

**DIADEM RESOURCES LTD.**  
**CONSOLIDATED FINANCIAL STATEMENTS**  
**(Unaudited)**  
**FEBRUARY 28, 2005**

**DIADEM RESOURCES LTD.**  
**CONSOLIDATED BALANCE SHEETS**  
(Unaudited)

(Expressed in Canadian Dollars)	February 28 2005	May 31 2004
	\$	\$
<b>ASSETS</b>		
<b>Current</b>		
Cash and term deposits	468,442	124,539
Marketable securities	-	36
Prepaid expenses and sundry receivables	67,153	94,009
	535,595	218,584
<b>Loan receivable</b> (Note 3)	-	62,947
<b>Mineral interests</b> (Note 4)	7,395,919	6,601,638
<b>Other investments</b> (Note 5)	20,000	20,000
<b>Equipment</b> (Note 6)	3,443	1,766
<b>Other assets</b>	238,534	44,728
	8,193,491	6,949,663
<b>LIABILITIES</b>		
<b>Current</b>		
Accounts payable and accrued liabilities	349,237	890,789
Convertible debenture (Note 7)	-	500,000
	349,237	1,390,789
<b>Long-term debt</b> (Note 8)	-	290,000
	349,237	1,680,789
<b>SHAREHOLDERS' EQUITY</b>		
<b>Capital stock</b> (Note 9)	30,291,060	26,890,189
<b>Warrants</b>	68,995	87,500
<b>Contributed surplus</b>	280,700	23,200
<b>Shares to be issued</b>	284,199	384,248
<b>(Deficit)</b>	(23,080,700)	(22,116,263)
	7,844,254	5,268,874
	8,193,491	6,949,663

See accompanying notes to the consolidated financial statements

**DIADEM RESOURCES LTD.**  
**CONSOLIDATED STATEMENTS OF OPERATIONS AND DEFICIT**

(Unaudited)

(Expressed in Canadian Dollars)	Three months ended February 28		Nine months ended February 28	
	2005	2004	2005	2004
	\$	\$	\$	\$
<b>REVENUE</b>				
Gain on sale of investment	23,022	-	22,894	125,000
Interest income	-	1,901	2,621	2,052
	23,022	1,901	25,515	127,052
<b>EXPENSES</b>				
Amortization	132	239	397	716
Interest	18,808	12,251	41,652	43,846
Financial consulting services	78,052	(26,078)	240,553	31,922
General corporate costs	94,933	183,625	347,018	401,485
Stock option benefit	-	-	257,500	-
Other	-	1,895	-	2,194
Foreign exchange (gain)	(90)	-	(273)	(332)
	191,835	171,932	886,847	479,831
<b>NET (LOSS) before taxes</b>	(168,813)	(170,031)	(861,332)	(352,779)
Recovery of future income taxes	286,664	361,150	286,664	361,150
<b>NET INCOME (LOSS) for the period</b>	117,851	191,119	(574,668)	8,371
Costs associated with issuance of capital stock	(380,081)	(434,485)	(389,769)	(464,485)
<b>(DEFICIT), beginning of period</b>	(22,818,470)	(18,576,407)	(22,116,263)	(18,363,659)
<b>(DEFICIT), end of period</b>	(23,080,700)	(18,819,773)	(23,080,700)	(18,819,773)
<b>Net income (loss) per share –basic</b>	0.001	0.003	(0.006)	0.000
<b>Net income (loss) per share-diluted</b>	0.001	0.003	(0.006)	0.000
<b>Weighted average number of shares-basic</b>	120,073,269	75,169,611	97,959,413	65,401,881
<b>Weighted average number of shares-diluted</b>	122,098,370	75,169,611	98,627,028	65,401,881

See accompanying notes to the consolidated financial statements

**DIADEM RESOURCES LTD.**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(Unaudited)

(Expressed in Canadian Dollars)	Three months ended February 28		Nine months ended February 28	
	2005	2004	2005	2004
	\$	\$	\$	\$
<b>CASH FLOWS PROVIDED BY (USED IN):</b>				
<b>OPERATING ACTIVITIES</b>				
Net income (loss) for the period	117,851	191,119	(574,668)	8,371
Adjustment for items not affecting cash:				
Amortization	132	239	397	716
Stock option benefit	-	-	257,500	-
Warrants issued for financial consulting services	-	-	62,500	-
Gain on sale of investment	(22,929)	-	(22,929)	(125,000)
Interest paid through issuance of shares	-	7,456	12,123	7,456
Issuance of shares to settle costs associated with debt financing	-	-	-	58,000
Recovery of future income taxes	(286,664)	(361,150)	(286,664)	(361,150)
	(191,610)	(162,336)	(551,741)	(411,607)
Net changes in non-cash working capital balances:				
Prepaid expenses and sundry receivables	(64,345)	(42,778)	26,856	(42,547)
Marketable securities	-	224	36	224
Accounts payable and accrued liabilities	(124,593)	(74,108)	(541,553)	225,026
Cash flows provided by (used in) operating activities	(380,548)	(278,998)	(1,066,402)	(228,904)
<b>INVESTING ACTIVITIES</b>				
Loan receivable	66,352	12,305	62,947	(277,695)
Equipment	-	-	(2,074)	-
Proceeds from sale of investment	22,929	100,000	22,929	125,000
Mineral interests	(650,424)	(186,854)	(794,281)	(710,291)
Exploration deposits	(193,806)	-	(193,806)	-
Cash flows (used in) investing activities	(754,949)	(74,549)	(904,285)	(862,986)
<b>FINANCING ACTIVITIES</b>				
Common shares issued for cash	1,133,200	895,950	3,201,200	1,395,950
Increase (decrease) in long-term debt	-	-	(290,000)	290,000
(Decrease) in convertible debenture	-	-	(500,000)	-
Costs associated with issuance of capital stock	(86,922)	(133,334)	(96,610)	(133,334)
	1,046,278	762,616	2,314,590	1,552,616
Change in cash during the period	(89,219)	409,069	343,903	460,726
<b>CASH, beginning of period</b>	557,661	55,477	124,539	3,820
<b>CASH, end of period</b>	468,442	464,546	468,442	464,546

**SUPPLEMENTAL INFORMATION** (Note 12)

**DIADEM RESOURCES LTD.**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**  
**FEBRUARY 28, 2005**  
(Unaudited)

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**1. GOING CONCERN**

The consolidated financial statements are prepared in accordance with Canadian generally accepted accounting principles and on the assumption that Diadem Resources Ltd. (the "Company" or "Diadem") will be able to realize the carrying value of its assets and discharge its liabilities in the normal course of operations as a going concern.

There is uncertainty about the Company's ability to realize the carrying value of its assets and discharge its liabilities as they come due. The ability of the Company to continue as a going concern is dependent upon, among other things, being able to obtain additional financing and maintain positive cash flows from operations. During October and November 2004, the Company issued 34,133,331 common shares for gross cash proceeds aggregating \$2,068,000. During December, 2004, the Company issued 7,554,670 flow-through units for proceeds of \$1,133,200 consisting of one flow-through common share and one-half of one flow-through purchase warrant. Each whole warrant entitles the holder to purchase one flow-through common share at a price of \$0.20 per share for a period of nine months following closing of the private placement. There is no assurance the Company can continue to finance its operations through the capital markets.

For the nine months ended February 28, 2005, the Company recorded a loss of \$574,668 compared to net income of \$8,371 during the corresponding period of 2004 and had negative operating cash flow for the nine months ended February 28, 2005. At February 28, 2005, the Company has working capital of \$186,358 and an accumulated deficit of \$23,080,700.

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

These interim unaudited consolidated financial statements include all adjustments that are, in the opinion of management, necessary for fair presentation. The results of operations for the three and nine months ended February 28, 2005 are not necessarily indicative of the results expected for the full year. The Company is in the process of acquiring, exploring and developing its mineral interests in North America and is thus considered to be a development stage company.

These interim consolidated financial statements are prepared in accordance with Canadian generally accepted accounting principles for the preparation of interim financial information and follow the same accounting policies and methods set forth in the Company's audited consolidated financial statements as at and for the year ending May 31, 2004 and should be read in conjunction with those audited financial statements and notes thereto. These interim financial statements have not been reviewed by the Company's auditors.

**3. LOAN RECEIVABLE**

Effective March 15, 2005, Diadem restructured the terms of its option and joint venture agreement with Darnley Bay Resources Ltd. Consequently, Diadem and Darnley Bay Resources Ltd. ("Darnley Bay") renounced amounts owing to each other. (See Note 4(a)).

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**4. MINERAL INTERESTS**

	February 28, 2005	May 31, 2004
	\$	\$
<i>Acquisition costs</i>		
Franklin Diamond Project, Northwest Territories	632,808	633,873
Attawapiskat Diamond Project, Ontario	15,000	-
Otish Diamond Project, Quebec	395,203	395,203
	<u>1,043,011</u>	<u>1,029,076</u>
<i>Deferred exploration costs</i>		
Franklin Diamond Project, Northwest Territories	958,694	617,085
Attawapiskat Diamond Project, Ontario	269,156	-
Otish Diamond Project, Quebec	803,885	655,332
Leek Springs Diamond Project, California	4,321,173	4,300,145
	<u>6,352,908</u>	<u>5,572,562</u>
	<u>7,395,919</u>	<u>6,601,638</u>

**(a) Franklin Diamond Project, Northwest Territories**

Effective November 26, 2003, the Company entered into an agreement to form a joint venture ("Franklin Diamond Project") with DBR for diamond exploration in an area near Paulatuk in the Northwest Territories.

Under the joint venture, Diadem was to expend \$5 million on diamond exploration north of the 68<sup>th</sup> parallel during the period to December 31, 2006. When that level of expenditure is completed, Diadem will be entitled to select up to 2.5 million acres of the project area for further exploration, and Diadem will have earned an undivided 50% participating interest in the selected lands, with DBR holding the other 50%. The Inuvialuit Development Corporation has the right to back into the Franklin Diamond Project for a 10% working interest (with dilution to be shared equally by Diadem and DBR) when a decision is made to place a diamond mine into production and a positive feasibility study is completed.

Effective March 15, 2005, Diadem's earn-in requirement on the lands north of the 68<sup>th</sup> parallel has been reduced to approximately \$3,100,000 and the earn-in period has been extended to December 31, 2007. Darnley Bay has relinquished its participating interest in the joint venture lands south of the 68<sup>th</sup> parallel and transferred to Diadem 100% ownership in the permits and claims south of the 68<sup>th</sup> parallel.

In addition, the terms of the Diamond Cooperation Agreement between the Inuvialuit Regional Corporation and Diadem and Darnley Bay have been amended and the \$2,000,000 exploration expenditure requirement by June 30, 2005 has been extended to September 30, 2005. With respect to the aforementioned Diamond Cooperation Agreement approximately \$953,000 has been spent on lands north of the 68<sup>th</sup> parallel.

**(b) Attawapiskat Diamond Project**

During December 2004, the Company paid \$15,000 to enter into an option agreement to acquire a 51% interest in the entire Attawapiskat diamond property of Vault Minerals Inc. The property consists of 219 contiguous claims (3,403 claim units) covering over 53,000 hectares located in the James Bay Lowlands area of Northern Ontario. Through February 28, 2005, Diadem had incurred \$269,156 on exploration of this property.

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During December 2004, the Company made the decision to proceed with phased exploration of the property. Diadem is required to expend at least \$500,000 by December 1, 2005 (of which \$300,000 was committed to be spent by April 1, 2005, which was done) on exploration and related costs with a further \$500,000 to be expended after that date and by December 1, 2006. If Diadem exercises its option on or before December 1, 2006, a 51/49 joint venture will be formed and Diadem will be the operator.

**(c) Otish Mountains, Quebec**

Effective August 27, 2003, the Company formed a wholly-owned subsidiary, Diadem Explorations Inc. ("DEI"), to implement agreements entered into by the Company on July 24, 2003 with several companies to acquire mining claims in the Otish Mountains region of Quebec. The acquisition of the claims was effected by issuing 384,248 Series B First Preference Shares of DEI having a value equal to the staking costs and cost of work carried out on the claims by the vendors.

The Series B First Preferred Shares are exchangeable, at any time after December 31, 2004 and up to December 31, 2006, into 3,256,338 Common Shares of the Company at the option of either the Company or the vendor based on a weighted average trading price of \$0.118 per share during the three month period ended December 31, 2004. During January and February 2005, three vendors exchanged 100,049 Series B First Preference Shares for 847,875 common shares of the Company.

**(d) Leek Springs, California**

The Company currently has a 43.8% vested interest in and held, until December 31, 2004, an option to acquire up to a 57.9% interest in 125 unpatented mining claims covering approximately 2,500 acres in the Leek Springs area of Eldorado County, California. This option was granted by the Silverstone Prospecting Syndicate ("SPS") which holds the remaining interest in the mining claims.

The Company is in discussions with SPS to restructure ownership of the project.

**5. OTHER INVESTMENTS**

At February 28, 2005, Diadem owned 4.0 units (May 31, 2004 - 4.0 units) representing 6.4% (May 31, 2004 - 6.4%) of the outstanding units of the Silverstone Prospecting Syndicate which are valued at \$20,000.

**6. EQUIPMENT**

Equipment, at each of the dates indicated is comprised as follows:

	February 28, 2005		May 31, 2004	
	Cost	Accumulated amortization	Net	Net
	\$	\$	\$	\$
Computer and office equipment	7,321	3,878	3,443	1,766
	7,321	3,878	3,443	1,766

**7. OTHER ASSETS**

Other assets, as at the dates indicated, are comprised as follows:

	February 28 2005	May 31 2004
	\$	\$
Investment in Belitung Limited	21	21
Exploration deposit	238,513	44,707
	238,534	44,728

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**8. CONVERTIBLE DEBENTURE**

The debenture was convertible in whole or in part at the option of the holder into common shares at any time on or before June 2, 2004 at a conversion price of \$0.10 per share. The debenture bore simple interest payable at the annual rate of 9.75%, payable monthly in cash or, at the option of the Company, in Common Shares valued at the greater of \$0.10 and the 10-trading day weighted average price of the common shares immediately prior to the payment date. The debenture matured on June 2, 2004 and the debenture holder made demand for payment.

Effective October 22, 2004, the debenture plus accrued interest was paid in full.

Included in interest expense is \$13,839 (2004-\$12,288) incurred in respect of the convertible debenture. On October 22, 2004, the Company paid the debenture holder \$61,314 to settle interest accrued on the debenture.

**9. LONG-TERM DEBT**

Long-term debt was incurred to fund a security deposit lodged in support of assessment work to be conducted on the Franklin Diamond Project in the Northwest Territories. The lender had a first security interest in all of the assets of Diadem including its joint venture with DBR. The loan bore simple interest, at 10% per annum, which was payable monthly in Diadem treasury common shares valued at \$0.10 per share. The loan which had no maturity date was repaid on October 22, 2004. During the nine month period ended February 28, 2005, 121,229 Common Shares with a fair value of \$12,123 were issued as payment of interest.

**10. SHAREHOLDERS' EQUITY**

**(a) Capital Stock**

Authorized capital stock of the Company consists of an unlimited number of special shares, redeemable and retractable at paid-up value and an unlimited number of common shares.

**(b) Issued and outstanding shares**

Details of issued and outstanding common shares are as follows:

	<u>Common shares</u>	
	<u>Number</u>	<u>Amount</u>
	#	\$
<b>Balance, May 31, 2004</b>	80,063,497	26,890,189
Interest paid	121,229	12,123
Exercise of warrants	500,000	102,500
Expiry of warrants	-	35,000
Private placement	33,333,331	2,000,000
Flow-through shares	7,554,670	1,133,200
Conversion of Series B First Preference Shares	847,875	100,048
Financial fee	300,000	18,000
<b>Balance, February 28, 2005</b>	<b>122,720,602</b>	<b>30,291,060</b>

**(c) Private placement**

Effective October 22, 2004, the Company completed a private placement of 33,333,331 Units at \$0.06 per Unit, for gross proceeds of \$2,000,000. Each Unit consists of one Common Share and one Common Share Purchase Warrant. Each whole Common Share Purchase Warrant entitles the holder to purchase one additional Common Share up to October 22, 2006 at a price of \$0.10.

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**(d) Financial advisory services**

Warrants to acquire 2,500,000 Common Shares, at a price of \$0.10 per share, for a period of two years from October 22, 2004 were issued as partial compensation for financial advisory services. In addition, 300,000 common shares were issued as partial compensation for financial advisory services.

**(e) Flow-through Financing**

During December 2004, the Company placed 7,554,670 Units at a price of \$0.15 per Unit for gross proceeds of \$1,133,200. Each Unit consisted of one flow-through common share and one-half of one flow-through common share purchase warrant. Each warrant entitles the holder to purchase one additional flow-through common share at a price of \$0.20 per share for a period of nine months after the closing of the private placement. A total of \$46,396 in cash commissions was paid and 309,307 non flow-through broker warrants were issued, exercisable for a period of nine months from the date of closing.

**(f) Stock Option Plan**

The Company has a stock option plan. At the annual general meeting of shareholders held November 30, 2004, the shareholders approved an increase in the aggregate number of common shares reserved for issuance under the stock option plan to 15,000,000 of which an aggregate of 9,600,000 are subject to options granted pursuant to the plan. The options are non-assignable and may be granted for a term not exceeding five years. The exercise price is fixed by the board of directors of the Company at the time of grant, subject to all applicable regulatory requirements.

On March 20, 2005, 50,000 options, exercisable at \$0.25 per share, expired without being exercised. On October 18, 2004, the board of directors granted options to purchase 1,750,000 common shares, exercisable at \$0.105 per share over five year terms. On November 1, 2004, the board of directors granted options to purchase 2,500,000 common shares at an exercise price of \$0.10 per share and cancelled options to acquire 2,060,000 common shares at a weighted average exercise price of \$0.12 per share.

Details of issued and outstanding stock options to acquire common shares are as follows:

	<b>Number of options #</b>	<b>Weighted average exercise price \$</b>
Balance, May 31, 2004	7,410,000	0.112
Options granted	4,250,000	0.102
Options cancelled	(2,060,000)	0.118
Balance, February 28, 2005	9,600,000	0.106

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The following is a summary of the common shares that are subject to options outstanding at February 28, 2005:

Expiry date	Common shares	Exercise price
	#	\$
March 20, 2005	50,000	0.112
April 30, 2005	400,000	0.200
December 31, 2005	1,300,000	0.100
February 20, 2008	750,000	0.100
February 21, 2008	250,000	0.100
May 28, 2008	3,400,000	0.100
October 8, 2008	350,000	0.115
October 8, 2008	500,000	0.110
November 20, 2008	100,000	0.100
October 18, 2009	1,750,000	0.105
November 1, 2009	750,000	0.100
	9,600,000	0.107

**(g) Stock-based compensation**

The fair value of each stock option grant is estimated on the date of the grant using the Black-Scholes option-pricing model with the following weighted average assumptions used for grants in the periods indicated: expected dividend yield of 0%, expected stock volatility of 100%, risk free interest rate of 4.5% to 5.0% and an expected option life of 60 months.

Valuation of options granted during the nine months resulted in a charge to operations aggregating \$257,500.

The fair value of warrants issued as partial compensation for financial advisory services and broker compensation is estimated on the date of the issue using the Black-Scholes option-pricing model with the following weighted average assumptions used for the issue: expected dividend yield of 0%, expected stock volatility of 100%, risk free interest rate of 4.5% to 5% and an expected warrant life of 9 months to 2 years.

Valuation of broker warrants issued during the nine months resulted in a charge to operations aggregating \$6,495. Valuation of warrants issued during the nine months in respect of financial advisory services resulted in a charge to operations aggregating \$62,500.

**(h) Warrants**

Details of issued and outstanding warrants to acquire common shares are as follows:

	Number of warrants	Weighted average exercise price
	#	\$
Balance, May 31, 2004	4,504,750	0.104
Warrants exercised	(500,000)	0.100
Warrants expired	(3,350,000)	0.100
Warrants issued	39,919,978	0.110
Balance, February 28, 2005	40,574,728	0.111

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Effective December 31, 2004 and pursuant to the relevant subscription agreement, 654,750 warrants entitling the holders to purchase 654,750 common shares until December 31, 2005 were re-priced from \$0.13 per common share to \$0.17 per common share.

The following is a summary of the common shares that are subject to warrants outstanding at February 28, 2005:

<b>Expiry date</b>	<b>Common shares #</b>	<b>Exercise price \$</b>
September 22, 2005	3,709,681	0.200
September 30, 2005	376,966	0.200
December 31, 2005	654,750	0.170
October 22, 2006	35,833,331	0.100
	<b>40,574,728</b>	<b>0.111</b>

**11. RELATED PARTY INFORMATION**

Included in accounts payable and accrued liabilities is \$7,617 (May 31, 2004-\$137,667) due to three directors for administrative services rendered to and expenses paid on behalf of the Company. Cost of services rendered, during the nine month period, to the Company was \$149,337 (2004-\$131,167) during the relevant periods of service as directors. A company controlled by one director was paid \$80,000 for financial advisory services during the period. These related party transactions are in the normal course of business and are measured at the exchange amount which is the amount of consideration established and agreed to by the related parties.

**12. SUPPLEMENTARY CASH FLOW INFORMATION**

The Company did not pay any income taxes during the respective periods of 2005 and 2004. During the nine month period ended February 28, 2005, the Company issued 121,229 common shares to settle \$12,123 of interest cost.

During the nine month period ended February 28, 2005, the Company recorded non-cash compensation aggregating \$257,500 as a consequence of the issue of stock options to the directors and officers of the Company as described in Notes 10(f) and 10(g).

The Company charged \$62,500 to operations as a consequence of valuing the issuance of 2,500,000 warrants as described in Notes 10(d) and 10(g) and broker warrants as described in Notes 10(e) and 10(g).