
Financial Statements

Avalon Ventures Ltd.

For the years ended August 31, 2008 and 2007

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MANAGEMENT’S RESPONSIBILITY FOR FINANCIAL REPORTING

The financial statements and other financial information for this annual report were prepared by the management of Avalon Ventures Ltd., reviewed by the Audit Committee of the Board of Directors, and approved by the Board of Directors.

Management is responsible for the preparation of the financial statements and believes that they fairly represent the Company's financial position and the results of operations in accordance with Canadian generally accepted accounting principles. Management has included amounts in the Company's financial statements based on estimates, judgements, and policies that it believes reasonable in the circumstances.

To discharge its responsibilities for financial reporting and for the safeguarding of assets, management believes that it has established appropriate systems of internal accounting control which provide reasonable assurance that the assets are maintained and accounted for in accordance with its policies and that transactions are recorded accurately in the Company's books and records.

Bolton & Bolton, Chartered Accountants were appointed as auditors by the shareholders of the Company.

“Donald S. Bubar”

President and CEO

“R. J. (Jim) Andersen”

CFO and Vice President Finance

Toronto, Ontario
October 16, 2008

BOLTON & BOLTON
Chartered Accountants

AUDITORS' REPORT

TO THE SHAREHOLDERS OF AVALON VENTURES LTD.

We have audited the balance sheets of Avalon Ventures Ltd. as at August 31, 2008 and 2007, and the statements of operations and deficit, cash flows and comprehensive loss for the years then ended. These financial statements are the responsibility of the company's management. Our responsibility is to express an opinion on these 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 financial statements present fairly, in all material respects, the financial position of the company as at August 31, 2008 and 2007, and the results of its operations and cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

“Bolton & Bolton”

Chartered Accountants
Licensed Public Accountants
Toronto, Ontario
October 16, 2008

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Avalon Ventures Ltd.

Balance Sheets
As at August 31

	2008	2007
Assets		
Current Assets		
Cash and cash equivalents	\$ 10,738,700	\$ 1,562,102
Receivables	152,165	174,651
Prepaid expenses	130,226	63,817
	<u>11,021,091</u>	<u>1,800,570</u>
Investments Available for Sale (note 3)	3,943	3,044
Resource Properties (note 4)	13,188,626	7,255,442
Property, Plant and Equipment (note 5)	<u>170,930</u>	<u>71,663</u>
	<u>\$ 24,384,590</u>	<u>\$ 9,130,719</u>
Liabilities		
Current Liabilities		
Accounts payable (note 10)	<u>\$ 892,806</u>	<u>\$ 626,635</u>
Shareholders' Equity		
Share Capital (note 6)	43,273,243	26,910,660
Contributed Surplus (note 7)	54,175	38,376
Deficit	(19,827,434)	(18,435,853)
Accumulated Other Comprehensive Loss (note 8)	<u>(8,200)</u>	<u>(9,099)</u>
	<u>23,491,784</u>	<u>8,504,084</u>
	<u>\$ 24,384,590</u>	<u>\$ 9,130,719</u>

Commitments (note 13, 14)

The accompanying notes form an integral part of these financial statements.

Approved on behalf of the Board of Directors:

"Donald S. Bubar", Director

"Brian MacEachen", Director

Avalon Ventures Ltd.

Statements of Operations and Deficit
For the Years Ended August 31

	2008	2007
Revenue		
Interest	\$ 357,539	\$ 92,446
Expenses		
Amortization	40,806	18,290
Consulting fees	88,504	17,428
Directors' fees	42,000	16,500
Insurance	43,727	41,842
Interest and financing costs (note 6a))	81,274	49,614
Office and general	36,722	20,393
Professional fees (note 10)	172,962	66,789
Public and investor relations	526,291	277,420
Rent and utilities	108,237	61,899
Salaries and benefits	655,765	289,223
Shareholders' information	32,069	30,143
Stock-based compensation (note 6d)	641,458	487,568
Transfer and filing fees	203,858	42,330
Travel	230,580	99,874
	<u>2,904,253</u>	<u>1,519,313</u>
Loss before the Undernoted Items	(2,546,714)	(1,426,867)
Write-down of Resource Properties (note 4g))	(228,367)	-
Gain on Sale of Investments	-	35,598
Recoveries of Resource Properties (note 9)	<u>10,000</u>	-
Loss before Income Taxes	(2,765,081)	(1,391,269)
Future Income Tax Recoveries (note 11g))	<u>1,373,500</u>	<u>488,250</u>
Net Loss for the Year	(1,391,581)	(903,019)
Deficit – Beginning of Year	<u>(18,435,853)</u>	<u>(17,532,834)</u>
Deficit - End of Year	<u>\$ (19,827,434)</u>	<u>\$ (18,435,853)</u>
Loss per Share, Basic and Fully Diluted	<u>\$ (0.02)</u>	<u>\$ (0.02)</u>
Weighted Average Number of Common Shares Outstanding, Basic and Fully Diluted	<u>61,658,223</u>	<u>50,462,019</u>

The accompanying notes form an integral part of these financial statements.

Avalon Ventures Ltd.

Statements of Comprehensive Loss
For the Years Ended August 31

	2008	2007
Net Loss for the Year	\$ (1,391,581)	\$ (903,019)
Other Comprehensive Income (Loss)		
Unrealized gains (losses) on available-for-sale financial assets arising during the year	<u>899</u>	<u>(9,099)</u>
Comprehensive Loss for the Year	<u>\$ (1,390,682)</u>	<u>\$ (912,118)</u>

The accompanying notes form an integral part of these financial statements.

Avalon Ventures Ltd.

Cash Flow Statements

For the Years Ended August 31

	2008	2007
Cash Flows from Operating Activities		
Cash paid to suppliers and employees	\$ (2,136,448)	\$ (921,816)
Interest received	357,539	92,446
Interest paid	(45,273)	(352)
	<u>(1,824,182)</u>	<u>(829,722)</u>
Cash Flows from Financing Activities		
Share capital – private placement(s) (note 6a))	15,527,155	1,556,100
Share capital – exercise of warrants (note 6a))	1,317,769	719,126
Share capital – exercise of options (note 6a))	265,500	414,000
	<u>17,110,424</u>	<u>2,689,226</u>
Cash Flows from Investing Activities		
Resource property expenditures	(5,979,571)	(2,314,653)
Recoveries of abandoned resource properties	10,000	-
Proceeds from sale of investments	-	45,598
Purchase of property, plant and equipment	(140,073)	(51,486)
	<u>(6,109,644)</u>	<u>(2,320,541)</u>
Change in Cash and Cash Equivalents	9,176,598	(461,037)
Cash and Cash Equivalents - Beginning of Year	<u>1,562,102</u>	<u>2,023,139</u>
Cash and Cash Equivalents - End of Year	<u>\$ 10,738,700</u>	<u>\$ 1,562,102</u>

The accompanying notes form an integral part of these financial statements.

Avalon Ventures Ltd.

Notes to the Financial Statements

For the Years Ended August 31, 2008 and 2007

1. Nature of Operations

The Company is in the process of exploring its mineral resource properties. To date, the Company has not earned significant revenues and is considered to be in the development stage.

The realization of amounts shown for resource properties is dependent upon the discovery of economically recoverable reserves, the ability of the Company to obtain the necessary financing to develop these properties, and future profitable production or proceeds of disposition from these properties.

The Company operates in one geographic area, Canada, and in one industry segment, mining exploration.

2. Summary of Significant Accounting Policies

These financial statements are prepared in accordance with accounting principles generally accepted in Canada, and reflect the following significant accounting policies:

a) New Accounting Policy

On September 1, 2007 the Company adopted the new recommendations of the Canadian Institute of Chartered Accountants (“CICA”) Handbook Section 1506, “Accounting Changes”. Under these new recommendations, voluntary changes in accounting policy are permitted only when they result in the financials statements providing more reliable and more relevant information, require changes in accounting policy to be applied retrospectively unless doing so is impracticable, require prior period errors to be corrected retrospectively and require enhanced disclosures about the effects of changes in accounting policies, estimates and errors on the financial statements. These recommendations also require the disclosure of new primary sources of generally accepted accounting principles that have been issued but are not yet effective.

The impact that the adoption of this section will have on the Company’s financial statements will depend on the nature of future accounting changes, and the required additional disclosure on Recent Accounting Pronouncements is disclosed in Note 15.

b) Use of Estimates

The preparation of the financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of operations during the reporting period. Significant estimates and assumptions include those related to the recoverability of resource properties, stock-based compensation and the fair value of warrants issued in conjunction with the issuance of the Company’s common shares. While management believes that the estimates and assumptions are reasonable, actual results could differ from those estimates.

c) Financial Instruments

Effective September 1, 2006, the Company adopted the new recommendations of the Canadian Institute of Chartered Accountants (“CICA”) Handbook Section 1530, Comprehensive Income, Section 3855, Financial Instruments, and Section 3865, Hedges.

These changes in accounting policy had been adopted prospectively without restatement.

Avalon Ventures Ltd.

Notes to the Financial Statements
For the Years Ended August 31, 2008 and 2007

2. Summary of Significant Accounting Policies (Continued)

These recommendations establish standards for recognizing and measuring financial instruments, which include financial asset, financial liabilities, derivatives and embedded derivatives. Under these recommendations, all financial instruments are to be recorded initially at fair value. In subsequent periods, all financial measurements are re-measured based on the classification adopted for the financial instrument: held for trading, available-for-sale, held to maturity, loans and receivables or other liabilities.

The Company has classified its financial instruments as follows:

<u>Financial Instrument</u>	<u>Classification</u>	<u>Accounting Treatment</u>
Cash and cash equivalents	Held for trading	Fair market value
Receivables	Loans and receivables	Amortized cost
Investments available for sale	Available-for-sale	Fair market value
Accounts payable	Other liabilities	Amortized cost

CICA Handbook Section 1530, Comprehensive Income, establishes new measurements of earnings in the financial statements. Other comprehensive income consists of changes to unrealized gains and losses on available-for-sale financial assets, changes to unrealized gains and losses on the effective portion of cash flow hedges and changes to foreign currency translation adjustments of self-sustaining foreign operations during the period. Comprehensive income measures net earnings for the period plus other comprehensive income. Amounts reported as other comprehensive income are accumulated in a separate component of shareholders' equity as "Accumulated Other Comprehensive Income (Loss)".

CICA Handbook Section 3865, Hedges, replaces CICA Handbook Accounting Guideline 13, Hedging Relationships, which establishes standards for when and how hedge accounting may be applied. Consistent with financial instruments, it requires that all derivatives, including those designated as hedges, be measured at fair value. Changes in the fair value of a derivative which hedges the Company's exposure to changes in the fair value of an asset or liability, a fair value hedge, are recognized in net income together with those of the respective offsetting hedged item. Changes in the fair value of a derivative which hedges the Company's exposure to changing cash flows, a cash flow hedge, are accumulated in other comprehensive income until the transaction being hedged affects net income.

d) Cash and Cash Equivalents

Cash and cash equivalents include bank deposits and highly liquid short-term money market investments such as bankers acceptance notes, treasury bills and guaranteed investment certificates.

e) Resource Properties

Acquisition costs of resource properties together with direct exploration and development expenditures thereon are deferred in the accounts. When production is attained, these costs will be amortized on a unit-of-production basis. If the properties are abandoned, sold or considered to be impaired in value, the costs of the properties and related deferred expenses will be written down at that time. When deferred expenditures on individual producing properties exceed the estimated net realizable value of undiscounted proven reserves, the properties are written down to the estimated fair value.

Avalon Ventures Ltd.

Notes to the Financial Statements

For the Years Ended August 31, 2008 and 2007

2. Summary of Significant Accounting Policies (Continued)

The Company is in the process of exploring and developing its mineral properties and has not yet determined the amount of reserves available. Senior management regularly reviews the carrying amount of mineral properties and deferred exploration and development costs to assess whether there has been any impairment in value.

f) Property, Plant and Equipment

Property, plant and equipment are carried at cost less accumulated amortization. Amortization is provided over the estimated useful lives of the Company's assets on the following basis and rates per annum:

Computer equipment	-	30% on a declining balance basis
Computer software	-	33 1/3% on a declining balance basis
Equipment	-	30% on a declining balance basis
Office furniture	-	25% on a declining balance basis
Leasehold improvements	-	straight line basis over the term of the lease

Additions during the year are amortized using the half-year rule.

g) Research and Development

Research and development costs related to a specific property are deferred as part of the costs of that property in accordance with the Company's policy on exploration and development expenditures. General research and development costs are expensed as incurred.

h) Flow-through Shares

A portion of the Company's exploration activities are financed by flow-through share arrangements. Under the terms of flow-through share agreements, the tax deductions of the related Canadian exploration expenses ("CEE") are renounced in favor of the investors. Accordingly, share capital issued through flow-through arrangements is recorded at net proceeds less the tax effect relating to the renunciation of the Company's CEE to investors.

i) Income Taxes

Future tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on future tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. Future tax assets are recorded only to the extent that, based on available evidence, it is more likely than not that they will be realized.

j) Stock Option Compensation

The Company has one stock option plan that is described in note 6d). The Company has adopted CICA Handbook Section 3870 "Stock-Based Compensation and Other Stock-Based Payments", which recommends the fair value-based method of accounting for stock-based transactions.

Avalon Ventures Ltd.

Notes to the Financial Statements

For the Years Ended August 31, 2008 and 2007

2. Summary of Significant Accounting Policies (Continued)

k) Foreign Currency Transactions

Transactions denominated in foreign currencies are recorded at the rate of exchange prevailing at the transaction date. Monetary assets and liabilities denominated in foreign currency are translated into Canadian dollars at the rate of exchange prevailing at the balance sheet date. Unrealized gains and losses on translation of monetary assets and liabilities are included in the determination of earnings for the year.

l) Related Party Transactions

All transactions with related parties are in the normal course of business and are measured at the exchange amount.

m) Share Issuance Costs

Costs incurred in connection with the issuance of share capital are netted against the proceeds received.

n) Basic and Diluted Loss per Share

The basic loss per share is computed based on the weighted average number of common shares outstanding during the year. The diluted loss per share is calculated using the treasury method, and is equal to the basic loss per share due to the anti-dilutive effect of share purchase options and warrants.

o) Comparative Figures

Certain comparative figures have been reclassified to conform with the current year's financial statement presentation.

3. Investments Available for Sale

Investments available for sale ("investments") consist of shares received as consideration for resource property interests. All investments are in publicly traded companies. The Company and Radiant Resources Inc. are related by a common director.

Effective September 1, 2006, investments are carried at fair value, any unrealized gains or losses are recognized as Other comprehensive income until the investment is disposed of, at which time any Cumulative unrealized gain or loss previously recognized in Accumulated other comprehensive income is transferred and recognized as Net income for the period.

	<u>2008</u>		<u>2007</u>	
	<u>Number</u>	<u>Amount</u>	<u>Number</u>	<u>Amount</u>
Alto Ventures Ltd.	28,571	\$ 2,143	28,571	\$ 2,571
Radiant Resources Inc.	45,000	<u>1,800</u>	45,000	<u>473</u>
		<u>\$ 3,943</u>		<u>\$ 3,044</u>

Avalon Ventures Ltd.

Notes to the Financial Statements

For the Years Ended August 31, 2008 and 2007

4. Resource Properties

August 31, 2008

	Separation Rapids Lithium- Tantalum Project	Warren Township Anorthosite Project	Thor Lake Rare Metals Project	U6 Savant Gold Project	Red Hill Copper- Zinc-Silver Project	East Kemptville Rare Metals Project	Other	Total
note	4(a)	4(b)	4(c)	4(d)	4(e)	4(f)		
Acquisition costs	\$ 1,154	\$ -	\$ -	\$ -	\$ -	\$ 991	\$ -	\$ 2,145
Community consultation	2,974	5,323	36,352	-	-	2,423	-	47,072
Diamond drilling	-	-	4,677,581	-	-	-	-	4,677,581
Environmental studies/permitting	-	1,679	82,496	-	-	-	-	84,175
Feasibility/engineering studies	5,443	1,482	32,517	-	-	52,945	-	92,387
Geochemical	-	-	-	-	-	7,972	-	7,972
Geology	4,451	1,359	367,954	-	10,021	172,850	7,272	563,907
Geophysical	-	-	11,078	-	1,813	15,550	-	28,441
Metallurgical/market studies	217,473	95,518	239,383	-	-	56,466	-	608,840
Other	12,840	1,800	24,991	-	-	9,400	-	49,031
Current expenditures	244,335	107,161	5,472,352	-	11,834	318,597	7,272	6,161,551
Balance - beginning of year	3,469,614	1,078,644	1,809,415	220,774	586,430	90,244	321	7,255,442
Write-down of resource properties	-	-	-	(220,774)	-	-	(7,593)	(228,367)
Balance - end of year	\$ 3,713,949	\$ 1,185,805	\$ 7,281,767	\$ -	\$ 598,264	\$ 408,841	\$ -	\$ 13,188,626

Avalon Ventures Ltd.

Notes to the Financial Statements

For the Years Ended August 31, 2008 and 2007

4. Resource Properties (Continued)

August 31, 2007

	Separation Rapids Lithium- Tantalum Project	Warren Township Anorthosite Project	Thor Lake Rare Metals Project	U6 Savant Gold Project	Red Hill Copper- Zinc-Silver Project	East Kemptonville Rare Metals Project	Other	Total
note	4(a)	4(b)	4(c)	4(d)	4(e)	4(f)		
Acquisition costs	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 157	\$ -	\$ 157
Diamond drilling	-	-	660,977	166,601	5,458	-	-	833,036
Environmental studies/permitting	10,607	35,391	60,450	-	-	-	-	106,448
Feasibility/engineering studies	-	-	208,167	-	-	-	-	208,167
Geology	5,434	-	181,385	6,000	-	82,246	321	275,386
Geophysical	-	-	1,425	-	94,115	1,000	-	96,540
Metallurgical/market studies	21,024	928,977	2,786	-	-	-	-	952,787
Other	1,500	-	15,422	-	-	-	-	16,922
Current expenditures	38,565	964,368	1,130,612	172,601	99,573	83,403	321	2,489,443
Balance - beginning of year	3,431,049	114,276	678,803	48,173	486,857	6,841	-	4,765,999
Balance - end of year	\$ 3,469,614	\$ 1,078,644	\$ 1,809,415	\$ 220,774	\$ 586,430	\$ 90,244	\$ 321	\$ 7,255,442

Avalon Ventures Ltd.

Notes to the Financial Statements

For the Years Ended August 31, 2008 and 2007

4. Resource Properties (Continued)

a) Separation Rapids Rare Metals Project, Ontario

Pursuant to a vested option agreement the Company owns a 100% interest (subject to a 2.0% net smelter returns royalty ("NSR"), half of which can be bought back for \$1.0 million) in certain claims in the Paterson Lake area of Ontario.

b) Warren Township Anorthosite Project, Ontario

The Company owns a 100% interest in certain claims located near Foleyet, Ontario, which were staked by the Company during the year ended August 31, 2003.

c) Thor Lake Rare Metals Project, Northwest Territories

During the year ended August 31, 2005 the Company acquired 100% interest (subject to a 5.5% NSR) in five mining leases covering the Thor Lake rare metals deposit located in the Mackenzie Mining District of the Northwest Territories.

d) U6 Savant Gold Project, Ontario

During the year ended August 31, 2005 the Company entered into an option agreement with Teck Cominco Limited ("Teck Cominco") to acquire a 100% interest (subject to a 2.0% NSR and certain back-in-rights) in certain claims located in the Savant Lake area of northwestern Ontario.

During the year ended August 31, 2008 the Company decided not to fund any further expenditures on the project, and the total costs incurred to date of \$220,774 have been written off.

e) Red Hill Copper-Zinc-Silver Project, British Columbia

During the year ended August 31, 2005 the Company entered into an option agreement with Teck Cominco to acquire a 100% interest (subject to a 2.0% NSR and certain back-in-rights) in Teck Cominco's Red Hill Copper-Zinc-Silver property located in the Kamloops Mining Division of British Columbia. To vest its 100% interest in the property, the Company must incur \$1,200,000 exploration expenditures by December 31, 2008 (of which \$631,855 (actual expenditures of \$574,414 plus notional project management fees of \$57,441) had been incurred by August 31, 2008). The Company will not meet this commitment and has requested an extension from Teck Cominco.

Teck Cominco retains the right to reacquire a 65% interest in the property, first by incurring exploration expenditures on the property equal to two and one half times the Company's expenditures to a maximum of \$3,000,000 to earn a 51% interest, then by completing a feasibility study on the property at Teck Cominco's sole cost to earn an additional 14% interest. Upon delivery of a positive feasibility study, Teck Cominco can increase its interest to 70% by arranging all the project financing required to bring a mine into production.

Avalon Ventures Ltd.

Notes to the Financial Statements

For the Years Ended August 31, 2008 and 2007

4. Resource Properties (Continued)

- f) East Kemptville Rare Metals Project, Nova Scotia

During the year ended August 31, 2007 the Company was granted a special exploration licence to search and prospect for all minerals except for coal, salt, potash and uranium within 4 claims totalling approximately 880 acres in the East Kemptville area of Yarmouth, Nova Scotia. In order to keep the licence in good standing, the Company must incur \$2,250,000 in exploration expenditures by July 31, 2010, of which \$325,694 had been incurred by August 31, 2008.

The Company also has ten regular exploration licences for 387 additional claims totalling approximately 15,480 acres in the same proximity to the claims covered under the special exploration licence.

- g) Resource properties written down during the years ended August 31, 2008 and 2007 consist of the following:

	<u>2008</u>	<u>2007</u>
U6 Savant Gold Project	\$ 220,774	\$ -
General Exploration	7,593	-
	<u>\$ 228,367</u>	<u>\$ -</u>

- h) Other Resource Properties

The Company has a 100% interest in several mining claims in the Lilypad Lakes Tantalum Property, a 2.0% NSR interest in certain mining claims of the East Cedartree Gold Property located near Kenora, Ontario, and a 0.4% NSR interest in the Wolf Mountain Platinum-Palladium Project.

5. Property, Plant and Equipment

	<u>2008</u>			<u>2007</u>		
	<u>Cost</u>	<u>Accumulated Amortization</u>	<u>Net</u>	<u>Cost</u>	<u>Accumulated Amortization</u>	<u>Net</u>
Computer equipment	\$ 25,520	\$ 14,360	\$ 11,160	\$ 23,646	\$ 9,978	\$ 13,668
Computer software	7,395	3,287	4,108	7,395	1,233	6,162
Exploration equipment	183,590	56,417	127,173	58,346	28,753	29,593
Office furniture and equipment	18,866	3,651	15,215	5,912	739	5,173
Leasehold improvements	18,963	5,689	13,274	18,963	1,896	17,067
	<u>\$ 254,334</u>	<u>\$ 83,404</u>	<u>\$ 170,930</u>	<u>\$ 114,262</u>	<u>\$ 42,599</u>	<u>\$ 71,663</u>

Avalon Ventures Ltd.

Notes to the Financial Statements
For the Years Ended August 31, 2008 and 2007

6. Share Capital

a) Issued and Outstanding:

	2008		2007	
	Number	Amount	Number	Amount
Common Shares				
Balance - beginning of year	52,128,123	\$ 25,645,316	47,602,598	\$22,980,488
Issued pursuant to:				
private placement(s)	10,360,000	15,248,752	1,500,000	1,440,000
exercise of warrants	1,414,125	1,640,312	1,925,525	1,052,818
exercise of options	747,500	480,820	1,100,000	679,160
Finder's fee paid	-	-	-	(18,900)
Commission and advisory fees paid	-	(1,013,076)	-	-
Commission – agents' compensation				
options issued	-	(384,597)	-	-
Issuance costs paid	-	(211,525)	-	-
Tax effect on issuance of flow-through shares	-	(1,373,500)	-	(488,250)
Balance - end of year	<u>64,649,748</u>	<u>40,032,502</u>	<u>52,128,123</u>	<u>25,645,316</u>
Warrants				
Balance - beginning of year	1,489,125	338,342	2,664,650	537,034
Issued pursuant to				
private placement(s)	3,805,000	1,634,248	750,000	135,000
Exercised	(1,414,125)	(322,543)	(1,925,525)	(333,692)
Cancelled/Expired	(75,000)	(15,799)	-	-
Commission and advisory fees paid	-	(108,574)	-	-
Commission – agents' compensation				
options issued	-	(41,123)	-	-
Issuance costs paid	-	(22,670)	-	-
Balance - end of year	<u>3,805,000</u>	<u>1,461,881</u>	<u>1,489,125</u>	<u>338,342</u>
Stock Options				
Balance - beginning of year	3,900,000	927,002	3,075,000	715,512
Granted	1,175,000	153,441	2,200,000	440,260
Exercised	(747,500)	(215,320)	(1,100,000)	(265,160)
Cancelled/Expired	-	-	(275,000)	(10,918)
Fair value of options recognized relating to previous option grants	-	488,017	-	47,308
Balance - end of year	<u>4,327,500</u>	<u>1,353,140</u>	<u>3,900,000</u>	<u>927,002</u>
Agents' Compensation Options				
Balance - beginning of year	-	-	-	-
Granted to agents	<u>725,000</u>	<u>425,720</u>	-	-
Balance – end of year	<u>725,000</u>	<u>425,720</u>	-	-
		<u>\$ 43,273,243</u>		<u>\$26,910,660</u>

Avalon Ventures Ltd.

Notes to the Financial Statements

For the Years Ended August 31, 2008 and 2007

6. Share Capital (Continued)

During the year ended August 31, 2008 the Company:

- i) completed a private placement (the "Offering") comprised of the issuance of 7,610,000 units (the "Units") at a price of \$1.55 per Unit and 2,750,000 flow-through common shares at a price of \$1.85 per share (of which 75,000 flow-through common shares were issued to directors and officers of the Company) for gross proceeds of \$16,883,000. Each Unit consisted of one common share and one-half of one common share purchase warrant. Each whole warrant entitles the holder to purchase one common share at an exercise price of \$2.00 per share until May 22, 2009.

The estimated fair value of the warrants totalled \$1,634,248 and this amount has been allocated to the warrant component of the Units.

In consideration for the services of the agents of the Offering, the Company paid commissions and advisory fees of \$1,121,650 in cash and granted compensation options to the agents to acquire up to 725,000 Units (the "Agents' Compensation Options") at a price of \$1.55 per Unit, exercisable until November 22, 2009. Any warrants issued pursuant to the exercise of the Agent's Compensation Options will expire on May 22, 2009. No warrants will be issued upon any exercise of the Agent's Compensation Options after May 22, 2009.

The estimated fair value of the Agents' Compensation Options totalled \$425,720. The fair values of the Agents' Compensation Options were estimated using the Black-Scholes pricing model, with the following assumptions: expected dividend yield of Nil; risk free interest rate of 3.70%; expected life of 2.0 years; and expected volatility of 65%.

The Company also paid other cash issuance costs of \$234,195 in connection with the Offering.

The total transaction costs of \$1,781,565 (including cash commissions and advisory fees, the estimated fair value of the Agents' Compensation Options and other cash issuance costs) has been allocated to the common shares and the warrants on a pro rata basis based on the fair values of the common shares and the warrants.

- ii) issued 1,414,125 non-flow-through common shares pursuant to the exercise of an equivalent number of common share purchase warrants for cash proceeds of \$1,317,769. The estimated fair value at issuance of these warrants was \$322,543, and this amount has been added to the recorded value of the issued shares.
- iii) issued 747,500 non-flow-through common shares pursuant to the exercise of an equivalent number of stock options for cash proceeds of \$265,500. The estimated fair value at issuance of these options was \$215,320, and this amount has been added to the recorded value of the issued shares.

During the year ended August 31, 2007 the Company:

- i) issued 1,500,000 flow-through units for proceeds of \$1,575,000 (of which 525,000 units were issued to directors and officers). Each unit consists of one flow-through common share and one-half of one non-transferable share purchase warrant, each whole warrant entitles the holder to purchase one non-flow-through common share at a price of \$1.35 per share until December 28, 2007.

Avalon Ventures Ltd.

Notes to the Financial Statements
For the Years Ended August 31, 2008 and 2007

6. Share Capital (Continued)

In connection with this private placement, the Company paid a finder's fee of \$18,900 in cash, which has been allocated to the common shares.

The estimated fair value of the warrants totalled \$135,000, and this amount has been allocated to the warrant component of the units.

- ii) issued 1,925,525 non-flow-through common shares pursuant to the exercise of an equivalent number of common share purchase warrants for cash proceeds of \$719,126. The estimated fair value of these warrants at issuance was \$333,692, and this amount had been added to the recorded value of the issued shares.
- iii) issued 1,100,000 non-flow-through common shares pursuant to the exercise of an equivalent number of stock options for cash proceeds of \$414,000. The estimated fair value at issuance of these options was \$265,160, and this amount had been added to the recorded value of the issued shares.

The fair values of the warrants were estimated on the issuance date using the Black-Scholes pricing model, with the following weighted average assumptions:

	<u>2008</u>	<u>2007</u>
Expected dividend yield	Nil	Nil
Risk-free interest rate	3.63%	3.96%
Expected life	1.5 years	1.0 year
Expected volatility	62%	77%

Warrant pricing models require the input of highly subjective assumptions including the expected price volatility. Changes in the subjective input assumptions can materially affect the fair value estimate, and therefore, the existing models do not necessarily provide a reliable measure of the fair value of the Company's warrants.

The Company incurred Part XII.6 interest expense of \$83,041 (2007 - \$32,275) on the monthly unspent portions of the proceeds from its flow-through financings. This amount has been included in the interest and financing costs.

b) Common and Preferred Shares

The Company is presently authorized to issue an unlimited number of common shares without par value. The Company is also authorized to issue up to 25,000,000 preferred shares without par value, of which none have been issued.

c) Warrants

As at August 31, 2008 the Company had 3,805,000 non-flow-through warrants outstanding. Each warrant entitles the holder to purchase one common share at \$2.00 per share and expires on May 22, 2009.

Avalon Ventures Ltd.

Notes to the Financial Statements

For the Years Ended August 31, 2008 and 2007

6. Share Capital (Continued)

During the years ended August 31, 2008 and 2007, warrants were issued, exercised and expired/cancelled as follows:

	2008		2007	
	Number of Warrants	Weighted Average Exercise	Number of Warrants	Weighted Average Exercise
Balance - beginning of year	1,489,125	\$ 0.94	2,664,650	\$ 0.41
Issued	3,805,000	2.00	750,000	1.35
Exercised	(1,414,125)	0.93	(1,925,525)	0.37
Expired/Cancelled	(75,000)	1.08	-	-
Balance - end of year	<u>3,805,000</u>	<u>\$ 2.00</u>	<u>1,489,125</u>	<u>\$ 0.94</u>

d) Stock Option Plan

The shareholders have approved a Stock Option Plan (the "Plan") that provides for the issue of up to 10% of the number of issued and outstanding common shares of the Company to eligible employees, directors and service providers of the Company.

The Plan authorizes the granting of options to purchase shares of the Company's common stock at an option price equal to or greater than the closing price of the shares for either the trading day prior to the grant, or the day of the grant. The options generally vest over a period of one to four years, and have a maximum term of 10 years.

During the years ended August 31, 2008 and 2007, stock options were granted, exercised and expired/cancelled as follows:

	2008		2007	
	Number of Options	Weighted Average Exercise	Number of Options	Weighted Average Exercise
Balance - beginning of year	3,900,000	\$ 0.91	3,075,000	\$ 0.43
Granted	1,175,000	1.35	2,200,000	1.31
Exercised	(747,500)	0.36	(1,100,000)	0.38
Expired/Cancelled	-	-	(275,000)	0.82
Balance - end of year	<u>4,327,500</u>	<u>\$ 1.13</u>	<u>3,900,000</u>	<u>\$ 0.91</u>
Vested options included in end of year balance above	<u>2,133,750</u>	<u>\$ 0.87</u>	<u>2,200,000</u>	<u>\$ 0.52</u>

Avalon Ventures Ltd.

Notes to the Financial Statements

For the Years Ended August 31, 2008 and 2007

6. Share Capital (Continued)

During the year ended August 31, 2008 the Company granted:

- i) 175,000 stock options to a newly appointed director of the Company and 50,000 stock options to an existing director of the Company. Each option entitles the holder to purchase one common share of the Company at a price of \$1.82 per share until November 27, 2012. These options vest at the rate of 25% every twelve months following November 27, 2007. The estimated fair value of these options totalled \$254,948 and this amount is being amortized and expensed as stock-based compensation over the vesting terms. As August 31, 2008, \$47,803 had been recognized and recorded as stock-based compensation expense.
- ii) an aggregate of 500,000 stock options to the Company's directors, officers and members of the company's advisory committee. Each option entitles the holder to purchase one common share of the Company at a price of \$1.20 per share until April 21, 2013. These options vest at the rate of 25% every twelve months following April 21, 2008. The estimated fair value of these options totalled \$340,900 and this amount is being amortized and expensed as stock-based compensation over the vesting terms. As August 31, 2008, \$31,033 had been recognized and recorded as stock-based compensation expense.
- iii) an aggregate of 200,000 stock options to two consultants of the Company. Each option entitles the holder to purchase one common share of the Company at a price of \$1.20 per share until April 21, 2010. These options vest at the rate of 25% every three months following April 21, 2008. As at August 31, 2008, 72,280 options had been earned. The estimated fair value of these options totalled \$58,294, and this amount had been recorded as stock-based compensation expense.
- iv) 200,000 stock options to an employee of the Company. Each option entitles the holder to purchase one common share of the Company at a price of \$1.24 per share until May 8, 2013. These options vest at the rate of 25% every twelve months following May 8, 2008. The estimated fair value of these options totalled \$165,860 and this amount is being amortized and expensed as stock-based compensation over the vesting terms. As August 31, 2008, \$13,070 had been recognized and recorded as stock-based compensation expense.
- v) 50,000 stock options to a consultant of the Company. Each option entitles the holder to purchase one common share of the Company at a price of \$1.80 per share until July 10, 2010. These options vest at the rate of 25% every three months following July 10, 2008. As at August 31, 2008, 7,065 options had been earned. The estimated fair value of these options totalled \$3,241, and this amount had been recorded as stock-based compensation expense.

During the year ended August 31, 2008, the Company also recorded stock-based compensation expense of \$488,017 related to previously granted stock options with graded vesting schedules which were earned during the year ended August 31, 2008.

Avalon Ventures Ltd.

Notes to the Financial Statements

For the Years Ended August 31, 2008 and 2007

6. Share Capital (Continued)

The fair value of stock options granted to employees and directors during the year ended August 31, 2008 was estimated at the grant date and the options to service providers were estimated at the service completion date based on the Black-Scholes pricing model, using the following weighted average assumptions:

	<u>2008</u>	<u>2007</u>
Expected dividend yield	Nil	Nil
Risk-free interest rate	3.34%	4.20%
Expected life	3.9 years	4.2 years
Expected volatility	77%	84%

Option pricing models require the input of highly subjective assumptions including the expected price volatility. Changes in the subjective input assumptions can materially affect the fair value estimate, and therefore, the existing models do not necessarily provide a reliable measure of the fair value of the Company's stock options.

As at August 31, 2008 the following options were outstanding:

<u>Option Price</u>	<u>Number of Options</u>		<u>Weighted Average Remaining Contractual Life</u>
	<u>Unvested</u>	<u>Vested</u>	
\$ 1.82	225,000	-	4.2 years
\$ 1.80	237,500	62,500	3.6 years
\$ 1.61	393,750	381,250	2.8 years
\$ 1.30	-	100,000	0.5 years
\$ 1.24	200,000	-	4.7 years
\$ 1.20	837,500	112,500	3.7 years
\$ 1.08	-	150,000	2.8 years
\$ 0.98	300,000	100,000	3.4 years
\$ 0.80	-	300,000	3.1 years
\$ 0.69	-	200,000	2.5 years
\$ 0.48	-	225,000	2.2 years
\$ 0.25	-	502,500	0.5 years
	<u>2,193,750</u>	<u>2,133,750</u>	

e) Agents' Compensation Options

As at August 31, 2008, the Company had 725,000 non-transferable Agents' Compensation Options issued and outstanding. Each Agents' Compensation Option entitles the agent to purchase one Unit at a price of \$1.55 per Unit, exercisable until November 22, 2009. Each Unit will consist of one common share and one-half of one common share purchase warrant. Each whole warrant entitles the holder to purchase one common share at an exercise price of \$2.00 per share until May 22, 2009. No warrants will be issued upon any exercise of the Agents' Compensation Options after May 22, 2009.

Avalon Ventures Ltd.

Notes to the Financial Statements

For the Years Ended August 31, 2008 and 2007

7. Contributed Surplus

Contributed surplus consists of expired warrants and options. The changes in contributed surplus during the years ended August 31, 2008 and 2007 are summarized as follows:

	<u>2008</u>	<u>2007</u>
Balance - beginning of year	\$ 38,376	27,458
Expired warrants	15,799	-
Expired options	-	10,918
	<hr/>	<hr/>
Balance - end of year	\$ 54,175	\$ 38,376

8. Accumulated Other Comprehensive Loss

Accumulated other comprehensive loss consists of the unrealized losses on the Company's investments available for sale. The changes during the years ended August 31, 2008 and 2007 are summarized below:

	<u>2008</u>	<u>2007</u>
Balance - beginning of year	\$ (9,099)	\$ -
Change in unrealized gains (losses) on investments available for sale	899	(9,099)
	<hr/>	<hr/>
Balance - end of year	\$ (8,200)	\$ (9,099)

9. Recoveries of Resource Properties

During the year ended August 31, 2008, the Company sold the technical data files related to one of its abandoned properties to a third party for cash proceeds of \$10,000.

10. Related Party Transactions

- a) During the year ended August 31, 2008 the Company incurred consulting fees of \$9,750 (2007 - \$54,500) with an officer and director, which were deferred as resource property costs. As at August 31, 2008 accounts payable included \$Nil (2007 - \$8,401) payable to this officer and director.
- b) During the year ended August 31, 2008 the Company incurred accounting fees of \$72,000 (2007 - \$32,193) with an accounting firm in which an officer is the principal. As at August 31, 2008 accounts payable included \$27,133 (2007 - \$19,588) payable to this accounting firm.
- c) During the year ended August 31, 2008 the Company incurred consulting fees of \$125,300 (2007 - \$22,750) with a company owned by an officer of the Company, which were deferred as resource property costs. As at August 31, 2008 accounts payable included \$16,170 payable to this company (2007 - \$8,533).

Additional related party transactions are described separately in note 6(a).

Avalon Ventures Ltd.

Notes to the Financial Statements
For the Years Ended August 31, 2008 and 2007

11. Income Taxes

a) Future Income Tax Assets

The tax effects of temporary differences that give rise to significant portions of the future income tax assets and liabilities at August 31, 2008 and 2007 are as follows:

	<u>2008</u>	<u>2007</u>
Difference in resource properties	\$ 510,378	\$ 1,698,555
Difference in investments available for sale	33,624	38,884
Difference in property, plant and equipment	25,484	16,609
Non-capital loss carry forwards	354,552	144,533
Capital loss carry forwards	240,345	275,951
Non-refundable investment tax credit carry forwards	441,074	369,388
	<u>1,605,457</u>	<u>2,543,920</u>
Less: valuation allowance	<u>(1,605,457)</u>	<u>(2,543,920)</u>
Net future income tax assets	<u>\$ -</u>	<u>\$ -</u>

A valuation allowance has been applied against all of the above future income tax assets.

b) Non-Capital Losses

The Company has non-capital losses carried forward of approximately \$1,313,000 (2007 - \$466,000) available to reduce future years' taxable income. These losses will expire as follows:

2009	\$ 15,000
2010	19,000
2014	40,000
2015	4,000
2026	156,000
2027	232,000
2028	847,000

c) Capital Losses

The Company has capital losses carried forward of approximately \$1,800,000 (2007 - \$1,800,000) available to reduce future years' capital gains.

d) Canadian Exploration and Development Expenses

The Company has cumulative Canadian development expenses of \$3,179,000 (2007 - \$3,187,000) and cumulative Canadian exploration expenses of \$10,913,000 (2007 - \$8,918,000) available to reduce future years' taxable income.

e) Scientific Research and Experimental Expenditures ("SR&ED")

The Company has SR&ED expenditures carry forward of \$964,000 (2007 - \$614,000) available to reduce future years' taxable income.

Avalon Ventures Ltd.

Notes to the Financial Statements
For the Years Ended August 31, 2008 and 2007

11. Income Taxes (Continued)

f) Non-refundable Investment Tax Credits

The Company has non-refundable investment tax credits of \$441,074 (2007 - \$369,388) available to reduce future years' federal income tax payable. These credits will expire as follows:

2018	\$ 43,866
2019	72,006
2020	14,159
2024	23,855
2025	19,486
2026	62,818
2027	133,198
2028	71,686

g) Future Income Tax Recoveries

During year ended August 31, 2008 the Company renounced CEE of \$5,087,500 (2007 - \$1,575,000) to the investors in the flow-through private placement completed in November, 2007.

This renunciation resulted in a reduction of the Company's future income tax assets of \$1,373,500 (2007 - \$488,250) and a corresponding reduction in share capital. However, as the Company has not recognized its future income tax assets, the \$1,373,500 (2007 - \$488,250) is recorded as a future income tax recovery on the statement of operations.

12. Financial Instruments

Fair Values

Except as disclosed elsewhere in these financial statements, the carrying amounts for the Company's financial instruments approximate their fair values because of the short-term nature of these items.

Credit Risk

The Company monitors the financial condition of its venture partners and counterparties to contracts. The Company does not have a significant exposure to any individual third party. Credit risk on amounts receivable is limited to the outstanding balance of such amounts.

13. Commitments

The Company has a standby letter of credit of \$76,580 for its closure plan at Separation Rapids related to the Company's advanced exploration permit, which is secured by a guaranteed investment certificate for the same amount.

The Company is required to incur CEE of \$5,087,500 by December 31, 2008 in accordance with the terms of the flow-through private placement completed in November, 2007, of which \$4,371,393 had been incurred as at August 31, 2008.

Avalon Ventures Ltd.

Notes to the Financial Statements

For the Years Ended August 31, 2008 and 2007

14. Lease Commitments

The Company has an operating lease for its office premises, the minimum lease commitments under this lease are as follows:

2009	\$ 88,858
2010	88,858
2011	88,858
2012	29,619

15. Recent Accounting Pronouncements

Recent accounting pronouncements issued and not yet effective:

Capital Disclosures

CICA Handbook Section 1535, Capital Disclosures, requires disclosure of an entity's objectives, policies and processes for managing capital, quantitative data about what the entity regards as capital and whether the entity has complied with any capital requirements and, if it has not complied, the consequences of such non-compliance. This standard is effective for the Company for the interim and annual financial statements beginning on September 1, 2008. The Company has not yet determined the impact that the adoption of this change will have on the disclosure in its financial statements.

Financial Instruments Disclosures

CICA Handbook Section 3862, Financial Instruments - Disclosures, increases the disclosures currently required that will enable the users to evaluate the significance of financial instruments for an entity's financial position and performance, including disclosures about fair value. In addition, disclosure is required of qualitative and quantitative information about exposure to risks arising from financial instruments, including specified minimum disclosures about liquidity risk and market risk. The quantitative disclosures must also include a sensitivity analysis for each type of market risk to which an entity is exposed, showing how net income and other comprehensive income would have been affected by reasonably possible changes in the relevant risk variable. This standard is effective for the Company for the interim and annual financial statements beginning on September 1, 2008. The Company has not yet determined the impact that the adoption of this change will have on the disclosure in its financial statements.

Financial Instruments Presentation

CICA Handbook Section 3863, Financial Instruments - Presentation, replaces the existing requirements on presentation of financial instruments which have been carried forward unchanged to this new section. This standard is effective for the Company for the interim and annual financial statements beginning on September 1, 2008. The Company does not expect the adoption of this standard to have a material impact on presentation in its financial statements.

Avalon Ventures Ltd.

Notes to the Financial Statements

For the Years Ended August 31, 2008 and 2007

15. Recent Accounting Pronouncements (Continued)

International Financial Reporting Standards (“IFRS”)

The CICA plans to incorporate IFRS into the CICA Handbook as a replacement for current Canadian Generally Accepted Accounting Principles for most publicly accountable enterprises effectively for fiscal years beginning on or after January 1, 2011. The transition date of September 1, 2011 for the Company will require restatement for comparative purposes of amounts reported by the Company for the year ended August 31, 2010. While the Company has begun assessing the adoption of IFRS for 2011, the financial reporting impact of the transition to IFRS has not been determined at this time.

16. Subsequent Event

Subsequent to the year ended August 31, 2008 the Company granted 32,000 stock options to a consultant. Each option entitles the holder to purchase one common share of the Company at a price of \$1.86 per share until September 1, 2010. These options vest at the rate of 25% every three months following September 1, 2008.