



(A Development Stage Company)

CONSOLIDATED FINANCIAL STATEMENTS

MAY 31, 2007 AND 2006

(Expressed in Canadian Dollars)



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CONSOLIDATED FINANCIAL STATEMENTS

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AUDITORS' REPORT

To the Shareholders of
DIADEM RESOURCES LTD.

We have audited the consolidated balance sheets of Diadem Resources Ltd. (a Development Stage Company) as at May 31, 2007 and 2006 and the consolidated statements of operations and deficit and cash flows for each of the years in the two-year period ended May 31, 2007. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at May 31, 2007 and 2006 and the results of its operations and its cash flows for each of the years in the two-year period ended May 31, 2007 in accordance with Canadian generally accepted accounting principles.

MCGOVERN, HURLEY, CUNNINGHAM, LLP

**Chartered Accountants
Licensed Public Accountants**

Toronto, Canada
July 31, 2007

DIADEM RESOURCES LTD.
 (A Development Stage Company)
CONSOLIDATED BALANCE SHEETS
 AS AT MAY 31

(Expressed in Canadian Dollars)	2007 \$	2006 \$
ASSETS		
CURRENT		
Cash	592,007	262,756
Accounts receivable-		
Due from related parties (Note 8)	4,453	-
Taxes recoverable (Note 4)	92,112	17,536
Other	-	1,555
Prepaid expenses	<u>3,338</u>	<u>4,513</u>
	691,910	286,360
MINERAL INTERESTS (Note 3)	2,760,573	2,788,881
EQUIPMENT (Note 5)	6,759	6,689
OTHER (Note 6)	<u>-</u>	<u>21</u>
	<u>3,459,242</u>	<u>3,081,951</u>
LIABILITIES		
CURRENT		
Accounts payable and accrued liabilities (Note 8)	318,432	449,970
Other taxes payable (Note 11)	<u>163,948</u>	<u>107,529</u>
	<u>482,380</u>	<u>557,499</u>
SHAREHOLDERS' EQUITY		
CAPITAL STOCK (Notes 7(a) and (b))	33,824,873	31,080,221
WARRANTS (Note 7(d))	543,799	783,430
CONTRIBUTED SURPLUS (Note 7(f))	1,664,828	872,805
SHARES TO BE ISSUED (Note 3(b))	-	54,475
DEFICIT	<u>(33,056,638)</u>	<u>(30,266,479)</u>
	<u>2,976,862</u>	<u>2,524,452</u>
	<u>3,459,242</u>	<u>3,081,951</u>

Commitments and contingencies (Notes 1, 3 and 11)

APPROVED ON BEHALF OF THE BOARD:

Signed "P. A. Carroll" _____, Director

Signed "Aime Bertrand" _____, Director

DIADEM RESOURCES LTD.
 (A Development Stage Company)
CONSOLIDATED STATEMENTS OF OPERATIONS AND DEFICIT
 FOR THE YEARS ENDED MAY 31

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(Expressed in Canadian Dollars)	2007 \$	2006 \$
REVENUE		
Gain on sale of investment and other	43,979	73,850
Interest income	22,005	13,511
Foreign exchange gain	-	135
	<u>65,984</u>	<u>87,496</u>
EXPENSES		
Amortization	2,210	2,898
Business development	2,357	2,875
Capital tax (recovered)	4,234	(1,795)
Advisory fees	106,200	-
Interest	94,265	56,081
Loss on disposal of equipment	-	175
Management fees, salaries and benefits	227,499	229,299
Office expenses and other	54,822	51,280
Professional fees	53,728	55,513
Shareholder relations	58,885	123,017
Travel	3,912	5,783
Stock-based compensation	8,593	143,365
Write-down of mineral interests (Note 3)	2,001,693	700,601
	<u>2,618,398</u>	<u>1,369,092</u>
Loss before income taxes	(2,552,414)	(1,281,596)
Future income taxes (Note 10)	<u>1,019,686</u>	<u>543,245</u>
NET LOSS FOR THE YEAR	(1,532,728)	(738,351)
DEFICIT , beginning of year	(30,266,479)	(28,959,851)
Costs associated with issuance of capital stock	<u>(1,257,431)</u>	<u>(568,277)</u>
DEFICIT , end of year	<u>(33,056,638)</u>	<u>(30,266,479)</u>
NET LOSS PER SHARE - basic and diluted	(0.10)	(0.08)
WEIGHTED AVERAGE NUMBER OF COMMON SHARES	15,413,488	9,754,818

See accompanying notes to the consolidated financial statements.

DIADEM RESOURCES LTD.
 (A Development Stage Company)
CONSOLIDATED STATEMENTS OF CASH FLOWS
 FOR THE YEARS ENDED MAY 31

(Expressed in Canadian Dollars)	2007 \$	2006 \$
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss for the year	(1,532,728)	(738,351)
Adjustment for items not affecting cash:		
Amortization	2,210	2,898
Write-down of mineral interests	2,001,693	700,601
Gain on disposal of investment and other	(43,979)	(73,850)
Loss on disposal of equipment	-	175
Stock-based compensation	8,593	143,365
Future income taxes	<u>(1,019,686)</u>	<u>(543,245)</u>
	<u>(583,897)</u>	<u>(507,857)</u>
Net changes in non-cash working capital balances:		
Prepaid expenses	1,175	713
Taxes recoverable	(55,587)	20,035
Other receivable	1,555	-
Receivable from related parties	(4,453)	-
Accounts payable and accrued liabilities	(137,538)	122,566
Other taxes payable	<u>56,419</u>	<u>12,286</u>
	<u>(138,429)</u>	<u>155,600</u>
Cash flows from operating activities	<u>(722,326)</u>	<u>(352,257)</u>
CASH FLOWS FROM FINANCING ACTIVITIES:		
Subscription receivable	-	10,000
Common shares issued for cash	2,856,053	-
Costs associated with issuance of capital stock	<u>(198,572)</u>	<u>(25,032)</u>
Cash flows provided from financing activities	<u>2,657,481</u>	<u>(15,032)</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Equipment	(2,280)	-
Proceeds from sale of investment and marketable securities	-	73,300
Mineral interests	(1,603,624)	(1,137,303)
Exploration deposits	<u>-</u>	<u>238,513</u>
Cash flows from investing activities	<u>(1,605,904)</u>	<u>(825,490)</u>
Increase in cash during the year	329,251	(1,192,779)
CASH , beginning of year	<u>262,756</u>	<u>1,455,535</u>
CASH , end of year	<u>592,007</u>	<u>262,756</u>

SUPPLEMENTAL INFORMATION (Note 9)

See accompanying notes to the consolidated financial statements.

(A Development Stage Company)**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

MAY 31, 2007 and 2006

(Expressed in Canadian Dollars)

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 North America 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.

Although the Company has taken steps to verify title to the properties on which it is conducting exploration and in which it has an interest, in accordance with industry standards for the current stage of exploration of such properties, these procedures do not guarantee the Company's title. Property title may be subject to unregistered prior agreements and non-compliance with regulatory requirements.

The recoverability of the amounts shown for mineral interests is dependent upon the existence of economically recoverable reserves, the ability of the Company to obtain necessary financing to complete the development of those reserves, upon future profitable production and/or the proceeds from the disposition thereof. To date, the Company has not earned significant revenues.

The consolidated financial statements are prepared in accordance with Canadian generally accepted accounting principles and on the assumption that the Company 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 achieve positive cash flows from operations.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting policies of the Company and its subsidiaries are in accordance with Canadian generally accepted accounting principles and their basis of application is consistent with that of the previous year. Outlined below are those policies considered particularly significant.

Basis of Consolidation:

The consolidated financial statements include the accounts of Diadem Resources Ltd. and its subsidiary.

Equipment and Amortization:

Equipment is recorded at cost and is amortized over its estimated useful life using the declining balance basis at the following annual rates:

Computer and office equipment	30%
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Financial Instruments:

The Company's financial instruments are comprised primarily of cash and cash equivalents, accounts receivable, prepaid expenses, accounts payable and accrued liabilities and other taxes payable. The fair value of these financial instruments approximates their carrying values due, primarily, to their immediate or short-term maturity.

The Company is exposed to fluctuations in interest rates, foreign currency exchange rates and commodity prices. The Company has not entered into any derivative financial instruments to manage fluctuations in these rates.

Continued...

(A Development Stage Company)**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

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2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**Foreign Currency Translation:**

The Company's functional and reporting currency is the Canadian dollar. Monetary assets and liabilities denominated in foreign currencies are translated into Canadian dollars at the rate of exchange prevailing at the statement date. Non-monetary assets and liabilities denominated in foreign currencies are translated into Canadian dollars at historical exchange rates. Revenue and expense items, other than amortization, are translated at the average rate of exchange for the year. An exchange gain or loss that arises on translation or settlement of a foreign currency denominated monetary item is included in operations for the period.

Mineral Interests:

The exploration activities of the Company are directed towards the search, evaluation and development of mineral properties. Major expenditures are required to locate and establish ore reserves to develop metallurgical processes and to construct mining and processing facilities at a particular site.

The recoverability of values assigned to mineral interests is dependent upon discovery of economically recoverable reserves, confirmation of the Company's interest in the mineral claims, the ability to obtain necessary financing to complete development and future profitable production or proceeds from disposition. Management reviews the carrying value of the Company's interest in each property on an annual basis or whenever events or changes in circumstances indicate that their carrying amount may not be recoverable and, where necessary, these properties are written down to their estimated recoverable amount. It is reasonably possible that certain events could adversely affect management's estimates of recoverable amounts and the need for, as well as the amount of, provision for impairment in the carrying value of mineral interests and related assets.

The cost of acquisition of mineral interests and related exploration costs are deferred until the properties to which they relate are placed into production, sold or allowed to lapse. These costs will be amortized over the estimated useful life of the properties following commencement of commercial production or written off if the properties are sold or allowed to lapse. The Company does not accrue future costs to keep the properties in good standing. Administrative expenditures, not directly related to property maintenance, are charged to operations as incurred.

The Company recognizes government assistance in the form of mineral exploration and mining tax credits when the amounts to be received can be reasonably estimated and collection can be reasonably assured. The amount of mineral exploration and mining tax credit reduces the Company's capitalized mineral property costs.

Stock-based Compensation:

All stock-based awards made to employees and non-employees are measured and recognized using a fair value based method. For employees, the fair value of the options at the date of grant is accrued and charged to operations or capitalized to a resource property, with the offsetting credit to contributed surplus, on a straight line basis over the vesting period. If and when the stock options are ultimately exercised, the applicable amounts of contributed surplus are transferred to share capital. For non-employees, the fair value of the options is measured on the earlier of the date at which the counterparty performance is complete or the date the performance commitment is reached or the date upon which the equity instruments are granted if they are fully vested and non-forfeitable.

Continued...

(A Development Stage Company)**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

MAY 31, 2007 and 2006

(Expressed in Canadian Dollars)

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**Use of Estimates:**

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities and the reported amounts of revenue and expenses during the year. Actual results could differ from estimates. During the fiscal years presented, management has made a number of significant estimates and valuation assumptions regarding the recoverability of investments in mining interests and deferred exploration costs. These estimates and valuation assumptions are in accordance with Canadian mining industry practice. Other significant estimates include the valuation of stock-based compensation, contingencies, asset retirement obligations and tax accounts.

Share Purchase Warrants:

The Company, from time-to-time, issues units which are normally comprised of a common share and a share purchase warrant. The common share is issued at the then current market value with the share purchase warrant exercisable at a price equal to or higher than the market value of the common share. The Company allocates the proceeds of the unit offering between the common shares and the share purchase warrants based on the fair value of each component.

Asset Retirement Obligations:

The fair value of a liability for an asset retirement obligation is recognized in the period in which it is incurred. Also, when the liability is initially recorded, a corresponding increase in the carrying amount of the related asset is recorded.

On an annual basis, the liability is increased by the interest factor that was applied in the initial measurement of fair value and the asset is amortized over the estimated life of the related asset. The amount of the liability will be subject to re-measurement at the end of each reporting period. Any adjustment to this liability will impact the related asset.

As at May 31, 2007 and 2006, the Company had no asset retirement obligations.

Loss Per Share:

Basic loss per share is calculated using the weighted number of shares outstanding for the period. Diluted loss per share is calculated using the treasury stock method. In order to determine diluted loss per share, the treasury stock method assumes that any proceeds from the exercise of dilutive stock options and warrants would be used to repurchase common shares at the average market price during the period, with the incremental number of shares being included in the denominator of the diluted loss per share calculation. The diluted loss per share calculation excludes any potential conversion of options and warrants that would increase earnings per share or decrease loss per share.

Flow-through Financing:

The Company has financed a portion of its exploration activities in Canada through the issue of flow-through shares, which transfers the tax deductibility of Canadian exploration expenditures to the investor. Proceeds received on the issue of such shares are credited to capital stock. The related exploration costs, when incurred, are charged to mining and resource properties.

Resource expenditure deductions for income tax purposes related to exploration and development activities funded by flow-through share arrangements are renounced to investors in accordance with income tax legislation. The tax benefit forgone on renunciation of Canadian exploration expenditures to investors is charged to deficit as a cost of equity financing when such amounts are renounced.

Continued...

(A Development Stage Company)

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

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2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

Income Taxes:

The Company uses the liability method of accounting for income taxes. Under the liability method of tax allocation, future income taxes are determined based on the differences between the financial reporting and tax bases of assets and liabilities. These income tax assets and liabilities are measured using the substantially enacted tax rates in which the income tax assets and liabilities are expected to be settled or realized. A valuation allowance is provided to the extent that it is more likely than not that future income tax assets will not be realized.

3. MINERAL INTERESTS

	Balance May 31, 2006 \$	Additions \$	Write-downs \$	Balance May 31, 2007 \$
Acquisition costs				
Franklin Project,				
Northwest Territories	1,190,764	-	(48,068)	1,142,696
Duquesne West, Quebec	<u>25,000</u>	<u>563,750</u>	<u>(588,750)</u>	<u>-</u>
	<u>1,215,764</u>	<u>563,750</u>	<u>(636,818)</u>	<u>1,142,696</u>
Deferred exploration costs				
Franklin Project,				
Northwest Territories	1,528,751	185,643	(96,517)	1,617,877
Duquesne West, Quebec	<u>44,366</u>	<u>1,223,992</u>	<u>(1,268,358)</u>	<u>-</u>
	<u>1,573,117</u>	<u>1,409,635</u>	<u>(1,364,875)</u>	<u>1,617,877</u>
	<u>2,788,881</u>	<u>1,973,385</u>	<u>(2,001,693)</u>	<u>2,760,573</u>
	Balance May 31, 2005 \$	Additions \$	Write-downs \$	Balance May 31, 2006 \$
Acquisition costs				
Franklin Project,				
Northwest Territories	1,190,764	-	-	1,190,764
Attawapiskat Project, Ontario	15,000	10,000	(25,000)	-
Duquesne West, Quebec	-	25,000	-	25,000
Mali, West Africa	-	19,886	(19,886)	-
	<u>1,205,764</u>	<u>54,886</u>	<u>(44,886)</u>	<u>1,215,764</u>
Deferred exploration costs				
Franklin Project,				
Northwest Territories	513,068	1,015,683	-	1,528,751
Attawapiskat Project, Ontario	327,098	36	(327,134)	-
Otish Mountains, Quebec	300,000	-	(300,000)	-
Duquesne West, Quebec	-	44,366	-	44,366
Mali, West Africa	-	28,581	(28,581)	-
	<u>1,140,166</u>	<u>1,088,666</u>	<u>(655,715)</u>	<u>1,573,117</u>
	<u>2,345,930</u>	<u>1,143,552</u>	<u>(700,601)</u>	<u>2,788,881</u>

Continued...

(A Development Stage Company)**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

MAY 31, 2007 AND 2006

(Expressed in Canadian Dollars)

3. MINERAL INTERESTS (Continued)**(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 375,000 Diadem common shares, valued at \$600,000. Paul Carroll, Chairman and CEO of Diadem, 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 in California) other than through Diadem or with the consent of Diadem.

Under the agreement, Diadem was to expend \$5,000,000 on diamond exploration within the Inuvialuit settlement region north of the 68th parallel by December 31, 2006. When this earn-in level of expenditure is completed, Diadem will have earned an undivided 50% participating interest in the selected lands, with DBR holding the other 50%. If a decision is made to carry out a feasibility study on the lands, 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 68th parallel was reduced to approximately \$3,100,000 and the earn-in period was extended to December 31, 2007. DBR relinquished its participating interest in the joint venture lands south of the 68th parallel and transferred to Diadem 100% ownership in the permits and claims south of the 68th parallel. The Company has since relinquished its permits to explore certain lands south of the 68th parallel. Consequently, the Company wrote off the acquisition costs and exploration expenses associated with these permits.

The Company and DBR entered into a Cooperation Agreement with the Inuvialuit Regional Corporation ("IRC") whereby the IRC agreed to cooperate to develop the diamond potential of certain Inuvialuit and crown lands. The agreement is for a term of 5 years commencing January 1, 2004 with provisions for renewal and termination. Diadem and DBR are 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 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 a positive feasibility is completed, 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.

Continued...

(A Development Stage Company)**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

MAY 31, 2007 AND 2006

(Expressed in Canadian Dollars)

3. MINERAL INTERESTS (Continued)**(b) 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 were 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 common share, being the weighted average trading price of the common shares during the three-month period ended December 31, 2004.

During 2007, vendors exchanged 54,475 (2006 – 229,724) Series B First Preference Shares for 28,850 (2006 – 121,676) common shares of the Company.

During 2006 and 2005, the Company decided not to renew these claims and wrote-off the carrying value of the Otish Mountains project.

(c) Tinkeleni, Diokeba, Dalakan and Sinzeni Projects, Mali, West Africa

Effective November 23, 2005, Diadem entered into a partnership agreement with La Société African Minerals Exploration SARL ("Amex") on 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 FCFA 4,000,000 obligation was settled through the payment of \$8,636.

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.

To maintain these options, Diadem issued 7,812 common shares valued at \$6,249 on March 27, 2006.

During 2006, the Company decided not to continue with the foreign exploration program and terminated the agreements with Amex and NAC and accordingly wrote-off the acquisition and exploration costs.

(d) 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 2005, the Company paid a further \$10,000 to maintain the option agreement and incurred \$352,134 of qualified expenditures on this property, plus a 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.

Continued...

(A Development Stage Company)

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

MAY 31, 2007 AND 2006

(Expressed in Canadian Dollars)

3. MINERAL INTERESTS (Continued)

(e) Duquesne West Project, Quebec

On April 18, 2006, Diadem entered into an option agreement to acquire a 50% vested interest and the right to increase the vested interest to 57.5% in the Duquesne West project north of Rouyn-Noranda, Quebec. The option agreement was with Jack Stoch Geoconsultant Services Inc. ("Vendor") and Globex Mining Enterprises Inc. ("Globex").

The option agreement became effective July 17, 2006. Under the agreement, Diadem could earn a 50% fully vested interest in the Project by spending \$6,000,000 over three years on exploration and development, of which \$1,000,000 is to be spent by June 30, 2007, an additional \$2,000,000 is to be spent by June 30, 2008 and an additional \$3,000,000 is to be spent by June 30, 2009. Diadem made initial cash payments to the Vendor of \$225,000, and issued to the vendor 1,250,000 Diadem common shares valued at \$338,750 based on the quoted, closing market price of the Company's shares on the day of closing of the agreement.

During May 2007, the Company elected not to proceed further with the project, allowed the option to lapse and wrote-off the carrying value of the project.

4. TAXES RECOVERABLE

Taxes recoverable consist of:

	<u>2007</u>	<u>2006</u>
	\$	\$
Province of Quebec income and mining tax credits	18,910	-
Province of Quebec sales tax credits	64,744	-
Government of Canada goods and services tax credits	<u>8,458</u>	<u>17,536</u>
	<u>92,112</u>	<u>17,536</u>

5. EQUIPMENT

	<u>2007</u>		<u>2006</u>	
	<u>Cost</u>	<u>Accumulated Amortization</u>	<u>Net</u>	<u>Net</u>
	\$	\$	\$	\$
Computer and office equipment	15,694	8,935	6,759	6,689

6. OTHER

Other assets, at May 31 of each of the years indicated are comprised as follows:

	<u>2007</u>	<u>2006</u>
	\$	\$
Investment in Belitung Limited	-	<u>21</u>
	<u>-</u>	<u>21</u>

During the year ended May 31, 2003, the Board of Directors of the Company elected to change the operating focus of the Company. Consequently, management and the Board of Directors of the Company decided to dispose of its then residual mineral interests in Mexico, Nicaragua, Indonesia, Ontario and Quebec ("Transferred Assets") to Belitung Limited ("Belitung"), a company controlled by its then Chairman, in consideration of Series A shares and 20% of the common shares of Belitung.

Continued...

(A Development Stage Company)**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

MAY 31, 2007 AND 2006

(Expressed in Canadian Dollars)

6. OTHER (Continued)

Belitung agreed to assume the liability to repay to the former Chairman \$160,278 of advances that were owed to him by the Company (the "Howe Payables"). Belitung will liquidate or develop the Transferred Assets, including collection of loans, as quickly as practicable and on terms that are commercially prudent. All net proceeds received by Belitung from the liquidation, development or other utilization of the Transferred Assets, whether in the form of sale proceeds, royalties, principal and interest on loans and advances, joint venture payments, property net revenues or otherwise, shall be applied in the following order of priority: (i) to pay normal operating expenses and taxes of Belitung and its subsidiaries, (ii) to repay to Howe the Howe Payables until repaid in full, and (iii) to the extent of 60% of the balance after the amounts referred to in (i) and (ii), to the redemption at par of Series A Shares. The balance of the net cash flow of Belitung shall be paid out as dividends on the common shares of Belitung when and as declared by the board of directors of Belitung, subject to retaining a reasonable operating reserve.

Since Belitung had not completed a bona fide sale of all of the Transferred Assets by November 30, 2003, the Company has a right of first refusal to acquire any unsold Transferred Assets on such terms, which will be cash only, as any offer received by Belitung to purchase such Transferred Assets.

Effective May 31, 2007, Diadem sold its investment in 20% of the common shares of Belitung to the former Chairman in settlement of a \$44,000 claim for prior services rendered while still a director of Diadem but subsequent to the aforementioned transfer of assets.

7. 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.

During 2006, the common shares of Company were consolidated on a 1-for-16 basis. These consolidated financial statements fully reflect this share consolidation.

(b) Issued and Outstanding Shares

Details of issued and outstanding common shares are as follows:

	2007		2006	
	#	\$	#	\$
Balance, beginning of year	9,679,394	31,080,221	9,550,038	30,844,248
Issued pursuant to:				
Shares issued for cash	110,000	33,000	-	-
Conversion of Series B Preference Shares (Note 3(b))	28,850	54,475	121,675	229,724
Flow-through financings (Note 7(c))	7,876,403	2,823,053	-	-
Shares issued for property (Note 3(c))	1,250,000	338,750	7,812	6,249
Issue of warrants (Notes 7 (c) and (d))	-	(504,626)	-	-
Adjustment for rounding due to share consolidation	-	-	(131)	-
Balance, end of year	<u>18,944,647</u>	<u>33,824,873</u>	<u>9,679,394</u>	<u>31,080,221</u>

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(A Development Stage Company)

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

MAY 31, 2007 AND 2006

(Expressed in Canadian Dollars)

7. SHAREHOLDERS' EQUITY (Continued)

(c) Flow-through Financings

During May 2005, the Company placed 1,880,000 common shares at a price of \$0.80 per share for gross proceeds of \$1,504,000. A total of \$57,950 in cash commissions was paid and 79,000 non-flow-through broker warrants were issued, exercisable for a period of one year from the date of closing with an exercise price of \$0.80. The broker warrants were valued at \$25,280. The fair value of the broker warrants was estimated using the Black-Scholes option-pricing model with the following weighted average assumptions: expected dividend yield of 0%, expected stock volatility of 100%, risk-free interest rate of 4.5% and an expected warrant life of 1 year.

During July 2006, the Company placed 1,813,454 flow-through common shares at a price of \$0.42 per share for gross proceeds of \$761,650.

During November 2006, the Company placed 4,767,654 Units at a price of \$0.34 per Unit for aggregate gross proceeds of \$1,621,002. Each Unit consisted of one flow-through common share and one common share purchase warrant. Each common share purchase warrant entitles the holder to purchase one additional common share for a period of one year with an exercise price of \$0.45 per share and thereafter at an exercise price of \$0.60 per share for the period ending 24 months from the date of issuance. The gross proceeds were prorated to capital stock and warrants based on the relative fair value of each component, as follows: capital stock - \$1,251,599; warrants - \$369,403. A total of \$81,050 in cash commissions was paid and 381,412 non-flow-through broker warrants were issued, exercisable for a period of one year with an exercise price of \$0.45 per share and thereafter at an exercise price of \$0.60 per share for the period ending 24 months from the date of issuance. The broker warrants were valued at \$39,173. The fair values of the warrants and broker warrants were estimated using the Black-Scholes option-pricing model with the following weighted average assumptions: expected dividend yield of 0%, expected stock volatility of 100%, risk-free interest rate of 4.18% and an expected warrant life of 2 years.

During December 2006, the Company placed 1,295,295 Units at a price of \$0.34 per Unit for gross proceeds of \$440,400. Each Unit consisted of one flow-through common share and one common share purchase warrant. Each common share purchase warrant entitles the holder to purchase one additional common share for a period of one year with an exercise price of \$0.45 per share and thereafter at an exercise price of \$0.60 per share for the period ending 24 months from the date of issuance. The gross proceeds were prorated to capital stock and warrants based on the relative fair value of each component, as follows: capital stock - \$305,177; warrants - \$135,223.

(d) Warrants

A summary of the Company's warrant activity during the years ended May 31, 2007 and 2006 is as follows:

	2007		2006	
	<u>Warrants</u>	<u>Weighted Average</u>	<u>Warrants</u>	<u>Weighted Average</u>
		<u>Exercise price</u>		<u>Exercise price</u>
	<u>#</u>	<u>\$</u>	<u>#</u>	<u>\$</u>
Outstanding, beginning of year	2,239,583	1.60	2,614,921	1.75
Issued	6,444,361	0.45	-	-
Exercised	-	-	-	-
Cancelled	(1,235,300)	(0.45)	-	-
Expired	<u>(2,239,583)</u>	1.60	<u>(375,338)</u>	(3.20)
Outstanding, end of year	<u>5,209,061</u>	0.45	<u>2,239,583</u>	1.60

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(A Development Stage Company)

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

MAY 31, 2007 AND 2006

(Expressed in Canadian Dollars)

7. SHAREHOLDERS' EQUITY (Continued)

A summary of warrants outstanding at May 31, 2007 is as follows:

<u>Expiry date</u>	<u>Warrants</u>	<u>Exercise Price</u>	<u>Fair Value</u>
	#	\$	\$
November 15, 2008	3,913,766	0.45/0.60	408,576
December 20, 2008	<u>1,295,295</u>	0.45/0.60	<u>135,223</u>
	<u>5,209,061</u>	0.45/0.60	<u>543,799</u>

(e) Stock Option Plan

The Company has a stock option plan to aid in retaining and encouraging directors, senior officers, employees and service providers of the Company. At the annual general meeting of shareholders held November 30, 2006, the shareholders adopted and approved an amendment to Diadem's stock option plan which permits reserving for issuance under the stock option plan, at any time, of a maximum of 10% of the issued and outstanding shares of the Company at the date of grant. 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.

A summary of the Company's stock option activity is as follows:

	<u>Options</u>	<u>Weighted average exercise price</u>
	#	\$
Outstanding, May 31, 2005	571,875	1.63
Expired	(96,875)	1.62
Granted	<u>337,500</u>	1.60
Outstanding, May 31, 2006	812,500	1.62
Expired	<u>(421,875)</u>	1.63
Outstanding, May 31, 2007	<u>390,625</u>	1.63

The following is a summary of stock options outstanding at May 31, 2007:

<u>Expiry Date</u>	<u>Exercise Price</u>	<u>Options</u>
	\$	#
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	6,250
October 8, 2008	1.60	31,250
November 20, 2008	1.60	6,250
October 18, 2009	1.68	15,625
November 1, 2009	1.60	46,875
July 19, 2010	1.60	<u>25,000</u>
		<u>390,625</u>

The weighted average fair value of options granted during 2006 was \$0.54. 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.

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(A Development Stage Company)

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

MAY 31, 2007 AND 2006

(Expressed in Canadian Dollars)

7. SHAREHOLDERS' EQUITY (Continued)

(f) Contributed Surplus

A summary of the Company's contributed surplus activity is as follows:

	<u>2007</u>	<u>2006</u>
	\$	\$
Balance, beginning of year	872,805	502,782
Stock-based compensation	8,593	143,365
Expiry of warrants	<u>783,430</u>	<u>226,658</u>
Balance, end of year	<u>1,664,828</u>	<u>872,805</u>

8. RELATED PARTY TRANSACTIONS AND BALANCES

Included in accounts receivable are amounts due from two corporations over which two directors have direction and control.

Included in accounts payable and accrued liabilities is \$12,040 (2006-\$120,167) due, directly and indirectly, to three directors for administrative, financial and geological services rendered to and expenses paid on behalf of the Company. Cost of services rendered to the Company, directly and indirectly, by the three directors was \$312,847 (2006-\$69,486) during 2007. 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.

Rent totalling \$36,000 (2006-\$36,000) was paid to a company controlled by a director of Diadem.

Directors and officers of the Company subscribed for 808,726 common shares of Diadem for gross proceeds of \$309,900 pursuant to the private placements described in notes 7(b) and 7(c).

9. SUPPLEMENTARY CASH FLOW INFORMATION

	<u>2007</u>	<u>2006</u>
	\$	\$
Income taxes paid	-	-
Interest paid	34,624	29,584
Value of Series B first preference shares exchanged for common shares of the Company (Note 3(b))	54,475	229,724
Disposal of investment to settle accounts payable	44,000	-
Common shares issued to acquire Mali, West Africa Claims	-	6,249
Common shares issued to acquire Duquesne West Project	338,750	-
Broker warrants issued	39,173	-

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(A Development Stage Company)

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

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(Expressed in Canadian Dollars)

10. INCOME TAXES

Provision for Income Taxes

Major items causing the Company's income tax rate to differ from the combined Canadian federal and provincial statutory rate of approximately 36% (2006 – 36%) were as follows:

	<u>2007</u>	<u>2006</u>
	\$	\$
(Loss) before income taxes:	<u>(2,552,414)</u>	<u>(1,281,596)</u>
Expected income tax benefit based on statutory rate	(922,000)	(463,000)
Adjustments to benefit resulting from:		
Non-taxable portion of capital gains	(8,000)	(13,000)
Equity finance costs	(72,000)	(8,000)
Non-deductible expenses	4,000	54,000
Expiry of losses	238,000	324,000
Mineral interests	-	253,000
Other	201,314	(39,245)
Change in valuation allowance	<u>(461,000)</u>	<u>(651,000)</u>
	<u>(1,019,686)</u>	<u>(543,245)</u>

Future Income Tax Balances

The tax effects of temporary differences that give rise to future income tax assets at May 31, 2007 and 2006 are as follows:

	<u>2007</u>	<u>2006</u>
	\$	\$
Non-capital losses	1,711,000	1,707,000
Financing costs	99,000	-
Capital losses	201,000	21,000
Resource properties	3,187,000	3,932,000
Equipment	140,000	139,000
Valuation allowance	<u>(5,338,000)</u>	<u>(5,799,000)</u>
Net future income tax asset	<u>-</u>	<u>-</u>

As at May 31, 2007, the Company had available for deduction against future taxable income, non-capital losses of approximately \$4,736,000 which expire as follows:

<u>Year</u>	<u>Amount</u>
	\$
2008	841,000
2009	921,000
2010	238,000
2014	732,000
2015	1,075,000
2026	369,000
2027	<u>560,000</u>
	<u>4,736,000</u>

In addition, the Company has capital losses aggregating \$1,111,000, Canadian exploration and development expenditures of \$5,728,000, and foreign exploration and development expenses aggregating \$12,168,000, each of which are available for deduction against future taxable income under certain circumstances.

Continued...

(A Development Stage Company)**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

MAY 31, 2007 AND 2006

(Expressed in Canadian Dollars)

10. INCOME TAXES (Continued)

During the year ended May 31, 2007, the Company issued 7,876,403 flow-through shares for proceeds of \$2,823,053. During February 2007 and 2006, respectively, the Company renounced the equivalent expenditure to its investors and recognized a non-cash future income tax recovery of \$1,019,686 (2006 - \$543,245).

At May 31, 2007, the Company had provided a valuation allowance of \$4,482,000 (2006 - \$4,899,000) against future tax assets. As a consequence of issuing flow-through shares the Company created taxable temporary differences which can be reduced by previously unrecognized future tax assets. The recognition of the previously unrecognized future income tax asset results in a credit to the statement of operations in the amount of \$1,019,686 (2006 - \$543,245) with an offsetting charge to deficit as a cost of financing the flow-through share issue.

11. COMMITMENTS AND CONTINGENCIES

As at May 31, 2007, the Company is committed to incur prior to December 31, 2007, on a best efforts basis, approximately \$2,600,000 in qualifying Canadian exploration expenditures ("CEE") pursuant to a private placement for which flow-through proceeds had been received during 2006 and renounced to the subscribers with an effective date of December 31, 2006. Diadem may not incur sufficient CEE to 2007 to fully satisfy its flow-through commitments. The extent of this cannot currently be calculated. In order to address the impact on subscribers to the Company's 2006 flow-through financings, the Company proposes to seek to enter into agreements with the affected subscribers to satisfy the indemnity provisions of the original subscription agreements.

Diadem may be subject to certain additional taxes and penalties as a result of any potential shortfall in CEE expenditures incurred during 2007. No accrual has been made as the magnitude of any potential shortfall is not yet determinable.

Other taxes payable consists of Part XII.6 tax on flow-through Canadian Exploration Expenditures incurred subsequent to the year of renunciation to investors. Should the Company not incur the amount renounced to investors prior to December 31, 2007, the Company may be assessed further penalties.