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continuous disclosure | update

British Columbia Securities Commission

MD&A GUIDANCE for junior resource companies

Includes MD&A example with explanatory notes

in this update:

Better Management Discussion and Analysis (MD&A)

How to improve this critical window on your company's performance

We have prepared this special edition of the Continuous Disclosure Update to assist management and directors of junior resource sector companies listed on the TSX Venture Exchange to comply with MD&A disclosure requirements for their annual and quarterly reports (BC form 51-901F). Currently, in Canada, all TSX Venture and many TSX listed companies are required to provide MD&A. However, in the next year, a new National Disclosure Rule is expected to be introduced that will require thorough MD&A disclosure by all Canadian public companies.

Investors are demanding better disclosure from public companies

The global trend to improved public disclosure

Corporate accounting scandals, economic conditions and their combined negative impact on capital markets have resulted in a new emphasis on public company accountability. The demand for more and better information from public companies is being driven by investors, and the impact is being felt by companies and regulators alike. From the investor's perspective, a company's "continuous disclosure record" — regulatory filings and other communications with shareholders and potential investors — is the *only* basis available for assessing its performance and integrity. This is the underlying reason efforts to improve public disclosure are being stepped up, locally and globally.

Good disclosure is good for business

Full public disclosure is a strong indicator to investors of a quality management team and a well-run operation. Conversely, a lack or inconsistency of information makes a strong negative statement. Even if a company's results are less positive than expected, or operational problems arise, management that explains on a timely basis *why* these events have occurred and their strategies for moving forward, cannot but help their public credibility. It is when information is withheld or misrepresented that today's investors show zero tolerance. So, beyond compliance, good disclosure is good for business. It promotes investor confidence in individual companies and in the markets as a whole, and can lead to positive market attention and greater share liquidity.

We're working to meet the needs of the public <u>and</u> reporting companies

As a regulator our role is to protect investors and maintain confidence in the capital markets. At the same time, we are working hard to ensure companies are not excessively burdened in ways that hamper their business. This is why we supply as much step-by-step information as possible to help junior public companies understand and meet their obligations. This guide to MD&A preparation is part of our effort to make the compliance process easier and help your company meet its obligations to the investing public.

BCSC

MD&A and Financial Statements:

The Management Discussion and Analysis (MD&A) was originally intended to be supplementary to a company's financial statements. However, with the trend to improved corporate disclosure, the MD&A itself has become an integral part of public company reporting. In November 2002, the Canadian Institute of Chartered Accountants (CICA) published extensive guidance on the disclosure now required in an MD&A, stating "the MD&A and the financial statements together now form the foundation for business reporting and comprise a stand-alone disclosure package."

"The MD&A, like financial statements, provides the opportunity for a company to demonstrate accountability to investors... for meeting important strategic objectives. Also, the discipline required to prepare an effective MD&A can strengthen internal management focus."

— CICA
'MD&A Guidance on Preparation and Disclosure'

The financial statements reflect *what* happened during a reporting period — the MD&A explains *why* these changes occurred

The MD&A accompanies your financial statements. Neither is a substitute for the other and each must contain the appropriate level of detail. In an MD&A, management must analyze the financial statements and discuss the dynamics of the business. The discussion is directed at current shareholders and potential investors, but is also often reviewed by others assessing the company. MD&A disclosure provides management with an opportunity to explain how the company has performed, and discuss its financial position and future prospects.

The BC Securities Commission's MD&A rules require that companies provide investors with a *meaningful* analysis and discussion of their operations. In other words, you must provide a clear explanation of the nature of, and reasons for, changes in your company's performance during the reporting period.

Example: The income statement tells shareholders how much has been spent. The MD&A should explain why the expenditures were made. If an expenditure level is being compared from one period to another, the MD&A must explain the reasons for the difference.

"Financial statements and MD&A complement one another. The financial statements show investors and others how funds were raised and spent; the MD&A explains why these transactions occurred and what impact they will have on future operations."

— *Doug Hyndman*
Chair, BCSC

The discussion should help readers to understand trends, events, transactions and expenditures, and their impact on future operations. Both positive and negative developments must be discussed. For example, if the company did not achieve a planned milestone within the budget or time frame previously disclosed, the reason for not achieving the milestone, and its impact on the company's future operations, has to be clearly explained. This is particularly important when a company has previously raised funds to finance a project or acquisition — investors have a right to know how funds they have invested are being spent.

Example: If you previously announced a plan to expand your plant facilities at an estimated cost of $400,000, and you spent $400,000 during the current reporting period but only accomplished 50% of the planned expansion, you must disclose this information to your investors and explain the impact the shortfall will have on your future plans.

The "Most common MD&A problems" and "Fundamental steps to improve your MD&A" sections that follow give other examples and describe key factors to consider in preparing an MD&A.

the new "core business-reporting package" (CICA, 11/02)

Benefits of MD&A disclosure for junior companies

MD&A disclosure is particularly important for junior companies that do not have a history of profitable operations which might otherwise give investors assurance about the company's long-term prospects. The MD&A offers an opportunity for you to provide investors, and others who review company information, with your perspective of how the company has performed and how that performance will likely affect future plans. In the MD&A, you can share your management strategy and put the information contained in the financial statements into context. In this way, a properly prepared MD&A can significantly improve an investor's understanding of your business and its operations.

No need for added cost in preparing your MD&A

Some smaller companies have expressed concern about the time and cost required to prepare their MD&A. Providing accurate, complete and timely disclosure of information to shareholders is a responsibility all public companies assume, regardless of size. While developing an initial MD&A may take added time, it becomes easier once the process and format are familiar. In terms of cost, preparing an MD&A should not necessitate the use of outside consultants, as the purpose is to provide management's interpretation of what happened during the reporting period. Therefore, management should be providing the discussion and analysis, as they know the company best.

"...improved disclosure can lead to a lower cost of capital, increased financial analyst coverage, improved corporate governance, a more appropriate risk premium and better capital allocation decisions."

— excerpt from CICA news release

We are significantly increasing the number of MD&As we review

As part of BCSC's Continuous Disclosure Review Program, we regularly review the information filed by the 1,800 BC-based public companies we regulate to ensure they comply with disclosure standards. Through this program, we have found that the MD&A disclosure of many companies does not meet the requirements. Of the companies we reviewed from April 1, 2000 to December 31, 2002 approximately 41% had to amend and refile their MD&As. In approximately 10% of cases, the quality was so poor, companies were put on the "Issuers in Default List" (see next page) without warning.

In keeping with the increased emphasis on MD&A disclosure, in the coming year we plan to review the financial statements and MD&A filings of many more companies than in previous years. All companies are potential candidates for continuous disclosure review. We select companies in two ways: using a risk-based system that takes several factors into account, and randomly, so that the chances of companies being selected are equal.

"Whenever I talk to CEOs or investor relations professionals and ask them if they prefer to have a majority of institutional investors or retail investors, without exception they say retail investors. That's because retail investors tend to side with management's point of view. Good MD&A gives you a better chance of acquiring that larger base of retail investors. To attract those retail investors you have to make your business understandable to them."

— John Bart
Founder, Canadian ShareOwner's Association

The costs of non-compliance

There are a number of costs associated with failing to provide adequate MD&A disclosure. Some are obvious, and some are less apparent but still potentially damaging to a business.

The BCSC generally takes a "benefit of the doubt" approach when encountering disclosure deficiencies, particularly on a first-time basis. That is, in addition to providing as much guidance as we can to help companies, we normally work on the assumption that when information has not been fully provided, the company simply may not be completely aware of the requirements. Our system of regulatory consequences reflects this approach, increasing in severity according to the seriousness of the compliance problem:

1 Correct the Information in Future Filings

If problems are relatively minor, we ask the company to improve its disclosure in future filings.

2 Amend and Refile

When there are more serious disclosure problems, we ask the company to amend and refile its materials and publish a comprehensive news release.

3 Issuers in Default List

A company can be placed on BCSC's Issuers in Default List without notice if its disclosure problems are serious or extensive enough. An example would be disclosing "nothing to report" in the MD&A section when the financial statements show significant activity. This list is posted on our website and is widely circulated every week through various news media, such as Market News and Bloomberg.

4 Cease Trading Order

In extreme cases, a Cease Trading Order may be issued against a company's securities, which remains in effect until the problems are corrected. For example, this would apply where we determine a company has made a material misrepresentation.

The negative impacts on a business from the above measures range from pure inconvenience at the lower end of the scale all the way to potential derailment of a financing in more serious cases. Here are some of the direct and indirect costs to keep in mind that can result from not providing full disclosure:

- the need to go back and explain previously filed information
- the need to file missing information
- administrative time of senior people to respond and comply
- the need to involve accountants, auditors, lawyers or other outside consultants
- the impact of a negative news release, coverage in key publications such as Stockwatch, and undermining of expensive investor relations campaigns
- inability to obtain a Certificate of Good Standing from the Commission that can lead to a failed financing
- undervalued shares because investors do not understand the business
- exposure to litigation

The most common MD&A PROBLEMS *we find in our reviews*

no meaningful analysis and discussion of operations; the company simply reproduces numeric information from its financial statements with no explanation of why significant changes in operating results occurred

no explanation of why the company failed to achieve significant milestones within previously disclosed time frames or the implications of not achieving those milestones

no discussion of future operating and financial plans, particularly important when a company has liquidity or solvency problems

focussing only on positive items and ignoring negative items, sometimes to the extent that the MD&A is little more than a company marketing vehicle

confusing technical jargon where simple explanations of business and technical concepts will be more appreciated by the reader

a discussion that is missing key pieces of basic, useful information for investors, such as what the company does and its objectives; assumes the reader knows this information

information that is inconsistent with the company's other public information, such as on its website

no reconciliation of how funds were spent to how they were budgeted in offering documents

MD&A not updated each quarter; just a repeat of previously disclosed information from press releases or earlier MD&As; no new information or analysis provided

required "subsequent events" information not included: no discussion of material changes in operations between the end of the fiscal reporting period and the date the MD&A is filed

"...to be useful to investors, MD&A disclosure must convincingly answer three basic questions: How does this company make money and create value? What makes this company valuable today and tomorrow? Why does this company deserve investors' money? The better a company communicates with those who assess its value in capital markets, the better the markets will understand and reward underlying potential and prospects."

— Jim Goodfellow, Chair, Canadian Performance Reporting Initiative Board

fundamental steps to impro

GENERAL

While the general information in this Continuous Disclosure Update applies to all junior resource sector companies, much of the information in this section and the following MD&A example focuses primarily on mining/exploration companies.

- use plain language and limit the use of technical jargon so the average investor can understand

- the discussion and analysis must be meaningful and comprehensive: the question to ask is "will a non-insider understand where the company is coming from (as reflected in the financial statements), where it is now, and where it plans to go?"

- provide a brief description of the company's business, for example, what types of minerals is it exploring for?

- the MD&A should stand on its own; investors should not have to hunt for disclosure in other sources such as press releases to understand the information

- discuss the nature and purpose of significant expenditures recorded during the period

- explain the reasons for significant changes in operating results and assets (including deferred costs) and liabilities; it is not sufficient to simply recite, without explanation, the changes from period to period that are easily determined from the financial statements

- ensure compliance with NP 51-201 by providing balanced disclosure, giving equal weight to both positive and negative information; do not simply report the best or highest values

- provide a meaningful discussion of your company's liquidity and solvency including, if applicable, future plans to resolve problems in these areas

- avoid promotional language: terms such as *extremely exciting, world class, sensational*, etc., take away credibility; instead, explain the significance of exploration results as this is more meaningful to the reader

ve your MD&A disclosure

- **if the company is in the development stage** (devoting substantially all its efforts to establishing a new business and planned principal operations have not commenced), and the current period's financial results are not fully comparable to those of the corresponding period in the prior year due to the rapidly changing nature of the company's business, consider comparing the current quarter's operating results to those of the immediately preceding quarter in addition to those of the prior year

- **ensure compliance with NI 43-101 disclosure rules** such as naming the Qualified Person (QP) on the property and qualifying historical information (pre-NI 43-101) with appropriate language on relevance and reliability

- **reference any supporting NI 43-101 technical reports** on public file

- **discuss any current or pending legal proceedings and contingent liabilities**

- **discuss the nature and purpose of related party transactions,** including details of the specific services provided

- **disclose any management changes**

- **if regulatory (exchange) approval of a particular transaction is required,** discuss if this approval has been sought and obtained for example, the acquisition or sale of a material mineral property

- **discuss significant events occurring subsequent to the fiscal reporting period,** up to the date the report is filed, that will have an impact on future operations

A COMPANY'S CONTINUOUS DISCLOSURE RECORD INCLUDES:

- regulatory filings and other communications with shareholders and potential investors such as quarterly and annual reports
- interim and annual financial statements
- Annual Information Forms (AIF) if applicable
- Information Circulars
- Material Change Reports
- information in press releases, on company websites, and in web-casts and speeches given by directors, officers and employees of the company

fundamental steps to improve your MD&A disclosure (continued)

DISCUSSION OF MINERAL EXPLORATION PROJECTS

- **provide a brief summary of the location of the property, ownership,** and terms of earn-in; disclose significant property payment due dates if applicable

- **provide a summary of exploration targets**

- **provide a summary of significant exploration results, positive and negative,** including such things as the quantity and type of drilling, trenching, and sampling completed; give context to the exploration results

- **compare actual results to the goals of previously announced exploration programs,** i.e., were all the exploration targets that were to be tested, tested adequately, and explain reasons for not completing any work that was recommended

- **compare actual exploration expenditures to those budgeted in offering documents** or other sources of public disclosure; explain significant variances and their impact, if any, on future objectives and milestones

- **discuss any decision points reached on the property in general,** or on specific prospects within the mineral property: have the exploration results or other factors led to a decision to drop, suspend, joint-venture, or advance the property?

- **if a formerly significant exploration target is no longer viewed as a priority,** or if an exploration property is dropped, explain the reasons why

- **if applicable, discuss how changing equity market conditions,** commodity prices, political and environmental issues or other factors have affected the company's strategy toward advancing the mineral properties, acquiring new properties or preserving capital

- **describe recommendations or plans for future work**, including the estimated cost and the anticipated time frame for carrying it out
- **if additional funds are required to finance further exploration work,** or make significant property payments, disclose how much is required and how the company intends to raise the funds

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DISCUSSION OF MINING ACTIVITY

- **discuss milestones** such as mine expansion plans, productivity improvements, or plans to develop a new mine; discuss the company's progress on achieving milestones and ability to finance its goals
- **discuss significance of new acquisitions, disposals, or write-downs** of mineral properties
- **discuss exploration success in the area of the mine,** including replacement of depleted mineral reserves or upgrade of confidence categories of mineral resources or mineral reserves
- **describe developments that could impact the company's mineral resources** or reserves, including change in commodity price, cut-off grade, technological advances, permitting, or significant results from engineering studies
- **explain reasons for changes to production** throughput, head-grade, cut-off grade, and metallurgical recovery, and discuss any expectations of future changes
- **explain reasons for any changes in operating costs,** unit production costs, and cash flow
- **discuss the impact of any hedging or derivative programs** on current or future cash flows
- **provide a brief explanation of how company is managing its environmental liabilities**

MD&A Example: the following example illustrates the type of Management Discussion and Analysis disclosure that should be provided by a development stage company. *Abbreviated financial statements are included simply as a reference for the purposes of highlighting portions of the example. This sample does not include all of the financial statement and Schedule B disclosure required by BC Form 51-901F.*

BLUE SKY MINING CORP.

September 30, 20X2

Description of Business

Briefly describes the company's business, including the geographic areas and metals it is focusing on.

Blue Sky Mining Corp. (the Company) is a development stage company engaged in the acquisition and exploration of mineral properties in British Columbia and the Yukon Territory. The Company is currently focusing its exploration activities on precious metals and holds an interest in two mineral properties located in the Cariboo and Omineca Mining Divisions of central British Columbia. The Company is a reporting issuer in British Columbia and Alberta, and trades on the TSX Venture Exchange under the symbol BSD.

Blackwater Gold-Silver Property

Briefly summarizes the property location, ownership and earn-in terms.

The Blackwater property is located in the Cariboo Mining Division of British Columbia, approximately 60 kilometers northwest of the town of Quesnel. Blue Sky acquired a 100% interest in 40 claim units by making staged cash payments of $500,000, issuing 1,000,000 shares, and spending $2 million on exploration. The vendors retain a 3% net smelter return, half of which Blue Sky can purchase for $2 million.

Prior to the current year, Blue Sky incurred exploration expenditures in excess of $2.5 million, including extensive surface and underground drilling. Blue Sky has outlined inferred resources for the Main and Northwest Veins totaling 1.65 million tonnes grading 6.5 gpt gold, 92.4 gpt silver, and 2.35% lead. This resource estimate was prepared in accordance with the requirements of NI 43-101 by Blue Sky's independent Qualified Person, Dr. John Smith, P.Eng., as set out in his technical report dated August 20X1.

Names the independent QP responsible for the mineral resource estimate and refers to the supporting technical report.

Exploration Program

In its prospectus dated September 25, 20X1, Blue Sky proposed a 4,000-meter core-drilling program to test five soil geochemistry or geophysics targets identified by previous exploration. Blue Sky also proposed to complete preliminary metallurgical and environmental studies. Management based this work program on the recommendations of Dr. Smith in his report. The estimated budget for this work was $690,000. David Jones, P.Geo., President, supervised the fieldwork and is the Qualified Person on the property.

Names the company QP on the property.

Table 1 – Reconciliation of Proposed & Actual Expenditures

Compares actual and budgeted expenditures and explains significant variances.

	Proposed	Actual	Variance
Assaying	$ 10,000	$ 6,591	$ (3,409)
Baseline Environmental Study	35,000	—	(35,000)
Camp Costs	50,000	62,276	12,276
Drilling	400,000	541,363	141,363
Geological Consulting	35,000	35,323	323
Labour	10,000	12,400	2,400
Metallurgical Testing	20,000	12,684	(7,316)
Road Construction	10,000	8,874	(1,126)
Transportation and Shipping	30,000	27,225	(2,775)
	600,000	706,736	106,736
Contingencies (15%)	90,000	—	(90,000)
Total	$ 690,000	$706,736	$ 16,736

Blue Sky was only able to complete eighteen of the 20 proposed drill holes, for a total of 3,865 meters. Drilling costs exceeded budgeted amounts by $141,363, largely as a result of broken ground and recovery problems encountered in many holes. In addition, Blue Sky abandoned and re-drilled two holes due to caving and loss of water circulation. As a result, the drill program lasted 12 days longer than was budgeted, increasing the field and support costs.

Compares actual and budgeted expenditures and explains significant variances.

Cost overruns were partially offset by reduced transportation, road construction, and assaying costs. In addition, Blue Sky's management, on Mr. Jones' recommendation, decided to scale back the metallurgical testing and postponed the baseline environmental study, saving $7,316 and $35,000 respectively. The total cost of the completed program was $706,736, a cost overrun of $106,736 – slightly in excess of the $90,000 contingency factored into the budget.

Exploration Results

Drilling on the Main Vein Extension target intersected a strong vein structure over a surface distance of 250 meters and to a depth of 100 meters. Management believes this may be the faulted-off southwest extension of the Main Vein system. Blue Sky drilled one extra hole in this area to follow up on positive results. Two of five holes intersected economically significant gold-silver grades over mineable widths of at least 1.5 meters. Blue Sky will need to complete further work to assess the possibility of additional resources in this area.

Summarizes significant explorations results, both positive and negative, and explains changes to original recommended work program.

Wide-spaced drilling on the West Zone target identified a previously unknown vein system, which was traced at surface for 500 meters and to a depth of 150 meters. Blue Sky drilled one additional hole on this structure to follow up on positive results. One of the five holes intersected economically significant grades over mineable widths of at least 1.5 meters. These results are very encouraging, however, Blue Sky will need to complete further drilling to determine the grade, width, and continuity of this vein system.

As a result of Mr. Jones' recommendations, Blue Sky drilled only four of the eight proposed holes for East Zone I & II gold soil geochemistry targets. Management approved these changes due to budget constraints and the largely negative results from the limited drilling. The work completed to date on these targets has not found any significant mineralization or vein structures. Blue Sky drilled the Northwest geophysical target to test for the possible northern extension of the Northwest Vein system. While drilling intersected several zones of weakly mineralized quartz veining, gold-silver values were disappointing and no recognizable mineralized structures were found. Management does not plan to do any further work on these three targets at this time.

The results of preliminary metallurgical testing indicate that mineralization from the Main Vein will be amenable to standard milling and froth flotation processing and that suitable gold and silver/lead concentrates can be produced. Further work is required to assess metal recoveries, optimal treatment and to determine if a saleable concentrate can be produced.

Future Developments

Management is pleased with the results of the work completed during the past year. By identifying two new mineral structures, Blue Sky has increased the potential for finding additional resources and developing an economic mineral deposit.

Management plans to conduct further exploration work on the property during the next fiscal year. Dr. Smith has proposed a program with an estimated cost of $1 million. Work will include 5,000 meters of definition and step-out drilling on the West Zone and Main Vein Extensions at an estimated cost of $650,000. Dr. Smith also budgeted $190,000 and $100,000 for field/support costs and contingencies respectively. Blue Sky is also planning to complete further metallurgical testing ($25,000) and the postponed baseline environmental study ($35,000).

Describes the company's plans for future work and provides the estimated costs and time frame.

This field program is anticipated to be completed over a two-month period starting in June 20X3. Results of the metallurgical study should be available 3 months after the field program is completed. Blue Sky plans to finance this work and anticipated general and administrative overhead ($350,000) for the next year with a future private placement.

Babine Gold-Copper Property

Discloses that regulatory approval of this material acquisition has been granted.

The Babine project is located in the Omineca Mining Division of British Columbia, approximately 60 kilometers northeast of the town of Smithers. The project is at a preliminary stage of exploration, covering porphyry gold-copper style mineralization and alteration recently exposed in a recent logging road cut. During the previous fiscal year, Blue Sky entered into an option to acquire a 100% interest in the property by making cash payments of $300,000 and issuing 500,000 shares over four years. In addition, Blue Sky is required to spend at least $1.5 million, in stages, over this period. The Vendor will retain a 2.5% net smelter return. Regulatory approval of this acquisition was required from the TSX Venture Exchange. This was obtained during the current fiscal year.

Discloses significant property payments due dates.

To date, Blue Sky has paid $50,000, issued 100,000 shares and spent $103,392 on exploration. A further payment of $50,000 was due and made October 31, 20X2. (See subsequent events page 15.) Blue Sky will need to make additional payments of $50,000 and 100,000 shares and complete further work commitments of $200,000 by October 31, 20X3 to maintain the option.

Exploration Program

Blue Sky carried out a program that included geological mapping, wide spaced soil and rock geochemistry and a magnetic survey, as recommended by Dr. Smith and as set out in the Company's prospectus. The estimated budget for this program, including contingencies, was $115,000. Final costs were $103,392 with the actual expenditures slightly higher than budgeted due to a longer than anticipated field program.

Table 2 - Reconciliation of Proposed & Actual Expenditures

	Proposed	Actual	Variance
Assaying	$ 20,000	$ 18,545	$ (1,455)
Camp Costs	21,000	23,792	2,792
Geological Consulting	27,000	28,765	1,765
Geophysical Survey	12,000	12,666	666
Labour	12,000	12,400	400
Transportation and Shipping	8,000	7,224	(776)
	100,000	103,392	3,392
Contingencies (15%)	15,000	—	(15,000)
Total	$115,000	$103,392	$ (11,608)

Exploration Results

Mapping of the limited rock exposure in the showing area confirmed a large area of porphyry style alteration, associated with elevated gold and copper values in rock samples. These are centered on a weak magnetic low. Coincidental with this alteration is a broader copper-gold soil geochemistry anomaly with scattered peripheral anomalies for lead, zinc and silver.

Future Developments

Management is encouraged by the positive results received to date. Preliminary results suggest the presence of a large porphyry gold-copper system on the claims. Dr. Smith has recommended additional work to assess the extent and grade of the mineralization. This work would include line cutting, an induced polarization survey, trenching, and a contingent diamond drill program to test priority targets. The cost of this work is estimated at $250,000.

Describes the company's plans for future work and provides the estimated costs and time frame.

Due to fiscal constraints and other commitments, Blue Sky decided in mid August 20X2 to seek a joint venture partner to further develop this property. In late September 20X2, Blue Sky entered into a joint venture agreement with ABC Major Mining Company Ltd. ABC can acquire a 20% interest in the project by completing the next phase of work and making the next payment of $50,000 to the underlying vendor. ABC can earn a further 30% interest by completing the remaining work commitments and cash payments required under Blue Sky's option agreement. ABC can acquire a further 20% by funding all further exploration and completing a bankable feasibility study recommending production. (See subsequent events page15.)

Finlayson Lake Lead-Zinc-Copper Property

In 19XX, Blue Sky entered into an option to acquire a 100% interest in 50 mineral claims in the Finlayson Lake area of the Yukon Territory covering prospective ground for volcanic-hosted massive-sulfide deposits. To date, Blue Sky spent in excess of $350,000 conducting initial sampling, mapping, geophysics, and a limited backpack-drilling program. This work confirmed the presence of a number of favorable mineralized horizons with local concentrations of economically interesting lead-zinc-copper grades. Dr. Smith has recommended further work to more fully delineate these structures and to identify prospective higher-grade sections.

Discusses the impact of changing metal prices and equity market conditions on company's ability to advance this property and explains why the company dropped the option.

During the past two fiscal years, Blue Sky has been unable to raise further capital to undertake these recommendations due to unfavorable base metal prices and the reluctance of venture capital markets to fund such projects. In order to maintain the current option, Blue Sky was required to make a property payment of $250,000 to the vendor during the current fiscal year. Attempts to renegotiate or postpone this payment were unsuccessful. As a result, Blue Sky made a decision to terminate the option and write off all expenditures and costs incurred to date on this property. Blue Sky will continue to focus its resources on its precious metal projects.

Related Party Transactions

The management and supervision of Blue Sky's mineral exploration activities are subcontracted to a company owned and operated by Mr. David Jones, President of Blue Sky. Labour and professional fees are billed at standard industry rates. Other direct costs are billed at cost plus a 15% administration fee. Third party contracts such as drilling and metallurgical studies are billed directly to Blue Sky at no markup. During the current fiscal year, Blue Sky paid a total of $256,081 to this company. At September 30, 20X2, Blue Sky owed Mr. Jones' company $16,140 ($50,830 at December 31, 20X1) for exploration expenditures.

Discusses the nature and purpose of related party transactions, including specific services provided.

In addition, a company owned by Ms. Jane Williams, a director of Blue Sky, receives management fees of $2,500 per month to provide day-to-day office management and administrative services.

General and Administrative

Accounting and legal costs in the current quarter reflect the involvement of Blue Sky's solicitor in the Babine project joint venture negotiations ($11,890). Costs for the three months ended September 30, 20X1 include $23,500 in professional fees incurred in connection with completion of the company's September 25, 20X1 prospectus.

Underlying reasons for the changes in financial statement items have been provided.

Underlying reasons for the changes in financial statement items have been provided.

Travel costs increased significantly during the current quarter as the company focused its efforts on expanding investor awareness of the company's exploration projects. In July Mr. David Jones, Dr. John Smith, and a representative from Blue Sky's investment relations firm traveled to Europe to give a presentation at an investment conference in Zurich, Switzerland and to potential investors in London, England ($19,580). The Zurich presentation resulted in preliminary discussions with several investors for a proposed $1.5 million private placement (see Liquidity and Solvency). In September the company participated in the New York Institutional Gold Conference ($14,000). Travel costs for the three months ended September 30, 20X1 include the cost of attending and participating in the 20X1 CIM Conference and Mining Exhibit in Toronto ($9,700).

Office expenditures and rent have increased significantly compared to last year as a result of the company moving into new offices earlier this year. The move was necessary because of the company's increased exploration and related financing activities on the Blackwater project. In addition, the company hired a full-time receptionist/secretary to handle day-to-day office activities.

Transfer agent and filing fees for the three months ended September 30, 20X2 are below those incurred in 20X1 as the prior year's figure includes filing fees paid to the exchange in connection with the company's prospectus ($5,000). On a year-to-date basis, such charges are also lower than the prior year as a result of the company's decision not to renew its contract with its SEDAR filing agent at the beginning of the year and, instead, to make its own filings on SEDAR.

Management of Blue Sky does not see any significant change to the quarterly administrative expenditures during the next three months or over the coming year. However, should Blue Sky not receive the required funding, Blue Sky will review all on-going expenditures and take appropriate action. (See liquidity and solvency below).

Investor Relations

Since May 20X2, Blue Sky has retained Onetwothree Communicators Ltd., a private company owned by Mr. Jonathan O'Connor, to provide investor relations services. These services include Onetwothree acting as Blue Sky's investor relations contact, creating and implementing a communication plan for Blue Sky, and being a liaison to the investment community. Onetwothree has been in the investment relation business for over 20 years and has significant expertise in the mineral exploration sector. Onetwothree is being paid a fee of $4,000 per month. Since Onetwothree was retained, Blue Sky has redesigned its website, prepared and disseminated brochures and a video at a cost of approximately $8,000. From June through November 20X1, Blue Sky had retained another investor relations firm for a fee of $4,000 per month.

Liquidity and Solvency

At September 30, 20X2, Blue Sky had a working capital deficiency of $14,438. In the short term, Blue Sky will be relying on loans from related parties and the exercise of options and share purchase warrants to fund the company.

Provides meaningful discussion of liquidity and solvency and the company's plans to resolve these problems.

Subsequent to September 30, 20X2, Blue Sky received $35,000 in proceeds from the exercise of stock option and share purchase warrants for 53,846 of Blue Sky's shares. In addition, a $100,000 private placement has been completed. The private placement consisted of 117,647 units at a price of $0.85 per unit. Each unit consisted of one share and one share purchase warrant exercisable to acquire one additional share at a price of $0.98 on or before November 2, 20X3. The private placement shares have a hold period of four months. All of the proceeds have been allocated towards general operating activities.

Blue Sky is in preliminary discussions with investors regarding a $1.5 million private placement to fund the next phase of exploration on the Blackwater project and general and administrative overhead for the next year. However, there is no guarantee Blue Sky will be able to raise these funds.

Subsequent Events

Subsequent to September 30, 20X2, Blue Sky's management was advised by ABC Major Mining Co. Ltd. that it would not be pursuing its joint venture with Blue Sky on the Babine Property due to budget constraints and changing priorities. Pursuant to the terms of the agreement, ABC made the required $50,000 payment to the underlying vendor but will not be undertaking the proposed next phase of exploration. As a result of the cancellation of the joint venture, Blue Sky's management successfully negotiated a one-year deferral of the next $200,000 work requirement with the vendor. Management is pursuing discussions with a number potential joint venture partners and is optimistic that a new joint venture agreement can be completed in the near future.

Discusses significant events that occurred subsequent to the fiscal reporting period.

MD&A Example:

Abbreviated financial statements are included simply as a reference for the purposes of highlighting portions of the MD&A example. This sample does not include all of the information required by BC Form 51-901F.

Specifically:

• the financial statements do not contain the statement of cash flows and note disclosure required by CICA Handbook sections 1540 and 1751.

• Schedule B information has not been provided.

BC FORM 51-901F

BLUE SKY MINING CORP.

BALANCE SHEET

SEPTEMBER 30, 20X2

(Unaudited – prepared by management)

	Sept. 30, 20X2	Dec. 31, 20X1
		(audited)
Assets		
Current		
Cash	$ 28,200	$ 907,790
Goods and services taxes recoverable	9,100	3,200
Prepaid expenses	13,730	50,330
	51,030	961,320
Capital assets	13,680	7,230
Mineral property acquisition costs (schedule)	1,072,300	1,090,900
	$ 1,137,010	$ 2,059,450
Liabilities and Shareholders' Equity		
Current		
Accounts payable	$ 49,328	$ 90,370
Due to related parties	16,140	50,830
	65,468	141,200
Shareholders' Equity		
Share capital	17,483,970	17,206,970
Deficit	(16,412,428)	(15,288,720)
	1,071,542	1,918,250
	$ 1,137,010	$ 2,059,450

BLUE SKY MINING CORP.

STATEMENT OF LOSS AND DEFICIT

FOR THE PERIODS ENDED SEPTEMBER 30, 20X2

(Unaudited – prepared by management)

	For the three months ended Sept. 30,		For the nine months ended Sept. 30,	
	20X2	20X1	20X2	20X1
General and administrative				
Accounting and legal	$ 13,770	$ 26,530	$ 21,730	$ 44,070
Amortization	250	880	1,840	2,650
Investor relations	18,700	13,250	29,840	21,520
Management fees	7,500	7,500	22,500	22,500
Office and miscellaneous	5,160	2,200	11,750	5,450
Rent	11,250	6,000	33,750	18,000
Salaries and benefits	12,200	6,310	36,600	19,110
Telephone	3,250	3,250	8,810	7,890
Transfer agent and filing fees	4,860	10,190	14,630	28,450
Travel	38,010	12,210	48,230	17,690
	114,950	88,320	229,680	187,330
Other				
Exploration (note and schedule)	660,210	254,530	828,028	498,320
Acquisition costs of mineral properties abandoned (schedule)	72,850	—	72,850	—
Interest income	(2,250)	(4,370)	(6,850)	(8,160)
Loss for the period	845,760	338,480	1,123,708	677,490
Deficit, beginning of period	15,566,668	14,689,110	15,288,720	14,350,100
Deficit, end of period	$16,412,428	$15,027,590	$16,412,428	$15,027,590
Loss per share	$ 0.02	$ 0.01	$ 0.02	$ 0.01

Note: The company capitalizes property acquisition costs in accordance with CICA Handbook section 3061.06 and expenses exploration costs in accordance with CICA Emerging Issues Committee Abstract #126.

BLUE SKY MINING CORP.

SCHEDULE OF CUMULATIVE MINERAL PROPERTY COSTS (1)

FOR THE PERIODS ENDED SEPTEMBER 30, 20X2

(Unaudited – prepared by management)

	For the three months ended September		
	Blackwater Property	Babine Property	Other (3)
Acquisition costs			
Balance, beginning of period	$ 925,650	$ 70,000	$ 111,440
Incurred during period	—	—	38,060
Mineral properties abandoned	—	—	(72,850)
Balance, end of period	925,650	70,000	76,650
Exploration expenditures			
Assaying	5,270	14,840	2,590
Camp costs	49,820	19,030	—
Drilling	433,090	—	—
Geological consulting	28,260	23,010	9,520
Geophysical survey	—	10,130	—
Labour	9,920	9,920	—
Metallurgical testing	10,150	—	—
Road construction	7,100	—	—
Transportation and shipping	21,780	5,780	—
	565,390	82,710	12,110
Balance, beginning of period	2,655,976	20,682	411,230
Mineral properties abandoned	—	—	(354,370)
Balance, end of period	3,221,366	103,392	68,970
Cumulative mineral property costs	$ 4,147,016	$ 173,392	$ 145,620

Note:

(1) *Paragraph 32 of CICA Accounting Guideline #11 recommends companies in the development stage provide a schedule of the amounts*

(2) *BC Rule 3(9)(b) requires companies in the development stage provide a detailed breakdown of expenditure on a property-by-property*

(3) *"Other" represents other non-material mineral properties*

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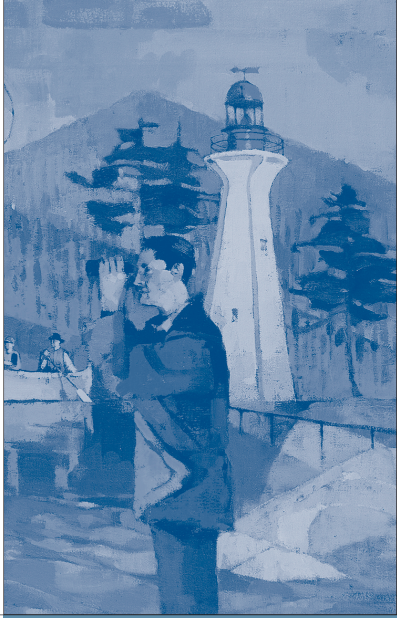
30, 20X2 (2)	For the nine months ended September 30, 20X2 (2)			
Total	Blackwater Property	Babine Property	Other (3)	Total
$ 1,107,090	$ 925,650	$ 70,000	$ 95,250	$ 1,090,900
38,060	—	—	54,250	54,250
(72,850)	—	—	(72,850)	(72,850)
1,072,300	925,650	70,000	76,650	1,072,300
22,700	6,591	18,545	2,590	27,726
68,850	62,276	23,792	—	86,068
433,090	541,363	—	—	541,363
60,790	35,323	28,765	15,310	79,398
10,130	—	12,666	—	12,666
19,840	12,400	12,400	—	24,800
10,150	12,684	—	—	12,684
7,100	8,874	—	—	8,874
27,560	27,225	7,224	—	34,449
660,210	706,736	103,392	17,900	828,028
3,087,888	2,514,630	—	405,440	2,920,070
(354,370)	—	—	(354,370)	(354,370)
3,393,728	3,221,366	103,392	68,970	3,393,728
$ 4,466,028	$4,147,016	$ 173,392	$ 145,620	$ 4,466,028

deferred or expensed to date for each significant project under development.
basis for each of the periods covered by the income statement and the statement of cash flows.



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If you have any questions about this CD Update, suggestions for future CD Update topics, or questions and comments about the BCSC's Continuous Disclosure Review Program, please call Larry Wilkins, CA, Manager, Continuous Disclosure Review at 604-899-6712 or email lwilkins@bcsc.bc.ca

MD&A information resources:

National Policy (NP) 51-201 Disclosure Standards (should be read in conjunction with this Update)

Instructions to Schedule C of BC Form 51-901F

Ontario Securities Commission Rule 51-501 (www.osc.gov.on.ca)

National Instrument (NI) 44-101F2 MD&A (for AIFs)

BCSC Continuous Disclosure Review Program, April 2000 Staff Report

BCSC Continuous Disclosure Updates

Canadian Performance Reporting Initiative Board: MD&A Guidance on Preparation and Disclosure (www.cica.ca)

Unless otherwise noted, all documents can be obtained from the BCSC website: www.bcsc.bc.ca