



ANNUAL GENERAL MEETING OF SHAREHOLDERS

Thursday, January 26, 2012 - 4:30 p.m. (Toronto time)
The Toronto Board of Trade - Room A/B/C/D
1 First Canadian Place, Toronto, Ontario

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Management Discussion and Analysis and Consolidated Financial Statements
for the year ended August 31, 2011



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NOTICE OF ANNUAL GENERAL MEETING OF SHAREHOLDERS

NOTICE IS HEREBY GIVEN that the annual general meeting (the "Meeting") of the shareholders of Avalon Rare Metals Inc. (the "Company") will be held at The Toronto Board of Trade, Room A/B/C/D (located on the 4th floor), 1 First Canadian Place, Toronto, Ontario, M5X 1C1 at 4:30 p.m. (Toronto time) on Thursday, January 26, 2012, for the following purposes:

- (1) to receive the audited financial statements of the Company for the financial year ended August 31, 2011 together with the report of the auditors thereon;
- (2) to elect directors of the Company for the ensuing year;
- (3) to appoint the auditors of the Company for the ensuing year and to authorize the directors of the Company to fix the remuneration of the auditors;
- (4) to approve to transact such other business as may properly be brought before the Meeting or any adjournment thereof.

Particulars of the foregoing matters are set forth in the accompanying information circular. A copy of the President's Letter and the audited financial statements of the Company as at and for the year ended August 31, 2011 and the report of the auditors of the Company thereon, also accompanies this notice of the Meeting. The directors of the Company have fixed the close of business on December 19, 2011 as the record date for the determination of the shareholders of the Company entitled to receive notice of the Meeting.

DATED at Toronto, Ontario this 21st day of December, 2011.

BY ORDER OF THE BOARD

A handwritten signature in black ink, appearing to read "DSB", is written over a horizontal line.

Donald S. Bubar
President and Chief Executive Officer

Shareholders who are unable to attend the Meeting in person are requested to complete, date, sign and return the accompanying form of proxy in the enclosed return envelope. All instruments appointing proxies to be used at the Meeting or at any adjournment thereof must be deposited with Equity Financial Trust Company, 200 University Avenue, Suite 400, Toronto, Ontario, Canada M5H 4H1, fax number: (416) 361-0470 not less than 48 hours, Saturdays, Sundays and holidays excepted, prior to the time of the holding of the Meeting or any adjournment thereof.



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INFORMATION CIRCULAR

As at and dated December 21, 2011

(Unless Otherwise Noted)

GENERAL PROXY INFORMATION

Solicitation of Proxies

This information circular (this "Information Circular") is furnished in connection with the solicitation of proxies by the management and the directors of AVALON RARE METALS INC. (the "Company") for use at the annual general meeting of the shareholders of the Company (the "Meeting") to be held at The Toronto Board of Trade, Room A/B/C/D (located on the 4th floor), 1 First Canadian Place, Toronto, Ontario, M5X 1C1 at 4:30 p.m. (Toronto time) on Thursday, January 26, 2012, and at all adjournments thereof for the purposes set forth in the accompanying notice of the Meeting (the "Notice of Meeting"). The solicitation of proxies will be made primarily by mail and may be supplemented by telephone or other personal contact by the directors, officers and employees of the Company. Directors, officers and employees of the Company will not receive any extra compensation for such activities. The Company may also retain, and pay a fee to, one or more professional proxy solicitation firms to solicit proxies from the shareholders of the Company in favour of the matters set forth in the Notice of Meeting. The Company may pay brokers or other persons holding common shares of the Company in their own names, or in the names of nominees, for their reasonable expenses for sending proxies and this Information Circular to beneficial owners of common shares and obtaining proxies therefrom. The cost of the solicitation will be borne directly by the Company.

No person is authorized to give any information or to make any representation other than those contained in this Information Circular and, if given or made, such information or representation should not be relied upon as having been authorized by the Company. The delivery of this Information Circular shall not, under any circumstances, create an implication that there has not been any change in the information set forth herein since the date hereof.

Non-Registered Shareholders

Only registered shareholders of the Company, or the persons they appoint as their proxies, are entitled to attend and vote at the Meeting. However, in many cases, common shares beneficially owned by a person (a "Non-Registered Shareholder") are registered either:

- (a) in the name of an intermediary (an "Intermediary") with whom the Non-Registered Shareholder deals in respect of the common shares (Intermediaries include, among others: banks, trust companies, securities dealers or brokers, trustees or administrators of a self-administered registered retirement savings plan, registered retirement income fund, registered education savings plan and similar plans); or

- (b) in the name of a clearing agency (such as The Canadian Depository for Securities Limited, in Canada, and the Depository Trust Company, in the United States) of which the Intermediary is a participant.

In accordance with the requirements of National Instrument 54-101 of the Canadian Securities Administrators, the Company has distributed copies of the Notice of Meeting, this Information Circular and its form of proxy (collectively the "Meeting Materials") to the Intermediaries and clearing agencies for onward distribution to Non-Registered Shareholders. Intermediaries are required to forward the Meeting Materials to Non-Registered Shareholders unless the Non-Registered Shareholders have waived the right to receive them. Intermediaries often use service companies to forward the Meeting Materials to Non-Registered Shareholders. Generally, Non-Registered Shareholders who have not waived the right to receive Meeting Materials will either:

- (a) be given a voting instruction form **which is not signed by the Intermediary** and which, when properly completed and signed by the Non-Registered Shareholder and **returned to the Intermediary or its service company**, will constitute voting instructions (often called a "voting instruction form"), which the Intermediary must follow. Typically, the voting instruction form will consist of a one page pre-printed form. Sometimes, instead of the one page pre-printed form, the voting instruction form will consist of a regular printed proxy form accompanied by a page of instructions which contains a removable label with a bar-code and other information. In order for the form of proxy to validly constitute a voting instruction form, the Non-Registered Shareholder must remove the label from the instructions and affix it to the form of proxy, properly complete and sign the form of proxy and submit it to the Intermediary or its service company in accordance with the instructions of the Intermediary or its service company; or
- (b) be given a form of proxy **which has already been signed by the Intermediary** (typically by a facsimile, stamped signature), which is restricted as to the number of common shares beneficially owned by the Non-Registered Shareholder but which is otherwise not completed by the Intermediary. Because the Intermediary has already signed the form of proxy, this form of proxy is not required to be signed by the Non-Registered Shareholder when submitting the proxy. In this case, the Non-Registered Shareholder who wishes to submit a proxy should properly complete the form of proxy and deposit it with **Equity Financial Trust Company, 200 University Avenue, Suite 400, Toronto, Ontario, Canada M5H 4H1.**

In either case, the purpose of these procedures is to permit Non-Registered Shareholders to direct the voting of the common shares they beneficially own. Should a Non-Registered Shareholder who receives either a voting instruction form or a form of proxy wish to attend the Meeting and vote in person (or have another person attend and vote on behalf of the Non-Registered Shareholder), the Non-Registered Shareholder should strike out the names of the persons named in the form of proxy and insert the Non-Registered Shareholder's (or such other person's) name in the blank space provided or, in the case of a voting instruction form, follow the directions indicated on the form. **In either case, Non-Registered Shareholders should carefully follow the instructions of their Intermediaries and their service companies, including those regarding when and where the voting instruction form or the proxy is to be delivered.**

Appointment and Revocation of Proxies

The persons named in the form of proxy accompanying this Information Circular are directors and/or officers of the Company. A shareholder of the Company has the right to appoint a person or company (who need not be a shareholder), other than the persons whose names appear in such form of proxy, to attend and act for and on behalf of such shareholder at the Meeting and at any adjournment thereof.

Such right may be exercised by either striking out the names of the persons specified in the form of proxy and inserting the name of the person or company to be appointed in the blank space provided in the form of proxy, or by completing another proper form of proxy and, in either case, delivering the completed and executed proxy to Equity Financial Trust Company, 200 University Avenue, Suite 400, Toronto, Ontario, Canada M5H 4H1 in time for use at the Meeting in the manner specified in the Notice of Meeting.

A registered shareholder of the Company who has given a proxy may revoke the proxy at any time prior to use by: (a) depositing an instrument in writing, including another completed form of proxy, executed by such registered shareholder or by his or her attorney authorized in writing or by electronic signature or, if the registered shareholder is a corporation, by an officer or attorney thereof properly authorized, either: (i) at the principal office of the Company, 130 Adelaide Street West, Suite 1901, Toronto, Ontario, Canada M5H 3P5, not less than 48 hours, Saturdays, Sundays and holidays excepted, prior to the time of the holding of the Meeting or any adjournment thereof, (ii) with Equity Financial Trust Company, 200 University Avenue, Suite 400, Toronto, Ontario, Canada M5H 4H1, not less than 48 hours, Saturdays, Sundays and holidays excepted, prior to the time of the holding of the Meeting or any adjournment thereof, or (iii) with the chairman of the Meeting on the day of the Meeting or any adjournment thereof; (b) transmitting, by telephone or electronic means, a revocation that complies with paragraphs (i), (ii) or (iii) above and that is signed by electronic signature, provided that the means of electronic signature permits a reliable determination that the document was created or communicated by or on behalf of such shareholder or by or on behalf of his or her attorney, as the case may be; or (c) in any other manner permitted by law including attending the Meeting in person.

A Non-Registered Shareholder who has submitted a proxy may revoke it by contacting the Intermediary through which the Non-Registered Shareholder's common shares are held and following the instructions of the Intermediary respecting the revocation of proxies.

Exercise of Discretion by Proxies

The common shares represented by an appropriate form of proxy will be voted or withheld from voting on any ballot that may be conducted at the Meeting, or at any adjournment thereof, in accordance with the instructions of the shareholder thereon. **In the absence of instructions, such common shares will be voted for each of the matters referred to in the Notice of Meeting as specified thereon.**

The enclosed form of proxy, when properly completed and signed, confers discretionary authority upon the persons named therein to vote on any amendments to or variations of the matters identified in the Notice of Meeting and on other matters, if any, which may properly be brought before the Meeting or any adjournment thereof. At the date hereof, management of the Company knows of no such amendments or variations or other matters to be brought before the Meeting. However, if any other matters which are not now known to management of the Company should properly be brought before the Meeting, or any adjournment thereof, the common shares represented by such proxy will be voted on such matters in accordance with the judgment of the person named as proxy therein.

Signing of Proxy

The form of proxy must be signed by the shareholder of the Company or the duly appointed attorney of the shareholder of the Company authorized in writing or, if the shareholder of the Company is a corporation, by a duly authorized officer of such corporation. A form of proxy signed by the person acting as attorney of the shareholder of the Company or in some other representative capacity, including an officer of a corporation which is a shareholder of the Company, should indicate the capacity in which such person is signing and should be accompanied by the appropriate instrument evidencing the qualification

and authority to act of such person, unless such instrument has previously been filed with the Company. A shareholder of the Company or his or her attorney may sign the form of proxy or a power of attorney authorizing the creation of a proxy by electronic signature provided that the means of electronic signature permits a reliable determination that the document was created or communicated by or on behalf of such shareholder or by or on behalf of his or her attorney, as the case may be.

VOTING SECURITIES AND PRINCIPAL HOLDERS THEREOF

Description of Share Capital

The Company is authorized to issue an unlimited number of common shares without par value and 25,000,000 preferred shares without par value. There are 103,136,986 common shares and no preferred shares issued and outstanding at December 21, 2011.

At a General Meeting of the Company, on a show of hands, every registered shareholder present in person and entitled to vote and every proxyholder duly appointed by a registered shareholder who would have been entitled to vote shall have one vote and, on a poll, every registered shareholder present in person or represented by proxy or other proper authority and entitled to vote shall have one vote for each share of which such shareholder is the registered holder. Common shares represented by proxy will only be voted if a ballot is called for. A ballot may be requested by a registered shareholder or proxyholder present at the Meeting or required because the number of votes attached to common shares represented by proxies that are to be voted against a matter is greater than 5% of the votes that could be cast at the Meeting.

Record Date

The directors of the Company have fixed December 19, 2011 as the record date for the determination of the shareholders of the Company entitled to receive notice of the Meeting. Shareholders of the Company of record at the close of business on December 19, 2011 will be entitled to vote at the Meeting.

Ownership of Securities of the Company

To the knowledge of the directors and executive officers of the Company, no person or company beneficially owns, directly or indirectly, or exercises control or direction over, voting securities carrying more than 10% of the outstanding voting rights of the Company other than MFC Global Investment Management (U.S.), LLC, which has reported that one or more funds or client accounts managed by it hold 10,734,406 common shares representing 10.4% of the outstanding common shares of the Company.

The directors and officers of the Company collectively own or control, directly or indirectly, in the aggregate, 2,912,500 common shares, representing approximately 2.8% of the outstanding common shares as at December 21, 2011.

PARTICULARS OF MATTERS TO BE ACTED UPON

1. Presentation of Financial Statements

At the Meeting, the Chairman of the Meeting will present to shareholders the financial statements of the Company for the year ended August 31, 2011 and the auditors' report thereon.

2. Election of Directors

The board of directors of the Company (the "Board") currently consists of eight directors. The table and the notes thereto state the names of all persons nominated by management for election as directors, all other positions and offices with the Company now held by them, their principal occupations or employment for the preceding five years, the period or periods of service as directors of the Company and the number of voting securities of the Company beneficially owned, directly or indirectly, or over which control or direction is exercised by each of them as of the date hereof.

Majority Voting Policy

As part of its ongoing review of corporate governance practices, on November 22, 2011 the Board of Directors adopted a policy providing that in an uncontested election of directors, any nominee who receives a greater number of votes "withheld" than votes "for" will tender his or her resignation to the Chairman of the Board of Directors promptly following the shareholders' meeting. The Compensation, Governance and Nominating Committee ("CGN Committee") will consider the offer of resignation and will make a recommendation to the Board on whether to accept it. In the making of such recommendation, the CGN Committee will consider all factors deemed relevant by members of such Committee. The CGN Committee will be expected to recommend acceptance of the resignation except in situations where relevant factors would, in the view of the CGN Committee, warrant the applicable director continuing to serve on the Board. The Board will make its decision and announce it in a press release within 60 days following the shareholders' meeting. A director who tenders his or her resignation pursuant to this policy will not participate in that particular item of business at any meeting of the Board or the CGN Committee at which the resignation is considered.

Proxies received in favour of management will be voted FOR the election of the named nominees, unless the shareholder has specified in the proxy that the common shares are to be withheld from voting in respect thereof. Management has no reason to believe that any of the nominees will be unable to serve as a director but, if a nominee is for any reason unavailable to serve as a director, proxies in favour of management will be voted in favour of the remaining nominees and may be voted for a substitute nominee unless the shareholder has specified in the proxy that the common shares are to be withheld from voting in respect of the election of directors.

Name, Province/State and Country of Residence	Position with the Company	Principal Occupation	Director Since	Common Shares Beneficially Owned, Directly or Indirectly or Controlled *
Donald S. Bubar Ontario, Canada	President and CEO	President and CEO of the Company	February 17, 1995	1,350,000
David Connelly Northwest Territories, Canada	Director	Self-employed Businessperson since 1997.	May 10, 2010	527,500
Alan Ferry ^{(1) (2)} Ontario, Canada	Director	Chairman of the Company and Self-employed Businessperson since July 2007; prior thereto, Vice-President, Metals and Minerals for D&D Securities Company (an investment dealer).	February 24, 2000	175,000
Phil Fontaine Ontario, Canada	Director	Special Advisor to the Royal Bank of Canada; prior thereto National Chief of the Assembly of First Nations for three consecutive terms.	September 8, 2009	Nil
Brian D. MacEachen ⁽¹⁾ Nova Scotia, Canada	Director	Executive Vice President of Brigus Gold Corp. (formerly Linear Gold Corp.), a gold mining company, since October 2009 and President and CEO of Linear Metals Corporation (a mining exploration company) since January 2008; prior thereto, CFO and Vice-President of Finance of Linear Gold and Metals Corporation.	November 16, 1998	340,000
Peter McCarter ⁽²⁾ Ontario, Canada	Director	Retired since September 2007; prior thereto, Executive Vice-President, Corporate Affairs, Aur Resources Inc., (an international mining company).	November 16, 2007	30,000

Name, Province/State and Country of Residence	Position with the Company	Principal Occupation	Director Since	Common Shares Beneficially Owned, Directly or Indirectly or Controlled *
Richard Morland Northwest Territories, Canada	Director	Consulting Mining Engineer since July 2010; prior thereto, BHP Billiton Diamonds Inc. (a mining company) from 2006 in the roles of Vice President, Operations and President and Chief Operating Officer.	September 1, 2011	10,000
Hari Panday ⁽¹⁾⁽²⁾ Ontario, Canada	Director	President and CEO, PanVest Capital Corporation since December 2009; prior thereto, founding-President and CEO, Wealth Management, North America, ICICI Group from April 2008 to October 2009; founding-President and CEO, ICICI Bank Canada from March 2003 to April 2008.	January 14, 2010	10,000
Notes: * As provided by the respective director. (1) Member of the Company's Audit Committee. (2) Member of the Company's CGN Committee.				

Each director elected at the Meeting will hold office until the next annual meeting or until his successor is duly elected or appointed.

As at the date of this Information Circular, the directors and senior officers of the Company as a group, directly and indirectly, beneficially own or exercise control or direction over 2,912,500 common shares representing approximately 2.8% of the issued and outstanding common shares.

No proposed director (including any personal holding company of a proposed director):

- (a) is, as at the date of this Information Circular, or has been, within the preceding 10 years, a director, chief executive officer or chief financial officer of any company (including the Company) that:
 - (i) was the subject of a cease trade or similar order (including a management cease trade order whether or not such person was named in the order) or an order that denied the relevant company access to any exemption under securities legislation, that was in effect for a period of more than 30 consecutive days, (an "Order") that was issued while the proposed director was acting in the capacity as director, chief executive officer or chief financial officer, other than Peter McCarter, who was a director and officer of Compressario Corporation when it became subject to cease trade orders that were

issued in 2003 by the Ontario, British Columbia and Alberta Securities Commissions for failure to file financial statements; or

- (ii) was subject to an Order that was issued after the proposed director ceased to be a director, chief executive officer or chief financial officer and which resulted from an event that occurred while that person was acting in the capacity as director, chief executive officer or chief financial officer.
- (b) is, as at the date of this Information Circular, or has been, within the preceding 10 years, a director or executive officer of any company (including the Company) that, while that person was acting in that capacity, or within a year of that person ceasing to act in that capacity became bankrupt, made a proposal under any legislation relating to bankruptcy or insolvency or was subject to or instituted any proceedings, arrangement or compromise with creditors or had a receiver, receiver manager or trustee appointed to hold its assets; or
- (c) has, within the 10 years before the date of this Information Circular, become bankrupt, made a proposal under any legislation relating to bankruptcy or insolvency or become subject to or instituted any proceedings, arrangement or compromise with creditors or had a receiver, receiver manager or trustee appointed to hold the assets of the proposed director; or
- (d) has been subject to:
- (i) since December 31, 2000, any penalties or sanctions imposed by a court relating to securities legislation or by a securities regulatory authority or has entered into a settlement agreement with a securities regulatory authority or before December 31, 2000, the disclosure of which would likely be important to a reasonable securityholder in deciding whether to vote for a proposed director; or
 - (ii) any other penalties or sanctions imposed by a court or regulatory body that would likely be considered important to a reasonable securityholder in deciding whether to vote for a proposed director;

3. Appointment of Auditors

McCarney Greenwood LLP, Chartered Accountants have been the auditors of the Company since October 14, 2010. Shareholders will be asked to consider and, if thought advisable, to pass an ordinary resolution to appoint the firm of McCarney Greenwood LLP to serve as auditors of the Company until the next annual meeting of shareholders and to authorize the directors of the Company to fix their remuneration as such.

Unless the shareholder directs that his or her common shares are to be withheld from voting in connection with the appointment of auditors, the persons named in the enclosed form of proxy intend to vote FOR the appointment of McCarney Greenwood LLP, to serve as auditors of the Company until the next annual meeting of the shareholders and to authorize the directors to fix their remuneration.

OTHER MATTERS WHICH MAY COME BEFORE THE MEETING

The management knows of no matters to come before the Meeting other than as set forth in the Notice of Meeting. However, if other matters are not known to the management should properly come before the Meeting, the accompanying proxy will be voted on such matters in accordance with the best judgment of the persons voting the proxy.

STATEMENT OF EXECUTIVE COMPENSATION

A. Named Executive Officers

For the purposes of this Information Circular, a named executive officer (“Named Executive Officer”) of the Company means each of the following individuals:

- (a) a chief executive officer (“CEO”) of the Company;
- (b) a chief financial officer (“CFO”) of the Company;
- (c) each of the Company’s three most highly compensated executive officers, or the three most highly compensated individuals acting in a similar capacity, other than the CEO and CFO, at the end of the most recently completed financial year whose total compensation was individually, more than \$150,000, as determined in accordance with subsection 1.3(6) of Form 51-102F6, for that financial year; and
- (d) each individual who would be an Named Executive Officer under paragraph (c) above but for the fact that the individual was neither an executive officer of the Company, nor acting in a similar capacity, at the end of the financial year.

B. Compensation Discussion and Analysis

Compensation, Governance and Nominating Committee

The CGN Committee is responsible for making recommendations to the Board with respect to the compensation of the executive officers of the Company as well as, among other things, with respect to the Company’s Stock Option Plan (the “Option Plan”) and any other employee benefits and/or plans and with respect to directors’ compensation. The Board (exclusive of the CEO, who is also a member of the Board) reviews such recommendations and gives final approval to the compensation of the executive officers. See also Schedule A hereto - Corporate Governance Disclosure.

The CGN Committee consists of Peter McCarter (Chair), Alan Ferry and Hari Panday, all of whom are independent. The CGN Committee has not to date felt it necessary to engage any compensation consultant or advisor to assist it in its performance of its duties.

Compensation Objectives and Structure

The overall compensation objective adopted by the CGN Committee is to ensure that executive compensation is fair and reasonable, rewards management performance and is, by being competitive, sufficient to attract and retain experienced and talented executives. Due to the nature of the mining industry, executive talent has significant mobility and, as a result, competition for experienced executives has been great. The Company’s compensation policies are designed to recognize the foregoing. The

foregoing objective also recognizes the fundamental value added by a motivated and committed management team in accomplishing the Company's current principal corporate objective, being the successful development of its Nechalacho rare earths project in the Northwest Territories.

Historically, the compensation provided by the Company to its executive officers, including the CEO, has had three components: base salary, bonuses and long term incentive compensation in the form of stock options (see "Stock Option Plan"). Bonus compensation is a cash component of management compensation in order to permit the recognition of outstanding individual efforts, performance, achievements and/or accomplishments by members of the Company's management team. Any specific bonus amounts are awarded on the recommendation of the CGN Committee and ultimately at the discretion of the Board, with bonus amounts for members of the Company's management team other than the CEO being based primarily on the recommendations of the CEO. The appropriateness and amount of any bonuses to the CEO and/or management team members has to date been considered annually by the CGN Committee and Board on a discretionary basis as no formal bonus plan based on quantitative and/or qualitative benchmarks has been established for the Company as yet. However, for 2012, it is the current intention to design and implement an incentive bonus program for the Company's senior management team based on a combination of individual and Company performance objectives and/or milestones with an aggregate target payout of up to 40% of the relevant executive's base salary level should all objectives be met or exceeded. The foregoing is in furtherance of the CGN Committee's overall compensation objectives and, in particular, facilitating the hiring and retention of experienced and talented mining executives given that, in today's marketplace, such talent has significant mobility, competition within the industry for experienced executives is severe and the Company is competing for such talent against larger and more advanced entities.

Base salary is the principal component of each executive officer's overall compensation as such reflects the fixed component of pay that compensates the relevant executive officer for fulfilling his day to day role and responsibilities. In terms of the setting of base salaries, the CGN Committee annually reviews and considers the individual performance of the CEO and of each other executive officer and compares executive compensation for other companies operating in the mining industry. It is important that the Company's CEO and other members of its senior management team are paid competitive base salaries that are in keeping with that offered by comparable companies within the industry.

In setting the salary and bonus, if any, to be awarded to the CEO for each year, the CGN Committee, in addition to reviewing the peer group data, reviews the achievements of the CEO for the prior year and looks at the overall performance of the Company in terms of the achievement of its corporate objectives, including the acquisition and advancement of projects. Also typically included in such overall assessment are specific initiatives undertaken in the year by the Company that have advanced the growth and progress of the Company and the enhancement of shareholder value during the year, including the reflection of such in the Company's share price. In setting the compensation of the other executive officers of the Company, the CGN Committee reviews with the CEO, the CEO's evaluation of each executive officer's performance during the year as well as the responsibilities, experience and qualifications of such executive officer and comparable industry compensation data. Given the nature of the Company as an exploration and development stage resource company without existing mineral production and without any attendant revenues derived thereon, compensation is generally based on comparative, qualitative or subjective, rather than quantitative or objective, measures. No specific benchmarks, weights or percentages are assigned to any of the measures or objectives upon which the executive compensation is generally based.

Annual salary adjustments are made on a calendar year basis and are typically determined towards the end of each calendar year and made effective January 1 of the following year.

The CGN Committee does not believe that the Company's compensation policies and practices, given the nature of the Company's business and affairs, would serve to encourage management to take inappropriate or excessive risks.

The CGN Committee has not instituted any policies related to the purchase by directors or officers of financial instruments that are designed to hedge or offset a decrease in market value of equity securities granted as compensation or held by any director or officer.

Base Salary and Bonus

The CGN Committee, in respect of the setting of the CEO's salary for 2011, compared the CEO compensation of the Company to the most recent CEO compensation data disclosed by a peer group (the "Peer Group") of TSX listed mining companies selected by the CGN Committee. Each company selected by the CGN Committee to comprise the Peer Group had a market capitalization between \$200 million and \$500 million as at August 31, 2010 (the Company's market capitalization at the time being approximately \$240 million) and one or more mineral properties in the scoping, pre-feasibility or feasibility study stage or under development. No distinction was made on the basis of the particular commodities that were the focus of any of the Peer Group companies' efforts. The companies comprising the Peer Group consisted of Alexco Resource Corp., Augusta Resource Corporation, Banro Corporation., Copper Mountain Mining Corporation, Duluth Metals Limited, General Moly, Inc., Greystar Resources Ltd., Keegan Resources Inc., Mountain Province Diamonds Inc., Nautilus Minerals Inc., Northland Resource S.A., Polymet Mining Corp., Potash One Inc. and Sabina Gold & Silver Corp. Of the Peer Group companies, ten had a market capitalization in excess of Avalon's then market capitalization while four had a lower market capitalization. Given the Company's growing profile as a significant rare metals entity, the CGN Committee also reviewed comparative CEO remuneration data for other entities involved in the rare metals industry; however, such data wasn't found to be particularly useful from a comparative point of view given the wide range in the market capitalizations, stages of development, CEO salary levels and jurisdictions of these various entities.

The CGN Committee and the Board, before the consideration of other factors, initially targets the CEO's salary compensation to be near the average and/or median CEO salary compensation for the Peer Group companies. The 2009 salaries for the Peer Group CEO's ranged from approximately \$165,000 to approximately \$672,000, with the average salary being approximately \$336,000 and the median salary being approximately \$305,000. The CGN Committee and the Board were also cognizant of the fact that the reported Peer Group salary levels were generally for the 2009 calendar year (and would have been set in late 2008) and hence there is in effect a two year lag when being used in connection with the setting of the 2011 salary for the Company's CEO. The average of the median and average Peer Group CEO salaries for 2009 plus 5% for two years' inflation was approximately \$337,000. The CGN Committee ultimately recommended and the Board approved a salary of \$350,000 for the CEO for 2011.

A discretionary bonus of \$40,000 was awarded to the CEO for 2010. The foregoing was principally based on the Company having raised sufficient additional equity capital in 2010 to assure that sufficient funds would be on hand to carry out the bankable feasibility study on the Company's Nechalacho rare earths project. The CEO also received a bonus of \$60,000 based on the market capitalization of the Company: (i) averaging at least \$210 million on a monthly basis over the course of calendar 2010; and (ii) being at least \$210 million as at the end of the last trading day on the TSX in 2010 (the "Market Cap Bonus"). The

Market Cap Bonus entitlement was granted to the CEO in 2009 at the time of the fixing of his compensation for 2010, all as described in the Company's Information Circular dated December 14, 2010.

Discretionary bonuses of \$25,000 were awarded to each of Messrs. Andersen, Mercer and Swisher in recognition of the efforts each such individual to their respective responsibilities during 2010 and that the facilitative effect such had on the completion of the Nechalacho pre-feasibility study during the year and the consequent ability of the Company to raise the aforesaid additional equity capital in 2010.

Options

The CGN Committee is of the view that the granting of options is an appropriate method of providing long-term incentives to senior management of the Company and, in general, aligns the interests of senior management with those of the shareholders by enabling senior management to participate in and be rewarded by an increase in the market price of the Company's common shares. Participation in the Stock Option Plan also provides a significant incentive to the Participants to enter into and subsequently to continue their employment with the Company, particularly when the Company may not have the financial resources and/or pension and other benefit plans advantageous in attracting and retaining experienced personnel. In addition, the CGN Committee is of the view that the Company's compensation levels and components must be consistent with industry norms and industry norms dictate that the Company provides a long-term compensation incentive, which is best realized by providing compensation linked to share performance such as options. The number and terms of options previously granted to the named executives have been and are expected to continue to be taken into account, as well as the number and terms of options granted by the Peer Group companies, in determining whether and in what quantity new option grants should be made in any year.

The Company's current practice under the Stock Option Plan is, during any five year period, to have granted to the CEO options to purchase 1,000,000 common shares and to have granted officers at the Vice-President level options to purchase between 200,000 to 600,000 common shares.

Circumstances Triggering Termination and Change of Control Benefits

As noted below under the heading "Employment Contracts", there are certain circumstances that trigger payments and other benefits to the CEO upon termination and change of control. The CGN Committee views such provisions as not only being fair and necessary to protect the CEO and other members of the Company's senior management but also to encourage such individuals to pursue corporately advantageous transactions such as mergers or take-overs that are beneficial to the Company and its shareholders but that may result in the termination of such individual's employment with the Company.

Stock Option Plan

The Stock Option Plan, approved by shareholders on January 27, 2011, is a fixed percentage plan that provides that the maximum number of options which may be outstanding under the Stock Option Plan and any other compensation arrangement of the Company is at any time 10% of the Company's issued and outstanding common shares. Eligible participants under the Stock Option Plan include insiders or employees of the Company or any of its subsidiaries, and any other person or company engaged to provide ongoing management, consulting or advisory services to the Company.

The Company maintains the Stock Option Plan primarily in order to provide effective incentives to directors, officers and senior management personnel of the Company and to enable the Company to attract and retain experienced and talented individuals in those positions by permitting such individuals to directly participate in an increase in per share value created for the Company's shareholders.

Incentive options granted under the Stock Option Plan entitle the purchase of shares at a price and for the length of time determined by the Board provided that the price cannot be lower than the market price of the common shares on the TSX on the day prior to or on the day of the grant and the expiry date cannot be more than 10 years after the date of the grant. Further, the policies of the Toronto Stock Exchange (the "TSX") also provide that the said exercise price of any options so granted cannot be reduced without shareholder approval.

Options under the Stock Option Plan are typically granted in such numbers as reflect the level of responsibility of the particular optionee and his or her contribution to the business and activities of the Company. Options may also be granted under the Stock Option Plan to consultants. Options granted under the Stock Option Plan typically have a five year term and are typically made cumulatively exercisable by the holders thereof as to a proportionate part of the aggregate number of shares subject to the options over specified time periods. In the event a take-over bid (within the meaning of the *Securities Act* (Ontario)) is made for the common shares of the Company, then all unvested options thereupon become exercisable by the holder. Options generally terminate either immediately or within a specified time period upon an optionee's employment with the Company being terminated (unless otherwise determined by the Board or the CGN Committee) or unless such termination is a result of the death, disability or retirement, in which case termination occurs upon the expiry of 12 months from the occurrence of the relevant event (subject to the earlier expiry of the options in the normal course).

As at December 21, 2011, 6,900,250 common shares, being 6.7% of the currently issued common shares of the Company, were issuable pursuant to unexercised options granted to such date under the Stock Option Plan.

Incentives to Participants under the Stock Option Plan may also be provided by the granting of stock appreciation rights. Stock appreciation rights, which can be attached to an option at the discretion of the Company at any time, entitle a Participant in the Stock Option Plan to elect, in lieu of exercising an outstanding Option, to receive the number of common shares equivalent in value to the difference between his or her option exercise price and the then existing market value of the shares multiplied by the number of common shares over which he or she could otherwise exercise his or her option. No stock appreciation rights have been granted under the Stock Option Plan to date.

The rules of the TSX require that all unallocated options, rights or other entitlements under plans such as the Stock Option Plan must be re-approved by a majority of the relevant issuer's directors and by shareholders every three years after institution of the relevant plan. Under the policies of the TSX, if the Company wishes to make certain amendments to the Stock Option Plan, it must obtain shareholder approval.

C. Performance Graph

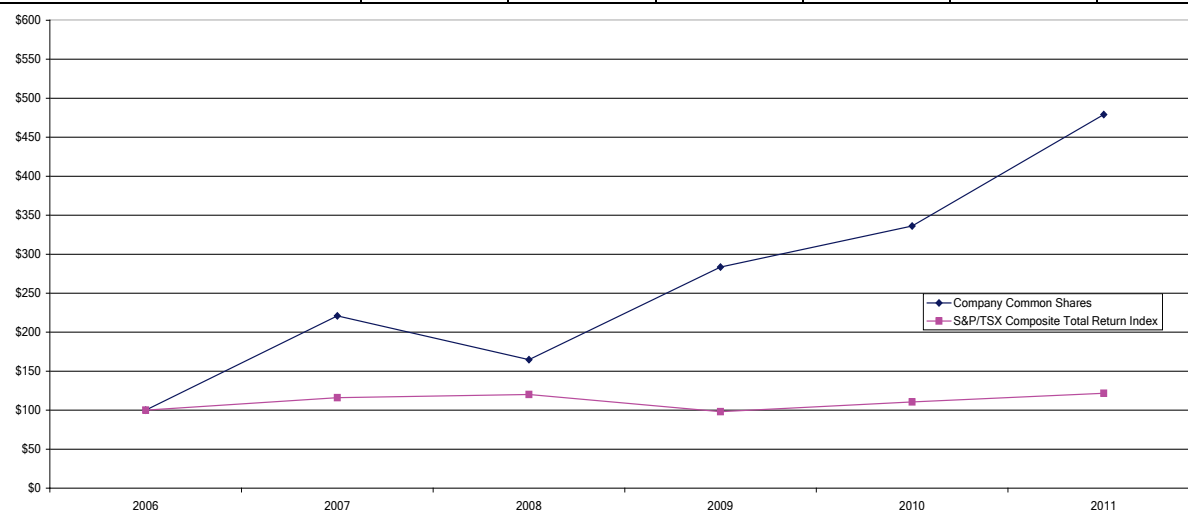
The following graph and table compares the yearly percentage change in the cumulative total shareholder return of the common shares for the period from August 31, 2006 to August 31, 2011 with the cumulative total return of the S&P/TSX Composite Total Return Index for the same period. The graph and table assume \$100 invested in common shares on August 31, 2006 and in the S&P/TSX Composite Total Return Index, which assumes dividend reinvestment.

Cumulative Total Return on \$100 Investment

There is no direct correlation between the market performance of the Company's common shares and executive compensation except that any increase in the market price of the common shares will increase the value of any options held by the relevant executives. The CGN Committee and the Board generally evaluate performance by reference to the achievement of corporate objectives rather than by short term changes in the Company's common share price, which may often be significantly influenced by overall economic, market and industry conditions. Indirectly, however, as the CGN Committee compares the executive compensation of the Company to the executive compensation paid by a peer group of companies having, among other things, comparable market capitalizations, any significant changes in the market capitalization of the Company attributable to changes in its share price affects the make-up of the peer group of companies and larger market capitalization companies typically have more generous executive salary structures.

Comparison of Cumulative Total Return

Month / Year	Aug 31, 2006	Aug 31, 2007	Aug 31, 2008	Aug 31, 2009	Aug 31, 2010	Aug 31, 2011
Avalon Rare Metals Inc.	\$100.00	\$220.88	\$164.84	\$283.52	\$336.26	\$479.12
S&P/TSX Composite Total Return Index	\$100.00	\$115.95	\$120.03	\$98.16	\$110.66	\$121.62



D. Summary Compensation Table

The table below contains a summary of the compensation paid to the Named Executive Officers' during the three most recently completed financial years.

Name and Principal Position	Year	Salary (\$)	Share based awards (\$)	Option-based awards ⁽¹⁾ (\$)	Non-Equity incentive plan compensation (\$)		Pension Value (\$)	All other compensation (\$)	Total compensation (\$)
					Annual incentive plans	Long-term incentive plans			
Donald S. Bubar ⁽²⁾ President and CEO	2011	335,000	Nil	1,782,570	100,000 ⁽³⁾	Nil	Nil	Nil	2,217,570
	2010	280,000	Nil	Nil	Nil	Nil	Nil	Nil	280,000
	2009	221,667	Nil	224,768	Nil	Nil	Nil	Nil	446,435
R. James Andersen CFO and VP, Finance	2011	140,000	Nil	1,026,940	25,000 ⁽⁴⁾	Nil	Nil	Nil	1,191,940
	2010	100,000	Nil	Nil	Nil	Nil	Nil	Nil	100,000
	2009	60,000	Nil	169,238	Nil	Nil	Nil	Nil	229,238
Brian Chandler ⁽⁵⁾ Senior VP and COO	2011	10,145	Nil	3,181,740	Nil	Nil	Nil	Nil	3,191,885
	2010	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
	2009	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
William Mercer VP, Exploration	2011	146,667	Nil	Nil	25,000 ⁽⁶⁾	Nil	Nil	56,250 ⁽⁷⁾	227,917
	2010	Nil	Nil	Nil	50,000 ⁽⁸⁾	Nil	Nil	180,923 ⁽⁷⁾	230,923
	2009	Nil	Nil	Nil	Nil	Nil	Nil	154,525 ⁽⁷⁾	154,525

Name and Principal Position	Year	Salary (\$)	Share based awards (\$)	Option-based awards ⁽¹⁾ (\$)	Non-Equity incentive plan compensation (\$)		Pension Value (\$)	All other compensation (\$)	Total compensation (\$)
					Annual incentive plans	Long-term incentive plans			
Pierre Neatby ⁽⁹⁾ VP, Sales and Marketing	2011	187,500	Nil	Nil	Nil	Nil	Nil	Nil	187,500
	2010	30,833	Nil	566,960	Nil	Nil	Nil	Nil	597,793
	2009	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Richard Pratt ⁽¹⁰⁾ VP, General Counsel and Corporate Secretary	2011	2,083	Nil	2,236,960	Nil	Nil	Nil	Nil	2,239,043
	2010	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
	2009	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
David Swisher ⁽¹¹⁾ VP, Operations	2011	191,193	Nil	Nil	25,000 ⁽⁴⁾	Nil	Nil	25,145 ⁽¹²⁾	241,338
	2010	157,092	Nil	773,800	Nil	Nil	Nil	Nil	930,892
	2009	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A

Notes:

- (1) The "grant date fair value" has been determined by using the Black-Scholes model, a mathematical valuation model that ascribes a value to a option based on a number of factors in valuing the option-based awards, including the exercise price of the option, the price of the underlying security on the date the option was granted, and assumptions with respect to the volatility of the price of the underlying security and the risk-free rate of return. Calculating the value of options using this methodology is very different from a simple "in-the-money" value calculation. In fact, options that are well out-of-the-money can still have a significant "grant date fair value" based in a Black-Scholes valuation, especially where, as in the case of the Company, the price of the common shares underlying the option is highly volatile. Accordingly, caution must be exercised in comparing grant date fair value amounts with cash compensation or an in-the-money option value calculation. The same caution applies to the total compensation amounts shown in the last column above, which are based in part the grant date fair value amounts set out in the column for option-based awards.
- (2) Mr. Bubar does not receive any additional compensation for serving as a director of the Company.
- (3) The Company paid Mr. Bubar a bonus of \$100,000 - see *Executive Compensation - Base Salary and Bonus*.
- (4) The Company paid each of Messrs. Andersen and Swisher a bonus of \$25,000 - see *Executive Compensation - Base Salary and Bonus*.
- (5) Mr. Chandler was appointed as Senior Vice-President and COO on August 22, 2011.
- (6) The Company paid Bill Mercer Geological Consulting Ltd. (a company owned by Mr. Mercer) a bonus of \$25,000 in 2010 - see *Executive Compensation - Base Salary and Bonus*.

- (7) Paid or accrued to Bill Mercer Geological Consulting Ltd. for mineral exploration consulting services pursuant to a consulting agreement dated May 1, 2007 with the Company. This consulting agreement was terminated on December 31, 2010.
- (8) The Company paid Bill Mercer Geological Consulting Ltd. a bonus of \$50,000 in 2009.
- (9) Mr. Neatby was appointed as Vice-President, Sales and Marketing of the Company on July 1, 2010.
- (10) Mr. Pratt was appointed as Vice-President, General Counsel and Corporate Secretary of the Company on August 1, 2011.
- (11) Mr. Swisher was appointed as Vice-President, Operations of the Company on November 1, 2009. In fiscal 2010, Mr. Swisher was paid a salary of US\$150,000 which was converted to C\$157,092 at an exchange rate of 1.04728 and in fiscal 2011, Mr. Swisher was paid a salary of US\$193,333 which was converted to C\$191,193 at an exchange rate of 0.9889.
- (12) Mr. Swisher (who is a US resident) was paid a tax equalization payment of \$25,415 which reflects the additional Canadian income tax paid by Mr. Swisher on his employment income earned from the Company.

E. Employment Contracts

Bubar Employment Agreement

The Company employs Donald S. Bubar as the Company's President and CEO pursuant to an employment agreement effective as of January 1, 2011 (the "Bubar Agreement"). The Bubar Agreement is for an indefinite term and can be terminated by either party. If the Bubar Agreement is terminated by Mr. Bubar, Mr. Bubar must provide at least 30 days notice and Mr. Bubar is entitled to be paid the then current salary under the Bubar Agreement prorated until the end of the notice period, and thereafter all obligations of the Company to Mr. Bubar will terminate. If the Bubar Agreement is terminated by the Company without cause, the Company will pay to Mr. Bubar a lump sum payment equal to three months of salary plus two months of salary for every full or partial year, recognizing that Mr. Bubar's employment began on March 1, 1995 to a maximum of 36 months. In the event of a change of control of the Company (as defined in the Bubar Agreement) and, if within one year of the change of control, Mr. Bubar's employment with the Company is terminated by the Company or Mr. Bubar elects to terminate the Bubar Agreement, the Company will pay to Mr. Bubar a lump sum in cash equal to three times his annual base salary amount in effect at the time.

Andersen Employment Agreement

The Company employs R. James Andersen as the Company's Vice-President, Finance and CFO pursuant to an employment agreement effective January 1, 2011 (the "Andersen Agreement"). The Andersen Agreement is for an indefinite term and can be terminated by either party. If the Andersen Agreement is terminated by Mr. Andersen, Mr. Andersen must provide at least 30 days notice and Mr. Andersen is entitled to be paid the then current salary under the Andersen Agreement prorated until the end of the notice period, and thereafter all obligations of the Company to Mr. Andersen will terminate. If the Andersen Agreement is terminated by the Company without cause, the Company will pay to Mr. Andersen a lump sum payment equal to three months of salary plus two months of salary for every full or partial year of employment, recognizing that Mr. Andersen's employment began on June 11, 2001 to a maximum of 36 months. In the event of a change of control of the Company (as defined by the Andersen Agreement) and if within one year of the change of control, Mr. Andersen's employment with the Company is terminated or in the event Mr. Bubar's employment is terminated, Mr. Andersen can elect to terminate the Andersen Agreement, and the Company will be obligated to pay to Mr. Andersen a lump sum in cash equal to 12 months of salary plus an additional two month's salary for every full or partial year of service, recognizing that Mr. Andersen's employment began on June 11, 2001 to a maximum of three times his annual base salary amount in effect at the time.

Chandler Employment Agreement

The Company employs Brian Chandler as the Company's Senior Vice-President and COO pursuant to an employment agreement effective August 22, 2011 (the "Chandler Agreement"). The Chandler Agreement is for an indefinite term and can be terminated by either party. If the Chandler Agreement is terminated by Mr. Chandler, Mr. Chandler must provide at least 30 days notice and Mr. Chandler is entitled to be paid the then current salary under the Chandler Agreement prorated until the end of the notice period, and thereafter all obligations of the Company to Mr. Chandler will terminate. If the Chandler Agreement is terminated by the Company without cause, the Company will pay to Mr. Chandler a lump sum payment equal to three months of salary plus one month of salary for every full or partial year of employment, recognizing that Mr. Chandler's employment began on August 22, 2011 to a maximum of 24 months. In the event of a change of control of the Company (as defined by the Chandler Agreement) and if within one year of the change of control, Mr. Chandler's employment with the Company is terminated by the Company, the Company will pay to Mr. Chandler a lump sum in cash equal to 12 months of salary plus an additional one month's salary for every full or partial year of employment, recognizing that Mr. Chandler's employment began on August 22, 2011 to a maximum of 24 months.

Mercer Employment Agreement

The Company employs William Mercer as the Company's Vice-President Exploration pursuant to an employment agreement effective January 1, 2011 (the "Mercer Agreement"). The Mercer Agreement is for an indefinite term and can be terminated by either party. If the Mercer Agreement is terminated by Mr. Mercer, Mr. Mercer must provide at least 30 days notice and Mr. Mercer is entitled to be paid the then current salary under the Mercer Agreement prorated until the end of the notice period, and thereafter all obligations of the Company to Mr. Mercer will terminate. If the Mercer Agreement is terminated by the Company without cause, the Company will pay to Mr. Mercer a lump sum payment equal to three months of salary plus one month of salary for every full or partial year, recognizing that Mr. Mercer's employment began on January 1, 2011 to a maximum of 24 months. In the event of a change of control of the Company (as defined in the Mercer Agreement) and if within one year of the change of control, Mr. Mercer's employment with the Company is terminated by the Company, the Company will pay to Mr. Mercer a lump sum in cash equal to 12 months of salary plus an additional one month's salary for every full or partial year of employment, recognizing that Mr. Mercer's employment began on January 1, 2011 to a maximum of 24 months.

Neatby Employment Agreement

The Company employs Pierre Neatby as the Company's Vice-President Sales and Marketing pursuant to an employment agreement effective January 1, 2011 (the "Neatby Agreement"). The Neatby Agreement is for an indefinite term and can be terminated by either party. If the Neatby Agreement is terminated by Mr. Neatby, Mr. Neatby must provide at least 30 days notice and Mr. Neatby is entitled to be paid the then current salary under the Neatby Agreement prorated until the end of the notice period, and thereafter all obligations of the Company to Mr. Neatby will terminate. If the Neatby Agreement is terminated by the Company without cause, the Company will pay to Mr. Neatby a lump sum payment equal to three months of salary plus one month of salary for every full or partial year, recognizing that Mr. Neatby's employment began on July 1, 2010 to a maximum of 24 months. In the event of a change of control of the Company (as defined in the Neatby Agreement) and if within one year of the change of control, Mr. Neatby's employment with the Company is terminated by the Company, the Company will pay to Mr. Neatby a lump sum in cash equal to 12 months of salary plus an additional one month's salary for every full or partial year of service, recognizing that Mr. Neatby's employment began on July 1, 2010 to a maximum of 24 months.

Pratt Employment Agreement

The Company employs Richard Pratt as the Company's Vice-President, Corporate Counsel and Corporate Counsel pursuant to an employment agreement effective August 1, 2011 (the "Pratt Agreement"). The Pratt Agreement is for an indefinite term and can be terminated by either party. If the Pratt Agreement is terminated by Mr. Pratt, Mr. Pratt must provide at least 30 days notice and Mr. Pratt is entitled to be paid the then current salary under the Pratt Agreement prorated until the end of the notice period, and thereafter all obligations of the Company to Mr. Pratt will terminate. If the Pratt Agreement is terminated by the Company without cause, the Company will pay to Mr. Pratt a lump sum payment equal to three months of salary plus one month of salary for every full or partial year, recognizing that Mr. Pratt's employment began on August 1, 2011 to a maximum of 24 months. In the event of a change of control of the Company (as defined in the Pratt Agreement) and if within one year of the change of control, Mr. Pratt's employment with the Company is terminated by the Company, the Company will pay to Mr. Pratt a lump sum in cash equal to 12 months of salary plus an additional one month's salary for every full or partial year of service, recognizing that Mr. Pratt's employment began on August 1, 2011 to a maximum of 24 months.

Swisher Employment Agreement

The Company employs David Swisher as the Company's Vice-President Operations pursuant to an agreement effective January 1, 2011 (the "Swisher Agreement"). The Swisher Agreement is for an indefinite term and can be terminated by either party. If the Swisher Agreement is terminated by Mr. Swisher, Mr. Swisher must provide at least 30 days notice and Mr. Swisher is entitled to be paid the then current salary under the Swisher Agreement prorated until the end of the notice period, and thereafter all obligations of the Company to Mr. Swisher will terminate. If the Swisher Agreement is terminated by the Company without cause, the Company will pay to Mr. Swisher a lump sum payment equal to three months of salary plus one month of salary for every full or partial year, recognizing that Mr. Swisher's employment began on November 1, 2009 to a maximum of 24 months. In the event of a change of control of the Company (as defined in the Swisher Agreement) and if within one year of the change of control, Mr. Swisher's employment with the Company is terminated by the Company, the Company will pay to Mr. Swisher a lump sum in cash equal to 12 months of salary plus an additional one month's salary for every full or partial year of service, recognizing that Mr. Swisher's employment began on November 1, 2009 to a maximum of 24 months.

Severance Payments

If a severance payment triggering event had occurred on August 31, 2011, the severance payments that would be contractually payable to each of the Named Executive Officers would be approximately as follows:

Name	Termination after a "change of control" of the Company (\$)
Donald S. Bubar	1,050,000
R. James Andersen	850,000
Brian Chandler	379,167
William Mercer	238,333
Pierre Neatby	256,667
Richard Pratt	270,833
David Swisher ⁽¹⁾	228,527
Total	3,273,527

Note: (1) Mr. Swisher is paid in US\$ and the amount shown has been converted to C\$ utilizing an exchange rate of US\$1= C\$0.9794.

F. Incentive Plan Awards

Outstanding Option-Based and Share-Based Awards

The table below sets out, for each Named Executive Officer, the incentive options (option-based awards) and share-based awards, outstanding as at August 31, 2011. The closing price of the Company's shares on the TSX on August 31, 2011 was \$4.36.

Name	Option-Based Awards ⁽¹⁾				Share-Based Awards	
	Number of securities underlying unexercised options (#)	Option exercise price (\$)	Option expiration date (\$)	Value of unexercised in-the-money options ⁽²⁾ (\$)	Number of shares or units of shares that have not vested (#)	Market or payout value of share-based awards that have not vested (\$)
Donald S. Bubar	250,000	1.20	January 30, 2012	790,000	Nil	Nil
	175,000	1.20	April 21, 2013	553,000		
	175,000	0.75	February 13, 2014	631,750		
	100,000	1.41	June 2, 2014	295,000		
	300,000	8.62	April 27, 2016	Nil		
R. James Andersen	75,000	1.20	April 21, 2013	237,000	Nil	Nil
	75,000	0.75	February 13, 2014	270,750		
	100,000	1.41	June 2, 2014	295,000		
	150,000	4.07	December 15, 2015	43,500		
	200,000	4.47	August 31, 2016	Nil		
Brian Chandler	600,000	7.06	May 22, 2016	Nil	Nil	Nil
William Mercer	400,000	1.61	June 21, 2012	1,100,000	Nil	Nil
Pierre Neatby	400,000	2.00	June 30, 2015	944,000	Nil	Nil
Richard Pratt	400,000	7.45	May 30, 2016	Nil	Nil	Nil
David Swisher	350,000	2.51	November 1, 2014	647,500	Nil	Nil
Notes:						
(1) Options initially granted to the Named Executive Officers generally vest as to 25% thereof on each of the first four anniversaries of the date of grant thereof, and generally have a term of five years. Option grants to replenish options that have expired or have been exercised within the last six months of the original expiry date vest as to 50% on the date of grant and 50% on the first anniversary of the date of grant.						
(2) The value of the in-the-money options currently held by each Named Executive Officer is based on the closing market price of the Company's common shares on the TSX as at August 31, 2011, being \$4.36, less the option exercise price.						

Value Vested or Earned During the Year

The following table sets forth, for each Named Executive Officer, the value of all incentive plan awards vested or earned during the year ended August 31, 2011:

Name	Option-Based Awards- Value vested during the year (\$)⁽¹⁾	Share-Based Awards- Value vested during the year (\$)	Non-Equity Incentive Plan Compensation- Value earned during the year (\$)
Donald S. Bubar	1,062,188	Nil	Nil
R. James Andersen	407,813	Nil	Nil
Brian Chandler	Nil	Nil	Nil
William Mercer	481,000	Nil	Nil
Pierre Neatby	470,000	Nil	Nil
Richard Pratt	Nil	Nil	Nil
David Swisher	169,000	Nil	Nil

Note:

(1) The value of the options vested during the year for each Named Executive Officer is based on the closing market price of the Company's common shares on the TSX on the vesting date less the option exercise price.

G. Pension Plan Benefits

There are no pension plan benefits in place for the Named Executive Officers.

H. Termination and Change of Control Benefits

Except as set forth above under "Employment Contracts", the Company is not party to any compensatory plan, contract or arrangement where a Named Executive Officer is entitled to receive any compensation from the Company in the event of resignation, retirement or any other termination of employment of such persons, change of control of the Company or a change in the Named Executive Officer's responsibilities following a change of control.

I. Director Compensation

The following table describes director compensation for non-executive directors for the year ended August 31, 2011:

Name ⁽¹⁾	Fees earned (\$)	Option-based awards ⁽²⁾ (\$)	All other compensation (\$)	Total compensation (\$)
David Connelly	27,850	Nil	Nil	27,850
Alan Ferry	42,000	Nil	Nil	42,000
Phil Fontaine	22,400	Nil	Nil	22,400
Brian D. MacEachean	34,800	Nil	Nil	34,800
Peter McCarter	33,400	Nil	Nil	33,400
Richard Morland ⁽³⁾	Nil	Nil	Nil	Nil
Hari Panday	37,600	Nil	Nil	37,600

Notes:

(1) This director compensation table does not include information for Donald S. Bubar who is both a director and a Named Executive Officer. The compensation paid to Mr. Bubar for the financial year ended August 31, 2011 has been reflected in the Named Executive Officer summary compensation table. The Company did not pay any additional compensation to Mr. Bubar for serving as a director of the Company.

(2) The “grant date fair value” has been determined by using the Black-Scholes model, a mathematical valuation model that ascribes a value to a option based on a number of factors in valuing the option-based awards, including the exercise price of the option, the price of the underlying security on the date the option was granted, and assumptions with respect to the volatility of the price of the underlying security and the risk-free rate of return. Calculating the value of options using this methodology is very different from a simple “in-the-money” value calculation. In fact, options that are well out-of-the-money can still have a significant “grant date fair value” based in a Black-Scholes valuation, especially where, as in the case of the Company, the price of the common shares underlying the option is highly volatile. Accordingly, caution must be exercised in comparing grant date fair value amounts with cash compensation or an in-the-money option value calculation. The same caution applies to the total compensation amounts shown in the last column above, which are based in part the grant date fair value amounts set out in the column for Option-based awards.

(3) Mr. Morland was appointed as a director of the Company on September 1, 2011.

Compensation of Directors

Directors of the Company (excluding Mr. Bubar, who is an officer of the Company) are currently paid an annual retainer of \$16,000 together with a fee of \$800 per Board or Committee meeting attended in person or by conference telephone. An additional retainer of \$6,000 is paid to each of the Chairman of the Board and the Chairman of the Audit Committee and an additional retainer of \$3,000 is paid to the Chairman of the CGN Committee.

The CGN Committee, as part of its overall determination of management compensation for 2012, also reviewed directors' compensation for the Peer Group companies. After such comparison, and given the increasing amounts of time Board members need to or must devote to the Company's affairs, including committee work, and the Company's NYSE Amex listing in late 2010, the CGN Committee recommended and the Board approved that, effective January 1, 2012, directors of the Company (excluding Mr. Bubar) would be paid an annual retainer of \$24,000 together with a fee of \$800 per Board or committee meeting attended in person or by conference telephone. An additional retainer of \$6,000 is to be paid to each of the Chairman of the Board and to the Chairman of any standing committee of the Board. Further, each

non-management director was granted an additional 50,000 stock options effective December 1, 2011 exercisable at \$3.43.

The directors are indemnified by the Company against all costs, charges and expenses reasonably incurred by such director in respect of any action or proceeding to which such director is made a party by reason of being a director of the Company, subject to the limitations in respect thereof contained in the *Canada Business Corporations Act*.

The Company maintains insurance coverage with respect of directors' and officers' liability which is limited to \$40,000,000 per claim and \$40,000,000 per policy period, subject to a deductible of \$100,000 as defined in the policy. The current policy is for a one-year term and expires on July 20, 2012. The premium paid by the Company in respect of said insurance in fiscal 2011 was \$270,906.

Option-Based and Share-Based Awards to Directors

The table below sets out for each non-officer director the incentive options (option-based awards) and share-based awards outstanding as of August 31, 2011. These incentive options vest as to 25% per annum. The closing price of the Company's shares on the TSX on August 31, 2011 was \$4.36.

Name	Option-Based Awards ⁽¹⁾				Share-Based Awards	
	Number of securities underlying unexercised options (#)	Option exercise price (\$)	Option expiration date (\$)	Value of unexercised in-the-money options (\$)	Number of shares or units of shares that have not vested (#)	Market or payout value of share-based awards that have not vested (\$)
David Connelly	175,000	2.25	May 26, 2015	369,250	Nil	Nil
Alan Ferry	50,000	1.80	August 24, 2012	128,000	Nil	Nil
	50,000	1.20	April 21, 2013	158,000		
	50,000	0.75	February 13, 2014	180,500		
	75,000	1.54	July 14, 2014	211,500		
Phil Fontaine	131,250	2.80	September 4, 2014	204,750	Nil	Nil
Brian D. MacEachen	50,000	1.20	April 21, 2013	158,000	Nil	Nil
	50,000	0.75	February 13, 2014	180,500		
	75,000	1.54	July 14, 2014	211,500		
Peter McCarter	175,000	1.82	November 27, 2012	444,500	Nil	Nil
Hari Panday	175,000	2.52	April 1, 2015	322,000	Nil	Nil
Note: (1) The value of the in-the-money options currently held by each director is based on the closing market price of the Company's common shares on the TSX as at August 31, 2011, being \$4.36, less the option exercise price.						

Value Vested or Earned During the Year

The following table sets forth, for each non-officer director, the value of all incentive plan awards vested or earned during the year ended August 31, 2011:

Name	Option-Based Awards- Value vested during the year (\$) ⁽¹⁾	Share-Based Awards- Value vested during the year (\$)	Non-Equity Incentive Plan Compensation- Value earned during the year (\$)
David Connelly	219,188	Nil	Nil
Alan Ferry	291,813	Nil	Nil
Phil Fontaine	21,875	Nil	Nil
Brian D. MacEachen	263,938	Nil	Nil
Peter McCarter	81,813	Nil	Nil
Hari Panday	21,875	Nil	Nil

Note:

(1) The value of the options vested during the year for each director is based on the closing market price of the Company's common shares on the TSX on the vesting date less the option exercise price.

SECURITIES AUTHORIZED FOR ISSUANCE UNDER EQUITY COMPENSATION PLANS

The following table provides information as at August 31, 2011 with respect to common shares issuable by the Company pursuant to the Stock Option Plan, which is the only equity compensation plan of the Company:

Plan Category	Number of securities to be issued upon exercise of outstanding options, warrants and rights (#)	Weighted- average exercise price of outstanding options, warrants and rights (\$)	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in first column) (#)
Equity compensation plans approved by securityholders ⁽¹⁾	6,305,250	3.38	3,956,541
Equity compensation plans not approved by securityholders	N/A	N/A	N/A
Total	6,305,250	3.38	3,956,541

Note:

(1) The Stock Option Plan has 3,956,541 options available for issuance which, when added to the 6,305,250 outstanding options, is equal to 10% of the Company's issued capital as at August 31, 2011.

INDEBTEDNESS OF DIRECTORS AND EXECUTIVE DIRECTORS

There was no indebtedness of any director, officer, employee, former directors, former executive officers or former employees, or proposed nominee for election as a director of the Company to, or guaranteed or supported by, the Company or any subsidiary thereof either pursuant to an employee stock purchase program or any other programs of the Company or a subsidiary or otherwise during the financial year of the Company ended August 31, 2011.

INTEREST OF CERTAIN PERSONS IN MATTERS TO BE ACTED UPON

No person who has been a director or an officer of the Company at any time since the beginning of its last completed financial year, no person or company by whom, on whose behalf, directly or indirectly, solicitation has been made, no proposed nominee for election as a director of the Company, nor any associate or affiliate of the aforementioned persons has any material interest, direct or indirect, by way of beneficial ownership of securities or otherwise, in any matter to be acted upon at the meeting, except as disclosed in this Information Circular.

INTEREST OF INFORMED PERSONS IN MATERIAL TRANSACTIONS

None of the directors or executive officers of the Company, no management proposed nominee for election as a director of the Company, none of the persons who have been directors or executive officers of the Company since the commencement of the Company's last financial year and no associate or affiliate of any of the foregoing has any material interest, direct or indirect, by way of beneficial ownership of securities or otherwise, in any matter to be acted upon at the Meeting.

STATEMENT OF CORPORATE GOVERNANCE PRACTICES

National Instrument 58-101 - Disclosure of Corporate Governance Practices ("NI 58-101") requires that if management of an issuer solicits proxies from its securityholders for the purpose of electing directors that certain prescribed disclosure in respect of corporate governance matters be included in its Information Circular. The TSX also requires listed companies to provide, on an annual basis, the corporate governance disclosure which is prescribed by NI 58-101.

The prescribed corporate governance disclosure for the Company is that contained in Form 58-101F1 which is attached to NI 58-101 ("Form 58-101F1 Disclosure"). Schedule B attached hereto sets forth the corporate governance practices of the Company, relative to Form 58-101F1 Disclosure.

ADDITIONAL INFORMATION

Additional information relating to the Company can be found at www.sedar.com and on the Company's website at www.avalonraremetals.com. Financial information is provided in the Company's comparative financial statements and related Managements' Discussion and Analysis for the financial year ended August 31, 2011.

A copy of the following documents may be obtained, without charge, upon request to the Corporate Secretary of the Company at Suite 1901, 130 Adelaide Street West, Toronto, ON Phone: (416) 364-4938, Fax: (416) 364-5162:

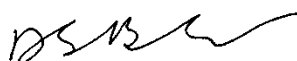
- (a) the comparative financial statements of the Company for the financial year ended August 31, 2011 together with the accompanying report of the auditors thereon and related Management's Discussion and Analysis and any interim financial statements of the Company for periods subsequent to August 31, 2011 and related Management's Discussion and Analysis; and
- (b) this Information Circular.

APPROVAL

The contents of this Information Circular and the sending thereof to the shareholders of the Company have been approved by the directors of the Company.

DATED at Toronto, Ontario this 21st day of December, 2011.

By ORDER of the Board of Directors



Donald S. Bubar
President and Chief Executive Officer

SCHEDULE A

CORPORATE GOVERNANCE DISCLOSURE

National Policy 58-201 - *Corporate Governance Guidelines* establishes corporate governance guidelines which apply to all public companies. The Company has reviewed its own corporate governance practices in light of these guidelines and, as prescribed by National Instrument 58-101 - *Disclosure of Corporate Governance Practices*, hereby discloses its corporate governance practices.

Disclosure Requirements	Comments
Disclose the identity of directors who are independent.	<ul style="list-style-type: none"> • Alan Ferry • Phil Fontaine • Brian MacEachen • Peter McCarter • Richard Morland • Hari Panday <p>For more information about each director, please refer to the section entitled “Election of Directors” of this Information Circular.</p>
Disclose the identity of directors who are not independent, and describe the basis for that determination.	<p>Donald S. Bubar, the President and CEO of the Company, is considered not independent by virtue of his position with the Company.</p> <p>David Connelly, a director of the Company, is considered not independent by virtue of his earning consulting fees from the Company in excess of \$75,000 in one of the past three years. Upon becoming a director, Mr. Connelly ceased to provide consulting services to the Company.</p>
Disclose whether or not a majority of directors are independent.	<p>The Board is currently composed of eight directors. After consideration of the criteria set forth in applicable securities legislation, the Board has concluded that six of the directors are independent.</p>

Disclosure Requirements	Comments
<p>If a director is presently a director of another issuer that is a reporting issuer (or the equivalent) in a jurisdiction or a foreign jurisdiction, identify both the director and the other issuer.</p>	<ul style="list-style-type: none"> • Donald S. Bubar Not applicable • David Connelly Not applicable • Alan Ferry Guyana Goldfields Inc., Guyana Precious Metals Inc., Inter-Rock Minerals Inc., and Macusani Yellowcake Inc. • Phil Fontaine Chieftain Metals Inc. and Plutonic Power Corporation • Brian D. MacEachen Linear Metals Corporation and Cangold Limited • Peter McCarter Thundermin Resources Inc. • Richard Morland Not applicable • Hari Panday Not applicable
<p>Disclose whether or not the independent directors hold regularly scheduled meetings at which non-independent directors and members of management are not in attendance. If the independent directors hold such meetings, disclose the number of meetings held since the beginning of the issuer's most recently completed financial year.</p>	<p>The Board meets without management present (and therefore without the presence of non-management directors) at the end of every Board meeting under the chairmanship of Alan Ferry. In the financial year ended August 31, 2011, six such meetings were held.</p>
<p>Disclose whether or not the chair of the board is an independent director. If the board has a chair or lead director who is an independent director, disclose the identity of the independent chair or lead director, and describe his role and responsibilities.</p>	<p>Alan Ferry is the Chairman of the Board and is an independent director.</p> <p>The Chairman has the responsibility, among other things, of ensuring that the Board discharges its responsibilities effectively. The Chairman acts as a liaison between the Board and the President and CEO and chairs Board meetings.</p>

Disclosure Requirements	Comments
<p>Disclose the attendance record of each director for all board meetings held since the beginning of the issuer's most recently completed financial year.</p>	<p>The Board held nine meetings in the financial year ended August 31, 2011 with the attendance record of each director as follows:</p> <ul style="list-style-type: none"> • Alan Ferry - 9/9 board meetings • Donald S. Bubar - 9/9 board meetings • David Connelly - 9/9 board meeting • Phil Fontaine - 9/9 board meetings • Brian D. MacEachen - 8/9 board meetings • Peter McCarter - 9/9 board meetings • Richard Morland ⁽¹⁾ - 0/0 board meetings • Hari Panday - 9/9 board meetings <p>Notes: (1) Mr. Morland was appointed as a director on September 1, 2011.</p>
<p>Disclose the text of the board's written mandate.</p>	<p>Please refer to Appendix "A" following this section.</p>
<p>Disclose whether or not the board has developed written position descriptions for the chair and the chair of each board committee. If the board has not developed written position descriptions for the chair and/or the chair of each board committee, briefly describe how the board delineates the role and responsibilities of each such positions.</p>	<p>The Board has developed and adopted a written position description for each of the following, as recommended by the CSA Guidelines:</p> <ul style="list-style-type: none"> • Chair of the Board; • Chair of the Audit Committee; and • Chair of the CGN Committee
<p>Disclose whether or not the board and CEO have developed a written position description for the CEO. If the board and CEO have not developed such a position description, briefly describe how the board delineates the role and responsibilities of the CEO.</p>	<p>The Board and the President and CEO have developed a written position description for the President and CEO, and the Board has adopted such position description.</p>
<p>Briefly describe what measure the board takes to orient new directors regarding:</p> <p>(i) the role of the board, its committees and its directors, and</p> <p>(ii) the nature and operation of the issuer's business.</p>	<p>There is currently no formal orientation program in place for new Board members. The Board as a whole and the Company informally provide such orientation and education as required, and provide copies of corporate policies and the Company's ongoing strategic plan. In light of the Company's size, nature and scope of operations, the Board believes this approach is practical and effective.</p>

Disclosure Requirements	Comments
<p>Briefly discuss what measures, if any, the board takes to provide continuing education for its directors. If the board does not provide continuing education, describe how the board ensures that its directors maintain the skill and knowledge necessary to meet their obligations as directors.</p>	<p>There is currently no formal continuing education program in place. Each director is responsible for ensuring that he maintains the skill and knowledge necessary to meet his obligations as a director, and Board members are entitled, at the Company's expense, to acquire educational materials and attend seminars they determine necessary or appropriate to keep them up-to-date with current issues relevant to their service as directors of the Company.</p>
<p>Disclose whether or not the board has adopted a written code for the directors, officers and employees. If the board has adopted a written code:</p> <p>(i) disclose how a person or company may obtain a copy of the code,</p> <p>(ii) describe how the board monitors compliance with its code, or if the board does not monitor compliance, explain whether and how the board satisfies itself regarding compliance with its code, and</p> <p>(iii) provide a cross-reference to any material change report filed since the beginning of the issuer's most recently completed financial year that pertains to any conduct of a director or executive officer that constitutes a departure from the code.</p>	<p>The Board has adopted a written Code of Conduct.</p> <p>(i) the Company's Code of Conduct referred to above can be viewed on the Company's website at www.avalonraremetals.com or a copy may be obtained by written request to the Company's Corporate Secretary, at Suite 1901, 130 Adelaide Street West, Toronto, Ontario M5H 3P5.</p> <p>(ii) the Board monitors compliance with its Code of Conduct by requiring that each director, officer and employee annually affirm, in writing, that he/she has read and understood the Code of Conduct and has agreed to abide by it in all aspects.</p> <p>(iii) none.</p>
<p>Describe any steps the board takes to ensure directors exercise independent judgment in considering transactions and agreements in respect of which a director or executive officer has a material interest.</p>	<p>Each director and executive officer is required to fully disclose his interest in respect of any transaction or agreement to be entered into by the Company. Once such interest has been disclosed, the Board as a whole determines the appropriate level of involvement the director or executive officer should have in respect of the transaction or agreement.</p>

Disclosure Requirements	Comments
<p>Describe any other steps the board takes to encourage and promote a culture of ethical business conduct.</p>	<p>In addition to the Code of Conduct, the Board has also adopted a Safety and Environmental Policy (“S&EP”) which recognizes that maintenance of environmental quality is vital to the Company’s existence, progress, and continued development.</p> <p>The S&EP provides that the Company will maintain high environmental standards limited only by technical and economic feasibility and that the Company will take positive action to protect the safety of its workers, conserve natural resources, and minimize the impact of its activities on the environment through diligent application of appropriate technology and responsible conduct at all stages of exploration, mine development, mining, mineral processing, de-commissioning, and reclamation. The purpose of the S&EP is to provide a measurable framework for the performance of the Company’s activities in an environmentally responsible manner, ensuring compliance by the Company and its employees with all applicable environmental regulations and commitments. The Company ensures that employees are educated in environmental matters and responsibilities relating to their assigned tasks and the Company works pro-actively with government and the public to define environmental priorities and participates where appropriate in the development of responsible laws for the protection of the environment. And finally, the Company has made the commitment to allocate sufficient resources to meet the Company’s safety and environmental goals which commitment includes an annual assessment of the projected costs of de-commissioning and reclamation to ensure that there will be sufficient cash reserves to pay for these costs upon project closure.</p>

Disclosure Requirements	Comments
Describe the process by which the board identifies new candidates for board nomination.	<p>The CGN Committee is responsible for recommending candidates for nomination to the Board. In making such recommendations, the CGN Committee considers:</p> <ul style="list-style-type: none"> (a) the qualifications, skills, expertise and competencies that the Board considers to be necessary for the Board, as a whole, to possess; (b) the qualifications, skills, expertise and competencies that the Board considers each existing director to possess; and (c) the qualifications, skills and competencies each new nominee will bring to the boardroom.
Disclose whether or not the board has a nominating committee composed entirely of independent directors.	The CGN Committee is composed of three directors, all of whom are independent.
If the board has a nominating committee, describe the responsibilities, powers and operation of the nominating committee.	<p>The CGN Committee is responsible for, among other things, identifying and recommending to the board of directors new candidates for the board of directors, annually reviewing the credentials of existing Board members to assess their suitability for re-election and ensuring that arrangements for the appropriate orientation and continuing education programs for new Board members and continuing education, as required, for all Board members are in place.</p> <p>The CGN Committee meets as often as is necessary to carry out its responsibilities.</p> <p>The CGN Committee is permitted access to all records and corporate information that it determines are required in order to perform its duties. The CGN Committee has the authority to engage independent counsel and other advisors as it determines necessary to carry out its duties and to set and pay the compensation for any advisors engaged by it.</p>

Disclosure Requirements	Comments
Describe the process by which the board determines compensation for the issuer's directors and officers.	The CGN Committee is responsible for reviewing the compensation of the Company's directors and officers and making recommendations to the Board with respect thereto. See also "Compensation Discussion and Analysis" of this Information Circular.
Disclose whether or not the board has a compensation committee composed entirely of independent directors.	The CGN Committee is composed of three directors, all of whom are independent.
If the board has a compensation committee, describe the responsibilities, powers and operation of the compensation committee.	<p>The CGN Committee reviews compensation levels for all officers and in particular compensation levels for the CEO. See also "Compensation Discussion and Analysis" of this Information Circular. The CGN Committee is responsible for, among other things, developing or approving performance indicators and corporate objectives which the President and CEO is responsible for meeting, determining or recommending to the Board the compensation of the President and CEO, and reviewing the adequacy and form of compensation of the Board and members of the Board's committees in light of the responsibilities and risks involved in being a director, in the case of the Board, and a chairman, in the case of Board committees. The CGN Committee meets as often as is necessary to carry out its responsibilities.</p> <p>The CGN Committee is permitted access to all records and corporate information that it determines are required in order to perform its duties. The CGN Committee has the authority to engage independent counsel and other advisors as it determines necessary to carry out its duties and to set and pay the compensation for any advisors engaged by it.</p>

Disclosure Requirements	Comments
<p>If a compensation consultant or advisor has, at any time since the beginning of the issuer's most recently completed financial year, been retained to assist in determining compensation for any of the issuer's directors and officers, disclose the identity of the consultant or advisor and briefly summarize the mandate for which they have been retained. If the consultant or advisor has been retained to perform any other work for the issuer, state that fact and briefly describe the nature of the work.</p>	<p>Not applicable.</p>
<p>If the board has standing committees other than the audit, compensation and nominating committees, identify the committees and describe their function.</p>	<p>The governance responsibilities in the CGN Committee's mandate include:</p> <ul style="list-style-type: none"> • to develop and enforce policy in the area of corporate governance and the practices of the Board in light of the Company's particular circumstances, the changing needs of investors and the Company, and changes in corporate governance guidelines. • to prepare and recommend to the Board annually a statement of corporate governance practices to be included in the Company's information circular and ensure that such disclosure is complete and provided in accordance with the regulatory requirements. • to monitor developments in the area of corporate governance and the practices of the Board and advise the Board accordingly; and • to develop, implement and maintain appropriate policies with respect to disclosure, confidentiality and insider trading.

Disclosure Requirements	Comments
<p>Disclose whether or not the board, its committees and individual directors are regularly assessed with respect to their effectiveness and contribution. If assessments are regularly conducted, describe the process used for the assessments.</p> <p>If assessments are not regularly conducted, describe how the board satisfies itself that the board, its committees, and its individual directors are performing effectively.</p>	<p>There is currently no formal assessment procedure in place.</p> <p>Board effectiveness is assessed by the Board as a whole, considering the operation of the Board's committees, the adequacy of information provided to the directors, the quality of communication between the Board and management and the historic growth and performance of the Company. The Board believes that this information assessment has permitted the Board to operate effectively.</p>
<p>The audit committee should be composed entirely of independent directors and should have a specifically defined mandate.</p>	<p>The Board has an Audit Committee composed of three directors, each of whom is independent. (Messrs. MacEachen, Ferry and Panday). A copy of the Audit Committee Charter can be found on the Company's website.</p>

APPENDIX A

MANDATE OF THE BOARD OF DIRECTORS

OF AVALON RARE METALS INC.

The board of directors of the Company explicitly acknowledges responsibility for the stewardship of the Company, including responsibility for:

- (i) to the extent feasible, satisfying itself as to the integrity of the Chief Executive Officer, (“CEO”) and other executive officers and that the CEO and other executive officers create a culture of integrity throughout the organization;
- (ii) adoption of a strategic planning process and approving on at least an annual basis, a strategic plan which takes into account, among other things, the opportunities and risks of the business;
- (iii) identification of the principal risks of the Company’s business and ensuring the implementation of appropriate systems to manage these risks;
- (iv) succession planning, including appointing, training and monitoring senior management;
- (v) adopting a communication policy for the Company;
- (vi) the integrity of the Company’s internal control and management information systems; and
- (vii) developing the Company’s approach to corporate governance, including developing a set of corporate governance principles and guidelines that are specifically applicable to the Company.

Approved by the board of directors the 18th day of July, 2006.



Management Discussion and Analysis of Financial Statements For the year ended August 31, 2011

This Management Discussion and Analysis ("MDA") of Avalon Rare Metals Inc. (the "Company" or "Avalon") provides analysis of the Company's financial results for the year ended August 31, 2011. The following information should be read in conjunction with the accompanying audited consolidated financial statements and the related notes thereto. Unless otherwise noted, all currency amounts included in the MDA are stated in Canadian dollars.

Certain of the statements that are not historical facts contained in this MDA are forward-looking statements that involve risks and uncertainties that could cause actual events or results to differ materially from estimated or anticipated events or results reflected in the forward-looking statements. Such statements reflect the Company's current views with respect to future events and are subject to risks and uncertainties and are necessarily based upon a number of estimates and assumptions that, while considered reasonable by the Company, are inherently subject to significant business, economic, competitive, political and social uncertainties and contingencies. Forward-looking statements include, among other things, statements regarding targets, estimates and/or assumptions in respect of reserves and/or resources, and are or may be based on assumptions and/or estimates related to future economic, market and other conditions. Factors that could cause actual results, developments or events to differ materially from those anticipated include, among others, the factors described or referred to under "Description of the Business - Risk Factors" in the Company's annual information for the year ended August 31, 2011, and:

- the estimation or realization of mineral resources;
- recovery rates and production costs of the rare metals and other minerals;
- the timing and amount of estimated future production;
- requirements for additional capital;
- future prices of rare metals and minerals;
- market demand for rare metals and minerals;
- the reliability of plant operations at production scale;
- energy costs;
- risks of the mining industry; and
- delays in obtaining governmental approvals, permits or financing or in the completion of development or construction activities.

Most of such factors are beyond Avalon's ability to control or predict. Although the Company has attempted to identify important factors that could cause actual actions, events or results to differ materially from those described in forward-looking statements, there may be other factors that cause actions, events or results not to be as anticipated, estimated or intended.

Readers can identify many of these statements by looking for words such as "believe", "expects", "will", "intends", "projects", "anticipates", "estimates", "continues" or similar words or the negative thereof. There can be no assurance that the plans, intentions or expectations upon which these forward-looking statements are based will occur.

The forward-looking statements contained herein are made as of the date of this MDA and are expressly qualified in their entirety by this cautionary statement. Readers should not place undue reliance on the forward-looking statements, which reflect management's plans, estimates, projections and views only as of the date hereof. The Company undertakes no obligation to publicly revise these forward-looking statements to reflect subsequent events or circumstances, except as required by applicable law.

Actual results may differ materially from those anticipated. Readers are cautioned not to put undue reliance on forward-looking statements due to the inherent uncertainty therein. This MDA is prepared as of **November 22, 2011**.

Nature of Business and Overall Performance

Avalon is a Canadian mineral exploration and development company that is listed on the Toronto Stock Exchange in Canada, on the NYSE Amex in the United States and also trades on the Frankfurt Stock Exchange in Germany. The Company seeks to build shareholder value by becoming a diversified producer and marketer of rare metals and minerals and expanding the markets for its mineral products. The technical information included in this MDA unless otherwise stated, has been reviewed and approved by Donald S. Bubar, P. Geo., President and Chief Executive Officer of the Company and Dr. William Mercer, P. Geo., Vice-President, Exploration of the Company. Mr. Bubar and Dr. Mercer are both Qualified Persons under National Instrument 43-101 ("NI 43-101").

Avalon operates primarily in Canada with a primary focus on the rare earth elements ("REE"), and other rare metals and minerals, including lithium, tantalum, niobium, cesium, indium, gallium, zirconium and a related base metal; tin. By definition, REE are the lanthanide series of elements (atomic numbers 57 - 71), whereas the term "rare metals" is a more general "umbrella" term that includes the REE as well as other rare metals including those named above.

The Company is in the process of exploring or developing six of its seven mineral resource properties. Four of the Company's active projects (Thor Lake, Separation Rapids, Warren Township, and East Kemptville) are rare minerals or rare metals properties that are at an advanced stage. The Thor Lake rare metals project ("Thor Lake" or the "Project") is the Company's most advanced project and the Company's primary material property.

The results of a positive pre-feasibility study ("PFS") on the development potential of the Nechalacho REE deposit on the Thor Lake project were announced on June 21, 2010, and the related technical report was filed on July 27, 2010. This report was subsequently amended and re-filed on September 21, 2010. The following year, Avalon produced an updated technical report in March 2011 and produced another updated technical report entitled "Technical Report on the Thor Lake Project, Northwest Territories, Canada" (the "August 2011 Technical Report") dated August 25, 2011, prepared by Roscoe Postle Associates Inc. ("RPA") (formerly Scott Wilson Roscoe Postle Associates Inc.) which was filed on August 26, 2011. The August 2011 Technical Report was prepared for disclosure of the results of the updated pre-feasibility study (the "Updated PFS") completed by RPA. Completion of a bankable feasibility study ("BFS") by the end of calendar 2012, is the Company's top priority and primary focus.

Management's Discussion and Analysis For the year ended August 31, 2011

Avalon has adopted the Prospectors and Developers Association of Canada ("PDAC")'s *E3 Plus* Principles of Responsible Exploration and the Mining Association of Canada's principles of "Towards Sustainable Mining" as policy of the Company and is making a strong commitment to corporate social responsibility ("CSR") best practice. In 2010, Avalon received PDAC's 2010 Environmental and Social Responsibility Award for its exceptional efforts in community engagement with Aboriginal Groups. Avalon applies these principles throughout its operations, particularly with respect to its environmental and community engagement practice on the Thor Lake project.

Industrial demand for the rare metals is growing due to their importance in an expanding array of applications in technology related to energy efficiency and a cleaner environment. Rare metals supplies are constrained, especially for the rare earth elements where China provides approximately 95% of the world's primary supply. Recent policy directives announced by the Chinese government are dictating reductions in exports of unprocessed rare earth elements leading to concern about security of supply of certain REE in major REE consuming countries such as Japan, Korea and the United States. Moreover, REE supply shortages both outside and inside China have caused prices to escalate dramatically over the past few years stimulating increased investor interest in rare earth companies.

During the quarter ended August 31, 2011 (the "Quarter"), the Company completed a prospectus offering and issued 7,692,900 common shares at a price of \$5.81 per share (or US\$6.15 per share) for gross proceeds of \$44,695,749 and, as of this date, remains well-funded to continue advancing its priority projects.

Selected Annual Information

The following selected financial data for each of the three most recently completed fiscal years are derived from the audited annual financial statements of the Company, which were prepared in accordance with Canadian generally accepted accounting principles. For a reconciliation to United States generally accepted accounting principles, see Note 16 of the notes to the Company's consolidated financial statements at and for the period ended August 31, 2011.

For the Years Ending August 31,	2011	2010	2009
	\$	\$	\$
Net revenues	605,142	80,557	159,982
Loss before discontinued operations and extraordinary items	9,421,386	4,099,300	2,954,919
Loss before discontinued operations and extraordinary items, per share basic and fully diluted	0.10	0.05	0.04
Net loss	9,421,386	4,099,300	2,954,919
Net loss, per share basic and fully diluted	0.10	0.05	0.04
Total assets	123,893,553	41,526,715	26,521,264
Total long term liabilities	-	-	-
Cash dividends	-	-	-

The Company has recorded losses in each of its three most recently completed fiscal years and expects to continue to record losses until such time as an economic resource is identified, developed and brought into profitable commercial operation on one or more of the Company's properties or otherwise disposed of at a profit. Since the Company has no revenue from operations, annual operating losses typically represent the sum of business expenses plus any write-offs of mineral properties abandoned during the period. The Company expects to continue to increase its level of business activity in coming years and consequently investors should anticipate that the Company's annual operating losses will also increase until an operation is brought into production or disposed of at a profit.

Results of Operations

Unless otherwise stated, the technical information contained in this section of the MDA relating to the Company's operations in respect of its Thor Lake and other projects and not attributed to RPA has been reviewed and approved by Dr. William Mercer, P.Geo., Vice-President, Exploration, who is a qualified person for the purposes of NI 43-101.

Exploration and Development Activities

Resource property expenditures for the year ended August 31, 2011 totalled \$17,828,302, a 37% increase over the level of expenditures in the comparable period of the previous fiscal year (\$13,051,666). Of these expenditures, 95% were incurred on Thor Lake, and 4% of these expenditures were incurred on the Company's new rare metals project located in the Spor Mountain area, Juab County in the State of Utah, USA ("Spor Mountain"). The increased expenditures on Thor Lake and the expenditures at Spor Mountain account for the majority of the increase. The increased expenditures on Thor Lake were related to expanded work programs mainly in the area of metallurgy as the project advanced into the bankable feasibility stage.

Resource property expenditures for the Quarter totalled \$4,969,406, a 36% increase over the level of expenditures in the comparable period of the previous fiscal year (\$3,643,336). The majority (94%) of these expenditures were incurred on Thor Lake. The increase was primarily caused by the increased level of activities, including metallurgical and market studies, and feasibility and engineering studies.

No properties were abandoned during the year ended August 31, 2011 and no expenditures were written off.

Thor Lake

Thor Lake is located in the Mackenzie Mining District of the Northwest Territories ("NWT"), about five kilometres north of the Hearne Channel of Great Slave Lake and approximately 100 kilometres southeast of the city of Yellowknife. The property is situated in an area referred to as the Akaitcho Territory, an area which is subject to a comprehensive native land claim negotiation involving several Akaitcho communities including, the four in direct proximity to the project: Yellowknives Dene (Ndilo and Dettah), Lutsel K'e and Deninu Kue.

The property is comprised of five contiguous mining leases totalling 10,449 acres (4,249 hectares) and three claims totalling 4,597 acres (1,869 hectares), the latter staked in 2009 to cover favourable geology to the west of the mining leases. The leases are subject to two

underlying royalty agreements entitling the royalty holders to a cumulative 5.5% Net Smelter Returns Royalty, of which 2.5% can be bought back at the principal amount of \$150,000 compounded annually at the average Canadian prime rate from May 2, 1982 to the buyback date (as at August 31, 2011, this amounts to approximately \$1.2 million). Since acquiring the property in 2005, Avalon has concentrated its exploration efforts on the largest known mineralized zone on the property, the Nechalacho REE Deposit ("Nechalacho deposit").

Expenditures during the year ended August 31, 2011, totalled \$16,939,635. Of this, approximately 58% was spent on drilling and geological work in support of the drilling program, 19% on metallurgical and market studies, 11% on pre-feasibility and feasibility studies, 8% on environmental studies and permitting work, with the balance funding community consultation work and annual lease payments.

Expenditures during the Quarter totalled \$4,692,409. Of this, approximately 56% was spent on drilling and geological work in support of the drilling program, 21% on metallurgical and market studies, 11% on feasibility and engineering studies, 7% on community consultation work and 5% on environmental studies and permitting work. The drilling done in the Quarter was with the objective of better defining the Nechalacho deposit, gathering geotechnical data for engineering purposes and collecting sample material for pilot plant work.

Metallurgical studies are ongoing to define the most efficient process for recovery of the REE. The flotation process testwork has advanced to the mini-pilot plant ("MPP") stage. The third of three such trials on a 3 tonne bulk sample was completed at an external consulting firm. This work was for the dual purpose of optimizing the flotation process flowsheet prior to initiating a large scale pilot trial in December, 2011, and producing more concentrate for ongoing bench scale hydrometallurgical process development. The expenditures on feasibility studies and engineering relate to the work on preparing the Updated PFS and commencement of a BFS. The results from the Updated PFS were announced on July 8, 2011, and are discussed below.

The information, tables and figures that follow relating to the Updated PFS and mineral resource estimates in connection with the Thor Lake project are derived from, and in some instances are extracts from, the August 2011 Technical Report prepared by RPA.

Nechalacho Deposit Drilling

Since July, 2007 Avalon has completed over 85,000 metres of drilling on the Nechalacho deposit as summarized in the Table below:

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Calendar Year	Holes	Metres
2007	16	2,551
2008	74	14,280
2009 winter	26	5,474
2009 summer	44	9,123
2010 winter	43	11,398
2010 summer	63	16,188
2011 winter	65	12,224
2011 summer	72	13,979
Total October 16, 2011	403	85,217

The 2011 summer drilling program commenced on June 20, 2011 with geotechnical drilling designed to test the proposed route for the production ramp. Upon completion of the ramp drilling, this drill commenced geotechnical drilling of the proposed area for the underground crusher. This drilling also provided additional intercepts of the Basal Zone.

The second drill rig, equipped to recover large diameter PQ core for bulk sample recovery, began drilling in mid-July. It continued a similar program as in the winter drilling, with the objective of completing in-fill holes within the Indicated Mineral Resources in the Basal Zone in the area where mining is expected to be initiated. This will result in additional Indicated Resources being re-classified to the Measured level of confidence, and will also provide additional mineralized material for metallurgical testing.

As of August 31, 2011, the summer drill program resulted in completion of 33 drill holes for 7,153 metres.

The 2011 summer drill program was concluded on October 16, 2011 at a total of 13,979 metres in 72 holes, bringing the total drill production to date to 85,217 metres in 403 holes.

As previously reported, the winter drill program was completed on April 28, 2011. All of the assay results from the 2011 winter drilling have been compiled, although some check analyses are still pending, and an updated resource estimate is currently in preparation. A resource update is expected to be available in December, 2011.

The resource estimates disclosed in the Updated PFS include drill results up to October, 2010.

Nechalacho Deposit Mineral Resource Estimates

The NI 43-101 compliant resource estimates originally established by independent consultants RPA for the PFS in 2010, were updated by the Company on January 27, 2011 to incorporate all the data generated from the 2010 drilling programs which totalled 27,586 metres in 106 holes. The PFS was then updated by the August 2011 Technical Report. For additional information on Thor Lake, please refer to the August 2011 Technical Report, which is available on SEDAR at www.sedar.com.

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The technical data used for the new resource estimate were compiled, validated and evaluated by the Company and was updated to include all the new drill hole information and assays generated in the 2010 drilling program. The new resource estimates resulted in significant increases in both Inferred and Indicated Resources for both the Basal Zone and the Upper Zone compared to the resource estimates prepared in 2010 for the PFS. Importantly, the Indicated Resources in the key Basal Zone part of the deposit increased to 57.49 million tonnes grading 1.56% TREO⁴ with 20.72% HREO³/TREO using the base case \$260 Net Metal Return (“NMR”²) cut-off. More significantly, distinct sub-zones with a higher average grade were discovered in the West Long Lake area. These can be identified by applying a higher NMR cut-off and the proportion of Indicated Mineral Resources estimated at the much higher \$600 NMR cut-off, now total 14.67 million tonnes at 2.19% TREO and 24.68% HREO/TREO. This motivated the Company to prepare a new mine development plan and a new estimate of Mineral Reserves, which formed the basis for an update of the discounted cash flow (“DCF”) analysis produced for the 2010 PFS, which was disclosed on July 7, 2011 and is discussed further below.

The Nechalacho deposit resource estimates as originally released on January 27, 2011, including values for the individual rare earth oxides, are summarized in the tables below. The NMR includes the value attributable to ZrO₂, Nb₂O₅, and Ta₂O₅ in the rock after metallurgical recoveries.

Nechalacho Deposit: NI 43-101 Mineral Resources

Updated Jan. 27, 2011

BASAL ZONE	Tonnes	TREO %	HREO %	HREO/TREO %	ZrO ₂ PPM	HfO ₂ PPM	Nb ₂ O ₅ PPM	Ta ₂ O ₅ PPM	La ₂ O ₃ PPM	Ce ₂ O ₃ PPM	Pr ₂ O ₃ PPM	Nd ₂ O ₃ PPM	Sm ₂ O ₃ PPM
INDICATED	57,486,089	1.56	0.33	20.72	29,895	593.5	4,024	396.0	2,511	5,713	706.3	2,773	596.9
INFERRED	107,586,753	1.35	0.26	18.97	28,268	557.0	3,726	353.7	2,214	5,046	635.0	2,503	516.5

UPPER ZONE													
INDICATED	30,642,037	1.48	0.15	10.26	21,007	371.8	3,064	191.9	2,776	6,295	764.6	2,953	547.4
INFERRED	119,293,791	1.26	0.13	10.15	24,135	447.2	3,472	208.9	2,269	5,344	661.9	2,575	469.1

TOTAL INDICATED	88,128,126	1.53	0.26	17.08	26,805	516.5	3,690	325.0	2,603	5,915	726.6	2,836	579.7
TOTAL INFERRED	226,880,544	1.30	0.19	14.33	26,095	499.3	3,592	277.5	2,243	5,203	649.1	2,541	491.5

BASAL ZONE	Tonnes	Eu ₂ O ₃ PPM	Gd ₂ O ₃ PPM	Tb ₂ O ₃ PPM	Dy ₂ O ₃ PPM	Ho ₂ O ₃ PPM	Er ₂ O ₃ PPM	Tm ₂ O ₃ PPM	Yb ₂ O ₃ PPM	Lu ₂ O ₃ PPM	Y ₂ O ₃ PPM	Ga ₂ O ₃ PPM	DENSITY g/cc
INDICATED	57,486,089	74.49	538.3	80.58	402.5	70.1	180.1	23.4	138.7	19.3	1,757.3	133.4	2.9
INFERRED	107,586,753	63.94	465.1	66.51	323.3	55.6	133.9	18.3	107.2	15.1	1,364.2	126.3	2.9

UPPER ZONE													
INDICATED	30,642,037	58.59	403.5	43.30	160.5	22.9	55.6	6.3	40.7	5.7	660.8	172.7	2.8
INFERRED	119,293,791	52.00	344.1	34.57	133.6	19.1	44.8	6.5	42.4	6.3	576.4	170.5	2.9

TOTAL INDICATED	88,128,126	68.96	491.4	67.62	318.3	53.7	136.8	17.5	104.6	14.5	1,376.1	147.1	2.9
TOTAL INFERRED	226,880,544	57.66	401.5	49.72	223.5	36.4	87.0	12.1	73.1	10.5	950.0	149.5	2.9

Notes:

1. CIM definitions were followed for Mineral Resources.
2. NMR is defined as “Net Metal Return” or the *in situ* value of all the payable rare metals in the ore net of estimated metallurgical recoveries and separation plant processing costs and estimated profits.
3. HREO (Heavy Rare Earth Oxides) is the total concentration of: Y₂O₃, Eu₂O₃, Gd₂O₃, Tb₂O₃, Dy₂O₃, Ho₂O₃, Er₂O₃, Tm₂O₃, Yb₂O₃ and Lu₂O₃.
4. TREO (Total Rare Earth Oxides) is HREO plus: La₂O₃, Ce₂O₃, Pr₆O₁₁, Nd₂O₃ and Sm₂O₃.

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5. Mineral Resources are estimated using price forecasts for 2014 for rare earth oxides prepared early in 2010 for the PFS. Rare earths were valued at an average net price of US\$21.94/kg, ZrO₂ at US\$3.77/kg, Nb₂O₅ at US\$45/kg, and Ta₂O₅ at US\$130/kg.
6. Mineral Resources are undiluted.
7. A cut-off NMR grade of CAD\$260 was used for the base case.
8. An exchange rate of US\$1.00 USD = CAD\$0.90 was used.
9. ZrO₂ refers to Zirconium Oxide, Nb₂O₅ refers to Niobium Oxide, Ta₂O₅ refers to Tantalum Oxide, Ga₂O₃ refers to Gallium Oxide.

This updated estimate was used as the basis for the Updated PFS. RPA validated the data set and the wireframes, and reviewed the interpolation methodology and the block model. RPA also reclassified a small quantity of Inferred Resources to Indicated Resources. For example the Indicated Resources for the Basal Zone increased from 57.49 million tonnes to 57.82 million tonnes with no change to TREO and HREO.

The resource estimate that was used in the Updated PFS by RPA is summarized below.

AREA	TONNES (millions)	TREO %	HREO %	ZrO ₂ %	Nb ₂ O ₅ %	Ta ₂ O ₅ ppm
Basal Zone Indicated						
Tardiff Lake	41.72	1.61	0.34	2.99	0.41	397
West Long Lake	16.11	1.42	0.31	2.98	0.38	392
Total Indicated	57.82	1.56	0.33	2.99	0.40	396
Basal Zone Inferred						
Tardiff Lake	19.18	1.66	0.36	3.08	0.42	423
Thor Lake	79.27	1.30	0.24	2.78	0.37	338
West Long Lake	8.82	1.16	0.21	2.71	0.33	346
Total Inferred	107.26	1.35	0.26	2.83	0.37	354

AREA	TONNES (millions)	TREO %	HREO %	ZrO ₂ %	Nb ₂ O ₅ %	Ta ₂ O ₅ ppm
Upper Zone Indicated						
Tardiff Lake	23.63	1.50	0.15	2.09	0.32	194
West Long Lake	7.02	1.40	0.13	2.14	0.27	186
Total Indicated	30.64	1.48	0.15	2.10	0.31	192
Upper Zone Inferred						
Tardiff Lake	28.66	1.34	0.12	1.96	0.32	175
Thor Lake	81.66	1.24	0.12	2.54	0.36	206
West Long Lake	5.67	1.34	0.12	1.95	0.26	170
Total Inferred	115.98	1.27	0.12	2.37	0.34	196

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AREA	TONNES (millions)	TREO %	HREO %	ZrO ₂ %	Nb ₂ O ₅ %	Ta ₂ O ₅ ppm
Total Indicated						
Upper and Basal	88.46	1.53	0.27	2.68	0.37	325
Total Inferred						
Upper and Basal	223.24	1.31	0.19	2.59	0.36	272

Notes:

1. CIM definitions were followed for Mineral Resources.
2. HREO is the total concentration of: Y₂O₃, Eu₂O₃, Gd₂O₃, Tb₂O₃, Dy₂O₃, Ho₂O₃, Er₂O₃, Tm₂O₃, Yb₂O₃ and Lu₂O₃.
3. TREO is HREO plus: La₂O₃, Ce₂O₃, Pr₆O₁₁, Nd₂O₃ and Sm₂O₃.
4. Mineral Resources are estimated using price forecasts for 2014 for rare earth oxides prepared early in 2010 for the PFS. Rare earths were valued at an average net price of US\$21.94/kg, ZrO₂ at US\$3.77/kg, Nb₂O₅ at US\$45/kg, and Ta₂O₅ at US\$130/kg.
5. A cut-off NMR grade of CAD\$260 per tonne was used.
6. An exchange rate of US\$1=CAD\$1.11 was used.
7. ZrO₂ refers to Zirconium Oxide, Nb₂O₅ refers to Niobium Oxide, Ta₂O₅ refers to Tantalum Oxide, Ga₂O₃ refers to Gallium Oxide.
8. Mineral Resources are inclusive of Mineral Reserves.

Probable Mineral Reserves

A Mineral Reserve estimate for the Project has been prepared by the Company and reviewed by RPA, which has been included in the August 2011 Technical Report.

	Tonnes (millions)	% TREO	% HREO	ZrO ₂ PPM	Nb ₂ O ₅ PPM	Ta ₂ O ₅ PPM	Y ₂ O ₃ PPM	HfO ₂ PPM
Probable Mineral Reserves	14.54	1.53%	0.40%	28,998	3,800	404	2,175	615

	Tonnes (millions)	La ₂ O ₃ PPM	Ce ₂ O ₃ PPM	Pr ₆ O ₁₁ PPM	Nd ₂ O ₃ PPM	Sm ₂ O ₃ PPM	Eu ₂ O ₃ PPM	Gd ₂ O ₃ PPM
Probable Mineral Reserves	14.54	2,325	5,173	658	2,593	590	78	574

	Tonnes (millions)	Tb ₄ O ₇ PPM	Dy ₂ O ₃ PPM	Ho ₂ O ₃ PPM	Er ₂ O ₃ PPM	Tm ₂ O ₃ PPM	Yb ₂ O ₃ PPM	Lu ₂ O ₃ PPM
Probable Mineral Reserves	14.54	95	508	93	245	32	189	26

Notes:

1. CIM definitions were followed for Mineral Reserves.
2. Mineral Reserves are estimated using price forecasts for 2015 for rare earth oxides (US\$46.31/kg average), zirconium oxide (US\$3.77/kg), tantalum oxide (US\$255.63/kg) and niobium oxide

(US\$55.86/kg).

3. HREO grade is the total of Y₂O₃, Eu₂O₃, Gd₂O₃, Tb₂O₃, Dy₂O₃, Ho₂O₃, Er₂O₃, Tm₂O₃, Yb₂O₃ and Lu₂O₃ grades. TREO grade comprises HREO plus La₂O₃, Ce₂O₃, Nd₂O₃, Pr₂O₃, and Sm₂O₃ grades.
4. An exchange rate of CAD\$0.95=US\$1.00 was used.
5. Mineral Reserves are estimated using a Net Metal Return cut-off value of CAD\$300/tonne.
6. A minimum mining width of five metres was used.
7. Totals may differ from sum or weighted sum of numbers due to rounding.

Updated PFS Financial Analysis

The Updated PFS is based principally on the updated Mineral Reserve estimate that was derived from a new mine plan developed from the updated mineral resource estimate disclosed in January, 2011. In addition, RPA updated the product price assumptions to reflect some of the considerable price appreciation that has occurred particularly for the rare earth oxides over the past 12 months. The new economic analysis also incorporates related updates to operating costs, foreign exchange rates and production ramp-up time-lines.

Like the original PFS, the Updated PFS assumes that Avalon will be selling a mixed rare earth oxide concentrate at a price derived using a model that discounts future individual oxide prices (by an average of 38%) to reflect the semi processed nature of the concentrate. In fact, Avalon now contemplates establishing its own separation and refining facility in North America, but has not yet completed a pre-feasibility study on this facility to allow it to be incorporated into the present Updated PFS.

Since the PFS was initially issued in July 2010, rare earth prices dramatically increased by in excess of 1,000%, well in excess of the price appreciation forecast in the PFS. The price increases outside China were partly due to the imposition of quotas and tariffs on the export of separated rare earth oxides. Prices also increased inside China due to supply shortages arising as a result of efforts by the government to consolidate the industry and make it more sustainable. More recently, prices have come off their highest levels reached in June, 2011, but remain much higher than Avalon's price forecast contained in the Updated PFS (July, 2011).

The average "basket" price calculated for the Nechalacho mixed rare earth concentrate and used in the original PFS was US\$21.94/kg. The average "basket" price for the Nechalacho mixed rare earth concentrate using the updated price forecast for 2015 is US\$46.33/kg. The Updated PFS bases the REE price assumption on a price forecast published by CIBC World Markets in its Rare Earth Industry Overview dated March 6, 2011. Current prices *FOB China* reported by services such as Metal-pages.com, are much higher than those used in the price forecast for the Updated PFS, reflecting the opinion of both RPA and the Company that future prices are likely to decrease from current record levels as new supply comes into the marketplace.

The Updated PFS produced a DCF analysis yielding a 39% Internal Rate of Return ("IRR") on a pre-tax basis (compared to 14% in the original study) and a 34% IRR on an after-tax basis (compared to 12% in the original study). The NPV at a 10% discount rate is now \$1.77 billion pre-tax and \$1.27 billion after-tax.

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Financial Analysis	Original PFS		Updated PFS	
	After-Tax (\$)	Pre-Tax (\$)	After-Tax (\$)	Pre-Tax (\$)
IRR	12%	14%	34%	39%
Net Cash Flow	1.5 billion	2.1 billion	4.48 billion	6.08 billion
NPV @ 8%	236 million	428 million	1.61 billion	2.22 billion
NPV @ 10%	97 million	246 million	1.27 billion	1.77 billion

Rare Earth Markets and Market Development Initiatives

The Company's product marketing effort is being led by Mr. Pierre Neatby, Vice-President, Sales and Marketing. The Company has implemented a proactive marketing plan including participation in various industry conferences with the overall objective of building relationships with strategic customers seeking to become investors in the Project, and identifying technology partners capable of assisting Avalon with process technology. Potential strategic partners and technology partners are seeking off-take agreements in return for their investment.

Avalon has entered into non-binding memorandums of understanding ("MOUs") with four industrial companies seeking to participate in the Project by investing and /or providing technical expertise in exchange for obtaining off-take rights. MOUs are commonly used to initiate a formal due diligence process and frame the discussions between the parties. However, each MOU requires the Company to maintain the confidentiality of the identity of the counterparty and the business terms until the negotiation process is completed and a definitive agreement is signed. Progress is being made with respect to all four MOUs and face to face meetings have taken place, or are scheduled to take place, in the last quarter of calendar 2011 with each party.

Metallurgical Process Development

Metallurgical process development work continued during the Quarter with both flotation and hydrometallurgical testwork underway. Bench scale flotation testing continues to enhance the process and a third flotation pilot, this time a continuous pilot plant scale concentrate production run, was completed in August 2011. This test processed 3 tonnes of Basal Zone mineralized material and is preliminary to the planned large scale, 40 tonne pilot test planned for December, 2011. It is largely intended to produce concentrate to be utilized in on-going, bench-scale hydrometallurgical testwork, as well as providing additional information to help finalize flowsheet parameters for the large scale pilot plant trial. Results from this production run, and results from locked cycle tests ("LCTs") carried out prior to the production run, yielded results indicating that the mineral recoveries projected in the Company's Updated PFS can be achieved.

The recoveries reported in the Updated PFS were 89.7% for zirconium oxide ("ZrO₂"), 79.5% for all rare earth oxides ("REO"), 68.9% for niobium oxide ("Nb₂O₅") and 63% for tantalum oxide ("Ta₂O₅"). The LCTs on the 3.7 tonne feed sample gave higher recoveries for Ta₂O₅ and Nb₂O₅, at an average of 74.3% and 73.9% respectively, similar recoveries for REE at an average of 78.5% and lower recoveries for ZrO₂ at an average of 83.8%. The concentrate production run also gave slightly higher Ta₂O₅ and Nb₂O₅ recoveries at 65.4% and 69.7% and lower REO recovery at 73.1% and ZrO₂ recovery at 82%.

The slightly lower average REO recoveries in the production run are due to full stability not being reached and the mass of slimes removed being above target (15.8% instead of targeted 8%). These issues are not expected to recur with the much larger sample size (40 tonnes) planned for the full scale pilot plant. It is considered that the LCTs provide the best indication of expected recoveries from the sample tested.

Bench scale hydrometallurgical testwork is continuing at a third-party consulting firm in Lakefield, Ontario with testing to focus on the solution chemistry, purification and precipitation of rare earths. A contract was signed with SGS Minerals for a hydrometallurgical pilot plant, and initial pilot scale test work has commenced with the acid bake portion of the process. The hydrometallurgical pilot scale work is expected to take up to 40 weeks to complete.

During the Quarter, the Company initiated work on a pre-feasibility study for a separation plant/refinery under a new contract with the same consultant that completed the scoping study in 2010. This study is scheduled for completion in January, 2012 and once received, the separation plant will be integrated into the overall development model and discounted cash flow analysis. For the purpose of this study, the Company has narrowed down its search for a site to a few locations in the southern United States which meet the key site selection criteria of proximity to transportation infrastructure, and proximity to suppliers of the principal reagents required which include hydrochloric acid and caustic soda.

Community, Environment, Health and Safety, Permitting

During the Quarter, the Company continued positive negotiations towards the completion of an accommodation agreement (often referred to as an impacts and benefits agreement) with the Deninu Kue First Nation ("DKFN"), Lutsel K'e Dene First Nation ("LKDFN") and the Yellowknives Dene First Nation ("YKDFN"). Negotiations are ongoing with the objective of concluding these agreements in early calendar 2012.

The Company has placed a high priority on its performance with respect to health and safety at Thor Lake. During the Quarter, there was one lost time accident at the site when a contractor stumbled on uneven ground around the camp suffering a sprained ankle requiring medical attention and losing 7 days off work

There was a land use inspection conducted during the quarter on July 21, 2011 by the Aboriginal Affairs and Northern Development Canada (formerly Indian and Northern Affairs Canada) Land Use inspector with no significant issues to report. As is the Company's practice, all land use inspection reports have been filed on the Company's website at www.avalonraremetals.com in the CSR/Sustainability section.

The Company is currently undergoing an environmental assessment conducted by the Mackenzie Valley Environmental Impact Review Board ("MVEIRB"). On May 20, 2011, the Company submitted the Developers Assessment Report ("DAR"), (otherwise known as an Environmental Impact Statement), just three months upon receiving the final terms of reference from MVEIRB. In November, 2011, the DAR was finally deemed by MVEIRB to be in conformity with the terms of reference and the process is now moving into the information request stage of the process. Avalon is working to ensure the Environmental Assessment Process is completed by the end of 2012. A copy of all information submitted by the Company can be found on MVEIRB's public registry at www.reviewboard.ca.

Activities at the Project are under a new land use permit issued by the MVLWB on June 23, 2011, for a period of 5 years beginning on July 5, 2011.

Project Schedule

The BFS is now targeted for completion in late calendar 2012 and it was disclosed in the Company's news release of November 9, 2011 that a further minor delay is possible due to the relatively slow progress of the metallurgical test program generally. This is not expected to impact the schedule to production start-up, which is still forecast for 2015.

During the year ended August 31, 2011 the Company had budgeted expenditures of approximately \$20 million for the Project (for the BFS, metallurgical studies (including MPP and pilot plant tests), environmental studies and further definition drilling on the Nechalacho deposit). However the Company had only incurred approximately \$17 million during the year, the short fall being primarily due to the delays in the metallurgical test program. The Company expects to incur approximately \$26 million in fiscal 2012 and \$3 million in fiscal 2013 in completing the BFS.

The Company believes that timely completion of the metallurgical pilot plant programs is the most significant risk factor for additional delays to the Project schedule. This is partly due to capacity issues with service providers as well as the potential for unanticipated results necessitating changes in the process flowsheet design. Timely receipt of all required operating permits is also a risk factor although this risk has been at least partly mitigated by the rapid submission of the DAR and the lack of local community opposition to the project development plan. However, as disclosed in the Company's news release dated November 9, 2011, the slow response times by MVEIRB to the Company's submissions do create some risk for a delay in receiving operating permits.

Finally, timely availability of project financing is also a significant risk factor which the Company is working to mitigate by seeking to arrange off-take agreements and to attract investment from prospective consumers of rare earth elements and minerals.

Other Projects

Separation Rapids

During the year ended August 31, 2011, the Company incurred \$70,641 in expenditures on the Separation Rapids Lithium-Tantalum Project which is host to the Big Whopper petalite deposit.

During the quarter ended May 31, 2011, the Company received an expression of interest from an industrial minerals company (the "Industrial Mineral Company") in processing and evaluating a bulk sample of the petalite ore for possible application in glass and ceramics applications. The Company had approximately 250 tonnes of crushed ore available that was collected in 2005 and stored in "big bags" at an outdoor site near Kenora. Most of the expenditures incurred during the year were related to work done to recover this material and packaging the material for shipment for detailed evaluation of its market potential.

Subsequent to the end of the Quarter, approximately 80 tonnes of sample material were shipped to the Industrial Mineral Company for processing and evaluation. Prior to shipping, a significant amount of work was undertaken to clean up the sample material as the bags had deteriorated and

the material had become contaminated with organic material. A process was established for washing and re-packaging the sample material and samples collected routinely for quality control purposes. The balance of the sample material not shipped, totalling approximately 120 tonnes, has been stored under cover for future testwork. As at the date of this MDA, no results from the evaluation of the sample had yet been communicated to the Company.

During the Quarter, the Company re-started the permitting process under the *Mining Act* in order to be ready to resume operations at the site. Initial work involving the preparation and filing of a detailed Project Description Report is now underway. This work is being done under the direction of the Company's external mineral tenure consultant.

Warren Township

Expenditures of \$33,261 were incurred on the Warren Township Anorthosite Project during the year ended August 31, 2011. During the quarter ended May 31, 2011, the Company received an expression of interest in the calcium feldspar product from the Industrial Minerals Company referred to above that expressed interest in the Company's petalite product. The majority of the costs incurred during the year were related to packaging and shipping the inventory of semi-processed material from the 2007 bulk sampling program for shipment for detailed evaluation.

During the Quarter, approximately 35 tonnes of material, that had been stored in a warehouse in Foleyet, Ontario was packaged and shipped to the industrial minerals company. As at the date of this MDA, no results from the evaluation of the sample had yet been communicated to the Company.

With the potential for renewing development work at the site, the Company also re-started the permitting process during the Quarter. Calcium feldspar production is regulated under the Aggregate Resources Act which is administered by the Ontario Ministry of Natural Resources ("MNR"). The permitting process was initiated in 2007-8 but was not completed when the project went dormant after the 2008. Following several meetings held with MNR officials during and subsequent to the end of the Quarter, a satisfactory solution was found for the issue over the size of the area to be permitted, that first arose in 2008.

The permitting process is now proceeding under the direction of the Company's external mineral tenure consultant. Work commenced subsequent to the end of the Quarter with a legal survey of the perimeter of the 720 hectare property and filing of the formal permit application. After a 20-day public consultation period, and if no objections are raised, the permit could be in place by as early as December, 2011.

East Kemptville

During the year ended August 31, 2011, the Company incurred expenditures totalling \$22,427 on the East Kemptville Tin-Rare Metals Project in Yarmouth Co., Nova Scotia. Most of these expenditures were related to routine project maintenance and continuing efforts to move forward with the proposed work program on the Special Licence required to complete the Preliminary Economic Assessment on the historic tin-indium resources in that area.

During the Quarter, the Company requested an extension from the Minister of Natural Resources of Nova Scotia to fulfill its expenditure obligations under the Special Licence by August 1, 2013.

The Company has been verbally assured that the extension is forthcoming but formal confirmation was still pending as at the date of this MDA.

Spor Mountain

During the year ended August 31, 2011, the Company incurred expenditures totalling \$692,337 on the Spor Mountain Rare Metals Project in Juab County, Utah. Most of these expenditures were incurred on claim staking and carrying out initial geological work and geophysical surveys on these new claims. The Company now holds 690 claims covering 13,902 acres (5,298 hectares) in this area. A minimum \$1,000,000 exploration program involving 3,000 metres of drilling is planned for the property in fiscal 2012.

General Exploration

During the year ended August 31, 2011, the Company incurred \$70,001 in general exploration expenditures related to new rare metals project generation. As a result of this project generative work, the Company staked 108 mineral claims in New Brunswick subsequent to the year ended August 31, 2011. A \$200,000 exploration program is proposed for 2012 to define drill targets on these claims which are collectively referred to as the Miramichi Tin project. The Miramichi Tin claims are considered prospective for tin-indium deposits similar to the East Kemptville deposit in Nova Scotia.

Administration

Operating expenses totalled \$10,078,736 for the year ended August 31, 2011, a 114% increase over the amount incurred during the year ended August 31, 2010 (\$4,714,554). Excluding non-cash stock-based compensation, operating expenses totalled \$5,004,292, an 87% increase compared to the same period in 2010. This increase reflects the ongoing expansion of the Company's business activities. The main areas of increased expenses were salaries and benefits, professional fees, transfer and filing fees, and public and investor relations.

Stock-based compensation increased to \$5,074,444 from \$2,041,755 compared to the year ended August 31, 2010. This increase is primarily a result of the increase in the number of options earned in the current year compared to 2010, as well as the significant increase in the value of the Company's options.

Salaries and benefits for the year ended August 31, 2011 totalled \$1,600,985, a 147% increase over the year ended August 31, 2010 (\$647,788). During the year ended August 31, 2011, the Company added eight full time employees to its management and technical staff team. To assist the Company in retaining and attracting top talents in the industry, the Company started an employee group insurance benefit plan in late fiscal 2010. The increase in salaries and benefits relates primarily to the increased number of staff on payroll, the recruitment costs to expand its work force as well as the premiums for the employee group insurance benefit plan.

Professional fees increased by \$350,942 to \$494,417 compared to the year ended August 31, 2010. The increase relates primarily to the legal and other professional fees incurred on the preparation and filing of the base shelf prospectus (the "Prospectus"), the Company's listing application to have its common shares listed on the NYSE Amex, and the continuance of the Company out of the Province of British Columbia and into the federal jurisdiction of Canada, as well as increased ongoing compliance costs associated with the listing of its shares on the NYSE

Management's Discussion and Analysis For the year ended August 31, 2011

Amex. As disclosed in the Company's news release dated May 5, 2011, the Prospectus was filed with the securities commissions in each of the provinces and territories of Canada, except Quebec, and a registration statement was also filed with the United States Securities and Exchange Commission during the quarter ended May 31, 2011.

Transfer and filing fees increased by \$330,614 compared with the fiscal year ended 2010. The increase relates primarily to the filing fees for the Prospectus, the increased listing fees associated with the Company's shares being listed on the NYSE Amex, and the listing fees for the common shares issued pursuant to the prospectus offerings completed in September, 2010 and August, 2011.

Expenditures on public and investor relations ("IR") activities for the year ended August 31, 2011 totalled \$876,036 compared to \$778,647 for fiscal 2010, due to increased investor relations activities generally. Consistent with the increased level of IR activities, travel expenses also increased by \$75,047 to \$332,762 during the year ended August 31, 2011. The strong investor and media interest in rare earths that existed earlier in the year began to subside during the Quarter when rare earth prices peaked and began to retreat in June, 2011. After experiencing strong demand from institutional shareholders for corporate presentations earlier this year, this demand also waned during the Quarter while the Company prepared the Updated PFS. Minimal institutional marketing was carried out during the Quarter due to declining markets and reduced investor interest generally during the summer months. The market correction that occurred in early August, 2011 further depressed investor interest and only five investor marketing initiatives were conducted subsequent to the end of the Quarter.

The increase of \$130,550 in insurance is primarily related to the increase in the coverage of the Company's directors and officers' indemnity insurance policy and the Company's general liability insurance policy.

Directors' fees for the current fiscal year increased by \$93,650 to \$198,050 compared to the fiscal year ended 2010. The foregoing arose from the increase in the number of directors serving on the board of directors (the "Board") from five to seven in fiscal 2010 and an increase in the level of fees paid to during fiscal 2011. The Company currently has eight directors serving on the Board.

Higher cash balances resulted in interest income increasing to \$605,142 compared with \$80,557 for the year ended August 31, 2010.

For the Quarter, operating expenses totalled \$2,636,248 compared with \$1,079,860 during the comparable period in fiscal 2010. Excluding non-cash stock-based compensation, operating expenses totalled \$1,250,896, compared with \$670,278 for the same quarter in fiscal 2010. The main areas of increased administrative expenditures for the Quarter were salaries and benefits, transfer and filing fees, professional fees and insurance.

Consistent with the increases for the year ended August 31, 2011, the increase of \$259,548 in salaries and benefits reflects the increase in the number of employees on payroll and recruitment costs for the two new senior officers who joined the Company during the Quarter. The increase of \$113,899 transfer and filing fees was directly related to the filing of the Prospectus and the listing fees on the common shares issued pursuant to the prospectus offering completed in August 2011. The increase of \$49,777 in professional fees is primarily related to preparation and filing of the

Management's Discussion and Analysis For the year ended August 31, 2011

Prospectus as well as the increased ongoing compliance costs with having the Company's shares listed on the NYSE Amex. The increase of \$42,443 in insurance is primarily related to the increase in the coverage of the Company's directors and officers' indemnity insurance policy and the Company's general liability insurance policy.

Summary of Quarterly Results

The following selected financial data is derived from the unaudited interim financial statements of the Company, which were prepared in accordance with Canadian generally accepted accounting principles.

Fiscal Year	2011				2010			
	Aug. 31	May 31	Feb. 28	Nov. 30	Aug. 31	May 31	Feb. 28	Nov. 30
For the Quarters Ended	\$	\$	\$	\$	\$	\$	\$	\$
Net revenues	210,048	163,878	137,529	93,687	19,015	21,583	16,688	23,271
Loss before discontinued operations and extraordinary items	2,370,211	3,145,596	2,480,080	1,425,499	1,079,860	893,979	1,295,917	829,544
Loss before discontinued operations and extraordinary items, per share, basic and fully diluted	0.02	0.03	0.03	0.02	0.01	0.01	0.02	0.01
Net loss	2,370,211	3,145,596	2,480,080	1,425,499	1,079,860	893,979	1,295,917	829,544
Net loss, per share, basic and fully diluted	0.02	0.03	0.03	0.02	0.01	0.01	0.02	0.01

The fluctuation on quarterly net loss is primarily due to stock-based compensation expenses recognized as stock options granted to directors, officers, employees and consultants of the Company are earned, the write-downs of resource properties and recovery of future income taxes. The costs of resource properties are written down at the time the properties are abandoned or considered to be impaired in value.

Liquidity and Capital Resources

In management's view, given the nature of the Company's operations, which consist of the exploration and development of mining properties, the most relevant financial information relates primarily to current liquidity, solvency, and planned property expenditures. The Company's financial success will be dependent on the economic viability of its resource properties and the extent to which it can discover and develop new mineral deposits. Such development may take several years to complete and the amount of resulting income, if any, is difficult to determine. The sales value of any mineralization discovered by the Company is largely dependent on factors beyond the Company's control, including the market value of the metals and minerals to be produced. The Company does not expect to receive significant revenue from any of its properties until 2015 at the earliest.

As at August 31, 2011, the Company had working capital of \$68,638,285 and cash and cash equivalents on hand of \$70,858,678. Substantially all of the company's cash and cash equivalents are held at a major Canadian chartered bank in cashable guaranteed investment certificates bearing annual interest rates between 1.9% and 2.1%.

Management's Discussion and Analysis For the year ended August 31, 2011

On August 3, 2011, the Company completed a prospectus offering and issued 7,692,900 common shares at a price of \$5.81 per share (or US\$6.15 per share) for gross proceeds of \$44,695,749 (the "August 2011 Prospectus Offering"). After commissions and expenses, the Company netted cash proceeds of \$41,286,721.

The Company's current operating expenditures, excluding expenditures on resource property work programs, are approximately \$500,000 per month. As at the date of this report, the Company's current anticipated resource property expenditures for fiscal year 2012 are budgeted at approximately \$29 million, with approximately \$26 million of these expenditures being allocated to Thor Lake for the BFS, metallurgical studies (including MPP and pilot plant tests), environmental studies and further definition drilling on the Nechalacho deposit.

The Company's present cash resources are sufficient to meet all of its current contractual obligations, administrative and overhead expenditures, and planned exploration and development work programs for at least the next twenty-four months. The Thor Lake, Warren Township, Separation Rapids, and Lilypad Lakes properties are all 100% owned by the Company with minimal holding costs, the most significant being annual lease rental fees on Thor Lake of \$20,998, annual claim renewal costs of approximately US\$110,000 related to the mining claims at Spor Mountain and the annual expenditures related to the mining lease at Separation Rapids totalling \$1,264.

Under the amended terms of the East Kemptville Special Licence, the Company had optional obligations to incur \$1.48 million in exploration expenditures by August 1, 2011. During the Quarter, the Company requested an extension from the Minister of Natural Resources of Nova Scotia to fulfill its expenditure obligations under the Special Licence by August 1, 2013. The Company has been verbally assured that the extension is forthcoming but formal confirmation was still pending as at November 22, 2011. There is no certainty that the extension will be granted, at which time the costs incurred to date on the special exploration licence will be written off.

A joint venture with an industry partner or end-user may represent an attractive alternative for financing the more advanced stages in the development of any of the Company's four advanced rare metals projects at Separation Rapids, Thor Lake, East Kemptville, or Warren Township projects, when capital requirements become relatively large.

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

The Company has two operating leases for its office premises. As at the date of this MDA, the minimum lease commitments under these leases are as follows:

2012	\$ 197,757
2013	\$ 279,544
2014	\$ 290,457
2015	\$ 296,967
2016	\$ 296,967
2017	\$ 98,989

Corporate Social Responsibility ("CSR")

The Company has embraced the principles of sustainability as core to its business practice and in 2008, the Company adopted the Principles and Guidelines for Responsible Exploration being developed by PDAC as policy of the Company. These principles for environmental and social best practice were announced by PDAC as part of the roll-out of its *e3 Plus* program ("Environmental Excellence in Exploration"), with the "Plus" referring largely to the inclusion of CSR principles as part of e3. In addition, the company has become an associate member of the Mining Association of Canada ("MAC"), with a view to gradual implementation of Towards Sustainable Mining ("TSM"). TSM is an initiative developed by the MAC to improve the industry's performance by aligning its actions with the priorities and values of Canadians. TSM provides a way of finding common ground with communities of interest in order to build a better mining industry, today and in the future. TSM is based on a set of guiding principles that are in turn supported by performance elements and indicators. The initiative is led by MAC's Board of Directors. Input and guidance come from the external Community of Interest Advisory Panel.

Since 2007, the Company has endeavoured to maximize Aboriginal employment at the site and partly through implementation of specific training initiatives have succeeded in maintaining 40-60% aboriginal of the 30 plus employees at the Thor Lake site. In addition, major service contracts for expediting and air charter services are with companies partnered with Aboriginal groups. During the quarter ended August 31, 2011, meetings were also held with each of the impacted Dene communities to discuss the Company's progress on its PFS, permitting, metallurgy, BFS and accommodation agreements. The impacted First Nations approached Avalon with regards to generating business capacity within their communities through future contracts related to the construction and operations phases of the Project. Avalon is currently awaiting a combined proposal from the Dene Communities which will set the groundwork for future construction and contractual opportunities.

Off Balance Sheet Arrangements

As at August 31, 2011, the Company had no material off balance sheet arrangements such as guaranteed contracts, contingent interests in assets transferred to an entity, derivative instrument obligations or any instruments that could trigger financing, market or credit risk to the Company.

Transactions with Related Parties

All transactions with related parties are in the normal course of business and are measured at the exchange amount. During the year ended August 31, 2011, the Company incurred:

- a) incurred consulting fees of \$81,250 with a company owned by an officer, of which \$56,250 were deferred as resource property costs;
- b) incurred consulting fees of \$45,354 with a person who is related to an officer, which were deferred as resource property costs. As at August 31, 2011, accounts payable included \$14,800 payable to this person;
- c) incurred consulting fees of \$36,000 with an officer. As at August 31, 2011, accounts payable included \$3,390 payable to this officer;

- d) incurred rental fees of \$20,750 for an apartment in Yellowknife, NT. with a company owned by a director, which were deferred as resource property costs; and
- e) issued 60,000 common shares at a price of \$5.81 per share to a director of the Company pursuant to the August 2011 Prospectus Offering.

Subsequent Events

Subsequent to the year ended August 31, 2011, the Company:

- a) issued 64,991 common shares pursuant to the exercise of an equivalent number of share purchase warrants for cash proceeds of \$198,508;
- b) issued 130,000 common shares pursuant to the exercise of an equivalent number of stock options for cash proceeds of \$279,250;
- c) issued 74,083 common shares and 37,041 warrants pursuant to the exercise of 74,083 Brokers' Compensation Warrants for cash proceeds of \$185,420;
- d) granted an aggregate of 425,000 stock options with a weighted average exercise price of \$3.77 per share to the Company's employees, officers, directors and technical advisory committee members. The weighted average contract life of these options was 5 years and the weighted average grant-date fair value of these stock options was \$2.68;
- e) granted 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 \$3.15 per share until October 12, 2013;
- f) cancelled 125,000 stock options with an weighted average exercise price of \$3.29 per share;
- g) had 3,889,633 share purchase warrants with the exercise price of \$3.60 per share expire unexercised; and
- h) had brokers' over-allotment option to purchase up to 472,100 common shares at the price of \$5.81 (or US\$6.15) per share expire unexercised.

Proposed Transactions

The Company is doing some project generative work through geological research into prospective new areas for rare metals deposits as described above, which resulted in the acquisition of two new mineral properties in Utah and in New Brunswick. A few other opportunities are under active review that could result in a decision to acquire additional mineral claims at any time.

The Company has no immediate plans for any equity offerings, but is in discussion with a number of potential strategic partners about off-take of rare metals products and project financing for the Nechalacho deposit. This could involve either equity financing or formation of a joint venture.

Critical Accounting Estimates

Critical accounting estimates used in the preparation of the financial statements include the value of stock-based compensation and the Company's estimate of recoverable value of its resource properties. These estimates involve considerable judgment and are, or could be, affected by significant factors that are out of the Company's control.

The factors affecting stock-based compensation include estimates of when stock options might be exercised and the stock price volatility. The timing for exercise of options is out of the Company's control and will depend upon a variety of factors, including the market value of the Company's shares and the financial objectives of the stock-based instrument holders.

The Company's recoverability of the recorded value of its resource properties is based on market conditions for minerals, underlying mineral resources associated with the properties and future costs that may be required for ultimate realization through mining operations or by sale. The Company is in an industry that is dependent on a number of factors, including environmental and legal risks, the existence of economically recoverable reserves, and the ability of the Company to obtain necessary financing to complete the development and future profitable production of its properties or to secure any proceeds from their disposition.

Changes in Accounting Policies Including Initial Adoption

There were no changes in accounting policies or newly adopted policies during the Quarter.

Recent accounting pronouncements issued and not yet effective:

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 Company will thus apply IFRS in Fiscal 2012. The Company will require restatement for comparative purposes of amounts reported by the Company for the year ending August 31, 2011 and accordingly the Company will need to prepare an opening balance sheet, in accordance with IFRS, as at September 1, 2010.

The Company has identified a three-phase transition plan: Phase 1 - initial diagnostic assessment and scoping, which involves the identification of significant differences between existing Canadian GAAP and IFRS as relevant to the Company's specific situation; Phase 2 - in-depth analysis and assessment, which involves the identification, evaluation and selection of the accounting policies necessary for the Company to changeover to IFRS; and Phase 3 -implementation, which will identify and implement updates to any internal procedures and systems in order for the Company to comply with IFRS requirements.

The Company has completed Phase 1, substantially completed Phase 2 and is currently engaged in Phase 3.

The differences that have been identified during Phase 1 are summarized below:

Resource Properties

Upon adoption of IFRS the Company will have a choice between continuing its existing policy of capitalizing all pre-feasibility exploration and development expenditures and electing to change its policy retrospectively to expense some or all of these costs. The Company has decided to retain its policy of capitalizing its resource property expenditures and further determined that the adoption of the provisions of "IFRS 6 - Exploration for and Evaluation of Mineral Resources" will not result in any significant transitional impact at September 1, 2010.

Stock-based Compensation

Under "IFRS 2 - Stock based compensation", when a share-based payment award vests in installments over the vesting period, each installment is accounted for separately. A distinct fair value must be determined for each vesting tranche. Canadian GAAP allows pooling and recognizing compensation on a straight-line basis. The Company has been recording stock based compensation on a straight line basis under Canadian GAAP so this will affect the compensation expense recorded.

For vesting conditions based on other than market conditions, IFRS 2 requires a company to calculate the expense based on the best available estimate of forfeitures. Under Canadian GAAP, the Company has not used forfeiture estimates in the stock-based compensation calculation.

Share-based payments to non-employees are measured based on the fair value of the goods or services received, at the date of receiving those goods or services whereas GAAP allows for measurement of the fair value of the award or fair value of the goods or services received. In the past, the Company has measured stock-based awards to non-employees based on the fair value of the award.

The Company plans to elect under "IFRS 1 - First Time Adoption of International Financial Reporting Standards" not to apply the requirement of IFRS 2 to stock options granted on or before September 1, 2002 and to those stock options that have fully vested on or before the transition date of September 1, 2010. The Company will re-measured its unvested stock options as at September 1, 2010 and include an estimated forfeiture rate in the stock-based compensation calculation, which may require an adjustment to deficit.

Accounting for Income Taxes with Respect to Flow-Through Shares

The Company has periodically financed its exploration activities by the issuance of flow-through shares. Income tax credits associated with these flow-through shares have all been renounced and all qualifying expenditures had been incurred prior to September 1, 2010.

There is no specific standard under IFRS that directly deals with flow-through shares, however under Canadian GAAP, since March 19, 2004 (the adoption date of EIC-146), the Company has been reducing the net proceeds of the flow-through share issuance by the future tax liability of the Company resulting from the renunciation of the exploration and development expenditures in favour of the flow-through share subscribers. Future income tax assets (loss carry forwards and/or deductible temporary differences) not previously recognized as a result of applying the "more likely than not" test are recognized as a reduction of the future income tax liability through a credit in the income statement.

The impact of the adoption of IFRS will be to reduce share capital and reduce deficit by a corresponding amount.

Provision for Mine Closures and/or Environmental Rehabilitation

IFRS 37 applies to a constructive obligation, where the event creates valid expectations that the entity will discharge the obligation, as well as a legal obligation. The amount recognized should be the best estimate of the expenditure required to settle the obligation at the balance sheet date. Present value should be used where the effect of the time value of money is material. The discount rate (or rates) utilized should be a pre-tax rate (or rates) that reflect(s) current market assessments of the time value of money and the risks specific to the liability. Provisions should be reviewed at each balance sheet date and adjusted to reflect the current best estimate. The Company has determined that there is no transitional impact.

Property, Plant & Equipment

IFRS-1 provides a choice between measuring property, plant and equipment at its fair value at the date of transition and using those amounts as deemed cost or using the historical valuation under the prior GAAP. The Company has decided to elect to use the historical cost carrying values as determined under Canadian GAAP for transitional purposes.

The Company does not anticipate any significant changes to its information technology, internal controls over financial reporting, disclosure controls and procedures or its business activities as a result of the conversion to IFRS. However, the Company expects to implement certain minor changes to its account descriptions as well as the calculation methodologies it currently uses for certain specific financial statement areas (e.g. share based compensation).

The International Accounting Standards Board continues to amend and add to current IFRS standards with several projects currently underway. The Company will continue to monitor the actual and anticipated changes to IFRS standards and the related rules and regulations and assess the impacts of these changes on the Company and its financial reporting.

Financial Instruments and Other Risk Factors

The Company's financial instruments consist of cash and cash equivalents, receivables, and accounts payable.

Management does not believe these financial instruments expose the Company to any significant interest, currency or credit risks arising from these financial instruments. The fair market values of cash and cash equivalents, receivables and accounts payable approximate their carrying values. Investments available for sale are carried at fair market value.

In conducting its business, the principal risks and uncertainties faced by the Company relate to exploration and development success as well as metal prices and market sentiment to a lesser extent.

Exploration for minerals and development of mining operations involve significant risks, including but not limited to economic risks, regulatory risks, environmental risks, and risks associated with

land title disputes including Aboriginal land title claims. In addition to the normal and usual risks of exploration and mining, the Company often works in remote locations that lack the benefit of infrastructure and easy access.

The prices of metals fluctuate widely and are affected by many factors outside of the Company's control. The relative prices of metals and future expectations for such prices have a significant impact on the market sentiment for investment in mining and mineral exploration companies. The Company relies on equity financing for its long term working capital requirements and to fund its exploration programs. The Company does not anticipate using existing funds to put any of its resource interests into production from its own financial resources. There is no assurance that other forms of financing will be available to the Company, or that such will be available on acceptable terms.

An additional risk factor that has developed over the past two years is access to adequate human resources to carry out work programs, particularly skilled professionals for which there is currently an industry-wide shortage, which can cause delays completing work programs on schedule and in meeting program budgets.

Disclosure Controls and Procedures

Disclosure controls and procedures are designed to provide reasonable assurance that material information is gathered and reported to senior management, including the Chief Executive Officer and Chief Financial Officer, as appropriate, to permit timely decisions regarding public disclosure.

Management, including the Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of the design and operation of the Company's disclosure controls and procedures as of August 31, 2011. Based on this evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that the Company's disclosure controls and procedures, as defined in Multilateral Instrument 52-109 - Certification of Disclosure in Issuer's Annual and Interim Filings, are designed effectively to ensure that the information required to be disclosed in reports that are filed or submitted under Canadian securities legislation are recorded, processed, summarized and reported within the time period specified in those rules.

During the process of review and evaluation, it was determined that the Company's disclosure controls and procedures are operating effectively as at August 31, 2011.

Design of Internal Controls

The Company evaluated the design of its internal controls and procedures over financial reporting, as defined under Multilateral Instrument 52-109, for the year ended August 31, 2011. This evaluation was performed by the Chief Executive Officer and the Chief Financial Officer, with the assistance of other corporate personnel to the extent necessary or appropriate. Based on this evaluation, the Chief Executive Officer and the Chief Financial Officer concluded that the design of these internal controls and procedures over financial reporting was effective.

The Company has very limited administrative staffing and in many instances, the implementation of internal controls relying on segregation of duties is not possible. The Company relies on senior management review and approval to ensure that the controls are as effective as possible.

There has been no change in the Company's internal control over financial reporting during Quarter.

Outstanding Share Data

a) *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.

As at August 31, 2011, the Company had 102,617,912 common shares issued and outstanding. Subsequent to the year ended August 31, 2011, the Company issued 269,074 common shares pursuant to the exercises stock options, warrants and brokers' compensation warrants. Accordingly, as at the date of this MDA, the Company had 102,886,986 common shares outstanding.

b) *Options*

As at August 31, 2011, the Company had an aggregate of 6,305,250 incentive stock options outstanding with a weighted average exercise price of \$3.38 (of which 2,549,000 were vested and 3,756,250 were unvested). Subsequent to the year ended August 31, 2011, 130,000 of these options were exercised, 475,000 stock options were granted and 125,000 stock options were cancelled (as described earlier under "Subsequent Events"). As at the date of this MDA, the Company has 6,525,250 incentive stock options with a weighted average exercise price of \$3.29 outstanding.

Other Information

Additional information on the Company is available on SEDAR at www.sedar.com and on the Company's website at www.avalonraremetals.com.

Notice Regarding Presentation of our Mineral Reserve and Resource Estimates

This MDA has been prepared in accordance with the requirements of Canadian securities laws, which differ from the requirements of United States securities laws. Unless otherwise indicated, all reserve and resource estimates included in this MDA have been prepared in accordance with NI 43-101. NI 43-101 is a rule developed by the Canadian Securities Administrators which establishes standards for all public disclosure an issuer makes of scientific and technical information concerning mineral projects.

Canadian standards, including NI 43-101, differ significantly from the requirements of the United States Securities and Exchange Commission (the "SEC"), and reserve and resource information contained in this MDA may not be comparable to similar information disclosed by United States companies. In particular, and without limiting the generality of the foregoing, the term "resource" does not equate to the term "reserve". Under United States standards, mineralization may not be classified as a "reserve" unless the determination has been made that the mineralization could be

economically and legally produced or extracted at the time the reserve determination is made. The SEC's disclosure standards normally do not permit the inclusion of information concerning "measured mineral resources", "indicated mineral resources" or "inferred mineral resources" or other descriptions of the amount of mineralization in mineral deposits that do not constitute "reserves" by United States standards in documents filed with the SEC. United States investors should also understand that "inferred mineral resources" have a great amount of uncertainty as to their existence and as to their economic and legal feasibility. It cannot be assumed that all or any part of an "inferred mineral resource" exists, is economically or legally mineable, or will ever be upgraded to a higher category. Under Canadian rules, estimated "inferred mineral resources" may not form the basis of feasibility or pre-feasibility studies except in rare cases. Disclosure of "contained ounces" in a resource estimate is permitted disclosure under Canadian regulations; however, the SEC normally only permits issuers to report mineralization that does not constitute "reserves" by SEC standards as in-place tonnage and grade without reference to unit measures. The requirements of NI 43-101 for identification of "reserves" are also not the same as those of the SEC, and reserves reported by Avalon in compliance with NI 43-101 may not qualify as "reserves" under SEC standards. Accordingly, information concerning mineral deposits set forth herein may not be comparable with information made public by companies that report in accordance with United States standards.



Consolidated Financial Statements

**For the years ended
August 31, 2011, 2010 and 2009**

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MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL REPORTING

The consolidated financial statements and other financial information for this annual report were prepared by the management of Avalon Rare Metals Inc. 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 consolidated 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 also accepts responsibility for ensuring the use of appropriate accounting policies and estimates in disclosure of information prepared following accounting principles generally accepted in the United States of America. Management has included amounts in the company's consolidated 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.

McCarney Greenwood LLP, Chartered Accountants were appointed as auditors by the shareholders the Company.

"Donald S. Bubar"
President and CEO

"R. J. (Jim) Andersen"
CFO and Vice President Finance

Toronto, Ontario
November 22, 2011

INDEPENDENT AUDITORS' REPORT

To the Shareholders of
Avalon Rare Metals Inc.

Report on the consolidated financial statements

We have audited the accompanying consolidated financial statements of Avalon Rare Metals Inc. ("the Company") which comprise the consolidated balance sheets as at August 31, 2011, 2010 and 2009 and the consolidated statements of operations and deficit, comprehensive loss and cash flows for each of the years then ended and a summary of significant accounting policies and other explanatory information.

Management's responsibility for the consolidated financial statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with Canadian generally accepted accounting principles, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' responsibility

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 and with the standards of the Public Company Accounting Oversight Board (United States of America). Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Avalon Rare Metals Inc. as at August 31, 2011, 2010 and 2009 and its results of operations and its cash flows for each of the years then ended in accordance with Canadian generally accepted accounting principles.

"McCarney Greenwood LLP"

Toronto, Canada
November 22, 2011

McCarney Greenwood LLP
Chartered Accountants
Licensed Public Accountants

Consolidated Balance Sheets As at August 31

	2011	2010	2009
Assets			
Current Assets			
Cash and cash equivalents	\$ 70,858,678	\$ 6,932,125	\$ 6,003,782
Receivables	650,454	1,057,660	598,468
Prepaid expenses	921,748	194,080	118,037
	<u>72,430,880</u>	<u>8,183,865</u>	<u>6,720,287</u>
Investments Available for Sale (note 3)	-	-	2,657
Resource Properties (note 4)	50,475,040	32,646,738	19,677,856
Property, Plant and Equipment (note 5)	<u>987,633</u>	<u>696,112</u>	<u>120,464</u>
	<u>\$ 123,893,553</u>	<u>\$ 41,526,715</u>	<u>\$ 26,521,264</u>
Liabilities			
Current Liabilities			
Accounts payable (note 10)	<u>\$ 3,792,595</u>	<u>\$ 2,178,140</u>	<u>\$ 1,429,712</u>
Shareholders' Equity			
Share Capital (note 6)	146,684,649	58,263,175	44,828,738
Contributed Surplus (note 7)	9,719,348	7,967,053	3,054,653
Deficit	(36,303,039)	(26,881,653)	(22,782,353)
Accumulated Other Comprehensive Loss (note 8)	<u>-</u>	<u>-</u>	<u>(9,486)</u>
	<u>120,100,958</u>	<u>39,348,575</u>	<u>25,091,552</u>
	<u>\$ 123,893,553</u>	<u>\$ 41,526,715</u>	<u>\$ 26,521,264</u>
Nature of Operations (note 1)			
Commitments (note 13, 14)			
Subsequent Events (note 18)			

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

Approved on behalf of the Board of Directors:

"Donald S. Bubar" _____, Director

"Brian MacEachen" _____, Director

Consolidated Statements of Operations and Deficit For the Years Ended August 31

	2011	2010	2009
Revenue			
Interest	\$ 605,142	\$ 80,557	\$ 159,982
Expenses			
Amortization	173,302	81,385	50,466
Consulting fees (note 10)	166,245	117,769	45,788
Directors' fees	198,050	104,400	38,000
Insurance	203,941	73,391	63,359
Interest and financing costs (note 6b)	8,549	10,581	13,485
Office and general	95,344	83,404	31,418
Professional fees (note 10)	494,417	143,475	179,736
Public and investor relations	876,036	778,647	593,728
Rent and utilities	252,842	160,479	111,978
Salaries and benefits	1,600,985	647,788	522,294
Shareholders' information	105,651	48,211	27,311
Stock-based compensation (note 7b)	5,074,444	2,041,755	1,016,933
Transfer and filing fees	496,168	165,554	67,969
Travel	332,762	257,715	152,536
	<u>10,078,736</u>	<u>4,714,554</u>	<u>2,915,001</u>
Loss before the Undernoted Items	(9,473,594)	(4,633,997)	(2,755,019)
Foreign Exchange Gain (Loss)	52,208	4,331	(6,341)
Write-down of Resource Properties (note 4f)	-	-	(598,559)
Loss on Sale of Investments	-	(9,837)	-
Loss before Income Taxes	(9,421,386)	(4,639,503)	(3,359,919)
Future Income Tax Recoveries (note 11g)	-	540,203	405,000
Net Loss for the Year	(9,421,386)	(4,099,300)	(2,954,919)
Deficit - Beginning of Year	<u>(26,881,653)</u>	<u>(22,782,353)</u>	<u>(19,827,434)</u>
Deficit - End of Year	<u>\$ (36,303,039)</u>	<u>\$ (26,881,653)</u>	<u>\$ (22,782,353)</u>
Loss per Share, Basic and Fully Diluted	<u>\$ (0.10)</u>	<u>\$ (0.05)</u>	<u>\$ (0.04)</u>
Weighted Average Number of Common Shares Outstanding, Basic and Fully Diluted	<u>93,074,790</u>	<u>77,865,072</u>	<u>67,603,514</u>

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

Consolidated Statements of Comprehensive Loss For the Years Ended August 31

	2011	2010	2009
Net Loss for the Year	\$ (9,421,386)	\$ (4,099,300)	\$ (2,954,919)
Other Comprehensive Income (Loss)			
Unrealized gains (losses) on available-for-sale financial assets arising during the year	-	-	(1,286)
Reclassification of previously unrealized losses on investments available for sale to net loss	-	9,486	-
Comprehensive Loss for the Year	<u>\$ (9,421,386)</u>	<u>\$ (4,089,814)</u>	<u>\$ (2,956,205)</u>

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

Consolidated Cash Flow Statements For the Years Ended August 31

	2011	2010	2009
Cash Flows from Operating Activities			
Cash paid to suppliers and employees	\$ (4,752,468)	\$ (2,518,676)	\$ (1,954,458)
Interest received	605,142	80,557	159,982
Interest paid	-	(3,264)	(72,969)
	<u>(4,147,326)</u>	<u>(2,441,383)</u>	<u>(1,867,445)</u>
Cash Flows from Financing Activities			
Share capital - equity offering(s) (note 6b)	69,497,735	16,106,016	1,400,625
Share capital - exercise of warrants (note 6b)	12,015,282	78,125	903,040
Share capital - exercise of options (note 6b)	2,091,766	661,144	516,625
Share capital - exercise of agents/brokers' compensation options/warrants (note 6b)	1,808,980	-	1,123,750
	<u>85,413,763</u>	<u>16,845,285</u>	<u>3,944,040</u>
Cash Flows from Investing Activities			
Resource property expenditures	(16,930,577)	(12,952,164)	(6,811,513)
Resource property - government contributions	-	131,332	-
Proceeds from sale of investments	-	2,306	-
Purchase of property, plant and equipment	(464,823)	(657,033)	-
	<u>(17,395,400)</u>	<u>(13,475,559)</u>	<u>(6,811,513)</u>
Change in Cash and Cash Equivalents	63,871,037	928,343	(4,734,918)
Foreign Exchange Effect on Cash	55,516	-	-
Cash and Cash Equivalents - Beginning of Year	<u>6,932,125</u>	<u>6,003,782</u>	<u>10,738,700</u>
Cash and Cash Equivalents - End of Year	<u>\$ 70,858,678</u>	<u>\$ 6,932,125</u>	<u>\$ 6,003,782</u>

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

1. Nature of Operations

The Company is in the process of exploring and developing 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 principally in one geographic area, Canada, and in one industry segment, mining exploration and development. During the year ended August 31, 2011 the Company's wholly-owned subsidiary Nolava Minerals Inc. commenced its exploration activities in the United States of America.

2. Summary of Significant Accounting Policies

a) Basis of Presentation

These consolidated financial statements are prepared in accordance with accounting principles generally accepted in Canada.

During the year ended August 31, 2011, the Company set up two wholly-owned subsidiaries Nolava Minerals Inc. and Avalon Rare Metals Processing Inc. Neither of these two subsidiaries has carried on any significant operations since their inceptions except for the acquisition of certain mining claims by Nolava Minerals Inc. as disclosed in Note 4.

These consolidated financial statements include the accounts of the Company and those of its wholly-owned subsidiaries. All intercompany accounts and transactions have been eliminated.

b) Capital Disclosures

Handbook Section 1535 requires disclosure of an entity's objectives, policies and process 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. The Company has included disclosures recommended by this Handbook section in note 9.

c) 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. These estimates are reviewed periodically and any adjustments necessary are reported income in the period they become known.

2. Summary of Significant Accounting Policies (continued)

d) Financial Instruments

Financial instruments are initially recognized at fair value and are subsequently re-measured based on their classification as: held-for-trading, available-for-sale, held-to-maturity, loans and receivables or other liabilities. Financial assets and liabilities held-for-trading are measured at fair value with the change in the fair value recognized in net income. Available-for-sale instruments are measured at fair value with any unrealized gains or losses recognized in other comprehensive income. Financial assets held-to-maturity, loans and receivables and financial liabilities other than those held-for-trading are measured at amortized cost, using the effective interest method.

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 value through statement of operations
Receivables	Loans and receivables	Amortized cost
Investments available for sale	Available-for-sale	Fair value through other comprehensive income
Accounts payable	Other financial liabilities	Amortized cost

e) 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.

f) 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.

The Company is in the process of exploring and developing its mineral properties and, other than on its Thor Lake property, 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.

g) 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:

Airstrip	-	8% on a declining balance basis
Computer equipment	-	30% on a declining balance basis
Computer software	-	33 1/3% on a declining balance basis
Exploration equipment	-	30% on a declining balance basis
Office furniture and equipment	-	25% on a declining balance basis
Leasehold improvements	-	straight line basis over the term of the lease

2. Summary of Significant Accounting Policies (continued)

g. Property, Plant and Equipment (continued)

Additions during the year are amortized using one-half of the normal rates.

The Company reviews property plant and equipment for impairment whenever events or changes in circumstances indicate that the carrying values are not recoverable, when indicators of impairment exist, and the carrying values are not greater than the sum of the undiscounted future net cash flows, an impairment loss is recognized to the extent the carrying value exceeds the fair value.

h) Asset Retirement Obligations

The Company will recognize the legal liability for obligations relating to the retirement of property, plant and equipment, and arising from the acquisition, construction, development, or normal operation of those assets in the period in which the liability is incurred. Such asset retirement costs will be recognized at fair value, when a reasonable estimate of fair value can be estimated, added to the carrying value of the related asset, and amortized into income on a systematic basis over the related asset's useful life. The liability will be adjusted for changes in the expected amounts and timing of cash flows required to discharge the liability and accreted to full value over time through periodic charges to net income.

As at August 31, 2011, no asset retirement obligations have been recognized as none of the Company's properties are estimated to require any remediation or other expenditures upon their retirement.

i) 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.

j) Flow-through Shares

A portion of the Company's exploration activities is 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.

k) Income Taxes

Future tax assets and liabilities are measured using substantially 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.

l) Stock Option Compensation

The Company has one stock option plan that is described in note 7(b). 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.

2. Summary of Significant Accounting Policies (continued)

m) Foreign Currency Transactions and Translation

The Company's functional currency is the Canadian dollar. 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. Non-monetary assets and liabilities are translated at the rates of exchange prevailing when the assets were acquired or the liabilities were assumed. Unrealized gains and losses on translation of monetary assets and liabilities are included in the determination of earnings for the year.

n) Related Party Transactions

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

o) Share Issuance Costs

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

p) 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.

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.

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.

As at August 31, 2011 and 2010, the Company had no investments. The investments consisted of the following as at August 31, 2009:

	2009	
	Number	Amount
Alto Ventures Inc.	28,571	\$ 857
Tiomin Resources Inc. ⁽¹⁾	45,000	1,800
		<u>\$ 2,657</u>

⁽¹⁾ Received in exchange for 45,000 shares of Radiant Resources Inc. as a result of the acquisition of Radiant Resources Inc. by Tiomin Resources Inc.

Notes to the Consolidated Financial Statements
For the Years Ended August 31, 2011, 2010 and 2009

4. Resource Properties

	August 31, 2011						
	Separation Rapids Lithium- Tantalum Project	Warren Township Anorthosit Project	Thor Lake Rare Metals Project	East Kemptville Rare Project	Spor Mountain Rare Project	Other	Total
note	4(a)	4(b)	4(c)	4(d)	4(e)	4(f,g)	
Property costs	\$ -	\$ -	\$ -	\$ -	\$ 437,027	\$ -	\$ 437,027
Community consultation	-	-	676,823	-	-	-	676,823
Diamond drilling	-	-	8,874,229	-	-	-	8,874,229
Environmental studies/permitting	5,350	2,750	1,362,923	-	-	-	1,371,023
Feasibility/engineering studies	-	600	1,901,454	-	-	-	1,902,054
Geology	6,492	-	899,475	22,427	134,543	70,001	1,132,938
Geophysical	-	-	-	-	65,290	-	65,290
Metallurgical/market studies	52,883	25,231	3,203,207	-	-	-	3,281,321
Other	5,916	4,680	21,524	-	55,477	-	87,597
Current expenditures	70,641	33,261	16,939,635	22,427	692,337	70,001	17,828,302
Balance - beginning of year	3,880,260	1,198,787	26,210,251	1,357,440	-	-	32,646,738
Balance - end of year	\$ 3,950,901	\$ 1,232,048	\$ 43,149,886	\$ 1,379,867	\$ 692,337	\$ 70,001	\$ 50,475,040

Notes to the Consolidated Financial Statements
For the Years Ended August 31, 2011, 2010 and 2009

4. Resource Properties (continued)

	August 31, 2010					
	Separation Rapids Lithium- Tantalum Project	Warren Township Anorthosit Project	Thor Lake Rare Metals Project	East Kemptville Rare Project	Other	Total
note	4(a)	4(b)	4(c)	4(d)	4(f,g)	
Property costs	\$ 1,750	\$ -	\$ -	\$ -	\$ -	\$ 1,750
Community consultation	-	-	315,142	-	-	315,142
Diamond drilling	-	-	7,137,159	186,947	-	7,324,106
Environmental studies/permitting	3,578	275	988,675	750	-	993,278
Feasibility/engineering studies	-	-	1,649,186	122,229	-	1,771,415
Geochemical	-	-	-	24,827	-	24,827
Geology	5,170	-	710,784	133,209	-	849,163
Geophysical	-	-	8,625	59,944	-	68,569
Linecutting	-	-	-	10,990	-	10,990
Metallurgical/market studies	11,375	294	1,612,380	35,777	-	1,659,826
Other	1,150	3,600	27,850	-	-	32,600
Current expenditures	23,023	4,169	12,449,801	574,673	-	13,051,666
Less: amounts recovered from:						
Government contributions	-	-	(82,784) ⁽¹⁾	-	-	(82,784)
Net current expenditures	23,023	4,169	12,367,017	574,673	-	12,968,882
Balance - beginning of year	3,857,237	1,194,618	13,843,234	782,767	-	19,677,856
Balance - end of year	\$ 3,880,260	\$ 1,198,787	\$ 26,210,251	\$ 1,357,440	\$ -	\$ 32,646,738

⁽¹⁾Contributions received from the Mine Training Society of the Northwest Territories ("MTS") under the Driller Training Program Contribution Agreement between the Company and MTS.

Notes to the Consolidated Financial Statements
For the Years Ended August 31, 2011, 2010 and 2009

4. Resource Properties (continued)

	August 31, 2009					
	Separation Rapids Lithium- Tantalum Project	Warren Township Anorthosit Project	Thor Lake Rare Metals Project	East Kemptville Rare Project	Other	Total
note	4(a)	4(b)	4(c)	4(d)	4(f,g)	
Property costs	\$ -	\$ -	\$ 590	\$ -	\$ -	\$ 590
Community consultation	-	3,325	204,462	-	-	207,787
Diamond drilling	-	-	3,365,819	-	-	3,365,819
Environmental studies/permitting	70,302	996	1,125,276	-	-	1,196,574
Feasibility/engineering studies	3,120	67	504,770	159,019	-	666,976
Geochemical	-	-	-	32,348	-	32,348
Geology	-	-	397,565	105,973	295	503,833
Geophysical	-	-	87,121	-	-	87,121
Metallurgical/market studies	60,387	4,125	903,214	76,586	-	1,044,312
Other	9,479	300	21,198	-	-	30,977
Current expenditures	143,288	8,813	6,610,015	373,926	295	7,136,337
Less: amounts recovered from:						
Government contributions	-	-	(48,548) ⁽¹⁾	-	-	(48,548)
Net current expenditures	143,288	8,813	6,561,467	373,926	295	7,087,789
Balance - beginning of year	3,713,949	1,185,805	7,281,767	408,841	598,264	13,188,626
Write-down of resource properties	-	-	-	-	(598,559)	(598,559)
Balance - end of year	\$ 3,857,237	\$ 1,194,618	\$ 13,843,234	\$ 782,767	\$ -	\$ 19,677,856

⁽¹⁾Contributions received from the Mine Training Society of the Northwest Territories ("MTS") under the Driller Training Program Contribution Agreement between the Company and MTS.

4. Resource Properties (continued)

a) Separation Rapids Rare Metals Project, Ontario

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 and a mining lease 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 a 100% interest (subject to a 5.5% NSR), of which 2.5% can be bought back at the principal amount of \$150,000 compounded annually at the average Canadian prime rate from May 2, 1982 to the buyback date (as at August 31, 2010, this amounted to approximately \$1.2 million), in five mining leases covering the Thor Lake rare metals deposit located in the Mackenzie Mining District of the Northwest Territories. In addition, three mineral claims were staked in 2009 to cover favourable geology to the west of the mining leases.

d) 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 four claims in the East Kemptville area of Yarmouth, Nova Scotia. In order to keep the licence in good standing, the Company was required to incur \$2,250,000 in exploration expenditures by August 1, 2011, of which \$777,941 had been incurred by August 31, 2011. During the quarter ended August 31, 2011, the Company requested an extension from the Minister of Natural Resources of Nova Scotia to fulfill its expenditure obligations under the Special Licence by August 1, 2013. The Company has been verbally assured that the extension is forthcoming but formal confirmation was still pending as at November 22, 2011. There is no certainty that the extension will be granted, at which time the costs incurred to date on the special exploration licence will be written off.

The Company also has a number of regular exploration licences covering certain mineral claims in the same proximity to the claims covered under the special exploration licence.

e) Spor Mountain Rare Metals Project, Utah

The Company owns a 100% interest in certain claims located in Juab County, Utah, USA, which were staked by the Company during the year ended August 31, 2011.

f) Write-down of Resource Properties

No resource properties were written down during the years ended August 31, 2011 and 2010.

During the year ended August 31, 2009 the Company decided not to fund any further expenditures on the Red Hill Copper-Zinc-Silver Project in British Columbia, and the total costs incurred to August 31, 2009 of \$598,559 had been written off.

Notes to the Consolidated Financial Statements
For the Years Ended August 31, 2011, 2010 and 2009

4. Resource Properties (continued)

g) 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

	2011		
	Cost	Accumulated Amortization	Net
Airstrip	\$ 523,242	\$ 61,115	\$ 462,127
Computer equipment	49,794	21,492	28,302
Computer software	69,694	18,176	51,518
Exploration equipment	629,724	220,407	409,317
Office furniture and equipment	53,342	20,475	32,867
Leasehold improvements	29,928	26,426	3,502
	\$ 1,355,724	\$ 368,091	\$ 987,633

	2010		
	Cost	Accumulated Amortization	Net
Airstrip	\$ 523,242	\$ 20,930	\$ 502,312
Computer equipment	28,064	14,019	14,045
Computer software	13,214	6,539	6,675
Exploration equipment	276,996	135,286	141,710
Office furniture and equipment	35,861	12,433	23,428
Leasehold improvements	25,725	17,783	7,942
	\$ 903,102	\$ 206,990	\$ 696,112

	2009		
	Cost	Accumulated Amortization	Net
Computer equipment	\$ 25,520	\$ 17,708	\$ 7,812
Computer software	7,395	4,656	2,739
Exploration equipment	183,590	94,569	89,021
Office furniture and equipment	18,866	7,455	11,411
Leasehold improvements	18,963	9,482	9,481
	\$ 254,334	\$ 133,870	\$ 120,464

Notes to the Consolidated Financial Statements
For the Years Ended August 31, 2011, 2010 and 2009

6. Share Capital

a) Authorized

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.

b) Common Shares Issued and Outstanding:

	<u>Number</u>	<u>Amount</u>
Balance - August 31, 2008	64,649,748	\$ 40,032,502
Issued pursuant to:		
private placement(s)	3,000,000	1,500,000
exercise of warrants	1,302,200	1,394,755
exercise of options	1,127,500	892,578
exercise of agents' compensation options	725,000	1,549,470
Finder's fees - paid cash	-	(99,375)
Finder's fees - compensation warrants issued	-	(36,192)
Tax effect on issuance of flow-through shares	-	(405,000)
	<hr/>	<hr/>
Balance - August 31, 2009	70,804,448	\$ 44,828,738
Issued pursuant to:		
private placement(s)	7,500,000	14,083,743
exercise of warrants	156,250	106,578
exercise of options	643,600	1,405,605
Cancellation of fractional shares	(28)	-
Commission - cash paid	-	(844,993)
Commission - brokers' compensation warrants issued	-	(488,925)
Other issuance costs	-	(287,368)
Tax effect on issuance of flow-through shares	-	(540,203)
	<hr/>	<hr/>
Balance - August 31, 2010	79,104,270	\$ 58,263,175
Issued pursuant to:		
prospectus offering(s)	16,932,900	71,340,213
exercise of warrants	4,401,475	15,608,329
exercise of options	1,526,150	4,517,609
exercise of brokers' compensation warrants	653,117	2,462,173
Commission - cash paid	-	(4,392,221)
Commission - compensation warrants issued	-	(204,835)
Other issuance costs	-	(909,794)
	<hr/>	<hr/>
Balance - August 31, 2011	<u>102,617,912</u>	<u>\$ 146,684,649</u>

6. Share Capital (continued)

During the year ended August 31, 2009 the Company:

- i) completed a private placement and issued 3,000,000 flow-through common shares at a price of \$0.50 per share for gross proceeds of \$1,500,000.

In connection with this private placement, the Company paid finders' fees of \$99,375 in cash and granted 198,750 non-transferable finders' warrants to the finders. Each warrant entitles the holder to purchase one common share at a price of \$0.50 per share, exercisable until December 15, 2010. The estimated fair value of the warrants totalled \$36,192.

- ii) issued 1,302,200 common shares pursuant to the exercise of an equivalent number of common share purchase warrants for cash proceeds of \$903,040. The estimated fair value at issuance of these options was \$491,715, and this amount has been added to the recorded value of the issued shares.
- iii) issued 1,127,500 common shares pursuant to the exercise of an equivalent number of stock options for cash proceeds of \$516,625. The estimated fair value at issuance of these options was \$375,953, and this amount has been added to the recorded value of the issued shares.
- iv) issued 725,000 common shares pursuant to the exercise of an equivalent number of agents' compensation options for cash proceeds of \$1,123,750. The estimated fair value at issuance of these compensation options was \$425,720, and this amount has been added to the recorded value of the issued shares.

During the year ended August 31, 2010, the Company:

- i) completed an offering (the "September 2009 Offering") pursuant to an agreement (the "Offering Agreement") with a syndicate of underwriters and issued 6,745,000 Special Warrants ("Special Warrants") at a price of \$2.30 per Special Warrant and 755,000 Flow-Through Special Warrants ("FT Special Warrants") at price \$2.65 per FT Special Warrant for total gross proceeds of \$17,514,250.

Each Special Warrant was exercisable into one unit (the "Series II Unit") of the Company without further payment. Each Series II Unit is comprised of one common share and one-half of a common share purchase warrant. Each whole warrant (a "Warrant") entitles the holder to purchase one additional common share of the Company, at a price of \$3.00 per common share, for a period of 24 months following September 17, 2009.

Each FT Special Warrant was exercisable into one flow-through common share of the Company without further payment.

All of the Special Warrants and FT Special Warrants were exercised during the year ended August 31, 2010, and accordingly, the Company issued 6,745,000 Series II Units and 755,000 flow-through common shares pursuant to these exercises.

Of the Special Warrant price of \$2.30, \$1.7914 was allocated to the common share component of the Series II Unit and the balance of \$0.5086 was allocated to the Warrant component of the Series II Unit.

These values were calculated on a pro rata basis based on the closing trading price of the Company's common shares on the date of the Offering Agreement, which was \$2.58, and the estimated fair value of a whole Warrant of \$1.4649 (which was estimated using the Black-Scholes pricing model, with the following assumptions: expected dividend yield of Nil; risk free interest rate of 1.28%; expected life of 2.0 years; and expected volatility of 117%).

6. Share Capital (continued)

In connection with the September 2009 Offering, the Company paid cash commissions totalling \$1,050,855 and issued 450,000 warrants ("Brokers' Compensation Warrants") to the underwriters of the 2009 Offering. Each Broker Warrant entitles the holder to purchase one Unit for a period of 24 months following September 17, 2009 at the exercise price of \$2.43 per Unit.

The estimated fair value of the Brokers' Compensation Warrants totalled \$608,040. The fair values of the Broker Warrants were estimated using the Black-Scholes pricing model, with the following assumptions: expected dividend yield of Nil; risk free interest rate of 1.28%; expected life of 2.0 years; and expected volatility of 117%.

The Company also paid other cash issuance costs of \$357,379 in connection to the September 2009 Offering.

The total transaction costs of \$2,016,274 (including cash commissions, the estimated fair value of the Brokers' Compensation Warrants 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 643,600 common shares pursuant to the exercise of an equivalent number of stock options for cash proceeds of \$661,144. The estimated fair value at issuance of these options was \$744,461, and this amount has been added to the recorded value of the issued shares.
- iii) issued 156,250 common shares pursuant to the exercise of an equivalent number of share purchase warrants for cash proceeds of \$78,125. The estimated fair value at issuance of these warrants was \$28,453, and this amount has been added to the recorded value of the issued shares.

During the year ended August 31, 2011, the Company:

- i) completed a short form prospectus offering and issued 9,240,000 units at a price of \$3.25 per unit for gross proceeds of \$30,030,000 ("September 2010 Offering"). Each unit consists of one common share and one-half of one common share purchase warrant. Each whole warrant entitles the holder to acquire one common share at a price of \$3.60 until September 30, 2011 (the "Unit").

Of the unit price of \$3.25, \$2.8836 was allocated to the common share component of the Unit and the balance of \$0.3664 was allocated to the warrant component of the Unit. These values were calculated on a pro rata basis based on the closing trading price of the Company's common shares on the date of the 2010 Offering which was \$3.58, and the estimated fair value of a whole warrant of \$0.9099.

In connection with the September 2010 Offering, the Company paid cash commissions totalling \$1,801,800 and issued 277,200 warrants ("Brokers' Compensation Warrants") to the underwriters of the September 2010 Offering. Each Brokers' Compensation Warrant entitles the holder to purchase one Unit for a period of 12 months following September 30, 2010 at the exercise price of \$3.25 per Unit. The estimated fair value of the Brokers' Compensation Warrants totalled \$230,852. The fair values of these warrants were estimated using the Black-Scholes pricing model, with the following assumptions: expected dividend yield of Nil; risk free interest rate of 1.39%; expected life of 1.0 years; and expected volatility of 64%.

The Company also paid other cash issuance costs of \$331,623 in connection to the September 2010 Offering.

The total transaction costs of \$2,364,275 (including cash commissions, the estimated fair value of the Brokers' Compensation Warrants 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.

6. Share Capital (continued)

- ii) completed a prospectus offering and issued 7,692,900 common shares (included 592,900 common shares issued pursuant to the partial exercise of the underwriters' option to purchase up to 1,065,000 additional common shares at the applicable offering price to cover over-allotments) at a price of \$5.81 (or US\$6.15) per share for gross proceeds of \$44,695,749 ("August 2011 Offering"), of which 60,000 common shares were issued to a director of the Company.

The Company paid cash commissions totalling \$2,793,484 to the underwriters of the August 2011 Offering and incurred other cash issuance costs of \$615,545 in connection to the this offering (of which \$314,438 were unpaid and included in accounts payable as at August 31, 2011).

As at August 31, 2011, the underwriters of the August 2011 Offering has the option to purchase up to 472,100 additional common shares at the same offering price of \$5.81 (or US\$6.15) to cover any over-allotments until September 2, 2011 ("Over-allotment Option"). The Over-allotment Option expired on September 2, 2011.

- iii) issued 4,401,475 common shares pursuant to the exercise of an equivalent number of share purchase warrants for cash proceeds of \$12,015,282. The estimated fair value at issuance of these warrants was \$3,593,047, and this amount has been added to the recorded value of the issued shares;
- iv) issued 1,526,150 common shares pursuant to the exercise of an equivalent number of stock options for cash proceeds of \$2,091,766. The estimated fair value at issuance of these options was \$2,425,843, and this amount has been added to the recorded value of the issued shares; and
- v) issued 653,117 common shares and 326,558 warrants pursuant to the exercise of 653,117 brokers' compensation warrants for cash proceeds of \$1,808,980. 194,715 of these warrants were exercised and have been included the number of warrants exercised during the year ended August 31, 2011 as described above, and the remaining 131,843 warrants are exercisable at the price of \$3.60 per share until September 30, 2011. The estimated fair value at issuance of these compensation warrants was \$742,204, of which \$653,193 has been added to the recorded value of the issued shares and the balance of \$89,011 has been allocated to the 131,843 outstanding warrants.

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

	<u>2011</u>	<u>2010</u>	<u>2009</u>
Expected dividend yield	Nil	Nil	Nil
Risk-free interest rate	1.39%	1.28%	1.49%
Expected life	1.0 years	2.0 years	2.0 years
Expected volatility	64%	117%	96%

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 \$Nil (2010 - \$Nil, 2009 - \$7,190) on the monthly unspent portions of the proceeds from its flow-through financings. This amount has been included in interest and financing costs.

Notes to the Consolidated Financial Statements
For the Years Ended August 31, 2011, 2010 and 2009

7. Contributed Surplus

Contributed surplus consists of the following:

	<u>2011</u>	<u>2010</u>	<u>2009</u>
Warrants	\$ 2,650,565	\$ 3,035,519	\$ 28,453
Stock Options	5,585,169	2,951,086	1,665,442
Brokers' Compensation Warrants	96,688	608,040	-
Expired Warrants	1,019,683	1,019,683	1,019,683
Expired Options	199,928	199,928	199,928
Cancelled Options	167,315	152,797	141,147
	<u>\$ 9,719,348</u>	<u>\$ 7,967,053</u>	<u>\$ 3,054,653</u>

	<u>Number</u>	<u>Amount</u>
Warrants		
Balance - August 31, 2008	3,805,000	\$ 1,461,881
Issued for finders' fees	198,750	36,192
Exercised	(1,302,200)	(491,715)
Expired	<u>(2,545,300)</u>	<u>(977,905)</u>
Balance - August 31, 2009	156,250	28,453
Issued pursuant to private placement(s)	3,372,500	3,430,507
Exercised	(156,250)	(28,453)
Commission - cash paid	-	(205,862)
Commission - brokers' compensation warrants issued	-	(119,115)
Issuance costs paid	<u>-</u>	<u>(70,011)</u>
Balance - August 31, 2010	3,372,500	3,035,519
Issued pursuant to private placement(s)	4,620,000	3,385,536
Issued upon exercise of brokers' compensation warrants	326,558	89,011
Exercised	(4,401,475)	(3,593,047)
Commission - cash paid	-	(203,063)
Commission - compensation warrants issued	-	(26,017)
Issuance costs paid	<u>-</u>	<u>(37,374)</u>
Balance - August 31, 2011	<u>3,917,583</u>	<u>\$ 2,650,565</u>

Notes to the Consolidated Financial Statements
For the Years Ended August 31, 2011, 2010 and 2009

7. Contributed Surplus (continued)

	<u>Number</u>	<u>Amount</u>
Stock Options		
Balance - August 31, 2008	4,327,500	\$ 1,353,140
Granted	1,907,000	-
Exercised	(1,127,500)	(375,953)
Expired	(350,000)	(198,448)
Cancelled	(457,000)	(130,230)
Fair value of options recognized in the year	<u>-</u>	<u>1,016,933</u>
Balance - August 31, 2009	4,300,000	1,665,442
Granted	2,075,000	-
Exercised	(643,600)	(744,461)
Cancelled	(175,000)	(11,650)
Fair value of options recognized in the year	<u>-</u>	<u>2,041,755</u>
Balance - August 31, 2010	5,556,400	2,951,086
Granted	2,325,000	-
Exercised	(1,526,150)	(2,425,843)
Cancelled	(50,000)	(14,518)
Fair value of options recognized in the year	<u>-</u>	<u>5,074,444</u>
Balance - August 31, 2011	<u>6,305,250</u>	<u>\$ 5,585,169</u>
Agents' Compensation Options		
Balance - August 31, 2008	725,000	\$ 425,720
Exercised	<u>(725,000)</u>	<u>(425,720)</u>
Balance - August 31, 2009, 2010 and 2011	<u>-</u>	<u>\$ -</u>
Brokers' Compensation Warrants		
Balance - August 31, 2008 and 2009	-	\$ -
Issued pursuant to private placement	<u>450,000</u>	<u>608,040</u>
Balance - August 31, 2010	450,000	608,040
Issued pursuant to private placement	277,200	230,852
Exercised	<u>(653,117)</u>	<u>(742,204)</u>
Balance - August 31, 2011	<u>74,083</u>	<u>\$ 96,688</u>
Cancelled/Expired Warrants and Options		
Balance - August 31, 2008		\$ 54,175
Expired warrants		977,905
Expired options		198,448
Cancelled options		<u>130,230</u>
Balance - August 31, 2009		1,360,758
Cancelled options		<u>11,650</u>
Balance - August 31, 2010		1,372,408
Cancelled options		<u>14,518</u>
Balance - August 31, 2011		<u>\$ 1,386,926</u>

7. Contributed Surplus (continued)

a) Warrants

During the year ended August 31, 2009 the Company amended the exercise price of 3,805,000 share purchase warrants that were expiring on May 22, 2009 from \$2.00 to \$0.70. Of these warrants, 1,259,700 were exercised and the balance of 2,545,300 expired unexercised.

During the years ended August 31, 2011, 2010 and 2009, warrants were issued, exercised and expired as follows:

	Number Of Warrants	Weighted Average Exercise Price
Balance - August 31, 2008	\$ 3,805,000	\$ 2.00
Issued pursuant to a private placement	198,750	0.50
Exercised	(1,302,200)	0.69
Expired	(2,545,300)	0.70
Balance - August 31, 2009	156,250	0.50
Issued pursuant to a private placement	3,372,500	3.00
Exercised	(156,250)	0.50
Balance - August 31, 2010	3,372,500	3.00
Issued pursuant to a prospectus offering	4,620,000	3.60
Issued upon exercise of brokers' compensation warrants	326,558	2.98
Exercised	(4,401,475) ⁽¹⁾⁽²⁾	2.73
Balance - August 31, 2011	<u>3,917,583</u>	<u>\$ 3.60</u>

⁽¹⁾ 3,329,000 of these warrants were eligible for the reduced exercise price of \$2.51 per share for the period from September 1, 2010 to September 30, 2010 and 3,303,650 of these warrants were exercised at the reduced exercise price of \$2.51 per share.

⁽²⁾ Included the 180,000 warrants issued upon exercise of the brokers' compensation warrants, which were exercised at the reduced exercise price of \$2.51 per share.

As at August 31, 2011, the Company had the following warrants issued and outstanding:

- i) 25,350 warrants entitling the holder to purchase one common share at \$3.00 per share, expiring September 17, 2011; and
- ii) 3,892,233 warrants entitling the holder to purchase one common share at \$3.60 per share, expiring September 30, 2011.

7. Contributed Surplus (continued)

b) 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 common shares of the Company at a price equal to or greater than the closing price of the shares on 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 generally have a term of two to five years (but can have a maximum term of 10 years).

During the years ended August 31, 2011, 2010 and 2009, stock options were granted, exercised, expired and cancelled as follows:

	Number Of Options	Weighted Average Exercise Price
Balance - August 31, 2008	\$ 4,327,500	\$ 1.13
Granted	1,907,000	1.00
Exercised	(1,127,500)	0.46
Expired	(350,000)	1.52
Cancelled	(457,000)	1.55
	<hr/>	
Balance - August 31, 2009	4,300,000	1.17
Granted	2,075,000	2.37
Exercised	(643,600)	1.03
Cancelled	(175,000)	1.41
	<hr/>	
Balance - August 31, 2010	5,556,400	1.63
Granted	2,325,000	6.23
Exercised	(1,526,150)	1.37
Cancelled	(50,000)	3.37
	<hr/>	
Balance - August 31, 2011	<u>6,305,250</u>	<u>\$ 3.38</u>

As at August 31, 2011, there were 2,549,000 options vested (2010 - 2,162,650, 2009 - 1,581,650) with the average exercised price of \$2.28 (2010 - \$1.20, 2009 - \$1.15).

During the year ended August 31, 2011, an aggregate of 2,225,000 stock options with the weighted average contract life of 5 years were granted to the Company's employees, officers, directors and advisory committee members. The weighted average grant-date fair value of these stock options was \$4.53.

7. Contributed Surplus (continued)

b) Stock Option Plan (continued)

During the year ended August 31, 2011, an aggregate of 100,000 stock options with the weighted average contract life of 2 years were granted to the Company's consultants. During the year ended August 31, 2011, 350,000 options were earned by the Company's consultants at their service completion date and the weighted average service completion-date fair value of these stock options was \$4.08.

Stock-based compensation expense relating to stock options is recognized on a straight-line basis over the vesting period. During the year ended August 31, 2011, the Company recorded stock-based compensation expense of \$5,074,444 (2010 - \$2,041,755, 2009 - \$1,016,933) related to stock options.

As at August 31, 2011, the following options were vested and outstanding:

Option Price Range	Number of Options		Weighted Average Remaining Contractual Life
	Unvested	Vested	
\$8.00 - \$8.99	175,000	150,000	4.7 years
\$7.00 - \$7.99	1,000,000	-	4.7 years
\$6.00 - \$6.99	100,000	-	4.3 years
\$5.00 - \$5.99	50,000	50,000	1.4 years
\$4.00 - \$4.99	275,000	225,000	4.8 years
\$3.00 - \$3.99	250,000	-	4.2 years
\$2.00 - \$2.99	1,262,500	392,750	3.3 years
\$1.00 - \$1.99	393,750	1,456,250	1.5 years
\$0.01 - \$0.99	250,000	275,000	2.2 years
	<u>3,756,250</u>	<u>2,549,000</u>	

The fair value of stock options to employees, officers and directors 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>2011</u>	<u>2010</u>	<u>2009</u>
Expected dividend yield	Nil	Nil	Nil
Risk-free interest rate	2.19%	2.30%	1.92%
Expected life	4.5 years	4.1 years	3.9 years
Expected volatility	93%	101%	103%

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.

7. Contributed Surplus (continued)

c) Brokers' Compensation Warrants

As at August 31, 2011, the Company had the following brokers' compensation warrants issued and outstanding:

- i) 67,500 brokers' compensation warrants. Each brokers' compensation warrant entitles the holder to purchase one unit of the Company at a price of \$2.43 per unit. Each unit consists of one common share of the Company and a half warrant. Each whole warrant entitles the holder to purchase one additional common share of the Company, at a price of \$3.00 per common share, and expires on September 17, 2011; and
- ii) 6,583 brokers' compensation warrants. Each brokers' compensation warrant entitles the holder to purchase one unit of the Company at a price of \$3.25 per unit. Each unit consists of one common share of the Company and a half warrant. Each whole warrant entitles the holder to purchase one additional common share of the Company, at a price of \$3.60 per common share, and expires on September 30, 2011.

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, 2011, 2010 and 2009 are summarized below:

	<u>2011</u>	<u>2010</u>	<u>2009</u>
Balance - beginning of year	\$ -	\$ (9,486)	\$ (8,200)
Reclassification of previously unrealized losses on investments available for sale to net loss	-	9,486	-
Change in unrealized gains and losses	-	-	(1,286)
Balance - end of year	<u>\$ -</u>	<u>\$ -</u>	<u>\$ (9,486)</u>

9. Capital Disclosures

Capital of the Company consists of the components of shareholders' equity.

The Company's objectives when managing capital are as follows:

- i) to safeguard the Company's assets and ensure the Company's ability to continue as a going concern;
- ii) to raise sufficient capital to finance its exploration and development activities on its Thor Lake Project; and
- iii) to raise sufficient capital to meet its general and administrative expenditures, and to explore and develop its other resource properties.

The Company manages its capital structure and makes adjustments to it, based on the funds available to the Company in light of changes in general economic conditions, the Company's short term working capital requirements, and its planned exploration and development program expenditure requirements.

As the Company is in the development stage, its principal source of capital is from the issuance of common shares. In order to achieve its objectives, the Company expects to spend its existing working capital and raise additional funds as required.

The Company does not have any externally imposed capital requirements and there were no changes to the Company's approach to capital management during the year ended August 31, 2011.

10. Related Party Transactions

- a) During the year ended August 31, 2011 the Company incurred consulting fees of \$81,250 (2010 - \$230,923, 2009 - \$154,525) with a company owned by an officer of the Company, of which \$56,250 (2010 - \$180,923, 2009 - \$154,525) were deferred as resource property costs. As at August 31, 2011 accounts payable included \$Nil payable to this company (2010 - \$18,645, 2009 - \$7,875).
- b) During the year ended August 31, 2011 the Company incurred accounting fees and share issuance costs of \$Nil (2010 - \$37,000, 2009 - \$57,000) with an accounting firm in which an officer is the principal. As at August 31, 2011 accounts payable included \$Nil (2010 - \$2,414, 2009 - \$14,000) payable to this accounting firm.
- c) During the year ended August 31, 2011 the Company incurred consulting fees of \$45,354 (2010 - \$14,793, 2009 - \$Nil), with a person who is related to an officer, which were deferred as resource property costs. As at August 31, 2011, accounts payable included \$14,800 (2010 and 2009 - \$Nil) payable to this person.
- d) During the year ended August 31, 2011 the Company incurred consulting fees of \$36,000 (2010 - \$30,000, 2009 - \$Nil) with an officer of the Company. As at August 31, 2011 accounts payable included \$3,390 payable to this officer (2010 - \$3,709, 2009 - \$Nil).
- e) During the year ended August 31, 2011 the Company incurred consulting fees of \$Nil (2010 - \$8,799, 2009 - \$Nil) and rental fees of \$20,750 (2010 - \$8,000, 2009 - \$Nil) for an apartment in Yellowknife, NT. with a company owned by a director of the Company, which were deferred as resource property costs.
- f) During the year ended August 31, 2010 the Company incurred consulting fees of \$33,000 (2009 - \$67,100) with a former officer (who retired from office during the year ended August 31, 2010) of the Company, of which \$23,238 (2009 - \$41,800) were deferred as resource property costs. As at August 31, 2010 accounts payable included \$6,215 payable to this former officer (2009 - \$5,775).

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

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, 2011, 2010 and 2009 are as follows:

	2011	2010	2009
Difference in resource properties	\$ 938,527	\$ 300,651	\$ 480,782
Difference in investments available for sale	-	-	33,972
Difference in property, plant and equipment	87,138	56,559	39,110
Difference in share issuance costs	1,395,184	433,083	243,153
Non-capital loss carry forwards	1,708,295	943,108	597,254
Capital loss carry forwards	238,309	238,309	240,345
Non-refundable investment tax credit carry forwards	2,336,700	1,320,444	800,065
	<u>6,704,153</u>	<u>3,292,154</u>	<u>2,434,681</u>
Less: valuation allowance	<u>(6,704,153)</u>	<u>(3,292,154)</u>	<u>(2,434,681)</u>
Net future income tax assets	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>

A valuation allowance has been applied against all of the above future income tax assets since it is not presently more likely than not that the benefits will be realized.

b) Non-Capital Losses

The Company has non-capital losses carried forward of approximately \$6,827,000 (2010 - \$3,777,000, 2009 - \$2,212,000) available to reduce future years' taxable income. These losses will expire as follows:

2014	\$ 40,000
2015	4,000
2026	156,000
2027	232,000
2028	847,000
2029	914,000
2030	1,584,000
2031	3,050,000

c) Capital Losses

The Company has capital losses carried forward of approximately \$1,906,000 (2010 - \$1,906,000, 2009 - \$1,800,000) available to reduce future years' capital gains.

d) Canadian Exploration and Development Expenses

The Company has cumulative Canadian development expenses of \$3,181,000 (2010 - \$3,181,000, 2009 - \$3,179,000), cumulative Canadian exploration expenses of \$40,296,000 (2010 - \$25,644,000, 2009 - \$15,621,000) and cumulative foreign resource expenses of \$66,000 (2010 and 2009 - \$23,000) available to reduce future years' taxable income.

Notes to the Consolidated Financial Statements
For the Years Ended August 31, 2011, 2010 and 2009

11. Income Taxes (continued)

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

The Company has SR&ED expenditures carry forward of \$9,993,000 (2010 - \$5,002,000, 2009 - \$2,635,000) available to reduce future years' taxable income.

f) Non-refundable Investment Tax Credits

The Company has non-refundable investment tax credits of \$2,337,000 (2010 - \$1,292,000, 2009 - \$802,000) available to reduce future years' federal income tax payable. These credits will expire as follows:

2018	\$ 44,000
2019	72,000
2020	14,000
2024	24,000
2025	19,000
2026	63,000
2027	133,000
2028	72,000
2029	361,000
2030	490,000
2031	1,045,000

g) Future Income Tax Recoveries

During year ended August 31, 2010 the Company renounced CEE of \$2,000,750 (2009 - \$1,500,000) to the investors in the flow-through private placement completed in September, 2009. This renunciation resulted in a reduction of the Company's future income tax assets of \$540,203 (2009 - \$405,000) and a corresponding reduction in share capital. However, as the Company has not recognized its future income tax assets, the \$540,203 (2009 - \$405,000) was recorded as a future income tax recovery on the statement of operations.

	2011	2010	2009
Net loss for the year before income taxes	\$ 9,421,386	\$ 4,639,503	\$ 3,359,919
Combined federal and provincial tax rate	27.0%	30.0%	31.2%
Expected income tax recovery at statutory rates	\$ 2,543,774	\$ 1,391,851	\$ 1,048,295
Stock-based compensation	(1,370,100)	(612,526)	(317,283)
Non-deductible expenses	(10,933)	(8,888)	(5,057)
Share issuance costs	454,326	172,941	92,978
Impact of tax rate reductions	(119,683)	(157,230)	(110,241)
Losses and other deductions for which no benefit has been recognized	(1,497,384)	(245,945)	(303,692)
Future income tax recoveries	\$ -	\$ 540,203	\$ 405,000

12. Financial Instruments

CICA section 3862 establishes a fair value hierarchy that reflects the significance of inputs used in making fair value measurements as follows:

- Level 1 quoted prices in active markets for identical assets or liabilities;
- Level 2 inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. from derived prices); and
- Level 3 inputs for the asset or liability that are not based upon observable market data.

Assets are classified in their entirety based on the lowest level of input that is significant to the fair value measurement. As at August 31, 2011, the Company's Cash and Cash Equivalents are classified as Level 1.

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.

The Company's risk exposures and the impact on the Company's financial instruments are summarized below:

Credit risk

The Company is not exposed to any significant credit risk as at August 31, 2011. The Company's cash and cash equivalents are either on deposit with two highly rated banking groups in Canada or invested in bankers acceptance notes or guaranteed investment certificates issued by two highly rated Canadian banking groups. The Company's receivables is primarily consisted of Goods and Services Tax/Harmonized Sales Tax receivable and Investment Tax Credits receivable and are therefore not subject to significant credit risk.

Liquidity risk

Liquidity risk is the risk that an entity will not be able to meet its financial obligations as they come due. The Company has sufficient funds to cover its working capital requirements for at least the next two years.

Market risk

(i) Interest rate risk

The Company has significant cash and cash equivalents balances and it has no interest-bearing debt. The Company's current policy is to invest its excess cash in highly liquid money market investments such as bankers acceptance notes, treasury bills and guaranteed investment certificates. These short term money market investments are subject to interest rate fluctuations.

(ii) Foreign currency risk

The Company's functional currency is primarily the Canadian dollar. The majority of the Company's purchases are transacted in Canadian dollars. As at August 31, 2011, the Company had cash of US\$1,625,121 and accounts payable of US\$221,013 denominated in US currency.

(iii) Price risk

The prices of metals and minerals fluctuate widely and are affected by many factors outside of the Company's control. The prices of metals and minerals and future expectation of such prices have a significant impact on the market sentiment for investment in mining and mineral exploration companies. This in turn may impact the Company's ability to raise equity financing for its long term working capital requirements.

12. Financial Instruments (continued)

Sensitivity analysis

Based on management's knowledge and experiences of the financial markets, the Company's management believes the following movements are "reasonably possible" over a three month period.

As at August 31, 2011, approximately 95% of the Company's cash and cash equivalents is at fixed interest rates beyond the next three months and is not subject to interest rate fluctuations within the next three months. The balance of the Company's cash and cash equivalents is subject to interest rate fluctuations. Sensitivity to a plus or minus 25 basis points change in rates would not have any significant effect on the Company's net loss over a three month period.

The Company had cash of US\$1,625,121 in cash and accounts payable of US\$221,013 denominated in US currency as at August 31, 2011 and its anticipated expenditures transacted in US dollars for the next three months is approximately US\$550,000. If the Canadian Dollar weakens (or strengthens) 5% against the United States Dollar with other variables held constant, the Company's expenditures would increase (or decrease) by approximately \$27,000 over a three month period which would be offset by a foreign exchange gain (or loss) of approximately \$69,000.

13. Commitments

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

14. Lease Commitments

The Company has two operating leases for its office premises, the minimum lease commitments under these leases are as follows:

2012	\$ 282,237
2013	279,544
2014	290,457
2015	296,967
2016	296,967
2017	98,989

15. Recent Accounting Pronouncements

Recent accounting pronouncements issued and not yet effective:

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 Company thus will apply IFRS in fiscal 2012. The Company will require restatement for comparative purposes of amounts reported by the Company for the year ending August 31, 2011 and accordingly the Company will need to prepare an opening balance sheet, in accordance with IFRS, as at September 1, 2010.

The Company has identified a three-phase transition plan: Phase 1 - initial diagnostic assessment and scoping, which involves the identification of significant differences between existing Canadian GAAP and IFRS as relevant to the Company’s specific situation; Phase 2 - in-depth analysis and assessment, which involves the identification, evaluation and selection of the accounting policies necessary for the Company to changeover to IFRS; and Phase 3 - implementation, which will identify and implement updates to any internal procedures and systems in order for the Company to comply with IFRS requirements.

The Company has completed Phase 1, substantially completed Phase 2 and is currently engaged in Phase 3.

The Company has identified the significant areas that potentially have the most significant impact on the Company’s financial report to be: exploration expenditures, stock-based compensation and income taxes. In addition, the Company anticipates a significant increase in disclosure requirements under IFRS and such requirements are also being evaluated along with the necessary system changes required to gather, process and review such disclosure. The Company does not anticipate any significant changes to its information technology, internal controls over financial reporting, disclosure controls and procedures or its business activities as a result of the conversion to IFRS.

16. Differences between Canadian and United States Generally Accepted Accounting Principles

These financial statements have been prepared in accordance with Canadian generally accepted accounting principles (“Canadian GAAP”). A description of United States generally accepted accounting principles and practices (collectively “US GAAP”) that result in material measurement and disclosure differences from Canadian GAAP is as follows:

Balance Sheets

The impact of the differences between Canadian GAAP and U.S. GAAP on the balance sheet line items is as follows:

	<u>2011</u>	<u>2010</u>	<u>2009</u>
Assets			
Resource properties under Canadian GAAP	\$ 50,475,040	\$ 32,646,738	\$ 19,677,856
Resource property expenditures expensed under U.S. GAAP	<u>(49,560,605)</u>	<u>(32,169,330)</u>	<u>(19,202,198)</u>
Resource properties under U.S. GAAP	<u>\$ 914,435</u>	<u>\$ 477,408</u>	<u>\$ 475,658</u>
Shareholders' Equity			
Closing shareholders' equity under Canadian GAAP	\$ 120,100,958	\$ 39,348,575	\$25,091,552
Adjustment to deficit for resource property expenditures expensed under U.S. GAAP	<u>(49,560,605)</u>	<u>(32,169,330)</u>	<u>(19,202,198)</u>
Closing shareholders' equity U.S. GAAP	<u>\$ 70,540,353</u>	<u>\$ 7,179,245</u>	<u>\$ 5,889,354</u>

16. Differences between Canadian and United States Generally Accepted Accounting Principles (continued)

Statements of Operations and Deficit

The impact of the differences between Canadian GAAP and U.S. GAAP on the statements of operations and deficit is as follows:

	2011	2010	2009
Net Loss			
Net loss under Canadian GAAP	\$ (9,421,386)	\$ (4,099,300)	\$ (2,954,919)
Resource property expenditures expensed under U.S. GAAP (a)	(17,619,891)	(13,117,726)	(7,276,378)
Write-down of resource properties (a)	-	-	574,709
Future income tax recoveries - flow-through shares (b)	-	(540,203)	(405,000)
Research & Development - ITC (e)	228,616	150,594	189,179
Net loss under U.S. GAAP	<u>\$ (26,812,661)</u>	<u>\$ (17,606,635)</u>	<u>\$ (9,872,409)</u>
Basic and Diluted Loss Per Share - U.S. GAAP	<u>\$ (0.29)</u>	<u>\$ (0.23)</u>	<u>\$ (0.15)</u>

Cash Flow Statements

The impact of the differences between Canadian GAAP and U.S. GAAP on the cash flow statement line items would be as follows:

	2011	2010	2009
Cash flows - Operating Activities			
Cash used in operating activities - Canadian GAAP	\$ (4,147,326)	\$ (2,441,383)	\$ (1,867,445)
Net cash used for resource property expenditures	(16,930,577)	(12,820,832)	(6,811,513)
Cash used in operating activities - U.S. GAAP	<u>\$ (21,077,903)</u>	<u>\$ (15,262,215)</u>	<u>\$ (8,678,958)</u>
Cash flows - Investing Activities			
Cash used in investing activities - Canadian GAAP	\$ (17,395,400)	\$ (13,475,559)	\$ (6,811,513)
Net cash used for resource property expenditures under Canadian GAAP	16,930,577	12,820,832	6,811,513
Cash used in investing activities - U.S. GAAP	<u>\$ (464,823)</u>	<u>\$ (654,727)</u>	<u>\$ -</u>

16. Differences between Canadian and United States Generally Accepted Accounting Principles (continued)

a) Resources Properties

Under Canadian GAAP, acquisition costs of resource properties together with direct exploration and development expenditures thereon, are carried at cost and written down if the properties are abandoned, sold or if management determines there to be an impairment in value.

Under US GAAP, expenditures incurred to acquire interests in resource properties or concessions are capitalized. However, all exploration and development expenditures relating to mineral properties for which commercial and legal feasibility has not yet been established are expensed as incurred. Accordingly, as at August 31, 2011, 2010 and 2009 capitalized acquisition costs would have been \$914,435, \$477,408 and \$475,658 respectively.

For Canadian GAAP, cash flows relating to resource property costs are reported as investing activities. For US GAAP, these costs are characterized as operating activities.

b) Flow-through Shares

Under Canadian income tax legislation a company is allowed to issue flow-through shares pursuant to which the Company renounces Canadian exploration expenditures to the flow-through share investors for an amount equal to the share issuance price. Under Canadian GAAP, the Company recognizes a future income tax benefit upon the renouncement of these exploration expenditures for the amount of the future tax value of the expenditures renounced.

Under US GAAP, the gross proceeds from the issuance of flow-through shares are allocated between the offering of the flow-through shares and any premium paid by investors for the benefit to be received in future upon renunciation. The allocation is made based on the difference between the quoted price of the shares and the amount the investor pays for the flow-through shares.

The calculated tax benefit is recognized as a liability until the Company has renounced the deductible expenditures, at which time the liability is reversed and is recorded as a tax recovery. This difference has not been material and has not been recognized for US GAAP purposes.

US GAAP also requires that the portion of the gross proceeds from flow-through shares not yet spent by the Company be disclosed as restricted cash since the funds are required to be spent on exploration in Canada in order to satisfy the requirements of the renunciation. There were no unspent gross proceeds from flow-through shares as at August 31, 2011, 2010 and 2009. Accordingly there was no adjustment for both unrestricted and restricted cash and cash equivalents under US GAAP as at August 31, 2011, 2010 and 2009.

c) Stock Option Compensation

For US GAAP purposes, all share-based payments to employees, including grants of employee stock options, are recognized in results from operations based on the fair values of options expected to vest. In calculating compensation to be recognized, US GAAP requires an estimate for forfeitures. For Canadian GAAP, the Company accounts for forfeitures as they occur. The effect of forfeitures is not material. Accordingly no adjustments for any of the periods were required.

16. Differences between Canadian and United States Generally Accepted Accounting Principles (continued)

d) Income Taxes

Under Canadian GAAP, future tax assets and liabilities are recorded at substantively enacted tax rates. Under US GAAP, deferred tax assets and liabilities are recorded at enacted tax rates. There were no significant differences between enacted and substantively enacted tax rates for any of the periods presented.

Financial Statement Accounting Board ("FASB") issued FIN 48, *Accounting for Uncertainty in Income Taxes, an Interpretation of FASB Statement 109*, (now accounting standards codification ("ASC") 740), which prescribes a recognition threshold and measurement criteria for the financial statement recognition of a tax position taken or expected to be taken in a tax return. The Company is required to determine whether it is more likely than not that a tax position will be sustained upon examination and such positions that meet this threshold will be measured at the largest amount of the benefit that is greater than 50% likely of being realized upon ultimate settlement.

The Company has reviewed its tax positions and determined that the application of FIN 48 does not result in any material adjustment for US GAAP purposes.

e) Research and Development and Investment Tax Credits

Under Canadian GAAP research and development expenditures are capitalized if the development activities meet certain criteria, including reasonable assurance regarding future benefits. Investment tax credits on eligible research and development expenditures that are non-refundable are treated as a reduction of the expenditure.

Under US GAAP research and development expenditures are expensed in the period that it is incurred. Non-refundable investment tax credits are treated as income tax benefits or as a reduction on income tax expense. Refundable investment tax credits can be recorded as a reduction of the expenditures or as a reduction of income tax expense.

f) Accounts Payable

Under U.S. GAAP, the components of accounts payable have to be reported separately on the balance sheet. Accordingly, the amount of accounts payable consists of trade payable of \$3,411,021 (August 31, 2010 - \$2,010,128, August 31, 2009 - \$1,073,691) and accrued liabilities of \$381,574 (August 31, 2010 - \$168,012, August 31, 2009 - \$356,021) as at August 31, 2011.

g) Adoption of New Accounting Pronouncements

The Company adopted new general standards of accounting for and disclosure of events that occur after the balance sheet date but before financial statements are issued or are available to be issued (ASC 855). The new guidelines require an entity to evaluate subsequent events to the date the financial statements were issued or were available to be issued. The Company adopted this standard in its 2010 fiscal year with no material impact to the financial statements.

The Company adopted the new ASC 105 and the hierarchy of generally accepted accounting principles which became effective on July 1, 2009. All other non-grandfathered non-SEC accounting literature not included in the ASC will become non-authoritative. The new ASC did not have a material impact on the financial statements.

16. Differences between Canadian and United States Generally Accepted Accounting Principles (continued)

g) Adoption of New Accounting Pronouncements (continued)

In December 2007, FASB issued new guidance for business combinations which requires an acquirer to recognize the assets acquired, the liabilities assumed, and any non-controlling interest in the acquiree at the acquisition date, measured at their fair values as of that date, with limited exceptions (now ASC 805). It also requires that the acquirer in a business combination achieved in stages to recognize the identifiable assets and liabilities, as well as the non-controlling interest in the acquiree, at the full amounts of assets and liabilities as if they had occurred on the acquisition date. In addition, all acquisition related costs must be expensed as incurred, rather than capitalized as part of the purchase price and those restructuring costs that an acquirer expected, but was not obligated to incur, to be recognized separately from the business combination. This guidance applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008. The Company adopted this guidance commencing September 1, 2009 and it had no material impact on the financial statements.

In December 2007, the FASB issued new accounting and reporting standards for the noncontrolling (minority) interest in a subsidiary and for the deconsolidation of a subsidiary (now ASC 810). The new standards clarify that a noncontrolling interest in a subsidiary is an ownership interest in the consolidated entity that should be reported as equity in the consolidated financial statements. It also requires consolidated net income and comprehensive income to be reported at amounts that include the amounts attributable to both the parent and the noncontrolling interest on the face of the consolidated statement of income. Changes in a parent's ownership interest in a subsidiary that do not result in deconsolidation must be accounted for as equity transactions for the difference between the parent's carrying value and the cash exchanged in the transaction. The Company adopted this guidance commencing September 1, 2009 and it did not have a material impact on the financial statements.

New guidance for fair value measurements and disclosures for nonfinancial assets and nonfinancial liabilities, other than for items that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually) became effective September 1, 2009 (now ASC 820). The adoption of this guidance did not have a material impact on the financial statements.

In June 2009, FASB issued FAS 167, *Amendments to FASB Interpretation No. 46(R)* ("FAS 167") (Accounting Standards Codification subtopic 810-10). FAS 167 eliminates FASB Interpretation 46(R)'s exceptions to consolidating qualifying special-purpose entities, contains new criteria for determining the primary beneficiary, and increases the frequency of required reassessments to determine whether a company is the primary beneficiary of a variable interest entity. FAS 167 also contains a new requirement that any term, transaction, or arrangement that does not have a substantive effect on an entity's status as a variable interest entity, a company's power over a variable interest entity, or a company's obligation to absorb losses or its right to receive benefits of an entity must be disregarded in applying FASB Interpretation 46(R)'s provisions. FAS 167 is effective for fiscal years beginning after November 15, 2009, and for interim periods within that first period, with earlier adoption prohibited. The Company's adopted this new standard on September 1, 2010. The application of this standard had no impact on the Company's financial statements.

In January 2010, FASB issued Accounting Standards Update No. 2010-06, "Fair Value Measurements Disclosures" which amends Sub topic 820-10. This amendment requires new disclosures for fair value measurements and provides clarification of existing disclosure requirements. This update requires (a) an entity to disclose separately the amounts of significant transfers in and out of Levels 1 and 2 fair value measurements and to describe the reasons for the transfers; and (b) information about purchases, sales, issuance and settlements to be presented separately (that is on a gross basis rather than net) in the reconciliation of fair value measurement using significant unobservable inputs (Level 3 inputs). This update clarifies existing disclosure requirements for the level of disaggregation of classes of assets and liabilities measured at fair value, and it requires disclosures about inputs and valuation techniques used to measure fair value for both recurring fair value measurement using Level 2 and Level 3 inputs. The application of this standard had no impact on the Company's financial statements.

16. Differences between Canadian and United States Generally Accepted Accounting Principles (continued)

h) Recently Issued Accounting Pronouncements

In July 2011, FASB issued Accounting Standards Update No. 2011-05, "Comprehensive Income" which amends topic 220. The amendments require that all nonowner changes in stockholders' equity be presented either in a single continuous statement of comprehensive income or in two separate but consecutive statements. In the two-statement approach, the first statement should present total net income and its components followed consecutively by a second statement that should present total other comprehensive income, the components of other comprehensive income, and the total of comprehensive income. The amendments in this update should be applied retrospectively. For public entities, the amendments are effective for fiscal years, and interim periods within those years, beginning after December 15, 2011. Early adoption is permitted.

17. Comparative Figures

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

18. Subsequent Events

Subsequent to the year ended August 31, 2011, the Company:

- a) issued 64,991 common shares pursuant to the exercise of an equivalent number of share purchase warrants for cash proceeds of \$198,508;
- b) issued 130,000 common shares pursuant to the exercise of an equivalent number of stock options for cash proceeds of \$279,250;
- c) issued 74,083 common shares and 37,041 warrants pursuant to the exercise of 74,083 Brokers' Compensation Warrants for cash proceeds of \$185,420;
- d) granted an aggregate of 425,000 stock options with a weighted average exercise price of \$3.77 per share to the Company's employees, officers, directors and technical advisory committee members. The weighted average contract life of these options was 5 years and the weighted average grant-date fair value of these stock options was \$2.68. The fair values of these options were estimated using the Black-Scholes pricing model, with the following assumptions: expected dividend yield of Nil; risk free interest rate of 1.44%; expected life of 5 years; and expected volatility of 93%;
- e) granted 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 \$3.15 per share until October 12, 2013;
- f) cancelled 125,000 stock options with an weighted average exercise price of \$3.29 per share;
- g) had 3,889,633 share purchase warrants with the exercise price of \$3.60 per share expire unexercised; and
- h) had the Over-allotment Option to purchase up to 472,100 common shares at the price of \$5.81 (or US\$6.15) per share expire unexercised.