



## **Talon Metals Corp.**

### **MANAGEMENT'S DISCUSSION AND ANALYSIS**

For the three and nine months ended September 30, 2013

Dated: November 14, 2013

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*This Management's Discussion and Analysis ("MD&A") of the consolidated financial position for the three and nine months ended September 30, 2013, should be read in conjunction with the condensed consolidated interim financial statements of Talon Metals Corp. ("Talon" or the "Company") and notes thereto for the three and nine months ended September 30, 2013.*

Unless otherwise indicated, all monetary statements in this document are in Canadian dollars.

## **FORWARD-LOOKING INFORMATION**

This MD&A contains certain "forward-looking information". All information, other than information pertaining to historical fact, which addresses activities, events or developments that the Company believes, expects or anticipates will or may occur in the future, including, among other things, estimates in respect of mineral resource quantities, mineral resource qualities, the preparation of mineral resource estimates and the timing thereof, the Company's targets, goals, objectives and plans, the potential for lump and sinter at the Trairão Project (defined below), the potential for further metallurgical and mineralogical results on the basis of further testing, the Company's business plans, priorities and budget, including those associated with the Trairão Project, the Company's plans to actively look for new projects that could generate near-term cash flow for the Company and to review the use and allocation of its existing financial resources, projections in respect of capital expenditures, plans, the Company's liquidity and capital resources (including any plans to dispose of marketable securities).

Forward-looking information reflects the current expectations or beliefs of the Company based on information currently available to the Company. With respect to forward-looking information contained in this MD&A, the Company has made assumptions regarding, among other things, future currency and interest rates, the regulatory framework (including tax and trade laws and policies) in the countries in which the Company conducts its business, and the Company's ability to obtain suitably qualified staff and equipment in a timely and cost-efficient manner to meet the Company's needs.

Forward-looking information is subject to significant risks and uncertainties and other factors that could cause the actual results to differ materially from those discussed in the forward-looking information, and even if such actual results are realized or substantially realized, there can be no assurance that they will have the expected consequences to, or effects on the Company. Factors that could cause actual results or events to differ materially from current expectations include, but are not limited to: failure to establish estimated mineral resources and any reserves; the grade, quality and recovery of mineral resources varying from estimates; risks related to the exploration stage of the Company's properties; the possibility that future exploration results and metallurgical testing will not be consistent with the Company's expectations (including identifying additional and/or more extensive mineralization and/or recovery); changes in iron-ore prices; delays in obtaining or failures to obtain necessary regulatory permits and approvals from government authorities, including approval of applications for licences required to conduct field based programs on Talon's iron ore projects and approval of environmental impact assessment applications; availability of new projects suitable for Talon; uncertainties involved in interpreting drilling results, and the beneficiation process and other geological and product related data; changes in the anticipated demand for iron and steel; changes in equity and debt markets; inflation; changes in exchange rates; declines in U.S., Canadian and/or global economies; uncertainties relating to the availability and costs of financing needed to complete exploration activities and demonstrate the feasibility of the Company's projects; exploration costs varying significantly from estimates; delays in the exploration, mineral processing and development of,

and/or commercial production from the properties Talon has an interest in; equipment failure; unexpected geological or hydrological conditions; political risks arising from operating in Brazil; delays or cancellation to proposed infrastructure upgrades in Brazil; imprecision in preliminary resource estimates; success of future exploration and development initiatives; the existence of undetected or unregistered interests or claims, whether in contract or in tort, over the property of Talon; changes in government regulations and policies (including proposed changes to Brazilian mining legislation); risks relating to labour; other exploration, development and operating risks; liability and other claims asserted against Talon; volatility in prices of publicly traded securities; and other risks involved in the mineral exploration and development industry and risks specific to the Company, including the risks discussed in this MD&A under "*Risks and Uncertainties*".

Forward-looking information speaks only as of the date on which it is made and, except as may be required by applicable securities laws, the Company disclaims any intent or obligation to update forward-looking information, whether as a result of new information, future events or results or otherwise. Although the Company believes that the assumptions inherent in the forward-looking information are reasonable, forward-looking information is not a guarantee of future performance and accordingly undue reliance should not be put on such information due to the inherent uncertainty therein.

The mineral resource figures referred to in this MD&A are estimates, and no assurances can be given that the indicated levels of iron ore will be produced. Such estimates are expressions of judgment based on knowledge, mining experience, analysis of drilling results, beneficiation tests and industry practices. Valid estimates made at a given time may significantly change when new information becomes available. While the Company believes that the resource estimates included in this MD&A are well established, by their nature, resource estimates are imprecise and depend, to a certain extent, upon statistical inferences which may ultimately prove unreliable. If such estimates are inaccurate or are reduced in the future, this could have a material adverse impact on the Company.

Mineral resources are not mineral reserves and do not have demonstrated economic viability. Inferred mineral resources are estimated on limited information not sufficient to verify geological and grade continuity or to allow technical and economic parameters to be applied. Inferred mineral resources are too speculative geologically to have economic considerations applied to them to enable them to be categorized as mineral reserves. There is no certainty that mineral resources can be upgraded to mineral reserves through continued exploration.

*Additional information relating to the Company, including the Company's Annual Information Form for the year ended December 31, 2012, is available on SEDAR at [www.sedar.com](http://www.sedar.com).*

### **SUMMARY OF QUARTERLY RESULTS**

The following table provides selected quarterly consolidated financial information for the periods ending as indicated. It is derived from the unaudited interim consolidated financial statements and the audited annual consolidated financial statements of the Company. All numbers below are unaudited.

	2013			2012			2011	
	Sept 30	June 30	March 31	Dec 31	Sept 30	June 30	March 31 <sup>(1)</sup>	Dec 31 <sup>(1)</sup>
Total revenues	19,623	21,028	18,838	19,740	15,843	24,207	93,524	367,868
Net income/(loss) from continuing operations	(584,886)	(2,405,320)	(1,294,104)	(13,679,030)	(691,255)	(2,763,338)	(1,028,262)	(1,317,629)
Net income/(loss) from continuing operations per share – basic and diluted	(0.01)	(0.03)	(0.01)	(0.15)	(0.01)	(0.03)	(0.01)	(0.01)
Net income/(loss) and comprehensive income/(loss)	(584,886)	(2,405,059)	(1,615,645)	(13,738,421)	(854,110)	(2,701,842)	(1,017,970)	(1,920,552)
Net income/(loss) and comprehensive income/(loss) per share – basic and diluted	(0.01)	(0.03)	(0.02)	(0.15)	(0.01)	(0.03)	(0.01)	(0.02)

**Note:**

(1) Takes into account prior year adjustments.

\*Certain figures in the chart above have been reclassified to conform to the current year's presentation.

Quarterly trends in total revenues reflect in most part interest received on cash balances. Trends in quarterly expenses are driven primarily by office and general expenses and salaries, benefits, consulting and management fees. The most variable component of total expenses generally over the past eight quarters has been stock option compensation payment expense.

### **REVIEW OF QUARTERLY RESULTS**

Certain amounts in the condensed consolidated interim statement of loss and comprehensive loss from the prior year have been reclassified to conform to the current year's presentation and, as such, the discussion that follows below takes into account such prior year reclassification. Specifically, certain amounts from office and general expenses; professional fees; salaries, benefits, consulting and management fees; and travel have been reclassified into project evaluation and due diligence expenses. Please also refer to Note 9 in the Company's Condensed Consolidated Interim Financial Statements for further details of this reclassification.

## REVENUE

Revenue is comprised solely of interest income on the Company's cash and cash equivalents balance. The amount in Q3 2013 of \$19,623 increased compared to the same quarter last year (\$15,843) due to slightly higher interest rates. Revenues for the nine month period ended September 30, 2013 (\$59,489) decreased compared to the same period last year (\$133,574), due in most part to the fact that the Company held a large amount of funds in Brazil in the first quarter of 2012 where interest rates are significantly higher than where the Company normally keeps its cash and cash equivalents.

## EXPENSES

Office and general expenses decreased in Q3 2013 (\$110,300) compared to Q3 2012 (\$412,731), mainly as a result of the Company's concerted effort to decrease costs wherever possible. The same trend is also apparent for the nine months ended September 30, 2013 (\$293,206) compared to September 30, 2012 (\$689,579).

Professional fees decreased in Q3 2013 (\$17,865) compared to the same quarter last year (\$52,935) and for the nine months ended September 30, 2013 (\$105,567) compared to the nine months ended September 30, 2012 (\$244,491). Auditor and legal fees are the major components of the professional fees expense. One of the main reasons for the decrease is that throughout 2012 and into 2013, the Company has performed more legal work in-house and, when possible, expects to continue to do so going forward.

Stock option compensation payments were lower both in Q3 2013 (\$134,761) compared to Q3 2012 (\$216,803) and for the nine months ended September 30, 2013 (\$462,811) compared to the nine months ended September 30, 2012 (\$615,631). The decreases were a result of (i) fewer options being granted in 2013, (ii) reduced amortization expense of options granted in previous periods, (iii) the Company's recent practice of issuing options at a premium to market prices, (iv) a lower Talon share price and, (v) a lower assumption in regards to volatility. Beginning in 2012, the Company began issuing the majority of options with vesting provisions (generally, over the course of two year periods, and in some instances, with earlier vesting occurring should certain thresholds in the price of the Company's shares be met) rather than having them vest on the date of grant, which had historically been the case. Vesting of options was enacted in order to better align the interests of employees with the interests of shareholders by incentivizing employees to stay with the Company longer-term, as well as by aligning compensation to share performance. From an accounting standpoint, this practice means that option grants that are subject to vesting are amortized over the course of the vesting period rather than being fully expensed in the quarter in which they are granted. As such, the stock option compensation payment expense in Q3 2013 takes into account not only options granted in the quarter but also those subject to vesting that were granted in previous quarters and are being amortized. The issuance of options subject to vesting is expected to continue.

Salaries, benefits, consulting and management fees remained relatively constant at \$181,402 in Q3 2013 compared to \$183,317 in Q3 2012. For the nine months ended September 30, 2013 (\$559,538), this expense decreased compared to the nine months ended September 30, 2012 (\$998,332) largely as the result of severance paid in Q1 2012 to Mr. Scholtz, the previous President & CEO of the Company.

Project evaluation and due diligence expenses increased to \$878,009 in Q3 2013 from \$303,221 in Q3 2012 and to \$1,977,640 for the nine months period ended September 30, 2013 from \$1,284,484 for the same period in the prior year. The increases were the result of the Company's increased focus on evaluating new projects with near term cash generating potential and in some instances, significant exploration upside potential. Specifically, the increases were the result of higher costs in the areas of salaries, benefits, consulting and management fees; professional fees and travel, offset by a decrease in property payments and licenses.

Listing and filing expenses remained fairly constant in Q3 2013 and for the nine month period ended September 30, 2013 compared to the same periods last year.

## INVESTMENTS

Foreign currency translation gain/loss changed from a loss of \$568,789 in Q3 2012 to a smaller loss of \$160,639 in Q3 2013. The balance changed from a loss of \$71,355 for the nine month period ended September 30, 2012 to a gain of \$184,710 for the nine month period ended September 30, 2013. This balance is highly variable due to the volatility of exchange rates and the Company's large cash balance. The decreased losses in the more recent periods are the result of a strengthening of the U.S. dollar where the company holds approximately 45% of its cash and cash equivalents.

The share of loss in Tlou Energy Limited ("**Tlou Energy**") decreased in Q3 2013 to nil compared to Q3 2012 (\$187,519) because early in Q2 2013 the Company changed the accounting of its Tlou Energy investment from the equity method to a financial instrument classified as held-for-trading. The accounting change was implemented in accordance with IFRS and was a result of the Company no longer having significant influence in Tlou Energy. In particular, the Company's ownership in Tlou Energy decreased to less than 20% in Q2 2013. Assuming the Company's interest in Tlou Energy remains below 20%, the investment in Tlou Energy will continue to be accounted for as a portfolio investment with mark-to-market gains and losses being reported on the income statement. For the nine month period ended September 30, 2013 compared to the nine month period ended September 30, 2012, the decrease was the result of the Company's declining ownership interest in Tlou Energy and the change in accounting policy described above.

For the three and nine months ended September 30, 2013, the Company had a mark-to-market gain of \$966,910 and a mark-to-market loss of \$465,694, respectively, as a result of change in the market value of the shares of Tlou Energy. The mark-to-market loss takes into account a discounted valuation of certain of the Tlou Energy shares held by the Company which are currently subject to the ASX Escrow (defined below). There was no similar loss or gain in prior periods, because, as discussed above, the Company first began accounting for Tlou Energy as a portfolio investment in Q2 2013.

The loss on investments in Q3 2013 of \$73,830 compares to a gain in Q3 2012 of \$236,663. For the nine month periods ended September 30, 2013 and September 30, 2012, the loss on investments was \$396,101 and \$851,911, respectively. These losses were due to a decrease in the value of the shares of Lago Dourado Minerals Ltd. ("**Lago Dourado**") and Brazilian Gold Corporation ("**Brazilian Gold**") held by the Company.

## **NET LOSS**

Net loss for the three month period ended September 30, 2013 was \$0.6 million or \$0.01 per share (basic and diluted), which was primarily due to administration expenses<sup>1</sup> offset by an investment gain in Tlou Energy. This compares to a net loss of \$1.7 million or \$0.02 per share (basic and diluted) for the three months ended September 30, 2012, which was primarily due to administration expenses.

Net loss for the nine month period ended September 30, 2013 was \$4.3 million or \$0.05 per share (basic and diluted), which was primarily due to administration expenses and investment losses in Tlou Energy and other investments. This compares to a net loss of \$4.5 million or \$0.05 per share (basic and diluted) for the nine month period of the prior year.

## **COMPANY OVERVIEW**

The Company is a mineral exploration company focused on the exploration and development of the Trairão iron project (the "**Trairão Project**") in Brazil. As of the date hereof, the only material property of the Company is the Trairão Project.

In September 2010, Talon acquired 100% of the rights to the Trairão Project, as well as to another iron ore project, the Inajá South iron project (the "**Inajá South Project**"), both situated in Pará State, Brazil. Talon acquired these projects pursuant to agreements with Codelco do Brasil Mineração Ltda and Barrick International (Barbados) Corp.

Pará State is one of the more recently developed iron ore producing districts in Brazil. The principal iron ore mines in the region are at Carajás, about 150 kilometres to the north of the Trairão Project. Exploration for iron ore by other companies continues both to the south and north of the Trairão Project.

The initial RC and diamond drilling programs have been completed at the Trairão Project. Pursuant to this initial drilling campaign, a total of 444 RC drill holes comprising 24,215 metres were drilled (346 of the RC drill holes were on Target Areas comprising the updated mineral resource estimate reported below) and a total of 92 diamond drill holes comprising 13,335 metres were drilled.

In March 2012, Talon reported an updated inferred mineral resource estimate and an initial indicated mineral resource estimate for Target Areas 1 to 6 as well as for Target Area 8 on the Trairão Project of approximately 1.4 Bt at an average grade of 34.27% Fe (using a 25% Fe cut-off) in the indicated category and approximately 1.2 Bt at an average grade of 29.48% Fe (using a 25% Fe cut-off) in the inferred category (see table below).

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<sup>1</sup> "administration expenses" include the following expenses: Office and General; Professional Fees; Salaries, Benefits, Consulting and Management Fees; Provision for Distribution of Rio Verde Shares to Option holders; Travel; Listing and Filing Expense; and Depreciation of Equipment.



Trairao Resources (Total Aggregated Resources)									
Cut Off Grade: 25% Fe									
Resource Class	Tonnes (Mt)	Fe (%)	SiO <sub>2</sub> (%)	Al <sub>2</sub> O <sub>3</sub> (%)	Mn (%)	P (%)	LOI (%)	FeO (%)	CaO (%)
<b>Grand Total</b>									
Indicated	1404.3	34.27	35.79	8.87	0.116	0.036	5.50	1.05	0.018
Inferred	1211.8	29.48	41.60	7.00	0.129	0.034	6.66	8.79	0.342
<i>The effective date of this resource estimate is March 2, 2012</i>									

Talon's independent technical consultants, Coffey Mining Pty Ltd. ("**Coffey**"), under the supervision of Mr. Porfírio Cabaleiro Rodriguez, who is a "qualified person" under National Instrument 43-101 ("**NI 43-101**"), prepared a NI 43-101 compliant technical report incorporating these results entitled "Fourth Independent Technical Report on Mineral Resources" dated March 30, 2012 (the "**Trairão Technical Report**").

Please refer to Talon's March 2, 2012 press release entitled "Talon Metals Announces Substantial Increase to Mineral Resources at the Trairão Iron Project, Brazil" as well as the Trairão Technical Report for further information on the Trairão Project. The press release and the Trairão Technical Report are available under Talon's SEDAR profile at [www.sedar.com](http://www.sedar.com).

On September 27, 2012 and November 22, 2012, the Company issued press releases entitled "Talon Metals Provides Operational Update on its Trairão Iron Project" and "Talon Metals Reports Positive Metallurgical Results for the Trairão Iron Project, Brazil" (the "**Update Press Releases**") which, among other things, provided updates on the recent work completed by the Company on the Trairão Project, including further mineralogical and metallurgical test work. Please refer to the Update Press Releases available under Talon's SEDAR profile at [www.sedar.com](http://www.sedar.com) for further information.

In addition, on March 25, 2013, the Company issued a press release entitled "Talon Metals Announces Lump and Sinter Feed Potential at the Trairão Iron Project, Brazil" which expanded on the Update Press Releases regarding the potential for a high grade, near surface resource that may be amenable to producing direct shipping ore from the Trairão Project. Please refer to this press release which is available under Talon's SEDAR profile at [www.sedar.com](http://www.sedar.com) for further information.

During the fourth quarter of this year, the Company plans to continue to engage with potential purchasers of lump and sinter in order to assess the likelihood of being able to profitably sell lump and/or sinter from the Trairão Project in the near future. The Company believes that engaging with potential purchasers prior to making a decision to commence further exploration activities is prudent, as the Company continues to manage and monitor its rate of investment into the Trairão Project. See also "*Outlook*" below.

The Company expects to spend approximately \$150,000 during the fourth quarter of 2013 on the Trairão Project.

A total of approximately \$160,000 was spent by Talon on the Trairão Project during the third quarter of 2013, compared to approximately \$460,000 during the third quarter of 2012.

Talon holds equity investments in a number of other public companies, including approximately 3.2 million common shares in Brazilian Gold and 500,000 common shares in Lago Dourado, both of which are listed on the TSX Venture Exchange.

In addition, as at the date hereof, Talon holds a total of 14,285,714 shares in Australian Securities Exchange (“**ASX**”) listed Tlou Energy (representing approximately a 14% interest in Tlou Energy). In accordance with the rules of the ASX, all of Talon’s current holding of Tlou Energy shares are subject to a mandatory two year escrow period (the “**ASX Escrow**”). The ASX Escrow began on the date of Tlou Energy’s listing in April 2013.

In September 2013, Talon sold 2,571,428 shares of Tlou Energy which were not subject to the ASX Escrow at A\$0.36 per Tlou Energy share.

Talon also holds options to purchase an aggregate of 4,945,055 Tlou Energy shares at an exercise price of A\$1.25 each, exercisable until May 9, 2015 (the “**Tlou Options**”). However, all of the Tlou Options are also subject to the ASX Escrow. Talon may not exercise or transfer any Tlou Options until the ASX Escrow has expired.

### **Qualified Persons**

Mike Shaw, Vice President, Exploration of Talon is a “Qualified Person” within the meaning of NI 43-101. Mr. Shaw has reviewed, approved and verified the data disclosed in this MD&A (other than the mineral resource estimates), including sampling, analytical and test data underlying the technical information.

The “Qualified Person”, as such term is defined in NI 43-101, who is responsible for the Trairão Technical Report is Porfírio Cabaleiro Rodriguez, who is a mining engineer, independent of Talon and an employee of Coffey. Mr. Rodriguez is responsible for the mineral resource estimates in this MD&A and has reviewed, approved and verified the data disclosed in this MD&A relating to the mineral resource estimates (including sampling, analytical and test data underlying the mineral resource estimates).

### **CAPITAL EXPENDITURES ON EXPLORATION PROJECTS**

The deferred exploration and development expenditures for the Company’s properties, including the Trairão Project, are comprised as follows:

	<b>Dec 31, 2012</b>	<b>2013 Additions</b>	<b>Sept 30, 2013</b>
<i>Mineral properties</i>			
Trairão Project	\$16,614,930	\$867,509	\$17,482,439
Inaja South Project	1,142,644	10,871	1,153,515
Campo Grande Gold Project	533,195	6,020	539,215
	<b>\$18,290,769</b>	<b>\$884,400</b>	<b>\$19,175,169</b>

Amounts incurred on the exploration of mineral properties for the three months ended September 30, 2013 and 2012, amounted to approximately \$170,000 and \$470,000, respectively.

Exploration expenditures incurred for the three months ended September 30, 2013 are primarily a result of spending on the Trairão Project. The above amount represents a decrease in quarterly spending compared to spending on the Trairão Project in the same period of last year.

## **FINANCIAL INSTRUMENTS**

	<b>Sept 30, 2013</b>	<b>Sept 30, 2012</b>	<b>Dec 31, 2012</b>
<i>Held for trading, measured at fair value:</i>			
Cash and cash equivalents	\$15,980,010	\$17,046,187	\$16,485,729
Investments	\$329,149	\$1,939,274	\$1,447,186
Investment – Tlou Energy	\$2,880,000	- (1)	- (1)

Note:

(1) At these points in time, Tlou Energy was accounted for as an equity investment.

Talon is exposed to various risks related to its financial assets and liabilities. The most significant of these risks are discussed below and are managed on an ongoing basis

### **Credit Risk Management**

Certain of the Company's financial assets are exposed to a degree of credit risk. The Company endeavors to mitigate credit risk by holding its cash and cash equivalents as cash deposits, short-term government treasury bills, money market funds and guaranteed investment certificates ("GICs") with major commercial banks.

Credit risk relating to accounts receivable arises from the possibility that any counterparty to an instrument fails to perform. The Company does not feel there is significant counterparty risk that could have an impact on the fair value of cash and cash equivalents and receivables.

### **Liquidity Risk**

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due or at reasonable cost. The Company has in place a planning and budgeting process to help determine the funds required to support the Company's normal operating requirements on an ongoing basis and its capital, development and exploration expenditures. The Company ensures that there are sufficient funds to meet its short-term requirements, taking into account its anticipated cash flows from operations and its holdings of cash and cash equivalents.

As of September 30, 2013, the Company had a cash and cash equivalents balance of \$15,980,010 (December 31, 2012 - \$16,485,729) to settle current liabilities of \$984,646 (December 31, 2012 - \$1,072,118).

### **Market Risk**

Market risk is the risk that changes in market prices, including foreign exchange rates and interest rates will affect the Company's income or the value of its financial instruments.

Talon revalues its marketable securities using the quarter end bid price and as such, values are subject to change. The Company monitors on an ongoing basis changes in bid prices associated with the Company's marketable securities and makes buy/sell/hold determinations based on a

number of factors, including the Company's current treasury position, the internal valuation associated with the company in question and market outlook.

A 5% change in the value of the Company's investments on the last day of the period with all other facts/assumptions held constant, would have affected the net loss of the Company for the nine month period ended September 30, 2013, by approximately \$160,000.

### **Foreign Exchange Risk**

The Company is exposed to movements in the United States dollar and the Brazilian real as transfers are made to the Brazilian subsidiaries of the Company in United States dollars and subsequently converted in Brazil to Brazilian reals. Talon manages its foreign exchange risk, to the extent possible, by only undertaking currency exchanges on an as-needed basis and maintaining minimal and prudent balances in foreign currencies.

At September 30, 2013, the Company had net monetary assets and liabilities in foreign currencies, as follows (Canadian dollar equivalent):

United States dollars	\$7,202,687
Brazilian real	\$ 138,769

If foreign exchange rates changed by 5% on the last day of the period with all other facts/assumptions held constant, there would be a change in the net loss of the Company for the nine month period ended September 30, 2013 of approximately \$370,000.

The Company entered into two foreign currency hedge contracts, spanning 26 days and 19 days, respectively, in February and March of 2012, in order to preserve the value of cash denominated in Brazilian real. Historically, the Company has not participated in hedging activities and further hedging activities are not anticipated in the future.

### **Interest Rate Risk**

The Company is exposed to interest rate risk only to the extent of its interest income on holding of government treasury bills, money market funds and GICs. These are typically short-term investments with a term of less than ninety days. It is management's opinion that the Company is not exposed to significant interest or credit risks arising from these financial instruments. The Company mitigates its risk by holding its short-term investments in instruments low in risk and highly rated with reputable financial institutions. The Company has no interest bearing debt.

The carrying values of the Company's financial instruments approximate their fair values unless otherwise noted.

The Company's financial instruments are classified as current assets or liabilities on the statement of financial position of the Company. For receivables/payables with a remaining life of less than one year, the notional amount is deemed to reflect the fair value.

### **Fair Value Hierarchy**

The fair value hierarchy establishes three levels to classify inputs to the valuation techniques used to measure fair value. Level 1 inputs are quoted market prices (unadjusted) in active markets for

identical assets or liabilities. Level 2 inputs are inputs other than quoted market prices included in Level 1 that are observable for the asset or liability, either directly, such as prices, or indirectly (derived from prices). Level 3 inputs are unobservable (supported by little or no market activity), such as non-corroborative indicative prices for a particular instrument provided by a third party.

The Company has classified its financial assets and liabilities as follows:

*Level 1*

Cash and cash equivalents	\$15,980,010
Investments	\$ 329,149

*Level 2*

None

*Level 3*

Investments	\$ 2,880,000
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A loss on investments in Q3 2013 of \$73,830 (Q3 2012 – gain of \$236,663) has been recognized in the Company's statement of loss and comprehensive loss for the period. This relates to the revaluation of investments based on the closing bid price of the investments at the end of each quarter and any realized gains or losses.

**FINANCIAL CONDITION, CASH FLOW, LIQUIDITY AND CAPITAL RESOURCES**

**Cash Flow Highlights**

	Nine months ended September 30, 2013 (unaudited)	Nine months ended September 30, 2012 (unaudited)	Year ended December 31, 2012
Operating activities	\$(2,808,651)	\$(3,620,732)	\$(4,495,955)
Investing activities	2,302,932	(933,498)	(618,733)
Financing activities	–	30,000	30,000
Increase/(decrease) in cash & cash equivalents	(505,719)	(4,524,320)	(5,084,688)
Beginning cash & cash equivalent balance	16,485,729	21,570,417	21,570,417
Ending cash & cash equivalents balance	15,980,010	17,046,187	16,485,729

***Operating Activities***

Operating activities for the nine months ended September 30, 2013 consumed \$2.8 million of cash primarily due to net operating expenses. This compares to utilization of \$3.6 million in the same period of last year also primarily due to net operating expenses. See "Review of Quarterly Results" for a discussion of operating expenses.

Operating activities for the year ended December 31, 2012 consumed \$4.5 million primarily due to net operating expenses.

### ***Investing Activities***

Investing activities for the nine month period ended September 30, 2013 produced \$2.3 million due to proceeds from the sale of (i) shares in Tlou Energy and Rio Verde Minerals Development Corporation, and (ii) equipment, offset by capitalized exploration costs. This compares to a utilization of \$0.9 million in the same period last year, primarily due to capitalized exploration costs offset by proceeds on sale of investments and equipment.

Investing activities for the year ended December 31, 2012 utilised \$0.6 million primarily due to capitalized exploration costs offset by proceeds on sale of investments and equipment.

In the short term, the Company may dispose of certain marketable securities.

### ***Financing Activities***

There were no financing activities during the nine month period ended September 30, 2013.

For the nine month period ended September 30, 2012 and the year ended December 31, 2012, financing activities were comprised of an option exercise that generated \$30,000.

The Company evaluates possible financing activities on an ongoing basis taking into account the Company's short and long term budgets in respect of its projects and working capital requirements, as well as the availability and costs associated with raising additional capital.

### **Liquidity and Capital Resources**

Cash and cash equivalents were approximately \$16.0 million as of September 30, 2013. The Company has sufficient liquidity to continue expected operations into the medium-term.

All cash equivalents are held in government treasury bills, money market funds and GICs with major commercial banks.

Historically, Talon's main source of funding has been the issuance of equity securities for cash. The Company's access to such funding is always uncertain and there can be no assurance of continued access to equity funding if required in order for the Company to meet its planned long-term business objectives. This is particularly true in the current uncertain global financial markets, which may continue to be characterised by significant reductions in liquidity and access to capital.

**A summary of Contributed Surplus for the period from January 1, 2011 to September 30, 2013 is as follows:**

Balance	January 1, 2011	\$7,864,955
Options	Exercised	(307,424)
Options	Granted 2011	6,020,178
Balance	December 31, 2011	13,577,709
Options	Granted 2012	1,024,194
Options	Exercised 2012	(29,250)
Balance	December 31, 2012	14,572,653
Options	Granted 2013	462,811
Balance	September 30, 2013	15,035,464

**DISCLOSURE OF OUTSTANDING SHARE DATA**

The following details the share capital structure of the Company as at November 14, 2013:

	<b>Expiry Date</b>	<b>Exercise Price</b>	<b>Total</b>
Common Shares			92,076,687
Stock Options	June 11, 2014	\$0.385	440,000
Stock Options	May 21, 2015	\$0.40	3,444,350
Stock Options	Oct 26, 2015	\$0.70	900,000
Stock Options	Jan 17, 2016	\$1.58	255,000
Stock Options	Feb 7, 2016	\$2.12	40,000
Stock Options	Mar 3, 2016	\$2.48	200,000
Stock Options	May 25, 2016	\$1.95	975,000
Stock Options	Oct 1, 2016	\$1.00	125,000
Stock Options	Jan 31, 2017	\$0.45	2,800,000
Stock Options	Apr 4, 2017	\$0.415	1,059,605
Stock Options	Apr 25, 2017	\$0.37	385,395
Stock Options	June 15, 2017	\$0.33	400,000
Stock Options	Feb 20, 2018	\$0.30	300,000
Stock Options	Feb 28, 2018	\$0.30	100,000
Stock Options	Mar 20, 2018	\$0.30	1,000,000
Stock Options	Aug 1, 2018	\$0.30	400,000
Stock Options	Oct 1, 2018	\$0.30	500,000
Total fully diluted number of shares			105,401,037

During the third quarter of 2013, the Company issued 400,000 stock options pursuant to the Company's incentive stock option plan (the "Plan"). The following details the stock options of the Company outstanding as at September 30, 2013:

	Options	Weighted Average Exercise Price
Outstanding – beginning of year	12,389,350	\$0.70
Cancelled	(80,013)	0.37
Cancelled	(200,000)	0.57
Cancelled	(50,000)	0.385
Cancelled	(225,000)	0.40
Cancelled	(219,987)	0.415
Cancelled	(125,000)	1.00
Cancelled	(50,000)	1.58
Cancelled	(115,000)	1.95
Cancelled	(300,000)	2.48
Granted	1,800,000	0.30
Outstanding – end of the period	12,824,350	\$0.65

Other than 2,733,733 stock options, all of the stock options outstanding have been issued pursuant to the Plan.

### Estimated fair value of stock options

The Company determined the fair value of the stock options issued during the year ended December 31, 2012 and the nine month period ended September 30, 2013, using the Black-Scholes option pricing model under the following range of assumptions:

Expected life	5 years
Risk-free interest rate	1.4-1.8%
Volatility	60-111%
Dividends	0%

In the third quarter of 2013, a total stock option compensation payment of \$134,761 was recognized in the Company's consolidated statements of loss and comprehensive loss, compared with \$216,803 in the third quarter of 2012. For the year ended December 31, 2012, a total stock option compensation payment of \$1,024,194 was recognized in the statement of loss and comprehensive loss.

### **RISKS AND UNCERTAINTIES**

Talon is subject to a number of risk factors due to the nature of the mineral business in which it is engaged, the limited extent of its assets and its stage of development.

The exploration operations of the Company are speculative due to the high-risk nature of its business which is primarily focused on the acquisition, exploration and development of mineral projects. The Company's activities in pursuit of its objectives are subject to a number of risks and uncertainties.

The following is a summary of the most significant of those risks and uncertainties affecting or that could affect the financial condition or results of operations of the Company. For a complete discussion of the risks and uncertainties facing the Company, please refer to the Company's Annual Information Form for the year ended December 31, 2012 under the heading "Risk Factors" available on SEDAR at [www.sedar.com](http://www.sedar.com). These risk factors could materially affect the Company's future operating results and could cause actual events to differ materially from those described in



forward-looking statements relating to the Company. The Company may face additional risks and uncertainties, including, risks and uncertainties that are unknown to the Company or risks and uncertainties that the Company now believes to be unimportant, which could have a material adverse effect on the business of the Company. If any of the risks actually occur, the business, financial condition or results of operations of the Company could be negatively affected.

#### *Exploration, Development and Operating Risks*

Although Talon's present activities are directed towards the acquisition, financing, exploration and development of mineral projects, it is anticipated that its activities shall also ultimately include mining operations.

The exploration for and development of mineral deposits involves significant risks which even a combination of careful evaluation, experience and knowledge may not eliminate. While the discovery of an ore body may result in substantial rewards, few properties that are explored are ultimately developed into producing mines. Major expenses may be required to locate and establish mineral reserves, to develop metallurgical processes and to construct mining and processing facilities at a particular site. Actual exploration, development and/or other costs and economic returns may differ significantly from those the Company has anticipated. It is impossible to ensure that the exploration programs planned by Talon will result in a profitable commercial mining operation. Talon cannot give any assurance that its current and future exploration activities and/or metallurgical testing will be consistent with the Company's expectations or result in any additional mineralization or improved recovery rates and/or a mineral deposit containing mineral reserves. Whether a mineral deposit will be commercially viable depends on a number of factors, some of which are: the particular attributes of the deposit, such as size, grade and proximity to infrastructure; metal and iron ore prices that are highly cyclical; and government regulations, including regulations relating to prices, taxes, royalties, land tenure, land use, importing and exporting of minerals and environmental protection. The exact effect of these factors cannot be accurately predicted, but the combination of these factors may result in Talon not receiving an adequate return on invested capital.

Mining and exploration operations generally involve a high degree of risk. Talon's operations are subject to all the hazards and risks normally encountered in the exploration, development, production and beneficiation of iron ore, including unusual and unexpected geologic formations, seismic activity, cave-ins, flooding and other conditions involved in the drilling and removal of material, any of which could result in damage to, or destruction of, mines and other producing facilities, damage to life or property, environmental damage and possible legal liability. Although adequate precautions to minimize risk will be taken, mining and exploration operations are subject to hazards such as equipment failure or failure of retaining dams around tailings disposal areas which may result in environmental pollution and consequential liability.

The economic viability of mineral projects, including iron projects such as the Trairão Project, is affected, in part, by the ability of the operator to mine, beneficiate and enter into off-take agreements with potential end users. No assurance can be made that Talon will be successful in entering into off-take agreements in respect of local and/or export sales or in accessing local smelting facilities.

### *Uncertainty Relating to Inferred and Indicated Mineral Resources*

There is a risk that the inferred and indicated mineral resources referred to in this MD&A cannot be converted into mineral reserves as the ability to assess geological continuity is not sufficient to demonstrate economic viability. Due to the uncertainty that may attach to inferred and indicated mineral resources, there is no assurance that inferred and indicated mineral resources will be upgraded to resources with sufficient geological continuity to constitute proven and probable mineral reserves as a result of continued exploration.

### *Legislative Changes*

The government of Brazil has announced its intention to amend the country's current mining legislation which governs certain of the operations and activities of the Company in Brazil. A draft of the legislative changes has been released but it is subject to further parliamentary review and possible changes. It is not known what the final form of such changes will comprise of or when the changes will be approved and implemented, if ever. Such changes in legislation could have a material adverse effect on the Company's business, financial condition and results of operations and cause increases in exploration expenses, capital expenditures or production costs, or abandonment or delays in development of the Company's existing and/or new properties, including the Trairão Project.

### *Iron Ore Prices*

The Company's current principal business is the exploration and development of iron. Iron ore prices have historically been volatile and are primarily affected by the demand for and price of steel in addition to the supply/demand balance. Given the historical volatility of iron ore prices and the particular effects of the recent global financial crisis, there are no assurances that the iron ore price will remain at current levels. An increase in iron ore supply without a corresponding increase in iron ore demand could be expected to result in a decrease in the price of iron ore. Similarly, a decrease in iron ore demand without a corresponding decrease in the supply of iron ore would be expected to result in a decrease in the price of iron ore. A continued decline in iron ore prices would adversely impact the business of Talon and could affect the feasibility of Talon's iron ore projects. A continued decline in iron ore prices would also be expected to adversely impact the Company's ability to attract financing.

Iron ore prices are also affected by numerous other factors beyond the Company's control, including the relative exchange rate of the U.S. dollar with other major currencies, global and regional demand, political and economic conditions, and transportation costs in major iron ore producing regions. Given the historical volatility of iron ore prices and the effects of the recent global financial crisis, there are no assurances that iron ore prices will remain at current levels.

### *Competition*

The mining industry is intensely competitive in all of its phases and the Company competes with many companies possessing greater financial and technical resources than it. Competition in the mining industry is primarily for properties that can be developed and produced economically; the technical expertise to find, develop, and operate such properties; the labour to operate the properties; and the capital for the purpose of funding such properties. Such competition may result in the Company being unable to acquire desired properties, to recruit or retain qualified employees or to acquire the capital necessary to fund its operations and develop its properties.

Existing or future competition in the mining industry could materially adversely affect the Company's prospects for mineral exploration and success in the future, in both iron and other commodities the Company is and/or may be interested in pursuing and developing.

#### *Infrastructure*

Mining, processing, development and exploration activities depend, to one degree or another, on adequate infrastructure. Reliable roads, bridges, power sources and water supply are important determinants, which affect capital and operating costs. Unusual or infrequent weather phenomena, sabotage, government or other interference in the maintenance or provision of such infrastructure could adversely affect the Company's operations, financial condition and results of operations.

#### *Land Title*

The Company's interests in mineral properties are comprised of exclusive rights under government licenses and contracts to conduct operations in the nature of exploration and, in due course if warranted, development and mining, on the license areas. Maintenance of such rights is subject to ongoing compliance with the terms of such licenses and contracts. While the Company intends to take all reasonable steps to maintain title to its mineral properties, there can be no assurance that it will be successful in extending or renewing mineral rights on or prior to the expiration of their term. The acquisition of title to mineral properties is a very detailed and time-consuming process. Title to, and the area of, mineral concessions may be disputed. Although the Company believes it has taken reasonable measures to ensure proper title to its properties, there is no guarantee that title to any of its properties will not be challenged or impaired. Third parties may have valid claims underlying portions of the Company's interests, including prior unregistered liens, agreements, transfers or claims (including native land claims) and title may be affected by, among other things, undetected defects. In addition, the Company may be unable to operate its properties as permitted or to enforce its rights with respect to its properties.

#### *Additional Capital*

The exploration and development of the Company's properties, including continuing exploration and development projects, and the construction of mining and beneficiation facilities and commencement of mining operations, will require substantial additional financing. Failure to obtain sufficient financing will result in a delay or indefinite postponement of development or production on any or all of the Company's properties or even a loss of a property interest. The main source of funds available to the Company is through the sale of equity capital, properties/equipment, royalty interests or the entering into of joint ventures. Additional financing may not be available when needed or if available, the terms of such financing might not be favourable to the Company and might involve substantial dilution to existing shareholders. Failure to raise capital when needed would have a material adverse effect on the Company's business, financial condition and results of operations. Global securities markets continue to experience volatility, which is resulting in difficulty in raising equity capital and market forces may render it difficult or impossible for the Company to secure placees to purchase any new share issuances at prices which will not lead to severe dilution to existing shareholders, or at all.

*Governmental Regulation; Environmental Risks and Hazards*

The mineral exploration activities of the Company are subject to various laws governing prospecting, development, production, taxes, labour standards and occupational health, mine safety, toxic substances and other matters. Mining, beneficiation and exploration activities are also subject to various laws and regulations relating to the protection of the environment. Although the Company believes that its exploration activities are currently carried out in accordance with all applicable rules and regulations, no assurance can be given that new rules and regulations will not be enacted or that existing rules and regulations will not be applied in a manner that could limit or curtail production or development of the Company's properties. Amendments to current laws and regulations governing the operations and activities of the Company or more stringent implementation thereof could have a material adverse effect on the Company's business, financial condition and results of operations and cause increases in exploration expenses, capital expenditures or production costs, reduction in levels of production at producing properties, or abandonment or delays in development of the Company's existing and/or new properties.

All phases of the Company's operations are subject to environmental regulation in the various jurisdictions in which it operates. Environmental legislation is evolving in a manner that will require stricter standards and enforcement, increased fines and penalties for non-compliance, more stringent environmental assessments of proposed projects and a heightened degree of responsibility for companies and their officers, directors and employees. There is no assurance that existing or future environmental regulation will not materially adversely affect the Company's business, financial condition and results of operations. Environmental hazards may exist on the properties on which the Company holds interests that are unknown to the Company at present and that have been caused by previous or existing owners or operators of the properties.

In particular, existing and possible future environmental and social impact legislation, regulations and actions, including the regulation of air and water quality, mining reclamation, solid and hazardous waste handling and disposal, the promotion of occupational health and safety, the protection of wildlife and ecological systems and the protection of the societies and communities of indigenous peoples, could cause significant expense, capital expenditures, restrictions and delays in the Company's activities, the extent of which cannot be predicted and which may well be beyond its capacity to fund. Environmental and social impact studies may be required for some operations, and significant fines and clean-up responsibilities may be imposed for companies causing damage to the environment in the course of their activities.

In addition, the Company could incur substantial losses as a result of loss of life, severe damage to and destruction of property, natural resources and equipment, pollution and other environmental damage, clean-up responsibilities, regulatory investigation and penalties, suspension of operations and repairs to resume operations.

Government approvals and permits are currently, or may in the future be, required in connection with the Company's operations. To the extent such approvals are required and not obtained, the Company may be curtailed or prohibited from proceeding with planned exploration or development of its properties.

Failure to comply with applicable laws, regulations and permitting requirements may result in enforcement actions thereunder, including orders issued by regulatory or judicial authorities causing operations to cease or be curtailed, and may include corrective measures requiring capital expenditures, installation of additional equipment, or remedial actions. Parties engaged in

mining and beneficiation operations, including the Company, may be required to compensate those suffering loss or damage by reason of such activities and may have civil or criminal fines or penalties imposed for violations of applicable laws or regulations, which may adversely affect the Company.

## **RELATED PARTY TRANSACTIONS AND BALANCES**

Related parties include the board of directors of the Company, close family members and enterprises which are controlled by these individuals as well as certain persons performing similar functions.

Effective April 1, 2011, the Company entered into a revised administrative and advisory services agreement (the "**Tau Agreement**") with Tau Capital Corp. ("**Tau**"). Warren Newfield and Greg Kinross, both directors of Talon are also directors of Tau. Under the Tau Agreement, Talon agreed to pay Tau a monthly service fee of \$58,500. Effective April 1, 2012, the parties agreed to lower the monthly service fee to \$25,000, given that Tau would be providing fewer direct services to Talon. On June 1, 2012, the Tau Agreement was terminated by the parties. For the nine months ended September 30, 2013, fees paid for these services were \$nil (2012 - \$225,500).

Effective April 1, 2011, Talon entered into a services agreement with a company owned by an officer and director of Talon (Luis Azevedo) (the "**Brazil Agreement**"). Pursuant to the Brazil Agreement, the company provides Talon with certain accounting, legal and general administrative functions in Brazil. The Brazil Agreement had an initial term of one year and automatically renewed for additional one year terms, until terminated in accordance with its terms. Under the Brazil Agreement, Talon agreed to pay a monthly service fee of US\$33,000. Effective May 1, 2012, the parties agreed to lower the monthly service fee to US\$23,000 and, on October 1, 2012, the parties agreed to further lower the monthly service fee to US\$18,000. Coupled with the revised fee in October 2012, the parties agreed to a one year term for the Brazil Agreement terminating September 30, 2013, unless extended by agreement of the parties. From October 1, 2013, the parties have agreed to extend the Brazil Agreement on a month-to-month basis. For the nine months ended September 30, 2013, fees paid amounted to \$158,000 (2012 - \$256,266).

Accounts payable and accrued liabilities at September 30, 2013 include \$nil payable to related parties (December 31, 2012 - \$1,919 payable to Tau).

The remuneration of directors and officers of the Company for the three and nine months ended September 30, 2013 and September 30, 2012 were as follows:

	<b>Three months ended Sept 30, 2013</b>	<b>Three months ended Sept 30, 2012</b>	<b>Nine months ended Sept 30, 2013</b>	<b>Nine months ended Sept 30, 2012</b>
Cash Compensation	\$462,775	\$329,375	\$1,304,158	\$1,006,661 <sup>(1)</sup>
Stock option compensation	107,205	91,908	414,028	494,988
Aggregate Compensation	<u>\$569,980</u>	<u>\$237,467</u>	<u>\$1,718,186</u>	<u>\$1,501,649</u>

Note:

(1) Cash compensation includes severance of \$189,000.

The following stock options were issued during the nine months ended September 30, 2013 to directors and executive officers of the Company:

<b>Date of Grant</b>	<b>Number</b>	<b>Exercise Price</b>	<b>Expiry Date</b>
February 20, 2013	200,000	\$0.30	February 20, 2018
February 20, 2013	75,000	\$0.30	February 20, 2018
February 28, 2013	100,000	\$0.30	February 28, 2018
August 1, 2013	300,000	\$0.30	August 1, 2018

## **CRITICAL ACCOUNTING ESTIMATES AND CHANGES IN ACCOUNTING POLICIES**

The preparation of consolidated financial statements in conformity with IFRS requires management to make estimates, judgments and assumptions that affect the application of accounting policies and the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the period. Actual results could differ from those estimates.

Significant assumptions about the future and other sources of estimation uncertainty that management has made at the statement of financial position date, that could result in a material adjustment to the carrying amounts of assets and liabilities, in the event that actual results differ from assumptions made, relate to, but are not limited to, the valuation of resource properties.

Talon considers the following accounting policies to be critical in the preparation of its financial statements:

### *Resource properties and deferred exploration and evaluation costs*

Interests in mineral exploration properties are recorded at cost. Exploration expenditures, other than those of a general nature, relating to mineral properties in which an interest is retained are deferred and carried as an asset until the results of the projects are known. If the project is unsuccessful or if exploration has ceased because continuation is not economically feasible, the cost of the property and the related exploration expenditures are written off. The Company only capitalizes costs on its core properties and expenses all costs related to properties that were of a secondary focus.

The cost of mineral properties includes the cash consideration paid and the negotiated value of shares issued on the acquisition of properties. Properties acquired under option agreements, whereby option payments are made at the discretion of the company, are recorded in the financial statements at the time payments are made. The proceeds from options granted on properties are credited to the cost of the related property.

Once the feasibility of a project has been established, deferred exploration expenses and other costs are segregated as deferred development expenditures. These costs are amortized over the estimated useful life of the related mineral property as commercial production commences. If the net carrying amount of the deferred exploration expenses is not recoverable, these costs are written down to net recoverable amount of the deferred exploration expense.

The amounts shown for mineral properties and deferred exploration costs represents cost to date, and do not necessarily represent present or future values as they are entirely dependent upon the economic recovery of future reserves.

The Company does not accrue the estimated future costs of maintaining its mineral properties in good standing.

#### *Stock option compensation payments*

The Plan allows employees, directors and consultants of the Company to acquire shares of the Company. The fair value of options granted is recognized as an employee or consultant expense with a corresponding increase in equity. An individual is classified as an employee when the individual is an employee for legal or tax purposes (direct employee) or provides services similar to those performed by a direct employee, and includes directors and most consultants of the Company. The fair value is measured at grant date and each tranche is recognized over the period during which the options vest. The fair value of the options granted is measured using the Black-Scholes option pricing model taking into account the terms and conditions upon which the options were granted.

#### *Impairment of non-financial assets*

At the end of each reporting period the carrying amounts of the Company's non-financial assets are reviewed to determine whether there is any indication that those assets have suffered an impairment loss. Where such an indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment, if any. The recoverable amount is the higher of fair value less costs to sell and value in use. Fair value is determined as the amount that would be obtained from the sale of the asset in an arm's length transaction between knowledgeable and willing parties. In order to determine fair value, the Company considers multiple valuation approaches, including the income, market and cost approaches. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. If the recoverable amount of an asset is estimated to be less than its carrying amount, the carrying amount of the asset is reduced to its recoverable amount and the impairment loss is recognized in the profit or loss for the period.

Where an impairment loss subsequently reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognized for the asset in prior years. A reversal of an impairment loss is recognized immediately in profit or loss.

#### *Impairment of financial assets*

Financial assets are assessed for indicators of impairment at the end of each reporting period. Financial assets are impaired where there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows of the investment have been impacted.

For all other financial assets objective evidence of impairment could include:

- significant financial difficulty of the issuer or counterparty; or
- default or delinquency in interest or principal payments; or
- it becoming probable that the borrower will enter bankruptcy or financial re-organization.

#### *Investments in associates*

Talon accounts for its investments in companies over which it has significant influence using the equity basis of accounting whereby the investments are initially recorded at cost and subsequently adjusted to recognize Talon's share of earnings or losses of the investee companies and reduced by dividends received, if any. Carrying values of investments are reviewed for indicators of impairment and written down to estimated fair values if there is evidence of impairment. Such impairment would be recorded in the condensed consolidated statements of operations.

### **INTERNAL CONTROL OVER FINANCIAL REPORTING**

No changes were made to the Company's internal control over financial reporting during the three months ended September 30, 2013 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

### **OUTLOOK**

Further to the Company's press release dated September 27, 2012, the Company continues to believe that it is prudent to carefully manage its rate of investment into the Trairão Project, given, among other things, the current negative state of the economic environment for junior exploration companies, such as Talon. As a result, the Company has already taken steps to reduce its expenditures in respect of the Trairão Project, while broadening its corporate strategy to include pursuing opportunities that can generate cash flow for the Company in the near-term, including the potential sale of lump and sinter from the Trairão Project.

In March 2013, the federal government of Brazil announced its plan to make a number of infrastructure improvements throughout Pará State, where the Trairão Project is located. In the event these infrastructure changes are implemented, such would positively impact the Company's ability to potentially transport lump and sinter from the Trairão Project.

As a result of these announcements by the government, during the second quarter of this year, the Company:

- completed the evaluation of samples from the Company's recent auger drilling program on the surficial deposit at the Trairão Project; and
- worked with various consultants on flow sheet test work of samples from the surficial deposit at the Trairão Project,

in an effort to determine whether there is true potential for lump and sinter production from the Trairão Project.

Based on the results of the above activities, the Company continues to believe that there is potential for some lump and sinter production from the Trairão Project.

During the third quarter of this year, the Company started to engage with potential purchasers of lump and sinter in order to assess the likelihood of being able to profitably sell lump and/or sinter



from the Trairão Project in the near future. These discussions will continue throughout the fourth quarter. The Company believes that engaging with potential purchasers prior to making a decision to commence further exploration activities is prudent, as the Company continues to manage and monitor its rate of investment into the Trairão Project.

In regards to other potential opportunities, management is presently spending a large portion of their time reviewing projects with near term cash generating potential, and in some instances, significant exploration upside. In 2013, the Company has seen a marked increase in the number and quality of opportunities being presented to the Company. The Company continues to undertake its due diligence on a number of these opportunities.

Talon also plans to continue to review the use and allocation of its existing financial resources, while continuing to cut expenses where appropriate.