

**DIADEM RESOURCES LTD.**

**(A Development Stage Company)**

**CONSOLIDATED FINANCIAL STATEMENTS  
(Unaudited)**

**FEBRUARY 28, 2006**

**DIADEM RESOURCES LTD.**  
(A Development Stage Company)  
**CONSOLIDATED BALANCE SHEETS**  
(Unaudited)

(Expressed in Canadian Dollars)	February 28 2006	May 31 2005
	\$	\$
<b>ASSETS</b>		
<b>Current</b>		
Cash and term deposits	385,414	1,455,535
Subscription receivable	-	10,000
Prepaid expenses and sundry receivables	12,786	44,351
	398,200	1,509,886
<b>Mineral interests</b> (Note 3)	2,773,129	2,345,930
<b>Equipment</b> (Note 4)	7,406	9,762
<b>Other assets</b> (Note 5)	238,534	238,534
	3,417,269	4,104,112
<b>LIABILITIES</b>		
<b>Current</b>		
Accounts payable and accrued liabilities	385,778	422,647
	385,778	422,647
<b>SHAREHOLDERS' EQUITY</b>		
<b>Capital stock</b> (Note 9)	31,073,972	30,844,248
<b>Warrants</b>	1,010,087	1,010,087
<b>Contributed surplus</b>	639,669	502,782
<b>Shares to be issued</b>	54,475	284,199
<b>(Deficit)</b>	(29,746,712)	(28,959,851)
	3,031,491	3,681,465
	3,417,269	4,104,112

**DIADEM RESOURCES LTD.**

(A Development Stage Company)

**CONSOLIDATED STATEMENTS OF OPERATIONS AND DEFICIT**

(Unaudited)

(Expressed in Canadian Dollars)	Three months ended February 28		Nine months ended February 28	
	2006	2005	2006	2005
	\$	\$	\$	\$
<b>REVENUE</b>				
Gain on sale of investment	62,825	23,022	73,300	22,894
Interest income and other income	3,267	-	11,065	2,621
	66,092	23,022	84,365	25,515
<b>EXPENSES</b>				
Amortization	717	132	2,181	397
Interest	2,076	18,808	6,379	41,652
Financial consulting services	-	78,052	-	240,553
General corporate costs	128,989	94,933	373,817	347,018
Stock-based compensation	37,194	-	136,887	257,500
Write-down of mineral interests (Note 3(b))	-	-	352,134	-
Foreign exchange (gain)	(119)	(90)	(172)	(273)
	168,857	191,835	871,226	886,847
<b>NET (LOSS) before taxes</b>	(102,765)	(168,813)	(786,861)	(861,332)
Income tax recovery (Note 9)	543,245	286,664	543,245	286,664
<b>NET INCOME (LOSS) for the period</b>	440,480	117,851	(243,616)	(574,668)
Costs associated with issuance of capital stock	(543,245)	(380,081)	(543,245)	(389,769)
<b>DEFICIT, beginning of period</b>	(29,643,947)	(22,818,470)	(28,959,851)	(22,116,263)
<b>DEFICIT, end of period</b>	(29,746,712)	(23,080,700)	(29,746,712)	(23,080,700)
<b>Net income (loss) per share –basic and diluted</b>	0.045	0.025	(0.025)	(0.140)
<b>Weighted average number of shares</b>	9,700,435	4,698,100	9,700,435	4,087,617

See accompanying notes to the consolidated financial statements

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

(Expressed in Canadian Dollars)	Three months ended February 28		Nine months ended February 28	
	2006	2005	2006	2005
	\$	\$	\$	\$
<b>CASH FLOWS PROVIDED BY (USED IN):</b>				
<b>OPERATING ACTIVITIES</b>				
Net income (loss) for the period	440,480	117,851	(243,616)	(574,668)
Adjustment for items not affecting cash:				
Amortization	717	132	2,181	397
Stock-based compensation	37,194	-	136,887	257,500
Warrants issued for financial consulting services	-	-	-	62,500
Gain on sale of investment	(62,825)	(22,929)	(73,300)	(22,929)
Loss on disposal of equipment	175	-	175	-
Interest paid through issuance of shares	-	-	-	12,123
Write-down of mineral interests	-	-	352,134	-
Recovery of future income taxes	(543,245)	(286,664)	(543,245)	(286,664)
	(127,504)	(191,610)	(368,784)	(551,741)
Net changes in non-cash working capital balances:				
Prepaid expenses and sundry receivables	17,236	(64,345)	31,565	26,856
Marketable securities	-	-	-	36
Accounts payable and accrued liabilities	(41,649)	(124,593)	(86,869)	(541,553)
Cash flows provided by (used in) operating activities	(151,917)	(380,548)	(424,088)	(1,066,402)
<b>INVESTING ACTIVITIES</b>				
Loan receivable	-	66,352	-	62,947
Equipment	-	-	-	(2,074)
Proceeds from sale of investment	62,825	22,929	73,300	22,929
Mineral interests	(38,299)	(650,424)	(729,333)	(794,281)
Exploration deposits	-	(193,806)	-	(193,806)
Cash flows (used in) investing activities	24,526	(754,949)	(656,033)	(904,285)
<b>FINANCING ACTIVITIES</b>				
Common shares issued for cash	-	1,133,200	10,000	3,201,200
Increase (decrease) in long-term debt	-	-	-	(290,000)
(Decrease) in convertible debenture	-	-	-	(500,000)
Costs associated with issuance of capital stock	-	(86,922)	-	(96,610)
	-	1,046,278	10,000	2,314,590
Change in cash during the period	(127,391)	(89,219)	(1,070,121)	343,903
<b>CASH, beginning of period</b>	512,805	557,661	1,455,535	124,539
<b>CASH, end of period</b>	385,414	468,442	385,414	468,442

**SUPPLEMENTAL INFORMATION (Note 8)**

See accompanying notes to the consolidated financial statements

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**1. NATURE OF OPERATIONS AND GOING CONCERN**

Diadem Resources Ltd. (the "Company" or "Diadem") is in the process of acquiring, exploring and developing its mineral interests in Canada and Mali and is thus considered to be a development stage company. The business of mining and exploring for minerals involves a high degree of risk and there can be no assurance that current exploration programs will result in profitable mining operations.

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. There is no assurance the Company can continue to finance its operations through the capital markets.

For the nine months ended February 28, 2006, the Company recorded a loss of \$243,616 (2005 - \$574,668) and had negative operating cash flow. At February 28, 2006, the Company had working capital of \$12,422 and an accumulated deficit of \$29.7 million.

**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 month periods ended February, 2006 are not necessarily indicative of the results expected for the full year.

These interim unaudited consolidated financial statements are prepared in accordance with Canadian generally accepted accounting principles 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, 2005 and should be read in conjunction with those audited financial statements and notes thereto.

**3. MINERAL INTERESTS**

	February 28, 2006 \$	May 31, 2005 \$
<i>Acquisition costs</i>		
Franklin Project, Northwest Territories	1,190,764	1,190,764
Attawapiskat Project, Ontario	-	15,000
Tinkeleni, Mali	13,636	-
Diokeba, Mali	-	-
	<u>1,204,400</u>	<u>1,205,764</u>
<i>Deferred exploration costs</i>		
Franklin Diamond Project, Northwest Territories	1,249,538	513,068
Attawapiskat Project, Ontario	-	327,098
Otish Mountains Project, Quebec	300,000	300,000
Tinkeleni, Mali	18,526	-
Diokeba, Mali	665	-
	<u>1,568,729</u>	<u>1,140,166</u>
<i>Total mineral interests</i>	<u>2,773,129</u>	<u>2,345,930</u>

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

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

The transaction results from an acquisition from Carnarvon Capital Corporation ("CCC") of that company's right to enter into the joint venture. To acquire the rights to form the joint venture, Diadem issued to CCC six million Diadem treasury shares, valued at \$600,000. Paul Carroll,

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President and CEO of Diadem at the time of the transaction, also is President of CCC and all of its share capital is owned by members of his immediate family. As part of the transfer to Diadem of the transaction with DBR, CCC and Mr. Carroll have agreed that during the period ending December 31, 2008 neither CCC nor Mr. Carroll would acquire a controlling interest in any diamond exploration or development project in Canada or California other than through Diadem or with the consent of Diadem. 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 this earning level of expenditure is completed, Diadem will be entitled to select up to 2.5 million acres of the project area for further exploration (the "Selected Lands"), 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 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.

The parties will allocate a portion of the earn-in amount to the Selected Lands. Diadem will be entitled to convert the balance of the earn-in amount not allocated to the Selected Lands into treasury common shares of DBR at the then market price, subject to regulatory approval, or to convert that amount (in increments of at least \$1 million) into a diamond royalty equal to 1% for each full \$1 million spent and not allocated to the Selected Lands, with the balance to be taken in DBR shares. DBR will have the right to purchase any such royalty for \$1.5 million for each 1% of the royalty if the purchase is made within 90 days of completion of a bankable feasibility study, or thereafter for \$2.5 million if the purchase is within 90 days of the start of commercial production.

If a decision is made to carry out a feasibility study on the lands selected by Diadem, it will have the right to fund the feasibility study, and if the property is placed into commercial production Diadem's interest will increase to 75% and DBR's interest will decrease to 25%.

Effective March 15, 2005, Diadem's earn-in requirement on the lands north of the 68<sup>th</sup> parallel was reduced to approximately \$3,100,000 and the earn-in period was extended to December 31, 2007. DBR 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.

The joint venture entered into a letter agreement with the Inuvialuit Regional Corporation ("IRC") under which the Company and DBR will enter into a Cooperation and Benefits Agreement with the Inuvialuit. This agreement covers an area in the Inuvialuit Settlement Region around Paulatuk of about 57,000 square kilometres (excluding the area around Paulatuk in which the Inuvialuit own the mineral rights and excluding the Tuktu Nogait National Park). The agreement is for 5 years from January 1, 2004 with provisions for renewal and termination consistent with the joint venture's mining rights in the area. The joint venture will be granted access to the Inuvialuit lands to conduct exploration, development and extraction operations for rough diamonds.

The joint venture will be required to obtain all necessary Inuvialuit permits and approvals, and will pay the fees and charges under the Inuvialuit Rules with a minimum amount payable each year of \$50,000. The joint venture was to incur at least \$2 million of work by June 30, 2005. On March 1, 2005 the Inuvialuit extended the date from June 30, 2005 to September 30, 2005. Subsequently, inclement weather and other operational issues impeded survey progress, consequently, expenditures through February 2006 were in excess of \$1.7 million.

The Inuvialuit will receive a 2% diamond royalty on mining rights exploited by the joint venture. (The Inuvialuit can hold certain claims in the area in which there is a 15-year deferral of Crown royalties. In such cases the Inuvialuit will receive an additional 4% royalty while the deferral applies.) If the joint venture completes a positive feasibility, the Inuvialuit have the right to acquire up to a 10% participating interest by paying the corresponding percentage of the cost of the feasibility study. Approximately \$1,000,000 has been spent on lands north of the 68<sup>th</sup> parallel as at May 31, 2005.

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**(b) Attawapiskat Project, Ontario**

During December 2004, the Company paid \$15,000 to enter into an option agreement to acquire a 51% interest in the entire Attawapiskat property of Vault Minerals Inc. During the nine months ended February 28, 2005, the Company paid a further \$10,000 to maintain the option agreement and incurred \$352,134 of qualified expenditures on this property, excluding the management fee.

During December 2005, the Company elected not to proceed further with the Attawapiskat property and allowed the option to lapse and wrote-down the carrying value of deferred exploration and acquisition costs associated with the project.

**(c) Tinkeleni Project, Mali**

Effective November 23, 2005, Diadem entered into a partnership agreement with La Société African Minerals Exploration SARL ("Amex") on the Amex's Tinkeleni gold property in Mali, West Africa. The partnership agreement required Diadem to pay Amex FCFA 4,000,000 for the right to conduct due diligence for a 150-day period (which expired April 22, 2006) following which the parties would enter into a formal option agreement. The payment was settled through the payment of CAD 8,636.

The option agreement that would be entered into contemplates a four year period during which the following payments (expressed in United States dollars) would be made:

(i)	Upon entering into the option agreement	25,000
(ii)	On the first anniversary	55,000
(iii)	On the second anniversary	60,000
(iv)	On the third anniversary	70,000
(v)	On or before the fourth anniversary	<u>160,000</u>
		<u>370,000</u>

The option agreement has not yet been entered into. Upon completion of the option payments, Diadem would own a 100% interest in the Tinkeleni property, subject to a 2% net smelter royalty ("NSR") in favour of Amex. The NSR may be acquired by Diadem, at any time, for US\$2,000,000.

**(d) Diokeba, Dalakan and Sinzeni Projects, Mali**

Effective December 1, 2005, Diadem signed letter agreements with North Atlantic Resources Ltd. ("NAC") to enter into an option and joint venture agreement whereby Diadem would explore NAC's 100%-owned Diokeba, Dalakan and Sinzeni gold properties in Mali, West Africa.

In order to earn a 60% interest in each of the properties Diadem must incur the following expenditures, expressed in Canadian dollars:

	Diokeba property \$	Dalakan property \$	Sinzeni property \$
Exploration and development expenditures required			
First year	250,000	250,000	125,000
Second year	250,000	250,000	125,000
Third year	500,000	500,000	250,000
Fifth year	1,000,000	1,000,000	500,000

To maintain each of the options, Diadem issued 7,812 common shares on March 27, 2006. On each of the next four anniversary dates, Diadem must issue 3,125 common shares in respect of each of the Diokeba and Dalakan properties, 25,000 common shares in aggregate. In respect of the Sinzeni property, Diadem must issue 1,564 common shares on each of the next four anniversary dates, 6,250 common shares in aggregate.

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Upon earning its 60% interest in each of the properties, Diadem can elect to be operator of the respective property.

**4. EQUIPMENT**

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

	February 28, 2006		May 31, 2005	
	Cost	Accumulated amortization	Net	Net
	\$	\$	\$	\$
Computer and office equipment	13,414	6,008	7,406	9,762
	13,414	6,008	7,406	9,762

**5. OTHER ASSETS**

Other assets at each of the dates indicated are comprised as follows:

	February 28, 2006	May 31, 2005
	\$	\$
Investment in Belitung Limited	21	21
Exploration deposits	238,513	238,513
	238,534	238,534

**6. 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:

	Common shares	
	Number #	Amount \$
<b>Balance, May 31, 2005</b>	152,800,602	30,844,248
Exchange of First Preferred Series B Shares (Note 6(d))	1,946,810	229,724
Share consolidation	(145,075,831)	-
<b>Balance, February 28, 2006</b>	<b>9,671,581</b>	<b>31,073,972</b>

At a special meeting of shareholders held on January 27, 2006, the shareholders approved that the outstanding common shares of the Company be consolidated on a one-for-sixteen basis (1:16). Subsequently, the TSX Venture Exchange granted its approval for the consolidation of common shares and the Articles of the Company were amended under the Business Corporations Act (Ontario).

Subsequent to February 28, 2006, The Company issued 7,812 common shares to North Atlantic Resources Ltd. (See Note 3(d)).

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**(c) Warrants**

A summary of the Company's warrant activity during the period June 1, 2005 through February 28, 2006 is as follows:

	<b>Warrants</b>	<b>Weighted average exercise price</b>
	#	\$
Outstanding, beginning of period	41,838,728	0.11
Share consolidation	(39,143,807)	
Post-consolidation	2,614,921	1.76
Expired	(296,337)	(3.14)
Outstanding, end of period	2,318,584	1.57

A summary of warrants outstanding February 28, 2006 is as follows:

<b>Expiry date</b>	<b>Warrants</b>	<b>Exercise price</b>
	#	\$
May 31, 2006	79,000	0.80
October 22, 2006	2,239,584	1.60
	2,318,584	

**(d) First Preferred Series B Shares**

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 First Preferred Series B Shares of DEI having a value equal to the staking costs and cost of work carried out on the claims by the vendors.

The First Preferred Series B Shares are exchangeable, at any time after December 31, 2004 and up to December 31, 2006, into common shares of the Company at the option of either the Company or the vendor at a price of \$1.888 per post-consolidation common share, being the weighted average trading price of the common shares during the three-month period ended December 31, 2004. Since the Company plans to issue its common shares in exchange for the First Preferred Series B Shares, they are reflected as shares to be issued.

During the nine months ended February 28, 2006, three vendors exchanged 229,724 First Preferred Series B Shares for 121,675 post-consolidation common shares of the Company. As at February 28, 2006, 54,475 First Preferred Series B Shares were outstanding which will be converted into 28,850 common shares of Diadem.

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**(e) Stock Option Plan**

Effective July 19, 2005, the board of directors granted options to purchase 337,500 common shares at an exercise price of \$1.60 per share.

The following is a summary of stock options outstanding at February 28, 2006:

Expiry Date	Exercise Price \$	Options #
February 20, 2008	1.60	46,875
February 21, 2008	1.60	15,625
May 28, 2008	1.60	196,875
October 8, 2008	1.84	21,875
October 8, 2008	1.60	31,250
November 20, 2008	1.60	6,250
October 18, 2009	1.68	109,375
November 1, 2009	1.60	46,875
July 19, 2010	1.60	337,500
		<b>812,500</b>

The weighted average fair value of options granted during the period was \$0.56 (post consolidation) or \$0.035 (pre-consolidation). The fair value of each option is estimated on the date of the grant using the Black-Scholes option-pricing model with the following weighted average assumptions: expected dividend yield of 0%, expected volatility of 100%, risk-free interest rate of 4.5% and an expected option life of 60 months. The statement of operations was charged \$136,887 for options vesting during the nine month period.

**7. RELATED PARTY INFORMATION**

Included in accounts payable and accrued liabilities is \$141,000 (May 31, 2005-\$163,571) due to three directors for administrative services rendered to and expenses paid on behalf of the Company. Cost of services rendered to the Company were \$142,881 during the nine month period (2005-\$149,337) and \$54,001 during the three month period (2005-\$74,337).

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.

**8. SUPPLEMENTARY CASH FLOW INFORMATION**

The Company did not pay any income taxes during the respective periods ended February 28, 2006 and 2005. During the nine months ended February 28, 2005, the Company issued 121,229 treasury Common Shares to settle interest aggregating \$12,123.

	2006 \$	2005 \$
Income taxes paid	-	-
Interest paid	-	-
Common shares issued in settlement of interest	-	12,123
Value of Series B First Preference Shares exchanged for common shares of the Company	229,724	-

**9. INCOME TAXES**

The Company utilizes the asset and liability method of accounting for income taxes.

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**Provision for Income Taxes**

Major items causing the Company's income tax rate to differ from the combined federal and provincial statutory rate of 36.62% (2004 – 36.62%) for the nine month periods were as follows:

	<u>2006</u>	<u>2005</u>
	\$	\$
(Loss) before taxes:	<u>(786,861)</u>	<u>(861,332)</u>
Expected income tax benefit based on statutory rate	(288,149)	(315,420)
Adjustments to benefit resulting from:		
Non-taxable portion of capital gains	(13,421)	(22,500)
Amortization of equity finance costs	(1,150)	(66,600)
Non-deductible expenses	1,175	700
Write-down of mineral interests and investments	128,952	-
Future income tax assets not previously recognized	<u>(370,652)</u>	<u>(57,216)</u>
Income tax recovery	<u>(543,245)</u>	<u>(286,664)</u>

As at February 28, 2006, the Company had available for deduction against future taxable income, non-capital losses of approximately \$4,700,000 which expire as follows:

In addition, the Company has capital losses aggregating \$3,298,000 and foreign exploration and development expenses aggregating approximately \$11,900,000, each of which are available for deduction against future taxable income.

**10 COMMITMENTS**

As at February 28, 2006, the Company was committed to incur approximately \$1,285,000 of qualifying Canadian exploration expenditures pursuant to a May 2005 private placement for which flow-through proceeds had been received and renounced to the subscribers.

**11. SUBSEQUENT EVENT**

Subsequent to February 28, 2006, Diadem entered into a binding option agreement to acquire a 50% vested interest and the right to increase the vested interest to 57.5% in the Duquesne West gold project ("Project") north of Rouyn-Noranda, Quebec. The option agreement is with Jack Stoch Geoconsultant Services Inc. ("Vendor") and Globex Mining Enterprises Inc. ("Globex").

Under the agreement, Diadem can earn a 50% fully vested interest in the Project by spending \$6.0 million over three years on exploration and development, of which the first \$1.0 million is to be spent in the period to June 30, 2007. Diadem will make initial cash payments to the Vendor of \$250,000 and issue to the vendor 1,250,000 Diadem treasury common shares (subject to normal restrictions and regulatory requirements). To maintain the option, Diadem would make cumulative cash payments of an additional \$350,000 to the Vendor over two further years, plus carry out an additional \$5.0 million of exploration and development of the Project. Upon Diadem acquiring its 50% interest in the Project, Diadem would grant to the Vendor a 2.25% gross metal royalty based on Diadem's 50% interest in the Project out of which the Vendor will pay an existing 1% NSR royalty on the Project. Once the 50/50 joint venture is formed, further exploration and development costs will be shared proportionately by Diadem and Globex.

Upon Diadem earning its 50% fully vested interest it will have a one-time option to complete, at its cost, a positive bankable feasibility study required to put the Project into commercial production. Upon completion of the positive bankable feasibility study, or upon Diadem putting the Project into commercial production, including arranging the financing therefore, it will have the right to acquire from Globex an additional 7.5% fully vested interest in the Project upon payment to Globex of \$250,000 cash and

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the issue to Globex of 5% of the then issued and outstanding (undiluted) common shares of Diadem, subject to normal restrictions and regulatory requirements.