



**Unaudited Interim Consolidated Financial Statements**

**Three and Nine Months Ended July 31, 2011**

**ADRIANA RESOURCES INC.**  
**(An Exploration Stage Company)**  
**Interim Consolidated Balance Sheets**  
**(Unaudited and expressed in Canadian dollars)**

| As at  | July 31<br>2011       | October 31<br>2010   |
|--|-----------------------|----------------------|
| <b>ASSETS</b>                                    |                       |                      |
| <b>Current assets</b>                            |                       |                      |
| Cash and cash equivalents                        | \$ 27,425,527         | \$ 1,879,633         |
| Marketable securities (Note 4)                   | 305,000               | -                    |
| Other receivables                                | 891,719               | 494,988              |
| Prepaid expenses                                 | 511,712               | 103,201              |
|  | <u>29,133,958</u>     | <u>2,477,822</u>     |
| <b>Capital assets</b> (Note 5)                   | 75,547,945            | 68,923,389           |
|  | <u>\$ 104,681,903</u> | <u>\$ 71,401,211</u> |
| <b>LIABILITIES</b>                               |                       |                      |
| <b>Current liabilities</b>                       |                       |                      |
| Accounts payable and accrued liabilities         | \$ 6,052,254          | \$ 4,145,664         |
| Current portion of interest payable (Note 6)     | -                     | 34,117               |
| Convertible debentures, current portion (Note 6) | -                     | 3,273,373            |
|  | <u>6,052,254</u>      | <u>7,453,154</u>     |
| <b>Interest payable</b> (Note 6)                 | 1,442,055             | 1,034,863            |
| <b>Convertible debentures</b> (Note 6)           | 5,977,640             | 5,678,968            |
| <b>Future income tax liabilities</b> (Note 7)    | 9,302,933             | 7,236,990            |
|  | <u>22,774,882</u>     | <u>21,403,975</u>    |
| <b>Non-controlling interest</b> (Note 8)         | 11,661,527            | 11,350,566           |
| <b>SHAREHOLDERS' EQUITY</b>                      |                       |                      |
| <b>Share capital</b> (Note 9)                    | 122,051,383           | 84,309,312           |
| <b>Equity portion of convertible debentures</b>  | 1,423,529             | 2,207,021            |
| <b>Warrants</b> (Note 9d)                        | 528,559               | 530,552              |
| <b>Contributed surplus</b> (Note 10)             | 4,780,369             | 4,667,714            |
| <b>Deficit</b>                                   | (58,538,346)          | (53,067,929)         |
|  | <u>70,245,494</u>     | <u>38,646,670</u>    |
|  | <u>\$ 104,681,903</u> | <u>\$ 71,401,211</u> |

Commitments and contingencies (Note 13)  
Subsequent event (Note 16)

*The accompanying notes form an integral part of the consolidated financial statements.*

**ADRIANA RESOURCES INC.****(An Exploration Stage Company)****Interim Consolidated Statements of Loss and Comprehensive Loss and Deficit****(Unaudited and expressed in Canadian dollars)**

|   | Three months ended July 31 |                      | Nine months ended July 31 |                      |
|---|----------------------------|----------------------|---------------------------|----------------------|
|   | 2011                       | 2010                 | 2011                      | 2010                 |
| <b>Administrative expenses</b>                              |                            |                      |                           |                      |
| Amortization  | \$ 31,386                  | \$ 3,617             | \$ 45,428                 | \$ 13,001            |
| Business development  | 214,466                    | 50,072               | 513,405                   | 197,235              |
| Conferences   | 268                        | 950                  | 14,388                    | 16,923               |
| Interest on convertible debentures                          | 264,192                    | 402,267              | 947,403                   | 1,152,745            |
| Investor relations  | 62,535                     | 7,322                | 150,238                   | 114,242              |
| Professional and consulting fees                            | 1,100,624                  | 225,862              | 2,556,622                 | 739,624              |
| Rent and office expenses                                    | 97,047                     | 147,502              | 244,278                   | 458,962              |
| Salaries and benefits                                       | 376,660                    | 321,153              | 1,146,345                 | 1,169,538            |
| Stock-based compensation (Note 9c)                          | 234,867                    | 252,501              | 670,308                   | 903,978              |
| Transfer agent and filing fees                              | 18,203                     | 5,610                | 84,657                    | 43,529               |
| Travel  | 9,617                      | 7,450                | 20,929                    | 36,470               |
| <b>Loss before the following:</b>                           | <b>2,409,865</b>           | <b>1,424,306</b>     | <b>6,394,001</b>          | <b>4,846,247</b>     |
| <b>Other (income) expenses</b>                              |                            |                      |                           |                      |
| Interest income   | (82,513)                   | (1,207)              | (131,724)                 | (4,762)              |
| Loss (gain) on foreign exchange                             | 185,343                    | 414,983              | 255,431                   | (137,215)            |
| Loss realized on former premises                            | -                          | 351,536              | -                         | 351,536              |
| Write-off of mineral property interests                     | -                          | 200,183              | -                         | 200,183              |
| Non-controlling interest (Note 8)                           | (105,996)                  | (170,971)            | (277,039)                 | (86,990)             |
| Unrealized loss   |                            |                      |                           |                      |
| on marketable securities (Note 4)                           | 340,000                    | -                    | 415,000                   | -                    |
| Gain on disposal of mineral property interests (Note 5biii) | -                          | 7,357                | (1,185,252)               | (740,091)            |
| <b>Loss and comprehensive loss for the period</b>           | <b>2,746,699</b>           | <b>2,226,187</b>     | <b>5,470,417</b>          | <b>4,428,908</b>     |
| <b>Deficit, beginning of the period</b>                     | <b>55,791,647</b>          | <b>48,894,335</b>    | <b>53,067,929</b>         | <b>46,691,614</b>    |
| <b>Deficit, end of the period</b>                           | <b>\$ 58,538,346</b>       | <b>\$ 51,120,522</b> | <b>\$ 58,538,346</b>      | <b>\$ 51,120,522</b> |
| <b>Basic and diluted loss per common share</b>              |                            |                      |                           |                      |
|   | \$ (0.02)                  | \$ (0.03)            | \$ (0.04)                 | \$ (0.06)            |
| <b>Weighted average number of shares outstanding</b>        |                            |                      |                           |                      |
|   | 131,397,400                | 77,993,189           | 130,038,764               | 79,399,260           |

*The accompanying notes form an integral part of the consolidated financial statements.*

**ADRIANA RESOURCES INC.**  
**(An Exploration Stage Company)**  
**Interim Consolidated Statements of Cash Flows**  
**(Unaudited and expressed in Canadian dollars)**

|   | Three months ended July 31 |                     | Nine months ended July 31 |                     |
|---|----------------------------|---------------------|---------------------------|---------------------|
|   | 2011                       | 2010                | 2011                      | 2010                |
| <b>Cash provided by (used in)</b>                         |                            |                     |                           |                     |
| <b>Operating activities</b>                               |                            |                     |                           |                     |
| Loss for the period                                       | \$ (2,746,699)             | \$ (2,226,187)      | \$ (5,470,417)            | \$ (4,428,908)      |
| Items not involving cash:                                 |                            |                     |                           |                     |
| Amortization  | 31,386                     | 3,617               | 45,428                    | 13,001              |
| Unrealized portion of foreign exchange loss (gain)        | 177,546                    | (2,858)             | 273,993                   | (138,736)           |
| Accretion on convertible debentures                       | 114,645                    | 181,513             | 432,194                   | 519,163             |
| Stock-based compensation                                  | 234,867                    | 252,501             | 670,308                   | 903,978             |
| Application of provision for loss on former premises      | (7,000)                    | 301,000             | (47,000)                  | 301,000             |
| Write-off of property interests                           | -                          | 200,183             | -                         | 200,183             |
| Unrealized loss on marketable securities                  | 340,000                    | -                   | 415,000                   | -                   |
| Non-controlling interest                                  | (105,996)                  | (170,971)           | (277,039)                 | (86,990)            |
| Loss (gain) on disposal of mineral property interests     | -                          | 7,357               | (1,185,252)               | (740,091)           |
|   | (1,961,251)                | (1,453,845)         | (5,142,785)               | (3,457,400)         |
| Changes in non-cash working capital:                      |                            |                     |                           |                     |
| Other receivables and prepaid expenses                    | (489,854)                  | (381,094)           | (465,738)                 | 90,791              |
| Accounts payable and accrued liabilities                  | 218,334                    | 178,746             | 1,130,935                 | 477,320             |
| <b>Cash used in operating activities</b>                  | <b>(2,232,771)</b>         | <b>(1,656,193)</b>  | <b>(4,477,588)</b>        | <b>(2,889,289)</b>  |
| <b>Investing activities</b>                               |                            |                     |                           |                     |
| Port facility expenditures                                | (200,222)                  | 303,633             | (579,963)                 | (314,607)           |
| Mineral property expenditures                             | (3,127,782)                | (1,913,545)         | (4,386,129)               | (3,155,807)         |
| Office equipment expenditures                             | (14,940)                   | (11,487)            | (33,816)                  | (19,832)            |
| Proceeds from disposal of mineral property interests      | -                          | (7,357)             | 465,252                   | 340,091             |
| <b>Cash used in investing activities</b>                  | <b>(3,342,944)</b>         | <b>(1,628,756)</b>  | <b>(4,534,656)</b>        | <b>(3,150,155)</b>  |
| <b>Financing activities</b>                               |                            |                     |                           |                     |
| Proceeds from share issuance, net of issue costs          | -                          | 3,558,043           | 33,651,723                | 8,176,566           |
| Proceeds from exercise of options and warrants            | 79,076                     | -                   | 906,415                   | 26,291              |
| <b>Cash provided by financing activities</b>              | <b>79,076</b>              | <b>3,558,043</b>    | <b>34,558,138</b>         | <b>8,202,857</b>    |
| <b>Increase (decrease) in cash and cash equivalents</b>   | <b>(5,496,639)</b>         | <b>273,094</b>      | <b>25,545,894</b>         | <b>2,163,413</b>    |
| <b>Cash and cash equivalents, beginning of the period</b> | <b>32,922,166</b>          | <b>2,252,188</b>    | <b>1,879,633</b>          | <b>361,869</b>      |
| <b>Cash and cash equivalents, end of the period</b>       | <b>\$ 27,425,527</b>       | <b>\$ 2,525,282</b> | <b>\$ 27,425,527</b>      | <b>\$ 2,525,282</b> |
| <b>Supplementary cash flow information</b>                |                            |                     |                           |                     |
| Interest paid   | \$ 115,607                 | \$ -                | \$ 142,112                | \$ -                |

*The accompanying notes form an integral part of the consolidated financial statements.*

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**ADRIANA RESOURCES INC.**  
**(An Exploration Stage Company)**  
**NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS**  
**FOR THE NINE MONTHS ENDED JULY 31, 2011 AND 2010**  
**(Unaudited and expressed in Canadian Dollars)**

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## **1. NATURE OF OPERATIONS**

Adriana Resources Inc. (and its subsidiaries, collectively the “Company”) was incorporated under the laws of British Columbia and continued under the *Canada Business Corporations Act*. The Company’s principal business activities include the acquisition, exploration and development of resource properties including its Lac Otnuk Iron Ore Project in Nunavik, Québec (the “Lac Otnuk Property”) and the development of an iron ore port facility in Brazil (the “Port Facility”). The Company’s Class “A” common shares (the “Common Shares”) are listed on the TSX Venture Exchange under the symbol ADI.V.

These consolidated financial statements include the accounts of the following subsidiaries (wholly-owned unless otherwise indicated), Brazore Resources Inc., Brazore Holdings Ltd. (“Brazore Holdings”) (60%), Brazore Representação, Importação, Exportação e Consultoria Ltda. (“Brazore Ltda.”) (effective interest 56.1%), Adriana Resources Mineracao Ltda., Adriana Resources (BVI) Inc. (inactive), Adriana Resources Mexico, SA de CV (inactive), Adriana Mining Corporation and Lac Otnuk Mines Inc. (inactive). The 60%-owned subsidiary Brazore Holdings Ltd. with its 93.5%-owned subsidiary Brazore Ltda. are collectively referred to as “Brazore” in these consolidated financial statements. All significant intercompany transactions and balances have been eliminated.

The Company has no source of operating cash flows, has not yet achieved profitable operation, has accumulated losses to July 31, 2011 of \$58,538,346 since its inception and expects to incur further losses in the development of its business; however, with the entering into, as of January 12, 2011, of a binding framework agreement (the “Framework Agreement”) with WISCO International Resources Development & Investment Limited (“WISCO”) (see *Note 5b*), together with the closing on March 23, 2011 of the private placement contemplated under the Framework Agreement, the Company is now in a position to proceed with the continued exploration of its Lac Otnuk and December Lake properties.

## **2. FINANCIAL STATEMENT PRESENTATION**

The accompanying interim consolidated financial statements include all adjustments that are, in the opinion of management of the Company, necessary for fair presentation. These interim consolidated financial statements do not conform in all respects to the requirements of generally accepted accounting principles for annual consolidated financial statements, as they do not include all necessary disclosures, and accordingly should be read in conjunction with the Company’s October 31, 2010 audited consolidated financial statements and notes thereto.

## **3. ACCOUNTING POLICIES**

The consolidated financial statements of the Company follow the same accounting principles and methods of application as those disclosed in Note 3 of the Company’s audited consolidated financial statements for the year ended October 31, 2010, other than the following.

### *Financial Instruments Held for Trading*

Held-for-trading financial assets are typically acquired for resale prior to maturity. They are measured at fair value on the balance sheet, with realized and unrealized gains and losses reported in the statement of loss.

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*Convergence with International Financial Reporting Standards*

In February 2008, the Accounting Standards Board confirmed that IFRS will replace Canadian GAAP for publicly accountable enterprises for financial periods beginning on and after January 1, 2011. The Company's first mandatory filing under IFRS, which will be for the quarter ending January 31, 2012, will contain IFRS-compliant information on a comparative basis, as well as reconciliations for that quarter and as at the November 1, 2010 transition date. Although IFRS uses a conceptual framework similar to Canadian GAAP, there are significant differences in recognition, measurement and disclosure. The Company has developed a plan for IFRS convergence and has started the implementation process. The Company is not currently in a position to fully determine the impact on the consolidated results on transition to IFRS.

**4. MARKETABLE SECURITIES**

The Company's marketable securities are comprised of 500,000 common shares of Cap-Ex Ventures Ltd. ("Cap-Ex") that were acquired as part of the proceeds on sale of the Company's remaining Bedford Labrador mineral claims (see *Note 5biii*) and are held for trading. The shares have a hold period that expired on August 19, 2011. The shares were written down to their market value as of July 31, 2011 (\$305,000), resulting in an unrealized fair-value loss in the three months ended July 31, 2011 of \$340,000 and in the nine months ended July 31, 2011 of \$415,000. Cap-Ex's shares are listed on the TSX Venture Exchange and trade under the stock symbol "CEV".

**5. CAPITAL ASSETS**

Capital assets consist of the following:

|                    | July 31, 2011<br>Cost    | Accumulated<br>Amortization | Net Book<br>Value    |
|--------------------|--------------------------|-----------------------------|----------------------|
| Port Facility      | \$ 56,866,004            | \$ -                        | \$ 56,866,004        |
| Mineral properties | 18,561,914               | -                           | 18,561,914           |
| Office             | 189,764                  | 69,737                      | 120,027              |
|                    | <b>\$ 75,617,682</b>     | <b>\$ 69,737</b>            | <b>\$ 75,547,945</b> |
|                    | October 31, 2010<br>Cost | Accumulated<br>Amortization | Net Book<br>Value    |
| Port Facility      | \$ 55,286,391            | \$ -                        | \$ 55,286,391        |
| Mineral properties | 13,505,360               | -                           | 13,505,360           |
| Office             | 182,088                  | 50,450                      | 131,638              |
|                    | <b>\$ 68,973,839</b>     | <b>\$ 50,450</b>            | <b>\$ 68,923,389</b> |

**a) Port Facility**

The Company currently holds an effective 56.1% indirect interest in the Port Facility through a 60% owned indirect subsidiary, Brazore Holdings, which owns a 93.5% interest in Brazore Ltda., the Company's Brazilian subsidiary which owns and is developing the Port Facility. Under the terms of a 2007 agreement between Brazore Holdings and Brazore Ltda. and the latter's minority shareholders, Brazore Holdings' interest will be increased to 96.75%, equivalent to a 58.5% indirect interest by Adriana, upon Brazore Ltda.'s expenditures on the Port Facility exceeding US\$55,000,000. Through July 31, 2011, approximately US\$31,758,000 (October 31, 2010 - US\$30,316,000) has been invested.

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Pursuant to an agreement dated August 21, 2007 with Athena Holdings LLC (“Athena”) (the “Brazore Transaction”), the Company transferred a 50% interest in its subsidiary, Brazore Holdings, to Athena in exchange for Athena’s 93.5% interest in Brazore Ltda. Under the terms of the agreement, the Company maintained and increased its interest in Brazore by funding Brazore Ltda.’s plan to develop the Port Facility as follows: (i) a first tranche of US\$5,000,000 by October 20, 2007 to maintain a 50% ownership interest; and (ii) a second tranche of US\$17,000,000 by November 29, 2007 to earn a 60% interest. The US\$22,000,000 (the “Two Tranches”) provided funding for the purchase of certain of the land for the Port Facility and for initial engineering and other environmental studies. On April 1, 2009, the Company provided notice to Athena that it would not proceed with the funding of an additional US\$33,000,000 to earn a 75% interest in Brazore. The existing agreement does not provide for any capital contributions by Athena, nor for any additional dilution of Athena’s interest beyond that provided for above. As of July 31, 2011, the Company has advanced an additional US\$11,566,000 in excess of the Two Tranches, which has been used to fund the continued advancement of the Port Facility in Brazil. On January 3, 2011, Athena gave notice of its intention to sell its 40% ownership in Brazore Holdings. Pursuant to the terms of the Brazore Transaction, Adriana had a right of first refusal until February 12, 2011, which right was not exercised.

In accordance with EIC 124, the Brazore Transaction was considered to be an asset acquisition for accounting purposes since Brazore did not constitute a business. When an asset is acquired other than in a business combination and the tax basis of that asset is less than its cost, the cost of future income taxes recognized at the time of acquisition is added to the cost of the asset since that forms part of the cost of acquisition. Accordingly, the Company has recorded the surplus of the asset’s carrying amount as an addition to the asset, which includes the income tax effect in accordance with Brazilian income tax rates. At July 31, 2011, this addition comprises \$20,665,379 of the asset and the associated future income tax liability was \$7,736,833 (October 31, 2010 - \$19,774,471 and \$7,236,990, respectively). The increase of \$499,843 in the related future income tax liability in the nine months ended July 31, 2011 includes a foreign exchange adjustment of \$196,934.

As at July 31, 2011, the primary asset of Brazore was the land for the Port Facility, comprised of certain parcels on the coast of Brazil, purchased in December 2007, and on the adjacent island, purchased in 2008.

Costs capitalized to the Port Facility include permitting, environmental, geological, topographical, seismic surveying, travel to port site and royalty payments paid to Athena as described above.

The carrying value of the Port Facility consists of the following land costs and port design and development expenditures:

|                             | October 31 2010      | Additions           | July 31, 2011        |
|-----------------------------|----------------------|---------------------|----------------------|
| Land                        | \$ 39,428,147        | \$ -                | \$ 39,428,147        |
| Port design and development | 15,858,244           | 1,579,613           | 17,437,857           |
|                             | <u>\$ 55,286,391</u> | <u>\$ 1,579,613</u> | <u>\$ 56,866,004</u> |

**b) Mineral Properties**

*Labrador Trough, Nunavik, Québec*

The Company’s Labrador Trough projects are comprised of the Lac Otelnuk Iron Ore Project and the December Lake Iron Ore Prospect and, in 2010, the Bedford Iron Ore Prospect.

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Mineral properties consist of the following deferred expenditures pertaining to the Labrador Trough projects:

|                                  | Three months ended<br>July 31, 2011 | Nine months ended<br>July 31, 2011 | Year ended<br>October 31, 2010 |
|----------------------------------|-------------------------------------|------------------------------------|--------------------------------|
| Balance, beginning of the period | \$ 14,829,909                       | \$ 13,505,360                      | 8,925,658                      |
| Acquisition and maintenance      | 19,402                              | 180,851                            | 194,652                        |
| Camp and expediting              | 1,886,886                           | 2,199,947                          | 1,851,887                      |
| Drilling                         | 1,086,093                           | 1,110,803                          | 1,463,697                      |
| Equipment                        | -                                   | 32,567                             | 258,612                        |
| Geochemistry and metallurgical   | 103,466                             | 413,427                            | 287,375                        |
| Geological and geophysics        | 24,405                              | 66,562                             | 46,630                         |
| Environmental                    | 431,127                             | 431,127                            | 134,601                        |
| Professionals and consultants    | 100,166                             | 511,142                            | 176,532                        |
| Project administration           | -                                   | -                                  | -                              |
| Salaries and benefits            | 660                                 | 2,360                              | 11,905                         |
| Surveying                        | -                                   | -                                  | 232,356                        |
| Travel                           | 79,800                              | 107,768                            | 121,638                        |
| Incurred during the period       | 3,732,005                           | 5,056,554                          | 4,779,885                      |
|                                  | 18,561,914                          | 18,561,914                         | 13,705,543                     |
| Less: written off on abandonment | -                                   | -                                  | (200,183)                      |
| Balance, end of the period       | \$ 18,561,914                       | \$ 18,561,914                      | \$ 13,505,360                  |

On January 12, 2011, the Company entered into a binding Framework Agreement with WISCO for a total investment of \$120,000,000, of which \$28,366,389 was contributed by way of a private placement on March 23, 2011. The Framework Agreement contemplates the formation of a joint venture or partnership to hold Adriana's current interests in the Company's Lac Otelnuk and December Lake iron ore properties in Nunavik, Quebec with WISCO contributing an additional \$91,633,611, being the balance of the original commitment. WISCO will in turn receive a 60% participating interest in the resulting joint venture or partnership. On the formation of the joint venture or partnership with WISCO, the Company will pay a fee of 10% of the additional WISCO cash contribution to an arm's length third party. The Company may, at its sole discretion, pay a portion of the fee in Common Shares.

Under the terms of the Framework Agreement, WISCO will use commercially reasonable efforts to assist the joint venture or partnership to obtain project financing for not less than 70% of the capital cost of the project as determined by a definitive feasibility study. The Framework Agreement provided that the parties had 60 days to settle and enter into a Definitive Agreement with respect to the Joint Venture, this being subsequently extended to June 30, 2011. Negotiations continue as to the precise structure of the joint venture or partnership.

**i) Lac Otelnuk Iron Ore Project, Nunavik, Québec**

On November 30, 2005, the Company entered into an option agreement (the "Lac Otelnuk Option") to earn a 100% interest in certain claims comprising part of the Lac Otelnuk Property. The Company has also staked additional mineral claims directly adjacent to and surrounding the claims subject to the Lac Otelnuk Option. Pursuant to the Lac Otelnuk Option, as amended, the optionor is entitled to a combination of cash, shares and work commitments, all of which have been fulfilled, and a royalty

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(the "Lac Otelnuik Royalty") equal to: (i) 2.5% from the sale of iron ore products mined from the claims subject to the Lac Otelnuik Option commencing in 2015 or earlier on commencement of commercial production with a minimum production royalty based on a certain specified pellet price and a minimum production of 10 million metric tonnes; and (ii) 2.5% net smelter returns from the sale of any other minerals mined from such properties annually. The Lac Otelnuik Royalty is subject to minimum advances of \$150,000 payable by November 30 of each year until commencement of commercial production. The Company has made all such necessary minimum payments to date. The Company may purchase one-half of the Lac Otelnuik Royalty for \$5.5 million at any time prior to December 31, 2015 and for \$11 million thereafter.

The Company filed an application with the Quebec Superior Court for a judicial interpretation of certain provisions of the Lac Otelnuik Option agreement. The clauses for which clarification was sought relate to the timing of the exercise of the option and certain aspects of the royalty payments. On August 19, 2011, the parties entered into a conditional settlement agreement. The litigation in the Quebec Superior Court was adjourned pending the satisfaction of the settlement's conditions.

**ii) December Lake Iron Ore Prospect, Nunavik, Québec, Canada**

The Company owns 159 mineral claims totalling approximately 74 square kilometres near December Lake which is 65 kilometres from the Lac Otelnuik Property and 230 kilometres north of Schefferville, in the Nunavik region of Northern Québec. The Company has identified over 20 kilometres of untested magnetic anomalies on this property and has access to certain non NI 43-101 compliant historical work completed on this property.

**iii) Bedford Iron Ore Prospect, Newfoundland and Labrador**

In June 2008, the Company entered into an option agreement to acquire a 100% interest in the Bedford Iron Ore Prospect, consisting of certain mineral claims in Labrador by, among other things, paying \$200,000 over the six-year option term, of which \$30,000 had been paid as of October 31, 2009. The agreement was terminated as of July 17, 2010 with no further payments and the Company wrote off incurred costs of \$200,183. Certain additional mineral claims directly adjacent to the Bedford Labrador mineral claims remained and were sold in April 2011 for cash proceeds of \$500,000 and 500,000 common shares of the purchaser, Cap-Ex Ventures Inc., with a then market value of \$720,000, resulting in a gain on disposal of \$1,185,252 being recognized in the quarter ended April 30, 2011.

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**6. CONVERTIBLE DEBENTURES**

|   | Three months ended<br>July 31, 2011 | Nine months ended<br>July 31, 2011 | Year ended<br>October 31, 2010 |
|---|-------------------------------------|------------------------------------|--------------------------------|
| Balance, beginning of period                        | \$ 7,808,339                        | \$ 8,952,341                       | \$ 8,248,928                   |
| Add: Accretion of liability component of debentures | 114,645                             | 432,194                            | 703,413                        |
| Less: Converted in period                           | (1,945,344)                         | (3,406,895)                        | -                              |
| Liability component of Convertible Debentures       | 5,977,640                           | 5,977,640                          | 8,952,341                      |
| Less: Current portion of liability                  | -                                   | -                                  | (3,273,373)                    |
| Balance, end of period                              | \$ 5,977,640                        | \$ 5,977,640                       | \$ 5,678,968                   |

On September 10, 2008, the Company issued \$10,000,000 of unsecured subordinated convertible debentures bearing interest at an annual rate of 7%. Of that amount, debentures with a face value of \$6,450,000 were issued to ArcelorMittal in connection with the Port Facility, and the balance was issued to other third parties. As a result of a subsequent agreement with ArcelorMittal, the Company has deferred payment of its annual interest payment of 7% on the convertible debenture held by ArcelorMittal for three years, along with a one-year deferral of repayment of the related principal, to September 10, 2012.

The debentures are convertible into Common Shares at a conversion price of \$0.99 per Common Share if converted prior to maturity. During the three month period ended July 31, 2011, a debenture with a face value of \$2,000,000 was converted, resulting in the issuance of 2,020,202 common shares. For the nine month period ended July 31, 2011, debentures with a face value of \$3,550,000 were converted, resulting in the issuance of 3,585,856 common shares.

Shares issued on the conversion of debentures are recorded at the accreted value of the underlying debenture together with its proportion of the amount previously recorded as the equity portion of convertible debentures, the resulting values recorded for such shares issued in the three and nine month periods ended July 31, 2011 being \$2,382,490 and \$4,186,129 respectively, these amounts including equity portions of \$441,404 and \$783,492 respectively.

The only remaining debenture is a debenture held by ArcelorMittal which matures on September 10, 2012. At July 31, 2011, there was \$nil current interest payable (October 31, 2010 – \$34,117). At July 31, 2011, interest payable of \$1,442,055 (October 31, 2010 – \$1,034,863), relating to this debenture, was accrued as non-current interest payable under long-term liabilities of the Company.

The debentures are recorded at amortized cost.

**7. FUTURE INCOME TAX LIABILITIES**

Future income tax liabilities are comprised of:

|  | July 31, 2011 | October 31, 2010 |
|--|---------------|------------------|
| Port Facility (Note 5a)  | \$ 7,736,833  | \$ 7,236,990     |
| Future income tax benefits on expenditures renounced to shareholders (Note 9b) | 1,566,100     | -                |
|  | \$ 9,302,933  | \$ 7,236,990     |

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**8. NON-CONTROLLING INTEREST**

|  | Three months ended<br>July 31, 2011 | Nine months ended<br>July 31, 2011 | Year ended<br>October 31, 2010 |
|--|-------------------------------------|------------------------------------|--------------------------------|
| Balance, beginning of period                                       | \$ 11,533,523                       | \$ 11,350,566                      | \$ 11,262,880                  |
| Non-controlling interest in cash contributions<br>to Port Facility | 234,000                             | 588,000                            | 423,956                        |
| Share of losses for period   | (105,996)                           | (277,039)                          | (336,270)                      |
| Balance, end of period   | \$ 11,661,527                       | \$ 11,661,527                      | \$ 11,350,566                  |

**9. SHARE CAPITAL**

a) Authorized

The Company is authorized to issue an unlimited number of Common Shares.

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b) Issued

The Company has the following Common Shares issued and outstanding:

|   | Shares                 | Amount                              |
|---|------------------------|-------------------------------------|
| <b>Common shares</b>  |                        |                                     |
| Balance, October 31, 2009   | 72,707,945             | \$ 75,296,033                       |
| Private placement of December 31, 2009<br>being flow-through common shares<br>less finders' fees and other issue costs  | 1,350,000              | 1,201,500<br>(110,634)              |
| Private placement of February 8, 2010<br>being flow-through common shares<br>less finders' fees and other issue costs   | 4,270,000              | 3,800,300<br>(272,643)              |
| Private placements of May 7, 2010<br>(i) net of warrants valued at \$530,552<br>(ii) being flow-through common shares<br>less commission, compensation options<br>and other issue costs | 5,000,000<br>4,255,320 | 1,469,448<br>2,000,000<br>(721,881) |
| Private placement of October 29, 2010<br>less finders' fees and other issue costs   | 5,405,404              | 2,000,000<br>(80,000)               |
| Shares issued on exercise of options<br>expenditures renounced to shareholders  | 100,001                | 48,189<br>(321,000)                 |
| <b>Balance, October 31, 2010</b>  | <b>93,088,670</b>      | <b>84,309,312</b>                   |
| Private placements of November 2010<br>less finders' fees and other issue costs   | 21,621,620             | 8,000,000<br>(491,384)              |
| Shares issued on exercise of options  | 738,830                | 828,397                             |
| Shares issued on exercise of warrants   | 102,187                | 72,780                              |
| Shares issued on debenture conversions  | 1,060,604              | 1,219,973                           |
| <b>Balance, January 31, 2011</b>  | <b>116,611,911</b>     | <b>93,939,078</b>                   |
| Private placement of March 23, 2011<br>less finders' fees and other issue costs   | 29,243,700             | 28,366,389<br>(2,223,282)           |
| Shares issued on exercise of options  | 355,425                | 234,265                             |
| Shares issued on exercise of warrants   | 237,087                | 207,805                             |
| Shares issued on debenture conversions  | 505,050                | 583,666                             |
| Future income tax benefits on<br>expenditures renounced to shareholders   |                        | (1,566,100)                         |
| <b>Balance, April 30, 2011</b>  | <b>146,953,173</b>     | <b>119,541,821</b>                  |
| Shares issued on exercise of compensation options   | 50,000                 | 20,000                              |
| Shares issued on debenture conversions  | 2,020,202              | 2,382,490                           |
| Shares issued on exercise of options  | 83,334                 | 107,072                             |
| <b>Balance, July 31, 2011</b>   | <b>149,106,709</b>     | <b>\$ 122,051,383</b>               |

The private placement that closed on December 31, 2009 was for gross proceeds of \$1,201,500, less finders' fees of \$60,075 and issue costs of \$50,559.

The private placement that closed on February 8, 2010 was for gross proceeds of \$3,800,300, less finders' fees of \$246,000 and issue costs of \$26,643.

The two private placements that closed on May 7, 2010 were for gross proceeds of \$4,000,000, less investor warrants valued at \$530,552, commission of \$280,000, compensation options valued at \$280,000 and other issue costs of \$161,881. These private placements were comprised of one of

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5,000,000 units (each consisting of one Common Share and one-half common share purchase warrant ("Warrant")) and the second of 4,255,320 flow-through Common Shares. Each whole Warrant issued entitles the holder thereof to acquire one Common Share at a price of \$0.50 per Common Share until May 7, 2012. The compensation options issued enable the underwriter to purchase 555,319 units (each consisting of one Common Share and one-half Warrant) at a unit price of \$0.40 per unit until May 7, 2012.

The private placement of October 2010 was for gross proceeds of \$10,000,000, the first tranche of which closed on October 29, 2010 and totalled \$2,000,000 less finders' fees of \$70,000 and issue costs of \$10,000. The second and third tranches of the private placement of October 2010 were received on November 11 and 18, 2010 for additional gross proceeds of \$8,000,000. These two tranches brought the total gross proceeds received pursuant to the private placement to \$10,000,000 and the total number of Common Shares issued pursuant to the private placement to 27,027,024. In connection with the private placement, the Company paid finders' fees in the aggregate amount of \$560,000.

Further to the Framework Agreement of January 12, 2011 with WISCO, the private placement contemplated thereunder closed on March 23, 2011 for gross proceeds of \$28,366,389, less finders' fees of \$1,985,647 and issue costs of \$237,635, with the issuance of 29,243,700 common shares representing 19.9% of the Company's issued and outstanding shares on a post-issuance basis.

Under the terms of WISCO's private placement of March 23, 2011 and the Framework Agreement of January 12, 2011, WISCO was granted certain rights including a pre-emptive right to subscribe for, at the same or equivalent cash subscription price, any equity securities that the Company proposes to issue, up to that number of offered securities as will enable WISCO, upon completion of the issuance, to maintain its then-current proportionate interest in the Company.

This pre-emptive right will terminate if (i) the closing of the proposed joint venture or partnership between WISCO and the Company is not completed under specified circumstances, and (ii) WISCO's ownership of common shares of the Company is reduced to less than 10% of the issued and outstanding common shares of the Company.

The Company financed a portion of its resource property exploration through the issuance of flow-through Common Shares whereby the Company transfers the tax deductions arising from the related resource expenditures to the investors. On the date the Company renounces the tax credits associated with the resource expenditures and the Company has reasonable assurance that the expenditures will be completed, a future income tax liability is recognized and share capital is reduced.

During the quarter ended April 30, 2011, as a result of the renunciation to investors of such exploration expenditures, the Company recorded a reduction in share capital of \$1,566,100 and a future income tax liability of \$1,566,100.

During the quarter ended July 31, 2011, the Company issued 2,153,536 Common Shares on the exercise of options and the conversion of a convertible debenture.

c) Options

Pursuant to the Company's stock option plan approved by the shareholders of the Company on April 28, 2011, options may be granted in respect of authorized and unissued shares provided that, the maximum aggregate number of shares reserved for issuance and which may be purchased upon the exercise of all options shall not exceed 10% of the issued and outstanding Common Shares. As of July 31, 2011, the maximum number of Common Shares which may be issued under the stock option plan is 14,910,670. The Company may grant options to a director, employee, consultant or consultant company. The exercise price per share shall be determined by the Company at the time the option is granted, but, in any event, shall not be less than the closing price of the shares on the

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TSX Venture Exchange on the trading day immediately preceding the date of the grant of the option, unless the grant of the option occurs during a blackout period, in which case the exercise price per share shall not be less than the closing price of the shares on the Exchange on the second trading day immediately following the expiry of the blackout period. Options granted pursuant to the plan shall vest and become exercisable by an optionee as to one third of the number of options vesting in six, twelve and eighteen months following the date of grant.

The continuity of options is as follows:

|   | Number of<br>options | Weighted average<br>exercise price |
|---|----------------------|------------------------------------|
| Balance, October 31, 2010                         | 7,978,334            | \$ 0.54                            |
| Granted   | 947,500              | 1.30                               |
| Exercised   | (700,000)            | 0.71                               |
| Cancelled/Forfeited                               | (415,000)            | 0.49                               |
| Expired   | (705,000)            | 1.10                               |
| Balance, January 31, 2011<br><i>(no activity)</i> | -                    | -                                  |
| Balance, April 30, 2011                           | 7,105,834            | 0.57                               |
| Granted   | 640,000              | 0.99                               |
| Exercised   | (83,334)             | 0.76                               |
| Expired   | (50,000)             | 1.10                               |
| Balance, July 31, 2011                            | 7,612,500            | \$ 0.60                            |

During the three months ended July 31, 2011, under the fair-value method, the amount of \$234,867 (2010 – \$252,501) in stock-based compensation costs was recorded for options granted to officers, employees and consultants. For the corresponding nine-month periods then ended, the amounts were \$670,308 and \$903,978 respectively.

The fair values of options granted during the three months ended July 31, 2011 were calculated using the Black-Scholes option pricing model with the following assumptions:

|  | 2011       |
|--|------------|
| Risk free interest rate                | 1.90%      |
| Expected dividend yield                | 0%         |
| Stock price volatility                 | 124.49%    |
| Expected life of options               | 3.25 years |
| Weighted average fair value of options | \$0.74     |

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As of July 31, 2011, the following options to purchase Common Shares were outstanding:

| Year<br>of Expiry | Number of<br>Options<br>Outstanding | Weighted<br>Average<br>Exercise Price | Weighted Average<br>Remaining<br>Contractual Life | Number of<br>Options<br>Exercisable | Weighted<br>Average<br>Exercise Price |
|-------------------|-------------------------------------|---------------------------------------|---|-------------------------------------|---------------------------------------|
| 2012              | 800,000                             | \$ 0.69                               | 0.555   | 800,000                             | \$ 0.69                               |
| 2013              | 275,000                             | 1.10                                  | 1.834   | 275,000                             | 1.10                                  |
| 2014              | 3,900,000                           | 0.35                                  | 2.941   | 3,900,000                           | 0.35                                  |
| 2015              | 1,050,000                           | 0.42                                  | 3.732   | 616,667                             | 0.43                                  |
| 2016              | 1,587,500                           | 0.18                                  | 4.665   | 315,333                             | 1.30                                  |
|                   | 7,612,500                           | \$ 0.60                               | 3.119   | 5,907,000                           | \$ 0.49                               |

d) Warrants and Compensation Options

The continuity of warrants is as follows:

|  | Exercise price | Number of<br>warrants | Amount     |
|--|----------------|-----------------------|------------|
| Balance, October 31, 2010  |                |                       |            |
| expiring May 7, 2012   | \$ 0.50        | 2,500,000             | \$ 530,552 |
| Exercised in the quarter   | 0.50           | (102,187)             | (21,686)   |
| Issued on exercise of compensation options<br>expiring May 7, 2012 | 0.50           | 19,415                | 9,670      |
| Balance, January 31, 2011  | 0.50           | 2,417,228             | 518,536    |
| Exercised in the quarter   | 0.50           | (237,088)             | (89,262)   |
| Issued on exercise of compensation options<br>expiring May 7, 2012 | 0.50           | 177,713               | 87,116     |
| Balance, April 30, 2011  | 0.50           | 2,357,853             | 516,390    |
| Issued on exercise of compensation options<br>expiring May 7, 2012 | 0.50           | 25,000                | 12,169     |
| Balance, July 31, 2011   | \$ 0.50        | 2,382,853             | \$ 528,559 |

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The continuity of compensation options is as follows:

|                           | Exercise price | Number of<br>Compensation Options |
|---------------------------|----------------|-----------------------------------|
| Balance, October 31, 2010 |                |                                   |
| expiring May 7, 2012      | \$ 0.40        | 555,319                           |
| Exercised in the quarter  | 0.40           | (38,830)                          |
| Balance, January 31, 2011 | 0.40           | 516,489                           |
| Exercised in the quarter  | 0.40           | (355,425)                         |
| Balance, April 30, 2011   | 0.40           | 161,064                           |
| Exercised in the quarter  | 0.40           | (50,000)                          |
| Balance, July 31, 2011    | \$ 0.40        | 111,064                           |

**10. CONTRIBUTED SURPLUS:**

|  | Three months ended<br>July 31, 2011 | Nine months ended<br>July 31, 2011 | Year ended<br>October 31, 2010 |
|--|-------------------------------------|------------------------------------|--------------------------------|
| Balance, beginning of period                         | \$ 4,601,409                        | \$ 4,667,714                       | \$ 3,273,206                   |
| Stock-based compensation for stock options           | 234,867                             | 670,308                            | 1,136,406                      |
| Stock-based compensation<br>for compensation options | -                                   | -                                  | 280,000                        |
| Exercise of stock and compensation options           | (55,907)                            | (557,653)                          | (21,898)                       |
| Balance, end of period                               | \$ 4,780,369                        | \$ 4,780,369                       | \$ 4,667,714                   |

**11. CAPITAL MANAGEMENT AND FINANCIAL INSTRUMENT-RELATED RISKS**

The Company's approach to capital management did not change during the period.

Certain financial assets and liabilities are measured at fair value and are classified using a fair value hierarchy that reflects the significance of the input used in making the measurements. The fair values of other receivables, accounts payable and accrued liabilities are considered by management of the Company to be a reasonable approximation of their carrying values due to their short term to maturity. There are three levels of fair value hierarchy that prioritize the inputs to valuation techniques used to measure fair value, with Level 1 inputs having the highest priority. The levels and the valuation techniques used to value the Company's financial assets and liabilities are described below:

Level 1 - Unadjusted quoted prices in active markets for identical assets or liabilities;

Level 2 - Inputs other than quoted prices that are observable for the asset or liability either directly or indirectly; and

Level 3 - Inputs that are not based on observable market data.

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The following table presents the classification of the Company's financial instruments within the fair value hierarchy as at July 31, 2011 and October 31, 2010:

|                           |               |         |         |               | July 31, 2011 |
|---------------------------|---------------|---------|---------|---------------|---------------|
|                           | Level 1       | Level 2 | Level 3 | Total         |               |
| Cash and cash equivalents | \$ 27,425,527 | \$ -    | \$ -    | \$ 27,425,527 |               |
| Marketable securities     | 305,000       | -       | -       | 305,000       |               |

  

|      |              |         |         |              | October 31, 2010 |
|------|--------------|---------|---------|--------------|------------------|
|      | Level 1      | Level 2 | Level 3 | Total        |                  |
| Cash | \$ 1,879,633 | \$ -    | \$ -    | \$ 1,879,633 |                  |

Cash equivalents are invested in 30-day term deposits or Banker's Acceptances.

**12. RELATED PARTY TRANSACTIONS**

Included in the periods, at their exchange amounts, are the following items paid or accrued to certain then-directors and companies controlled by certain then-directors of the Company for services provided. Exchange amounts are the amounts agreed upon by the transacting parties on terms and conditions similar to arm's-length transactions.

|                            | Nine months ended |               |
|----------------------------|-------------------|---------------|
|                            | July 31, 2011     | July 31, 2010 |
| Geological consulting fees | \$ -              | \$ 48,180     |

**13. COMMITMENTS AND CONTINGENCIES**

- a) The Company's annual commitments for rental agreements are as follows:

|      | Office leases |
|------|---------------|
| 2011 | \$ 106,300    |
| 2012 | 249,000       |
| 2013 | 258,600       |
| 2014 | 234,700       |
| 2015 | 176,100       |
| 2016 | 73,400        |

Included in the above lease commitments is the cost of the Company's 50% share of rental obligations for its former premises in Vancouver, now sublet to third parties at a future cash cost for the remaining lease term of approximately \$250,000. The fair value of this amount has been provided for. Should the former co-occupant fail to meet its share of rental obligations, the Company will be further committed under the terms of the head lease to additional net outlays representing their proportionate share of the loss from the date of default.

- b) Pursuant to the issuance of flow-through Common Shares in December 2009 and February and May 2010, the Company is committed to spending \$7,001,500 on qualified expenditures, of which \$1,201,500 was required to be spent by December 31, 2010, and the balance by December 31, 2011. Subsequent to July 31, 2011, the Company completed the expenditures of the entire required amount of \$7,001,500 on qualified expenditures.

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- c) In the ordinary course of business, the Company enters into contracts which contain indemnification provisions, including loan agreements, purchase contracts, service agreements, licensing agreements, asset purchase and sale agreements, joint venture agreements, operating agreements, leasing agreements and land use agreements. In such contracts, the Company may indemnify counterparties to the contracts if certain events occur. These indemnification provisions vary on an agreement-by-agreement basis. In some cases, there are no pre-determined amounts or limits included in the indemnification provisions and the occurrence of contingent events that will trigger payment under them is difficult to predict. Therefore, the maximum potential future amount that the Company could be required to pay cannot be estimated.
- d) The Company is committed to certain cash payments as described in Note 5b.
- e) In connection with the development of the Port Facility, the Company has made certain conditional commitments to the local municipality to pay for certain municipal improvements. As of July 31, 2011, the value of the contingent commitments approximated \$500,000. Settlement of the commitments is conditional on receipt by the Company of all necessary permits.
- f) The Company's Brazilian subsidiary is a defendant in certain legal actions in Brazil pursuant to which a third party is seeking the payment of approximately \$4,200,000 under a conditional agreement entered into by the Company in 2008 for the purchase of certain lands. The Company is vigorously defending itself including seeking the return of its initial payment of approximately \$1,000,000 and the annulment of the agreement on the basis of misrepresentations therein. Although the ultimate outcome of these actions cannot be ascertained at this time and the results of legal proceedings cannot be predicted with certainty, it is the opinion of management of the Company that these claims are without merit and the resolution of these matters will not have a material adverse effect on the financial position of the Company.

#### **14. NON-CASH TRANSACTIONS**

During the three and nine months ended July 31, 2011 and 2010, there were the following non-cash transactions:

|  | Three months ended |               | Nine months ended |               |
|--|--------------------|---------------|-------------------|---------------|
|  | July 31, 2011      | July 31, 2010 | July 31, 2011     | July 31, 2010 |
| Funding of non-controlling interest's share in the Port Facility                     | \$ 234,000         | \$ 11,352     | \$ 588,000        | \$ 291,956    |
| Value of warrants issued on exercise of compensation options                         | 12,169             | -             | 210,959           | -             |
| Future income taxes on renunciation to shareholders of certain tax deductions        | -                  | -             | 1,566,100         | 321,000       |
| Marketable securities received as part of proceeds of disposal of mineral properties | -                  | -             | 720,000           | -             |
| Issued for financing:  |                    |               |                   |               |
| Compensation options   | -                  | -             | -                 | 280,000       |
| Investor warrants  | -                  | -             | -                 | 411,250       |
| Conversion of debentures   | 1,945,344          | -             | 3,406,895         | -             |

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**15. SEGMENTED INFORMATION**

The Company has two reportable business segments: the exploration and development of mineral resource properties in Nunavik, Québec, Canada, and the development of an iron ore port facility in Brazil. The Company currently operates in two geographic segments. Geographic distribution of operating results in the geographic segments is as follows:

|  | As at, and for the nine months ended, July 31, 2011 |               |                |
|--|---|---------------|----------------|
|  | Brazil  | Canada        | Total          |
| Total assets                           | \$ 57,521,807                                       | \$ 47,160,096 | \$ 104,681,903 |
| Cash, cash equivalents and securities  | 296,266   | 27,434,261    | 27,730,527     |
| Capital assets                         | 56,925,549  | 18,622,396    | 75,547,945     |
| Net loss for the period                | 620,872   | 4,849,545     | 5,470,417      |
| Cash expenditures<br>on capital assets | 579,963   | 4,419,945     | 4,999,908      |

  

|  | As at, and for the nine months ended, July 31, 2010 |               |               |
|--|---|---------------|---------------|
|  | Brazil  | Canada        | Total         |
| Total assets                           | \$ 55,262,923                                       | \$ 16,444,858 | \$ 71,707,781 |
| Cash                                   | 31,431  | 2,493,851     | 2,525,282     |
| Capital assets                         | 55,015,354  | 12,948,019    | 67,963,373    |
| Net loss for the period                | 393,041   | 4,035,867     | 4,428,908     |
| Cash expenditures<br>on capital assets | 314,607   | 2,835,548     | 3,150,155     |

**16. SUBSEQUENT EVENT**

The Company filed an application with the Quebec Superior Court for a judicial interpretation of certain provisions of the Lac Otelnuk Option agreement. The clauses for which clarification was sought relate to the timing of the exercise of the option and certain aspects of the royalty payments. On August 19, 2011, the parties entered into a conditional settlement agreement. The litigation in the Quebec Superior Court was adjourned pending the satisfaction of the settlement's conditions.