



**CONSOLIDATED FINANCIAL STATEMENTS**

**Years ended December 31, 2008 and 2007**

**(Expressed in thousands of Canadian dollars except where otherwise noted)**

## Management's Responsibility for Financial Reporting

All information in the Company's continuous disclosure documents, including the consolidated financial statements and management's discussion and analysis of the consolidated financial position and results of operation ("MD&A") of the Company, is the responsibility of the management of the Company and has been approved by its Board of Directors. The consolidated financial statements and MD&A were prepared by management in accordance with accounting principles and disclosure requirements generally accepted in Canada.

The preparation of financial statements and MD&A requires the selection of appropriate generally accepted accounting principles and the use of estimates and judgment by management to present fairly and consistently the consolidated financial position and the results of operations of the Company. Estimates are necessary when transactions affecting the current accounting period cannot be finalized with certainty until future periods. In management's opinion, such estimates have been properly reflected in the consolidated financial statements and MD&A. Systems of internal accounting controls are designed and maintained by management in order to provide reasonable assurance, on a cost effective basis, of the reliability of this financial information.

The Board of Directors is responsible for ensuring that management fulfills its responsibilities for financial reporting and is ultimately responsible for reviewing and approving the consolidated financial statements and MD&A. The Board carries out this responsibility principally through its Audit Committee, which is comprised of three independent directors. The committee meets periodically with management and the Company's independent auditors to discuss internal controls over the financial reporting process, auditing matters and financial reporting issues and to review the consolidated financial statements and MD&A and the independent auditors' report to the shareholders. The Committee reports its findings to the Board for consideration when approving the annual consolidated financial statements and MD&A for issuance to shareholders. The Committee also considers, for review by the Board and approval by the shareholders, the engagement or re-appointment of the Company's independent auditors.

The consolidated financial statements have been audited on behalf of the shareholders by the Company's independent auditors, KPMG LLP, in accordance with generally accepted auditing standards. The auditors' report outlines the scope for their examination and their opinion on the consolidated financial statements.

A handwritten signature in blue ink, appearing to read "A. Terrance MacGibbon".

A. Terrance MacGibbon  
Chairman and Chief Executive Officer

A handwritten signature in blue ink, appearing to read "R. Gagel".

Ronald P. Gagel  
Senior Vice President and Chief Financial Officer

March 25, 2009

## **Auditors' Report**

### **To the Shareholders of FNX Mining Company Inc.**

We have audited the consolidated balance sheets of FNX Mining Company Inc. as at December 31, 2008 and 2007 and the consolidated statements of operations, cash flow, comprehensive income (loss) and retained earnings (deficit) for each of the years in the two year period ended December 31, 2008. 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 consolidated financial statements are free of material misstatements. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation.

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2008 and 2007 and the results of its operations and cash flows for each of the years in the two year period ended December 31, 2008 in accordance with Canadian generally accepted accounting principles.

A handwritten signature in black ink that reads "KPMG LLP". The signature is written in a cursive style and is underlined with a single horizontal stroke.

Chartered Accountants, Licensed Public Accountants

Toronto, Ontario  
March 25, 2009

**Consolidated Balance Sheets**

As at December 31

(in thousands of Canadian dollars)

	2008	2007
	\$	\$
<b>Assets</b>		
<b>Current</b>		
Cash and cash equivalents	129,561	35,160
Accounts receivable (note 22)	59,324	103,257
Inventory (note 4)	2,307	4,060
Prepaid and other	1,504	1,142
	<b>192,696</b>	<b>143,619</b>
<b>Investments (note 6)</b>	<b>4,009</b>	<b>35,603</b>
<b>Investment in Gold Wheaton (note 7)</b>	<b>215,620</b>	<b>-</b>
<b>Property, plant and equipment (note 8)</b>	<b>435,114</b>	<b>815,376</b>
<b>Intangible assets (note 9)</b>	<b>-</b>	<b>6,605</b>
<b>Reclamation deposits (note 10)</b>	<b>6,485</b>	<b>6,485</b>
	<b>853,924</b>	<b>1,007,688</b>
<b>Liabilities</b>		
<b>Current</b>		
Accounts payable and accrued liabilities (note 22)	36,136	72,405
Deferred revenue (note 13)	26,433	975
	<b>62,569</b>	<b>73,380</b>
<b>Long-term deferred revenue (note 13)</b>	<b>368,969</b>	<b>-</b>
<b>Mine closure and site restoration (note 11)</b>	<b>5,393</b>	<b>5,087</b>
<b>Future income and resource taxes (note 14)</b>	<b>60,499</b>	<b>178,180</b>
	<b>434,861</b>	<b>183,267</b>
	<b>497,430</b>	<b>256,647</b>
<b>Shareholders' equity</b>		
Share capital (note 15)	571,750	567,700
Contributed surplus – stock-based compensation (note 16)	13,741	9,816
Retained earnings (deficit)	(220,580)	167,960
Accumulated other comprehensive income (loss) (note 3)	(8,417)	5,565
	<b>356,494</b>	<b>751,041</b>
	<b>853,924</b>	<b>1,007,688</b>

*Subsequent events (notes 8, 12 and 26), commitments (note 23), and contingencies and litigation (note 25). The accompanying notes are an integral part of these consolidated financial statements.*

On behalf of the Board of Directors



A. Terrance MacGibbon  
 Chairman and Chief Executive Officer



Donald M. Ross  
 Director

**Consolidated Segmented Balance Sheets**

As at December 31, 2008

(in thousands of Canadian dollars)

	<b>Mining</b>	<b>DMC</b>	<b>Total</b>
<b>Assets</b>	<b>\$</b>	<b>\$</b>	<b>\$</b>
Cash and cash equivalents	120,131	9,430	129,561
Accounts receivable	44,459	14,865	59,324
Other current assets	2,823	988	3,811
	167,413	25,283	192,696
<b>Investments</b>	<b>4,009</b>	<b>-</b>	<b>4,009</b>
<b>Investment in Gold Wheaton</b>	<b>215,620</b>	<b>-</b>	<b>215,620</b>
<b>Property, plant and equipment</b>	<b>409,718</b>	<b>25,396</b>	<b>435,114</b>
<b>Reclamation deposits</b>	<b>6,485</b>	<b>-</b>	<b>6,485</b>
	<b>803,245</b>	<b>50,679</b>	<b>853,924</b>
<b>Liabilities</b>			
Accounts payable and accrued liabilities	28,469	7,667	36,136
Deferred revenue	25,456	977	26,433
	53,925	8,644	62,569
<b>Long-term deferred revenue</b>	<b>368,969</b>	<b>-</b>	<b>368,969</b>
<b>Mine closure and site restoration</b>	<b>5,393</b>	<b>-</b>	<b>5,393</b>
<b>Future income and resource taxes</b>	<b>59,374</b>	<b>1,125</b>	<b>60,499</b>
	<b>433,736</b>	<b>1,125</b>	<b>434,861</b>
	<b>487,661</b>	<b>9,769</b>	<b>497,430</b>

**Consolidated Segmented Balance Sheets**

As at December 31, 2007

(in thousands of Canadian dollars)

	<b>Mining</b>	<b>DMC</b>	<b>Total</b>
<b>Assets</b>	<b>\$</b>	<b>\$</b>	<b>\$</b>
Cash and cash equivalents	24,247	10,913	35,160
Accounts receivable	63,148	40,109	103,257
Other current assets	4,366	836	5,202
	91,761	51,858	143,619
<b>Investments</b>	<b>35,603</b>	<b>-</b>	<b>35,603</b>
<b>Property, plant and equipment</b>	<b>785,054</b>	<b>30,322</b>	<b>815,376</b>
<b>Intangible assets and reclamation deposits</b>	<b>6,485</b>	<b>6,605</b>	<b>13,090</b>
	<b>918,903</b>	<b>88,785</b>	<b>1,007,688</b>
<b>Liabilities</b>			
Accounts payable and accrued liabilities	48,402	24,003	72,405
Deferred revenue	-	975	975
	48,402	24,978	73,380
<b>Mine closure and site restoration</b>	<b>5,087</b>	<b>-</b>	<b>5,087</b>
<b>Future income and resource taxes</b>	<b>175,807</b>	<b>2,373</b>	<b>178,180</b>
	<b>180,894</b>	<b>2,373</b>	<b>183,267</b>
	<b>229,296</b>	<b>27,351</b>	<b>256,647</b>

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



**Consolidated Statements of Operations**

For the Years Ended December 31

(in thousands of Canadian dollars except earnings per share)

	2008	2007
	\$	\$
<b>Operating revenues</b>	<b>378,062</b>	322,043
<b>Operating expenses</b>		
Expenses, excluding depreciation and amortization	329,601	150,081
Depreciation and amortization	56,151	28,297
	<b>385,752</b>	178,378
	<b>(7,690)</b>	143,665
<b>Expenses</b>		
Administration	14,348	9,254
Capital taxes	(1,803)	1,719
Depreciation	853	489
Stock-based compensation (note 16)	4,056	3,427
Asset impairments (note 5)	501,490	1,077
Other expenses (income) (note 17)	(10,814)	(4,524)
	<b>508,130</b>	11,442
<b>Earnings (loss) before taxes</b>	<b>(515,820)</b>	132,223
<b>Income and resource taxes recovery (expense)</b> (note 14)	<b>128,880</b>	(22,276)
<b>Share of loss of equity investee</b> (note 7)	<b>(1,600)</b>	-
<b>Net earnings (loss) for the year</b>	<b>(388,540)</b>	109,947
<b>Basic earnings (loss) per share</b> (note 15(b))	<b>(4.59)</b>	1.31
<b>Diluted earnings (loss) per share</b> (note 15(b))	<b>(4.59)</b>	1.30

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



### Consolidated Segmented Statement of Operations

For the Year Ended December 31, 2008

(in thousands of Canadian dollars)

	Mining	DMC	Total
	\$	\$	\$
<b>Operating revenues</b>	<b>244,958</b>	<b>133,104</b>	<b>378,062</b>
<b>Operating expenses</b>			
Expenses, excluding depreciation and amortization	200,570	129,031	329,601
Depreciation and amortization	47,472	8,679	56,151
	<b>248,042</b>	<b>137,710</b>	<b>385,752</b>
	<b>(3,084)</b>	<b>(4,606)</b>	<b>(7,690)</b>
<b>Expenses</b>			
Administration	14,348	-	14,348
Capital taxes	(1,803)	-	(1,803)
Depreciation	853	-	853
Stock-based compensation	2,206	1,850	4,056
Asset impairments	490,574	10,916	501,490
Other expenses (income)	(14,332)	3,518	(10,814)
	<b>491,846</b>	<b>16,284</b>	<b>508,130</b>
<b>Earnings (loss) before taxes</b>	<b>(494,930)</b>	<b>(20,890)</b>	<b>(515,820)</b>
<b>Income and resource taxes recovery (expense)</b>	<b>126,100</b>	<b>2,780</b>	<b>128,880</b>
<b>Share of loss of equity investee</b>	<b>(1,600)</b>	<b>-</b>	<b>(1,600)</b>
<b>Net earnings (loss) for the year</b>	<b>(370,430)</b>	<b>(18,110)</b>	<b>(388,540)</b>

### Consolidated Segmented Statement of Operations

For the Year Ended December 31, 2007

(in thousands of Canadian dollars)

	Mining	DMC	Total
	\$	\$	\$
<b>Operating revenues</b>	<b>267,751</b>	<b>54,292</b>	<b>322,043</b>
<b>Operating expenses</b>			
Expenses, excluding depreciation and amortization	100,317	49,764	150,081
Depreciation and amortization	26,332	1,965	28,297
	<b>126,649</b>	<b>51,729</b>	<b>178,378</b>
	<b>141,102</b>	<b>2,563</b>	<b>143,665</b>
<b>Expenses</b>			
Administration	9,254	-	9,254
Capital taxes	1,719	-	1,719
Depreciation	489	-	489
Stock-based compensation	3,020	407	3,427
Asset Impairment and other expenses (income)	(3,375)	(72)	(3,447)
	<b>11,107</b>	<b>335</b>	<b>11,442</b>
<b>Earnings (loss) before taxes</b>	<b>129,995</b>	<b>2,228</b>	<b>132,223</b>
<b>Income and resource taxes recovery (expense)</b>	<b>(21,287)</b>	<b>(989)</b>	<b>(22,276)</b>
<b>Net earnings (loss) for the year</b>	<b>108,708</b>	<b>1,239</b>	<b>109,947</b>

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

**Consolidated Statements of Cash Flow**

For the Years Ended December 31

(in thousands of Canadian dollars)

	2008	2007
	\$	\$
<b>Operating activities</b>		
Net earnings (loss) for the year	(388,540)	109,947
Non-cash items		
Depreciation and amortization	57,004	28,786
Stock-based compensation	5,161	3,427
Future income and resource taxes expense (recovery)	(114,926)	9,861
Gain on disposal of shares	(8,461)	(15,480)
Asset impairments	501,490	1,077
Decrease in value of investments held-for-trading	746	260
Share of loss of equity investee	1,600	-
Mark-to-market of Gold Wheaton note receivable	14,846	-
Gain on Gold Wheaton common shares acquired	(2,700)	-
Other	(635)	123
	<b>65,585</b>	<b>138,001</b>
Net change in non-cash working capital (note 18)	<b>11,581</b>	<b>29,241</b>
	<b>77,166</b>	<b>167,242</b>
<b>Financing activities</b>		
Common shares issued	2,814	9,727
Bank line of credit advances	45,837	-
Bank line of credit payments	(45,837)	-
	<b>2,814</b>	<b>9,727</b>
<b>Investing activities</b>		
Investments	(10,000)	(2,821)
Property, plant and equipment	(167,751)	(210,037)
Reclamation term deposits	-	(2,786)
Proceeds from disposal of investments	21,441	25,512
Investment in DMC	-	(59,476)
Proceeds on sale of gold equivalent units	175,000	-
Gold Wheaton transaction costs	(4,366)	-
Deferred payment obligation	-	(7,500)
	<b>14,324</b>	<b>(257,108)</b>
Effect of exchange rate changes on cash	97	182
<b>Change in cash and cash equivalents for the year</b>	<b>94,401</b>	<b>(79,957)</b>
<b>Cash and cash equivalents – beginning of year</b>	<b>35,160</b>	<b>115,117</b>
<b>Cash and cash equivalents – end of year</b>	<b>129,561</b>	<b>35,160</b>

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



## Consolidated Segmented Statement of Cash Flow

For the Year Ended December 31, 2008

(in thousands of Canadian dollars)

	Mining	DMC	Total
	\$	\$	\$
<b>Operating activities</b>			
Net earnings (loss) for the year	(370,430)	(18,110)	(388,540)
Non-cash items			
Depreciation and amortization	48,325	8,679	57,004
Stock-based compensation	3,311	1,850	5,161
Future income and resource taxes expense (recovery)	(113,135)	(1,791)	(114,926)
Gain on disposal of shares	(8,461)	-	(8,461)
Asset impairments	490,574	10,916	501,490
Decrease in value of investments held-for-trading	746	-	746
Share of loss of equity investee	1,600	-	1,600
Mark-to-market of Gold Wheaton note receivable	14,846	-	14,846
Gain on Gold Wheaton common shares acquired	(2,700)	-	(2,700)
Other	(538)	(97)	(635)
	<b>64,138</b>	<b>1,447</b>	<b>65,585</b>
Net change in non-cash working capital	4,561	7,020	11,581
	<b>68,699</b>	<b>8,467</b>	<b>77,166</b>
<b>Financing activities</b>			
Common shares issued	2,814	-	2,814
Bank line of credit advances	45,837	-	45,837
Bank line of credit payments	(45,837)	-	(45,837)
	<b>2,814</b>	<b>-</b>	<b>2,814</b>
<b>Investing activities</b>			
Investments	(10,000)	-	(10,000)
Property, plant and equipment	(157,704)	(10,047)	(167,751)
Proceeds from disposal of investments	21,441	-	21,441
Proceeds on sale of gold equivalent units	175,000	-	175,000
Gold Wheaton transaction costs	(4,366)	-	(4,366)
	<b>24,371</b>	<b>(10,047)</b>	<b>14,324</b>
Effect of exchange rate changes on cash	-	97	97
<b>Change in cash and cash equivalents for the year</b>	<b>95,884</b>	<b>(1,483)</b>	<b>94,401</b>
<b>Cash and cash equivalents – beginning of year</b>	<b>24,247</b>	<b>10,913</b>	<b>35,160</b>
<b>Cash and cash equivalents – end of year</b>	<b>120,131</b>	<b>9,430</b>	<b>129,561</b>

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



**Consolidated Segmented Statement of Cash Flow**

For the Year Ended December 31, 2007

(in thousands of Canadian dollars)

	<b>Mining</b>	<b>DMC</b>	<b>Total</b>
	\$	\$	\$
<b>Operating activities</b>			
Net earnings (loss) for the year	108,708	1,239	109,947
Non-cash items			
Depreciation and amortization	26,821	1,965	28,786
Stock-based compensation	3,020	407	3,427
Future income and resource taxes expense (recovery)	9,861	-	9,861
Gain on disposal of shares	(15,480)	-	(15,480)
Asset impairment	1,077	-	1,077
Decrease in value of investments held-for-trading	260	-	260
Other	87	36	123
	134,354	3,647	138,001
Net change in non-cash working capital	21,603	7,638	29,241
	155,957	11,285	167,242
<b>Financing activities</b>			
Common shares issued	9,727	-	9,727
<b>Investing activities</b>			
Investments	(2,821)	-	(2,821)
Property, plant and equipment	(209,135)	(902)	(210,037)
Reclamation term deposits	(2,786)	-	(2,786)
Proceeds from disposal of investments	25,512	-	25,512
Investment in DMC	(59,824)	348	(59,476)
Deferred payment obligation	(7,500)	-	(7,500)
	(256,554)	(554)	(257,108)
Effect of exchange rate changes on cash	-	182	182
<b>Change in cash and cash equivalents for the year</b>	<b>(90,870)</b>	<b>10,913</b>	<b>(79,957)</b>
<b>Cash and cash equivalents – beginning of year</b>	<b>115,117</b>	<b>-</b>	<b>115,117</b>
<b>Cash and cash equivalents – end of year</b>	<b>24,247</b>	<b>10,913</b>	<b>35,160</b>

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



**Consolidated Statements of Retained Earnings (Deficit)**

For the Years Ended December 31

(in thousands of Canadian dollars)

	<b>2008</b>	2007
	\$	\$
<b>Retained earnings – beginning of year</b>	<b>167,960</b>	58,013
<b>Net earnings (loss) for the year</b>	<b>(388,540)</b>	109,947
<b>Retained earnings (deficit) – end of year</b>	<b>(220,580)</b>	167,960

**Consolidated Statements of Comprehensive Income (Loss)**

For the Years Ended December 31

(in thousands of Canadian dollars)

	<b>2008</b>	2007
	\$	\$
<b>Net earnings (loss) for the year</b>	<b>(388,540)</b>	109,947
<b>Other comprehensive income (loss), net of tax</b>		
Unrealized gains (losses) on available for sale investments (note 3)	<b>(17,337)</b>	1,391
Cumulative translation adjustment (note 3)	<b>2,093</b>	371
<b>Comprehensive income (loss) for the year</b>	<b>(403,784)</b>	111,709

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



## NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

For the years ended December 31, 2008 and 2007  
(amounts in thousands of Canadian dollars except where otherwise noted)

### 1. Nature of operations

FNX Mining Company Inc. ("**FNX**" or the "**Company**") is a Canadian company active in the mineral resource business which includes the acquisition, exploration, development and mining of mineral properties. FNX's mineral properties are located in the Sudbury mining district of Canada from which the Company currently produces and sells nickel, copper, platinum, palladium, gold and cobalt.

On July 15, 2008, the Company entered into an agreement with Gold Wheaton Gold Corp. ("**Gold Wheaton**", formerly known as Kadywood Capital Corp.), whereby the Company agreed to sell 50% of the gold, platinum and palladium metal contained in ore mined and shipped from certain of its deposits for consideration of \$175 million in cash, 350 million Gold Wheaton common shares with a then fair value of \$175 million representing approximately 38% of the then issued Gold Wheaton common shares outstanding to the Company, and a deferred payment of \$50 million in Gold Wheaton warrants, shares or cash due on January 15, 2009 (note 7).

On October 15, 2007, the Company acquired a mining services business from Sherritt International Corporation ("**Sherritt**"), which was rebranded as DMC Mining Services in October of 2008 ("**DMC**"), and is comprised of a Canadian division and DMC Mining Services Corporation ("**DMC USA**") which provides mining services in the United States. The principal activities of DMC consist of contract mining, mine shaft sinking, lateral mine development, mine construction, civil underground construction, raise boring and Alimak raising. Accordingly, the comparative consolidated financial statements include the results of operations for DMC for the period from October 16, 2007 to December 31, 2007.

### 2. Accounting policies and basis of presentation

The consolidated financial statements have been prepared in accordance with accounting principles generally accepted in Canada ("**GAAP**"). Summarized below are those policies considered significant to the Company.

#### (a) Basis of presentation

The consolidated statements include, in addition to the Sudbury Mining and Canadian mining services divisions, the accounts of all of the companies that FNX controls including Aurora Platinum Corp. ("**Aurora**", which was amalgamated with FNX on January 1, 2009), FNX Mining Company USA Inc. and DMC USA. Investments in companies over which FNX has significant influence are accounted for using the equity method. Investments in companies FNX does not control or have significant influence over are carried at cost.

The segmented statements reflect the management structure of the Company and its operating business units. FNX has two operating segments comprised of the Mining segment and the DMC segment. All mining and exploration properties, including the Levack Footwall Deposit ("**LFD**"), of the Mining segment are located in the Sudbury mining district of Canada and include the McCreedy West, Levack and Podolsky mines and all other mineral exploration properties and the activities of the Company's head office in Toronto. The Mining



segment is essentially the business that FNX carried on prior to the acquisition of DMC on October 15, 2007. The DMC segment is comprised of the Canadian DMC division and DMC USA, and operates in both Canada and the United States.

**(b) Use of estimates**

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the year. Significant estimates and assumptions include, among other things, the reserves and resources and the recoverability of mining properties and mineral exploration properties, the composition of future income tax assets and tax liabilities, and metal sales receivables. While management believes that these estimates and assumptions are reasonable, actual results could vary significantly.

**(c) Revenue recognition, deferred revenue and receivables**

*(i) Mining revenue*

FNX produces crushed ore and does not own processing facilities. Revenue is recognized at the time that the crushed ore is delivered to the third party processor, which is also the time that title transfers. The contained metal in the shipped crushed ore is assayed and, pursuant to sales contracts, the appropriate negotiated amount of recoverable metal contained therein is recorded in revenue. The shipped crushed ore is sold under contracts that provide for final prices that are determined by quoted market prices in a period subsequent to the date of sale. Variations from the provisionally priced sales are recognized as revenue adjustments as they occur until the price is finalized. Provisional pricing is based upon market prices in the month of recognition. FNX does not receive provisional payments for ore sold as payment is only received after metal prices are finalized.

Pursuant to an agreement with Gold Wheaton, dated July 15, 2009, FNX sells to Gold Wheaton 50% of the gold equivalent ounces contained in each shipment of crushed ore it produces from certain of its deposits and delivers to a third party processor. Revenue is recognized at the time title passes to Gold Wheaton for Gold Wheaton's share of gold equivalent ounces which is immediately prior to delivery to the third party processor and is comprised of a fixed amount per gold equivalent ounce and the applicable portion of deferred revenue per gold equivalent ounce.

*(ii) DMC contract revenue*

Revenue from DMC is earned primarily on a cost reimbursable basis or on a unit-of-production basis such as meters drilled, meters of advance on underground development, tons of ore mined and hourly charges for work performed and is recognized at the time that the service has been performed.

*(iii) Deferred revenue*

Mining deferred revenue relates to the upfront \$400 million payment received from Gold Wheaton for the future delivery and sale of gold equivalent ounces and is recognized in the statement of operations on the basis of the proportion of gold equivalents sold to Gold Wheaton over the life of mine of the Gold Wheaton deposits.

DMC deferred revenue relates to cash payments received in advance of being earned. DMC deferred revenue is recognized in revenue as it is earned over the terms of the relevant contract.

**(d) Cash and cash equivalents**

Cash and cash equivalents include cash on deposit, term deposits and other interest bearing investments that have maturities of less than 90 days from the date of acquisition.

**(e) Investments**

Effective January 1, 2007, the Company prospectively adopted the Canadian Institute of Chartered Accountants (“CICA”) recommendations pertaining to financial instruments, which established standards for the recognition, measurement, disclosure and presentation of financial assets, financial liabilities and non-financial derivatives. These recommendations require that fair value be used to measure financial assets that are held-for-trading or available-for-sale, financial liabilities that are held for trading and all derivative financial instruments. In accordance with the new standards, as of January 1, 2007, the Company has classified its investments in common shares as available-for-sale. Unrealized holding gains and losses related to available-for-sale investments are excluded from net earnings and included in Other Comprehensive Income (“OCI”) until such gains or losses are realized or an other than temporary impairment is determined to have occurred. Warrants held by the Company are for long-term investment purposes; however, due to their nature, they meet the definition of a derivative and are marked-to-market on a quarterly basis. Mark-to-market gains and losses relating to the warrants are included in net earnings in the period they occur. The Company estimates the fair value of its investments in common shares at the balance sheet date using quoted market prices for available-for-sale securities and a Black-Scholes option pricing model for private warrants held.

**(f) Investment in Gold Wheaton**

The investment in Gold Wheaton is accounted for using the equity method whereby the Company’s share of Gold Wheaton’s earnings or losses is included in the statement of operations and the Company’s investment therein adjusted by an equivalent amount. The notes receivable include an embedded derivative and are marked-to-market on a quarterly basis. Mark-to-market gains and losses on derivatives are included in net earnings in the period in which they occur.

**(g) Inventory**

*(i) In-process inventory*

In-process inventory includes ore mined and brought to surface but not yet shipped and is valued at the lower of cost and net realizable value. Cost of production includes costs to mine and crush ore and any depreciation charges associated with mining activities, including an appropriate portion of fixed and variable overhead expenditures. Cost is determined on a first-in, first-out basis.

Pre-production inventory includes ore mined and brought to surface from a mine that has not achieved commercial production and is valued at the lower of cost and net realizable value less estimated processing costs. Cost of production includes costs to mine and crush ore, including an appropriate portion of fixed and variable overhead expenditures. Cost is determined on a first-in, first-out basis

(ii) *DMC Supplies inventory*

DMC supplies inventory includes non-capital spare parts, consumable operating supplies and cost of inventory held on mine insignificant sites for installation at customers' facilities and is valued at the lower of cost and net realizable value. Cost is determined on a weighted average basis.

**(h) Property, plant and equipment**

(i) *Property acquisition, exploration and development*

Acquisition, exploration and development costs associated with mineral exploration properties are deferred. When the Board of Directors approves a decision to proceed to commercial production, accumulated costs to date for that project are transferred from mineral exploration properties to properties under development. Commercial production occurs when a mining asset or property is substantially complete and ready for its intended use. The criteria considered in determining when commercial production commences include: achieving production at a pre-determined percentage of mine design capacity; sustaining continuous production and output; and, reaching an expected net margin and/or cash flow during the pre-production period. In a phased mining situation, consideration is given to achieving milestones at each phase of completion. Management will assess the operation's ability to sustain production over a period of from one to three months, depending upon the complexity of the situation and the stability of continuous operation. Commercial production will be considered to have commenced at the beginning of the month in which the criteria are met. Any income from production prior to commercial production is offset against development costs. When the property achieves commercial production, the accumulated costs to date are transferred from properties under development to mining properties. Accumulated costs are amortized into the in-process inventory, using a unit-of-production basis over the expected life of the mine, once commercial production is achieved.

(ii) *Plant and equipment*

Expenditures for plant and equipment additions, major replacements and improvements are recorded at cost. Plant and equipment assets are amortized, once commercial production is achieved, on either a unit-of-production or a straight-line basis over the lesser of estimated useful life or expected life of the mine. The estimated useful life of equipment that is depreciated on a straight-line basis is as follows:

	<u>Mining</u>	<u>DMC</u>
Buildings	-	20 years
Mobile equipment	5 years	5-10 years
Furniture and fixtures	5 years	5 years
Computer equipment	3 years	3 years
Vehicles	3 years	3 years
Leasehold improvement	Term of lease plus one renewal option	

(iii) *Impairment of long-lived assets*

FNX reviews and evaluates the carrying value of its operating mines and mineral exploration and development properties for impairment when events or circumstances indicate that the carrying amounts of related assets or groups of assets may not be recoverable. If the total estimated future cash flows on an undiscounted basis for mining properties are less than the

carrying amount of the asset, an impairment loss is measured and assets are written down to fair value, which is normally the discounted value of future cash flows, with a provision being charged to earnings. Future cash flows are estimated based on estimated future recoverable mine production, expected sales prices (considering current and historical prices, price trends and related factors), production levels, cash costs of production, capital and reclamation costs, all based on life of mine plans. Future recoverable mine production is determined from proven and probable reserves and measured, indicated and inferred mineral resources after taking into account estimated dilution and recoveries during mining, and the accountable amount of metal to be recovered after ore processing, smelting and refining. Estimates of recoverable production from measured, indicated and inferred mineral resources are based on management's confidence in converting such resources to proven and probable reserves. Assumptions underlying future cash flow estimates are subject to risks and uncertainties. It is possible that changes in estimates could occur which may affect the expected recoverability of FNX's investments in mineral properties.

The accumulated costs for properties that are abandoned are charged to earnings when the property is abandoned. Accumulated costs on mineral exploration properties that are considered to be impaired through either external economic conditions or failure to advance the property to the development stage within a reasonable period of time are written down.

*(iv) Corporate and other assets*

Corporate and other assets include equipment not used in mining operations or at DMC. Corporate and other assets are recorded at cost less accumulated amortization. Amortization is calculated on a straight-line basis over a three to five year period.

**(i) Mine closure and site restoration**

The fair value of a liability for mine closure and site restoration, also known as an asset retirement obligation, is recognized in the period in which it is incurred. When a liability is initially recorded, a corresponding increase in the carrying amount of the related asset is recorded. The asset is amortized on a unit-of-production basis over the estimated life of the mine and the liability is increased, through accretion, by the interest factor that was applied in the initial measurement of fair value. FNX makes periodic assessments as to the reasonableness of its mine closure and site restoration obligation estimates and revises those estimates accordingly. Any revision to those estimates results in the respective asset and liability balances being adjusted, with a related increase or decrease in the amounts expensed for amortization or accretion in future periods.

The long-term mine closure and site restoration obligation is based on environmental plans in compliance with current environmental and regulatory requirements. Due to uncertainties concerning environmental remediation, the ultimate cost to the Company of future mine closure and site restoration could differ from the amounts provided. The estimate of the total liability of future mine closure and site restoration costs is subject to change based on amendments to laws and regulations and as new information concerning the Company's operations becomes available. Future changes, if any, to the estimated total liability as a result of amended regulations, laws and operating assumptions may be significant and would be recognized prospectively as a change in an accounting estimate when applicable. Environmental laws are continually evolving and FNX is not able to determine the impact, if any, of environmental laws and regulations that may be enacted in the future on its results of operations or financial position due to the uncertainty surrounding the ultimate form that such future laws and regulations may take.

**(j) Income taxes**

FNX uses the asset and liability method of accounting for income and mining taxes. Under this method of tax allocation, future income and mining tax assets and liabilities are determined based on differences between the financial statement carrying amounts of existing assets and liabilities and their respective income and mining tax basis (temporary differences). Future income and mining tax assets and liabilities are measured using enacted or substantively enacted tax rates expected to be in effect in the years in which those temporary differences are expected to be recovered or settled. The effect of a change in tax rates on future income and mining tax assets and liabilities is recognized in earnings in the year in which the change is enacted or substantively enacted. The amount of future income and mining tax assets recognized is limited to the amount that is more likely than not to be realized.

Many provincial jurisdictions charge a tax based on a corporation's taxable capital. This expense, however, is a deductible expense in the determination of taxable income and is separately disclosed in the statements of operations. During 2008, capital taxes were eliminated in the Province of Ontario for mining companies operating in Ontario retroactive to January 1, 2007.

**(k) Stock-based compensation**

FNX accounts for all stock-based compensation using the fair value based method. Under this method, compensation costs attributable to options or deferred share units granted are measured at fair value at the date of grant. Any consideration received upon the exercise of a stock option is credited to share capital. The expense for stock options is recognized over the vesting period of the stock-based award, while the expense for deferred share units is recognized in the period for which the service was rendered. FNX's stock-based compensation plans are described in note 16.

**(l) Earnings per share**

Basic earnings per share are computed by dividing the earnings for the year by the weighted average number of common shares outstanding for the year. Diluted earnings per share are similar to basic earnings per share, except that the denominator is increased to include the number of additional common shares that would have been outstanding if the dilutive potential common shares had been issued using the treasury stock method.

**(m) Foreign exchange**

The Canadian dollar is the functional currency of the Company. Mining revenues, DMC USA's revenues and certain expenses are denominated in United States dollars. Monetary assets and liabilities are translated at period end exchange rates and non-monetary assets and liabilities are translated at historical rates. Gains and losses on translation of monetary assets and liabilities are recorded in earnings.

The financial statements of self sustaining foreign operations such as DMC USA are translated using the current rate method whereby all assets and liabilities are translated at year end exchange rates with income statement items translated at average exchange rates for the year. Translation adjustments arising from changes in exchange rates form part of the change in the cumulative foreign currency translation adjustment component of OCI.

**(n) Changes in accounting policies**

Effective January 1, 2007, the Company prospectively adopted the CICA recommendations pertaining to financial instruments, which established standards for the recognition, measurement, disclosure and presentation of financial assets, financial liabilities and non-financial derivatives. These recommendations require that fair value be used to measure financial assets that are held-for-trading or available-for-sale, financial liabilities that are held-for-trading and all derivative financial instruments. Other financial assets, such as loans and receivables and investments that are held to maturity and other financial liabilities are measured at their carrying value. This change in accounting policy had the following effect on the consolidated financial statements: investments with a book value of \$30,380 were classified as available-for-sale and measured at a fair value of \$50,535 as of January 1, 2008, which resulted in a revaluation gain of \$16,507, net of tax. The revaluation gains have been recognized in accumulated OCI (note 3).

Effective January 1, 2008, the Company prospectively adopted *Section 1535, Capital Disclosures*, which specifies the requirements for the disclosure of information relating to objectives, policies and processes for managing capital. There has been no material effect on the consolidated financial statements of the Company upon adoption of this standard.

Effective January 1, 2008, the Company prospectively adopted *Section 3031, Inventories*, which relates to the accounting for inventories and revises and enhances the requirements for assigning costs to and disclosure of inventories. There has been no material effect on the consolidated financial statements of the Company upon adoption of this standard.

Effective January 1, 2008, the Company prospectively adopted *Section 3862, Financial Instruments - Disclosures, and Section 3863, Financial Instruments - Presentations*, which replaced *Section 3861, Financial Instruments – Disclosure and Presentation*, which revise and enhance the disclosure requirements and carry forward unchanged the presentation requirements. There has been no material effect on the consolidated financial statements of the Company upon adoption of this standard.

**(o) New accounting pronouncements**

*(i) Goodwill and intangible assets*

In February 2008, the CICA replaced Section 3062, Goodwill and Other Intangible Assets with Section 3064, Goodwill and Intangible Assets. This section gives the definition and establishes standards for the recognition, measurement and disclosure of goodwill and intangible assets. Accounting for goodwill and intangible assets following a business combination remains unchanged. Section 3064 gives guidance about internally generated intangible assets. This section applies to fiscal years beginning on or after October 1, 2008. The Company is assessing the impact of this new section and will adopt this standard in 2009

*(ii) Section 1582, Business Combinations; Section 1601, Consolidated Financial Statements; and Section 1602, Non-controlling Interests*

The CICA issued three new accounting standards in January 2009: *Section 1582, Business Combinations; Section 1601, Consolidated Financial Statements; and Section 1602, Non-controlling Interests*. These new standards will be effective for fiscal years beginning on or after January 1, 2011 and earlier adoption is permitted as of the beginning of a fiscal year. The Company is in the process of evaluating the requirements of the new standards.

Section 1582 replaces Section 1581, *Business Combinations*, and establishes standards for the accounting for a business combination. It provides the Canadian equivalent to International Financial Reporting Standards IFRS 3 - Business Combinations.

Sections 1601 and 1602 together replace section 1600, *Consolidated Financial Statements*. Section 1601 establishes standards for the preparation of consolidated financial statements. Section 1602 establishes standards for accounting for a non-controlling interest in a subsidiary in consolidated financial statements subsequent to a business combination. It is equivalent to the corresponding provisions of International Financial Reporting Standard IAS 27 - *Consolidated and Separate Financial Statements*.

(iii) *Credit risk and the fair value of financial assets and financial liabilities*

In January 2009, the CICA issued EIC-173, *Credit Risk and the Fair Value of Financial Assets and Financial Liabilities*. The Emerging issues committee (“EIC”) reached a consensus that an entity’s own credit risk and the credit risk of the counterparty should be taken into account in determining the fair value of financial assets and financial liabilities, including derivative instruments. This accounting treatment should be applied retrospectively without restatement of prior periods. The Company is assessing the impact of this new section and will adopt this standard in 2009.

(iv) *IFRS*

In February 2008, the Canadian Accounting Standards Board confirmed that use of International Financial Reporting Standards (“IFRS”) will be required for publicly accountable profit-oriented enterprises. The official changeover date is for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2011. The Company continues to evaluate the impact of adopting IFRS.

**3. Accumulated other comprehensive income (loss)**

	<u>2008</u>	<u>2007</u>
	\$	\$
Balance – beginning of year	5,565	-
Adjustment at beginning of period due to change in accounting for assets available-for-sale <sup>1</sup>	-	16,507
Changes in fair value of assets available-for-sale <sup>2</sup>	(17,337)	1,391
Reclassification adjustment of gains included in net earnings <sup>3</sup>	(7,145)	(12,704)
Reclassification adjustment for write-down of investment <sup>4</sup>	8,407	-
Cumulative translation adjustment	<u>2,093</u>	<u>371</u>
Balance – end of year	<u>(8,417)</u>	<u>5,565</u>

<sup>1</sup> Tax impact of \$nil (\$3,648 in 2007)

<sup>2</sup> Tax impact of \$3,031 (\$811 in 2007)

<sup>3</sup> Tax impact of \$1,115 (\$2,776 in 2007)

<sup>4</sup> Tax impact of \$1,313 (\$nil in 2007)

#### 4. Inventory

	<u>2008</u>	<u>2007</u>
	\$	\$
In-process		
Cash costs	1,530	1,618
Non-cash costs	<u>465</u>	<u>997</u>
	<u>1,995</u>	<u>2,615</u>
Pre-production	-	769
DMC supplies	<u>312</u>	<u>676</u>
	<u><b>2,307</b></u>	<u><b>4,060</b></u>

Mining in-process inventory represents the lower of cost or net realizable value of the ore that has been mined and brought to surface but has not been shipped to Vale Inco Limited (“Vale Inco”), for concentrating, smelting and refining as at the balance sheet date. Cash costs include mining costs and all costs up to and including crushing but not haulage to the concentrator. Non-cash costs represent the amount of mine depreciation and amortization deferred to in-process inventories as at the balance sheet date. The mine depreciation and amortization included in the carrying value of in-process inventories is charged to Mining depreciation and amortization expense on the statement of operations as the ore is delivered to Vale Inco.

DMC supplies inventory includes non-capital spare parts, consumable operating supplies, as well as the cost of inventory held on sites for installation at customers’ facilities.

#### 5. Asset Impairments

	<u>2008</u>	<u>2007</u>
	\$	\$
Strategic Resource Acquisition Corporation (“SRA”)	10,000	-
Intangible assets <sup>2</sup>	4,128	-
DMC equipment	6,788	-
Mineral exploration properties	107,273	1,077
Mining properties	<u>373,301</u>	<u>-</u>
	<u><b>501,490</b></u>	<u><b>1,077</b></u>

The decline in the value of the investment in common shares of SRA was determined to be other-than-temporary and the investment was considered to be impaired as at September 30, 2008 (note 6).

The intangible assets that arose from the acquisition of DMC from Sherritt on October 15, 2007 were determined to be impaired as at September 30, 2008 (note 9).

As a result of the deterioration of equity, credit and commodities markets that took place during the latter part of the third quarter and the entire fourth quarter of 2008, FNX suspended commercial production of nickel ores from both the McCreedy West and Levack mines of the Levack Complex in late 2008. The above were considered to be a triggering event for purposes of performing impairment tests on the carrying values of the Company’s long-lived assets. FNX performed impairment analyses in accordance with *Section 3063 – Impairment of Long-Lived Assets*. For FNX’s mining properties, the Company compared the carrying value of property, plant and equipment with their estimated undiscounted cash flows and, as these were below their carrying values, with their estimated discounted cash flows to determine their fair values. The Company used current and forward metal prices and foreign

exchange rates, a discount rate of 6% and other recoverable metal and operating assumptions for the discounted cash flow analysis. Based on the analysis performed, the Levack Complex and Podolsky mining operations were written down to the greater of their estimated discounted cash flow (which management believes to be the approximate measure of fair value to be used in the Company's circumstances) and estimated net recoverable value of the equipment. A similar analysis was performed on the LFD. The estimated undiscounted cash flows for the LFD were greater than the carrying value and, therefore, no impairment charge was necessary.

Impairment tests for mineral exploration properties may be triggered by, among other things, the following: a significant adverse change in the business climate; a significant drop in metal prices; a significant deterioration in the availability of financing; exploration results over a period of three or more years not resulting in the discovery of economic mineralization that could be advanced to the development stage in the foreseeable future; and, management's decision not to continue to do ongoing exploration. Accordingly, an impairment test was performed by FNX at December 31, 2008. FNX has been exploring its mineral exploration properties for in excess of three years and, other than the LFD, has not discovered economic mineralization that could be advanced to the development stage in the foreseeable future. In addition, the Company has not currently allocated exploration funds to be expended on mineral exploration properties other than the LFD in the 2009 budget and further exploration will be re-evaluated in 2010 or when metal prices rebound from their current lows. Accordingly, mineral exploration properties other than the LFD were written down to \$nil. Certain DMC equipment was also determined to be impaired and was written down to its fair value.

## 6. Investments

	<b>2008</b>		<b>2007</b>	
	<b>Shares</b>	<b>Amount</b>	<b>Shares</b>	<b>Amount</b>
	<b># 000s</b>	<b>\$ 000s</b>	<b># 000s</b>	<b>\$ 000s</b>
Lake Shore Gold Corp.	<b>1,500</b>	<b>2,130</b>	13,300	23,275
INV <sup>1</sup> (common shares)	<b>7,662</b>	<b>1,226</b>	7,662	6,895
Fieldex Exploration Inc.	<b>6,500</b>	<b>293</b>	6,500	1,723
Northern Resources Inc. (formerly Superior Diamonds Inc.)	<b>6,861</b>	<b>241</b>	6,861	2,573
Visible Gold Mines Inc.	<b>1,066</b>	<b>80</b>	1,066	351
INV (common share purchase warrants)	<b>2,348</b>	<b>39</b>	3,154	786
		<b><u>4,009</u></b>		<b><u>35,603</u></b>

<sup>1</sup> International Nickel Ventures Corporation ("INV")

Investments with a book value of \$30,380 were classified as available-for-sale and measured as of January 1, 2007 at a fair value of \$50,535 which resulted in a revaluation gain of \$16,507, net of tax. During the twelve months ended December 31, 2008, the investments were measured at a fair value of \$4,009 resulting in a revaluation loss of \$15,456, net of tax, recognized in accumulated OCI. Warrants with a book value of \$692 were measured at a fair value of \$39, a decline of \$653 recognized in other expenses (income).

On June 23, 2008, the Company disposed of 11.8 million shares of Lake Shore Gold Corp ("Lake Shore") to Hochschild Mining Holdings Limited at a price of \$1.82 per share for proceeds of \$21,441. A gain in the amount of \$8,461 was recognized during the second quarter on the disposition of the Lake Shore shares.



Pursuant to an agreement dated February 6, 2008, FNX acquired 3.509 million common shares of SRA or approximately 10.7% of the then issued and outstanding common shares of SRA through a private transaction. The shares were acquired at \$2.85 per share, which represented a 5% discount to the closing pricing of the SRA common shares on January 31, 2008, the date the negotiations had commenced. DMC USA provided contract mining services to a wholly-owned subsidiary of SRA in the United States until October 9, 2008.

In light of SRA's financial difficulties, the precipitous decline in metal prices including zinc, and the recent turmoil in the debt and equity markets, the Company concluded that the decline in the fair value of the SRA investment was other-than-temporary. Accordingly, the investment in SRA was written down to \$nil at September 30, 2008. Prior to year end, SRA was delisted from the Toronto Stock Exchange and FNX sold its entire investment in SRA for a nominal amount.

## 7. Investment in Gold Wheaton

	<b>December 31</b>
	<b>2008</b>
	<b>\$</b>
Initial investment	<b>175,000</b>
Transaction costs	<b>4,366</b>
Received on renegotiation of deferred share purchase warrants	<b>2,700</b>
Share of loss of equity investee	<b>(1,600)</b>
	<b>180,466</b>
Note receivable	<b>35,154</b>
	<b>215,620</b>

On July 15, 2008, FNX entered into an agreement with Gold Wheaton whereby the Company agreed to sell 50% of the gold, platinum and palladium metal contained in ore mined, shipped and delivered from the Company's PM and 700 Deposits at the McCreedy West Mine, the Levack Footwall, Rob's and 1900 Deposits at the Levack Mine, and the 2000 and North Deposits at the Podolsky Mine to Gold Wheaton in consideration for an up-front cash payment of \$175,000, 350 million Gold Wheaton common shares with a fair value of \$175,000 representing ownership of approximately 38% of the then issued Gold Wheaton common shares outstanding, a note receivable for deferred warrants with a fair value of \$50,000 that were to be converted on January 15, 2009 into either Gold Wheaton share purchase warrants, shares or cash, and pay, on an ongoing basis, a cash payment equal to the lesser of US\$400 (subject to an inflationary adjustment three years after the anniversary date) per gold equivalent ounce and the then prevailing market price per ounce of gold.

The common shares of Gold Wheaton issued to FNX were subject to a statutory hold period which expired on November 16, 2008. On July 15, 2008, 25% of the Gold Wheaton common shares were released from escrow with an additional 25% to be released every six months thereafter.

The note receivable deferred warrants of \$50,000 was renegotiated on December 8, 2008 to extend the due date of the note receivable to July 16, 2010, at which time the note receivable may be repaid at either FNX's or Gold Wheaton's option through the issuance of that number of additional common shares of Gold Wheaton determined by dividing the \$50,000 by the lesser of: (a) \$1.00, and (b) the greater of: (i) the 20-day volume weighted average price of the Gold Wheaton common shares ending June 30, 2010, and (ii) \$0.20. As partial consideration for extending the due date of the note receivable, Gold Wheaton issued 10 million common shares with a fair value of \$2,700 to FNX. In addition, as the due date is not



until July 16, 2010, the note receivable was discounted by \$4,291, which amount will be accreted to earnings over the period to June 30, 2010. Due to the nature of the renegotiated note receivable, both a call and put option exist on the derivative which must be fair valued at each balance sheet date with any changes thereto charged or credited to earnings. As a result of the above, the carrying value of the note receivable at December 31, 2008 was \$35,154.

In addition to FNX's 38% ownership of the then issued shares of Gold Wheaton outstanding, the Company was granted the right to nominate two directors for membership on the Board of Directors which, combined, constitute a position of significant influence over Gold Wheaton. Consequently, the Company recorded the Gold Wheaton investment on an equity basis whereby the Company's proportionate share of reported Gold Wheaton income or loss is added to or deducted from the carrying value of its investment.

As at December 31, 2008 the market value of FNX's 360 million Gold Wheaton shares was approximately \$91.8 million and the Company's interest in Gold Wheaton was 38%. Subsequent to year end, Gold Wheaton issued 460 million common shares (note 26).

## 8. Property, plant and equipment

	December 31, 2008		
	Cost	Accumulated Amortization	Net
	\$	\$	\$
Mining			
Levack Complex			
Property and development	284,439	(58,486)	225,953
Transfer to LFD	(13,130)	746	(12,384)
Impairment	(271,309)	57,740	(213,569)
	-	-	-
Plant and equipment	102,876	(22,433)	80,443
Transfer to LFD	(50,824)	8,507	(42,317)
Impairment	(12,129)	3,967	(8,162)
	39,923	(9,959)	29,964
	39,923	(9,959)	29,964
Podolsky			
Property and development	151,146	(14,113)	137,033
Impairment	(151,146)	14,113	(137,033)
	-	-	-
Plant and equipment	35,965	(5,653)	30,312
Impairment	(17,025)	2,488	(14,537)
	18,940	(3,165)	15,775
	18,940	(3,165)	15,775
	58,863	(13,124)	45,739
Exploration	371,554	(9,253)	362,301
Corporate	3,446	(1,768)	1,678
Mining segment	433,863	(24,145)	409,718
DMC	40,622	(7,672)	32,950
Impairment	(9,947)	2,393	(7,554)
DMC segment	30,675	(5,279)	25,396
	464,538	(29,424)	435,114

	December 31, 2007		
	<b>Cost</b>	<b>Accumulated Amortization</b>	<b>Net</b>
	\$	\$	\$
Mining			
Levack Complex			
Property and development	248,371	(42,697)	205,674
Plant and equipment	81,077	(11,353)	69,724
	<u>329,448</u>	<u>(54,050)</u>	<u>275,398</u>
Property under development			
Podolsky	136,988	-	136,988
Exploration	371,182	-	371,182
Corporate	2,402	(916)	1,486
Mining	<u>840,020</u>	<u>(54,966)</u>	<u>785,054</u>
DMC	31,466	(1,144)	30,322
	<u><u>871,486</u></u>	<u><u>(56,110)</u></u>	<u><u>815,376</u></u>

**(a) Levack Complex**

FNX holds a 100% interest in the Levack Complex, which is located in the Sudbury mining district of Ontario and is comprised of two adjacent mining operations, McCreedy West and Levack. The two adjacent properties are considered to be one mining operation as they are integrated from an operational perspective, produce similar ore and sell all production to the same purchaser, Vale Inco.

Certain long-lived assets were transferred from the Levack Complex to the LFD. An impairment test was performed by FNX at December 31, 2008 and the carrying values of the remaining long-lived assets at the Levack Complex were written down to their fair values (note 5).

**(b) Podolsky**

FNX holds a 100% interest in Podolsky, which is located in the Sudbury mining district region of Ontario. Commencing January 1, 2008, mining revenues and expenses from ore mined from the Podolsky property have been included in the statement of operations and the accumulated costs to date were transferred from property under development to the appropriate categories of mining property and development and plant and equipment.

An impairment test was performed by FNX at December 31, 2008 and the carrying value of Podolsky was written down to its fair value (note 5).

(c) Mineral exploration properties

	2008				2007
	Cost	Impairment	Amort	Net	
	\$	\$	\$	\$	\$
LFD exploration	307,600	-	-	307,600	269,773
Transfer from Levack	63,954	-	(9,253)	54,701	-
LFD	371,554	-	(9,253)	362,301	269,773
Falconbridge Footwall	49,598	(49,598)	-	-	48,911
Foy-Offset	26,652	(26,652)	-	-	26,576
Other Properties	16,058	(16,058)	-	-	16,020
Victoria	9,712	(9,712)	-	-	6,359
Podolsky Nickel Ramp	2,773	(2,773)	-	-	1,063
Kirkwood	2,480	(2,480)	-	-	2,480
	<b>478,827</b>	<b>(107,273)</b>	<b>(9,253)</b>	<b>362,301</b>	<b>371,182</b>

The carrying value of the mineral exploration properties represents the accumulated costs to date for the acquisition and exploration costs incurred by FNX on its non-producing mineral exploration properties, net of exploration losses. Mineral exploration properties are not being amortized.

As at December 31, 2008, FNX held a 100% interest in the LFD, Victoria and Kirkwood mineral exploration properties, all of which are located in the Sudbury mining district of Ontario. The Podolsky Nickel Ramp project is located on the Podolsky property but is at the exploration stage.

The Falconbridge Footwall, Foy-Offset and Other Properties (formerly collectively referred to as the "Aurora Properties") are located in the Sudbury mining district of Ontario. All of Aurora's non-Sudbury properties were sold during 2007. All of the above mentioned properties, as well as the LFD, Victoria and Kirkwood properties are in the exploration stage and there can be no assurance that commercially viable mineral deposits or reserves exist therein.

The Falconbridge Footwall and Foy-Offset mineral properties are subject to a joint venture agreement (the "**Falconbridge Joint Venture**") with Xstrata Nickel ("**Xstrata Nickel**"), a business unit of Xstrata Canada Corporation. As Xstrata Nickel elected not to participate in the 2008 exploration program, Xstrata Nickel's interest continued to be diluted, such that, as at December 31, 2008, the Company and Xstrata Nickel held an 80% and 20% (2007 - 78% and 22%) interest, respectively, in the Falconbridge Joint Venture. The Company is the operator of the Falconbridge Joint Venture. FNX holds between 30% and 100% interests in the Other Properties.

A 15,027 ton bulk sample was extracted from the 4000 Level exploration drift accessed from Xstrata Nickel's Craig Mine and 10,683 tons thereof were shipped to Vale Inco for processing at the Clarabelle Mill in early July 2008. Final analytical results from the shipped tonnage combined with management's estimated payable metals and processing cost terms, resulted in a \$5,854 pre-production credit to the carrying value of the LFD in 2008 related to the 10,683 tons processed to date.

An impairment test was performed by FNX at December 31, 2008 on all of its mineral exploration properties and the carrying value of all exploration properties, other than the

LFD, was written down to \$nil (note 5). Subsequent to year end, the LFD was approved for development for commercial production by the Company's Board of Directors and the accumulated net costs will be transferred from mineral exploration properties to property under development.

**(d) Corporate**

Corporate assets consist of vehicles, computer hardware and software, office equipment, and furniture and fixtures at the Toronto head office and the Sudbury exploration office.

**(e) DMC**

Long-lived assets included in DMC are comprised of mobile mining equipment and related furniture, fixtures and computer hardware and software to support DMC's activities.

An impairment test was performed by FNX at December 31, 2008 on DMC's equipment and the carrying value of the equipment was written down by \$6,788, on which a translation loss of \$766 was booked, for a total of \$7,554.

**9. Intangible assets**

	<u>2008</u>	<u>2007</u>
	\$	\$
Cost	7,431	7,431
Accumulated amortization	(3,303)	(826)
Impairment	(4,128)	-
	<u>-</u>	<u>6,605</u>

Intangible assets arose from the acquisition of DMC from Sherritt on October 15, 2007. In the third quarter of 2008, FNX concluded that events and changes in circumstances indicated that the carrying value of FNX's intangible assets may not be recoverable. The triggering event and change in circumstances included both the deterioration of equity, credit and commodities markets in the latter half of 2008, as well as the loss of several customer contracts which had previously significantly contributed to the value of the intangible assets. FNX performed an impairment analysis in accordance with *Section 3063 – Impairment of Long-lived Assets*, which compared the carrying values of all intangible assets with their fair values. Based on the analysis performed, it was determined that there remained no future value in FNX's intangible assets and they were, therefore, written down to \$nil, with the \$4.1 million unamortized balance being charged to the statement of operations in the third quarter of 2008.

**10. Reclamation deposits**

Reclamation term deposits support letters of credit of various amounts in favour of Vale Inco and government agencies in the Province of Ontario in connection with the Levack Complex and the Podolsky properties. The balance remains unchanged in 2008.



**11. Mine closure and site restoration**

	<u>2008</u>	<u>2007</u>
	\$	\$
Balance – beginning of year	5,087	2,631
Accretion expense	306	157
Revisions to estimated obligations	-	2,299
Balance – end of year	<u>5,393</u>	<u>5,087</u>

FNX's asset retirement obligations relate to the final mine closure and site reclamation costs at the Levack Complex and Podolsky. FNX estimates the total future mine closure and site reclamation costs associated with the Sudbury mining operations to be approximately \$6,485 (2007 - \$6,485). These estimates are formally reviewed by technical personnel every year or more frequently if required by regulatory agencies. A credit adjusted risk free rate of 6.0% was utilized to determine the mine closure and site restoration obligation recorded in the consolidated balance sheets. Management anticipates that such obligations will be substantially settled one year after the permanent closure of the relevant mining operation.

**12. Bank indebtedness**

On April 1, 2008, the Company established a US\$100 million secured line of credit facility (the "LOC") with a consortium of major banks, which provided the Company with the right to borrow for working capital and general corporate purposes. The LOC was to mature on March 31, 2009, subject to an extension option, as well as a right to elect a one-year term-out of the LOC, in which case repayment of outstanding amounts would be made in four equal installments commencing on June 30, 2009 and ending on March 31, 2010. Borrowings could be made in the form of United States Base Rate loans or London Interbank Offered Rate ("LIBOR") loans. Borrowings bore interest, when drawn, at the United States Base Rate (plus a margin ranging from 0.250% to 0.875%) or at LIBOR (plus a margin ranging from 1.250% to 1.875%) depending on the Company's then current leverage ratio and whether the LOC had been converted from revolving to non-revolving. The LOC was secured by a first priority general security interest in all present and future personal property pursuant to a general security agreement (subject to permitted encumbrances) and contained covenants and events of defaults customary to this type of facility. Costs associated with establishing the LOC were deferred and were to be amortized over a two year period.

During the second and third quarters of 2008, FNX borrowed and repaid a total of \$45,837 under the LOC. As at December 31, 2008, the Company did not have any amounts drawn down on the LOC.

As a result of the current global credit crisis, the cost of borrowing money has increased dramatically from that of April 1, 2008, the date when FNX entered into the LOC. The terms of the LOC required FNX to notify the lenders by January 31, 2009 of the Company's intention to renew the LOC for another year. Market conditions beyond FNX's control indicated that there would be significant costs to renew the LOC, including material extension fees and increases in both the standby fees and interest rates. Given the Company's existing cash balances and investments and the budgeted expenditure level for the year, FNX determined that the Company did not have a requirement to borrow any funds under the LOC to achieve its operating plan and budget for 2009. Accordingly, FNX elected not to renew and cancelled the LOC effective February 5, 2009.

### 13. Deferred revenue

	2008		
	Mining	DMC	Total
	\$	\$	\$
Balance – beginning of year	-	975	975
Received in year	400,000	827	400,827
Recognized in year	(5,575)	(825)	(6,400)
Balance – end of year	394,425	977	395,402
Current portion	(25,456)	(977)	(26,433)
	<u>368,969</u>	<u>-</u>	<u>368,969</u>

  

	2007		
	Mining	DMC	Total
	\$	\$	\$
Balance – beginning of year	-	-	-
Received in year	-	975	975
Recognized in year	-	-	-
Balance – end of year	-	975	975
Current portion	-	(975)	(975)
	<u>-</u>	<u>-</u>	<u>-</u>

On July 15, 2008, Gold Wheaton paid FNX up-front amounts totaling \$400,000, which amount was included in deferred revenue (note 7). Deferred revenue is recognized in earnings on the basis of the proportion of gold equivalent ounces sold to Gold Wheaton to the total gold equivalent ounces in the life of mine plans for the Gold Wheaton deposits.

Current and long-term deferred revenue amounts for Gold Wheaton were allocated based on the estimated production of gold equivalent units in the next year expressed as a percentage of total expected production over the life of the deposits subject to the Gold Wheaton agreement.

### 14. Income taxes

#### (a) Future tax liability

Future income tax liability at December 31, 2008 is comprised of the following:

	2008	2007
	\$	\$
Future income tax liabilities		
Properties	63,475	179,547
Investments	(860)	2,423
Other	(2,116)	(3,790)
	<u>60,499</u>	<u>178,180</u>

#### (b) Provision for income taxes

	2008	2007
	\$	\$
Current	(13,954)	12,415
Future	(114,926)	9,861
	<u>(128,880)</u>	<u>22,276</u>

Income tax expense differs from the amount that would have been computed by applying the combined federal and provincial statutory income tax rate of 34% (2007 - 36%) to earnings before income taxes. The reasons for the differences are a result of the following:

	<u>2008</u>	<u>2007</u>
	\$	\$
Earnings before income taxes	<u>(515,820)</u>	<u>132,223</u>
Expected tax at statutory rates	<u>(172,800)</u>	47,759
Future tax rate reductions	<u>28,034</u>	(25,408)
Ontario mining taxes	<u>(7,658)</u>	7,180
Resource allowance (deduction)	<u>(1,331)</u>	(3,731)
Non-taxable capital loss (gain)	<u>3,415</u>	(4,004)
Valuation allowance	<u>19,691</u>	-
Non-deductible/(non-taxable) income	<u>1,769</u>	480
	<u><u>128,880</u></u>	<u><u>22,276</u></u>

#### 15. Share capital and earnings (loss) per share

##### (a) Common shares issued and outstanding

	<u>2008</u>		<u>2007</u>	
	<u>Shares</u> <u># 000s</u>	<u>Amount</u> <u>\$</u>	<u>Shares</u> <u># 000s</u>	<u>Amount</u> <u>\$</u>
Balance – beginning of year	<u>84,564</u>	<u>567,700</u>	83,736	560,266
Stock options exercised	<u>313</u>	<u>2,814</u>	1,318	9,727
From contributed surplus (note 16)	-	<u>1,236</u>	-	4,518
Share cancellation	-	-	(490)	(6,811)
Balance – end of year	<u><u>84,877</u></u>	<u><u>571,750</u></u>	<u><u>84,564</u></u>	<u><u>567,700</u></u>

FNX is authorized to issue an unlimited number of common shares.

##### (b) Earnings (loss) per share

	<u>2008</u>	<u>2007</u>
<b>Net earnings (loss) available to shareholders (\$)</b>		
Basic and diluted	<u><u>(388,540)</u></u>	<u><u>109,947</u></u>
<b>Weighted average shares outstanding (#000s)</b>		
Basic	<u>84,714</u>	84,026
Effect of dilutive stock options	-	646
Diluted	<u><u>84,714</u></u>	<u><u>84,672</u></u>
Stock options excluded from dilution	<u><u>1,226</u></u>	<u><u>527</u></u>
<b>Earnings (loss) per share</b>		
Basic	<u><u>(\$4.59)</u></u>	<u><u>\$1.31</u></u>
Diluted	<u><u>(\$4.59)</u></u>	<u><u>\$1.30</u></u>



**16. Contributed surplus**

	<u>2008</u>	<u>2007</u>
	\$	\$
Balance – beginning of year	9,816	7,710
Stock-based compensation	5,161	2,864
Transfer of exercised options to share capital	(1,236)	(4,518)
Receipt and cancellation of shares	-	3,760
Balance – end of year	<u>13,741</u>	<u>9,816</u>

The following table summarizes information regarding FNX's stock-based compensation expense for the years ended December 31, 2008 and 2007:

	<u>2008</u>	<u>2007</u>
	\$	\$
Stock options	5,161	2,864
Deferred share units	(1,105)	563
Stock-based compensation expense	<u>4,056</u>	<u>3,427</u>

FNX has two stock-based compensation plans: a stock option plan (the “**Option Plan**”); and a deferred share unit plan (the “**DSU Plan**”). The Board of Directors has implemented a policy requiring all directors and the Chief Financial Officer to hold a minimum of 5,000 common shares and/or deferred share units (“**DSUs**”) and for the Chief Executive Officer to hold a minimum equal to two times his base salary in common shares and/or DSUs, within five years of their appointment to qualify for membership on the Board or appointment as the Chief Executive Officer or Chief Financial Officer of the Company.

**(a) Stock option plan**

The maximum number of FNX common shares that may be reserved for issuance under the Option Plan is 5% of all issued and outstanding FNX common shares at the time of the grant (on a non-diluted basis). As at December 31, 2008, an aggregate of 2.1 million FNX common shares (representing approximately 2.5% of the issued and outstanding FNX common shares) were reserved for issuance under the Option Plan.

Options may only be granted to directors, officers, employees, insiders and other specified service providers and, subject to the discretion of the Board of Directors or its compensation committee and the terms of certain employment agreements, in the event that an optionee ceases to be an eligible optionee, no further options previously granted to such optionee will vest and the optionee will be entitled to exercise vested options for a period of 90 days (or one year in the event of the optionee’s death).

The exercise price of each option is determined on the basis of the market price at the time the option is granted but may not be less than the closing price of a FNX common share on the Toronto Stock Exchange on the last trading day before the day the option is granted. The shares purchased on the exercise of an option must be paid for in full at the time of exercise.

Options cannot have a term exceeding five years unless the option expires in a blackout period, in which case the options will be exercisable for a period of five days after the blackout period has ended.



Options granted prior to 2004 vested at the discretion of FNX's Board of Directors, while options granted in 2004 vested 50% after one year from the date of grant with the balance vesting after two years from the date of grant. Options granted on or after January 1, 2005, have a five year term and vest 33.3% on the anniversary date of each of the first three years following the grant date.

Subject to the terms of certain employment agreements, in the event of an Acceleration Event, as defined in the Option Plan to include, among other things, the acquisition of more than 50% of FNX's outstanding voting securities and a sale of substantially all of the assets of FNX, the Board of Directors may permit optionees to exercise options regardless of any vesting provisions.

Except in specified circumstances, options are not assignable and are non-transferable. A reduction in the exercise price of an option or an extension of the term of an option for an insider requires the approval of disinterested shareholders.

The following table summarizes information regarding FNX's outstanding and exercisable stock options as at December 31, 2008:

Range of exercise prices per share	Outstanding			Exercisable	
	Shares	Weighted average months remaining	Weighted average exercise price per share	Shares	Weighted average exercise price per share
5.04	13	8	5.04	13	5.04
7.40	203	15	7.40	203	7.40
8.15 to 12.99	369	31	11.20	236	10.92
13.00	62	24	13.00	62	13.00
13.01 to 13.83	158	27	13.64	130	13.65
14.01 to 18.04	130	32	15.69	78	15.66
18.05 to 29.66	893	49	25.03	85	26.55
30.20 to 34.65	45	41	31.20	16	31.16
37.53	257	47	37.53	86	37.53
	<u>2,130</u>			<u>909</u>	

The following table summarizes information regarding FNX's stock options as at and for the years ended December 31, 2008 and 2007:

	2008		2007	
	Shares	Weighted average exercise price per share	Shares	Weighted average exercise price per share
	# 000s	\$	# 000s	\$
Balance – beginning of year	1,959	18.07	2,672	9.15
Granted	937	23.61	677	32.09
Exercised	(313)	9.00	(1,318)	7.38
Expired	(50)	8.15	-	-
Forfeited/Cancelled	(403)	25.25	(72)	14.77
Balance – end of year	<u>2,130</u>		<u>1,959</u>	



For purposes of stock-based compensation, the fair value of each option was estimated on the date of grant using the Black-Scholes option pricing model with the year to date weighted average assumptions used for grants as follows: dividend yield of 0% (2007 - 0%), expected volatility of 45% (2007 - 44%), risk-free interest rate of 3.1% (2007 - 4.0%) and expected life of 36 months (2007 - 36 months).

**(b) Deferred share units plan**

The purpose of the DSU Plan is to promote a greater alignment of interests between shareholders and Directors and executive employees by providing a mechanism to permit linking a portion of Director and executive employee compensation to the future value of FNX's common shares. The DSU Plan is only eligible to Directors and executive employees of FNX and is to allow Directors and executive employees the choice to receive, in increments of 25%, up to 100% of retainer fees, in the case of Directors, and annual incentive awards, in the case of executive employees, in the form of DSUs rather than by way of an immediate cash payment. Under the terms of the DSU Plan, the number of DSUs granted is based upon the fair market value of FNX's common shares at that time. DSUs can only be paid out in cash and are only paid out upon the Director's or executive employee's death or resignation from the Board or termination from the Company. Included in accrued liabilities is \$151 related to 54,650 DSUs.

**17. Other expenses (income)**

	<u>2008</u>	<u>2007</u>
	\$	\$
Foreign exchange	(17,377)	15,092
Loss on mark-to-market of Gold Wheaton note receivable (note 7)	14,846	-
Gain on disposal of investments	(8,461)	(15,480)
Provision for doubtful accounts (note 22(a))	4,242	-
Gain on Gold Wheaton shares acquired (note 7)	(2,700)	-
Interest income	(2,505)	(4,288)
Loss (gain) on investments held for trading	710	260
Interest on bank indebtedness	374	-
Miscellaneous	57	(108)
	<u>(10,814)</u>	<u>(4,524)</u>

**18. Supplementary cash flow information**

	<u>2008</u>	<u>2007</u>
	\$	\$
Net change in non-cash working capital		
Accounts receivables	51,232	(361)
Inventory	1,744	(626)
Prepaid and other assets	(378)	(724)
Accounts payable and accrued liabilities	(35,442)	30,952
Deferred revenue	(5,575)	-
	<u>11,581</u>	<u>29,241</u>
Other information		
Interest paid	374	-
Income and resource taxes paid	7,555	10,988



**19. Related party transactions**

Upon signing the Gold Wheaton agreement on July 15, 2008, Gold Wheaton became a significantly-influenced investee of FNX and thus became a related party. All transactions conducted with Gold Wheaton are measured at the exchange amount. Sales to Gold Wheaton in 2008 totaled \$15,232, and amounts receivable from Gold Wheaton are \$8,594 as at December 31, 2008.

INV terminated the January 1, 2006 administrative services agreement between FNX and INV effective December 31, 2007 and, other than one common director, FNX and INV do not have any common directors, officers or employees. Accordingly, INV ceased to be a related party at that time. There have been no related party transactions in fiscal 2008.

**20. Segmented information**

FNX has two operating segments: Mining and DMC, the latter being acquired on October 15, 2007.

The Mining segment operates in one geographic location, Ontario, Canada, and is responsible for mineral exploration, development and mining.

The DMC segment, comprised of the Canadian mining services division and DMC USA, provides mining and civil underground construction services in Canada and the United States.

The following tables summarize information regarding FNX's operations by geographic location as at and for the years ended December 31, 2008 and 2007.

	<b>2008</b>		
	<b>Canada</b>	<b>United States</b>	<b>Total</b>
	\$	\$	\$
Operating revenues	<b>284,341</b>	<b>93,721</b>	<b>378,062</b>
Operating expenses			
Expenses, excluding depreciation and amortization	<b>240,120</b>	<b>89,481</b>	<b>329,601</b>
Depreciation and amortization	<b>54,470</b>	<b>2,534</b>	<b>57,004</b>
Asset impairments	<b>496,069</b>	<b>5,421</b>	<b>501,490</b>
Other expenses (income)	<b>1,559</b>	<b>4,228</b>	<b>5,787</b>
Total operating expenses	<b>792,218</b>	<b>101,664</b>	<b>893,882</b>
Earnings before taxes	<b>(507,877)</b>	<b>(7,943)</b>	<b>(515,820)</b>
Property, plant and equipment	<b>423,994</b>	<b>11,120</b>	<b>435,114</b>
Capital expenditures	<b>159,373</b>	<b>8,378</b>	<b>167,732</b>

	2007		
	Canada	United States	Total
	\$	\$	\$
Operating revenues	290,621	31,422	322,043
Operating expenses			
Expenses, excluding depreciation and amortization	121,912	28,169	150,081
Depreciation and amortization	28,331	455	28,786
Other expenses (income)	10,980	(27)	10,953
Total operating expenses	161,223	28,597	189,820
Earnings (loss) before taxes	129,398	2,825	132,223
Property, plant and equipment	803,332	12,044	815,376
Capital expenditures	209,876	161	210,037

## 21. Capital management

The Company's objectives when managing capital are to:

- ensure that the Company has the financial capacity to support its operations throughout the metals cycles;
- ensure that the Company has the capital and capacity to support the current mine development plans and the long-term growth strategy; and
- provide investors with superior returns over time.

The Company's capital structure reflects the requirements of a company focused on significant growth in a capital intensive industry that experiences lengthy development lead times, as well as risks associated with capital costs and timing of project completion due to factors that are beyond the Company's control, including the availability of resources, the issuance of necessary permits, costs of various inputs and the volatility of metals prices.

The adequacy of the Company's capital structure is assessed on an ongoing basis and adjusted as necessary after taking into consideration the Company's strategy, the metals markets, the mining industry, economic conditions and the associated risks.

In order to maintain or adjust its capital structure, the Company may adjust its capital spending, issue new shares, purchase shares for cancellation pursuant to normal course issuer bids or issue new debt or repay existing debt.

Although the Company has not historically utilized debt facilities as part of its capital management program, as at April 1, 2008, FNX finalized a US\$100 million LOC with a group of banks to assist in managing working capital and possible adverse currency and commodity price fluctuations. The Company cancelled the LOC in February 2009 (note 12).

## 22. Financial instruments

The carrying amount of the Company's financial instruments, which include cash and cash equivalents, accounts receivable, investments, reclamation deposits and accounts payable and accrued liabilities, approximate their fair values due to the short-term maturities of these financial instruments.



The carrying value of the Gold Wheaton note receivable is marked-to-market at each period end which approximates fair value.

As described below, the Company has exposure to credit risk, liquidity risk, foreign exchange risk and market risk from its use of financial instruments. In addition, other quantitative disclosures regarding these risks are included throughout these consolidated financial statements.

**(a) Credit risk**

Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its contractual obligations. The Company's maximum counterparty credit exposure at year end, which approximates fair value, consists of the following:

	<b>Carrying amount</b>	
	<b>December 31 2008</b>	December 31 2007
	\$	\$
Cash and cash equivalents	129,561	35,160
Accounts receivable	59,324	103,257
Reclamation deposits	6,485	6,485
	<u>195,370</u>	<u>144,902</u>

FNX has historically and continues to invest all surplus cash resources in conservative deposits with major Canadian chartered banks.

*(i) Trade and accounts receivable*

Except for 50% of the gold, platinum and palladium metal contained in ore mined and shipped from certain of the mineral deposits at the Levack Complex and the Podolsky Mine which is sold to Gold Wheaton, FNX's Mining segment sells all of the other metals contained in the ore it produces from the Levack Complex and Podolsky to Vale Inco. Accordingly, Vale Inco and Gold Wheaton are the only two customers of the Mining segment.

During 2008, 41% of DMC revenues were derived from one client, SRA, at its sole producing operation, the Mid-Tennessee Zinc ("MTZ") mine. On October 1, 2008, SRA announced by news release that "it is in discussion with significant holders of its Series 1 Notes to restructure aspects of the company's senior secured debt". On October 9, 2008, SRA announced by news release that it had placed the MTZ mine on care and maintenance until such time "when zinc prices improve and funding becomes available". In light of SRA's financial difficulties, the precipitous decline in metal prices including zinc, and the recent turmoil in the debt and equity markets, a provision for doubtful accounts for the full \$4,242 amount owed by SRA to DMC USA was charged to earnings as at September 30, 2008 (note 17) and was written off at December 31, 2008.



The maximum exposure to credit risk for trade accounts receivables included in the total accounts receivable balance at the reporting date by customer type was:

	<b>Carrying amount</b>	
	<b>December 31 2008</b>	December 31 2007
	<u>\$</u>	<u>\$</u>
Mining Operations - Vale Inco	<b>34,750</b>	62,803
Mining Operations - Gold Wheaton	<b>8,594</b>	-
DMC - Vale Inco	<b>5,598</b>	7,760
DMC - SRA	-	12,242
DMC - Other contracts	<b>9,297</b>	20,158
	<b><u>58,239</u></b>	<u>102,963</u>

The Company establishes an allowance for doubtful accounts that represents its estimate of incurred losses in respect of trade and other receivables. The main components of this allowance are a specific provision that relates to individually significant exposures, and a general provision established for groups of similar assets in respect of losses that have been incurred but not yet identified. The general provision is determined based on historical data of payment statistics for similar financial assets. As at the reporting date, the balance in the allowance for doubtful accounts was \$nil (December 31, 2007 - \$nil).

The aging of trade accounts receivable at the reporting date was:

	<u>Gross</u>	<u>Allowance</u>
	<u>\$</u>	<u>\$</u>
Not past due	<b>54,816</b>	-
Past due 0-30 days	<b>1,385</b>	-
Past due 31-120 days	<b>2,038</b>	-
More than one year	-	-
	<b><u>58,239</u></b>	<u>-</u>

*(ii) Investments*

Investment certificates are maintained on deposit with certain investment dealers.

*(iii) Guarantees*

The Company has provided certain financial guarantees to the Ontario Government and Vale Inco with respect to estimated future reclamation expenditures. Letters of credit covering the estimated expenditures are maintained with a major Canadian chartered bank. In the normal course of business, certain of DMC's contracts require DMC to provide the customer with a performance or surety bond from an insurance company. The Company has provided guarantees to an insurance company that has issued surety bonds in the United States on behalf of DMC. As at December 31, 2008, the aggregate principal amount of the surety bonds which the Company has guaranteed totaled \$13,033 (US\$10,700).

**(b) Liquidity risk**

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due. The Company's approach to managing liquidity is to ensure that, as far as possible, it will always have sufficient liquidity to meet its liabilities when due, under both

normal and stressed conditions, without incurring unacceptable losses or risking damage to the Company's reputation. FNX strives to maintain sufficient financial liquidity at all times in order to participate in investment opportunities as they arise, as well as to withstand sudden adverse changes in economic circumstances. Management forecasts cash flows for its current and subsequent fiscal periods to identify financing requirements which could be addressed through a combination of credit facilities and access to equity markets.

**(c) Price risk**

Price risk is the risk that changes in market prices, such as foreign exchange rates, commodity prices, interest rates and equity prices will affect the Company's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimizing the return on risk.

*(i) Currency risk*

Fluctuations in the Canadian/US dollar exchange rate can impact FNX's earnings and cash flows. Most of FNX's revenues are denominated in US dollars, whereas certain of FNX's obligations and operating expenses are denominated in Canadian dollars and other foreign currencies. If the value of the Canadian dollar increases relative to the US dollar, FNX's results of operations, financial condition and liquidity could be materially adversely affected. The Company converts a majority of its US dollars into Canadian dollars upon receipt; however, its self-sustaining US subsidiary, DMC USA, maintains sufficient cash on hand in order to fund internal operations.

Management estimates each \$0.10 change in the value of the Canadian/US dollar exchange rate impacts US dollar denominated financial instruments at December 31, 2008 and earnings before tax by approximately \$2,700.

*(ii) Commodity Prices and interest rates*

The profitability of the Company will be significantly affected by changes in the market price of nickel and copper and to a lesser extent by cobalt, platinum, palladium and gold. The level of interest rates, the rate of inflation, world supply and demand of base metals and precious metals and stability of exchange rates can all cause significant fluctuations in base metal and precious metal prices. Such external economic factors are in turn influenced by changes in international investment patterns and monetary systems and political developments. The price of base metals and precious metals has fluctuated widely in recent years, and future serious price declines could cause continued commercial production to be impracticable. Depending on the price of base metals and precious metals, cash flow from mining operations may not be sufficient to cover operating costs. Any figures for reserves and resources presented by FNX will be estimates and no assurance can be given that the anticipated tonnages and grades will be achieved or that the indicated level of recovery will be realized. Market fluctuations and the price of base metals and precious metals may render reserves and resources uneconomic. Moreover, short-term operating factors relating to the reserves, such as the need for orderly development of the ore bodies or the processing of new or different grades of ore, may cause a mining operation to be unprofitable in any particular accounting period.

The crushed ore shipped to Vale Inco is sold to Vale Inco or Gold Wheaton (for the relevant gold equivalent ounces) under terms that provide for final prices that are determined by quoted market prices in a period subsequent to the date of sale. Variations from the



provisionally priced sales are recognized as revenue adjustments as they occur until the price is finalized. Management estimates that for each US\$1.00 change in the price per pound of nickel or US\$0.25 change in the price per pound of copper would impact the December 31, 2008 trade accounts receivable from Vale Inco and Gold Wheaton and earnings before tax by approximately \$2,700 and \$4,700, respectively.

Gold equivalents are sold to Gold Wheaton at US\$400 per ounce of gold equivalent plus the related portion of the deferred revenue.

(iii) *Market risk*

The value of certain of the Company's financial instruments will fluctuate as a result of changes in market prices, therefore the Company is subject to market risk. The extent to which the Company is exposed to market risk is outlined as follows:

	<b>Fair value</b>	
	<b>December 31 2008</b>	December 31 2007
	<b>\$</b>	<b>\$</b>
Available-for-sale investments	<b>4,009</b>	35,603
Note receivable	<b>35,154</b>	-
Equity investment in Gold Wheaton	<b>180,466</b>	-
	<b>219,629</b>	<b>35,603</b>

FNX has not entered into any hedging agreements in respect of metal prices or foreign exchange rates at this time. Such contracts would prevent losses in situations where the price changed adversely and would prevent gains in situations where the price changed favourably.

**23. Commitments and other**

**(a) Operating leases**

The Company is committed to payments under operating leases for office space and equipment. Annual payments are as follows:

	<b>\$</b>
2009	<b>2,525</b>
2010	<b>2,301</b>
2011	<b>2,100</b>
2012	<b>1,817</b>
2013	<b>1,780</b>
and thereafter	<b>2,894</b>
	<b>13,417</b>

**24. Fair value of financial instruments**

The carrying amount of accounts receivable and current liabilities approximate their fair value due to the short-term maturities of these instruments. Available-for-sale investments are carried at fair value and the Gold Wheaton note receivable is marked-to-market as required for derivative instruments. FNX does not currently have any other derivative instruments.

## **25. Contingencies and litigation**

### **(a) DMC**

In the normal course of business DMC enters into agreements that contain indemnification commitments and may contain features that meet the expanded definition of guarantees. The terms of these indemnification agreements will vary based on the contract and typically do not provide for a limit on the maximum potential liability. The Company has not made any payments under such indemnifications and no amounts have been accrued in the financial statements with respect to these indemnification commitments.

DMC is involved from time to time in litigation which arises in the normal course of operations. With respect to these claims, the Company believes the claims are without merit and that any impact on the operations of the Company will either not be material or a sufficient provision has been made. The Company's policy is to recognize the losses, if any, on any such litigation when the outcome becomes reasonably determinable.

### **(b) Mining**

The payable metals Vale Inco is required to pay for ore shipped by FNX are determined based on the metal which Vale Inco is able to recover from the various ore deposits. This will vary depending on the particular metallurgical composition of each ore deposit as determined by metallurgical testing of the various ore deposits. There are several different final payable metals terms for the various ore deposits at McCreedy West to reflect the differences in the metallurgical composition of the ore deposits.

Interim processing costs terms and interim payable metals terms, based on preliminary and limited metallurgical testing, have been established for the Levack and Podolsky mines. Extensive metallurgical testing has been and will continue to be conducted in order to determine final payable metals terms and processing costs terms for both mines. Management anticipates this to be completed during 2009.

Podolsky's interim payable metals and processing costs terms are effective for all ore shipped from September 2007, the date ore shipments commenced from the Podolsky Mine, until final payable metals and processing costs terms are determined. FNX's pre-production revenue credits accrued at December 31, 2007 were previously based on management's estimated payable metals and processing costs terms. The pre-production revenue credits were revalued using the new interim payable metals and processing costs terms, resulting in a \$1,370 increase in the carrying value of the Podolsky Mine being recorded in the first quarter of 2008 as these amounts were previously offset against the carrying value.

Levack's revised interim payable metals and processing costs terms replaced the Levack interim provisional terms that had been used up to December 31, 2007, which were based on those at McCreedy West. Levack's revised interim terms are effective from January 1, 2008 until final payable metals and processing costs terms are determined, which management anticipates to be in place during 2009, and are less favourable to FNX than the previous interim terms. Once final payable metals and processing costs terms are determined, it is expected that they will also be applied to ore shipped from Levack in 2006 and 2007. The Company cannot, at this time, determine the amount, if any, of such adjustment. Depending on the outcome of the final payable metals and costs terms there may be a material increase or decrease in payable metals and/or processing costs to be recorded.



Pre-production revenue credits for the LFD are based upon estimated metals, pricing and processing costs.

**26. Subsequent event**

On March 5, 2009, Gold Wheaton announced the closing of an equity financing in which 460 million units were issued (including 60 million units to the underwriters as an over-allotment option) at \$0.25 per unit for gross proceeds of \$115,000. Each unit consists of one common share and one-half common share purchase warrant.

As a result of this transaction, FNX's equity interest in Gold Wheaton was reduced from 38% to 26% and FNX will be required to report a dilution loss at March 31, 2009 of approximately \$23,000.