

NORTHERN FINANCIAL CORPORATION
CONSOLIDATED FINANCIAL STATEMENTS
MARCH 31, 2006 AND 2005

June 29, 2006

To Our Shareholders

Year in Review

Our year ended March 31, 2006 ("Fiscal 2006") was a positive year for Northern Financial Corporation ("Northern" or the "Company") and its wholly owned subsidiary, Northern Securities Inc. ("Northern Securities"). At Northern we focus exclusively on small cap companies.

Our highlights in Fiscal 2006 included the growth in our Capital Markets revenue to \$9.4 million from \$7.5 million in the prior fiscal year ("Fiscal 2005"), we increased revenue in our Private Client group to \$6.4 million from \$5.1 million, and we generated merchant banking revenue of \$6.4 million.

The brokerage and investment business is about client relationships, making sure that we meet the objectives of our clients on a consistent and relentless basis. We are fortunate that we have been engaged by the same clients on multiple financings and on multiple advisory assignments. Repeat business is very important in the brokerage business.

Our mergers and acquisitions business has expanded with the addition of personnel in Fiscal 2006. We believe that we can continue to grow this business.

Our core business is the brokerage and investment banking business, and merchant banking has become an important supplementary business. In merchant banking, we invest our capital with our clients in undervalued opportunities where the market is making a serious mistake. Generally, but not always, these opportunities consist of companies that have substantial cash resources that are redundant to the business. In some cases, the public company in question has no business, only substantial cash resources.

Another major development in Fiscal 2006 was the consolidation of our shares on a 1 for 100 basis to reduce the number of shares outstanding to approximately 8.6 million. This was an important step for Northern as we take steps to move to the next level.

Fiscal 2006 was the first profitable year for Northern. This result is due to the excellent team we have at Northern and the trust our clients have placed in Northern's ability to carry out our client objectives. We are pleased to have a great team and a great client base. We aspire to grow both our team and our client base given our track record of delivering results for our clients.

On behalf of the Board of Directors, we thank our employees, clients and shareholders for their terrific support.

Vic Alboini
Chairman and Chief Executive Officer

MANAGEMENT'S DISCUSSION AND ANALYSIS

June 29, 2006

Overview

During fiscal 2006, Northern Financial Corporation (the "Company") undertook a number of initiatives to reduce certain brokerage expenses to better match revenue. From the financial results achieved, along with a strong commodities market, the initiatives undertaken were a success.

The Company's balance sheet continues to be strong with \$19,570,003 in cash, deposits, securities and long-term investments at cost, as at March 31, 2006.

Revenue

Total revenue for the year ended March 31, 2006 was \$25,730,802 compared with \$15,037,055 in the prior year; this represented an increase of 71%. The increase in revenue was a direct result of the Company engaging in merchant banking transactions that were not undertaken in the past and as a result of a strong commodities market, which allowed the Company to complete a significant number of underwritings during the year.

Looking at specific revenues for the year ended March 31, 2006 compared to the prior year, commission revenue increased by 24% to \$6,359,416 from \$5,123,074. Trading revenue increased 240% to \$2,359,786 from \$694,563. Interest revenue decreased 19% to \$1,148,436 from \$1,616,433.

Underwriting and advisory revenue increased 26% to \$9,423,377 from \$7,486,029 as a result of strong Mining and Oil and Gas sectors as well as a generally buoyant small capitalization sector where the Company concentrates its business.

Revenue of the Company is largely dependent upon the strength of the commodities market and the general condition of the financial markets. Fluctuations in the financial markets, and in particular the movement in the value of the short term and long term investments maintained by the Company, have a significant effect on the financial results of the Company.

Expenses

Total expenses for the year ended March 31, 2006, were \$25,116,388 compared with expenses of \$18,213,789 in the prior year. Brokerage operations costs increased to \$18,788,716 from \$15,486,357. The increase is attributable largely to an increase in variable compensation paid by the Company.

Interest expense decreased to \$1,028,784 from \$1,089,367; this represents a 6% decrease which is largely attributable to a partial repayment of the promissory note.

Merchant banking expense for the year ended March 31, 2006 was \$3,735,076 compared with an expense of nil in the prior year. The year ended March 31, 2006 was the first year that the Company undertook merchant banking transactions. The expense represents variable compensation.

General and administrative and depreciation and amortization expenses are consistent with the prior year.

Liquidity, Capital Resources and Cash Flows

The Company requires capital for operating and for regulatory purposes. Most of the assets reflected on the balance sheet are highly liquid. The Company's assets consist primarily of cash or assets that are readily convertible into cash. The value of securities held by the Company fluctuates with market values and may be affected by a variety of factors, such as economic and market conditions.

The Company had cash, deposits, securities and long-term investments at cost of \$19,570,003 as at March 31, 2006 compared with \$15,190,476 as at March 31, 2005. The Company generated \$436,000 of cash in its operations for the year ended March 31, 2006 compared to using \$2,091,664 last year.

The Company used cash of \$212,170 in investing activities for the year ended March 31, 2006 compared with \$6,231,089 for the year ended March 31, 2005. The decrease in cash use is attributable to fewer long term investments made by the Company in 2006.

The Company used cash from financing activities in the amount of \$515,604 for the year ended March 31, 2006 compared to generating \$7,594,601 last year. The use of cash is primarily the result of the Company making a principal repayment on the promissory note outstanding. For the year ended March 31, 2005 the Company generated cash from financing activities primarily as a result of the completion of certain private placements and a promissory note.

In the past, the Company has always been able to generate sufficient amounts of cash and cash equivalents from the issuance of common shares, debentures or promissory notes. The Company has relied upon these methods to generate cash and cash equivalents to meet current working capital requirements.

A portion of the cash of the Company is maintained by Northern Securities, the Company's wholly owned subsidiary. The Company must receive consent from Northern Securities' self-regulated organization prior to the repatriation of any cash.

The Company has never defaulted on any interest or dividend payments and currently has no amounts in arrears.

Outlined below are the contractual obligations including payments due for each of the next five years and thereafter:

Payments Due by Period

Contractual Obligations	Total	Less than 1 year	1 to 3 years	4 to 5 years	After 5 years
Long Term Debt	\$2,819,396	\$1,080,000	\$1,739,396	-	-
Operating Leases	\$1,872,000	\$1,135,000	\$613,000	\$124,000	-
Total Contractual Obligations	\$4,691,396	\$2,215,000	\$2,352,396	\$124,000	-

Annual Financial Information

	Year ended Mar. 31, 2006	Year ended Mar. 31, 2005	Year ended Mar. 31, 2004
Total revenues	\$25,730,802	\$15,037,055	\$19,030,681
Net income (loss) from operations	\$614,414	(\$3,176,734)	(\$914,725)
Net income (loss) per share	\$0.07	(\$0.45)	(\$0.19)
Long term debt	\$2,819,396	\$3,451,000	\$893,000
Total assets	\$23,972,331	\$19,684,795	\$11,688,255

Quarterly Financial Information

	Fiscal year ended March 31, 2006				Fiscal year ended March 31, 2005			
	\$				\$			
	Fourth Quarter	Third Quarter	Second Quarter	First Quarter	Fourth Quarter	Third Quarter	Second Quarter	First Quarter
Total Revenues	12,341,825	4,478,293	5,013,732	3,896,952	5,989,669	4,463,719	2,184,769	2,398,898
Net Inc. (Loss)	987,394	(113,302)	191,861	(451,539)	366,439	(835,813)	(1,700,400)	(1,006,960)
Net Inc. (Loss) per share	0.12	(0.02)	0.00	(0.05)	0.00	(0.11)	(0.27)	(0.17)

During the fourth quarter of 2006 a decision was made by management to dispose of certain long term investments of the Company. As a result of this decision, the investments were reported as current assets and carried at market value instead of their original cost, resulting in the recognition of significant merchant banking revenue.

A large portion of the Company's revenue was derived from underwriting and advisory revenue and merchant banking revenue. By nature, underwriting and advisory revenue and merchant banking revenue are not readily predictable. Underwriting and advisory revenue is reported when transactions are complete, whereas merchant banking revenue is primarily based on mark-to-market adjustments. In addition, commission revenue is generally dependent on the condition of the commodities market, which may lead to fluctuations in quarterly revenue.

Financial Instruments

The following is a description and analysis of the risks associated with financial instruments that may affect the Company:

Fair Value:

Canadian generally accepted accounting principles require that the Company disclose information about the fair value of its financial assets and liabilities. Fair value estimates are made at the balance sheet date, based on relevant market information and information about the financial instrument. These estimates are subjective in nature and involve uncertainties in significant matters of judgment and therefore cannot be determined with precision. Changes in assumptions could significantly affect these estimates.

The carrying amounts for deposit with carrying broker, securities owned, accounts receivable, prepaid expenses and deposits, taxes recoverable, accounts payable and accrued liabilities, and securities sold short on the balance sheet approximate fair value because of the limited term of these instruments. The carrying value of the debentures and notes payable are a reasonable estimate of their respective fair values due to the relative short period of time since the issuance of these financial instruments.

Risk Management:

Risk management at the Company is an integrated process with independent oversight, which requires constant communication, judgment and knowledge of specialized products and markets. The Company's senior management takes an active role in the risk management process and has developed policies and procedures that require specific administration and business functions to assist in the identification, assessment and control of various risks.

Market Risk:

Market risk is the risk that a change in market prices, interest rate levels, indices, liquidity and other market factors will result in losses. The Company is exposed to market risk as a result of its principal trading in equity securities and fixed income securities. Securities held for trading are valued at market and as such, changes in market value affect earnings (losses) as they occur. The Company mitigates its market risk exposure through controls to limit concentration levels and capital usage within its inventory trading accounts.

Credit Risk:

The Company incurs credit risk when entering into, settling and financing various proprietary and client transactions. Credit risk arises from the potential that investees, clients or counterparties fail to satisfy their obligations. Credit risk is managed by dealing with counterparties the Company believes to be creditworthy and by actively monitoring credit exposure and the financial health of the counterparties.

Interest Rate Risk:

Interest rate risk arises from the possibility that changes in interest rates will affect the value of financial instruments. The Company does not hedge its exposure to interest rate risk as it is minimal.

Foreign Exchange Risk:

Foreign exchange risk is the risk that the market value of financial instruments and the associated revenues will fluctuate due to changes in exchange rates. The Company does not use derivatives to modify the foreign exchange risk.

Share Capital Information

Outlined below is selected current share capital information related to the Company:

Description	Amount
Common shares issued and outstanding	8,583,146
Common share purchase warrants issue and outstanding	124,584
Common share purchase options issue and outstanding	142,002
Unissued vested common shares pursuant to the Employee Equity Incentive Plan	35,000

Disclosure Controls

The Company's Chief Executive Officer and Chief Financial Officer are responsible for the Company's disclosure. They are assisted in this responsibility by the Chairman of the Audit Committee who serves as an independent director of the Company.

The Chief Executive Officer and Chief Financial Officer, after evaluating the effectiveness of the Company's disclosure controls and procedures as at March 31, 2006, have concluded that the Company's disclosure controls

and procedures were adequate and effective to ensure that material information relating to the Company and its subsidiaries would have been known to them.

Management's Responsibility for Financial Statements

The information provided in this report, including the financial statements, is the responsibility of management. In the preparation of these financial statements, estimates are sometimes necessary to make a determination of future values for certain assets and liabilities. The most significant estimates are related to the valuation of broker warrants, stock-based compensation, contingent liabilities, and income tax accounts. Accordingly, actual results could differ from those estimates. Management believes such estimates have been based on careful judgment and have been properly reflected in the financial statements.

Management maintains a system of internal controls to provide reasonable assurance that the Company's assets are safeguarded and to facilitate the preparation of relevant and timely information.

Promissory Note Payable

As at March 31, 2006, the Company had a promissory note payable outstanding in the amount of \$1,739,396 (2005 – \$2,500,000). The promissory note facility entitles the Company to draw up to \$2,500,000. The promissory note payable matures on May 17, 2007, bears interest at 13%, and is secured by certain securities owned by the Company with a market value of approximately \$12,400,000, a general security agreement, covering all property of the Company, and a personal guarantee by the President of the Company. A director of the Company is also a director and officer of the trustee of the promissory note payable.

Commitments and Contingencies

The following is a summary of material commitments and contingencies of the Company:

- a) The Company has contracted Penson Financial Services Canada Ltd. ("Penson") to perform certain trading and clearing activities for clients of the Company, according to the Introducing Broker Agreement (the "Agreement") between Penson and the Company. The Company has indemnified Penson for all obligations to pay for securities purchased and to deliver securities sold by clients. In the event of default by any of its clients on payments due or delivery of securities to Penson, the Company has agreed to pay Penson an amount up to its "excess risk adjusted capital". As at March 31, 2006, the amount of the Company's excess risk adjusted capital was \$1,320,000 (2005 – \$1,306,000).
- b) The Company is party to legal proceedings in the ordinary course of its operations. Management does not expect the outcome of any of these proceedings to have a materially adverse effect on the results of the Company's financial position or operations.
 - The Company is the defendant in a number of legal actions where the plaintiffs are claiming damages totaling approximately \$550,000. The Company believes that the actions are without merit, however, it is premature to make an estimate of the potential outcome of financial impact of these actions.
 - Market Regulation Services Inc. ("RS") has commenced a regulatory proceeding against the Company and two of its officers alleging certain historical deficiencies in its supervision and compliance monitoring systems. The Company believes that the allegations are very technical and without merit. No provision for this proceeding has been made.

Litigation is subject to many uncertainties and the outcome of individual matters is not predictable. It is possible that the final resolution of these matters may require the Company to make expenditures over an extended period of time and in a range of amounts that cannot be reasonably estimated and may differ significantly from any amounts recorded in these consolidated financial statements.

- c) The future minimum annual payments for each fiscal year on equipment and office premises under existing operating leases approximate the following:

2007	\$1,135,000
2008	523,000
2009	90,000
2010	76,000
2011 and thereafter	48,000
Total	<u>\$1,872,000</u>

The Company is also responsible for its portion of property taxes and common area costs related to leases for premises.

- d) The Company has available a credit facility in the amount of \$250,000 at prime plus 1%, secured by a general security agreement covering all assets of the Company and certain guarantees provided personally by the President of the Company and a corporation controlled by the President of the Company. As at March 31, 2006, \$245,000 was owing under the credit facility.
- e) The Company has made various principal investment guarantees related to its merchant banking business. These guarantees require the Company to reimburse certain realized losses, if any, on completion of certain merchant banking transactions. As at March 31, 2005, the total guaranteed amount approximated \$1,000,000. Included in this amount is a guarantee for \$500,000 for which the underlying investment had declined in value by \$317,000. An accrual related to this guarantee of \$317,000 has been included in accounts payable and accrued liabilities. At March 31, 2006, the remaining \$500,000 of guaranteed investments had quoted market values in excess of the guaranteed amounts.

Subsequent Events

The following is a summary of events that have occurred subsequent to the Company's year end, March 31, 2006:

- a) The Company formed an investor group which acquired approximately 48% of the issued shares of Lakeside Steel Corporation ("Lakeside"). The Company invested \$400,000 in the investor group, representing approximately 13% of the \$3,000,000 paid by the investor group or 6% of Lakeside. Lakeside owns three steel pipe and tube fabricating facilities in Welland, Ontario.

Prior to the investment by the Company's investor group, Lakeside was owned 100% by Rompsen Investment Corporation ("RIC"). A director of the Company is also a director and officer of RIC and of Lakeside.

On June 8, 2006, Lakeside entered into a letter agreement to merge with Canadian Tubulars (1997) Ltd., TSI Tubular Services Inc. and 911499 Alberta Inc. (collectively referred to as "Tubulars"). The merged company will be owned 50% by the shareholders of Lakeside and 50% by the shareholders of Tubulars. This transaction will dilute the Company's interest to approximately 3%. Pursuant to the agreement with the investor group, the Company may earn a greater percentage than its equity interest on any gain on this investment.

The President of the Company has been appointed Chairman of Lakeside and will remain Chairman of the merged company. A director of the Company has been appointed President of Lakeside.

- b) On June 4, 2006, the Company entered into a letter of intent ("LOI") to acquire Energy Finance (UK) Ltd. ("EF"). EF is an investment dealer located in London, England. The acquisition is subject to a six-month trial period during which the Company may elect to complete the acquisition for consideration equal to 5% of revenues generated by EF over a three and one-half year period to a maximum £300,000 (\$609,000), subject to minimum payments of £25,000 (\$51,000) on the closing date of the acquisition, £25,000 (\$51,000) on the 12 month anniversary of the closing, £25,000 (\$51,000) on the 18 month anniversary of the closing and £25,000 (\$51,000) on the 24 month anniversary of the closing. The consideration may be paid in cash or in common shares of the Company, at the option of the Company.
- c) On June 5, 2006, the board of directors of the Company approved an employee share purchase plan ("ESPP"). The ESPP allows employees to purchase common shares of the Company equal to 5% of their annual compensation, to a maximum amount of \$5,000 per year, with the Company matching the number of shares purchased at no additional cost to the employee. The ESPP is subject to shareholder and regulatory approval. As at June 9, 2006, no grants had been made under the ESPP.



McGovern, Hurley, Cunningham, LLP
Chartered Accountants

AUDITORS' REPORT

To the Shareholders of
Northern Financial Corporation

We have audited the consolidated balance sheets of Northern Financial Corporation as at March 31, 2006 and 2005 and the consolidated statements of operations and deficit and cash flows for each of the years in the two-year period ended March 31, 2006. These consolidated financial statements are the responsibility of the Company's management. 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 plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at March 31, 2006 and 2005 and the results of its operations and its cash flows for each of the years in the two-year period ended March 31, 2006 in accordance with Canadian generally accepted accounting principles.

McGOVERN, HURLEY, CUNNINGHAM, LLP

McGovern, Hurley, Cunningham, LLP

Chartered Accountants

TORONTO, Canada
June 9, 2006

NORTHERN FINANCIAL CORPORATION
CONSOLIDATED BALANCE SHEETS
AS AT MARCH 31

	2006 \$	2005 \$
ASSETS		
CURRENT		
Cash and cash equivalents (Note 16)	3,148,744	3,440,518
Deposit with carrying broker (Note 3)	831,053	945,800
Securities owned, at market value (Note 4)	14,852,206	2,543,114
Accounts receivable	86,413	280,175
Deferred development costs (Note 8)	225,784	-
Prepaid expenses and deposits	143,570	127,845
Commodity taxes recoverable	37,514	39,323
	<u>19,325,284</u>	<u>7,376,775</u>
LONG-TERM INVESTMENTS (Note 5)	738,000	8,261,044
EQUIPMENT (Note 6)	863,311	877,194
GOODWILL (Note 7(a))	3,024,468	3,024,468
INTANGIBLE ASSETS (Note 7(b))	21,268	145,314
	<u>23,972,331</u>	<u>19,684,795</u>
LIABILITIES		
CURRENT		
Short-term loan payable (Note 13(f))	245,000	-
Debentures payable (Note 10)	1,020,000	-
Accounts payable and accrued liabilities	6,564,283	2,629,796
Deferred revenue	84,626	50,000
Securities sold short, at market value (Note 4)	22,060	148,909
	<u>7,935,969</u>	<u>2,828,705</u>
DEBENTURES PAYABLE (Note 10)	-	951,000
PROMISSORY NOTE PAYABLE (Note 9)	1,739,396	2,500,000
	<u>9,675,365</u>	<u>6,279,705</u>
TOTAL LIABILITIES		
COMMITMENTS AND CONTINGENCIES (Note 13)		
SHAREHOLDERS' EQUITY		
SHARE CAPITAL (Note 11(a))	41,648,487	41,617,237
WARRANTS (Note 11(e))	129,489	453,144
CONTRIBUTED SURPLUS (Note 11(f))	1,603,042	1,033,175
DEFICIT	<u>(29,084,052)</u>	<u>(29,698,466)</u>
	<u>14,296,966</u>	<u>13,405,090</u>
	<u>23,972,331</u>	<u>19,684,795</u>

APPROVED ON BEHALF OF THE BOARD:

Signed "Ian Bradley", Director

Signed "Vic Alboini", Director

NORTHERN FINANCIAL CORPORATION
CONSOLIDATED STATEMENTS OF OPERATIONS AND DEFICIT
 FOR THE YEARS ENDED MARCH 31

	2006 \$	2005 \$
REVENUES		
Commissions	6,359,416	5,123,074
Underwriting and advisory	9,423,377	7,486,029
Merchant banking	6,439,787	-
Trading – net	2,359,786	694,563
Interest	1,148,436	1,616,433
Other	-	116,956
Total revenues	<u>25,730,802</u>	<u>15,037,055</u>
OPERATING EXPENSES		
Brokerage operations	18,788,716	15,486,357
Merchant banking	3,735,076	-
General and administrative	1,213,713	1,249,731
Long-term debt interest expense	321,507	182,954
Other interest expense	707,277	906,413
Depreciation and amortization	350,099	388,334
Total operating expenses	<u>25,116,388</u>	<u>18,213,789</u>
Income (loss) before income taxes	614,414	(3,176,734)
Income taxes (Note 12(a))	-	-
NET INCOME (LOSS) FOR THE YEAR	<u>614,414</u>	<u>(3,176,734)</u>
REDUCTION OF STATED CAPITAL (Note 11(a)(iii))	-	45,963,275
DEFICIT , beginning of year	<u>(29,698,466)</u>	<u>(72,485,007)</u>
DEFICIT , end of year	<u>(29,084,052)</u>	<u>(29,698,466)</u>
INCOME (LOSS) PER SHARE – Basic and diluted	0.07	(0.45)
WEIGHTED AVERAGE COMMON SHARES OUTSTANDING – Basic and diluted	8,575,077	7,094,790

See accompanying notes to the consolidated financial statements.

NORTHERN FINANCIAL CORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS
 FOR THE YEARS ENDED MARCH 31

	2006 \$	2005 \$
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income (loss) for the year	614,414	(3,176,734)
Items not involving cash:		
Depreciation and amortization	350,099	388,334
Shares issued for services	-	706,667
Long-term investment impairment	335,087	
Accretion of debentures	69,000	58,000
	<u>1,368,600</u>	<u>(2,023,733)</u>
Changes in non-cash working capital balances:		
Deposit with carrying broker	114,747	56,256
Securities owned	(5,121,135)	(1,143,214)
Accounts receivable	(32,022)	262,993
Prepaid expenses and deposits	(15,725)	65,702
Income taxes	1,809	28,950
Accounts payable and accrued liabilities	4,211,949	603,924
Securities sold short	(126,849)	7,458
Deferred revenue	34,626	50,000
	<u>(932,600)</u>	<u>(67,931)</u>
Cash flows from operating activities	<u>436,000</u>	<u>(2,091,664)</u>
CASH FLOWS FROM INVESTING ACTIVITIES:		
Acquisition of equipment (net)	(198,041)	(122,669)
Acquisition of long-term investments	-	(6,108,420)
Acquisition of intangible assets	(14,129)	-
Cash flows from investing activities	<u>(212,170)</u>	<u>(6,231,089)</u>
CASH FLOWS FROM FINANCING ACTIVITIES:		
Repayment of promissory note	(760,604)	-
Increase in line of credit	245,000	-
Promissory note issued	-	2,500,000
Proceeds from exercising stock options	-	26,217
Proceeds from issuance of common stock pursuant to acquisition (Note 11(a)(vi))	-	1,027,384
Proceeds from private placements, net of issue costs	-	3,750,000
Proceeds from exercising warrants	-	291,000
Cash flows from financing activities	<u>(515,604)</u>	<u>7,594,601</u>
(Decrease) in cash and cash equivalents	(291,774)	(728,152)
Cash and cash equivalents, beginning of year	<u>3,440,518</u>	<u>4,168,670</u>
Cash and cash equivalents, end of year	<u>3,148,744</u>	<u>3,440,518</u>

SUPPLEMENTAL INFORMATION (Note 16)

See accompanying notes to the consolidated financial statements.

NORTHERN FINANCIAL CORPORATION
NOTES TO THE UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEAR ENDED MARCH 31, 2006

1. NATURE OF OPERATIONS

In 1999, Northern Financial Corporation (the "Company") acquired Northern Securities Inc. ("NSI"), a member firm of the Investment Dealers Association ("IDA"). The Company carries on a traditional brokerage business as well as a merchant banking business.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting policies of the Company are in accordance with generally accepted accounting principles in Canada and are consistent with that of the previous year. Outlined below are those policies considered particularly significant:

Principles of consolidation:

These consolidated financial statements include the accounts of the Company and all its subsidiaries. All significant intercompany accounts and balances have been eliminated upon consolidation.

Foreign currency translation:

Monetary assets and liabilities are translated at the rate of exchange prevailing at the year end; equipment and intangible assets are translated at the rates prevailing at the acquisition dates; and revenue and expenses are translated at average rates of exchange during the year, with the exception of amortization which is translated at historical exchange rates. Exchange gains and losses are included in the consolidated statement of operations and deficit.

Cash and cash equivalents:

The Company considers all highly liquid debt instruments with an original maturity date of 90 days or less to be cash equivalents. Included in cash and cash equivalents are amounts on deposit with the carrying broker that can be used in normal operations.

Securities owned and securities sold short:

Securities owned and securities sold short are stated at market values at the balance sheet date. Realized and unrealized changes in fair value are recognized in income from principal transactions in the period in which the changes occur.

Equipment:

Equipment is recorded at cost less accumulated depreciation. Depreciation is provided on a declining-balance basis at the following annual rates:

Office equipment	20%
Leasehold improvements	20%
Computer hardware	30%

Artwork is not depreciated.

Goodwill and intangible assets:

The Company has unamortized goodwill, which arose from previous acquisitions, of \$3,024,468. Goodwill is tested for impairment annually or more frequently if events or changes in circumstances indicate the asset may be impaired.

Computer software is amortized 50% in the year of acquisition and 50% in the year thereafter.

Client agreements and relationships are amortized on a straight-line basis over their estimated useful lives of three years and are tested annually for impairment.

Patents and trademarks are amortized on a straight line basis over their estimated useful lives of ten years and are tested annually for impairment.

Deferred development costs:

Deferred development costs consist of forgivable loans extended to investment advisors and capital market professionals as a hiring and retention incentive. These loans are initially recorded at their principal amount, are non-interest bearing and are forgiven on a straight-line basis over the period of the individual employment contract, which vary in length from six months to four years. The forgiven amount is recorded as an operating expense.

Long-term investments:

Long-term investments are carried at cost. If it is determined that an investment has suffered a decline in value that is other than temporary, it is written down to its estimated net realizable value.

Revenue recognition:

Customer and principal securities transactions and the applicable commissions earned from these transactions are recorded on a trade-date basis. Underwriting and advisory revenues are recorded at the time the transaction or service is completed and the related income is reasonably determinable. Securities owned and sold short which are freely tradable are recorded at market value and any unrealized gains and losses are included in earnings. Market value is based on quoted market prices and includes the Company's participation in merchant banking transactions.

Use of estimates:

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of

NORTHERN FINANCIAL CORPORATION
NOTES TO THE UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS
 FOR THE YEAR ENDED MARCH 31, 2006

contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the year. The most significant estimates are related to the valuation of broker warrants, stock-based compensation, contingent liabilities, and income tax accounts. Accordingly, actual results could differ from those estimates. Management believes that the estimates are reasonable.

Leases:

Leases have been classified as either capital or operating. A lease which transfers substantially all of the benefits and risks incidental to the ownership of property is accounted for as if it were an acquisition of an asset and the incurrence of an obligation at the inception of the lease. All other leases are accounted for as operating leases wherein rental payments are charged to operations as incurred. Assets recorded under the capital leases are amortized on a declining balance basis over their estimated useful lives.

Stock-based compensation plan:

The Company records as compensation all stock-based awards made to non-employees and employees at fair value. Any consideration paid on exercise of stock options is credited to capital stock. The Company's stock-based compensation plans are described further in Notes 11(c) and (d).

Income taxes:

The Company accounts for and measures future tax assets and liabilities in accordance with the liability method. Under this method, future tax assets and liabilities are recognized for future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Future tax assets and liabilities are measured using enacted or substantively enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on future tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the date of enactment or substantive enactment of the change. When the future realization of income tax assets does not meet the test of being more likely than not to occur, a valuation allowance in the amount of the potential future benefit is taken and no net asset is recognized.

Income (loss) per share:

Basic income (loss) per share is calculated using the weighted average number of shares outstanding. Diluted income (loss) per share is calculated using the treasury stock method. In order to determine diluted income (loss) per share, the treasury stock method assumes that any proceeds from the exercise of dilutive stock options and warrants would be used to repurchase common shares at the average market price during the period, with the incremental number of shares being included in the denominator of the diluted income (loss) per share calculation. The diluted income (loss) per share calculation excludes any potential conversion of options and warrants that would increase earnings per share or decrease income (loss) per share.

Comparative figures:

Certain comparative figures have been restated to conform with the current year's presentation. Capital stock has been restated to reflect the 2006 100 to 1 share consolidation (Note 11(a)(i)).

3. SERVICE AGREEMENT

The Company has contracted Penson Financial Services ("Penson") to perform certain trading and clearing activities for clients of the Company, according to the Introducing Broker Agreement (the "Agreement") between Penson and the Company. As a Type 2 Introducing Broker, the Company does not carry client accounts, nor receive, deliver or hold cash and securities in connection with such clients. At March 31, 2006, the Company maintained deposits with Penson and another carrying broker of \$831,053 (2005 - \$945,800), which cannot be used in the normal course of operations. As at March 31, 2006, Penson had offset Nil (2005 - \$646,000) against this deposit for under margined and delinquent accounts of clients of the Company. Penson performs its services for a flat fee per trade, subject to certain additional charges. Interest related to client accounts is also split according to the Agreement.

4. SECURITIES OWNED AND SECURITIES SOLD SHORT

Securities owned consist of the following:

	<u>2006</u>	<u>2005</u>
	\$	\$
Publicly traded equities	13,952,206	1,593,114
Broker warrants	900,000	950,000
	<u>14,852,206</u>	<u>2,543,114</u>

Securities sold short consist of the following:

	<u>2006</u>	<u>2005</u>
	\$	\$
Publicly traded equities	22,060	148,909

Included in publicly traded equities is an investment in Jura Energy Corporation ("Jura") (formerly Proprietary Industries Inc.) representing 11% (2004 - 14.8%) of the outstanding common shares of Jura.

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5. LONG-TERM INVESTMENTS

Long-term investments consist of the following:

	<u>2006</u>	<u>2005</u>
	\$	\$
Cybersurf Corp.	738,000	1,073,087
Jura Energy Corporation ("Jura") (formerly Proprietary Industries Inc.)	-	6,804,390
Other investments	-	383,567
	<u>738,000</u>	<u>8,261,044</u>

The market value of the long-term investments is approximately \$738,000 as at March 31, 2006 (2005 - \$7,100,000).

As at March 31, 2006, management believes that the decline in market value of this long-term investment may be other than temporary. As a result, an impairment loss in the amount \$335,087 has been recognized in 2006.

The Company's long-term investments in Jura Energy Corporation ("Jura") (formerly Proprietary Industries Inc.) and other investments were reclassified to securities owned during the year. See Note 4. At March 31, 2005, the Company's investment in Jura represented 14.8% of the outstanding common shares of Jura and included the cost of shares paid for in cash by the Company of \$3,675,592, 861,049 shares of the Company exchanged for shares of Jura valued at \$2,152,624 and transaction costs of \$976,174.

6. EQUIPMENT

	<u>2006</u>		
	Cost	Accumulated Amortization	Net
	\$	\$	\$
Office equipment	702,075	452,208	249,867
Leasehold improvements	463,813	244,401	219,412
Computer hardware	1,573,544	1,192,426	381,118
Artwork	12,914	-	12,914
	<u>2,752,346</u>	<u>1,889,035</u>	<u>863,311</u>
	<u>2005</u>		
	Cost	Accumulated Amortization	Net
	\$	\$	\$
Office equipment	683,262	393,213	290,049
Leasehold improvements	393,381	201,325	192,056
Computer hardware	1,464,750	1,082,575	382,175
Artwork	12,914	-	12,914
	<u>2,554,307</u>	<u>1,677,113</u>	<u>877,194</u>

7. GOODWILL AND INTANGIBLE ASSETS

a) Goodwill:

	<u>2006</u>	<u>2005</u>
	\$	\$
Balance	<u>3,024,468</u>	<u>3,024,468</u>

Management has calculated the fair market value of the publicly traded stock of the Company and compared it to the book value of the stock and concluded that there was no impairment of goodwill.

b) Intangible Assets:

	<u>2006</u>		
	Cost	Accumulated Amortization	Net
	\$	\$	\$
Client agreements and relationships	377,000	375,082	1,918
Computer software	533,438	516,456	16,982
Patents and trademarks	8,624	6,256	2,368
	<u>919,062</u>	<u>897,794</u>	<u>21,268</u>

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	2005		
	Cost \$	Accumulated Amortization \$	Net \$
Client agreements and relationships	377,000	252,181	124,819
Computer software	519,308	503,772	15,536
Patents and trademarks	8,624	3,665	4,959
	<u>904,932</u>	<u>759,618</u>	<u>145,314</u>

8. DEFERRED DEVELOPMENT COSTS

The net carrying value of deferred development costs consists of the following:

	<u>Cost</u> \$	<u>Accumulated</u> <u>Amortization</u> \$	<u>Net</u> <u>2006</u> \$	<u>Net</u> <u>2005</u> \$
Recruitment loans	<u>423,970</u>	<u>198,186</u>	<u>225,784</u>	<u>-</u>

Recruitment loans are provided to investment advisors and capital market professionals as a hiring incentive. These loans are non-interest bearing and are forgiven on a straight-line basis over the term of the individual employment contract, which vary in length from six months to four years. The forgiven amount for the year of \$198,186 (2005 - \$Nil) is recorded as an operating expense.

9. PROMISSORY NOTE PAYABLE

As at March 31, 2006, the Company had a promissory note payable outstanding in the amount of \$1,739,396 (2005 - \$2,500,000). The promissory note facility entitles the Company to draw up to \$2,500,000. The promissory note payable matures on May 17, 2007, bears interest at 13%, and is secured by certain securities owned by the Company with a market value of approximately \$12,400,000, a general security agreement, covering all property of the Company, and a personal guarantee by the President of the Company. A director of the Company is also a director and officer of the trustee of the promissory note payable. Interest expense related to the promissory note payable approximated \$358,000 (2005 - \$37,000).

During 2006, the President of the Company was granted 27,272 common shares of the Company as consideration for his personal guarantee of the promissory note payable. The shares were valued at approximately \$68,000 based on the quoted market price of the Company's shares at the date of approval of such share issuance. The fee is being expensed over the term of the promissory note. Approximately \$61,000 has been expensed and credited to contributed surplus as at March 31, 2006. Subsequent to March 31, 2006 these common shares were issued.

10. DEBENTURES PAYABLE

As at March 31, 2006, the Company had issued debentures with a principal face value of \$1,080,000. The debentures are unsecured, mature on December 31, 2006, carry a 9% interest rate and have one share purchase warrant for each ten dollars of principal amount issued. The share purchase warrants have an exercise price of \$5.00 up to December 31, 2006.

The 108,000 warrants were valued at \$200,000 using the Black-Scholes pricing model with the following assumptions: expected dividend yield of 0%, expected volatility of 100%, risk free interest rate of 3%, and an expected life of three years. During 2005, 97,000 of these warrants were exercised.

11. CAPITAL STOCK

a) Share Capital:

Authorized:

Unlimited number of common shares
 2,000,000 voting, convertible, redeemable preference shares

Issued and outstanding:

8,583,146 common shares

\$41,648,487

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Share capital activity for the years ended March 31, 2006 and 2005 is summarized as follows:

	Shares #	Amount \$
Balance, March 31, 2004	5,593,536	79,446,620
Private placements (ii)	1,351,515	3,750,000
Reduction of stated capital (iii)	-	(45,963,275)
Exercise of stock options	6,767	26,217
Exercise of warrants	97,000	471,000
Shares issued as management compensation (iv)	147,047	571,667
Settlement of credit facility commitment obligation (v)	33,750	135,000
Shares issued to acquire Sylre (vi)	476,476	1,027,384
Shares issued to acquire investment in Jura (Note 5)	861,049	2,152,624
Balance, March 31, 2005	8,567,140	41,617,237
Shares issued as management compensation (iv)	15,609	31,250
Share consolidation adjustment (i)	396	-
Balance, March 31, 2006	8,583,146	41,648,487

- (i) Effective November 20, 2005, the common shares of the Company were consolidated on a 1 for 100 basis. These consolidated financial statements fully reflect this share consolidation.
- (ii) During 2005, the Company raised gross proceeds of \$3,750,000 upon the completion of private placements for the issuance of 1,351,515 common shares of the Company as follows: 533,333 common shares at \$1.875 per share, 333,333 common shares at \$2.25 per share, and 484,848 common shares at \$4.125 per share. A total of 550,983 shares for gross proceeds of \$1,287,909 were subscribed for by the President of the Company, a family member of the President of the Company, and a corporation controlled by the President of the Company. An additional 41,445 common shares for gross proceeds of \$140,127 were subscribed for by a director of the Company.
- (iii) The Company eliminated the accumulated deficit relating to its previous mining operations by reducing share capital as ratified by shareholders at the September 30, 2004 annual and special meeting of shareholders.
- (iv) Certain employees receive a portion of their compensation in common shares of the Company. During 2006, 15,609 common shares (2005 - 147,047) were granted to employees in settlement of compensation amounts.
- (v) The Company issued 33,750 common shares to settle amounts due of \$135,000 in connection with a credit facility arrangement.
- (vi) The Company acquired 100% of the outstanding common shares of Sylre Ltd. ("Sylre"). Sylre had no operations at the time of acquisition and the acquisition has therefore been recorded as a financing transaction. The Company issued 476,476 common shares and acquired cash totaling \$1,027,384 net of transaction costs of \$525,661 and cash paid for Sylre shares. During 2006, the Company disposed of its interest in Sylre for gross proceeds of \$222,000. This gain has been included in merchant banking revenue.

b) Capital Requirements:

The Company's investment dealer subsidiary, NSI, is subject to rules of the IDA which require NSI to maintain a certain level of regulatory capital. This capital was provided by the Company and is eliminated upon consolidation as a loan between the parent and subsidiary.

As at March 31, 2006 the capital of NSI exceeded the requirements of the IDA.

c) Stock Options:

Effective August 28, 2003 the Company discontinued the stock option plan (the "Plan"), whereby no further options will be granted pursuant to the Plan and all options outstanding will remain in effect until either exercised or cancelled.

As at March 31, 2006, there were 142,002 common share purchase options outstanding, expiring at various dates to January 21, 2013. The options have an exercise price equal to the Company's market closing share price on the day prior to the date of grant and vest over the first twenty-four or thirty months, in equal monthly installments, beginning in the month of grant, and are exercisable over ten years.

Stock option activity for the years ended March 31, 2006 and 2005 is summarized as follows:

	<u>Stock Options</u> #	<u>Weighted Average</u> <u>Exercise Price</u> \$
Balance March 31, 2004	198,780	0.19
Cancelled	(17,962)	11.04
Exercised	(6,767)	3.87
Balance March 31, 2005	174,051	14.03
Cancelled	(32,049)	11.04
Balance March 31, 2006	142,002	14.71

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The following is a summary of common share purchase options outstanding as at March 31, 2006:

<u>Range of Exercise Prices</u> \$	<u>Stock Options</u> #	<u>Average Remaining Life</u> (Years)	<u>Weighted Average Price</u> \$
3.50-10.00	113,287	5.87	5.77
10.00-70.00	28,715	4.23	49.99
	<u>142,002</u>	5.24	14.71

d) Employee Equity Incentive Plan:

On September 30, 2004, the shareholders of the Company approved the establishment of an equity incentive plan whereby up to 6% of the outstanding common shares of the Company may be issued annually to certain new or existing employees of the Company as a means of attracting and retaining exceptional employees.

During 2005 and 2006, the following transactions pursuant to the equity incentive plan took place:

- i) 125,000 common shares were granted, vesting in equal installments on June 1, 2005, 2006 and 2007. On June 1, 2005, 30,000 common shares vested and the Company settled its obligation related to these vested shares. A total of 71,666 common shares of the initial grants were cancelled prior to vesting requirements being met. At March 31, 2006, 23,334 common shares remain, vesting equally on June 1, 2006 and 2007. Included in contributed surplus is an accrual of approximately \$60,000 related to these common shares.
- ii) 6,000 common shares were granted vesting in equal installments on June 15, 2005 and 2006. On June 15, 2005, 3,000 shares vested and the Company settled its obligation related to these vested shares. The remaining 3,000 shares were cancelled prior to vesting requirements being met.
- iii) \$100,000 of common shares were granted vesting on each of August 2, 2005, 2006 and 2007. On August 2, 2005, shares valued at \$100,000 vested and the Company settled its obligation related to these vested shares by extinguishing existing amounts owed to the Company of approximately \$30,000 and by agreeing to issue 46,191 common shares of the Company valued at approximately \$60,000. The value of the common shares is based on the quoted market value of the Company's stock at the vesting date. As at March 31, 2006, these common shares had not been issued and \$60,000 remained credited to contributed surplus.

The Company settled vested amounts under the equity incentive plan for consideration valued at approximately \$64,000 less than amounts accrued. These settlement differences have been credited to contributed surplus.

e) Warrants:

As at March 31, 2006, there were 124,584 common share purchase warrants issued and outstanding, expiring at various dates to January 2, 2007.

Common share purchase warrant activity for the years ended March 31, 2006 and 2005 is summarized as follows:

	<u>Warrants</u> #	<u>Weighted Average Exercise Price</u> \$
Balance, March 31, 2004	425,917	6.86
Exercised	(97,000)	3.00
Expired	(79,440)	7.00
Balance, March 31, 2005	<u>249,477</u>	7.36
Expired	(124,893)	9.96
Balance, March 31, 2006	<u>124,584</u>	4.93

The fair value of the warrants granted during 2004 at the date of grant was estimated using the Black-Scholes option pricing model based on the following assumptions: risk-free interest rate of 3%; expected life of three years; dividend rate of 0%; and volatility of 100%.

The following is a summary of common share purchase warrants outstanding as at March 31, 2006:

<u>Date of Grant</u>	<u>Date of Expiry</u>	<u>Warrants</u> #	<u>Exercise Price</u> \$
August 15, 2001	August 15, 2006	105,000	5.00
September 16, 2001	September 16, 2006	667	5.00
November 18, 2001	November 18, 2006	7,917	4.00
December 19, 2003	December 31, 2006	4,000	5.00
January 26, 2004	January 26, 2007	7,000	5.00
		<u>124,584</u>	

NORTHERN FINANCIAL CORPORATION
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f) Contributed surplus:

Contributed surplus activity for the years ended March 31, 2006 and 2005 is summarized as follows:

Balance, March 31, 2004	\$904,950
Expired warrants	128,225
Balance, March 31, 2005	<u>\$1,033,175</u>
Guarantee fees (Note 9)	61,000
Equity incentive plan (Note 11(d))	185,867
Expired warrants	323,000
Balance, March 31, 2006	<u>\$1,603,042</u>

12. INCOME TAXES

a) Provision for Income Taxes

Major items causing the Company's income tax rate to differ from the Canadian combined federal and provincial statutory rate of approximately 36% (2005 - 36%) approximated the following:

	<u>2006</u>	<u>2005</u>
	\$	\$
Income (loss) before taxes	<u>614,414</u>	<u>(3,176,734)</u>
Expected income tax expense (benefit) based on statutory rate	221,000	(1,147,000)
Adjustments to expense (benefit) resulting from:		
Finance costs	-	(155,000)
Tax benefit of losses not previously recognized	(263,000)	-
Expiry of loss carry-forward balances	<u>464,000</u>	<u>140,000</u>
	422,000	(1,162,000)
Change in valuation allowance	<u>(422,000)</u>	<u>1,162,000</u>
Income tax provision	<u>-</u>	<u>-</u>

b) Future Income Tax Balances

The tax effects of temporary differences that give rise to future income tax assets in Canada approximate the following:

	<u>2006</u>	<u>2005</u>
	\$	\$
Future tax assets		
Non-capital losses carried forward	6,847,000	7,311,000
Share issue costs	86,000	170,000
Equipment and intangible assets	(9,000)	(135,000)
Resource deductions	<u>1,524,000</u>	<u>1,524,000</u>
	8,448,000	8,870,000
Valuation allowance	<u>(8,448,000)</u>	<u>(8,870,000)</u>
Total	<u>-</u>	<u>-</u>

The Company has loss carry forwards in Canada of approximately \$19,019,000, which under certain circumstances may be utilized to offset future taxable income. These losses expire as follows:

2007	\$4,794,000
2008	7,888,000
2009	1,366,000
2010	3,044,000
2011	1,089,000
2015	<u>838,000</u>
Total	<u>\$19,019,000</u>

13. COMMITMENTS AND CONTINGENCIES

- a) The Company has indemnified Penson for all obligations to pay for securities purchased and to deliver securities sold by clients. In the event of default by any of its clients on payments due or delivery of securities to Penson, the Company has agreed to pay Penson an amount up to its "excess risk adjusted capital". As at March 31, 2006, the amount of the Company's excess risk adjusted capital was \$1,320,000 (2005 - \$1,306,000).
- b) The Company is party to legal proceedings in the ordinary course of its operations. Management does not expect the outcome of any of these proceedings to have a materially adverse effect on the results of the Company's financial position or operations.
- The Company is the defendant in a number of legal actions where the plaintiffs are claiming damages totaling approximately \$550,000. The Company believes that the actions are without merit, however, it is premature to make an estimate of the potential outcome of financial impact of these actions.

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- Market Regulation Services Inc. ("RS") has commenced a regulatory proceeding against the Company and two of its officers alleging certain historical deficiencies in its supervision and compliance monitoring systems. The Company believes that the allegations are very technical and without merit. No provision for this proceeding has been made.

Litigation is subject to many uncertainties and the outcome of individual matters is not predictable. It is possible that the final resolution of these matters may require the Company to make expenditures over an extended period of time and in a range of amounts that cannot be reasonably estimated and may differ significantly from any amounts recorded in these consolidated financial statements.

- c) The future minimum annual payments for each fiscal year on equipment and office premises under existing operating leases approximate the following:

2007	\$1,135,000
2008	523,000
2009	90,000
2010	76,000
2011 and thereafter	48,000
Total	<u>\$1,872,000</u>

The Company is also responsible for its portion of property taxes and common area costs related to leases for premise.

- f) Under the terms of the asset purchase agreement with Georgia Pacific Securities Corporation ("GP") dated December 20, 2002, the Company was contingently liable to pay 50% of the profits resulting from the GP operations for the next three years to a maximum of approximately \$2,500,000. During the year ended March 31, 2006, this commitment expired with no payments being required by the Company.
- g) The Company is required to share certain gains on disposal, if any, of its investment in Jura (Note 4). Accruals for this sharing arrangement have been made based on the quoted market value of the underlying shares at March 31, 2006.
- h) The Company has available a credit facility in the amount of \$250,000 at prime plus 1%, secured by a general security agreement covering all assets of the Company and certain guarantees provided personally by the President of the Company and a corporation controlled by the President of the Company. As at March 31, 2006, \$245,000 was owing under the credit facility.
- i) The Company has made various principal investment guarantees related to its merchant banking business. These guarantees require the Company to reimburse certain realized losses, if any, on completion of certain merchant banking transactions. As at March 31, 2006, the total guaranteed amount approximated \$1,000,000. Included in this amount is a guarantee for \$500,000 for which the underlying investment had declined in value by \$317,000. An accrual related to this guarantee of \$317,000 has been included in accounts payable and accrued liabilities. At March 31, 2006, the remaining \$500,000 of guaranteed investments had quoted market values in excess of the guaranteed amounts.

14. FINANCIAL INSTRUMENTS

Fair Value:

Canadian generally accepted accounting principles require that the Company disclose information about the fair value of its financial assets and liabilities. Fair value estimates are made at the balance sheet date, based on relevant market information and information about the financial instrument. These estimates are subjective in nature and involve uncertainties in significant matters of judgment and therefore cannot be determined with precision. Changes in assumptions could significantly affect these estimates.

The carrying amounts for deposit with carrying broker, securities owned, accounts receivable, prepaid expenses and deposits, taxes recoverable, accounts payable and accrued liabilities, and securities sold short on the balance sheet approximate fair value because of the limited term of these instruments. The carrying value of the debentures and notes payable are a reasonable estimate of their respective fair values due to the relative short period of time since the issuance of these financial instruments.

Risk Management:

Risk management at the Company is an integrated process with independent oversight, which requires constant communication, judgment and knowledge of specialized products and markets. The Company's senior management takes an active role in the risk management process and has developed policies and procedures that require specific administration and business functions to assist in the identification, assessment and control of various risks.

Market Risk:

Market risk is the risk that a change in market prices, interest rate levels, indices, liquidity and other market factors will result in losses. The Company is exposed to market risk as a result of its principal trading in equity securities and fixed income securities and merchant banking activities. Securities held for trading are valued at market and as such, changes in market value affect earnings (losses) as they occur. The Company mitigates its market risk exposure through controls to limit concentration levels and capital usage within its inventory trading accounts.

NORTHERN FINANCIAL CORPORATION
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Credit Risk:

The Company incurs credit risk when entering into, settling and financing various proprietary and client transactions. Credit risk arises from the potential that investees, clients or counterparties fail to satisfy their obligations. Credit risk is managed by dealing with counterparties the Company believes to be creditworthy and by actively monitoring credit exposure and the financial health of the counterparties.

Interest Rate Risk:

Interest rate risk arises from the possibility that changes in interest rates will affect the value of financial instruments. The Company does not hedge its exposure to interest rate risk as it is minimal.

Foreign Exchange Risk:

Foreign exchange risk is the risk that the market value of financial instruments and the associated revenues will fluctuate due to changes in exchange rates. The Company does not use derivatives to modify the foreign exchange risk.

15. RELATED PARTY TRANSACTIONS

Related party transactions, disclosed elsewhere in these consolidated financial statements, are in the normal course of operations and are recorded at the exchange amount, being the amount of consideration established and agreed to by the related parties.

See Notes 9 and 11(a)(ii) and 17(a).

16. SUPPLEMENTAL INFORMATION – STATEMENT OF CASH FLOWS

	<u>2006</u>	<u>2005</u>
	\$	\$
Interest paid	1,028,784	1,089,367
Shares issued as management compensation (Note 11(a)(iv))	31,250	571,667
Shares issued to acquire Jura (Note 5)	-	2,152,624
Cash and cash equivalents consist of the following:		
Cash	398,097	1,158,563
Due from carrying broker	<u>2,750,647</u>	<u>2,281,955</u>
	<u>3,148,744</u>	<u>3,440,518</u>

17. SUBSEQUENT EVENTS

- a) The Company formed an investor group which acquired approximately 48% of the issued shares of Lakeside Steel Corporation ("Lakeside"). The Company invested \$400,000 in the investor group, representing approximately 13% of the \$3,000,000 investor group. Lakeside owns three steel pipe and tube fabricating facilities in Welland, Ontario.

Prior to the investment by the Company's investor group, Lakeside was owned 100% by Rompsen Investment Corporation ("RIC"). A director of the Company is also a director and officer of RIC and of Lakeside.

On June 8, 2006, Lakeside entered into a letter agreement to merge with Canadian Tubulars (1997) Ltd., TSI Tubular Services Inc. and 911499 Alberta Inc. (collectively referred to as "Tubulars"). The merged company will be owned 50% by the shareholders of Lakeside and 50% by the shareholders of Tubulars. This transaction will dilute the Company's interest to approximately 3%. Pursuant to the agreement with the investor group, the Company may earn a greater percentage than its equity interest of any gain on this investment.

The President of the Company has been appointed Chairman of Lakeside and will remain Chairman of the merged company. A director of the Company has been appointed President of Lakeside.

- d) On June 4, 2006, the Company entered into a letter of intent ("LOI") to acquire Energy Finance (UK) Ltd. ("EF"). EF is an investment dealer located in London, England. The acquisition is subject to a six-month trial period during which the Company may elect to complete the acquisition for consideration equal to 5% of revenues generated by EF over a three and one-half year period to a maximum £300,000 (\$609,000), subject to minimum payments of £25,000 (\$51,000) on the closing date of the acquisition, £25,000 (\$51,000) on the 12 month anniversary of the closing, £25,000 (\$51,000) on the 18 month anniversary of the closing and £25,000 (\$51,000) on the 24 month anniversary of the closing. The consideration may be paid in cash or in common shares of the Company, at the option of the Company.
- e) On June 5, 2006, the board of directors of the Company approved an employee share purchase plan ("ESPP"). The ESPP allows employees to purchase common shares of the Company equal to 5% of their annual compensation, to a maximum amount of \$5,000 per year, with the Company matching the number of shares purchased at no additional cost to the employee. The ESPP is subject to shareholder and regulatory approval. As at June 9, 2006, no grants had been made under the ESPP.

CORPORATE INFORMATION

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BOARD OF DIRECTORS

Vic Alboini, *Chairman*

R. Ian Bradley
President and CEO
Lakeside Steel Corporation

William Grant
Consultant

Wesley Roitman
Partner
Romspen Investment Corporation

SHARE INFORMATION

Listed on the Toronto Stock Exchange under the trading symbol **NFC**

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