



**LYDIAN INTERNATIONAL LIMITED**  
**CONSOLIDATED FINANCIAL STATEMENTS**  
**FOR THE YEARS ENDED**  
**DECEMBER 31, 2016 AND 2015**

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# LYDIAN INTERNATIONAL LIMITED

## COMPANY PARTICULARS

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### DIRECTORS

Mr Gordon Wylie, Non-Executive Director and Chairman of the Board  
Mr Willan Abel, Non-Executive Director  
Mr Stephen J. Altmann, Non-Executive Director  
Dr Gillian Davidson, Non-Executive Director  
Mr Josh Parrill, Non-Executive Director  
Mr Timothy Read, Non-Executive Director  
Mr John Stubbs, Non-Executive Director  
Mr Howard Stevenson, Director

### OFFICERS

Mr Howard Stevenson, President and Chief Executive Officer  
Mr Douglas Tobler, Chief Financial Officer

### REGISTERED OFFICE

Suite 3  
5/6 Esplanade  
St Helier, Jersey, JE2 3QA  
Channel Islands  
Tel: +44 1534 747 890  
Website: [www.lydianinternational.co.uk](http://www.lydianinternational.co.uk)

### AUDITORS

Grant Thornton LLP  
Suite 501, 201 City Centre Drive,  
Mississauga Ontario, L5B 2T4  
Canada

### LEGAL COUNSEL

Stikeman Elliott  
5300 Commerce Court West  
199 Bay Street  
Toronto, Ontario M5L 1B9  
Canada

### BANKERS

Bank of Nova Scotia  
P.O. Box 4234 STN A 47696  
Toronto, Ontario M5W 5P6  
Canada

# LYDIAN INTERNATIONAL LIMITED

## MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL REPORTING

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The accompanying consolidated financial statements, the notes thereto, and other information in Management's Discussion and Analysis of Lydian International Limited and its subsidiaries (the "Company"), are the responsibility of Management and have been approved by the Board of Directors.

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board and reflect Management's best estimates, judgments and policies that it believes appropriate in the circumstances.

The Company maintains a system of internal accounting controls which provide on a reasonable basis, assurance that the financial information is relevant, reliable, accurate and that the Company's assets are appropriately accounted for and safeguarded.

The Board of Directors, principally through the Audit Committee, is responsible for ensuring Management fulfills its responsibilities for financial reporting and internal control. The Audit Committee is composed of three directors, all of whom are independent, and meets periodically with Management and the external auditors to review accounting, auditing, internal control and financial reporting matters.

The consolidated financial statements have been audited by Grant Thornton LLP, Chartered Professional Accountants, Licensed Public Accountants who were appointed by the shareholders. The auditor's report outlines the scope of their examination and their opinion on the consolidated financial statements.

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*Signed "Howard Stevenson"*  
President and CEO

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*Signed "Douglas Tobler"*  
Chief Financial Officer

March 30, 2017

# LYDIAN INTERNATIONAL LIMITED

## INDEPENDENT AUDITOR'S REPORT

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To the Shareholders of Lydian International Limited:

We have audited the accompanying consolidated financial statements of Lydian International Limited, and its subsidiaries, which comprise the consolidated statements of financial position as of December 31, 2016 and December 31, 2015, and the consolidated statements of profit and loss and comprehensive profit and loss, statements of cash flows and statements of changes in equity, for the years then ended, and a summary of significant accounting policies and other explanatory information.

### *Management's Responsibility for the Consolidated Financial Statements*

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

### *Auditor's Responsibility*

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

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

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

### *Opinion*

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of Lydian International Limited, and its subsidiaries as of December 31, 2016 and December 31, 2015, and their financial performance and cash flows for the years then ended in accordance with International Financial Reporting Standards.

*Signed* "Grant Thornton LLP"  
Chartered Professional Accountants  
Licensed Public Accountants  
March 30, 2017  
Mississauga, Canada

# LYDIAN INTERNATIONAL LIMITED

## CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

(expressed in US Dollars)

		As of	
	Notes	December 31, 2016	December 31, 2015
<b>ASSETS</b>			
<i>Current assets</i>			
Cash and cash equivalents		\$ 137,195,785	\$ 28,553,813
Restricted cash	5	9,077,823	-
Other current assets	6	1,058,428	518,012
Total current assets		<u>147,332,036</u>	<u>29,071,825</u>
<i>Non-current assets</i>			
Mineral property, plant and equipment, net	7	111,648,064	72,705,639
Derivative assets	12	7,591,788	-
Deferred financing costs	8	18,954,581	2,538,164
Other non-current assets	9	5,952,019	3,633,342
<b>TOTAL ASSETS</b>		<u>\$ 291,478,488</u>	<u>\$ 107,948,970</u>
<b>LIABILITIES</b>			
<i>Current liabilities</i>			
Accounts payable and accrued liabilities	10	\$ 5,904,983	\$ 2,010,337
Advances under stream agreement, net	11	-	24,925,588
Total current liabilities		<u>5,904,983</u>	<u>26,935,925</u>
<i>Non-current liabilities</i>			
Stream liability	11	60,268,697	-
Debt	11	10,981,333	-
Derivative liabilities	12	25,950,964	-
Provisions	13	451,782	338,498
Total liabilities		<u>103,557,759</u>	<u>27,274,423</u>
<b>EQUITY</b>			
Share capital	14	268,608,480	164,137,851
Employee share-based plan reserves		3,293,875	3,573,967
Translation of foreign operations		(18,472,308)	(19,265,294)
Accumulated deficit		(65,509,318)	(67,771,977)
Total equity		<u>187,920,729</u>	<u>80,674,547</u>
<b>TOTAL LIABILITIES AND EQUITY</b>		<u>\$ 291,478,488</u>	<u>\$ 107,948,970</u>
Commitments	23		
Contingencies	24		
Subsequent events	25		

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

# LYDIAN INTERNATIONAL LIMITED

## CONSOLIDATED STATEMENTS OF PROFIT AND LOSS AND COMPREHENSIVE PROFIT AND LOSS

(expressed in US Dollars)

		For the years ended December 31,	
		2016	2015
	Notes		
Interest income		\$ 313,360	\$ 28,901
<b>Total income</b>		<u>313,360</u>	<u>28,901</u>
Employee salaries and benefits expense	16	3,805,017	3,094,030
General and administrative expense	17	3,199,510	2,952,602
Depreciation and amortization expense		43,945	78,752
Gain on financial instruments at fair value	12	(9,853,933)	-
Other expense, net	18	856,162	316,889
<b>Total expense (income)</b>		<u>(1,949,299)</u>	<u>6,442,273</u>
<b>Income (loss) before income taxes</b>		2,262,659	(6,413,372)
Income taxes	19	-	-
<b>Net income (loss)</b>		<u>\$ 2,262,659</u>	<u>\$ (6,413,372)</u>
<b>Net income (loss) per share (basic and diluted)</b>	20	<u>\$ 0.00</u>	<u>\$ (0.04)</u>
<b>Other comprehensive income (loss):</b>			
Net income (loss)		\$ 2,262,659	\$ (6,413,372)
Other comprehensive Income (loss):			
Currency translation adjustment		792,986	(1,417,934)
<b>Total comprehensive income (loss)</b>		<u>\$ 3,055,645</u>	<u>\$ (7,831,306)</u>

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

# LYDIAN INTERNATIONAL LIMITED

## CONSOLIDATED STATEMENTS OF CASH FLOWS

(expressed in US Dollars)

		For the year ended December 31,	
	Notes	2016	2015
Cash flows from operating activities			
Net income (loss)		\$ 2,262,659	\$ (6,413,372)
<i>Adjustments for:</i>			
Depreciation and amortization		43,945	78,752
Impairment		474,676	-
Loss on disposal of plant and equipment		31,839	20,638
Write-off deferred finance costs		240,799	-
Interest income		(313,360)	(28,901)
Loss (gain) on financial instruments at fair value	12	(9,853,933)	-
Share-based compensation payments	16	747,506	614,645
<i>Working capital changes:</i>			
Change in other current assets		(571,673)	(218,973)
Change in accrued liabilities and other payables		84,201	(850,283)
<b><i>Cash used in operations</i></b>		<b><u>(6,853,341)</u></b>	<b><u>(6,797,494)</u></b>
Cash flows from investing activities			
Acquisition of mineral property, plant and equipment		(29,690,797)	(12,278,484)
Change in other non-current assets		(1,579,171)	-
Proceeds from short term investments		-	1,600,000
Interest income received		313,360	17,628
<b><i>Cash used in investing activities</i></b>		<b><u>(30,956,608)</u></b>	<b><u>(10,660,856)</u></b>
Cash flows from financing activities			
Proceeds from debt	11	45,000,000	25,000,000
Increase in restricted cash	5	(9,077,823)	-
Financing cost		(6,783,034)	(2,260,943)
Proceeds from issuance of share capital		118,346,559	13,142,107
<b><i>Cash generated from financing activities</i></b>		<b><u>147,485,702</u></b>	<b><u>35,881,164</u></b>
Net increase in cash and cash equivalents		109,675,753	18,422,814
Foreign exchange effect on cash		(1,033,781)	682,660
Cash and cash equivalents, beginning of period		28,553,813	9,448,339
Cash and cash equivalents, end of the period		<b><u>\$ 137,195,785</u></b>	<b><u>\$ 28,553,813</u></b>

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



# LYDIAN INTERNATIONAL LIMITED

## CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

(expressed in US Dollars)

	Share capital	Reserves			Accumulated deficit	Total
		Employee share option plan reserve	Restricted stock unit plan reserve	Translation of foreign operations		
<b>Balance at January 1, 2015</b>	\$ 150,199,754	\$ 3,755,312	\$ -	\$ (17,847,360)	\$ (61,358,605)	\$ 74,749,101
Issue of new shares	14,238,570	-	-	-	-	14,238,570
Cost of share issue	(1,096,463)	-	-	-	-	(1,096,463)
Attributable to expired options	795,990	(795,990)	-	-	-	-
Share based compensation	-	614,645	-	-	-	614,645
Total comprehensive loss	-	-	-	(1,417,934)	(6,413,372)	(7,831,306)
<b>Balance at December 31, 2015</b>	<u>\$ 164,137,851</u>	<u>\$ 3,573,967</u>	<u>\$ -</u>	<u>\$ (19,265,294)</u>	<u>\$ (67,771,977)</u>	<u>\$ 80,674,547</u>
Issue of new shares	118,346,559	-	-	-	-	118,346,559
Cost of share issue	(6,358,610)	-	-	-	-	(6,358,610)
Issue of warrants	(8,695,044)	-	-	-	-	(8,695,044)
Attributable to expired options	1,177,724	(1,177,724)	-	-	-	-
Share based compensation	-	229,018	668,614	-	-	897,632
Total comprehensive gain	-	-	-	792,986	2,262,659	3,055,645
<b>Balance at December 31, 2016</b>	<u>\$ 268,608,480</u>	<u>\$ 2,625,261</u>	<u>\$ 668,614</u>	<u>\$ (18,472,308)</u>	<u>\$ (65,509,318)</u>	<u>\$ 187,920,729</u>

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

# LYDIAN INTERNATIONAL LIMITED

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Years ended December 31, 2016 and 2015

(expressed in US Dollars, unless otherwise stated)

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### 1. GENERAL INFORMATION

Lydian International Limited ("Lydian") is a corporation continued under the laws of Jersey effective on December 12, 2007 (formerly existing under the laws of Alberta, Canada). The registered office address of Lydian is Suite 3, 5/6 Esplanade, St Helier, Jersey JE2 3QA Channel Islands. Lydian has two securities listed on the Toronto Stock Exchange ("TSX"). Its ordinary shares ("Ordinary Shares") began trading under the symbol LYD on January 10, 2008, and certain warrants ("Public Warrants") began trading under the symbol LYD.WT on May 26, 2016.

Lydian, together with its subsidiaries (the "Company"), is a gold development company, focusing on construction at its 100%-owned Amulsar Gold Project ("Amulsar"), located in south-central Armenia. Development at Amulsar is being conducted under the mining right issued by the Republic of Armenia in May 2016.

In conducting development activities in Armenia, the Company is subject to considerations and risks not typically associated with companies operating in Jersey, the United Kingdom, or Canada. These include but are not limited to risks such as political, economic and legal environments in emerging markets. The Company's results may be adversely affected by changes in political and social conditions and by changes in governmental policies with respect to mining laws and regulations, currency conversion, remittance abroad, rates and methods of taxation, and other factors.

### 2. BASIS OF PRESENTATION, CRITICAL ACCOUNTING JUDGMENTS AND KEY ESTIMATION UNCERTAINTIES

#### Statement of compliance

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board, effective as of December 31, 2016, and interpretations of the International Financial Reporting Interpretations Committee.

#### Basis of measurement

The consolidated financial statements have been prepared on the historical cost basis except for certain financial instruments which are measured at fair value through profit and loss as discussed in Note 13. All amounts are presented in United States Dollars ("US Dollars") unless otherwise stated.

#### Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and entities controlled by the Company (its "subsidiaries"). Control is achieved where the Company is exposed to variable returns and has the ability to affect those returns through power to direct the relevant activities.

The results of any subsidiaries acquired or disposed of during a period are included in the consolidated statement of profit and loss from the effective date of acquisition or up to the effective date of disposal, as appropriate. Where necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies into line with those used by other members of the Company. All intercompany transactions and balances are eliminated in full on consolidation.

# LYDIAN INTERNATIONAL LIMITED

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Years ended December 31, 2016 and 2015

(expressed in US Dollars, unless otherwise stated)

Details of the Company's direct and indirect subsidiaries as of December 31, 2016 and 2015 are as follows:

Name of subsidiary	Place of incorporation or registration	Functional currency	Effective ownership interest		Principal activity
			2016	2015	
Lydian International Holdings Ltd.	British Virgin Islands	USD	100%	100%	Intermediate holding company
Lydian Resources Kosovo	British Virgin Islands	CAD	100%	100%	Intermediate holding company
Lydian Resources Armenia	British Virgin Islands	USD	100%	100%	Intermediate holding company
Lydian Resources Georgia Limited	Jersey	CAD	100%	100%	Intermediate holding company
Lydian U.S. Corporation	U.S.A.	USD	100%	100%	Management company
Lydian Armenia CJSC (Lydian Armenia)	Armenia	USD	100%	100%	Mineral exploration and development
Georgian Resource Company LLC	Georgia	GEL	100%	100%	Mineral exploration
Kavkaz Zoloto CJSC	Armenia	AMD	95%	95%	Dormant company

### Critical accounting judgments in applying the Company's accounting policies

In applying the Company's accounting policies, management is required to make judgments, estimates and assumptions that affect the application of accounting principles and reported amounts of certain assets, liabilities, equity, income and expenses in instances when valuation is not readily apparent from other sources. These judgments, estimates and assumptions are based on historical experience and other factors considered relevant. Actual results may differ from these estimates. In management's opinion, all adjustments considered necessary for fair presentation have been included in these financial statements.

Certain events and transactions occurring during the years ended December 31, 2016 and 2015, required management to apply the following additional significant judgments:

*Impairment of development assets* – The Company had sufficient financial resources and therefore decided to proceed with construction of Amulsar in May 2016. Upon this decision, costs previously recorded as exploration and evaluation assets were reclassified to development assets. Evaluation of the recoverability of the Amulsar development asset was required at that time and will be performed each reporting period thereafter. The recoverability assessment is dependent on a number of judgments. These include consideration of indications of impairment and, if necessary to proceed with an assessment, such factors as mineral reserves and recoverable mineral products, execution of the development plan as intended, sufficiency of estimated future cash flows from mining operations, potential proceeds from dispositions, maintenance and receipt of necessary authorizations, and adequacy of financing. The Company will use the evaluation work of professional geologists, geophysicists and engineers for estimates in determining whether to continue development. These estimates generally rely on scientific and economic assumptions, which in some instances may not reflect actual outcomes and thereby affect the ultimate recoverability of the carrying value of development assets.

*Impairment of exploration and evaluation assets* – The assessment of impairment of exploration and evaluation assets requires judgment to determine whether indicators of impairment exist including factors such as, the period for which the Company has the right to explore, expected renewals of exploration rights, whether

# LYDIAN INTERNATIONAL LIMITED

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Years ended December 31, 2016 and 2015

(expressed in US Dollars, unless otherwise stated)

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substantive expenditures on further exploration and evaluation of resourced properties are budgeted and results of exploration activities up to the reporting date.

*Change in functional currency* – Effective May 26, 2016, the Company determined that the functional currency of Lydian Armenia changed from the Armenian Dram to the U.S. Dollar. This change was deemed appropriate as it became evident that Lydian Armenia's underlying transactions, particularly capital spending and financing of Amulsar, are predominantly denominated in U.S. Dollars. In connection with the change in functional currency of Lydian Armenia, the intermediary holding companies Lydian Resources Armenia and Lydian International Holdings Limited also changed. This change in judgment has been accounted for prospectively in accordance with IAS 21, *The Effects of Changes in Foreign Exchange Rates*.

Effective January 1, 2015, the parent company determined that that a change to its functional currency was appropriate from the Canadian Dollar to the U.S. Dollar as it became evident that the underlying transactions and events are predominantly denominated in U.S. Dollars. This shift occurred as a greater percentage of expenditures for technical and administrative services are denominated in U.S. Dollars. No other consolidated entities were affected by this change in functional currency. This change in judgment has been accounted for prospectively in accordance with IAS 21, *The Effects of Changes in Foreign Exchange Rates*.

*Stream liability* – The Company entered into a stream agreement ("Stream Agreement") on November 30, 2015 and subsequently received an initial advance of cash. As set out in the consolidated financial statements for the year ended December 31, 2015, management treated the cash received as an advance based on consideration of the characteristics of the cash advance and contractual terms of the agreement. In May, 2016 the Company derecognized the advance which was replaced with a financial liability, as it was management's judgment that the financing arrangement was best characterized as a financial liability as the Company met the conditions precedent to the agreement. This determination was based predominantly on conditions of the Stream Agreement permitting cash settlements.

### Key estimation uncertainties

Accounting estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimate is revised if the revision affects only that period or in the period of the revision and future periods if the revision affects both current and future periods.

The application of the Company's accounting policy for assessing impairment of development assets requires judgment. In completing impairment assessments, the Company utilized certain findings as reported in its technical report dated November 20, 2015 ("2015 Amulsar Technical Report"), which was prepared in accordance with National Instrument 43-101 – Standards for Disclosure of Mineral Projects ("NI 43-101"). This included the amount and timing of cash flows, reflecting findings such as mineral resources, mineral reserves, recovery rates, capital costs, operating costs, and royalty and tax burdens. Management also estimated gold and silver prices for the impairment assessments. Each of these considerations and judgments applied by management in completing the impairment assessments represent key sources of estimation uncertainty.

The Company entered into several financing agreements on November 30, 2015 that contained provisions giving rise to financial derivatives. Also, on May 26, 2016 the Company issued two forms of warrants, each representing financial derivatives. These derivatives are accounted for at fair value and marked to market each reporting period thereafter. In determining fair value, management judgment is required in respect of input variables of the financial model used for estimation purposes. These variables include such inputs as the Company's stock prices, stock price volatility, trading volumes of the Public Warrants, risk-free rates of return, the credit-risk-premium, LIBOR terms and associated rates, availability of alternative financing, gold and silver price forward curves, gold and silver price volatilities, timing

# LYDIAN INTERNATIONAL LIMITED

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Years ended December 31, 2016 and 2015

(expressed in US Dollars, unless otherwise stated)

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of future production, timing of draws upon financing facilities, timing of repayments of financing facilities, expected future LIBOR rates, timing of achieving commercial production, availability of positive cash flows from operations, and other factors.

The fair value of financial instruments that are not traded on an active market or do not have sufficient trading volumes are determined using valuation techniques. Management uses its judgment to select a variety of methods and makes assumptions that are mainly based on market conditions at the end of each reporting period.

### 3. ACCOUNTING POLICIES

#### *Foreign currencies:*

The individual financial statements of each entity of the Company are prepared in the currency of the primary economic environment in which the entity operates (its "functional currency"). The consolidated financial statements are expressed in US Dollars, which is the presentation currency.

In preparing the financial statements of the individual entities, transactions in currencies other than the entity's functional currency (foreign currencies) are recorded at the rates of exchange prevailing at the dates of the transactions. At each reporting date, monetary items denominated in foreign currencies are retranslated at rates prevailing at the reporting date and are recognized in profit and loss in the period in which they arise. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated.

For the purpose of presenting consolidated financial statements, the assets and liabilities of the Company's operations are expressed in US Dollars using exchange rates prevailing at the reporting date. Income and expense items are translated at the average exchange rates for the period, unless exchange rates fluctuated significantly during that period, in which case the exchange rates at the dates of the transactions are used. Translation differences arising are recognized in other comprehensive income and recorded in the Translation of foreign operations reserve.

#### *Cash and cash equivalents:*

Cash and cash equivalents comprise cash on hand, at banks and other highly liquid short-term instruments with initial maturities of 90 days or less. Short-term investments include money market based investments where initial maturity is between 91 days and one year.

#### *Restricted cash:*

Cash subject to restrictions that prevent its use for general purposes is excluded from cash and cash equivalents. Restricted cash is separately reported on the balance sheet as current or non-current depending on the expected disposition of the use restrictions.

#### *Materials and supplies inventories:*

Material and supplies inventories consist mostly of equipment parts and other items required to support drilling and excavation activities and are valued at the lower of average cost and net realizable value.

#### *Financial instruments (assets):*

The Company's financial assets include cash and cash equivalents, restricted cash, accounts receivable measured at the amount receivable less adjustment for the time value of money, and derivative assets which are carried at fair value.

#### *Financial instruments (liabilities):*

The Company's financial liabilities include accounts payable and accrued liabilities, other payables, and debt which are initially recognized at fair value and subsequently stated at amortized cost and derivative liabilities carried at fair value. Accounts payables are classified as current liabilities unless the Company has an unconditional right to defer settlement of the liability for at least 12 months after the reporting date.

# LYDIAN INTERNATIONAL LIMITED

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Years ended December 31, 2016 and 2015

(expressed in US Dollars, unless otherwise stated)

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The Company classifies financing arrangements giving consideration to cash flow characteristics, contractual terms and relevant business objectives. Financing arrangements such as the Stream Agreement are classified as a financial liability when all or a significant portion of the commitment can be settled in cash and, in management's judgment, other considerations are insufficient to support an alternative accounting method.

Derivatives, other than those deemed to be swaps, are accounted for at fair value on the inception date. Swap derivatives have a zero fair value at inception as the strike price of the underlying variable will be equal to the market price. After inception, all derivatives are adjusted to fair value as of the financial statement date, with the amount of adjustment being recognized currently as a gain or loss in the statement of profit and loss.

### *Financing costs:*

Costs incurred for debt and equity arrangements are recorded as financing costs. Such costs include legal and accounting fees, fees from independent engineers, printing costs, investment banker or registration fees, agency fees, arrangement fees, and the fair value of derivatives resulting from such debt and equity arrangements. As proceeds from financing transactions are received, the associated costs are allocated to and reclassified against such financing arrangements. Financing costs associated with debt are expensed over time as interest expense using the effective interest rate method. In the event that a financing effort is abandoned or unsuccessful, allocable financing costs are charged to expense.

### *Exploration and evaluation assets:*

Exploration and evaluation expenditures comprise costs incurred directly in exploration and evaluation, as well as the cost of mineral licenses. Such costs are capitalized as exploration and evaluation assets subsequent to acquisition of the licenses and pending determination of the feasibility of the project and an affirmative construction decision by the Company.

Expenditures are considered to be development costs when the work completed supports the future development of the property through the issuance of a technical report, issued in accordance with NI 43-101, and such development receives appropriate Board approvals. In addition to economic viability, the Board also considers the ability to obtain commercial financing and the Company's ability to execute within time and cost limitations. Once sufficiently supported, property-specific exploration and evaluation costs shall be reclassified as development assets, and future development costs are capitalized.

The Company reviews and evaluates the carrying value of its exploration and evaluation assets for impairment when events or changes in circumstances indicate that the carrying amounts of the related asset may not be recoverable. The identification of such events or changes and the performance of the assessment requires significant judgment. Furthermore, management's estimates of many of the factors relevant to completing this assessment, including commodity prices, foreign currency exchange rates, mineral resources, and operating, capital and reclamation costs, are subject to risks and uncertainties that may further affect the determination of the recoverability of the carrying amount.

At each reporting period, management reviews exploration and evaluation assets for indicators of impairment. If any such indicator exists, the recoverable amount of the asset is estimated 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. In determining the recoverable amounts of the Company's exploration and evaluation assets, the Company uses the fair value less costs to sell approach until such time as a value in use can be determined. 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. When there is no binding sales agreement, fair value less costs to sell is estimated as the discounted future pre-tax, post royalty cash flows expected to be derived from the asset, less an amount for costs to sell estimated based on similar transactions. The inputs used in the fair value measurement constitute Level 3 inputs under the fair value hierarchy. When discounting estimated future cash flows, the Company uses a discount rate that would approximate what market

# LYDIAN INTERNATIONAL LIMITED

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Years ended December 31, 2016 and 2015

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(expressed in US Dollars, unless otherwise stated)

participants would assign. Estimated cash flows are based on expected future production, metal selling prices, operating costs and capital costs.

If the recoverable amount of the asset is 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 and loss for that period. Impairment is assessed at the level of cash-generating units ("CGUs"), which are identified as the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other assets.

### *Development assets:*

Development assets consist of the Amulsar Gold Project. Development costs include costs directly related to bringing the mine to production. Development costs include:

- costs of exploration reclassified to development once economic recoverability is demonstrable and development is approved by the Board;
- engineering costs to design the size and scope of the project;
- environmental assessment and permitting costs;
- costs to acquire surface rights;
- pre-construction work such as early on-site infrastructure upgrades;
- construction in progress;
- asset rehabilitation costs;
- stripping costs;
- interest costs; and
- other costs directly associated with mine development

Upon entering the commercial production phase, development costs will be transferred to producing properties and will be amortized using the units of production method based on recoverable ounces of gold over the estimate period of economically recoverable reserves.

### *Construction in progress:*

Assets under construction are capitalized as construction in progress and included in development costs. The cost of construction in progress comprises its purchase price and any costs directly attributable to bringing it into working condition for its intended use. On completion, the cost of construction is transferred to the appropriate category of plant and equipment. No amortization or depreciation is recorded until the assets are substantially complete and available for their intended use.

### *Impairment of development assets:*

The Company reviews and evaluates the carrying value of its development assets for impairment when events or changes in circumstances indicate that the carrying amounts of the related asset may not be recoverable. The identification of such events or changes and the performance of the assessment requires significant judgment. Furthermore, management's estimates of many of the factors relevant to completing this assessment, including commodity prices, foreign currency exchange rates, mineral resources, and operating, capital and reclamation costs, are subject to risks and uncertainties that may further affect the determination of the recoverability of the carrying amount.

At each reporting period, management reviews development assets for indicators of impairment. If any such indicator exists, the recoverable amount of the asset is estimated 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. In determining the recoverable amounts of the Company's development assets, the Company uses the fair value less costs to sell approach until such time as a value in use can be determined. 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. When there is no binding sales agreement, fair value less costs to sell is estimated as the discounted future pre-tax, post royalty cash flows expected to

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be derived from the asset, less an amount for costs to sell estimated based on similar transactions. The inputs used in the fair value measurement constitute Level 3 inputs under the fair value hierarchy. When discounting estimated future cash flows, the Company uses a discount rate that would approximate what market participants would assign. Estimated cash flows are based on expected future production, metal selling prices, operating costs and capital costs.

If the recoverable amount of the asset is 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 and loss for that period. Impairment is normally assessed at the level of cash-generating units ("CGUs"), which are identified as the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other assets.

### *Capitalized Interest:*

Interest costs for qualifying assets are capitalized. Qualifying assets are assets that require a significant amount of time to prepare for their intended use, including projects that are in development or construction stages. Capitalized interest costs are considered an element of the cost of the qualifying asset. Capitalization ceases when the asset is available for use in the manner intended by management or if active development is suspended or ceases. Where the funds used to finance a qualifying asset form part of general borrowings, the amount capitalized is calculated using a weighted average of rates applicable to the relevant borrowings during the period. Where funds borrowed are directly attributed to a qualifying asset, the amount capitalized represents the borrowing costs specific to those borrowings.

### *Plant and equipment:*

Plant and equipment are stated at cost, less accumulated depreciation and any accumulated impairment losses.

The gain or loss arising on the disposal or retirement of an item of plant and equipment is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognized in the statement of profit and (loss).

Expenditure to replace a component of an item of plant or equipment that is accounted for separately is capitalized and the existing carrying amount of the component written off. Other subsequent expenditure is capitalized if future economic benefits will arise from the expenditure. All other expenditures, including repair and maintenance, are recognized in the statement of profit and (loss) as incurred.

Depreciation during construction is charged to development assets based on the cost, less estimated residual value, of the asset on a straight-line basis over the estimated useful life. Depreciation commences when the assets are available for use. The estimated useful lives are as follows:

Machinery and equipment	1 – 5 years
Motor vehicles	3 – 5 years
Office equipment	1 – 9 years

### *Impairment of plant and equipment:*

Assets that are subject to depreciation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognized for the amount by which the asset's carrying amount exceeds its recoverable amount.

The recoverable amount is the higher of the fair value less costs to sell and value in use. If the recoverable amount of an asset or cash generating unit is estimated to be less than its carrying amount, the carrying amount of the asset or cash-generating unit is reduced to its recoverable amount.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized, the previously recognized impairment loss is reversed through profit and loss to the extent that the carrying amount of plant and equipment at the date the impairment is reversed



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does not exceed what the cost less accumulated depreciation would have been had the impairment not been recognized.

### *Restoration and rehabilitation:*

A provisional liability for restoration and rehabilitation is recognized when there is a present obligation as a result of exploration or development activities undertaken, it is probable that an outflow of economic benefits will be required to settle the obligation, and the amount of the provision can be measured reliably. The estimated future obligations include the costs of dismantling and removal of facilities, restoration and monitoring of the affected areas. The provision for future restoration costs is the best estimate of the present value of the expenditure required to settle the restoration obligation at the reporting date. Future restoration costs are reviewed annually and any changes in the estimate are reflected in the present value of the restoration provision at each reporting date.

The initial estimate of the restoration and rehabilitation provision relating to exploration and development activities is capitalized into the cost of the related asset and amortized on the same basis as the related asset. Changes in the estimate of the provision of restoration and rehabilitation are treated in the same manner, except that the unwinding of the effect of discounting on the provision is recognized as a finance cost rather than being capitalized into the cost of the related asset.

### *Share-based compensation:*

Equity-settled awards, including share options, are measured at fair value at the date of grant and recognized over the vesting period, based on the Company's estimate of equity settled awards that will eventually vest, along with a corresponding increase in equity. Amounts related to expired and exercised options are transferred from share-based compensation reserve to share capital when the related expiration or exercise takes place.

Under the Company's Restricted Stock Unit Plan ("RSU Plan"), awards can be either equity or cash settled upon vesting at the discretion of the Board of Directors. As the Company does not have a present obligation to settle in cash, the awards are treated as equity-settled instruments and measured at fair value at the date of award and recorded in restricted share unit reserve. The vesting terms for RSUs awarded are specific to each individual award as determined and approved by the Board of Directors. The fair value of the RSUs is expensed over the vesting period specific to the grant. On exercise of the RSUs, the accumulated amount in the reserve is credited to share capital.

Compensation costs for the Option Plan and RSU Plan are recorded in share-based compensation expense unless directly attributable to development costs, in which case such costs are included in development assets.

### *Taxation:*

The Company has no taxable profit and no current income tax. Deferred tax is recognized on differences between the carrying amounts of assets and liabilities in the consolidated financial statements and the corresponding tax base used in the computation of taxable profit, and are accounted for using the liability method. Deferred tax liabilities are generally recognized for all taxable temporary differences, and deferred tax assets are generally recognized for all deductible temporary differences to the extent that it is probable that taxable profits will be available against which those deductible temporary differences can be utilized. Such assets and liabilities are not recognized if the temporary difference arises from goodwill or from the initial recognition (other than in a business combination) of the related asset or liability in a transaction that affects neither the taxable profit nor the accounting profit.

Deferred tax liabilities are recognized for taxable temporary differences associated with investments in subsidiaries except where the Company is able to control the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future. Deferred tax assets arising from deductible temporary differences associated with such investments are only recognized to the extent that it is probable that there will be sufficient taxable profits against which to utilize the benefits of the temporary differences and they are expected to reverse in the foreseeable future.

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The carrying amount of deferred tax assets is reviewed at each reporting date and increased or reduced to the extent that it is probable, or no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

Deferred tax assets and liabilities are measured at tax rates that are expected to apply in the period in which the liability is settled or the asset realized based on tax rates that have been enacted or substantively enacted by the reporting date. The measurement of deferred tax liabilities and assets reflects the tax consequences that would follow from the manner in which the Company expects, at the reporting date, to recover or settle the carrying amount of its assets and liabilities.

Current and deferred tax are recognized as expense or income in the profit and loss, except when they relate to items credited or debited directly to equity, in which case the tax is also recognized directly in equity, or where they arise from the initial accounting in a business combination.

### *Operating leases:*

Operating lease payments are recognized as an expense on a straight-line basis over the lease term, except where another systematic basis is more representative of the time pattern in which economic benefits from the leased asset are consumed.

### *Equity:*

An equity instrument is any contract that evidences a residual interest in the assets of the Company after deducting all of its liabilities. Equity instruments issued by the Company are recorded at the proceeds received, net of direct issue costs.

### *Net earnings (loss) per share:*

Basic earnings (loss) per ordinary share are calculated by dividing the net loss attributed to shareholders of the parent for the period by the weighted average number of Ordinary Shares outstanding during the period. Diluted earnings (loss) per ordinary share is calculated by adjusting the weighted average number of Ordinary Shares outstanding to assume conversion of all dilutive potential Ordinary Shares.

### *Segment information:*

The Company has identified its operating segments based on the internal reports that are reviewed and used by executive management (collectively, the Chief Operating Decision Maker, or "CODM") in assessing performance and in determining the allocation of resources. The CODM considers the business from a geographic perspective and assesses the performance of geographic segments based on measures of profit and loss as well as assets and liabilities. These measures include operating expenditures, expenditures on exploration and development, plant and equipment, non-current assets and total debt, if any.

The Company operates under a single geographic segment engaged in mineral exploration and development in the Caucasus region. Financial information is reported to the CODM on at least a monthly basis. As the operations comprise a single segment, amounts disclosed in the consolidated financial statements also represent segment amounts.

## **4. ADOPTION OF NEW AND REVISED ACCOUNTING STANDARDS**

### **Standards and interpretations effective in the current period**

The accounting policies adopted, other than policies associated with changes in circumstances, are consistent with those of the previous financial year.

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### Amendments to IFRS 11 Joint Arrangements

These amendments provide guidance on the accounting for acquisitions of interests in joint operations constituting a business. The amendments require all such transactions to be accounted for using the principles on business combinations accounting in IFRS 3 'Business Combinations' and other IFRS standards except where those principles conflict with IFRS 11. Acquisitions of interests in joint ventures are not impacted by this new guidance.

The amendments are effective for reporting periods beginning on or after January 1, 2016 and didn't have a material impact on the consolidated financial statements.

### **Standards and interpretations issued but not yet adopted**

Management anticipates that those standards and interpretations deemed applicable to the Company's business will be adopted in the Company's financial statements of future periods as they become effective and that the adoption will have no material impact on the financial statements of the Company in the periods of initial application other than for additional disclosures. Those which management currently believes are or will be applicable are as follows:

IFRS 9, *Financial Instruments* – The IASB published IFRS 9 in July 2014, effective for annual periods beginning on or after January 1, 2018. IFRS 9 replaces IAS 39, *Financial Instruments: Recognition and Measurement*, and includes a logical model for classification and measurement, a single, forward-looking 'expected loss' impairment model, and a substantially reformed approach to hedge accounting. The treatment of financial liabilities was little changed relative to IAS 39. Management has not yet assessed the impact of IFRS 9 on the consolidated financial statements.

IFRS 15, *Revenue from Contracts with Customers* – The IASB published IFRS 15 in July 2014, effective for annual periods beginning on or after January 1, 2018. IFRS 15 presents new requirements for the recognition of revenue, replacing IAS 18 'Revenue', IAS 11 'Construction Contracts', and several revenue-related Interpretations. The new standard establishes a control-based revenue recognition model and provides additional guidance in many areas not covered in detail under existing IFRSs, including how to account for arrangements with multiple performance obligations, variable pricing, customer refund rights, supplier repurchase options, and other common complexities. Management has not yet assessed the impact of IFRS 15 on the consolidated financial statements.

IFRS 16, *Leases* – The IASB published IFRS 16 in January 13, 2016 effective for annual periods beginning on or after January 1, 2019, though a company can choose to apply IFRS 16 before that date but only in conjunction with IFRS 15 *Revenue from Contracts with Customers*. The standard establishes the principles that an entity should use to determine the recognition, measurement, presentation and disclosure of leases for both parties to a contract, i.e. the customer ('lessee') and the supplier ('lessor'). IFRS 16 replaces the previous leases Standard, IAS 17, *Leases*, and related Interpretations. The Company is currently assessing the impact of this standard.

## 5. RESTRICTED CASH

As of December 31, 2016, the company held certain cash amounts, advanced under a credit agreement, that are required to be used to acquire equipment for Amulsar. Such cash amounts are restricted until expenditures are required to purchase equipment acceptable to the lender.

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### 6. OTHER CURRENT ASSETS

	As of	
	December 31, 2016	December 31, 2015
Supplies	\$ 252,137	\$ 128,366
Refundable VAT	50,553	58,638
Deposits	93,639	110,467
Prepayments and other receivables	662,099	220,541
	<u>\$ 1,058,428</u>	<u>\$ 518,012</u>

### 7. MINERAL PROPERTY, PLANT AND EQUIPMENT, NET

	Exploration and Evaluation Assets	Development Assets	Plant and Equipment	Total
<b>Cost</b>				
As of January 1, 2015	\$ 58,921,727	\$ -	\$ 4,558,990	\$ 63,480,717
Additions	9,584,651	-	3,965,316	13,549,967
Disposals	(18,182)	-	(16,302)	(34,484)
Foreign exchange differences	(1,291,045)	-	(81,109)	(1,372,154)
As of December 31, 2015	<u>\$ 67,197,151</u>	<u>\$ -</u>	<u>\$ 8,426,895</u>	<u>\$ 75,624,046</u>
Additions	3,943,314	32,306,484	2,812,726	39,062,524
Re-class to Development Assets	(71,653,671)	76,453,825	(4,800,154)	-
Impairment / Disposals	(482,214)	-	(249,161)	(731,375)
Foreign exchange differences	995,420	82,725	116,367	1,194,512
As of December 31, 2016	<u>\$ -</u>	<u>\$ 108,843,034</u>	<u>\$ 6,306,673</u>	<u>\$ 115,149,707</u>
<b>Accumulated Depreciation</b>				
As of January 1, 2015	\$ -	\$ -	\$ 2,125,661	\$ 2,125,661
Additions	-	-	797,902	797,902
Disposals	-	-	(5,938)	(5,938)
Foreign exchange differences	-	-	782	782
As of December 31, 2015	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 2,918,407</u>	<u>\$ 2,918,407</u>
Additions	-	-	774,078	774,078
Disposals	-	-	(220,754)	(220,754)
Foreign exchange differences	-	-	29,912	29,912
As of December 31, 2016	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 3,501,643</u>	<u>\$ 3,501,643</u>
<b>Carrying Amount</b>				
As of December 31, 2015	<u>\$ 67,197,151</u>	<u>\$ -</u>	<u>\$ 5,508,488</u>	<u>\$ 72,705,639</u>
As of December 31, 2016	<u>\$ -</u>	<u>\$ 108,843,034</u>	<u>\$ 2,805,030</u>	<u>\$ 111,648,064</u>

Amulsar entered the development phase effective May 26, 2016 when conditions for its financing were met and the Company made a formal construction decision. As a result, previously capitalized exploration and evaluation assets of \$71,653,671 were reclassified to development assets. In the period between May 26, 2016 and December 31, 2016, development costs were incurred at Amulsar for project planning, detailed engineering and design, expanding its

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owner's team, equipment reviews, construction management, contracting, environmental and social activities, permitting, land and equipment rentals, as well as advances to vendors for construction in progress, and other related expenditures. Certain amounts, including the acquisition of surface rights, have been reclassified from property plant and equipment to development assets to conform to current year presentation.

The table below summarizes non-cash additions to exploration and development assets.

	As of	
	<u>December 31, 2016</u>	<u>December 31, 2015</u>
Interest	\$ 5,281,231	\$ 323,311
Depreciation	715,736	719,150
Rehabilitation obligation	107,028	-
Share based compensation	150,126	-
	<u>\$ 6,254,121</u>	<u>\$ 1,042,461</u>

Capitalized interest for the years ended December 31, 2016 and 2015, totaled \$5,483,585 and \$323,311, respectively.

### 8. DEFERRED FINANCING COSTS

	<u>Financing Costs</u>
As of January 1, 2015	\$ -
Additions	2,538,164
As of December 31, 2015	<u>\$ 2,538,164</u>
Additions	26,273,001
Reclassified to equity	(6,229,295)
Reclassified to stream liability	(3,386,490)
Write-offs	(240,799)
As of December 31, 2016	<u>\$ 18,954,581</u>

Additions to financing costs in 2016 include \$17.6 million of non-cash items related to the derivatives discussed in Note 12.

### 9. OTHER NON-CURRENT ASSETS

	As of	
	<u>December 31, 2016</u>	<u>December 31, 2015</u>
Refundable VAT	\$ 4,277,543	\$ 3,453,125
Rehabilitation and monitoring prepayment	955,495	180,217
Prepaid rent	718,981	-
	<u>\$ 5,952,019</u>	<u>\$ 3,633,342</u>

Input VAT will be refunded by the tax authorities or offset with other tax liabilities through future exports of products.

According to the updated mining agreement signed with the Armenian Government, Lydian Armenia is required to make payments to the Armenian Government for the amount of determined rehabilitation costs as a guarantee for post-mine rehabilitation. A first installment was paid during December 2014 and the second installment in December 2016, the remainder will be paid in 12 equal annual installments throughout the mine life. The prepayment for rehabilitation will be refunded to the Company after mine closure when rehabilitation is completed and accepted by the

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Armenian Government. The prepayments for rehabilitation totaled \$841,000. Lydian Armenia is also required to pay advances for post mining monitoring to be undertaken by the government. The prepayments for monitoring totaled \$114,495.

### 10. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

	As of	
	December 31, 2016	December 31, 2015
Accounts payable and accrued liabilities	\$ 4,753,606	\$ 1,876,332
Wage accruals	1,151,377	134,005
	<u>\$ 5,904,983</u>	<u>\$ 2,010,337</u>

### 11. FINANCING ARRANGEMENTS

On November 30, 2015, the Company entered into definitive financing agreements ("Agreements") with Orion Mine Finance ("Orion") and Resource Capital Funds ("RCF") to provide up to \$325 million in construction financing for Amulsar.

The Agreements include:

- \$60 million gold and silver purchase and sale agreement ("Stream Agreement");
- Credit agreement consisting of:
  - i) \$160 million term loan ("Term Loan"); and
  - ii) \$14 million cost overrun facility ("COF"), as amended;
- \$80 million equity private placements ("Private Placements"); and
- Gold-sales offtake agreement ("Offtake Agreement");

The Stream Agreement, Term Loan and COF shall be accounted for as liabilities and as discussed in this note and Note 12, Financial Instruments. Derivative financial instruments resulting from the Agreements are discussed in Note 12, Financial Instruments. The Private Placements are discussed in Note 14, Share Capital.

#### Key provisions of the Stream Agreement:

- \$60 million advanced in two deposits.
- Delivery obligations of 6.75% of gold production up to 2.1 million refined ounces and 100% of silver production up to 0.7 million refined ounces.
- Payment upon delivery to be the lower of prevailing market prices or \$400/oz for gold and \$4/oz for silver, each subject to escalation.
- The Company may elect to reduce metal deliveries by 50% on either the second or the third anniversaries of achieving commercial production by making a payment of \$55 million or \$50 million, respectively.
- Expiration is the earlier of the date (i) the aggregate stated gold and silver quantities have been delivered or (ii) 40 years.
- Security includes, among other things: guarantees of the Company and its subsidiaries, share pledges, and a mortgage over the assets and rights of the Company's Armenian operating subsidiary, Lydian Armenia.

The initial \$25 million deposit under the Stream Agreement was received in December 2015. At that time, the Agreements were subject to certain conditions that limited availability of additional funding under the Agreements. As such, the Company accounted for this initial advance as a current liability. Upon satisfaction of the conditions in May 2016, management derecognized the advance and replaced it with the non-current stream liability. On September 30,

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2016, the Company received the second deposit under the Stream Agreement in the amount of \$35 million for a total of \$60 million.

The effective interest rate on the stream liability is estimated at 14.7%. The difference between the derecognition and replacement values was credited to financing costs.

In addition to the stream liability, the provisions of the Stream Agreement contain the following derivatives:

- The Company's option to reduce metal deliveries by 50% represents a derivative asset ("Stream Prepayment Option"); and
- Gold and silver prices relative to the contractual prices payable upon delivery give rise to a derivative asset or liability ("Stream Commodity Linked Repayment").

See Note 12, Financial Instruments, for additional information relating to these derivative financial instruments.

### Key provisions of the Term Loan:

- \$160 million to be advanced in two tranches.
- Interest based on the 3-month US dollar LIBOR rate, subject to a minimum of 1%, plus a 6.5% margin.
- Principal (including capitalized interest) will be paid through quarterly scheduled installments and a 30% cash sweep of excess cash flow beginning June 30, 2018 and continuing through maturity on September 30, 2021.
- Orion and RCF received an aggregate of 5 million ordinary share purchase warrants ("Loan Fee – Warrants") on May 26, 2016. The warrants have a three-year term and a strike price of C\$0.39 per share.
- Security will be identical to security for the Stream Agreement, and will rank pari passu with the security for the stream obligation.

On October 21, 2016, the Company entered into an amendment to the Term Loan. The amendment, among other things, aligns the availability periods under the Term Loan with the Amulsar cash flow requirements. The initial \$50 million tranche has been extended to June 30, 2017 and the second \$110 million tranche has been extended to March 31, 2018. Funding under each tranche of the term loan is subject to applicable conditions precedent, including satisfaction of the conditions of the initial tranche by December 31, 2016. The Company met or received waivers for all conditions precedent at December 31, 2016.

No amounts were advanced under the Term Loan as of December 31, 2016.

### Key provisions of the COF:

- Availability of \$25 million, less 50% of the oversubscription amount of the public offering. The COF was amended to \$14 million in October 2016.
- Interest based on the 3-month US dollar LIBOR rate, subject to a minimum of 1%, plus a 9.5% margin.
- A cash sweep of 30% of excess cash flow will be used to repay the COF. Any remaining balance will be due in full on September 30, 2020.
- If the COF is drawn, Orion and RCF will receive an aggregate of 5 million ordinary share purchase warrants. If issued, the warrants will have a three-year term and strike price equal to 130% of the volume weighted average closing price of the Company's ordinary shares during the 20 business days preceding initial drawdown of the COF.
- Security provided to secure the Term Loan will also secure the obligations under the COF.

No amounts were advanced under the COF as of December 31, 2016. The warrants associated with the COF will represent a financial instrument. These warrants have not been issued as of December 31, 2016.

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#### Key provisions of the Offtake Agreement:

- Applies to 100% of gold production up to 2.1 million refined ounces less gold ounces deliverable under the Stream Agreement.
- Payment for refined gold shall be based on prevailing market prices during a three to six day quotational period following each delivery
- The quotational period may be reduced subject to the fulfillment of certain milestones. The COF was amended in Q1 2017 to reflect a one-day reduction in the Company's opportunity to shorten the quotational period.

No deliveries were made under the Offtake Agreement during the twelve months ended December 31, 2016. The offtake agreement is an executory contract with an embedded gold-price derivative associated with the quotational period, ("Offtake Agreement Derivative"). See Note 12, Financial Instruments, for additional information.

#### Ameriabank Credit Facility with Lydian Armenia:

On November 22, 2016, the Company, through its wholly owned Armenian operating subsidiary, entered into a \$24 million secured credit facility with Ameriabank CJSC ("Ameriabank Credit Facility"). Proceeds from the secured credit facility will be used for equipment purchases at the Amulsar project in Armenia.

- Maximum principal amount of \$24 million, available in multiple tranches, no minimum or maximum amount with each tranche payable over a 10-year period from date of advance.
- Proceeds will be used for equipment purchases.
- Security consists of specific equipment financed by Ameriabank.
- Initial principal grace period of one year.
- Interest at Libor plus 8.75%, commitment fee of 2% on undrawn portion of the facility.
- Unsecured guarantee is provided by Lydian.
- Advances are subject to satisfaction of certain conditions.
- Payments are due quarterly beginning 2018 through 2026.

The Company received an initial loan advance of \$10 million in December 2016.

#### Caterpillar Credit Facility with Lydian Armenia:

On December 28, 2016, the Company, through its wholly owned Armenian operating subsidiary, entered into a secured credit facility with Caterpillar Financial Services:

- Maximum principal amount of \$42 million.
- Proceeds will be used for Caterpillar mining equipment.
- Drawn in multiple advances through June 2018, each advance is repayable over a 75-month term, inclusive of a six-month initial repayment grace period.
- Interest rate of Libor plus 4.5%.
- Security consists of specific equipment financed by Cat Financial.
- Unsecured guarantee is provided by Lydian.
- Advances are subject to satisfaction of certain conditions.

The Company has not drawn funds from the Caterpillar Credit Facility as of December 31, 2016.

The table below summarizes activity of the financing arrangements for the year ended December 31, 2016:



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	Advances Under Stream Agreement	Stream Liability	Term Loan	Equipment Financing	Total
As of January 1, 2015	\$ -	\$ -	\$ -	\$ -	\$ -
Advances under stream agreement	25,000,000	-	-	-	25,000,000
Financing costs	(397,723)	-	-	-	(397,723)
Accrued interest	323,311	-	-	-	323,311
As of December 31, 2015	\$ 24,925,588	\$ -	\$ -	\$ -	\$ 24,925,588
Accrued interest	1,670,861	-	-	-	1,670,861
Subtotal	\$ 26,596,449	\$ -	\$ -	\$ -	\$ 26,596,449
Derecognition/replacement	(26,596,449)	23,452,086	-	-	(3,144,363)
Debt additions	-	35,000,000	981,333	10,000,000	45,981,333
Financing costs	-	(1,793,759)	-	-	(1,793,759)
Accrued interest	-	3,610,370	-	-	3,610,370
As of December 31, 2016	\$ -	\$ 60,268,697	\$ 981,333	\$ 10,000,000	\$ 71,250,030

See Note 25, Subsequent Events, for equipment financing arrangements completed after December 31, 2016.

## 12. FINANCIAL INSTRUMENTS

The Company recognized certain financial instruments relating to the Agreements, including the advance under streaming agreement, streaming liability, and derivatives discussed in Note 11, Financing Arrangements. None of these financial instruments are held for trading, and the Company does not currently engage in hedge activities. The Agreements were executed in contemplation of one another and the cash flows and embedded derivatives were fair valued in consideration of all the agreements in combination to determine an effective yield on the date the agreements were considered effective.

The advance under streaming agreement was initially recorded at fair value and replaced with the fair value of the stream liability on May 26, 2016. Thereafter, the stream liability was carried at amortized cost using the effective interest method. Debt is initially recorded at fair value and subsequently carried at amortized cost. The table below sets out the fair value hierarchy levels, carrying values, and fair values of these financial instruments as of:

	Fair Value Hierarchy Level <sup>1</sup>	December 31, 2016		December 31, 2015	
		Carrying Value	Fair Value	Carrying Value	Fair Value
Financial Liabilities:					
Advances under streaming agreement, net	2	\$ -	\$ -	\$ 24,925,588	\$ 25,000,000
Stream liability	3	\$ 60,268,697	\$ 61,289,251	\$ -	\$ -
Debt	2	\$ 10,981,333	\$ 10,981,333	\$ -	\$ -

Derivatives associated with the Agreements are measured at fair value on a recurring basis. As such, carrying values are adjusted to fair value as of the end of each reporting period. The table below sets out the fair value hierarchy levels, carrying values, and fair values of these financial instruments as of:

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	Fair Value Hierarchy Level <sup>1</sup>	December 31, 2016		December 31, 2015	
		Carrying Value	Fair Value	Carrying Value	Fair Value
<b>Derivative Assets:</b>					
Stream Prepayment Option	3	\$ 1,308,160	\$ 1,308,160	\$ -	\$ -
Stream Commodity Linked Repayment	3	\$ 6,283,628	\$ 6,283,628		
Total Derivative Assets		<u>\$ 7,591,788</u>	<u>\$ 7,591,788</u>	<u>\$ -</u>	<u>\$ -</u>
<b>Derivative Liabilities:</b>					
Offtake Agreement Derivative	3	\$21,177,962	\$21,177,962	\$ -	\$ -
Warrants, Loan Fee	2	\$ 511,551	\$ 511,551	\$ -	\$ -
Warrants, Public Offering	2	\$ 4,261,451	\$ 4,261,451	\$ -	\$ -
Total Derivative Liabilities		<u>\$25,950,964</u>	<u>\$25,950,964</u>	<u>\$ -</u>	<u>\$ -</u>

<sup>1</sup> The levels of the fair value hierarchy are defined as:

- Level 1 – Unadjusted quoted prices in active markets for identical assets or liabilities;
- Level 2 – Inputs other than quoted prices that are observable, directly or indirectly; and
- Level 3 – Inputs that are not based on observable market data.

The following table presents the carrying value of the derivatives and gains and losses recognized:

Summary of Derivatives	Derivative Assets (Liabilities)				Gain (Loss)
	Stream Prepayment Option	Offtake Agreement	Stream Commodity Linked Repayment	Warrants	
Fair value at May 26, 2016	\$ 3,068,790	\$ (21,921,971)	\$ -	\$ (9,359,928)	
Change in fair value	(1,760,630)	744,009	6,283,628	4,586,926	9,853,933
Fair value at December 31, 2016	<u>\$ 1,308,160</u>	<u>\$ (21,177,962)</u>	<u>\$ 6,283,628</u>	<u>\$ (4,773,002)</u>	

Impact upon Fair Value at December 31, 2016 of:

10% change in gold price <sup>2</sup>	\$ 1,049,437	\$ (2,158,391)	\$ (9,327,073)	N/A	\$ (10,436,027)
10% change in silver price <sup>2</sup>	\$ 130,960	N/A	\$ (864,888)	N/A	\$ (733,928)
10% change in 3-month LIBOR rate <sup>2</sup>	\$ 66,236	\$ 42,446	\$ (122,489)	N/A	\$ (13,807)

<sup>2</sup> The above impacts reflect an increase in the stated variables on the resulting value of the asset and liability; the opposite would occur if the stated variables decreased.

### Fair Value Measurement

#### Level 1 Fair Value Estimates

Fair value of the advance against the Streaming Agreement and debt were initially estimated using Level 1 criteria, which was the advance amount or proceeds from debt received by the Company. Fair value is measured on a non-recurring basis, and there have been no events or conditions requiring subsequent fair value adjustments.

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### Level 2 Fair Value Estimates

Fair value of the warrants was estimated using Level 2 criteria. The Company used a Black-Scholes option pricing model to estimate the fair value of warrants. This method was applied to the Public Offering - Warrants because, in management's opinion, trading volumes were insufficient to support use of the quoted market price. The warrants issued in connection with the Term Loan ("Loan Fee - Warrants") are not trading instruments, therefore, use of a pricing model was deemed appropriate. Inputs used for calculating fair value of the warrants included:

	Public Offering - Warrants		Loan Fee - Warrants	
	December 31, 2016	May 26, 2016	December 31, 2016	May 26, 2016
Warrants outstanding	99,187,500	99,187,500	5,000,000	5,000,000
Expected remaining life in years	0.90	1.50	2.40	3.00
Expected volatility	61.6%	81.6%	78.4%	81.6%
CAD Stock price per share on valuation date	\$0.33	\$0.35	\$0.33	\$0.35
CAD Exercise price	\$0.36	\$0.36	\$0.39	\$0.39
Risk free interest rate	1.14%	0.76%	1.55%	1.03%
USD/CAD Exchange rate	0.7445	0.7640	0.7445	0.7640
Expected dividend per share	\$Nil	\$Nil	\$Nil	\$Nil

### Level 3 Fair Value Estimates

Fair value of the stream liability and derivatives other than the warrants were estimated using Level 3 criteria. The financial modeling technique applied to these estimates were more complex, require additional inputs such as estimated future production, simulated gold and silver prices, and other inputs based on non-observable market data. Key inputs for Level 3 fair value estimates included:

	December 31, 2016	May 26, 2016
Gold spot price per ounce	\$1,150.00	\$1,223.85
Silver spot price per ounce	\$15.94	\$16.46
Risk free interest rate	2.38%	1.82%
3-month LIBOR rate	0.935%	0.674%

The initial fair value of the stream liability, and of the value of the stream prepayment option, were based on a Monte Carlo Simulation of correlated spot gold, spot silver, and similar debt yields of mining companies. The other key inputs and assumptions to the valuations include the risk free interest rate, production volumes consistent with the NI 43-101, gold and silver prices consistent with forward price curves, the availability of additional financing, and the volatility of gold and silver prices over a 3-year period.

The offtake agreement was valued using an option pricing model similar to Black-Scholes. The key inputs used include the gold price and volatility.

The stream commodity linked repayment is modeled as a swap. A swap has a zero fair value at inception because the strike price is equal to the market price. As market prices change, the fair value of the stream commodity linked repayment derivative will change.

## 13. PROVISIONS

The provision for restoration and rehabilitation represents the present value of future outflow of economic benefits that will be required by the mining agreement signed between Lydian Armenia and the Armenian Government. The provision

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recognized as of December 31, 2016 relates only to the rehabilitation of Amulsar mine areas affected by exploration and development activities. The balance represents provision for rehabilitation still outstanding.

	Provisions
As of January 1, 2015	\$ 344,754
Foreign exchange differences	(6,256)
As of December 31, 2015	\$ 338,498
Additions	113,284
As of December 31, 2016	\$ 451,782

### 14. SHARE CAPITAL

Share capital consists of one class of fully paid Ordinary Shares, with no par value. The Company is authorized to issue an unlimited number of Ordinary Shares. All shares are equally eligible to receive dividends and repayment of capital and represent one vote at the Company's shareholders' meetings.

	Number	Value
Shares outstanding, January 1, 2015	152,153,926	\$ 150,199,754
Shares issued for cash, net of issuance costs	32,478,661	13,142,107
Amount attributable to expired options	-	795,990
Shares outstanding, December 31, 2015	184,632,587	\$ 164,137,851
Shares issued for cash, net of issuance costs	514,816,666	111,987,949
Amount attributable to warrants	-	(8,695,044)
Amount attributable to expired options	-	1,177,724
Shares outstanding, December 31, 2016	699,449,253	\$ 268,608,480

#### *2015 Transactions:*

On February 4, 2015, the Company completed a bought deal transaction with a syndicate of underwriters (the "2015 Offering"). The Company issued and sold 30,000,000 ordinary shares at a price C\$0.55 per ordinary share. The proceeds net of underwriter fees, were C\$15,460,660.

In connection with the 2015 Offering, IFC exercised its Pre-Emptive Right to purchase Ordinary Shares of the Company on a private placement basis, which included an aggregate of 2,478,661 Ordinary Shares at a purchase price of C\$0.55 per Share, for aggregate gross proceeds of C\$1,363,264. The private placement to IFC closed on March 25, 2015.

#### *2016 Transactions:*

##### *Public Offering:*

On March 17, 2016, the Company closed a public offering of an aggregate of 115,000,000 subscription receipts in the capital of the Company, at a price of C\$0.29. In connection with this offering, the Company issued a further 17,250,000 Subscription Receipts pursuant to the over-allotment option granted to the underwriters, which closed on March 23, 2016. Each Subscription Receipt entitled the holder thereof to receive, upon the satisfaction or waiver of the escrow release conditions without payment of additional consideration or further action, one ordinary share in the capital of the Company and three-quarters of one ordinary share purchase warrant of the of the Company. Each Warrant entitled the holder to purchase one ordinary share of the Company (each a "Warrant") at a price of C\$0.36 for a period of 18 months following their date of issuance. The gross proceeds of C\$38,352,500 (\$29,569,778) less 50% of the

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underwriters' fee of C\$1,054,694 (\$813,169), and all interest and other income thereon, were held by Computershare Trust Company of Canada until the satisfaction of the escrow release conditions.

On May 26, 2016, the Company met the escrow release conditions, and each of the Company's outstanding subscription receipts was exchanged for one Lydian ordinary share and three-quarters of one Warrant, as outlined above. An aggregate of 132,250,000 ordinary shares and 99,187,500 Warrants were issued. Gross proceeds of C\$38,352,500 were released to the Company. The Warrants began trading on the TSX under the ticker symbol "LYD.WT". The Warrants were recognized as a financial liability whereas the ordinary shares were recognized as share capital. The transfer of the estimated fair value of the Warrants from the stock proceeds to the liability is included in the table above. See Note 12 regarding Financial Instruments, inclusive of the Warrants.

### *Private Placements:*

On March 11, 2016, in connection with the Agreements (Note 11), the Company entered into subscription agreements with affiliates of RCF and Orion to effect the Private Placements at a price of C\$0.30 per ordinary share as follows: (1) \$55 million worth of ordinary shares to RCF; and (2) \$25 million worth of ordinary shares to Orion, in each case subject to the applicable exchange rate. The Private Placements closed and an aggregate of 349,066,666 ordinary shares on May 26, 2016 upon the satisfaction of the escrow release conditions under the offering. Gross proceeds of C\$104,720,000 (\$80,000,000) were released to the Company.

Concurrently with the closing of the Private Placements, the Company issued 5,000,000 Loan Fee - Warrants. Each Loan Fee - Warrant entitles the holder to purchase one ordinary share of the Company at a price of C\$0.39 for a period of 36 months from their date of issuance. These warrants were determined to be a financial liability and were recognized at fair value, with subsequent changes in fair value being recognized through profit and loss. See Note 12.

Following completion of the Private Placements, Orion's affiliate held 109,083,333 ordinary shares and 4,391,892 Loan Fee - Warrants (together representing 16.9% of the issued and outstanding ordinary shares on a partially diluted basis) and RCF's affiliate held 243,183,333 ordinary shares and 608,108 Loan Fee - Warrants (together representing 36.6% of the issued and outstanding ordinary shares on a partially diluted basis), inclusive of 3,200,000 ordinary shares held by RCF prior to the Private Placements. The 3,200,000 ordinary shares held by RCF represented 1.7% of the issued and outstanding ordinary shares prior to the Private Placements and the exchange of the Company's outstanding subscription receipts. Each subscriber also received participation rights in any future equity or equity linked offerings by the Company, and the right to nominate one director so long as equity ownership remains above 10% and a second director so long as equity ownership exceeds 20%.

On August 15, 2016, the Company entered into a Subscription Agreement with the European Bank for Reconstruction and Development (the "EBRD Private Placement") for the purchase of ordinary shares of the Company. The Company issued an aggregate of 33,500,000 ordinary shares at a price of C\$0.34 (\$0.26) per share, for aggregate gross proceeds of C\$11,390,000 (\$8,803,048). Share issuance costs of \$129,315 were recorded.

### *Warrants:*

Warrants outstanding include:

	Number of Warrants	Weighted Average Exercise Price (CAD)	Weighted Average Remaining Life (Yrs.)
Balance as of December 31, 2015	-	\$0.00	-
Warrants granted	104,187,500	\$0.36	0.98
Balance as of December 31, 2016	104,187,500	\$0.36	0.98

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### 15. SHARE-BASED COMPENSATION

#### *Stock Option Plan:*

The Company's employee share option plan grants options to employees, directors and service providers of the Company to purchase Ordinary Shares of the Company. In accordance with terms of the employee share option plan, the exercise price of the granted options shall be determined at the time the option is granted provided that such price shall be not less than the market price of the Ordinary Shares. Share options granted under the plan carry no rights to dividends and no voting rights.

Each of the Company's share options is convertible into one ordinary share of the Company. Share options may be exercised at any time from the date of vesting to the date of their expiry.

Charges in relation to equity settled share-based compensation are credited to an "Employee share option plan reserve", therefore no liabilities have been recorded in respect of these plans.

The following summarizes the outstanding share options granted under the employee share option plan:

	<u>Number of Options</u>	<u>Weighted Average Exercise Price</u>
Balance as of January 1, 2015	5,650,000	\$ 1.15
Granted	2,480,000	0.43
Expired	<u>(1,230,000)</u>	0.78
As of December 31, 2015	6,900,000	\$ 0.74
Granted	240,000	0.28
Expired	<u>(1,380,000)</u>	1.32
As of December 31, 2016	<u>5,760,000</u>	<u>\$ 0.68</u>

Options were priced using the Black-Scholes Option Pricing Model using the following assumptions:

	<u>2016</u>	<u>2015</u>
Expected volatility	77%	74% - 75%
Expected option life	5 years	5 years
Risk free rate	.72%	.59%
Dividend yield	0%	0%
Forfeiture rate	0%	0%

During the year ended December 31, 2016, \$229,018 (2015: \$614,645) was included in employee benefits expense in the consolidated income statement.

The share options outstanding and exercisable as of December 31, 2016 had a weighted average remaining contractual life of 2.65 years (2015: 2.79 years).

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Range of exercise price	Outstanding options			Exercisable options		
	Number outstanding	Weighted average remaining life (years)	Weighted average exercise price	Number exercisable	Weighted average remaining life (years)	Weighted average exercise price
\$0 to \$.74 (CAD\$0-\$1.00)	3,470,000	3.15	\$ 0.46	1,990,003	3.03	\$ 0.51
\$.74 to \$1.48 (CAD\$1.01-\$2.00)	2,290,000	2.31	\$ 0.84	2,290,000	2.31	\$ 0.84
	5,760,000	2.81	\$ 0.68	4,280,003	2.65	\$ 0.68

### Restricted Stock Unit Plan:

On June 23, 2016 the shareholders approved the Company's RSU Plan. Under the RSU Plan, awards can be either cash or equity settled upon vesting at the discretion of the Board of Directors. As the Company does not have a present obligation to settle in cash, the awards were treated as equity-settled instruments and measured at fair value at the date of grant and recorded in equity. The associated compensation cost is recorded in share-based compensation expense unless directly attributable to development assets.

The following table summarizes the outstanding restricted share units granted under the employee RSU Plan for the year ended December 31, 2016.

	Number of RSU's	Weighted Average Award Price
Balance as of December 31, 2015	-	\$ -
Granted	6,078,400	0.30
Expired	(649,428)	0.30
Balance as of December 31, 2016	5,428,972	\$ 0.30

## 16. EMPLOYEE SALARIES AND BENEFITS EXPENSE

	For the year ended December 31,	
	2016	2015
Salaries and other compensation	\$ 3,057,511	\$ 2,479,385
Share-based compensation	747,506	614,645
	<u>\$ 3,805,017</u>	<u>\$ 3,094,030</u>

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### 17. GENERAL AND ADMINISTRATIVE EXPENSE

	For the year ended December 31,	
	2016	2015
Travel	\$ 687,171	\$ 812,565
Professional fees	1,532,355	835,779
Office operating	212,935	314,709
Community development	40,922	247,708
Insurance	155,104	145,998
Investor and public relations	299,636	166,580
Consulting and contractors	132,816	124,653
Contributions	27,010	83,714
Other	111,561	220,896
	<u>\$ 3,199,510</u>	<u>\$ 2,952,602</u>

Certain of the above amounts have been reclassified to conform to current year presentation.

### 18. OTHER EXPENSES, NET

	For the year ended December 31,	
	2016	2015
Foreign currency loss	\$ 227,092	\$ 241,173
Loss on disposal of equipment	-	20,638
Other losses, net	629,070	55,078
	<u>\$ 856,162</u>	<u>\$ 316,889</u>

### 19. INCOME TAXES

There were no income taxes payable by the Company for the year ended December 31, 2016 and the corresponding period in 2015.

	For the year ended December 31,	
	2016	2015
Accounting income (loss) for the year	\$ 2,262,659	\$ (6,413,372)
Statutory tax rate	20%	20%
Income tax payable (recoverable) based on above rates	\$ 452,532	\$ (1,282,674)
Items which are not deductible for tax purposes	(472,789)	942,544
Difference in foreign tax rates	221,563	(260,105)
Temporary differences	193,424	-
Losses (income) not recognized	(12,528)	600,235
Utilization of net operating loss carryforwards	(382,202)	-
Income tax expense (benefit)	<u>\$ -</u>	<u>\$ -</u>

The Company had tax losses under the jurisdiction of Armenia, US and Georgia as of December 31, 2016 amounting to approximately \$5,954,376 (2015: \$7,814,889) that have not been recognized, as there is insufficient evidence of future



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taxable profits at this time. Losses incurred in Jersey (Channel Islands) are considered not deductible for tax calculation purposes. Tax losses incurred by Armenian companies expire in the fifth year after they are incurred. Tax losses in Georgia have expired due to legislative changes and tax losses in the US expire after seven years.

The tax rate is 20% in Armenia, 40% in the US and 15% in Georgia. The effective tax rate for these consolidated financial statements is considered to be 20%.

### 20. NET LOSS PER SHARE

	For the year ended December 31,	
	2016	2015
Net income (loss)	\$ 2,262,659	\$ (6,413,372)
Weighted average shares outstanding	484,677,883	181,274,425
Net income (loss) per share - basic	\$ 0.00	\$ (0.04)
Net income (loss) per share - fully diluted	\$ 0.00	N/A

### 21. FINANCIAL RISK MANAGEMENT

As of December 31, 2016, the Company's financial instruments consist of cash and cash equivalents, restricted cash, other receivables, the rehabilitation prepayment, accounts payable, accrued liabilities, debt and derivative contracts. The Company estimates that the fair values of these items approximate their carrying values at December 31, 2016.

The Company manages its exposure to financial risks by operating in a manner that minimizes its exposure to the extent practical. The main financial risks affecting the Company are discussed below.

#### Capital management

The Amulsar Gold Project is in the development stage, as such, the Company is dependent on external financing to fund its activities. The Company manages its capital structure and adjusts it based on changes in economic conditions and the risk characteristics of the underlying assets. To maintain or adjust the capital structure, the Company may attempt to issue new shares, incur, repay or restructure debt, and acquire or dispose of assets to facilitate the management of its capital requirements. The Company prepares annual expenditure budgets that are updated as necessary depending upon various factors, including successful capital deployment and general industry conditions. The annual and updated budgets are approved by the Board of Directors. The Board of Directors does not establish quantitative return on capital criteria for management, but rather relies on the expertise of the Company's management to sustain future development of the business.

Capital is comprised of the aggregate of total equity attributable to owners, accounts payable and accrued liabilities, stream liability and debt. As of December 31, 2016, the Company's share capital was \$187,920,729 (2015: \$80,674,547), it had accounts payable and accrued liabilities of \$5,904,893 (2015: \$2,010,337), a stream liability and debt, net of unamortized debt issuance costs of \$71,250,030 (2015: \$24,925,588).

The capital required for the development of the Amulsar Gold Project was raised through the issuance of common shares and associated warrants, deposits received in connection with the stream liability, and proceeds from debt. The net proceeds raised are used to advance the development of the Amulsar Gold Project and provide sufficient working capital to meet the Company's ongoing obligations. Access to available funds are subject to satisfaction or waiver of certain conditions.

During 2016, the Company issued 514,816,666 Ordinary Shares for net proceeds of \$111,987,949, 99,187,500 Public Offering Warrants for no additional net proceeds at the time of issuance, but with an exercise price of CAD \$0.36, and

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5,000,000 Loan Fee Warrants for no additional net proceeds at the time of issuance but with an exercise price of CAD \$0.39, as discussed in Note 14. As of December 31, 2016, the Company's share price was CAD \$0.33.

The Company has entered into debt arrangements as discussed in Notes 11 and 25. Should the Company need additional funds for the completion of the Amulsar Gold Project, the Company may be able to issue additional shares, negotiate additional funding from the stream or debt instruments, or incur additional debt subject to market conditions. However, the Company's Financing Agreements limit the amount of additional indebtedness. Consent of certain lenders would be required to increase a stream liability or the debt limitation.

### Financial risk management

The Company has exposure to a variety of financial risks: market risk (including currency risk, interest rate risk and commodity price risk), credit risk and liquidity risk from its use of financial instruments. This note presents information about the Company's exposure to each of these risks, the Company's objectives, policies and processes for measuring and managing risk.

The Board of Directors has overall responsibility for the establishment and oversight of the Company's risk management framework. The Company manages its exposure to financial risks by operating in a manner that minimizes its exposure to the extent practical. The main financial risks affecting the Company are discussed below.

#### (a) Market risk

Market risk is the risk that changes in market factors, such as foreign exchange rates, interest rates or commodity prices, will affect the value of the Company's financial instruments.

##### *(i) Currency Risk*

Currency risk is the risk that the fair value of, or future cash flows from, the Company's financial instruments will fluctuate because of changes in foreign exchange rates. The Company's functional currency is the United States dollar and its primary operations are in Armenia.

The Company's net assets and liabilities are predominately held in US dollars, Armenian drams, Canadian dollars and the Euro. The sensitivity analysis below indicates an influence on net income where the US dollar strengthens 10% against the relevant currency, resulting in a loss of foreign currency exchange. If the US dollar weakens, an opposite impact on net income would be realized.

	For the year ended December 31,	
	2016	2015
Armenian dram	\$ (363,689)	\$ (6,942,611)
Canadian dollar	(1,347,321)	(95,185)
Euro	(384,098)	-
	<u>\$ (2,095,108)</u>	<u>\$ (7,037,796)</u>

The Company's currency risk policy is to hold funds primarily in the US Dollar, with funds held in the Armenian dram, the Canadian Dollar and the Euro roughly in proportion to expected future expenditure over the next quarter.

##### *(ii) Interest rate risk*

Interest rate risk is the impact that changes in interest rates could have on the Company's earnings and assets. The Company's exposure to interest rate fluctuations is due primarily to its long-term debt, which have interest rates based on LIBOR. The Company has not entered into any agreements to hedge against unfavorable changes in the LIBOR rate. Currently the Company's interest rate risk exposure is limited to the Ameriabank Credit Facility. The Company evaluates, on an ongoing basis, opportunities to hedge its interest rate exposure on long-term debt.

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Advances from the Term Loan bear interest at LIBOR plus 6.5% (subject to a minimum of 1%) and advances from Ameriabank Credit Facility bear interest at LIBOR plus 8.75%. Advances under the ING Credit Facility bear interest at LIBOR plus 2.85% and advances under the Cat Credit Facility bear interest at LIBOR plus 4.5%.

The Company deposits cash into fully liquid bank business accounts. As such, the Company does not consider its interest rate risk exposure to be significant as of December 31, 2016 with respect to its cash and cash equivalent and restricted cash positions.

Sensitivity to a 1% point change in interest rates with all other variables held constant as at December 31, 2016, would affect the Consolidated Statements of Profit and Loss and Comprehensive Profit and Loss by a de minimus amount in both 2016 and 2015.

### *(iii) Commodity price risk*

The Company is subject to commodity price risk from fluctuations in the market prices for gold and silver. Commodity price risks are affected by many factors that are outside the Company's control including global or regional consumption patterns, the supply of and demand for metals, speculative activities, the availability and costs of metal substitutes, inflation and political and economic conditions. There is no assurance that a profitable market will exist for gold and silver produced by the Company.

The financial instruments impacted by commodity prices are the embedded derivatives related to the Stream Agreement and the Offtake Agreement. See Note 12.

As of December 31, 2016, no gold or silver ounces had been delivered under these contacts. See Note 12 for the impact of a 10% appreciation or depreciation of gold or silver prices on the embedded derivatives.

### **(b) Credit risk**

Credit risk arises when a failure by counter parties to discharge their obligations could reduce the amount of future cash inflows from financial assets on hand at the reporting date.

As the Company has no revenue or trade receivables, management considers credit risk as low. Advances are on occasion paid to major suppliers primarily relating to construction. Payment of these deposits is considered by the management on a case by case basis. The VAT receivable and rehabilitation payments are with the Republic of Armenia. The VAT will be refunded in future periods.

The below table shows the Company's balances as of December 31, 2016 and 2015:

	For the year ended December 31,	
	2016	2015
Advances to contractors	\$ 3,726,928	\$ -
VAT Receivables	4,328,096	2,596,802
Rehabilitation and monitoring prepayment	955,495	670,000
	<u>\$ 9,010,519</u>	<u>\$ 3,266,802</u>

The Company has a concentration of cash at a major Canadian bank, but management considers its credit risk on cash and cash equivalents to be limited because the counterparties are financial institutions with high credit ratings assigned by international credit rating agencies.

During the years ended December 31, 2016 and 2015, there were no material impairment provisions required for any of the financial assets. There are no material financial assets that the Company considers past due. The carrying amount of

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financial assets recorded in the consolidated financial statements represents the Company's maximum exposure to credit risk.

### (c) Liquidity risk

Liquidity risk is the risk that the Company will not have sufficient cash resources to meet its financial obligations as they come due. The Company's approach to managing liquidity is to ensure that it will have sufficient liquidity to meet liabilities when due, to the extent the Company does not believe it has sufficient liquidity to meet obligations, it will consider securing additional equity or debt funding. The Company's liquidity may be adversely affected if its access to the capital and debt markets are hindered, whether as a result of a downturn in market conditions generally, or as a result of conditions specific to the company. To date, the Company has relied on shareholder, advances under the stream, and debt funding to finance its operations and development of the Amulsar Gold Project. The Company's ability to settle borrowings and other long term liabilities when due is dependent upon future liquidity from capital sources or positive cash flows from commercial operations.

Though the Company currently has financing arrangements in place to meet its development obligations, access to these funds is subject to meeting certain conditions. There is no assurance that the Company will be able to meet the conditions at the time funds are required, therefore, liquidity risk is present until such a time as the conditions are satisfied.

The ultimate responsibility for liquidity risk rests with the Board of Directors, which has designed an appropriate risk management framework for the management of the Company's short, medium and long-term funding requirements.

The Company's cash and cash equivalents are held in fully liquid bank accounts which are available on demand by the Company.

The Company's financial obligations consist of accounts payable and accrued liabilities, the stream, debt, and a provision for restoration and rehabilitation. During 2016, the advance under stream was derecognized and replaced with the stream liability. The stream liability consists of a defined delivery obligation of ounces of gold and silver (6.75% of refined gold ounces up to an aggregate 142,454 ounces and 100% of refined silver ounces, up to an aggregate of 694,549 ounces) over an estimated ten years. See Note 11.

Maturity of the Company's financial liabilities, except for the stream, as of December 31, 2016 and 2015 are as follows:

	For the year ended December 31, 2016			
	Up to 1 year	1 to 5 years	Over 5 years	Total
Accounts payable and accrued liabilities	\$ 5,904,983	\$ -	\$ -	\$ 5,904,983
Debt and interest	777,280	10,339,067	5,356,632	16,472,979
Provisions	-	-	451,782	451,782
	<u>\$ 6,682,263</u>	<u>\$ 10,339,067</u>	<u>\$ 5,808,414</u>	<u>\$ 22,829,744</u>

	For the year ended December 31, 2015			
	Up to 1 year	1 to 5 years	Over 5 years	Total
Accounts payable and accrued liabilities	\$ 2,010,337	\$ -	\$ -	\$ 2,010,337
Advance under stream	24,925,588	-	-	24,925,588
Provisions	-	-	338,498	338,498
	<u>\$ 26,935,925</u>	<u>\$ -</u>	<u>\$ 338,498</u>	<u>\$ 27,274,423</u>

# LYDIAN INTERNATIONAL LIMITED

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Years ended December 31, 2016 and 2015

(expressed in US Dollars, unless otherwise stated)

### (d) Fair value of financial assets and liabilities

The fair value hierarchy prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). See Note 12.

## 22. RELATED PARTY TRANSACTIONS

The parent and ultimate controlling party of the Company is Lydian International Limited. No individual party had overall control of the Company during the periods being presented. Transactions between the Company and its subsidiaries, which are related parties of the Company, have been eliminated on consolidation and are not disclosed in this note. Details of transactions between the Company and other related parties are disclosed below.

Related parties include the Board of Directors, key management personnel, close family members and enterprises which are controlled by these individuals as well as certain persons performing similar functions.

The non-executive members of the Board of Directors do not have employment or service contracts with Lydian International Limited and neither are they entitled to any termination benefits. None of the directors are entitled to pension benefits.

Compensation awarded to key management for the periods indicated below was as follows:

	For the year ended December 31,	
	2016	2015
Salaries and other compensation	\$ 1,784,053	\$ 1,225,409
Share-based compensation	494,360	388,556
	<u>\$ 2,278,413</u>	<u>\$ 1,613,965</u>

## 23. COMMITMENTS

### Leases

The Company leases space for accommodations and office for administrative and operational purposes. In 2011, the Company, through Lydian Armenia, entered into long term rental contracts for lands under the rock allocation area and other areas associated with mine development. Though these operating leases are cancelable, rental obligations are listed below.

	As of December 31,	
	2016	2015
Up to one year	\$ 1,933,446	\$ 762,589
More than one year and not later than five years	5,597,388	2,677,473
More than five years	8,264,996	6,629,799
	<u>\$ 15,795,830</u>	<u>\$ 10,069,861</u>

The projected cost of the Amulsar Gold Project is \$369.9 million. In May 2016, Lydian Armenia signed an amended mining agreement with the Ministry of Energy, Infrastructure and Natural Resources of Armenia. Under the agreement, Lydian Armenia previously paid a deposit to the Armenian Government in the amount of 279.7 million Armenian Drams ("AMD") or \$589,000, as a guarantee for post-mining environmental rehabilitation and AMD38.1 million, or \$80,000, for ongoing monitoring. The amounts paid represented 15% of the contractual obligation. The remainder of the rehabilitation guarantee will be paid in equal installments of AMD121.9 million, or \$252,000, over thirteen years commencing in 2016, and the remainder of the monitoring will be paid in equal installments of AMD16.6 million, or \$34,300, over thirteen years commencing in 2016. In addition, Lydian Armenia is committed to invest annually AMD61.0

# LYDIAN INTERNATIONAL LIMITED

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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million, or \$126,300, after mine closure for workforce social mitigation and AMD61.5 million, or \$127,300, for adjacent communities' social-economic development. The rehabilitation guarantee will be refunded to the Company after mine closure when rehabilitation is completed and accepted by the Armenian Government.

As of the date of this report, the Company has entered into key supply contracts for the mining fleet, material handling systems, gold recovery plant electrical systems, and worker accommodations. The aggregate value of these contracts is \$120 million. The contracts provide for termination provisions common to the industry. The provisions generally provide payment for i) the reasonable, direct, documented costs incurred as a result of such early termination, ii) if the contract paid on a cost reimbursable basis, the amount owed for work performed to the termination date; or (iii) if the contract is on a unit price or lump sum basis, an amount that is proportionate to the number of units completed or to the percentage of the work that has been completed as of the termination date as compared to the total work that was to have been completed.

### 24. CONTINGENCIES

#### *Newmont Transaction*

On April 23, 2010, the Company purchased all of Newmont's interests in the Company's joint venture which included Newmont's interests in the Amulsar gold property. The consideration was a combination of committed and contingent payments. The committed payments included 3 million ordinary shares of the Company, which have now been issued and three payments of \$5 million, the first was paid in 2010, the second on March 13, 2012 and the third was paid on October 25, 2013. This third and final payment included an additional payment of \$409,669 representing accrued interest.

In addition, the Company agreed to pay Newmont, following the start of commercial production, a 3% Net Smelter Royalty ("NSR"). However, between April 23, 2010 and the date that is 20 days following commencement of commercial production, Lydian may, at its option, elect to buy out the 3% NSR and instead pay to Newmont the aggregate sum of \$20 million, without interest, in 20 equal quarterly installments of \$1 million commencing on the first day of the third calendar month following the start of commercial production. Furthermore, the Company has a one-time option prior to the commencement of commercial production to prepay these quarterly installments in a single cash payment using an annual discount rate of 10%. This equates to a single payment of approximately \$15.7 million.

These potential post-production payments do not meet the definition of an obligation or a constructive obligation as the triggering event, commencement of commercial production, has not occurred. These potential payments are therefore not recognized in the consolidated Statement of Financial Position as of December 31, 2016.

### 25. SUBSEQUENT EVENTS

The consolidated financial statements for the year ended December 31, 2016 have been approved for issue by the Board of Directors on March 30, 2017 and subsequent events have been reviewed through the date of approval.

On February 9, 2017, the Company entered into a secured credit facility with ING Bank N.V. ("ING Bank") for the purchase of crushing, conveying and electrical equipment for Amulsar. Key provisions of the ING Credit Facility include:

- Maximum principal amount of up to \$50 million, which can be drawn in multiple advances through April 2018;
- Each advance is repayable over a 51-month term;
- Interest rate of Libor plus 2.95%;
- Security consists of equipment to be specified and a guarantee covering 85% of principal and interest under the ING Credit Facility, which has been issued by the Swedish Export Credits Guarantee Board ("EKN"). The cost of the EKN guarantee shall be financeable using proceeds from the ING Term Facility;

## LYDIAN INTERNATIONAL LIMITED

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- Proceeds from the term facility financed by ING Bank, and guarantee covering 85% of principal and interest under the ING Term Facility has been issued by the Swedish Export Credits Guarantee Board ("EKN");
- Lydian has provided an unsecured guarantee; and
- Advances are subject to satisfaction of certain conditions.