit. The cross sections shown in Section 7.0 show the style of splitting of the coal seams across the deposit area.

To date, the following four studies have been completed on the Ulaan Ovoo Property: Russian study completed in 1995; Mongolian University study completed in 1992-1995; Behre Dolbear study completed in 2006; and Minarco study completed in 2009. Each of these studies has produced its own coal seam nomenclature system, as well as criteria for applying nomenclature criteria. In order to not further confuse this issue, it was decided to use the nomenclature developed by Minarco in their 2009 NI-43-101 report.

Drilling

The Company has conducted three drilling programmes on the property. Eleven holes were drilled by Red Hill in 2006 to obtain coal resource and coal quality information. Average core recovery was reported at over 90% for 10 of the holes and over 98% for 6 of the holes. Core recovery for hole UGL-06-002 was less than 35% and the hole was re-drilled as hole UGL-06-003. One drill hole was drilled in 2010 for grade control and marketing efforts. Nine drill holes were drilled in 2011 within the mine pit area to obtain grade control information and rock mechanics data. The 2011 drill holes generally had poor core recovery because the drilling was done in the winter.

Sampling & Analysis

Sampling during the 1979 and 1992-1995 programmes focused on determining the quality and calorific value of the coal, its petrography and composition and strength properties of the confining sediments and partings. Coal seams were sampled separately from over, inter and under-burden material. Different tests were run on different coal samples depending upon visual features in the coal.

The sampling from the 2006, 2010 and 2011 Ulaan Ovoo drilling was done at constant intervals to allow for comparison of coal quality. Samples were taken every 0.9 m to 1.2 m for oxidised coal and every 3 m to 5 m for non-oxidised coal. When partings were greater than 0.1 m in thickness, they were sampled separately for analysis.

Security of Samples

The coal sampling undertaken for the 2006 and 2011 drilling programmes followed standard industry procedures. Sampling was conducted in 1 m intervals and at the start and stop of core runs and in a timely fashion after all necessary core descriptions and photography tasks had been completed. The core was then washed to remove contaminants and allowed to drain away from the core. The core was then placed in plastic sleeves (15 micron) and into wooden core boxes for protection.

The criteria used for selecting sample intervals included: Bone coal was sampled in the same way as coal. Partings that were less than 0.3 m thick were included with coal; where partings were encountered between 0.3 m and 1.0 m in thickness they were split into three, the upper and lower splits were sent to the lab and the middle split was archived. For partings over 1.0 m thick, the lower and upper 0.5 m were sampled separately and sent to the lab and the middle split was archived; Where the coal seam is flanked by rock then samples were taken from above and below the coal seam and are referred to as the roof and floor materials. Stray Coal seams greater than or equal to 0.5 m were sampled; and maximum sample intervals were limited to the core barrel length (3.05 m) where coal was not interrupted by partings greater than 0.3 m thickness.

All lab analysis was conducted following ASTM standard procedures by SGS Laboratories in Denver, Colorado and all lab duplicate samples are stored there. All non-lab core is stored in wooden boxes in a secure warehouse on site. All sampling handling used chains of custody to monitor the distribution of the samples.

Data Verification

In March 2010, Wardrop verified the data as part of a study to estimate the reserves and economics of a starter pit. They reviewed the available Ulaan Ovoo digital data, visiting the Property and conducted meetings with Red Hill's geological staff and decided that the following data from the Minarco 2009 study was acceptable and would be used: drill hole data from the 2006 programme; coal seam nomenclature and correlations; gridded surfaces for coal seams and partings; central, east, south and west faults; coal outcrop, burned coal (clinker) area coal resource classification criteria; and the coal resource area. The coal seam correlations developed by the Minarco 2009 study were correct and the coal resources reported in the Behre Dolbear 2006 and Minarco 2009 reports were considered valid.

Mining

A recommendation was made for the coal deposit to be mined by open pit methods.

A mining contractor was to mine 250,000 tonnes (t) of product coal in 2010 and 1.1 million (M) t of product coal in 2011. It was assumed that the contractor would operate the owner's mining equipment in year 2011 on a fee basis. Mining has been done by an owner-operated mining team starting in year 2012.

Contract mining was completed using an 85 t backhoe loading 50 t capacity haul trucks. Since the initial mining was near the surface, the use of drilling and blasting methods was not employed. Use of a contractor allowed for sufficient time to purchase, manufacture and ship the owner-operated mining fleet to site in 2011 for operation in 2012.

The proposed "owner-operated" mining methodology is to employ conventional drill and blast techniques, using a rotary drill capable of drilling the blast holes in a single pass. A high mining recovery is anticipated. Dilution and losses of 0.10 m and 0.25 m per contact or parting respectively have been factored into the recovered tonnage figures. Loading and hauling will use 11.5 cubic metre (m³) front end loaders, with 90.9 t rigid frame dump trucks. Track dozers are being used to clean coal-waste interfaces and thus minimise the losses and dilution.

A fleet of support and maintenance equipment has been included to maximise availability. Considerable emphasis has been placed on good design and construction of mine haul roads and other infrastructure to ensure high productivity. Emphasis is being placed on training the local labour force for the unskilled and semi-skilled jobs. The majority of the managerial, technical and skilled staff are either ex-patriots or from other regions of Mongolia. Sites adequate for the disposal of waste rock and a suitable stockpile area for the high ash coal exist within the property in the immediate area of the open pit.

Mineral Reserves

The material captured within the Mineral Reserve has been categorised as 100% Measured material. The reserve estimation only includes coal contained within the G3, G2, G1a, G1b, G1c, G1d coal seams as set out as the nomenclature for the Gol coal seam.

The other seams present at the Ulaan Owoo Property do not fall within the pit design and are therefore excluded from the Mineral Reserve estimate. Further exclusions from the Mineral Reserve estimation are any coal occurrences to the south of a 200 m “No Mining Limit” from the northern banks of the Zelter River. Therefore it could be said that the Mineral Reserve estimate considers only the first phase of the project development of the Mineral resources contained in the Ulaan Owoo Property.

Losses and dilution factors have been applied globally to the partings and the separate coal seams to derive a final Mineral Reserve. The block model created in SURPAC® was prepared and exported for use with the Whittle Optimiser software. The resultant pit shells that were created in Whittle formed the basis of the pit design which was conducted using the GEMS software package. The pit design took account of the assumed slope angles and ramp angles as recommended by the MUST “Summary of Feasibility Study for the Development of Ulaan Owoo Bituminous Coal Deposit” (2004) conducted on behalf of Red Hill.

Once completed, the phased pit designs were imported into SURPAC and reported from the original block model to derive the in-situ reserves by seam. This data was then compiled in Microsoft Excel to derive a total in-situ reserve estimate. The losses and dilution parameters were applied to the in-situ reserves and the resultant changes can be seen in Table 1.

**Table 1
Ulaan Owoo Coal Reserve Statement**

Coal Reserve Statement Description	Amount
Product Coal (kt)	20,724
Waste (kBCM)	37,268
Stripping Ratio (BCM:t)	1.8
Ash Content (%)	11.3
Calorific Value (kcal/kg)	5,040
Moisture (%)	21.7
Mine Life (years)	10.7
Process Rate (kt/a)	2,000

Note: BCM – Bank Cubic Metre

*Coal qualities are stated on an “as-received” basis.

The reserve extraction is considered to be 98.6% as a ratio of In-situ reserve to Saleable Product. The In-situ Reserve calculations were validated by internal checks as part of the Wardrop internal quality control system. A further 720,000 t of High Ash coal will be stockpiled and washed at a later time but cannot be considered within this reserve estimate because it has been assumed that there are no wash plant facilities available on site.

The resource extraction is considered to be 10.7% as a ratio of Saleable Product to Measured & Indicated Mineral Resource. This illustrates the phased approach of Resource Development that has been considered in this study. It is recommended for further project development that more drilling is

carried out North and South of the River Zelter and a separate more detailed analysis is carried out to include the engineering and costs to divert the river in order to include more of the Mineral Resource in a more detailed reserve estimate.

The estimated reserve and other mine characteristics are shown in Table 1.

Coal product tonnages and qualities stated in Table 1 are stated on a Run-of-Mine (ROM) basis and take into account mining loss and rock dilution at coal/rock interfaces. The total proven Mineral Reserve Estimate is 20.7 Mt of Product (Low Ash) Coal.

As there is no coal beneficiation to be undertaken, any high ash coal is to be stockpiled so that it will be available if a wash-plant is built in the future. In general the product coal is G3, G2, G1a, G1b, G1c and G1d. The "Mod" or M series of seams are high ash and are not recovered. Opportunity exists to recover these seams if a wash-plant is constructed at some point in the future.

The southern edge of the pit is defined by the location of the Zelter River plain. Construction of a capital intensive river diversion, water cut-off wall and flood containment berm will be required to prevent water inflow into the pit if the river valley is encroached by the pit limit.

Environmental

Wardrop has not been requested to perform any evaluation or review of the environmental assessments or permits as part of this report. However a detailed Environmental Impact Assessment has been completed and approved by the Mongolian Government in 2008 and an Annual Environmental Protection Plan for 2010 has also been approved by the Mongolian Ministry of Environmental Protection.

Prophecy Coal has supplied Wardrop with details of additional environmental and mining permits approved by the Mongolian authorities. These include the mine plan approval, land use permission, water utilisation permission, emergency response plan, border zone permission and road repair permit. An amount of US \$2 M has been included in the financial evaluation for mine reclamation.

Cost Estimates

Operating

The operating cost estimate is summarised in Table 2.

Table 2
Ulaan Ovoo Operating Cost Estimate

Area	Unit Cost (US \$/ Product Coal)
Coal Mining	9.40
On-Site Coal Handling	0.35
Administration & Overhead	0.48
Total	10.23

The above unit operating cost is the average for life-of-mine including contractor and owner-operated mining. Contractor costs include equipment lease costs.

Capital

Table 3 outlines the estimated initial project capital cost by category. Mobile equipment fleet includes the main production equipment such as loaders, blast-hole drills and haulage trucks as well as support ancillary equipment. Site infrastructure costs include site earthworks, buildings, and services such as water, electrical and sewage. Road transport includes road and bridge refurbishment and road haulage

fleet. Project indirect cost includes EPCM (engineering, procurement, construction and management), freight, equipment spares and first fills. Owner's costs include land acquisition and head office costs.

Table 3
Ulaan Ovoo Capital; Initial Capital Summary

Area	Unit Cost (US \$ M)
Mobile Equipment Fleet	32.3
Site Infrastructure	7.0
Project Indirect	6.4
Owners Cost	0.3
Road Transport	15.5
Reclamation	0.3
Subtotal	61.8
Working Capital	4.0
Contingency	3.9
Total	69.7

Sustaining capital is listed in Table 4. Sustaining capital is for replacement of major mining equipment at the end of life. This includes loaders, haul trucks, dozers and graders. An annual value of US \$500,000 per year has been applied for sustaining capital site infrastructure.

Table 4
Capital; Sustaining Capital Summary

Area	Unit Cost (US \$ M)
Mobile Equipment Fleet	14.0
Site Infrastructure	4.5
Total	18.5

Financial Analysis

A financial evaluation of the Ulaan Ovoo Property was prepared by Wardrop based on a post-tax financial model. For the 10.7 year mine life the following pre-tax financial parameters were calculated: a 25.5% Internal Rate of Return (IRR); 4.5 years payback on US \$85.9 M capital and US \$71.0 M Net Present Value (NPV) at 10% discount value.

Sensitivity analyses were carried out to evaluate the project economics with plus 30%, minus 30% the base case coal price.

Table 5
Ulaan Ovoo Coal Price Scenarios

Scenario	Coal (US \$ /t)
Minus 30%	28.0
Minus 20%	32.0
Minus 10%	36.0
Base Case	40.0
Plus 10%	44.0
Plus 20%	48.0
Plus 30%	52.0

The post-tax financial model was established on a 100% equity basis, excluding debt financing and loan interest charges. The financial outcomes have been tabulated for NPV, IRR and pay back of capital. Discount rates of 10% were applied to all cases identified by coal price scenario. The results are presented in Table 6.

Table 6
Ulaan Ovoo Summary of Post-Tax NPV, IRR, and Payback

Scenario	NPV 10 (US \$ M)	IRR (%)	Payback (Yrs)
Minus 30%	-62.28	-4.4	13.1
Minus 20%	-17.82	6.1	10.7
Minus 10%	26.58	15.8	7.0
Base Case	70.98	25.5	4.5
Plus 10%	115.38	35.7	3.6
Plus 20%	159.77	46.8	3.1
Plus 30%	204.17	59.2	2.7

Conclusions

The financial evaluation indicates that the project should be economically viable given the coal pricing assumption of US \$40 per product tonne sold at the Russia/Mongolia border port of Naushki. To date the Company's revenue from coal has come from sales prices of less than half to two thirds that figure. Viability of the deposit is contingent on being able to market the Ulaan Ovoo coal at higher prices such as into Russia where these prices can be obtained.

Project Risks and Mitigation

There are a number of project risks which have been mitigated where possible. The regional coal market has been difficult to penetrate and yet earn an acceptable margin on the coal. Though a number of coal contracts have been signed for Ulaan Ovoo coal only a handful are for substantial volumes or have reasonable margins. The market is not fully open where an independent producer has an equal opportunity to compete. Transportation is not always available at the time, in the capacity, or at the cost desired. These risks have been mitigated to some degree by decreasing mining, overhead, and transportation costs which recently appear to have made other markets available. Most recently receivable amounts from the large utility customers have become overdue. The decreased revenues forced temporarily idling the mine.

The Ulaan Ovoo Property does not include a preparation plant risking the production of non-specification coal. To mitigate this situation, high ash coal and partings are separated from the coal in-pit. This is done by the mine geologist identifying these materials, monitoring their removal by trained excavator operators during daylight hours, and constant supervision. Continual grade control sampling and assaying is performed and coal quality predictions made. This work has made for better control of the grades of coal produced.

Groundwater inflow to the pit, especially where recharged by the Zelter River is a risk to mining operations. Pumping water from the mine pit has stopped production at times. Larger capacity pumps were purchased which have partially mitigated this risk. The May 2009 Minarco report recommended construction of a dike to divert the north meander of the Zelter River away from the mine. During 2011 dewater wells were proposed and budgeted to reduce the water inflow. The dewater wells were installed during 2012 and reduced water inflow into the mine.

Operation Statistics

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 Ulaan Ovoo PFS. 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 are as follows:

Resources mt	Reserves mt	Life of Mine years	Heating Value kcal/kg	Ash wt, %	Moisture wt, %	Strip Ratio BCM/t
209	20.7	10.7	5,040	11.3	21.7	1.8

Resources are from the 2006 Behre Dolbear NI 43-101 report. All resources are in the measured and indicated reliability categories. Reserves, life of mine, 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 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. Coal quality is stated on the as-received basis. 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.

The mine, which started operations in November 2010 through the mining contractor, Leighton Asia Limited ("**Leighton**") 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. Prophecy Coal discontinued its mining contract with Leighton in August 2011 to reduce mining costs. Prophecy Coal then recruited and trained its own employees to mine at the Ulaan Ovoo mine.

Prophecy Coal acquired its two fleets of mining equipment for \$14.7 million including: One CAT 390 Excavator, one CAT 385C Excavator, three CAT 773D Dump Trucks, three CAT 773E Dump Trucks, two CAT D8R Dozers, one CAT 160K Grader, one CAT 160H Grader, one CAT 928G Loader, one Liebherr 580 Loader, eighteen Scania 30t Tipper trucks, two Nissan Water Trucks (for purpose of road maintenance), four 20t Nissan tipper trucks, one road roller, diesel generating and lighting plants and other equipment. In 2013, approximately \$0.5 million was spent on an Explorer 1500 3D coal screener, a CAT C18 diesel power generator, three water pumps and surveying equipment.

Prophecy Coal has completed a geologic model of the area comprising the two Ulaan Ovoo licenses. This model was used to develop mine plans and schedules for use in near and long term mine management and coal marketing.

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). Prophecy Coal laid-off 108 mining staff and paid aggregate severance of \$73,100 to comply with local employment laws. Some 18 staff members remained on site for equipment and site maintenance, shipping and security operations during the suspension. With little local employment competition, the local labour force was expected to remain available for prompt rehire when needed. Transport of inventory coal from existing coal stockpiles resumed during November 2012.

The Company pumped the water from the pit and prepared to mine coal during October 2013. The leased equipment was recalled, employees rehired, and other preparations made and mining restarted November 2013.

Prophecy Coal secured a rail siding at Sukhbaatar with capacity of 40,000 tonnes. During the year ended December 31, 2013, Prophecy Coal trucked approximately 122,711 tonnes of coal from the mine to the rail siding (123,213 tonnes - December 31, 2012).

During August 2011, Prophecy Coal signed coal sales agreements with Mongolian and Russian power plants for total sales of 92,000 tonnes of coal. Prophecy Coal sold 133,895 tonnes of coal of two grades - 4,200 GCV and 5,100 GCV (arb) to both Mongolian and Russian companies during 2011. For the year ended December 31, 2012, Prophecy Coal sold 131,739 tonnes of coal. The coal inventory as at December 31, 2012 was 131,899 tonnes. For the year ended December 31, 2013, Prophecy Coal sold 124,897 tonnes of coal and had 119,900 tonnes of coal in inventory as of year end. Subsequent to year end, the Company shipped approximately 40,000 tonnes of coal to local customers. The coal stockpile balance is approximately 103,000 tonnes as at the date of this AIF.

Since the Ulaan Ovoo mine is still in pre-commercial production status, revenue from coal sales are being credited to, and the related cost of production are being charged against and capitalized to property and equipment, respectively.

Impairment Write Down of Ulaan Ovoo Property

The impairment write down of Ulaan Ovoo Property is described in the section 3.1 - *Summary of Five Principal Mineral Projects* above.

5.2 Chandgana Properties

The Chandgana Properties consist of the Khavtgai Uul and Chandgana Tal licenses. These licenses are approximately 10 kilometers apart and are located in similar physiographic and geologic settings.

Khavtgai Uul Property

Project Description and Location

The Khavtgai Uul Minerals Exploration License held by Chandgana Coal LLC, a subsidiary of Prophecy Coal is one of the Chandgana Properties and is found in the southwest portion of the Nyalga Coal Basin. The license is located 295 kilometres east of Ulaanbaatar in Moron soum (sub-province) of Khentii aimag (province), Mongolia. The coal-bearing portion comprises approximately 1,636 hectares. The other coal exploration licenses adjacent to the resource area are held to the north by Tethys, a fully-owned subsidiary of Companhia Vale do Rio Doce, and to the west by Adamas Mining LLC. The resource area has a continental climate with short warm summers and longer cold winters and is generally favourable for development of the coal resource.

The resource area is located in the Nyalga Depression within the Khentii Zone of the Khangai-Khentii fold system and is part of the Shorvogo Steppe physiographic province along the northern margin of the Gobi Desert. The topography is relatively featureless with a mean surface elevation of 1,142 metres.

The coal seams belong to the Early Cretaceous age Zuunbayan Formation and are part of the southern end of the headwall portion of a faulted syncline. The coal seams subcrop at and just west of the western border of the license and dip approximately 4.5° to the southeast. The resource area is bounded to the southeast by the Nyalga Basin Fault Zone.

Accessibility, Climate, Local Resources, Infrastructure and Physiography

Accessibility

Access to the Chandgana Property is possible by ground vehicle and helicopter or possibly small airplane. Ground vehicles may enter the resource area by driving the Ulaanbaatar-Ondorhaan highway (A0501) 295 kilometres east then turning south on any of several unpaved roads and driving 16 kilometres to the resource area. The highway is an all-weather road capable of supporting truck traffic. The unpaved roads on the resource area are generally in good condition and drivable throughout the year. However, the dirt roads can only support truck traffic when dry and only on certain sections. Helicopters may fly to the resource area and land almost anywhere. Small airplanes may also fly to the resource area but landing and take-off is only possible on several stretches of unpaved road. The elevation is not too great for helicopters or small planes although winds may be an issue at certain times of the year.

There is no access by railroad or water. The nearest railroad spurs end at Bor-Ondor, 118 kilometres south and the Baganuur Coal Mine, 124 kilometres west of the Chandgana Property and adjacent to the Ulaanbaatar-Ondorhaan highway. The Herlen River is the closest major river and is not navigable.

Climate and Vegetation

The resource area has a continental climate with warm and dry but short summers and cold and dry winters. The area is generally windy with wind direction from the northwest or northeast at speeds of 4-7 m/sec but reaching 20 m/sec in the spring. The warmest temperatures are during June to July with highs around 40° C and the coldest during December to January with lows around -30° C. Snow accumulation averages 10 cm in flat areas but may drift to 1 metre deep. The annual precipitation varies from 10 to 50 cm and most falls as rain in August (Behre Dolbear, 2007).

The surface is predominantly grass-covered although there are some low shrubs on the hills. There are no forested areas in or near the resource area.

Local Resources

Surface water is not readily available in the resource area. The nearest flowing water is the Herlen River 30 kilometres to the southeast. Otherwise surface water may only be available from dry stream courses and ephemeral lakes during the summer wet season. There are no lakes or reservoirs. Groundwater appears to be available because the 2007 exploration drilling encountered an artesian aquifer in three of the seven drill holes and water was observed in other 2007 and 2010 drill holes. The size and production capacity of this aquifer has not been evaluated.

Infrastructure and Population Centres

The only infrastructure within or nearby the Chandgana Property is the Ulaanbaatar-Ondorhaan highway (A0501), a 110 kV power transmission line to the south, a 35 kV distribution line to the Chandgana Coal Mine, and cellular phone coverage. The highway is located 16 kilometres north and is a paved all-weather highway. There are no water or natural gas pipelines, telephone lines, canals, or water retention structures within or nearby the resource area.

Physiography

The resource area is located within an intermontane valley between the Nyalga Depression to the southwest and the Shorvogo Basin to the northeast. The Khentii Mountain Range is northwest and the Hongor Mountains are southeast of the resource area. The physiography of the resource area consists of a broad flat with low hills to the northwest and east otherwise there are no prominent physiographic features. The drainage bottoms are 1 to 5 metres below the adjacent surface and are usually dry. The bottoms of the ephemeral lakes are 0.5 to 4 metres below the adjacent surface.

The surface elevations of the resource area vary from 1,129 metres to 1,164 metres making for a relief of approximately 35 metres. The low flat areas average 1,135 metres and the hills 1,152 metres in elevation.

History

The Khavtgai Uul Minerals Exploration License was originally granted to Deej Bayalag LLC and issued on April 7, 2007 under registration number 9011039094. No previous licenses are known. The second year license fee was paid on May 22, 2007. The license was transferred to Red Hill on October 12, 2007, under registration number 90190101078 with no change in the size or boundaries. The license was readjusted to decrease its size on April 8, 2009 and it now has an expiration date of April 7, 2012. The holder (issue) of the readjusted license is Chandgana Coal LLC, a subsidiary of Prophecy Coal.

There has been previous exploration for coal near and within the resource area. The former Soviet government explored for coal by drilling and trenching in 1962 and drilling in 1980 in the northern end of the Nyalga Basin (Behre Dolbear, 2007). Red Hill explored the Chandgana Tal coal licenses in the same area during the summers of 2007 and 2011. Eight core holes were drilled the results of which are more fully described by Behre Dolbear (2007). Trenching was performed during 2009 to locate the coal subcrop. RedHill drilled 13 drill holes and performed seismic survey lines during 2010. Red Hill drilled 15 drill holes during the summer of 2011 to better define the resource of the Chandgana Tal licenses. Both Tethys Mining and Adamas Mining conducted coal exploration on their licenses contiguous to Prophecy Coal's license during 2007 and 2008. There is previous and current mining at the Chandgana Property on the portion owned by Berkh-Uul.

Geological Setting

The resource area is located in the Nyalga Basin which is a portion of the Khentii Zone of the Khangai-Khentii fold system. The Khangai-Khentii fold system is a series of folded Silurian to Cretaceous age sedimentary rocks found in eastern Mongolia (Behre Dolbear, 2007).

Surficial Deposits and Sedimentary Rocks

Surficial materials include surface deposits and sedimentary rocks. Surface deposits appear to be Holocene in age and include alluvium, colluvium and playa deposits and are up to 70 metres thick. Sedimentary rocks are found in small areas at the surface but comprise all the subsurface rocks. These rocks range in age from Silurian to Tertiary and include nonmarine sand, clay, conglomerate, sandstone, siltstone, claystone, shale, and coal. A minimum thickness of 3,350 metres of sedimentary rocks is known.

Resource Area Geology

Unconsolidated Holocene age sediments are found at the surface and no bedrock is exposed. The rocks found immediately below the surficial deposits belong to the nonmarine Early Cretaceous Zuunbayan Formation. The coal resource is found in the Zuunbayan Formation. Igneous dikes and sills have not been found to cut the Zuunbayan Formation.

Structural Geology

The coal resources are found within the southern end of the Nyalga Basin. The basin appears to be a faulted syncline though seismic surveys suggest the coal-bearing rocks continue on the southeast side of the Nyalga Basin Fault Zone. The basin then may extend farther to the southeast than has been considered before. The coal seams subcrop along the western margin of the syncline, strike from N 20° to 65°E, and dip approximately 45° to the southeast. The wide variation in strike may be a result of faulting but cannot be proven with the information available. Resistivity-IP and seismic lines across the former Nyalga Basin Fault indicate a horst exists at this location. The former Nyalga Basin Fault is the northwest normal fault bounding the horst while another normal fault about 570 metres southeast bounds the horst on the other side. These two faults and possible smaller faults indicated by the seismic survey lines justified renaming the area the Nyalga Basin Fault Zone. The location of the fault zone is also partly supported by the change in lithology of float material, drilling results, apparent slight topographic expression and azimuth of topographic contours, and the change in lithology of the portion of the Zuunbayan Formation penetrated in drill holes on either side of the fault. Displacement along both faults is approximately 300 metres at their north and south ends but appears to decrease at the middle. At this time the Nyalga Basin Fault Zone is considered to have a tectonic origin based on the type of deformation and observations from drill core which also agrees with the structural history of the area. Mass wasting that may affect the reliability of the coal resource estimate or impact coal recoverability has not been found.

The two drill holes southeast of the Nyalga Basin Fault did not encounter coal. These holes were plug drilled with a full face PDC bit to total depth with limited coring in zones of poor circulation. The cuttings and core samples were logged but the holes were not geophysically logged. The holes were plugged with cement upon completion of drilling.

Drilling provided the most reliable information including depth and thickness of coal seams and core samples. This allowed better mapping of the extent, elevation and thickness of the coal seams and better estimation of coal quality. The B Coal Seam is found throughout the resource area and is thick but locally thins in the west central and northeast portions of the area. Otherwise the B Coal Seam was found to be slightly thicker than expected. The other coal seams are thicker and have a greater extent than previously shown though they are found in the same general area. The elevation of the coal seams varies more than previously described suggesting local folds or faults are present. Assays of the coal core samples shows coal quality to be similar to that described previously. The greatest changes are a slight increase in moisture and ash and slight decrease in heaving value.

Exploration

Subsequent to the 2008 technical report much more exploration has been completed. The goals of this exploration were to place all of the resource in the measured and indicated assurance of existence categories, obtain more information on the depth, thickness, and grade of the coal seams, and locate the geologic limits of the resource more accurately. The exploration concept was that commonly used for relatively low dipping stratiform deposits where exploration was planned and executed to obtain information on depth, thickness, continuity, and quality of the resource. This information was obtained by surface mapping, trenching, drilling and geophysical methods. Two shallow trenches were excavated in 2009 for a total length of 189 metres. Approximately 15.7 kilometres of resistivity-induced polarization and 15.7 kilometres of magnetometer lines were run across the Nyalga Basin Fault in 2008. During 2010 Prophecy Coal completed 13 drill holes and ran 11.3 kilometres of reflection seismic lines and 27.8 kilometres of magnetometer lines. This exploration supplemented that completed in 2007 which included remote imagery interpretation, surface mapping, trenching, and seven core drill holes. The new information has placed all of the resource in the measured and indicated assurance of existence categories, enabled more accurate mapping of the geologic limits of the resource area, and made for better characterization of the geology and estimation of coal resources and quality. Three drill holes were drilled during 2011. These drill holes helped to better define the coal seam subcrop and possible faulting. Trenching was performed during 2012 also to better define the coal seam subcrop and possible faulting. No development work or operations are active in the resource area.

Mineralization

Nine coal seams that contain coal resources are found in the resource area. The B Coal Seam contains 80% of the resource, followed by the F Coal Seam (8%) and E Coal Seam (7%) with the remaining coal seams containing smaller portions. The B Coal Seam is found throughout the resource area, has an average resource thickness of 34.2 metres and range from 6.2 to 60.5 metres thick including several, mostly thin partings. The known depth to the B Coal Seam varies from 27.7 to 266.8 metres but is probably even shallower in the northwest corner of the license. Other coal seams (formerly the Upper Coal Seams) are found above the B Coal Seam. These coal seams have a thinner resource thickness (0 to 16.0 metres) and are less extensive yet contain significant resources also. The coal seams are black, friable, readily slake and have poor competency. The partings are poorly indurated and have a moderate slake potential. The overburden is also poorly indurated with a moderate slake potential but contains few structural discontinuities. The coal seams are moderate grade low rank thermal coals. The thickness-weighted average in-place assay (as-received basis) of the sampled coal seams (A, B and C Coal Seam) within the resource area is 36.5% moisture, 10.1% ash, 3,636 kcal/kg heating value, and 0.6% sulphur. Their agglutinating properties have not been assayed, but the coals are expected to be non-agglutinating. The apparent ASTM rank of the coal is between Subbituminous C and B based on the moist, mineral matter-free gross calorific value of core sample assays.

Table 8

WEIGHTED AVERAGE A, B AND C COAL SEAM QUALITY				
(as-received basis)				
Parameter	Moisture (wt. %)	Ash (wt. %)	Heating Value (kcal/kg)	Total Sulphur (wt. %)
	36.54	10.10	3,636	0.59

Drilling

For the 2007 drilling, Landdrill International Inc. of Ulaanbaatar, Mongolia, was contracted to drill the holes and used a truck-mounted Longyear Model 44 rig. The procedure was to (1) drill with a 132 mm (HWT) full face PDC bit and set conductor casing, (2) drill the overburden to core point with a 96 mm (HQ) full face PDC bit using polymer as a medium, and (3) core from core point to total depth with an HQ-3 core drilling string. Coring was done using HQ rods behind a 96 mm OD diamond core bit with inert polymer as a medium. Wireline coring methods were used with a sleeved 3 metre core barrel assembly. All drilling was done on a 24-hour schedule. The drilling method, drilling procedures, and size of core obtained is considered appropriate for the logistics of the area, goals of the drilling, and type of analyses desired.

Five of the drill holes were drilled northwest of the Nyalga Basin Fault Zone and two southeast of the fault zone. Those in the resource area west of the fault zone were located to maximize characterisation of the resource and the reliability of the resource estimate. These five drill holes penetrated nearly the full thickness of the upper member of the Zuunbayan Formation. The two drill holes southeast of the Nyalga Basin Fault Zone were drilled to confirm the lack of coal and to help locate and characterize the fault zone. The drill hole locations and elevations were obtained by ground survey methods using a theodolite.

Drill cuttings were collected at one metre intervals, described and the lithologic information logged onto forms. The drill core was described in white light and ultraviolet light, the information logged on forms at a scale of 3 cm=0.5 m, and the core photographed with a digital camera. The core information logged includes lithology, rock mechanics, and sampled intervals. Other information was noted during drilling and logging including water and gas encountered and unusual drilling conditions. After completion of the core logging, the core was sampled, placed in plastic sleeves, and the samples noted on the core log. The lithology and rock mechanics information are considered to be logged in acceptable detail.

After reaching total depth, the drill holes in the resource area were geophysically logged. Some of these were logged through the core rods if the hole was not stable. The logging suite included gamma, spontaneous potential, gamma-gamma density, single point resistivity, and caliper. Printed field copies at a scale of 1cm=2 metres and Log ASCII Standard (LAS) electronic files of the logs were provided to Red Hill.

Upon completion of logging the drill holes in the resource area or reaching total depth for the drill holes outside the resource area, the holes were plugged with bentonite chips and capped with 2 to 5 metres of cement. The conductor casing was pulled from some of the drill holes. A marker with drill hole identification information was placed in the top of the cement.

The 2010 drilling was performed by Best Drilling Inc. of Ulaanbaatar, Mongolia using a skid-mounted Longyear Model 44 rig. The drilling procedure was the same as that used in 2007. The drilling method, drilling procedures, and size of core obtained is considered appropriate for the logistics of the area, goals of the drilling, and type of analyses desired. Geologic data and samples were obtained using the same methods practised during the 2007 drilling. The lithology and rock mechanics information are considered to be logged in acceptable detail. Geophysical logging was performed similar to that performed in 2007 with one exception. The exception is that spontaneous potential was not logged, otherwise natural gamma, gamma-gamma density, single point resistivity, and caliper were logged.

Best Drilling performed the 2011 drilling and followed similar procedures as those in 2010. Geologic data and samples were obtained using methods similar to those of 2010 and the information logged in acceptable detail. This drilling did not change the amount or reliability of the resource estimate or the mineability of the resource.

Summary and Interpretation of Results

The drilling provided the most reliable data to characterise the geology of the resource area, estimate resources and estimate coal quality. The drilling - (1) provided more information on the areal extent and thickness of the coal seams, (2) further defined the structural geology, (3) confirmed the presence of a significant coal resource, (4) placed all of the resource in the measured and indicated assurance-of-existence categories, (5) better defined the geologic boundaries of the resource, (6) better characterized the type, grade and rank of the coal seams, and (7) gave indications of groundwater and mining conditions.

Accurate measurements of the depth and thickness of all the coal seams are now available and the closer spacing between drill holes allows all the coal seams to be correlated more reliably. Nine major coal seams are now known. The A Coal Seam is the stratigraphically lowest coal seam followed, in ascending order by the very thick B Coal Seam then seven (C through I) thinner coal seams. The B Coal Seam is the thickest ranging from 6.2 to 61.1 metres thick, is found at a maximum depth of 311.7 metres, and has the greatest areal extent. The E and F Coal Seams are thinner (0 to 23.5 m) but are found over most of the resource area. The other coal seams are thinner and are less extensive. All the coal seams contain partings that range in thickness from 0.1 to 9.1 metres thick.

The attitude of the rocks and faulting is much better known. The resource area has a more complex geology than previously thought in that there is either folding or faulting though overall dip is still to the southeast. The extent of the basin is slightly larger because the coal seams subcrop farther northwest and the coal-bearing rocks are probably present on the southeast side of the Nyalga Basin Fault Zone. The former Nyalga Basin Fault is now considered to be a fault zone with a central horst.

The drill hole spacing placed all of coal resources in the measured and indicated assurance-of-existence categories. Analyses confirmed the coal to be a moderate grade, low rank thermal coal. Cores allowed visual characterisation of rock properties and provided samples for assay. The overburden and interburden rocks and the coal are weak being poorly to moderately lithified but with few fractures. Finally, the drilling mapped a 33.0 to 42.5 metres thick moderately artesian sandstone aquifer between the B and E Coal Seams.

The 2011 drilling confirmed the subcrop to be outside the license as described in 2010. The location of possible faults was inconclusive.

Sampling & Analysis

In planning the 2007 exploration, exposures in the nearby Chandgana Coal Mine were considered. These exposures suggested that at least one of the coal seams should be very thick, low rank and dip at a low angle to the southeast. Thus, having a thick stratiform deposit and considering that the exploration is the first in the resource area, the approach used was to obtain samples that gave a reliable gross estimate of coal quality. To meet this goal, sampling was planned to (1) obtain samples at widely spaced locations, (2) sample the full thickness of the coal seam, (3) determine the limit of weathered coal, and (4) ensure the samples are representative of the grade and rank of the coal. The desire to obtain samples at widely spaced locations complimented the desire to place as much of the resource in the higher assurance-of-existence categories as possible.

Drilling and trenching were then considered most appropriate for obtaining samples. Large diameter HQ drill cores were obtained using a three metre core barrel. Only the B Coal Seam was cored because the existence of the upper coal seams was not known. The full thickness of the B Coal Seam was cored where possible. Unfortunately, in some cases a portion of the top of the coal seam was rotary drilled before changing to the core drilling string because the structure of the coal seam was not known.

A similar sampling approach was used for the 2010 drilling. But the stratigraphically higher coal seams were core drilled in two drill holes besides the B Coal Seam. Since the structure of the coal seam was known fairly well core was obtained from all of the targeted coal seams but one where the upper few metres were rotary drilled. The representativeness of the core samples obtained during the 2007 and 2010 drilling was enhanced in several ways. These included (1) selecting large diameter core to increase core recovery, (2) core drilling on a 24 hour schedule to increase core recovery, and (3) using inert drilling fluids when possible to reduce core contamination. The core sampled (including core loss) intervals and analysed intervals are indicated relative to the entire coal seam thickness in Figures 5 and 6.

Trenching with an excavator was primarily done to locate the B Coal Seam subcrop, but secondarily to obtain samples to be assayed. The portion of the coal seam exposed in Trenches C and D were sampled. The representativeness of the trench samples was enhanced by obtaining large samples and placing the sample in plastic bags as soon as possible to preserve in-situ moisture.

The sampling of cores during the 2007, 2010 and 2011 drilling followed the same methods. Sampling was started and completed as soon as possible after lithologic descriptions and photographs were done. The sampling method followed that of ASTM D 5192 where practical. Sample treatment methods included rinsing the core of contaminants and allowing sufficient time for the free water to drain from the core to enhance sample representativeness. Sample preservation included placing the core in 6 mil plastic sleeves to minimize moisture loss then placement on wooden core boxes for protection. The samples were removed from the core tray in lengths up to 1metre depending on the thickness of partings and the beginning and end of core runs.

Security of Samples

All the drill core and trench samples were prepared and assayed in accordance to ASTM International (ASTM), International Organization for Standardization (ISO), or Australian Standards (AS) procedures in the coal laboratories of SGS-CSTC Standard Technical Services Co., Ltd. These laboratories are located in Ulaanbaatar, Mongolia (SGS Mongolia), the test centre in Tianjin, China (SGS Mineral Fuels), and the geochemical and ores laboratory in Tianjin, China (SGS Geochemical and Ores). Sample preservation, security and tracking was established and well maintained from the drill site to reporting of the results for the 2007, 2010, and 2011 drilling.

Sample security was ensured from the drill site to the assay report. A chain of custody form was completed by Mr. Robeck for the 2007 samples and by Mr. Kravits for the 2010 and 2011 samples that

gives sufficient information to identify the samples and describes the analyses required. The chain of custody accompanied the samples during shipment from the drill site to the laboratory and was signed by all parties involved in the transport of the samples and SGS Mongolia upon receipt. All the samples were shipped under Red Hill or Prophecy Coal control directly to SGS Mongolia. Upon delivery the samples were jointly inventoried by a Prophecy Coal representative and SGS staff before SGS signed for receipt of the samples. The signed sample chains of custody are on file at Prophecy Coal's Ulaanbaatar office. SGS Mongolia then entered the sample information into their laboratory information management system (LIMS) which generated unique laboratory identification numbers. Sample preparation and laboratory worksheets are then prepared by the LIMS to track each sample to the final report. The laboratory managers review the sample tracking while the samples are in process and review the final assay reports to ensure the correct sample identifying information accompanies the correct assays (Murray, 2007 and Rao, 2010). This responsibility is part of the laboratory accreditation which for the 2007 samples was validated by ISO (Murray, 2007). No assay results were found to have been misidentified.

Once in the custody of SGS, the samples were sealed and stored in a secure lockable location to prevent tampering. The storage conditions are controlled to protect the samples from heat, light and humidity (Rao, 2010). No samples were lost, stolen or tampered with during any of the three years of drilling.

None of the samples were handled by Mr. Robeck, Mr. Kravits, or any contractors, employees, officers or directors of Red Hill or Prophecy Coal after receipt by SGS and none of these parties were involved in preparation or assay of the samples.

Data Verification

There are five types of data used in this updated technical report: topographic data, stratigraphic data, trench data, geophysical data and assay data. Each type of data was reviewed to verify that it represents the location, depth and/or other descriptive information of its source. The quality of the data was then assessed by a review for accuracy and errors. The methods used vary according to the type of data and were performed using practices common in the coal industry or the industry that produces such data.

The topographic data and the map produced from this data were verified by Mr. Kravits during the site inspection and with information obtained during the inspection (Kravits Geological Services, 2007). This was done by comparing the coordinates and elevation of the drill holes, trenches, and license corners determined with a handheld GPS receiver to the coordinates and elevations on the geologic map.

The stratigraphic data obtained from the 2010 and 2011 drill holes were verified by Mr. Kravits in two ways. These included comparison of the identification, location, and other information of the 2007 drill holes in the stratigraphic database to the information on the geophysical and lithologic log headers and the information obtained during the site inspection and comparison of the interpreted and correlated geophysical logs by Mr. Kravits to those of Mr. Robeck. For the 2010 drill holes this was not necessary because Prophecy Coal geologists and Mr. Kravits located the drill holes with a GPS receiver prior to drilling and the completed drill hole was surveyed by Oyu Survey LLC (Oyu Survey, 2010). The GPS coordinates and surface elevation were placed on the geophysical log headers to better tie the log to the drill hole.

The trench data were verified against observations made and coordinates obtained by Mr. Kravits during the site visit and notes made and pictures obtained by Mr. Robeck during the trenching. The geophysical data were verified by comparison of the contractor supplied coordinates of their activities to evidences of their activity and coordinates obtained by Oyu Survey or Mr. Kravits.

The 2010 and 2011 assay data were verified by comparison of the descriptive information (drill hole number, depth interval, sample number, and lithology) and assay results accompanying the quality data to that of the same information on the core log and chain of custody and the recorded lithology. Transcribed data were reviewed twice for errors.

Mineral Resources and Reserves

The total coal resource within the resource area is 1,048.1 million tonnes of which 509.3 million tonnes are in the measured and 538.8 million tonnes are in the indicated assurance of existence categories. All the coal resources fall within the measured and indicated categories, there is none in the inferred category. The in-place strip ratio averages 2.2:1 over the resource area and varies from a minimum of 0.2:1 at the northwest corner of the license to a maximum of 5.3:1 to the north.

**Table 9
Chandgana**

COAL SEAM RESOURCES			
Coal Seam	Assurance-of-Existence Category		Total
	Measured	Indicated	
I Coal Seam	0.2	0.1	0.3
H Coal Seam	3.1	4.6	7.7
G Coal Seam	3.9	5.4	9.4
F Coal Seam	41.8	41.0	82.8
E Coal Seam	35.8	39.2	75.0
D Coal Seam	3.2	2.4	5.7
C Coal Seam	15.8	13.7	29.5
B Coal Seam	403.5	430.7	834.3
A Coal Seam	1.9	1.5	3.4
Subtotal	509.3	538.8	1,048.1
Total Measured and Indicated	1,048.1		

Resources are in millions of tonnes

The Chandgana Property 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.

Future Exploration and Development

Further exploration, analyses and tests are recommended to better understand the geology in the western portion of the license, map the coal seams above the B Coal Seam and better characterize the quality and utilization characteristics of the coal. This includes reprocessing of the acquired seismic data, rotary and core drilling, bulk sampling and more thorough and detailed analyses and tests of core samples and a bulk sample.

The Company is currently exploring the economics and feasibility of using coal from the Chandgana Property in a mine-mouth power plant project which the Mongolian government is supportive of and has issued a conditional permit to Prophecy Coal in respect of.

Chandgana Tal Property

Project Description and Location

The Chandgana Tal property consists of mining licenses MV-016767 and MV-010126. The licenses are held by Chandgana Coal LLC, a subsidiary of Prophecy Coal and are found in the northeast portion of the Nyalga Coal Basin. The licenses are located 285 kilometres east of Ulaanbaatar in Moron soum (sub-province) of Khentii aimag (province), Mongolia. The coal-bearing portion comprises approximately 1,636

hectares. There are coal exploration licenses adjacent to the resource area that is held by Tethys Mining LLC, a fully-owned subsidiary of Companhia Vale do Rio Doce. The resource area has a continental climate with short warm summers and longer cold winters and is generally favourable for development of the coal resource.

The resource area is located in the Nyalga Depression within the Khentii Zone of the Khangai-Khentii fold system and is part of the Shorvogo Steppe physiographic province along the northern margin of the Gobi Desert. The topography is relatively featureless with a mean surface elevation of 1,142 metres.

The coal seams belong to the Early Cretaceous age Zuunbayan Formation and are part of the northern end of the headwall portion of a faulted syncline. The coal seams subcrop in the northern portion of the license and dip approximately 4.5° to the south and southwest. The resource area is bounded to the southeast by the Nyalga Basin Fault Zone.

Accessibility, Climate, Local Resources, Infrastructure and Physiography

Accessibility

Access to the Chandgana Tal licenses is possible by ground vehicle and helicopter or possibly small airplane. Ground vehicles may enter the resource area by driving the Ulaanbaatar-Ondorhaan highway (A0501) 290 kilometres east then turning south on any of several unpaved roads and driving 16 kilometres to the resource area. The highway is an all-weather road capable of supporting truck traffic. The unpaved roads on the resource area are generally in good condition and drivable throughout the year. However, the dirt roads can only support truck traffic when dry and only on certain sections. Helicopters may fly to the resource area and land almost anywhere. Small airplanes may also fly to the resource area but landing and take-off is only possible on several stretches of unpaved road. The elevation is not too great for helicopters or small planes although winds may be an issue at certain times of the year.

There is no access by railroad or water. The nearest railroad spurs end at Bor-Ondor, 118 kilometres south and the Baganuur Coal Mine, 134 kilometres west of the Chandgana Tal licenses and adjacent to the Ulaanbaatar-Ondorhaan highway. The Herlen River is the closest major river and is not navigable.

Climate and Vegetation

The resource area has a continental climate with warm and dry but short summers and cold and dry winters. The area is generally windy with wind direction from the northwest or northeast at speeds of 4-7 m/sec but reaching 20 m/sec in the spring. The warmest temperatures are during June to July with highs around 40° C and the coldest during December to January with lows around -30° C. Snow accumulation averages 10 cm in flat areas but may drift to 1 metre deep. The annual precipitation varies from 10 to 50 cm and most falls as rain in August (Behre Dolbear, 2007).

The surface is predominantly grass-covered although there are some low shrubs on the hills. There are no forested areas in or near the resource area.

Local Resources

Surface water is not readily available in the resource area. The nearest flowing water is the Herlen River 30 kilometres to the southeast. Otherwise surface water may only be available from dry stream courses and ephemeral lakes during the summer wet season. There are no lakes or reservoirs. Groundwater appears to be available because the 2007 and 2011 exploration drilling encountered water in the drill holes. The size and production capacity of the aquifer has not been evaluated.

Infrastructure and Population Centres

The only infrastructure within or nearby the Chandgana Property is the Ulaanbaatar-Ondorhaan highway (A0501), a 110 kV power transmission line to the south, a 35 kV distribution line to the Chandgana Coal Mine, and cellular phone coverage. The highway is located 3 kilometres north and is a paved all-weather highway. There are no water or natural gas pipelines, telephone lines, canals, or water retention structures within or nearby the resource area.

Physiography

The resource area is located within an intermontane valley between the Nyalga Depression to the southwest and the Shorvogo Basin to the northeast. The Khentii Mountain Range is northwest and the Hongor Mountains are southeast of the resource area. The physiography of the resource area consists of a broad flat with low hills to the northwest and east otherwise there are no prominent physiographic features. The drainage bottoms are 1 to 5 metres below the adjacent surface and are usually dry. The bottoms of the ephemeral lakes are 0.5 to 4 metres below the adjacent surface.

The surface elevations of the resource area vary from 1,129 metres to 1,164 metres making for a relief of approximately 35 metres. The low flat areas average 1,135 metres and the hills 1,152 metres in elevation.

History

Mining license MV-016767 was originally granted as an exploration licenses to Belchir LLC and was issued on March 19, 2004. No previous licenses are known. The license was transferred to Tugrug Nuurn Energy LLC and registered by the head of the Office of Geological and Mining Cadastre in his decision no. 444 of 2005. The exploration license was later transferred to Coal Khentii LLC and registered by the head of the Office of Geological and Mining Cadastre in his decision no. 318 of 2006. Red Hill Energy LLC acquired this license in 2006 with government approval. The license was converted to a mining license January 27, 2011.

Mining license MV-010126 was granted to Tugrug Nuurn Energy LLC with the right to mine on July 8, 2005. The exploration license was later transferred to Coal Khentii LLC and registered by the head of the Office of Geological and Mining Cadastre in his decision no. 318 of 2006. Red Hill Energy LLC acquired this license in 2006 with government approval.

There has been previous exploration for coal within and near the licenses. The former Soviet government performed survey work during 1926 to describe the coal deposit and during 1958 to assess the resource of radioactive elements. The Soviet government further explored for coal by drilling and trenching in 1962 and drilling in 1980 (Behre Dolbear, 2007). Red Hill explored Chandgana Tal Coal licenses during the summer of 2007. Eight core holes were drilled the results of which are more fully described by Behre Dolbear (2007). Red Hill drilled 15 drill holes during 2011. Tethys conducted coal exploration on their licenses contiguous to Prophecy Coal's license during the years 2007 through 2012. There is previous and current mining at the Chandgana Property on the portion owned by Berkh-Uul.

Geological Setting

The resource area is located in the Nyalga Basin which is a portion of the Khentii Zone of the Khangai-Khentii fold system. The Khangai-Khentii fold system is a series of folded Silurian to Cretaceous age sedimentary rocks found in eastern Mongolia (Behre Dolbear, 2007).

Surficial Deposits and Sedimentary Rocks

Surficial materials include surface deposits and sedimentary rocks. Surface deposits appear to be Holocene in age and include alluvium, colluvium and playa deposits and are up to 70 metres thick. Sedimentary rocks are found in small areas at the surface but comprise all the subsurface rocks. These

rocks range in age from Silurian to Tertiary and include nonmarine sand, clay, conglomerate, sandstone, siltstone, claystone, shale, and coal. A minimum thickness of 3,350 metres of sedimentary rocks is known.

Resource Area Geology

Unconsolidated Holocene age sediments are found at the surface and no bedrock is exposed. The rocks found immediately below the surficial deposits belong to the nonmarine Early Cretaceous Zuunbayan Formation. The coal resource is found in the Zuunbayan Formation. Igneous dikes and sills have not been found to cut the Zuunbayan Formation.

Structural Geology

The coal resources are found within the northern end of the Nyalga Basin. The basin appears to be a faulted syncline though seismic surveys suggest the coal-bearing rocks continue on the southeast side of the Nyalga Basin Fault Zone. The basin then may extend farther to the southeast than has been considered before. The coal seams subcrop along the western margin of the syncline, strike from N 20° to 65°E, and dip approximately 4.5° to the southeast. The wide variation in strike may be a result of faulting but cannot be proven with the information available. Resistivity-IP and seismic lines across the former Nyalga Basin Fault indicate a horst exists at this location. The former Nyalga Basin Fault is the northwest normal fault bounding the horst while another normal fault about 570 metres southeast bounds the horst on the other side. These two faults and possible smaller faults indicated by the seismic survey lines justified renaming the area the Nyalga Basin Fault Zone. The location of the fault zone is also partly supported by the change in lithology of float material, drilling results, apparent slight topographic expression and azimuth of topographic contours, and the change in lithology of the portion of the Zuunbayan Formation penetrated in drill holes on either side of the fault. Displacement along both faults is approximately 300 metres at their north and south ends but appears to decrease at the middle. At this time the Nyalga Basin Fault Zone is considered to have a tectonic origin based on the type of deformation and observations from drill core which also agrees with the structural history of the area. Mass wasting that may affect the reliability of the coal resource estimate or impact coal recoverability has not been found.

The drilling of 2007 and especially later during 2011 provided the most reliable information including depth and thickness of coal seams and core samples. This allowed better mapping of the extent, elevation and thickness of the coal seams and better estimation of coal quality. The S2 Coal Seam is found throughout the resource area and is thick but locally thins. The elevation of the coal seams generally decreases to the southeast.

Exploration

Subsequent to the 2007 technical report much more exploration has been completed. The goals of this exploration were to obtain more information on the depth, thickness, and grade of the coal seams and locate the geologic limits of the resource more accurately. The exploration concept was that commonly used for relatively low dipping stratiform deposits where exploration was planned and executed to obtain information on depth, thickness, continuity, and quality of the resource. This information was obtained by trenching and drilling. Four shallow trenches were excavated in 2009. During 2011 Prophecy Coal completed 15 from which the coal seams were sampled in detail. This exploration supplemented that completed in 2007 which included remote imagery interpretation, surface mapping, trenching, and drilling. The new information made for a much more accurate resource estimate, enabled more accurate mapping of the geologic limits of the resource area, and made for better estimation of coal quality. No development work or operations are active in the resource area.

Mineralization

The S2 coal seam contains most of the coal resources found within the licenses (Boyd Co, 2011). Other thinner coal seams comprise smaller portions of the resource and most are mineable based on thickness.

The S2 Coal Seam is found throughout the resource area, has an average resource thickness of 40.7 metres and locally exceeds 60 metres thick including several, mostly thin partings. The known depth to the B Coal Seam varies from 0 to 75. Other coal seams are found above and below the S2 Coal Seam. These coal seams have a thinner resource thickness (0 to 12.0 metres) and are less extensive yet contain mineable resources. The coal seams are black, friable, readily slake and have poor competency. The partings are poorly indurated and have a moderate slake potential. The overburden is also poorly indurated with a moderate slake potential but contains few structural discontinuities. The coal seams are moderate grade low rank thermal coals. The weighted average in-place assay (as-received basis) of the S2 Coal Seam within the resource area is 40.9% moisture, 10.8% ash, 3,306 kcal/kg heating value, and 0.6% sulphur. Their agglutinating properties have not been assayed, but the coals are expected to be non-agglutinating. The apparent ASTM rank of the coal is lignite A based on the moist, mineral matter-free gross calorific value of core sample assays.

Table 10

WEIGHTED AVERAGE S2 COAL SEAM QUALITY				
(as-received basis)				
Parameter	Moisture (wt. %)	Ash (wt. %)	Heating Value (kcal/kg)	Total Sulphur (wt. %)
	40.9	10.80	3,306	0.6

Drilling

For the 2007 drilling, Landrill International Inc. of Ulaanbaatar, Mongolia, was contracted to drill the holes and used a truck-mounted Longyear Model 44 rig. The procedure was to (1) drill with a 132 mm (HWT) full face PDC bit and set conductor casing, (2) drill the overburden to core point with a 96 mm (HQ) full face PDC bit using polymer as a medium, and (3) core from core point to total depth with an HQ-3 core drilling string. Coring was done using HQ rods behind a 96 mm OD diamond core bit with inert polymer as a medium. Wireline coring methods were used with a sleeved 3 metre core barrel assembly. All drilling was done on a 24-hour schedule. The drilling method, drilling procedures, and size of core obtained is considered appropriate for the logistics of the area, goals of the drilling, and type of analyses desired.

The drill holes were distributed about the licenses. The drill holes penetrated nearly the full thickness of the upper member of the Zuunbayan Formation. The drill hole locations and elevations were obtained by ground survey methods using a theodolite.

Drill cuttings were collected at one metre intervals, described and the lithologic information logged onto forms. The drill core was described in white light and ultraviolet light, the information logged on forms at a scale of 3 cm=0.5 m, and the core photographed with a digital camera. The core information logged includes lithology, rock mechanics, and sampled intervals. Other information was noted during drilling and logging including water and gas encountered and unusual drilling conditions. After completion of the core logging, the core was sampled, placed in plastic sleeves, and the samples noted on the core log. The lithology and rock mechanics information are considered to be logged in acceptable detail.

After reaching total depth, the drill holes in the resource area were geophysically logged. Some of these were logged through the core rods if the hole was not stable. The logging suite included gamma, spontaneous potential, gamma-gamma density, single point resistivity, and caliper. Printed field copies at a scale of 1cm=2 metres and Log ASCII Standard (LAS) electronic files of the logs were provided to Red Hill.

Upon completion of logging the drill holes were plugged with bentonite chips and capped with 2 to 5 metres of cement. The conductor casing was pulled from some of the drill holes. A marker with drill hole identification information was placed in the top of the cement.

The 2011 drilling was performed by Best Drilling Inc. of Ulaanbaatar, Mongolia using a skid-mounted Longyear Model 44 rig. The drilling procedure was the same as that used in 2007. The drilling method, drilling procedures, and size of core obtained is considered appropriate for the logistics of the area, goals of the drilling, and type of analyses desired. Geologic data and samples were obtained using the same methods practised during the 2007 drilling. The lithology and rock mechanics information are considered to be logged in acceptable detail. Geophysical logging was performed similar to that performed in 2007 with one exception. The exception is that spontaneous potential was not logged, otherwise natural gamma, gamma-gamma density, single point resistivity, and caliper were logged.

Best Drilling performed the 2011 drilling and followed similar procedures as those in 2010. Geologic data and samples were obtained using methods similar to those of 2010 and the information logged in acceptable detail. This drilling did not change the amount or reliability of the resource estimate or the mineability of the resource.

Summary and Interpretation of Results

The drilling provided the most reliable data to characterise the geology of the resource area, estimate resources and estimate coal quality. The drilling - (1) provided more information on the areal extent and thickness of the coal seams, (2) further defined the structural geology, (3) confirmed the presence of a significant coal resource, (4) better defined the geologic boundaries of the resource, and (5) better characterized the type, grade and rank of the coal seams.

Accurate measurements of the depth and thickness of all the coal seams are now available and the closer spacing between drill holes allows all the coal seams to be correlated more reliably. Two major coal seams are now known. The S4 Coal Seam is the stratigraphically lowest coal seam followed, in ascending order by the S3 coal seam. The very thick S2 Coal Seam then two (S3 and S4 coal seams). The combined S2 Coal Seam is the thickest ranging from 15 to 50 metres thick, is found at a maximum depth of 75 metres, and has the greatest areal extent. The E and F Coal Seams are thinner (0 to 23.5 m) but are found over most of the resource area. The other coal seams are thinner and are less extensive. All the coal seams contain partings that range in thickness from 0.1 to 9.1 metres thick.

The attitude of the rocks and faulting is much better known. The resource area has a more complex geology than previously thought in that there is either folding or faulting though overall dip is still to the southeast. The extent of the basin is slightly larger because the coal seams subcrop farther northwest and the coal-bearing rocks are probably present on the southeast side of the Nyalga Basin Fault Zone. The former Nyalga Basin Fault is now considered to be a fault zone with a central horst, low rank thermal coal. Cores allowed visual characterisation of rock properties and provided samples for assay. The overburden and interburden rocks and the coal are weak being poorly to moderately lithified but with few fractures.

The 2012 drilling confirmed the subcrop to be outside the license as described in 2012.

Sampling & Analysis

In planning the 2007 exploration, exposures in the nearby Chandgana Coal Mine were considered. These exposures suggested that at least one of the coal seams should be very thick, low rank and dip at a low angle to the southeast. Thus, having a thick stratiform deposit and considering that the exploration is the first in the resource area, the approach used was to obtain samples that gave a reliable gross estimate of coal quality. To meet this goal, sampling was planned to (1) obtain samples at widely spaced locations, (2) sample the full thickness of the coal seam, (3) determine the limit of weathered coal, and (4) ensure the samples are representative of the grade and rank of the coal. The desire to obtain samples at widely spaced locations complimented the desire to place as much of the resource in the higher assurance-of-existence categories as possible.

Drilling and trenching were then considered most appropriate for obtaining samples. Large diameter HQ drill cores were obtained using a three metre core barrel. Only the S2 Coal Seam was cored because the

existence of the upper coal seams was not known. The full thickness of the S2 Coal Seam was cored where possible. Unfortunately, in some cases a portion of the top of the coal seam was rotary drilled before changing to the core drilling string because the structure of the coal seam was not known.

A similar sampling approach was used for the 2010 drilling. But the stratigraphically higher coal seams were core drilled in two drill holes besides the B Coal Seam. Since the structure of the coal seam was known fairly well core was obtained from all of the targeted coal seams but one where the upper few metres were rotary drilled. The representativeness of the core samples obtained during the 2007 and 2010 drilling was enhanced in several ways. These included (1) selecting large diameter core to increase core recovery, (2) core drilling on a 24 hour schedule to increase core recovery, and (3) using inert drilling fluids when possible to reduce core contamination.

Trenching with an excavator was primarily done to locate the S2 Coal Seam subcrop, but secondarily to obtain samples to be assayed. The portion of the coal seam exposed in trenches were sampled. The representativeness of the trench samples was enhanced by obtaining large samples and placing the sample in plastic bags as soon as possible to preserve in-situ moisture.

The sampling of cores during the 2007 and 2011 drilling followed the same methods. Sampling was started and completed as soon as possible after lithologic descriptions and photographs were done. The sampling method followed that of ASTM D 5192 where practical. Sample treatment methods included rinsing the core of contaminants and allowing sufficient time for the free water to drain from the core to enhance sample representativeness. Sample preservation included placing the core in 6 mil plastic sleeves to minimize moisture loss then placement on wooden core boxes for protection. The samples were removed from the core tray in lengths up to one metre depending on the thickness of partings and the beginning and end of core runs.

Security of Samples

All the drill core and trench samples were prepared and assayed in accordance to ASTM International (ASTM), International Organization for Standardization (ISO), or Australian Standards (AS) procedures in the coal laboratories of SGS-CSTC Standard Technical Services Co., Ltd. These laboratories are located in Ulaanbaatar, Mongolia (SGS Mongolia), the test centre in Tianjin, China (SGS Mineral Fuels), and the geochemical and ores laboratory in Tianjin, China (SGS Geochemical and Ores). Sample preservation, security and tracking was established and well maintained from the drill site to reporting of the results for the 2007, 2010, and 2011 drilling.

Sample security was ensured from the drill site to the assay report. A chain of custody form was completed by Mr. Robeck for the 2007 samples and by Mr. Kravits for the 2010 and 2011 samples that gives sufficient information to identify the samples and describes the analyses required. The chain of custody accompanied the samples during shipment from the drill site to the laboratory and was signed by all parties involved in the transport of the samples and SGS Mongolia upon receipt. All the samples were shipped under Red Hill or Prophecy Coal control directly to SGS Mongolia. Upon delivery the samples were jointly inventoried by a Prophecy Coal representative and SGS staff before SGS signed for receipt of the samples. The signed sample chains of custody are on file at Prophecy Coal's Ulaanbaatar office. SGS Mongolia then entered the sample information into their laboratory information management system (LIMS) which generated unique laboratory identification numbers. Sample preparation and laboratory worksheets are then prepared by the LIMS to track each sample to the final report. The laboratory managers review the sample tracking while the samples are in process and review the final assay reports to ensure the correct sample identifying information accompanies the correct assays (Murray, 2007 and Rao, 2010). This responsibility is part of the laboratory accreditation which for the 2007 samples was validated by ISO (Murray, 2007). No assay results were found to have been misidentified.

Once in the custody of SGS, the samples were sealed and stored in a secure lockable location to prevent tampering. The storage conditions are controlled to protect the samples from heat, light and humidity (Rao, 2010). No samples were lost, stolen or tampered with during any of the three years of drilling.

None of the samples were handled by Mr. Robeck, Mr. Kravits, or any contractors, employees, officers or directors of Red Hill or Prophecy Coal after receipt by SGS and none of these parties were involved in preparation or assay of the samples.

Data Verification

There are five types of data used in this updated technical report: topographic data, stratigraphic data, trench data, geophysical data and assay data. Each type of data was reviewed to verify that it represents the location, depth and/or other descriptive information of its source. The quality of the data was then assessed by a review for accuracy and errors. The methods used vary according to the type of data and were performed using practices common in the coal industry or the industry that produces such data.

The topographic data and the map produced from this data were verified by Mr. Kravits during the site inspection and with information obtained during the inspection (Kravits Geological Services, 2007). This was done by comparing the coordinates and elevation of the drill holes, trenches, and license corners determined with a handheld GPS receiver to the coordinates and elevations on the geologic map.

The stratigraphic data obtained from the 2010 and 2011 drill holes were verified by Mr. Kravits in two ways. These included comparison of the identification, location, and other information of the 2007 drill holes in the stratigraphic database to the information on the geophysical and lithologic log headers and the information obtained during the site inspection and comparison of the interpreted and correlated geophysical logs by Mr. Kravits to those of Mr. Robeck. For the 2012 drill holes this was not necessary because Prophecy Coal geologists and Mr. Kravits located the drill holes with a GPS receiver prior to drilling and the completed drill hole was surveyed by Oyu Survey LLC (Oyu Survey, 2012). The GPS coordinates and surface elevation were placed on the geophysical log headers to better tie the log to the drill hole.

The trench data were verified against observations made and coordinates obtained by Mr. Kravits during the site visit and notes made and pictures obtained by Mr. Robeck and staff geologists during the trenching. The geophysical data were verified by comparison of the contractor supplied coordinates of their activities to evidences of their activity and coordinates obtained by Oyu Survey or Mr. Kravits.

The 2007 and 2011 assay data were verified by comparison of the descriptive information (drill hole number, depth interval, sample number, and lithology) and assay results accompanying the quality data to that of the same information on the core log and chain of custody and the recorded lithology. Transcribed data were reviewed twice for errors.

Mineral Resources and Reserves

The total coal resource within the resource area is 124.4 million tonnes of which all is in the measured assurance of existence category. Since all the coal resources fall within the measured and indicated categories, there is none in the inferred category. The in-place strip ratio averages 0.7:1 over the resource area.

**Table 11
Chandgana**

COAL SEAM RESOURCES			
Coal Seam	Assurance-of-Existence Category		Total
	Measured	Indicated	
S2 Coal Seam	124.4	0.0	124.4
Total Measured and Indicated	124.4		

Resources are in millions of tonnes

The Chandgana Property 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.

Future Exploration and Development

Further exploration, analyses and tests are recommended to better understand the geology in the western portion of the license, map the coal seams above the S2 Coal Seam and better characterize the quality and utilization characteristics of the coal. This includes reprocessing of the acquired seismic data, rotary and core drilling, bulk sampling and more thorough and detailed analyses and tests of core samples and a bulk sample.

The Company is currently in the process of obtaining the remaining agreements, appropriate approvals and permits, and close on project financing to take the project into development.

6. RISK FACTORS

The Company is in the business of acquiring, exploring and developing mineral properties, and is exposed to a number of risks and uncertainties that are common to other junior mineral exploration and development 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 modest coal sales as a source of revenue in addition to interest on cash balances. The Company will rely mainly on coal sales, operating lines of credit and 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 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 base or 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. 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.

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.

Local Laws

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 and/or expensive to develop such projects and carry out 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 Company 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’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’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 Company 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 Company'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 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.

Reliance on Contractors

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.

Anti-Corruption Legislation

Prophecy Coal is subject to anti-corruption legislation including 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.

Dividends

To date, the Company has not paid any dividends on its outstanding shares and this is unlikely to occur in the foreseeable future. Any decision to pay dividends on the Prophecy Coal Shares will be made by its corporate governance and compensation committee on the basis of its earnings, financial requirements and other conditions.

Insurance 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 Company's Act* (British Columbia).

7. DIVIDENDS

The Company has not paid any dividends on its Shares and it is not contemplated that the Company will pay any dividends in the immediate or foreseeable future. It is the Company's intention to use all available cash flow to finance further operations and exploration of its resource properties. Holders of Prophecy Coal Shares will be entitled to receive dividends, if, as and when declared by the Company's board of directors out of profits, capital or otherwise.

There are no restrictions that could prevent the Company from paying dividends on the Shares except that the Company may not pay dividends if that payment would render it insolvent.

8. DESCRIPTION OF CAPITAL STRUCTURE

8.1 General Description of Capital Structure

The authorized capital of Prophecy Coal consists of an unlimited number of Shares without par value. As of the date of this AIF, there are 249,387,569 Prophecy Coal Shares issued and outstanding. The holders of Prophecy Coal Shares are entitled to vote at all meetings of shareholders of Prophecy Coal to receive dividends if, as and when declared by the Board and to participate rateably in any distribution of property or assets upon the liquidation, winding-up or other dissolution of Prophecy Coal. The Shares carry no pre-emptive rights, conversion or exchange rights, redemption, retraction, repurchase, sinking fund or purchase fund provisions. There are no provisions requiring the holders of the Shares to contribute additional capital and there are no restrictions on the issuance of additional securities by Prophecy Coal. There are no restrictions on the repurchase or redemption of the Shares by the Company except to the extent that any such repurchase or redemption would render Prophecy Coal insolvent pursuant to the BCBCA.

As of the date hereof, the Company also has Options outstanding to purchase up to 22,053,750 Shares with each Option exercisable to purchase one Prophecy Coal Share at exercise prices ranging from \$0.08 to \$0.80 and having expiry dates ranging from July 17, 2014 to February 3, 2019.

As of the date hereof, the Company has Warrants outstanding to purchase up to 13,225,583 Shares with each whole Warrant exercisable to purchase one Share at exercise price of \$0.18 and having expiry dates ranging from April 21, 2015 to October 28, 2015.

Stock Option Plan

The Company has adopted a 20% rolling stock option plan (the “**Stock Option Plan**”). The purpose of the Stock Option Plan is to allow the Company to grant Options to directors, officers, employees and consultants, as additional compensation, and as an opportunity to participate in the success of Prophecy Coal. The granting of Options is intended to align the interests of such persons with that of the Company’s Shareholders. Options are exercisable for up to 10 years or as determined by the Board and are required to have exercise prices equal to or greater than the Market Price (as defined by the Exchange and based on the volume weighted average trading price of the Shares as reported on the Exchange for the five trading days immediately preceding the day that Options are granted). Pursuant to the Stock Option Plan, the Board may from time to time authorize the issuance of Options to directors, officers, employees and consultants of Prophecy Coal or employees of companies providing management or consulting services to Prophecy Coal. The maximum number of Shares which may be reserved for issuance under the Stock Option Plan is equal to 20% of the issued and outstanding common shares at the date of grant.

Any Options granted under the Stock Option Plan vest at 12.5% per quarter over a two year period unless determined otherwise by the Board. The Stock Option Plan provides that if a Substitution Event as defined therein, such as a change of control occurs, any surviving or acquiring company must assume and Stock Options outstanding under the Stock Option Plan on substantially the same terms and conditions or substitute similar stock options. In addition, the Board may accelerate the vesting date, permit the conditional exercise of Stock Options, amend or modify the terms of the Stock Options, or terminate Stock Options not exercised prior to the completion of such Substitution Event.

9. MARKET FOR SECURITIES

9.1 Trading Price and Volume

The Company’s Shares trade on the TSX under the symbol “PCY”. Prior to October 19, 2011, the Company’s common shares traded on the TSX Venture Exchange. The following table shows the high and low trading prices and average daily trading volume of the Shares of the Company on the TSX and TSX Venture Exchange, as applicable, for the periods listed.

MONTH	HIGH (\$)	LOW (\$)	VOLUME
TSX			
March 2014 ⁽¹⁾	0.09	0.06	3,867,366
February 2014	0.095	0.08	67,493
January 2014	0.11	0.075	161,587
December 2013	0.095	0.06	226,959
November 2013	0.105	0.075	81,008
October 2013	0.125	0.075	106,229
September 2013	0.125	0.075	238,608
August 2013	0.135	0.11	98,970
July 2013	0.14	0.12	53,793
June 2013	0.175	0.12	89,214
May 2013	0.185	0.095	235,038
April 2013	0.14	0.08	118,567
March 2013	0.145	0.13	95,630
February 2013	0.165	0.13	329,433
January 2013	0.175	0.115	194,775
December 2012	0.15	0.11	215,800
November 2012	0.17	0.13	297,400
October 2012	0.16	0.13	283,000
September 2012	0.19	0.15	409,600
August 2012	0.20	0.16	369,800
July 2012	0.27	0.16	393,400
June 2012	0.33	0.23	449,100
May 2012	0.38	0.22	510,000
April 2012	0.44	0.33	215,800
March 2012	0.54	0.42	432,000
February 2012	0.55	0.43	751,400
January 2012	0.48	0.40	719,600
December 2011	0.49	0.39	297,600
November 2011	0.63	0.46	291,400
October 2011 ⁽²⁾	0.58	0.39	285,500
TSX Venture Exchange			
September 2011	0.74	0.46	440,600
August, 2011	0.77	0.54	1,130,600
July, 2011	1.00	0.50	2,145,700
June, 2011	0.76	0.57	164,900
May, 2011	0.85	0.61	694,700
April, 2011	0.99	0.83	402,600
March, 2011	1.12	0.87	539,500
February, 2011	1.11	0.88	735,600
January, 2011	1.17	0.91	1,078,700

Notes:

(1) Up to and including March28, 2014 being the date of the AIF.

(2) Trading on TSX began October 19, 2011.

9.2 Prior Sales of Unlisted Securities

The Company has no class of securities that is outstanding but not listed or quoted on a market place.

9.3 Escrowed Securities

As of the date of this AIF, no Shares of the Company are being held in escrow.

10. DIRECTORS AND OFFICERS

10.1 Name, Occupation and Security Holding

The following table sets forth the names and residencies of all directors and executive officers of the Company, the positions and offices with the Company held by such persons and their principal occupations. As of the date of this AIF, the directors and executive officers of the Company, as a group, beneficially own, or control or direct, directly or indirectly approximately 9.67% of the Company's Shares.

Name, Jurisdiction of Residence, Offices	Principal Occupation During Last Five Years ⁽⁴⁾	Director/Officer Since	Number of Common Shares Beneficially Owned, Controlled or Directed, Directly or Indirectly ⁽⁶⁾
John Lee, Taipei, Taiwan, Interim CEO, Executive Chairman and Director	President, Mau Capital Management LLC (private investor relations firm) from 2004 to present, CEO of Prophecy Coal from October 2009 to November 2012, Interim CEO of Prophecy Coal from November 2012 to present; Chairman of Prophecy Coal from June 2011 to January 2013; Executive Chairman of Prophecy Coal from January 2013 to present	June 13, 2011 (Director of Pre-amalgamated company ⁽⁵⁾ since October 21, 2009)	12,035,003 ⁽⁷⁾
D. Greg Hall, Vancouver, B.C., Director ⁽¹⁾⁽²⁾⁽³⁾	Self-employed businessman; Director of Silvercorp Metals Inc. from March 2005 to September 2010; Chairman and Director Ivory Energy Inc., (junior oil and gas issuer listed on the TSX-V Exchange) June 2006 to March 2009; former Executive Vice-President, Leede Financial Markets Inc. (investment brokerage house), February 2004 to February, 2005; Secretary and Director, Makevco Consulting Inc. (private consulting company), March 2000 to present	June 13, 2011 (Director of Pre-amalgamated company ⁽⁵⁾ since October 21, 2009)	1,590,000
Chuluunbaatar Baz Ulaanbaatar, Mongolia Director	President and CEO of Monnis International from 1998 to Present	Since June 13, 2011 (Director of Pre-amalgamated company ⁽⁵⁾ since October 29, 2009)	10,300,000
Harald Batista, Brazil, Director ⁽¹⁾⁽²⁾⁽³⁾	Co-Founder, consult at Bayesco from August 2012 to present, Power Messaging Coach at Corporate Visions Inc. from 2008 to present	July 27, 2012 (Special Advisor to Pre-amalgamated company ⁽⁵⁾ since January 5, 2010)	150,000
Irina Plavutska, Port Coquitlam, BC, Chief Financial Officer	Controller, C. Dikeakos Architects Inc. from August 2006 to August 2010. Controller, Prophecy Coal Corp. from August 2010 to August 2011, Interim CFO from August 2011 to November 2012, (appointed back as) Controller from November 2012 to September 9, 2013, CFO from September 2013 to present	September 11, 2013	42,500

Name, Jurisdiction of Residence, Offices	Principal Occupation During Last Five Years ⁽⁴⁾	Director/Officer Since	Number of Common Shares Beneficially Owned, Controlled or Directed, Directly or Indirectly ⁽⁶⁾
Tony Wong, Vancouver, BC, Corporate Secretary	Senior Legal Counsel, BC Securities Commission from November 2005 to November 2010. Senior Corporate Counsel, Global Relay Communications Inc. from December 2010 to May 2011. Lawyer (sole practitioner) from June 2011 to January 2014. General Counsel & Corporate Secretary, Prophecy Coal Corp. from February 2014 to present	February 3, 2014	Nil

Notes:

- (1) Member of the Audit Committee.
- (2) Member of the Compensation Committee.
- (3) Member of the Corporate Governance Committee.
- (4) The information as to principal occupation, business or employment and shares beneficially owned or controlled is not within the knowledge of the management of Prophecy Coal and has been furnished by the respective individuals. Each director or officer has held the same or similar principal occupation with the organization indicated or a predecessor thereof for the last five years.
- (5) Northern Platinum Ltd., Prophecy Holdings Inc. and Prophecy Resource Corp. were amalgamated on June 13, 2011 as one company under the name Prophecy Resource Corp. Prophecy Resource Corp. changed its name to Prophecy Coal Corp. on June 14, 2011.
- (6) The approximate number of Shares in all circumstances beneficially owned directly or indirectly, or over which control or direction is exercised by each proposed nominee as at the date hereof is based on information furnished by the named persons.
- (7) 9,230,170 of these Common Shares are held by Merit Holdings Ltd., a private company wholly owned and controlled by Mr. Lee.

11. PROMOTERS

Other than its directors and officers, there is no person who is or who has been within the two years immediately preceding the date of this AIF, a promoter of Prophecy Coal as defined under applicable Canadian securities laws.

12. LEGAL PROCEEDINGS

The Company has not been a defendant in any potentially material legal proceedings or regulatory actions during this fiscal year. The Company accrues for liabilities when it is probable and the amount can be reasonably estimated.

13. INTEREST OF MANAGEMENT AND OTHERS IN MATERIAL TRANSACTIONS

Except as otherwise disclosed in this AIF the Company is not aware of any material interest, direct or indirect, of any director or executive officer of the Company, any person or company beneficially owning or controlling, directly or indirectly, more than 10% of the Shares of the Company or any associate or affiliate of any such person in any transaction entered into by the Company in the most recently completed financial years that has materially affected or is reasonably expected to materially affect the Company.

John Lee, Harald Batista, and Greg Hall, who are directors and/or officers of the Company, were also directors and/or officers of Wellgreen Platinum. Messrs. Hall and Lee abstained from voting as directors of Prophecy Coal and of Wellgreen Platinum in respect of the Wellgreen Platinum Arrangement described in section 3.1. Prophecy Coal securities held by Messrs. Hall and Lee were treated in the same manner under the Wellgreen Platinum Arrangement as Prophecy Coal securities held by any other Prophecy Coal security holder.

Chuluunbaatar Baz is president, director and a control person of Monnis International LLC, a private company from which Prophecy Coal acquired mining equipment for the Ulaan Ovoo Property. Transactions with Monnis are negotiated at fair market value and Mr. Baz abstains from voting as a director of Prophecy Coal in respect of such transactions.

14. REGISTRAR AND TRANSFER AGENT

The Registrar and Transfer Agent for the Company is CompuShare Investor Services Inc., 3rd Floor, 510 Burrard Street, Vancouver, British Columbia, V6C 3B9.

15. MATERIAL CONTRACTS

Except for contracts entered into in the ordinary course of business, the only contracts entered into by the Company in the three years immediately prior to the date of this AIF that can reasonably be regarded as presently material to the Company are:

- (a) the arrangement agreement dated March 30, 2011 between the Prophecy Coal and Wellgreen Platinum concerning the Wellgreen Platinum Arrangement;
- (b) the credit agreement dated July 16, 2012 between Prophecy Coal and Waterton concerning the \$10 million Loan;
- (c) the Tariff Agreement dated May 14, 2013 between Prophecy Power and the Chandgana project working group designated by the Mongolian Ministry of Energy concerning tariff terms for 25 years for the coal mine mouth power plant project; and
- (d) the CSA dated June 5, 2013 between Chandgana Coal LLC and Prophecy Power concerning the supply of 3.6 million tonnes of coal per year for 25 years.

The material contracts specified above are available under Prophecy Coal's SEDAR profile at www.SEDAR.com.

16. INTERESTS OF EXPERTS

Prophecy Coal retained Wardrop Engineering Inc. to prepare an independent NI 43-101 pre-feasibility report on the Ulaan Ovoo Property located in Mongolia and an independent report on the Wellgreen Property. The Ulaan Ovoo Technical Report and the Wellgreen Report are referenced in Section 1.4 of this AIF - *Documents Incorporated by Reference*.

Prophecy Coal retained Kravits Geological Services, LLC to prepare an independent NI 43-101 report on the Chandgana Property located in Mongolia. The Chandgana Technical Report is referenced in Section 1.4 of this AIF - *Documents Incorporated by Reference*.

Prophecy Coal retained John T. Boyd Company to prepare an independent NI 43-101 report on the coal resources and preliminary economic assessment on the Chandgana Tal Coal Project. The PEA is referenced in Section 1.4 of this AIF.

Davidson & Company LLP, Chartered Accountants prepared the auditor's report for the audited annual financial statements of Prophecy Coal for the year ended December 31, 2013. Davidson & Company LLP is an independent auditor in accordance with the Rules of Professional Conduct of the Institute of Chartered Accountants of British Columbia.

Ernst & Young LLP, Chartered Accountants prepared the auditor's report for the audited annual financial statements of Prophecy Coal for the year ended December 31, 2012. Ernst & Young LLP is an independent auditor in accordance with the Rules of Professional Conduct of the Institute of Chartered Accountants of British Columbia.

To the best knowledge of the Company, none of the above mentioned experts or their respective associates or affiliates, beneficially owns, directly or indirectly, any securities of Prophecy Coal, has received or will receive any direct or indirect interests in the property of Prophecy Coal or is expected to be elected, appointed or employed as a director, officer or employee of Prophecy Coal or any associate or affiliate thereof.

17. ADDITIONAL INFORMATION

Additional information relating to the Company:

- (a) may be found under the Company's profile on SEDAR at www.SEDAR.com;
- (b) including directors and officers remuneration and indebtedness, principal holders of the Company's securities and securities authorized for issuance under equity compensation plans is contained in the Information Circular for the Company's most recent annual meeting of shareholders; and
- (c) is provided in the Company's financial statements and management discussion and analysis for its most recently completed financial year.

18. CORPORATE GOVERNANCE

18.01 Audit Committee

The Company has an Audit Committee comprised of directors D. Greg Hall (Chair) and Harald Batista each of whom is an independent director and financially literate within the meaning of National Instrument 52-101 *Audit Committees*.

The education and experience of each member of the Audit Committee relevant to the performance of his responsibilities as an Audit Committee member is as follows:

D. Greg Hall – Mr. Hall is a seasoned financial market professional with over 25 years of experience as a broker, senior executive officer and founder of a number of successful brokerage firms. Mr. Hall has also had extensive experience as a board member and executive director for a number of Canadian and United States public and private companies. He is a graduate of the SME Board program at the Rotman School of Management, University of Toronto, and a member of the Institute of Corporate Directors.

Harald Batista – Mr. Batista is an accomplished entrepreneur with over two decades of international sales and marketing experience. He holds an MBA degree from Santa Clara University in California.

The Audit Committee's mandate and responsibilities are detailed in its charter, a copy of which is attached as Appendix "A" hereto.

Pre-Approval Policies and Procedures

Under section 1(a)(iv) of the Audit and Risk Committee Charter, the Audit Committee shall approve in advance all audit and permitted non-audit services provided by the Company external auditors. However, the Audit Committee has not adopted any specific policies or procedures for the engagement of non-audit services.

External Auditor Service Fees (By Category)

The aggregate fees billed by the Company's external auditors in each of the last two fiscal years for audit fees are as follows:

Financial Year Ending	Audit Fees⁽¹⁾	Audit Related Fees⁽²⁾	Tax Fees⁽³⁾	All Other Fees⁽⁴⁾
December 31, 2013 Davidson & Company LLP	\$180,000	\$0	\$15,000	\$0
December 31, 2012 Ernst & Young LLP	\$381,600	\$50,000	\$41,000	\$0

Notes:

- (1) *“Audit Fees” include fees necessary to perform the annual audit and quarterly reviews of the Company’s financial statements and includes the fees of the Company’s auditor, Davidson & Company LLP for 2013, Ernst & Young LLP, for the fiscal year of 2012 and Smythe Ratcliffe LLP, for the fiscal year of 2011. Audit fees also include fees for review of tax provisions and for accounting consultations on matters reflected in the financial statements. Audit Fees also include audit or other attest services required by legislation or regulation, such as comfort letters, consents, reviews of securities filings and statutory audits.*
- (2) *“Audit-Related Fees” include services that are traditionally performed by the auditor. These audit-related services include employee benefit audits, due diligence assistance, accounting consultations on proposed transactions, internal control reviews and audit or attest services not required by legislation or regulation.*
- (3) *“Tax Fees” include fees for all tax services other than those included in “Audit Fees” and “Audit-Related Fees”. This category includes fees for tax compliance, tax planning and tax advice. Tax planning and tax advice includes assistance with tax audits and appeals, tax advice related to mergers and acquisitions, and requests for rulings or technical advice from tax authorities.*
- (4) *“All Other Fees” include all other non-audit service.*

18.02 Corporate Governance and Compensation Committee

The Company has a Corporate Governance and Compensation Committee comprised of directors D. Greg Hall (Chair) and Harald Batista.

APPENDIX "A"

AUDIT AND RISK COMMITTEE CHARTER

1. Purpose: Responsibilities and Authority

The Audit and Risk Committee (the "Audit Committee" or "Committee") shall carry out its responsibilities under applicable laws, regulations and stock exchange requirements with respect to the employment, compensation and oversight of the Company's independent auditor, and other matters under the authority of the Committee. The Committee also shall assist the Board of Directors in carrying out its oversight responsibilities relating to the Company's financial, accounting and reporting processes, the Company's system of internal accounting and financial controls, the Company's compliance with related legal and regulatory requirements, and the fairness of transactions between the Company and related parties. In furtherance of this purpose, the Committee shall have the following responsibilities and authority:

(a) Relationship with Independent Auditor.

(i) Subject to the law of British Columbia as to the role of the Shareholders in the appointment of independent auditors, the Committee shall have the sole authority to appoint or replace the independent auditor.

(ii) The Committee shall be directly responsible for the compensation and oversight of the work of the independent auditor (including resolution of disagreements between management and the independent auditor regarding financial reporting) for the purpose of preparing or issuing an audit report or related work.

(iii) The independent auditor shall report directly to the Committee.

(iv) The Committee shall approve in advance all audit and permitted non-audit services of the independent auditor, including the terms of the engagements and the fees payable; provided that the Committee Chairman may approve services to be performed by the independent auditors and the fee therefore between Committee meetings if the amount of the fee does not exceed \$◆, provided that any such approval shall be reported to the Committee at the next meeting thereof. The Committee may delegate to a subcommittee the authority to grant pre-approvals of audit and permitted non-audit services, provided that the decision of any such subcommittee shall be presented to the full Committee at its next scheduled meeting.

(v) At least annually, the Committee shall review and evaluate the experience and qualifications of the lead partner and senior members of the independent auditor team.

(vi) At least annually, the Committee shall obtain and review a report from the independent auditor regarding:

(A) the independent auditor's internal quality-control procedures;

(B) any material issues raised by the most recent internal quality-control review, or peer review, of the auditor, or by any inquiry or investigation by governmental or professional authorities within the preceding five years respecting one or more independent audits carried out by the firm;

(C) any steps taken to deal with any such issues; and

(D) all relationships between the independent auditor and the Company.

(vii) At least annually, the Committee shall evaluate the qualifications, performance

and independence of the independent auditor, including considering whether the auditor's quality controls are adequate and the provision of permitted non-audit services is compatible with maintaining the auditor's independence.

(viii) The Committee shall ensure the rotation of the lead (or coordinating) audit partner having primary responsibility for the audit, the concurring partner responsible for reviewing the audit, and other audit partners as required by law.

(ix) The Committee shall consider whether, in order to assure continuing auditor independence, it is appropriate to adopt a policy of rotating the independent auditing firm on a regular basis.

(x) The Committee shall recommend to the Board policies for the Company's hiring of employees or former employees of the independent auditor who were engaged on the Company's account or participated in any capacity in the audit of the Company.

(b) **Financial Statement and Disclosure Review.**

(i) The Committee shall review and discuss with management and the independent auditor the annual audited financial statements, including disclosures made in management's discussion and analysis, and recommend to the Board whether the audited financial statements should be filed with applicable securities regulatory authorities and included in the Company's annual reports.

(ii) The Committee shall review and discuss with management (and, to the extent the Committee deems it necessary or appropriate, the independent auditor) the Company's quarterly financial statements, including disclosures made in management's discussion and analysis, and recommend to the Board whether such financial statements should be filed with applicable securities regulatory authorities.

(iii) The Committee shall review and discuss with management and the independent auditor significant financial reporting issues and judgments made in connection with the preparation of the Company's financial statements, including the independent auditor's assessment of the quality of the Company's accounting principles, any significant changes in the Company's selection or application of accounting principles, any major issues as to the adequacy of the Company's internal controls over financial reporting and any special steps adopted in light of material control deficiencies.

(iv) At least annually and prior to the publication of annual audited financial statements, the Committee shall review and discuss with management and the independent auditor a report from the independent auditor on:

(A) all critical accounting policies and practices used by the Company;

(B) all alternative accounting treatments of financial information that have been discussed with management since the prior report, ramifications of the use of such alternative disclosures and treatments, the treatment preferred by the independent auditor, and an explanation of why the independent auditor's preferred method was not adopted; and

(C) other material written communications between the independent auditor and management since the prior report, such as any management letter or schedule of unadjusted differences, the development, selection and disclosure of critical accounting estimates, and analyses of the effect of alternative assumptions, estimates or GAAP methods on the Company's financial statements.

(v) Prior to their filing or issuance, the Committee shall review the Company's Annual Information Form/Annual Report to the SEC, quarterly and annual earnings press releases, and other financial press releases, including the use of "pro forma" or "adjusted" non-GAAP information.

(vi) The Committee shall review and discuss with management the financial information and earnings guidance provided to analysts and rating agencies. Such discussion may be specific or it may be in general regarding the types of information to be disclosed and the types of presentations to be made.

(c) **Conduct of the Annual Audit.** The Committee shall oversee the annual audit, and in the course of such oversight the Committee shall have the following responsibilities and authority:

(i) The Committee shall meet with the independent auditor prior to the audit to discuss the planning and conduct of the annual audit, and shall meet with the independent auditor as may be necessary or appropriate in connection with the audit.

(ii) The Committee shall ascertain that the independent auditor is registered and in good standing with the Canadian Public Accounting Board and the Public Company Accounting Oversight Board and that the independent auditor satisfies all applicable Canadian independence standards, Independence Standards Board Standard No. 1, and SEC Regulation S-X, Section 2-01. The Committee shall obtain from the auditor a written statement delineating all relationships between the auditor and the Company as per ISB Standard 1, and review relationships that may impact the objectivity and independence of the auditor.

(iii) The Committee shall discuss with the independent auditor the matters required to be discussed by Statement on Auditing Standards No. 61 relating to the conduct of the audit, including

(A) the adoption of, or changes to, the Company's significant auditing and accounting principles and practices as suggested by the independent auditor, internal auditors or management;

(B) the management letter provided by the independent auditor and the Company's response to that letter; and

(C) any difficulties encountered in the course of the audit work, including any restrictions on the scope of activities or access to requested information, and any significant disagreements with management.

(iv) The Committee shall obtain from the independent auditor assurance that the audit was conducted in a manner consistent with Section 10A of the Securities Exchange Act of 1934 and that, in the course of conducting the audit, the independent auditor has not become aware of information indicating that an illegal act has or may have occurred or, if such an act may have occurred, that the independent auditor has taken all action required by Section 10A(b) of the Securities Exchange Act of 1934.

(v) The Committee shall make such inquiries to the management and the independent auditor as they deem necessary or appropriate to satisfy themselves regarding the efficacy of the Company's financial and internal controls and procedures and the auditing process.

(d) **Compliance and Oversight.**

(i) The Committee shall meet periodically with management and the independent auditor in separate executive sessions. The Committee may also, to the extent it deems necessary or appropriate, meet with the Company's investment bankers and financial analysts who follow the Company.

(ii) The Committee shall discuss with management and the independent auditor the effect of regulatory and accounting initiatives as well as off-balance sheet structures on the Company's financial statements.

(iii) The Committee shall discuss with management the Company's major financial risk exposures and the steps management has taken to monitor and control such exposures, including the Company's risk assessment and risk management policies.

(iv) At least annually and prior to the filing of the AIF/Annual Report to the SEC, the Committee shall review with management and the independent auditor the disclosure controls and procedures and confirm that the Company (with CEO and CFO participation) has evaluated the effectiveness of the design and operation of the controls within 90 days prior to the date of filing of the AIF/Annual Report to the SEC. The Committee also shall review with management and the independent auditor any deficiencies in the design and operation of internal controls and significant deficiencies or material weaknesses therein and any fraud involving management or other employees who have a significant role in the Company's internal controls. As a part of that review, the Committee shall review the process followed in preparing and verifying the accuracy of the CEO and CFO annual certifications required to be included in the Annual Report to the SEC.

(v) At least annually and prior to the filing of the AIF/Annual Report to the SEC, the Committee shall review with management and the independent auditor management's internal control report and assessment of the internal controls and procedures, and the independent auditor's report on and assessment of the internal controls and procedures.

(vi) The Committee shall establish procedures for the receipt, retention and treatment of complaints received by the Company regarding accounting, internal accounting controls or auditing matters, and the confidential, anonymous submission by employees of concerns regarding questionable accounting or auditing matters.

(vii) The Committee shall discuss with management and the independent auditor any correspondence with regulators or governmental agencies and any employee complaints or reports which raise material issues regarding the Company's financial statements or accounting policies.

(viii) At least annually, the Committee shall meet with the Company's legal counsel and discuss any legal matters that may have a material impact on the financial statements or the Company's compliance policies.

(ix) The Committee shall prepare all reports required under applicable laws, regulations and stock exchange requirements.

(x) The Committee shall exercise oversight with respect to anti-fraud programs and controls.

(e) **Internal Audit.**

(i) The Audit Committee shall have the sole authority to appoint or replace the internal auditor.

(ii) The internal auditor shall report directly to the Audit Committee, provided however that for functional and administrative purposes the internal auditor shall report to the CFO.

(iii) The Audit Committee shall be directly responsible for the compensation and oversight of the work of the internal auditor, including approval of the annual budget of the internal audit department.

(iv) At least annually, the Audit Committee shall review the Internal Audit Charter and the qualifications, performance and independence of the internal auditor.

(v) The Audit Committee shall receive regular reports from the internal auditor on the matters specified in the Internal Audit Charter. The Audit Committee may also request that the internal auditor provide such additional information and advice as the Audit Committee may request.

(f) **Related Party Transactions.**

(i) The Committee shall review for fairness to the Company proposed transactions, contracts and other arrangements between the Company and its subsidiaries and any related party or affiliate, and make recommendations to the Board whether any such transactions, contracts and other arrangements should be approved or continued. The foregoing shall not include any compensation payable pursuant to any plan, program, contract or arrangement subject to the authority of the Company's Compensation Committee.

(ii) As used herein the term "related party" means any officer or director of the Company or any subsidiary, or any shareholder holding a greater than 10% direct or indirect financial or voting interest in the Company, and the term "affiliate" means any person, whether acting alone or in concert with others, that has the power to exercise a controlling influence over the Company and its subsidiaries. "Related party" includes Hunter Dickinson Services Inc.

(g) **Additional duties.** The Committee shall perform the following additional duties:

(i) The Committee shall review and make recommendations to the full Board of Directors regarding transactions of a fundamental nature such as amalgamations, mergers and material acquisitions and dispositions, excluding Portfolio Investments as defined in the Investment Committee Charter.

(ii) The Committee shall review and make recommendations to the full Board of Directors regarding proposed new business activities that require an allocation of resources in excess of C\$◆.

(iii) The Committee shall review and make recommendations to the full Board of Directors regarding any proposed material change to a business or strategic plan that has been previously approved by the Board of Directors.

(iv) To the extent not otherwise provided in this Charter, the Committee shall review disclosure of financial information and other documents required by law to be approved by the Board of Directors before release to the public.

(v) The Committee shall oversee the Company's risk assessment and risk management policies, and regularly review the top risks identified by the Risk Steering Committee and the policies and practices adopted by the Company to mitigate those

risks.

(vi) The Committee shall review and approve hedging, investment and dividend policies.

(vii) The Committee shall oversee the Company's insurance program and approve insurance policy limits.

(viii) The Committee shall review the appointment of senior financial personnel and make recommendations to the Board of Directors regarding the appointment of the Chief Financial Officer.

(ix) The Committee shall oversee company sponsored pension plans.

(x) The Audit Committee shall recommend to the Nominating and Governance

(xi) Committee the qualifications and criteria for membership on the Committee.

2. **Structure and Membership**

(a) **Number and qualification.** The Committee shall consist of three persons unless the Board should from time to time otherwise determine. All members of the Committee shall meet the experience and financial literacy requirements of National Instrument NI 52-110 and the rules of the Toronto Stock Exchange and the NYSE Amex. At least one member of the Committee shall be a "financial expert" as defined in Item 407 of SEC Regulation S-K.

(b) **Selection and Removal.** Members of the Committee shall be appointed by the Board, upon the recommendation of the Nominating and Governance Committee. The Board may remove members of the Committee at any time with or without cause.

(c) **Independence.** All of the members of the Committee shall be "independent" as required for audit committees by National Instrument NI 52-110, the rules of the Toronto Stock Exchange and the NYSE Amex, and SEC Rule 10A.

(d) **Chair.** Unless the Board elects a Chair of the Committee, the Committee shall elect a Chair by majority vote.

(e) **Compensation.** The compensation of the Committee shall be as determined by the Board.

(f) **Term.** Members of the Committee shall be appointed for one-year terms. Each member shall serve until his or her replacement is appointed, or until he or she resigns or is removed from the Board or the Committee.

3. **Procedures and Administration**

(a) **Meetings.** The Committee shall meet as often as it deems necessary in order to perform its responsibilities, but not less than quarterly. The Committee shall keep minutes of its meetings and any other records as it deems appropriate.

(b) **Subcommittees.** The Committee may form and delegate authority to one or more subcommittees, consisting of at least one member, as it deems appropriate from time to time under the circumstances.

(c) **Reports to the Board.** The Committee shall report (orally or otherwise) regularly to the Board following meetings of the Committee with respect to such matters as are relevant to the

Committee's discharge of its responsibilities, and shall report in writing on request of the Chairman of the Board.

(d) **Charter.** The Committee shall, at least annually, review and reassess the adequacy of this Charter and recommend any proposed changes to the Board for approval.

(e) **Independent Advisors.** The Committee shall have the authority to engage such independent legal and other advisors as it deems necessary or appropriate to carry out its responsibilities. Such independent advisors may be regular advisors to the Company. The Committee is empowered, without further action by the Board, to cause the Company to pay appropriate compensation to advisors engaged by the Committee.

(f) **Investigations.** The Committee shall have the authority to conduct or authorize investigations into any matters within the scope of its responsibilities as it deems appropriate, including the authority to request any Officer or other person to meet with the Committee and to access all Company records.

(g) **Annual Self-Evaluation.** The Committee shall evaluate its own performance at least annually.

4. Additional Powers

The Committee shall have such other duties as may be delegated from time to time by the Board of Directors.

5. Limitation of Committee's Role

While the Committee has the responsibilities and powers set forth in this Charter, it is not the duty of the Committee to plan or conduct audits or to determine that the Company's financial statements and disclosures are complete and accurate and are in accordance with GAAP and applicable rules and regulations. These are the responsibilities of management and the independent auditor.

6. Committee Member Independence and Financial Literacy Requirements

A. Independence

(a) See Appendix 2 of the Company's Corporate Governance Overview and Guidelines.

B. Financial Literacy Requirements

NI 52-110

Section 3.1(4) states that each audit committee member must be financially literate.

Section 1.6 defines the meaning of financial literacy as follows:

"For the purposes of this Instrument, an individual is financially literate if he or she has the ability to read and understand a set of financial statements that present a breadth and level of complexity of accounting issues that are generally comparable to the breadth and complexity of the issues that can reasonably be expected to be raised by the issuer's financial statements."

NYSE AMEX Section 803(B)(2)(a)(iii)

Each issuer must have an Audit Committee of at least three members, each of whom:

"is able to read and understand fundamental financial statements, including a company's balance sheet, income statement, and cash flow statement. Additionally, each issuer

must certify that it has, and will continue to have, at least one member of the audit committee who is financially sophisticated, in that he or she has past employment experience in finance or accounting, requisite professional certification in accounting, or any other comparable experience or background which results in the individual's financial sophistication, including but not limited to being or having been a chief executive officer, chief financial officer, other senior officer with financial oversight responsibilities. A director who qualifies as an audit committee financial expert under Item 407(d)(5)(ii) of Regulation S-K . . . is presumed to qualify as financially sophisticated."

C. Financial Expert

ITEM 407(d)(5)(ii) OF REGULATION S-K, DEFINITION OF FINANCIAL EXPERT

For purposes of this Item, an audit committee financial expert means a person who has the following attributes:

- (A) An understanding of generally accepted accounting principles and financial statements;
- (B) The ability to assess the general application of such principles in connection with the accounting for estimates, accruals and reserves;
- (C) Experience preparing, auditing, analyzing or evaluating financial statements that present a breadth and level of complexity of accounting issues that are generally comparable to the breadth and complexity of issues that can reasonably be expected to be raised by the small business issuer's financial statements, or experience actively supervising one or more persons engaged in such activities;
- (D) An understanding of internal control over financial reporting; and
- (E) An understanding of audit committee functions.

A person shall have acquired such attributes through:

- (A) Education and experience as a principal financial officer, principal accounting officer, controller, public accountant or auditor or experience in one or more positions that involve the performance of similar functions;
- (B) Experience actively supervising a principal financial officer, principal accounting officer, controller, public accountant, auditor or person performing similar functions;
- (C) Experience overseeing or assessing the performance of companies or public accountants with respect to the preparation, auditing or evaluation of financial statements; or
- (D) Other relevant experience.