

**Condensed Interim Consolidated Financial Statements**  
**ESSAR STEEL ALGOMA INC.**  
(Unaudited)  
For the three-month period ended June 30, 2011

**ESSAR Steel Algoma Inc.**  
**Condensed Interim Consolidated Statement of Comprehensive Income**  
*(Unaudited)*  
Expressed in millions of Canadian dollars

	Three months ended June 30, 2011	Three months ended June 30, 2010 <small>(Note 2 and 27)</small>
<b>Revenue (Note 6)</b>	<b>\$ 566.0</b>	<b>\$ 475.7</b>
<b>Operating expenses</b>		
Cost of sales (Note 7)	483.3	434.4
Administrative and selling (Note 8)	21.9	19.1
<b>Income from operations</b>	<b>60.8</b>	<b>22.2</b>
Finance income	(0.1)	-
Finance costs	21.0	21.3
Foreign exchange gain	(2.2)	(40.7)
	<b>18.7</b>	<b>(19.4)</b>
<b>Income before income taxes</b>	<b>42.1</b>	<b>41.6</b>
Income taxes (Note 20)	8.9	20.5
<b>Net income</b>	<b>33.2</b>	<b>21.1</b>
<b>Other comprehensive income, net of income tax</b>		
Unrealized foreign exchange (loss) gain on translation to presentation currency	(0.1)	13.1
<b>Total comprehensive income</b>	<b>\$ 33.1</b>	<b>\$ 34.2</b>

**ESSAR Steel Algoma Inc.**  
**Condensed Interim Consolidated Statements of Changes in Shareholder's (Deficit) Equity**  
*(Unaudited)*  
Expressed in millions of Canadian dollars

	Capital Stock (Note 22)	Contributed surplus (Note 23)	Accumulated other comprehensive income (loss)	Deficit	Total shareholder's equity
Balance at April 1, 2011	\$ 490.4	\$ 58.2	\$ (22.7)	\$ (593.6)	\$ (67.7)
Net income				33.2	33.2
Other comprehensive income (loss)					
Foreign exchange (loss) on translation to presentation currency			(0.1)		(0.1)
<b>Balance at June 30, 2011</b>	<b>\$ 490.4</b>	<b>\$ 58.2</b>	<b>\$ (22.8)</b>	<b>\$ (560.4)</b>	<b>\$ (34.6)</b>

	Capital Stock (Note 22)	Contributed surplus (Note 23)	Accumulated other comprehensive income (loss)	Deficit	Total shareholder's equity
Balance at April 1, 2010 (Note 27)	\$ 490.4	\$ 58.2	\$ -	\$ (289.6)	\$ 259.0
Net income				21.1	21.1
Other comprehensive income (loss)					
Foreign exchange gain on translation to presentation currency			13.1		13.1
<b>Balance at June 30, 2010 (Note 27)</b>	<b>\$ 490.4</b>	<b>\$ 58.2</b>	<b>\$ 13.1</b>	<b>\$ (268.5)</b>	<b>\$ 293.2</b>

See accompanying notes to the condensed interim consolidated financial statements

**ESSAR Steel Algoma Inc.****Condensed Interim Consolidated Statement of Financial Position***(Unaudited)*

Expressed in millions of Canadian dollars

	<u>June 30,</u> <u>2011</u>	<u>March 31,</u> <u>2011</u> <small>(Note 2 and 27)</small>	<u>April 1,</u> <u>2010</u> <small>(Note 2 and 27)</small>
<b>Assets</b>			
<b>Current</b>			
Cash	\$ 15.9	\$ 5.7	\$ 40.2
Accounts receivable (Note 9)	221.7	160.4	203.5
Income taxes receivable	1.6	2.5	21.4
Loan receivable from related party (Note 25)	11.1	11.0	-
Inventories (Note 10)	286.8	278.4	289.3
Prepaid expenses	6.5	4.5	7.4
<b>Total current assets</b>	<u>543.6</u>	<u>462.5</u>	<u>561.8</u>
<b>Non-current</b>			
Property, plant and equipment, net (Note 11)	1,238.0	1,277.8	1,475.9
Intangible assets, net (Note 12)	86.7	90.6	111.1
Other assets	1.0	1.2	2.0
Deferred income tax assets	1.0	1.4	1.5
<b>Total non-current assets</b>	<u>1,326.7</u>	<u>1,371.0</u>	<u>1,590.5</u>
<b>Total assets</b>	<u>\$ 1,870.3</u>	<u>\$ 1,833.5</u>	<u>\$ 2,152.3</u>
<b>Liabilities and shareholder's equity</b>			
<b>Current</b>			
Bank indebtedness (Note 13)	\$ 168.2	\$ 184.5	\$ 92.2
Accounts payable and accrued liabilities (Note 14)	197.5	181.4	194.4
Current portion of provisions (Note 18)	1.1	1.1	1.3
Current portion of other long term liabilities (Note 19)	0.9	0.9	0.9
<b>Total current liabilities</b>	<u>367.7</u>	<u>367.9</u>	<u>288.8</u>
<b>Non-current</b>			
Long term debt (Note 15)	739.7	742.8	776.5
Accrued pension liability	304.9	308.1	262.2
Accrued post-employment benefit obligation	444.9	440.9	404.8
Provisions (Note 18)	3.8	3.8	3.5
Other long term liabilities (Note 19)	1.4	1.6	2.4
Deferred income tax liabilities	42.5	36.1	155.1
<b>Total non-current liabilities</b>	<u>1,537.2</u>	<u>1,533.3</u>	<u>1,604.5</u>
<b>Total liabilities</b>	<u>1,904.9</u>	<u>1,901.2</u>	<u>1,893.3</u>
<b>Shareholder's equity</b>			
Accumulated other comprehensive loss	(22.8)	(22.7)	-
Deficit	(560.4)	(593.6)	(289.6)
	<u>(583.2)</u>	<u>(616.3)</u>	<u>(289.6)</u>
Capital stock (Note 22)	490.4	490.4	490.4
Contributed surplus (Note 23)	58.2	58.2	58.2
	<u>(34.6)</u>	<u>(67.7)</u>	<u>259.0</u>
<b>Total liabilities and shareholder's equity</b>	<u>\$ 1,870.3</u>	<u>\$ 1,833.5</u>	<u>\$ 2,152.3</u>

See accompanying notes to the condensed interim consolidated financial statements

**ESSAR Steel Algoma Inc.**  
**Condensed Interim Consolidated Statements of Cash Flows**

*(Unaudited)*

Expressed in millions of Canadian dollars

	<b>Three months ended June 30, 2011</b>	<b>Three months ended June 30, 2010</b>
		(Note 2 and 27)
<b>Operating activities</b>		
<b>Net income</b>	<b>\$ 33.2</b>	<b>\$ 21.1</b>
Adjustments and items not affecting cash:		
Depreciation on property, plant and equipment	42.5	47.9
Amortization of intangible assets and depreciation of non-productive property, plant and equipment	5.6	5.5
Deferred income tax expense	6.8	12.4
Current income tax expense	2.1	8.1
Pension expense in excess of current funding	(2.3)	(4.9)
Unrealized foreign exchange loss (gain) on accrued pension liability	0.5	(12.0)
Post-employment benefit expense in excess of payments	4.0	3.5
Unrealized foreign exchange loss (gain) on accrued post-employment benefit obligation	2.2	(19.1)
Finance costs	21.0	21.3
Loss on disposal of property, plant and equipment	-	0.7
Unrealized foreign exchange loss (gain) on deferred income taxes	0.1	(7.3)
Other	1.5	0.4
	<u>117.2</u>	<u>77.6</u>
Changes in non-cash operating working capital (Note 24)	(59.5)	0.1
Cash generated from operating activities before interest and taxes	<u>57.7</u>	<u>77.7</u>
Interest paid	(19.8)	(21.3)
Income taxes recovered (paid)	1.2	(0.4)
<b>Cash generated from operating activities</b>	<u><u>39.1</u></u>	<u><u>56.0</u></u>
<b>Investing activities</b>		
Acquisition of property, plant and equipment	(12.1)	(14.0)
Acquisition of intangible asset	(1.0)	(0.6)
Loan receivable from related party (Note 25)	(0.1)	(11.1)
<b>Cash used for investing activities</b>	<u><u>(13.2)</u></u>	<u><u>(25.7)</u></u>
<b>Financing activities</b>		
Bank indebtedness, net	(15.4)	(26.2)
Other	(0.1)	(0.4)
<b>Cash used for financing activities</b>	<u><u>(15.5)</u></u>	<u><u>(26.6)</u></u>
<b>Effect of exchange rate changes on cash</b>	<u>0.2</u>	<u>2.5</u>
<b>Cash</b>		
Change	10.2	6.2
Opening balance	5.7	40.2
<b>Ending balance</b>	<u><u>\$ 15.9</u></u>	<u><u>\$ 46.4</u></u>

See accompanying notes to the condensed interim consolidated financial statements

**ESSAR STEEL ALGOMA INC.**

**Notes to the Condensed Interim Consolidated Financial Statements (Unaudited)**

**Expressed in millions of Canadian dollars**

**1. GENERAL INFORMATION**

Essar Steel Algoma Inc. (the "Company") is an integrated steel producer with its active operations located entirely in Canada. The Company produces sheet and plate products that are sold primarily in Canada and the United States. The Company is incorporated under the laws of Ontario, Canada. The Company's ultimate parent company is Essar Global Limited. The address of the Company's registered office is 105 West Street, Sault Ste. Marie, Ontario, P6A 7B4, Canada. The condensed interim consolidated financial statements of the Company for the three month period ended June 30, 2011, are comprised of the Company and its subsidiaries.

**2. BASIS OF PRESENTATION**

**Statement of compliance**

The Company has prepared the financial statements for the first time using accounting policies consistent with International Financial Reporting Standards ("IFRS") issued by the International Accounting Standards Board (the "IASB").

The Company prepared these condensed interim consolidated financial statements for the three month period ended June 30, 2011 in accordance with IAS 34 - Interim Financial Reporting, IFRS 1 – First-time Adoption of IFRS and the accounting policies that the Company expects to adopt as at and for the year ending March 31, 2012.

The Company's annual consolidated financial statements, formerly prepared in accordance with previous Canadian Generally Accepted Accounting Principles ("previous CGAAP"), differ from IFRS in some areas. In preparing the IFRS statements, the Company amended certain accounting and valuations methods that had been applied under previous CGAAP. The 2010 and 2011 comparative figures have been restated to reflect these adjustments.

The Company's date of transition was April 1, 2010 ("Transition Date"). Reconciliations and descriptions of the effect of transition from previous CGAAP to IFRS on the Company's consolidated financial statements are provided in Note 27.

**Basis of presentation**

The condensed interim consolidated financial statements have been prepared on a going concern assumption using historical cost basis and financial instruments that are measured at fair values, as explained in the accounting policies below.

**Functional and presentation currency**

The Company's functional currency is the United States dollar ("US dollar"). The US dollar is the currency of the primary economic environment in which the Company and subsidiaries operates. The items included in the condensed interim consolidated financial statements are measured using the US dollar.

The condensed interim consolidated financial statements are presented in millions of Canadian dollars ("C\$").

**ESSAR STEEL ALGOMA INC.**  
**Notes to the Condensed Interim Consolidated Financial Statements (Unaudited)**  
**Expressed in millions of Canadian dollars**

**3. SIGNIFICANT ACCOUNTING POLICIES**

**Basis of consolidation**

These condensed interim consolidated financial statements include the accounts of the Company and its controlled subsidiaries. Control exists when the Company has the power, directly or indirectly, to govern the financial and operating policies of an entity/arrangement so as to obtain benefits from its activities. The Company's interest in all its subsidiaries is 100%.

Significant subsidiaries:

Name of Subsidiary	Principal Business	Place of Incorporation and Operation	Proportion of Ownership and Voting Power held by the Company		
			June 30, 2011	March 31, 2011	April 1, 2010
<b>Essar Steel Algoma USA Inc.</b>	Commission based steel sales in United States	Incorporated: Delaware, USA. Head Office: Chicago, Illinois, USA Operations: USA	100%	100%	100%
<b>Cannelton Iron Ore Company</b>	Inactive	Incorporated: Delaware, USA	100%	100%	100%

Intercompany balances and transactions and any unrealized income and expenses arising from intercompany transactions are eliminated in preparing these condensed interim consolidated financial statements.

**Foreign currency translations**

*Functional and presentation currency*

The Company and its subsidiaries functional currency is the US dollar because this is the currency of the primary economic environment in which the Company operates. The Company uses the Canadian dollar as its presentation currency. In accordance with IFRS, all amounts presented in these consolidated financial statements are translated into Canadian dollars using the current rate method whereby all revenues, expenses and cash flows are translated at the average rate that was in effect during the period and all assets and liabilities are translated at the following end of the period prevailing closing rates:

Period End Date	Canadian Dollar per US \$1.00
June 30, 2011	\$0.9645
March 31, 2011	\$0.9696
June 30, 2010	\$1.0646
April 1, 2010	\$1.0158

Equity transactions have been translated at historical rates. The resulting net translation adjustment has been recorded in comprehensive income (loss) for the period.

**ESSAR STEEL ALGOMA INC.**  
**Notes to the Condensed Interim Consolidated Financial Statements (Unaudited)**  
**Expressed in millions of Canadian dollars**

**3. SIGNIFICANT ACCOUNTING POLICIES** *(continued)*

*Foreign exchange transactions*

Transactions in currencies other than the Company's functional currency are recognized at the rates of exchange prevailing at the dates of the transactions. At the end of each reporting period, monetary items denominated in foreign currencies are translated at the rates prevailing at that date. Non-monetary items that are measured in terms of historical cost are not re-translated. Exchange gains or losses arising from translations of foreign currency monetary assets, liabilities and transactions are recorded in foreign exchange loss (gain) in the condensed interim consolidated statements of comprehensive income.

**Financial Instruments**

*Recognition and Measurement*

Financial assets and financial liabilities, including derivatives, are recognized on the consolidated statement of financial position when the Company becomes a party to the contractual provisions of a financial instrument or non-financial derivative contract. All financial instruments are required to be measured at fair value on initial recognition. Transaction costs that are directly attributable to financial assets and financial liabilities other than those at fair value through net earnings are added to or deducted from the fair value of the financial assets or financial liabilities as appropriate on initial recognition.

The Company classifies financial instruments, at the time of initial recognition, according to their characteristics and management's choices and intentions related thereto for the purposes of ongoing measurement.

*Impairment*

Financial instruments are examined to determine if any impairment has occurred. An impairment loss is recognized when the carrying amount of the financial instrument exceeds the present value of estimated future cash flows discounted at the financial asset's original effective interest rate. Impairment losses are recognized in net earnings for the period.

*Classification and Measurement*

Classification choices for financial assets and liabilities include:

- a) Fair value through profit or loss ("FVTPL")  
Financial instruments are classified as FVTPL when the financial instrument is either held for trading or designated as such upon initial recognition. Financial assets are classified as held for trading if acquired principally for the purpose of selling in the near future or it has been part of an identified portfolio of financial instruments that the Company manages together and has a recent actual pattern of short-term profit-making. Derivatives are also categorized as held for trading unless they are designated as hedges. Financial instruments classified as FVTPL are measured at fair value, with changes in fair value recorded in net earnings in the period in which they arise.
- b) Loans and receivables  
Loans and receivables are financial assets with fixed or determinable payments that are not quoted in an active market. Subsequent to initial recognition, loans and receivables are measured at amortized cost using the effective interest method, less any impairment losses, with gains and losses recognized in net earnings in the period that the asset is derecognized or impaired.
- c) Other liabilities  
Subsequent to initial recognition, other financial liabilities are measured at amortized cost using the effective interest method with gains and losses recognized in net earnings in the period that the liability is derecognized.

**ESSAR STEEL ALGOMA INC.**  
**Notes to the Condensed Interim Consolidated Financial Statements (Unaudited)**  
**Expressed in millions of Canadian dollars**

**3. SIGNIFICANT ACCOUNTING POLICIES** *(continued)*

Subsequent measurement of these assets and liabilities is based on either fair value or amortized cost using the effective interest method, depending upon their classification.

Financial assets and liabilities are offset and the net amount is presented in the consolidated financial statements when and only when, the Company has a legal right to offset the amounts and intends either to settle on a net basis or to realize the asset and settle the liability simultaneously.

The Company's financial assets and financial liabilities are generally classified and measured as follows:

<b>Asset/Liability</b>	<b>Category</b>	<b>Measurement</b>
Cash	Loans and receivables	Amortized cost
Accounts receivable	Loans and receivables	Amortized cost
Loans receivable from related party	Loans and receivables	Amortized cost
Long-term receivables and other assets	Loans and receivables	Amortized cost
Bank indebtedness	Other liabilities	Amortized cost
Accounts payable and accrued liabilities	Other liabilities	Amortized cost
Long term debt	Other liabilities	Amortized cost
Other long term liabilities (finance lease obligations)	Other liabilities	Amortized cost
Derivative instruments	FVTPL	Fair Value

*Basis for fair values*

The Company uses a fair value hierarchy to categorize the inputs used to measure the fair value of financial assets and financial liabilities. The following presents the financial instruments measured at fair value classified by the fair value hierarchy, the levels of which are:

<b>Fair Value Hierarchy Level</b>	<b>Description of Fair Value Hierarchy Level</b>
Level 1	Inputs are unadjusted quoted prices of identical instruments in active markets;
Level 2	Inputs are other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly; and
Level 3	Inputs are not based on observable market data.

The fair values of derivatives reflect the credit risk of the instrument and include adjustments to take account of the credit risk of the Company and counterparty when appropriate.

*Derecognition of financial instruments*

A financial asset is derecognized when the contractual rights to the cash flows from the asset expire or when the Company transfers the financial asset to another party without retaining control or substantially all the risks and rewards of ownership of the asset. Any interest in transferred financial assets that is created or retained by the Company is recognized as a separate asset or liability.

A financial liability is derecognized when its contractual obligations are discharged, cancelled or expire.

**ESSAR STEEL ALGOMA INC.**

**Notes to the Condensed Interim Consolidated Financial Statements (Unaudited)**

**Expressed in millions of Canadian dollars**

**3. SIGNIFICANT ACCOUNTING POLICIES (continued)**

*Derivative instruments*

To manage risks associated with future variability in cash flows attributable to certain commodity purchases, the Company uses natural gas swap contracts with maturities of 12 months or less. To manage its interest rate risks, the Company may utilize interest rate swaps for portions of its outstanding long term debt. The Company does not apply hedge accounting and does not utilize derivative financial instruments for trading or speculative purposes.

*Embedded derivatives*

An embedded derivative is a component of a financial instrument or another contract of which the characteristics are similar to a derivative. All derivative instruments including embedded derivatives are measured at fair value with changes in fair value recognized in net earnings. Embedded derivatives (elements of contracts whose cash flows move independently from the host contract) are required to be separated and measured at their respective fair values unless certain criteria are met. Other than the embedded derivatives disclosed in Note 15, the Company does not have any significant embedded derivatives in contracts that require separate accounting and disclosure.

**Accounts receivable**

Accounts receivable are recognized initially at fair value and subsequently measured at amortized cost using the effective interest method, less an allowance for impairment, if any. The fair value of accounts receivable is estimated to be reasonably approximated by their carrying value due to their short-term nature. The allowance for impairment of accounts receivable is established when there is objective evidence that the Company will not be able to collect all amounts due according to the original terms of the receivables. When an account receivable is uncollectible, it is written off against the allowance account for accounts receivable. Subsequent recoveries of amounts previously written off are credited against administrative and selling expenses in the consolidated statement of comprehensive income.

**Loans receivable**

Loans receivable are initially measured at fair value plus directly attributable transaction costs, and are subsequently measured at their amortized cost using the effective interest method, net of impairment losses.

**Inventories**

Raw materials, work in process and finished products inventories are measured at the lower of average cost and net realizable value. Supplies inventories are measured at the lower of average cost and replacement cost. Average cost for finished goods and work in process is comprised of direct costs and an allocation of production overheads, including depreciation expense.

**Property, plant and equipment, net**

Items of property, plant and equipment are measured and stated at cost, net of accumulated depreciation and any recognized impairment in value. Land is stated at cost less any recognized impairment in value. The cost of an item of property or equipment comprises costs that can be directly attributed to its acquisition and to bringing the asset to a working condition for its intended use, including borrowing costs that meet the criteria for capitalization and initial estimates of the cost of dismantling and removing the item and restoring the site on which it is located. The cost of self-constructed and self-installed assets includes the cost of direct labour in addition to the costs listed above.

**ESSAR STEEL ALGOMA INC.**  
**Notes to the Condensed Interim Consolidated Financial Statements (Unaudited)**  
**Expressed in millions of Canadian dollars**

**3. SIGNIFICANT ACCOUNTING POLICIES** *(continued)*

Depreciation is calculated generally by the straight-line method based on estimated remaining useful lives as follows:

<b>Category of Property, Plant and Equipment</b>	<b>Range of Estimated Useful Life</b>
Buildings	5 - 40 years
Machinery and equipment	5 - 20 years
Computer hardware	5 years
Mill rolls	1 - 15 years

Capital costs related to extending the useful life of the blast furnace are amortized over its remaining useful life on a unit of production basis.

The Company also separately recognizes the cost of replacement parts and major overhaul or inspection costs if the cost of the item can be reliably measured or estimated and it is probable that the future economic benefits will be realized by the Company. When such items are replaced the carrying amount of the replaced component is derecognized. The costs of maintenance and repairs of property, plant and equipment are recognized in net earnings as incurred.

*Componentization*

When significant components of an item of property, plant and equipment have different useful lives, they are accounted for as separate items and depreciated over the respective useful lives.

*Useful life, depreciation method, residual value*

Estimates of useful lives are based on management's judgment as to the physical and economic useful lives of assets and as such are subject to change in future periods. Depreciation methods, useful lives and residual values are reviewed at each reporting date with the effect of any changes in estimate being accounted for on a prospective basis.

*Derecognition of property plant and equipment*

An item of property, plant and equipment is derecognised upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on the disposal or retirement of an item of property, plant and equipment is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognised in net earnings.

**Assets under finance lease**

Leases are classified as finance leases whenever the terms of the lease transfer substantially all of the risks and rewards of ownership to the Company. All other leases are classified as operating leases. Assets held under finance leases are depreciated over their expected useful lives on the same basis as owned assets or, where shorter, the term of the relevant lease.

Where the Company is the lessee, rent payable under an operating lease is charged to the consolidated statement of comprehensive income on a straight-line basis over the term of the relevant lease. Assets held under finance leases are recognized as assets of the Company at their fair value or, if lower, at the present value of the minimum lease payments, each determined at the inception of the lease. The corresponding liability is included in the statement of financial position as a finance lease obligation. Lease payments are apportioned between finance cost and reduction of the lease obligations so as to achieve a constant rate of interest on the remaining balance of the liability. Finance cost and depreciation expense on the underlying leased asset, are charged to the consolidated statements of comprehensive income.

**ESSAR STEEL ALGOMA INC.**  
**Notes to the Condensed Interim Consolidated Financial Statements (Unaudited)**  
**Expressed in millions of Canadian dollars**

**3. SIGNIFICANT ACCOUNTING POLICIES** *(continued)*

**Intangible assets, net**

Finite life intangible assets are amortized on a straight-line basis over their estimated remaining useful lives, as follows:

Category of Intangible Asset	Range of Estimated Useful Life
In-process research and development	5 to 10 years
Customer relationships	12 to 14 years
Technology	5 to 10 years
Supply agreements	Over terms of specific agreements, ranging from 5 to 15 years
Essar Centre naming rights	Over term of specific agreement, 10 years
Computer software	5 years

*Internally-generated intangible assets - research and development*

Expenditure on research activities is recognised as an expense in the period in which it is incurred. An internally-generated intangible asset arising from is recognised if, and only if, all of the following have been demonstrated:

- the intention to complete the intangible asset and use it;
- the ability to use the intangible asset;
- how the intangible asset will generate probable future economic benefits;
- the availability of adequate technical, financial and other resources to complete the development and to use the intangible asset; and
- the ability to measure reliably the expenditure attributable to the intangible asset during its development.

The amount initially recognised for internally-generated intangible assets is the sum of the expenditure incurred from the date when the intangible asset first meets the recognition criteria listed above. Where no internally-generated intangible asset can be recognised, the expenditure is recognised in net earnings in the period in which it is incurred.

Subsequent to initial recognition, internally-generated intangible assets are reported at cost less accumulated amortisation and accumulated impairment losses, on the same basis as intangible assets that are acquired separately.

*Intangible assets acquired in a business combination*

Intangible assets acquired in a business combination are initially recognised at their fair value at the acquisition date. This fair value is considered their cost. Subsequent to initial recognition, intangible assets acquired in a business combination are reported at cost less accumulated amortisation and accumulated impairment losses, on the same basis as intangible assets that are acquired separately.

*Derecognition of intangible assets*

An intangible asset is derecognised on disposal, or when no future economic benefits are expected from use or disposal. Gains or losses arising from derecognition of an intangible asset, measured as the difference between the net disposal proceeds and the carrying amount of the asset is recognised in net earnings when the asset is derecognised.

**ESSAR STEEL ALGOMA INC.**  
**Notes to the Condensed Interim Consolidated Financial Statements (Unaudited)**  
**Expressed in millions of Canadian dollars**

**3. SIGNIFICANT ACCOUNTING POLICIES** *(continued)*

**Impairment of tangible and intangible assets**

Property, plant and equipment and intangible assets are reviewed at the end of each reporting period to determine whether there is any indication of impairment. If any such indication exists then the recoverable amount of the asset is estimated. The recoverable amount of an asset is defined as the higher of its fair value less costs to sell and its value in use. Where it is not possible to estimate the recoverable amount of an individual asset, the Company estimates the recoverable amount of the Cash Generating Unit ("CGU") to which the asset belongs. The CGU corresponds to the smallest identifiable group of assets whose continuing use generates cash inflows that are largely independent of the cash flows from other groups of assets.

An impairment loss is recognized when the carrying amount of an asset, or of the CGU to which it belongs, exceeds the recoverable amount. In determining value in use, the Company estimates cash flows before taxes based on most recent actual results and forecasts and then determines the current value of future estimated cash flows.

Impairment losses are recognized in the consolidated statements of comprehensive income. Impairment losses recognized for other assets in prior periods are assessed at the end of each reporting period for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. The increased carrying amount of an asset attributable to a reversal of impairment loss may not exceed the carrying amount that would have been determined had no impairment loss been recognized in prior periods.

**Borrowing costs**

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, which are assets that necessarily take a substantial period of time to get ready for their intended use or sale, are added to the cost of those assets, until such time as the assets are substantially ready for their intended use or sale.

All other borrowing costs are recognised in net earnings in the period in which they are incurred.

**Retirement benefit costs**

The Company provides pensions and certain health care, dental care, life insurance and other benefits for certain retired employees pursuant to Company policy. For defined benefit pension plans and other post-employment benefits, the net periodic pension expense is actuarially determined on an annual basis by independent actuaries using the projected benefit method, prorated on service and is charged to expense as services are rendered. The determination of a benefit expense requires assumptions such as the expected return on assets available to fund pension obligations, the discount rate to measure obligations, the expected mortality, the expected rate of future compensation increases and the expected healthcare cost trend rate. For the purpose of calculating the expected return on plan assets, the assets are valued at fair value. The expected return on plan assets is based on the fair value of plan assets. Actual results will differ from estimated results which are based on assumptions.

**ESSAR STEEL ALGOMA INC.**  
**Notes to the Condensed Interim Consolidated Financial Statements (Unaudited)**  
**Expressed in millions of Canadian dollars**

**3. SIGNIFICANT ACCOUNTING POLICIES** *(continued)*

The vested portion of past service cost arising from plan amendments is recognized immediately in net earnings. The unvested portion is amortized on a straight-line basis over the average remaining period until the benefits become vested. The asset or liability recognized in the consolidated statement of financial position is the present value of the defined benefit obligation at the end of the reporting period less the present value of plan assets, together with adjustments for unrecognized past service costs and asset ceiling restrictions. The present value of the defined benefit obligation is determined by discounting the estimated future cash outflows. The discount rate used for this purpose is the interest rate of high-quality Canadian corporate bonds and that have terms to maturity approximating the terms of the related pension liabilities. The present value of the plan assets is determined by discounting the estimated future inflows. The discount rate used for this purpose based on the expected rate of return on the plan assets. All actuarial gains and losses that arise in calculating the present value of the defined benefit obligation and the plan assets are recognized immediately in other comprehensive income. Any defined benefit asset resulting from this calculation is limited to the total of unrecognized net actuarial gains and losses and past service cost and the present value of any economic benefit in the form of refunds from the plan or reduction in future contributions to the plan.

Payments to defined contribution retirement benefit plans are recognised as an expense when employees have rendered service entitling them to the contributions.

**Termination benefits**

Termination benefits are recognized as an expense when the Company is demonstrably committed, without realistic possibility of withdrawal, to a formal detailed plan to either terminate employment before the normal retirement date, or to provide termination benefits as a result of an offer made to encourage voluntary redundancy. Termination benefits for voluntary redundancies are recognized as an expense if the Company has made an offer encouraging voluntary redundancy, it is probable that the offer will be accepted, and the number of acceptances can be estimated reliably.

**Short-term benefits**

Short-term employee benefit obligations are measured on an undiscounted basis and are expensed as the related service is provided. A liability is recognized for the amount expected to be paid under short-term cash bonus or profit-sharing plans if the Company has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

**Accounts payable and accrued liabilities**

Accounts payable and accrued liabilities are recognized initially at fair value and subsequently measured at amortized cost.

**Provisions**

A provision is recognized if, as a result of a past event, the Company has a present legal or constructive obligation that can be estimated reliably and it is probable that an outflow of economic benefits will be required to settle the obligation. The amount recognized as a provision is the best estimate of the consideration required to settle the present obligation at the end of the reporting period, taking into account risks and uncertainty of cash flow. Where the effect of discounting is material, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the liability. Where the future cash flow estimates have been adjusted for the risks specific to the liability, the discount rate does not reflect the risks specific to the liability. The unwinding of the discount is recognized as finance cost.

**ESSAR STEEL ALGOMA INC.**  
**Notes to the Condensed Interim Consolidated Financial Statements (Unaudited)**  
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**3. SIGNIFICANT ACCOUNTING POLICIES** *(continued)*

*Onerous contracts*

Present obligations arising under onerous contracts are recognised and measured as provisions. An onerous contract is considered to exist where the Company has a contract under which the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be received from the contract.

*Site restoration and decommissioning provisions*

The Company recognizes the fair value of a future site restoration and decommissioning provisions (asset retirement obligations) as a liability in the period in which it incurs either a legal obligation or a constructive obligation associated with the retirement of property, plant and equipment that results from the acquisition, construction, development, and/or normal use of the assets. The Company concurrently recognizes a corresponding increase in the carrying amount of the related property, plant and equipment that is amortized over the life of the asset. Subsequent to the initial measurement, the site restoration and decommissioning provision is adjusted at the end of each period to reflect the passage of time and changes in the estimated future cash flows underlying the obligation. Changes in the provision due to the passage of time are recognized in net earnings as an operating expense. Changes in the provision due to changes in estimated cash flows are recognized as an adjustment of the carrying amount of the related property, plant and equipment that is amortized over the remaining life of the asset.

**Long term debt**

Long term debt is recognized initially at fair value, net of transaction costs incurred. Borrowings are subsequently stated at amortized cost; transaction costs related to the Senior Secured Note and the Senior Notes are amortized in net earnings using the effective interest rate method.

**Revenue recognition**

*Sale of goods*

Revenue from the sale of goods is measured at the fair value of the consideration received or receivable, net of provisions for returns, customer claims and other adjustments. Revenue is recognized when the significant risks and rewards of ownership have been transferred to the buyer, recovery of the consideration is probable, the associated costs and possible return of goods can be estimated reliably, there is no continuing management involvement with the goods and the amount of revenue can be measured reliably. Transfers of risk and rewards vary depending on the individual terms of the contract of sale. Under the terms of contract, transfer usually occurs when goods are loaded to the relevant carrier or when goods are received at the customer's point of delivery.

*Freight revenue*

Revenue derived from the shipment of goods sold is measured at the fair value of the consideration received or receivable, net of provisions for returns, customer claims and other adjustments. Freight revenue is recognized concurrent with the recognition of the revenue on the goods being shipped.

The Company reflects amounts billed to customers in a sale transaction relating to shipping and handling as revenue and freight costs associated with shipping its products to customers as a component of cost of sales.

*Government rebates*

Government rebates are not recognized until there is reasonable assurance that the Company will comply with the conditions attaching to them and that the rebates will be received.

Government rebates are recognized in net earnings on a systematic basis over the periods in which the Company recognises as expenses the related costs for which the rebates are received. Government rebates that are received or receivable against expenses already incurred are recognized in net earnings in the period in which they become receivable.

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**3. SIGNIFICANT ACCOUNTING POLICIES** *(continued)*

**Research and Development**

Research costs are charged to operations as incurred, due to the nature of the projects. Where government incentives in the form of investment tax credits and grants are received for research and development projects initiated by the Company for its own purposes, these incentives are deducted from the applicable category of expenditures, that is, either cost of sales or property, plant and equipment.

**Finance cost**

Finance cost is comprised of interest expense on borrowings and impairment losses recognized on financial assets that are recognized in net earnings. Borrowing costs that are not directly attributable to the acquisition, construction or production of a qualifying asset are recognized in net earnings using the effective interest method.

Financing costs associated with the Revolving Facility are amortized using the straight-line basis over 5 years as a component of interest expense. Financing costs related to the Senior Secured Notes and the Senior Notes are recorded as a component of the carrying amount of the related debt and are amortized to net earnings using the effective interest method.

**Taxation**

Income tax expense represents the sum of the tax currently payable and deferred income tax.

*Current tax*

The tax currently payable is based on taxable profit for the year. Taxable profit differs from profit as reported in the consolidated statement of comprehensive income because of items of income or expense that are taxable or deductible in other years and items that are never taxable or deductible. The Company's liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the end of the reporting period.

*Deferred income tax*

Deferred income tax is recognised on temporary differences between the carrying amounts of assets and liabilities in the consolidated financial statements and the corresponding tax bases used in the computation of taxable profit. Deferred income tax liabilities are generally recognised for all taxable temporary differences. Deferred income tax assets are generally recognised for all deductible temporary differences to the extent that it is probable that taxable profits will be available against which those deductible temporary differences can be utilised.

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

Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply in the period in which the asset realised or the liability is settled, based on tax rates and tax laws that have been enacted or substantively enacted by the end of the reporting period. The measurement of deferred income tax assets and liabilities reflects the tax consequences, based on management's expectation at the end of the reporting period that would follow from the recovery or settlement of the carrying amount of its assets and liabilities.

*Current and deferred income tax for the year*

Current and deferred income tax are recognised in net earnings, except when they relate to items that are recognised in other comprehensive income or directly in equity, in which case, the current and deferred income tax are also recognised in other comprehensive income or directly in equity respectively.

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**3. SIGNIFICANT ACCOUNTING POLICIES** *(continued)*

**Comprehensive Income (Loss)**

Other comprehensive income (loss) ("OCI(L)") includes foreign exchange loss (gain) on translation to the Company's presentation currency from the US functional currency. OCI(L) also includes actuarially determined gains and losses on post employment benefits offered to certain employees. OCI(L) is presented below net income (loss) on the consolidated statements of comprehensive income (loss). Comprehensive income (loss) is composed of net income (loss) and OCI(L).

Accumulated OCI(L) is a separate component of shareholder's equity which includes the accumulated balances of all components of OCI(L) which are recognized in comprehensive income (loss) but excluded from net income (loss).

**Standards and Interpretations issued and not yet adopted**

*Financial Instruments*

In November 2009 and October 2010, the IASB issued IFRS 9 – Financial Instruments ("IFRS 9"), Classification and Measurement of Financial Assets and Financial Liabilities, respectively. IFRS 9 will replace IAS 39 – Financial Instruments: Recognition and Measurement ("IAS 39") in its entirety. IFRS 9 uses a single approach to determine whether a financial asset or liability is measured at amortized cost or fair value, replacing the multiple rules in IAS 39. For financial assets, the approach in IFRS is based on how an entity manages its financial instruments in the context of its business model and the contractual cash flow characteristics of the financial assets. The new standard also requires a single impairment method to be used, replacing the multiple impairment methods in IAS 39. For financial liabilities measured at fair value, fair value changes due to changes in the Company's credit risk are presented in other comprehensive income ("OCI"), instead of net income (loss), unless this would create an accounting mismatch. IFRS 9 is effective for annual periods beginning on or after January 1, 2013. Early adoption is permitted. The Company is assessing the potential impact of this standard.

*Financial Instruments: Disclosure*

In October 2010, the IASB amended IFRS 7 – Financial instruments: Disclosures, which will be applied prospectively for annual periods beginning on or after July 1, 2011. The amendments require additional disclosures on transferred financial assets. The Company is assessing the potential impact of these amendments.

*Consolidated Financial Statements*

In May 2011, the IASB issued IFRS 10 which provides additional guidance to determine whether an investee should be consolidated. The guidance applies to all investees, including special purpose entities. The standard is required to be adopted for periods beginning January 1, 2013. The Company is assessing the potential impact of this standard.

*Joint Arrangements*

In May 2011, the IASB issued IFRS 11 which presents a new model for determining whether an entity should account for joint arrangements using proportionate consolidation or the equity method. An entity will have to follow the substance rather than legal form of a joint arrangement and will no longer have a choice of accounting method. The standard is required to be adopted for periods beginning January 1, 2013. The Company is assessing the potential impact of this standard.

*Disclosure of Interests in Other Entities*

In May 2011, the IASB issued IFRS 12 which aggregates and amends disclosure requirements included within other standards. The standard requires a company to provide disclosures about subsidiaries, joint arrangements, associates and unconsolidated structured entities. The standard is required to be adopted for periods beginning January 1, 2013. The Company is assessing the potential impact of this standard.

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**3. SIGNIFICANT ACCOUNTING POLICIES** *(continued)*

*Fair Value Measurement*

In May 2011, the IASB issued IFRS 13 to provide comprehensive guidance for instances where IFRS requires fair value to be used. The standard provides guidance on determining fair value and requires disclosures about those measurements. The standard is required to be adopted for periods beginning January 1, 2013. The Company is assessing the potential impact of this standard.

*Presentation of Items of Other Comprehensive Income*

In June 2011, the IASB issued amendments to IAS 1 Presentation of Financial Statements to split items of OCI between those that are reclassified to net earnings and those that do not. The standard is required to be adopted for periods beginning on or after July 1, 2012. The Company is assessing the potential impact of this standard.

*Employee Benefits*

In June 2011, the IASB issued amendments to IAS 19 that introduced changes to the accounting for defined benefit plans and other employee benefits. The amendments include elimination of the options to defer or recognize in full in earnings, actuarial gains and losses and instead mandates the immediate recognition of all actuarial gains and losses in other comprehensive income and requires use of the same discount rate for both the defined benefit obligation and the expected return on assets when calculating interest cost. Other changes include modification of the accounting for termination benefits and classification of other employee benefits. The amendment is effective for annual period beginning on or after January 1, 2013. The company is assessing the potential impact of this standard.

**4. CRITICAL ESTIMATES AND JUDGMENTS**

The preparation of these condensed interim consolidated financial statements, in accordance with IFRS, 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 reporting period. Actual results could differ from those estimates.

Judgement is used mainly in determining whether a balance or transaction should be recognized in the consolidated financial statements. Estimates and assumptions are used mainly in determining the measurement of recognized transactions and balances. However, judgment and estimates are often interrelated.

The Company has applied judgment in the classification of leases, the recognition of tax losses and provisions, the determination of cash generating units, identifying the indicators of impairment for property and equipment and intangible assets with finite useful lives, and the level of componentization of property and equipment.

Judgments, estimates and assumptions are continually evaluated and are based on historical experience and other factors including expectations of future events that are believed to be reasonable under the circumstances. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in future periods affected.

The following discussion sets forth management's most critical estimates and assumptions in determining the value of assets and liabilities:

*Revenue Recognition*

Revenues from goods sold are net of estimated customer returns, claims and allowances. Customer returns, claims and allowances are estimated based on current trends and past experience.

*Allowance for doubtful accounts*

The Company assesses the collectability of accounts receivable. An allowance for doubtful account is estimated based on customer creditworthiness, current economic trends and past experience.

**ESSAR STEEL ALGOMA INC.**  
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**4. CRITICAL ESTIMATES AND JUDGMENTS** *(continued)*

*Inventories*

Inventories are valued at the lower of cost and net realizable value. Net realizable value is the estimated net selling price in the ordinary course of business. Management reviews the provision for net realizable value to assess whether, based on economic conditions, it is adequate.

*Useful lives of Property, plant and equipment and Intangible assets*

The Company reviews the estimated useful lives of property, plant and equipment and intangible assets at the end of each annual reporting period, and whenever events or circumstances indicate a change in useful life. Estimated useful lives of items of property, plant and equipment and intangible assets are based on a best estimate and the actual useful lives may be different.

*Impairment of Property, plant and equipment and Intangible assets*

Determining whether property, plant and equipment and intangible assets are impaired requires the Company to determine the recoverable amount of the CGU to which the asset is allocated. To determine the recoverable amount of the CGU, management is required to estimate its fair value by evaluating expected future cash flows, using an appropriate growth rate, the estimated costs to sell and a suitable discount rate to calculate the value in use.

*Defined Benefit Retirement Plans*

The Company's determination of employee benefit expense and obligations requires the use of assumptions such as the expected return on assets available to fund pension obligations, the discount rate to measure obligations, expected mortality, the expected rate of increase of future compensation and the expected healthcare cost trend rate. Since the determination of the cost and obligations associated with employee future benefits requires the use of various assumptions, there is measurement uncertainty inherent in the actuarial valuation process. Actual results could differ from estimated results which are based on assumptions.

*Taxation*

The Company computes an income tax provision in each of the jurisdictions in which it operates. Actual amounts of income tax expense only become final upon filing and acceptance of the tax return by the relevant authorities, which occur subsequent to the issuance of the financial statements. Additionally, the estimation of income taxes includes evaluating the recoverability of deferred income tax assets based on an assessment of the ability to use the underlying future tax deductions before they expire against future taxable income. The assessment is based upon existing tax laws and estimates of future taxable income. To the extent estimates differ from the final tax return, earnings would be affected in a subsequent period. The Company files tax returns that may contain interpretations of tax law and estimates. Positions taken and estimates utilized by the Company may be challenged by the relevant tax authorities. Rulings that alter tax returns filed may require adjustment in the future.

*Provisions*

The Company has made certain other estimates that, while not involving the same degree of judgment as the estimates described above, are important to understanding the Company's consolidated financial statements. These estimates are in the areas of site restoration and decommissioning reserves, legal matters and other items. On an ongoing basis, management evaluates its estimates and judgments in these areas based on its substantial historical experience and other relevant factors. Management's estimates as of the date of the financial statements reflect its best judgment giving consideration to all currently available facts and circumstances. As such, these estimates may require adjustment in the future, as additional facts become known or as circumstances change.

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**5. CAPITAL MANAGEMENT**

The Company's objectives when managing capital are:

- (i) to maintain a flexible capital structure which optimizes the cost of capital at acceptable risk;
- (ii) to meet external capital requirements on debt and credit facilities;
- (iii) to ensure adequate capital to support long-term growth strategy; and
- (iv) to provide an adequate return to shareholders.

The Company continuously monitors and reviews the capital structure to ensure the objectives are met.

Management defines capital as the combination of its indebtedness and equity balances and manages the capital structure within the context of the business strategy, general economic conditions, market conditions in the steel industry and the risk characteristics of assets.

External factors, such as the economic environment and the transition to IFRS have not changed the Company's objectives in managing capital.

The Company is in compliance with the covenants under its existing debt agreements at June 30, 2011 and through out the first quarter of the Company's 2012 fiscal year.

**6. REVENUE AND SEGMENTED INFORMATION**

The Company is viewed as a single business segment involving basic steel production for purposes of internal performance measurement and resource allocation.

*The total revenue is comprised of:*

	<b>Three months ended 6/30/11</b>	Three months ended 6/30/10
Sheet and strip	\$ 405.9	\$ 337.9
Plate	111.1	93.5
Freight	34.4	34.0
Non-steel revenue	14.6	10.3
	<b>\$ 566.0</b>	<b>\$ 475.7</b>

*The geographical distribution of total revenue is as follows:*

Sales to customers in Canada	\$ 301.5	\$ 257.5
Sales to customers in the United States	255.5	191.2
Sales to customers in the rest of the world	9.0	27.0
	<b>\$ 566.0</b>	<b>\$ 475.7</b>

For the periods ended June 30, 2011 and June 30, 2010, no single customer represented greater than 10% of total revenue.

**ESSAR STEEL ALGOMA INC.**  
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**7. COST OF SALES**

	<b>Three months ended 6/30/11</b>	<b>Three months ended 6/30/10</b>
Cost of steel revenue	\$ 391.7	\$ 342.2
Cost of freight revenue	34.4	34.0
Cost of non-steel revenue	14.7	10.3
Depreciation included in cost of sales	42.5	47.9
	<b>\$ 483.3</b>	<b>\$ 434.4</b>

Included in cost of sales for the period ended June 30, 2011 is \$0.1 million (June 30, 2010 - \$0.6 million) of write-downs of inventories as a result of net realizable value being lower than cost. There has been no reversal of any previously recorded inventory write-down during the period ended June 30, 2011 (June 30, 2010 - nil).

During the period ended June 30, 2011, inventories recognized as cost of sales were \$461.2 million (June 30, 2010 - \$411.1 million).

**8. ADMINISTRATIVE AND SELLING EXPENSES**

	<b>Three months ended 6/30/11</b>	<b>Three months ended 6/30/10</b>
Personnel expenses	\$ 9.1	\$ 7.2
Amortization of intangible assets and non-production assets	5.6	5.5
Other administrative and selling	7.2	6.4
	<b>\$ 21.9</b>	<b>\$ 19.1</b>

**9. ACCOUNTS RECEIVABLE**

	<b>June 30, 2011</b>	<b>March 31, 2011</b>	<b>April 1, 2010</b>
Accounts receivable	\$ 215.9	\$ 155.2	\$ 198.1
Allowance for doubtful accounts	(1.6)	(1.6)	(2.2)
Other accounts receivable	6.7	3.0	5.7
Accounts receivable from related party (Note 25)	0.7	3.8	1.9
Total	<b>\$ 221.7</b>	<b>\$ 160.4</b>	<b>\$ 203.5</b>

*Accounts receivable pledged as security*

The Company's accounts receivable have been pledged to secure the borrowings of the Company. Please see Note 13.

**ESSAR STEEL ALGOMA INC.**

**Notes to the Condensed Interim Consolidated Financial Statements (Unaudited)**

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**10. INVENTORIES**

	<u>June 30, 2011</u>	<u>March 31, 2011</u>	<u>April 1, 2010</u>
Raw materials and consumables	\$ 168.2	\$ 180.9	\$ 160.2
Work in progress	68.9	51.5	62.6
Finished goods	49.7	46.0	66.5
Total	<u>\$ 286.8</u>	<u>\$ 278.4</u>	<u>\$ 289.3</u>

*Inventories pledged as security*

The Company's inventories have been pledged to secure the borrowings of the Company. Please see Note 13.

**11. PROPERTY PLANT AND EQUIPMENT**

Carrying amount of	<u>June 30, 2011</u>	<u>March 31, 2011</u>	<u>April 1, 2010</u>
Freehold Land	\$ 17.6	\$ 17.7	\$ 18.5
Buildings	109.0	110.4	130.7
Machinery and Equipment	1,040.6	1,080.0	1,256.0
Computer Hardware	19.7	20.5	18.5
Mill Rolls	4.4	4.7	6.3
Assets under finance lease	1.8	2.0	3.1
Construction in progress	44.9	42.5	42.8
	<u>\$ 1,238.0</u>	<u>\$ 1,277.8</u>	<u>\$ 1,475.9</u>

Cost:	Freehold Land	Buildings	Machinery and Equipment	Mill Rolls	Computer Hardware	Assets under finance lease	Property under Construction	Total
Balance at April 1, 2010	\$ 18.5	\$ 186.4	\$ 1,664.5	\$ 29.6	\$ 8.9	\$ 5.7	\$ 42.8	\$ 1,956.4
Additions	-	3.7	34.6	14.8	-	-	1.7	54.8
Disposals	-	-	-	(12.4)	-	-	-	(12.4)
Foreign Exchange	(0.8)	(8.6)	(77.3)	(1.5)	(0.4)	(0.2)	(2.0)	(90.8)
Balance at March 31, 2011	17.7	181.5	1,621.8	30.5	8.5	5.5	42.5	1,908.0
Additions	-	3.0	3.9	2.5	-	0.1	2.6	12.1
Foreign Exchange	(0.1)	(1.0)	(8.0)	(0.2)	(0.1)	(0.1)	(0.2)	(9.7)
<b>Balance at June 30, 2011</b>	<b>\$ 17.6</b>	<b>\$ 183.5</b>	<b>\$ 1,617.7</b>	<b>\$ 32.8</b>	<b>\$ 8.4</b>	<b>\$ 5.5</b>	<b>\$ 44.9</b>	<b>\$ 1,910.4</b>

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**11. PROPERTY PLANT AND EQUIPMENT** *(continued)*

Accumulated Depreciation:	Freehold Land	Buildings	Machinery and Equipment	Mill Rolls	Computer Hardware	Assets under finance lease	Property under Construction	Total
Balance at April 1, 2010	\$ -	\$ 55.7	\$ 408.5	\$ 11.1	\$ 2.6	\$ 2.6	\$ -	\$ 480.5
Eliminated on disposals of assets	-	-	-	(10.0)	-	-	-	(10.0)
Depreciation Expense	-	18.8	160.3	9.3	1.3	1.0	-	190.7
Foreign Exchange	-	(3.4)	(27.0)	(0.4)	(0.1)	(0.1)	-	(31.0)
Balance at March 31, 2011	-	71.1	541.8	10.0	3.8	3.5	-	630.2
Eliminated on disposals of assets	-	-	-	-	-	-	-	-
Depreciation Expense	-	3.8	37.9	3.1	0.3	0.3	-	45.4
Foreign Exchange	-	(0.4)	(2.6)	-	(0.1)	(0.1)	-	(3.2)
<b>Balance at June 30, 2011</b>	<b>\$ -</b>	<b>\$ 74.5</b>	<b>\$ 577.1</b>	<b>\$ 13.1</b>	<b>\$ 4.0</b>	<b>\$ 3.7</b>	<b>\$ -</b>	<b>\$ 672.4</b>

*Depreciation of property, plant and equipment*

Depreciation of property, plant and equipment for the period ended June 30, 2011 was \$45.4 million (June 30, 2010 - \$46.9 million). Depreciation included in inventories at June 30, 2011 amounted to \$10.1 million (March 31, 2011 - \$8.5 million; April 1, 2010 - \$12.5 million).

*Acquisitions and disposals*

During the period ended June 30, 2011, property, plant and equipment were acquired at an aggregate cost of \$12.1 million (June 30, 2010 - \$14.0 million). There were no disposals of property, plant and equipment during the period ended June 30, 2011. During the period ended June 30, 2010, the Company disposed of property, plant and equipment with a carrying amount of \$0.7 million.

*Assets pledged as security*

All of the Company's assets have been pledged to secure the borrowings of the Company. Please see Note 13.

**12. INTANGIBLE ASSETS**

The following table presents the changes to accumulated amortization and impairments on the Company's intangible assets for the period ended June 30, 2011.

Carrying amount of	June 30, 2011	March 31, 2011	April 1, 2010
Customer relationships	\$ 62.5	\$ 64.7	\$ 74.9
Technology	5.2	5.5	6.8
In-process research and development	2.0	2.1	2.8
Supply agreements	5.1	5.5	7.4
Essar Centre naming rights	1.0	1.0	1.2
Software	6.4	8.2	16.5
Software in development	4.5	3.6	1.5
	<u>\$ 86.7</u>	<u>\$ 90.6</u>	<u>\$ 111.1</u>

**ESSAR STEEL ALGOMA INC.**  
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**12. INTANGIBLE ASSETS (continued)**

Cost	Customer Relationships	Technology	In-process research and development	Supply agreements	Essar Centre naming rights	Software	Software in Development	Total
Balance at April 1, 2010	\$ 95.1	\$ 9.9	\$ 4.3	\$ 19.2	\$ 1.4	\$ 36.5	\$ 1.5	\$ 167.9
Additions	-	-	-	-	-	-	2.2	2.2
Disposals	-	-	-	(7.3)	-	(0.2)	-	(7.5)
Foreign Exchange	(4.3)	(0.4)	(0.2)	(0.5)	-	(1.6)	(0.1)	(7.1)
Balance at March 31, 2011	90.8	9.5	4.1	11.4	1.4	34.7	3.6	155.5
Additions	-	-	-	-	-	-	1.0	1.0
Disposals	-	-	-	-	-	-	-	-
Foreign Exchange	(0.5)	(0.1)	-	(0.1)	-	(0.2)	(0.1)	(1.0)
<b>Balance at June 30, 2011</b>	<b>\$ 90.3</b>	<b>\$ 9.4</b>	<b>\$ 4.1</b>	<b>\$ 11.3</b>	<b>\$ 1.4</b>	<b>\$ 34.5</b>	<b>\$ 4.5</b>	<b>\$ 155.5</b>
Accumulated Amortization	Customer Relationships	Technology	In-process research and development	Supply agreements	Essar Centre naming rights	Software	Software in Development	Total
Balance at April 1, 2010	\$ 20.2	\$ 3.1	\$ 1.5	\$ 11.8	\$ 0.2	\$ 20.0	\$ -	\$ 56.8
Eliminated on disposals of intangible assets	-	-	-	(7.3)	-	-	-	(7.3)
Amortization Expense	7.2	1.1	0.6	1.6	0.2	7.6	-	18.3
Foreign Exchange	(1.3)	(0.2)	(0.1)	(0.2)	-	(1.1)	-	(2.9)
Balance at March 31, 2011	26.1	4.0	2.0	5.9	0.4	26.5	-	64.9
Eliminated on disposals of intangible assets	-	-	-	-	-	-	-	-
Amortization Expense	1.7	0.3	0.1	0.4	-	1.8	-	4.3
Foreign Exchange	-	(0.1)	-	(0.1)	-	(0.2)	-	(0.4)
<b>Balance at June 30, 2011</b>	<b>\$ 27.8</b>	<b>\$ 4.2</b>	<b>\$ 2.1</b>	<b>\$ 6.2</b>	<b>\$ 0.4</b>	<b>\$ 28.1</b>	<b>\$ -</b>	<b>\$ 68.8</b>

*Amortization of intangible assets*

Amortization of intangible assets for the period ended June 30, 2011 was \$4.3 million (June 30, 2010 - \$4.0 million).

All of the Company's assets have been pledged to secure the borrowings of the Company. Please see Note 13.

**13. BANKING FACILITIES**

On June 20, 2007, the Company entered into a five-year Revolving Credit Agreement. The agreement provides the Company with a revolving credit facility ("Revolving Facility") equal to the lesser of a maximum lender commitment and a calculated borrowing base determined by the levels of the Company's accounts receivable and inventories, less certain reserves. The Revolving Facility is secured by substantially all of the Company's assets. Under the General Security Agreement, the Revolving Facility has priority claim on the accounts receivable and inventories of the Company and a secondary claim on the rest of the Company's assets. In addition to satisfying the borrowing base requirements in order to make borrowings under the Revolving Facility, the Company is required to either meet a fixed charge coverage ratio test or maintain a minimum excess availability of 10% of the Revolving Facility commitment. At June 30, 2011, the Company is required to maintain a minimum excess availability equal to US \$35 million.

**ESSAR STEEL ALGOMA INC.****Notes to the Condensed Interim Consolidated Financial Statements (Unaudited)****Expressed in millions of Canadian dollars****13. BANKING FACILITIES (continued)**

The Revolving Facility permits borrowings of Canadian or US dollars. Canadian borrowings bear interest at either the Canadian bankers' acceptance rate plus a margin of 1.25% - 2.0% or Canadian prime rate plus a margin of 0.25% - 1.0%. US borrowings bear interest at either the London Inter-Bank Overnight Rate ("LIBOR") plus a margin of 1.25% - 2.0% or the lender's corporate base rate plus a margin of 0.25% - 1.0%. The applicable margin is dependent on the average excess availability under the Revolving Facility for the preceding fiscal quarter.

The Revolving Facility also provides for payment to the lenders of an unused line fee on the average daily excess availability of 0.25% per annum and a letter of credit fee ranging from 1.25% to 2.00%, depending on the average excess availability under the Revolving Facility. A commitment fee of 0.25% of the full amount of the Revolving Facility and a funding fee of 0.75% of the full amount of the Revolving Facility were incurred to establish the Revolving Facility and are being amortized to expenses using a straight-line method over 5 years. The unamortized balance of the Revolving Facility fees at June 30, 2011 is \$1.0 million (March 31, 2011 - \$1.2 million; April 1, 2010 - \$2.2 million).

At June 30, 2011, there was \$168.2 million (includes US dollar denominated borrowings of US \$174.4 million) and \$184.5 million at March 31, 2011 (includes US dollar denominated borrowings of US \$185.0 million) and \$92.2 million at April 1, 2010 (includes US denominated borrowings of nil) outstanding under the Revolving Facility and \$113.6 million (March 31, 2011 - \$71.0 million; April 1, 2010 - \$163.9 million) of unused availability after taking into account \$18.6 million (March 31, 2011 - \$16.8 million; April 1, 2010 - \$16.6 million) of outstanding letters of credit and the US \$35 million minimum excess availability requirement. In addition, the Company had \$15.9 million of unrestricted cash at June 30, 2011 (March 31, 2011 - \$5.7 million; April 1, 2010 - \$40.2 million)

Under the terms of the Revolving Facility, the Company is required to be in compliance with various restrictive covenants which, among other things, limit the incurrence of additional indebtedness, limit investments, capital expenditures and dividends and restrict transactions with affiliates, permitted acquisitions, asset sales, liens and encumbrances and other matters customarily restricted in such agreements. The Company was in compliance with the financial covenant requirements of the Revolving Facility at June 30, 2011.

**14. ACCOUNTS PAYABLE AND ACCRUED LIABILITIES**

	<u>June 30, 2011</u>	<u>March 31, 2011</u>	<u>April 1, 2010</u>
Accounts payable	\$ 104.3	\$ 75.9	\$ 80.7
Accrued liabilities	46.6	58.6	66.0
Wages and accrued vacation payable	43.7	44.0	44.7
Payroll taxes payable	2.9	2.9	3.0
	<u>\$ 197.5</u>	<u>\$ 181.4</u>	<u>\$ 194.4</u>

**ESSAR STEEL ALGOMA INC.**  
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**15. LONG TERM DEBT**

	<u>June 30, 2011</u>	<u>March 31, 2011</u>	<u>April 1, 2010</u>
9.375 Senior Secured Notes denominated in US dollars due March 15, 2015	\$ 385.8	\$ 387.8	\$ 406.1
9 7/8 Senior Notes denominated in US dollars due June 15, 2015	<u>371.0</u>	<u>373.0</u>	<u>390.8</u>
	\$ 756.8	\$ 760.8	\$ 796.9
Less; unamortized financing costs, premiums and/or discounts	<u>17.1</u>	<u>18.0</u>	<u>20.4</u>
	<u>\$ 739.7</u>	<u>\$ 742.8</u>	<u>\$ 776.5</u>

The aggregate amount of principal repayments in each of the next five years and thereafter at current exchange rates is as follows:

2012	\$ -
2013	-
2014	-
2015	385.8
2016	<u>371.0</u>
	<u>\$ 756.8</u>

On December 14, 2009, the Company issued US \$400 million of 9.375% Senior Secured Notes ("Secured Notes"). The Secured Notes bear interest at 9.375% per annum which is payable on March 15 and September 15 of each year and will mature on March 15, 2015. Under an Inter-creditor Agreement, the Secured Notes have priority claim on all of the Company's assets except for accounts receivable and inventories. In addition, the Secured Notes have a secondary claim on accounts receivable and inventories. The Company applied the net proceeds from the sale of the Secured Notes to repay all amounts outstanding on the Term Loan facility that was in place prior to the Secured Notes issue, and to reduce the balance of the Revolving Facility and for general corporate purposes.

Subject to certain conditions, at any time prior to March 15, 2013, the Company may redeem up to 35% of the principal amount of the Secured Notes at a redemption price of 109.375% of the principal amount plus accrued and unpaid interest with the proceeds of a public equity offering. At any time prior to March 15, 2013, the Company may also redeem all or a part of the Secured Notes at a redemption price equal to 100% of the principal amount of the Secured Notes redeemed plus accrued and unpaid interest and a specified premium. On or after March 15, 2013, the Company may redeem all or a part of the Secured Notes at the following redemption prices, plus accrued and unpaid interest:

	<u>%</u>
2013	104.6875
2014 and thereafter	<u>100.0000</u>

The prepayment options in the Secured Notes are required to be accounted for as embedded call option derivative instruments, which require bifurcation and are accounted for at fair value. The embedded call options were included in other assets and have an estimated fair value of nil at June 30, 2011 (March 31, 2011 - nil; April 1, 2010 - \$0.1 million).

**ESSAR STEEL ALGOMA INC.**

**Notes to the Condensed Interim Consolidated Financial Statements (Unaudited)**  
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**15. LONG TERM DEBT** *(continued)*

The Company also has US \$384.7 million of 9 7/8% Senior Notes (“Senior Notes”) outstanding. The Senior Notes were issued on June 20, 2007. The Senior Notes bear interest of 9 7/8% per annum which is payable on June 15 and December 15 each year. The Senior Notes are unsecured and are subordinated in right of payment to all existing and future secured indebtedness of the Company to the extent of the assets securing such indebtedness. The total Senior Notes outstanding on the issue date was \$450 million. During fiscal 2009, the Company purchased and cancelled US \$65.3 million of Senior Notes, leaving a remaining balance of US \$384.7 million.

Subject to certain conditions, at any time prior to June 15, 2010, the Company was allowed to redeem up to 35% of the principal amount of the Senior Notes at a redemption price of 109.875% of the principal amount plus accrued and unpaid interest with the proceeds of a public equity offering. At any time prior to June 15, 2011, the Company was allowed to redeem all or a part of the Senior Notes at a redemption price equal to 100% of the principal amount of the Senior Notes redeemed plus accrued and unpaid interest and a specified premium. On or after June 15, 2011, the Company may redeem all or a part of the Senior Notes at the following redemption prices, plus accrued and unpaid interest:

	<u>%</u>
2011	104.938
2012	102.469
2013 and thereafter	<u>100.000</u>

The prepayment options in the Senior Notes are required to be accounted for as embedded call option derivative instruments, which require bifurcation and are accounted for at fair value. The embedded call options were included in other assets and have an estimated fair value of nil at June 30, 2011 (March 31, 2011 - \$nil; April 30, 2010 - \$0.1 million).

Total transaction costs and discounts related to the Secured Notes and Senior Notes amounted to \$30.3 million. Unamortized financing costs and discounts or premiums related to the Secured Notes and the Senior Notes totalling \$17.1 million at June 30, 2011 (March 31, 2011 - \$18.0 million; April 1, 2010 - 20.4 million) are recorded as a component of the carrying amount of the related debt and are amortized to net earnings using the effective interest rate method.

Under the terms of the Secured Notes and the Senior Notes, the Company is required to be in compliance with various restrictive covenants which, among other things, limit the incurrence of additional indebtedness, limit investments and dividends and restrict transactions with affiliates, permitted acquisitions, asset sales, liens and encumbrances and other matters customarily restricted in such agreements. The Company was in compliance with these requirements at June 30, 2011.

**ESSAR STEEL ALGOMA INC.**  
**Notes to the Condensed Interim Consolidated Financial Statements (Unaudited)**  
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**16. PENSION BENEFITS**

**Defined contribution plans**

The Company initiated a defined contribution pension plan in 2004 for non-unionized employees joining the Company after January 1, 2003. As part of the contract negotiations with the Company and its locals which concluded on July 31, 2010, the locals and the Company agreed to include in this plan all unionized employees hired subsequent to August 1, 2010 and to offer to all the current employees the option to move to the Defined Contribution Pension Plan. The plan was revised during the year; these revisions went into effect March 1, 2011. Prior to March 1, 2011 the Company provided a base contribution of 3% of salary and also matched employee contributions to a maximum of 4%, depending on years of service. After March 1, 2011, the Company provides a base contribution of 5% of salary and also matches employee contributions to a maximum of 2%, depending on years of service for non-unionized employees. Additionally, the Company provides a contribution for unionized employees equal to two dollars and fifty cents per qualified hour. The pension expense under this plan is equal to the Company's contribution. The pension expense for the period ended June 30, 2011 was \$0.1 million (June 30, 2010 - \$0.1 million).

**Defined benefit plans**

The Company maintains non-contributory defined benefit pension plans that cover all employees not covered under the Defined Contribution Pension Plan (including pensioners retiring after January 1, 2002, which is the date that the Ontario Pension Benefit Guarantee Fund assumed some of the assets and obligations of the pension plans). The benefits are based on years of service and average earnings for a defined period prior to retirement.

The Company also maintains a closed plan for pensioners who retired prior to January 1, 2002. This plan provides the pensioners with a pension benefit in excess of the limits provided by the Ontario Pension Benefit Guarantee Fund.

The most recent actuarial valuations of plan assets and the present value of the defined benefit obligation were carried out at August 1, 2010 by Mercer (Canada) Limited.

Amounts recognized in net earnings in respect of these defined benefit plans are as follows:

	<b>Three months ended June 30, 2011</b>	Three months ended June 30, 2010
Current service cost	\$ 5.6	\$ 5.6
Interest cost	14.6	14.3
Expected return on plan assets	(10.3)	(10.9)
Total defined benefit cost recognized in the condensed interim consolidated statement of comprehensive income	<u>\$ 9.9</u>	<u>\$ 9.0</u>
Define benefit costs recognized in cost of sales	\$ 8.9	\$ 8.1
Defined benefit costs recognized in administrative and selling expense	<u>1.0</u>	<u>0.9</u>
	<u>\$ 9.9</u>	<u>\$ 9.0</u>

**Cash flow information**

Total pension funding for the period ended June 30, 2011 was \$12.2 million (period ended June 30, 2010 - \$13.9 million). Contributions for the period ended June 30, 2011 were based on actuarial valuations at August 1, 2010.

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**17. OTHER POST-EMPLOYMENT BENEFITS**

The Company offers post-employment life insurance, health care and dental care to some of its retirees. These obligations are not pre-funded.

The most recent actuarial valuations of the present value of the other post-employment benefit obligation were carried out at March 31, 2011 by Mercer (Canada) Limited.

Amounts recognized in net earnings in respect of these post-retirement benefit plans are as follows:

	<b>Three months ended June 30, 2011</b>	<b>Three months ended June 30, 2010</b>
Current service cost	\$ 1.2	\$ 1.2
Net Interest cost	<u>6.2</u>	<u>5.9</u>
Total other post employment benefit costs recognized in the condensed interim consolidated statement of comprehensive income	<u>\$ 7.4</u>	<u>\$ 7.1</u>
Other post employment benefit costs recognized in cost of sales	\$ 6.7	\$ 6.4
Other post employment benefit costs recognized in administrative and selling expense	<u>0.7</u>	<u>0.7</u>
	<u>\$ 7.4</u>	<u>\$ 7.1</u>

**Cash flow information**

Payments made for other post-employment benefits were \$3.4 million for the period ended June 30, 2011 (June 30, 2010 - \$3.6 million), and are on a pay-as-you-go basis.

**18. PROVISIONS**

	<b>Mining Related Obligations</b>	<b>Site Restoration &amp; Decommissioning</b>	<b>Total</b>
Balance at April 1, 2010	\$ 3.4	\$ 1.4	\$ 4.8
Charges net of reversals	1.3	0.3	1.6
Utilizations	(1.4)	-	(1.4)
Change in discount rate	(0.1)	-	(0.1)
Balance at March 31, 2011	<u>\$ 3.2</u>	<u>\$ 1.7</u>	<u>\$ 4.9</u>
Charges	-	-	-
Balance at June 30, 2011	<u>\$ 3.2</u>	<u>\$ 1.7</u>	<u>\$ 4.9</u>

**ESSAR STEEL ALGOMA INC.**  
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**18. PROVISIONS (continued)**

	<b>Mining Related Obligations</b>	<b>Site Restoration &amp; Decommissioning</b>	<b>Total</b>
April 1, 2010			
Current Portion	\$ 0.9	\$ 0.4	\$ 1.3
Long Term Portion	2.5	1.0	3.5
<b>Total</b>	<b>\$ 3.4</b>	<b>\$ 1.4</b>	<b>\$ 4.8</b>
March 31, 2011			
Current Portion	\$ 0.1	\$ 1.0	\$ 1.1
Long Term Portion	3.1	0.7	3.8
<b>Total</b>	<b>\$ 3.2</b>	<b>\$ 1.7</b>	<b>\$ 4.9</b>
<b>June 30, 2011</b>			
<b>Current Portion</b>	<b>\$ 0.1</b>	<b>\$ 1.0</b>	<b>\$ 1.1</b>
<b>Long Term Portion</b>	<b>3.1</b>	<b>0.7</b>	<b>3.8</b>
<b>Total</b>	<b>\$ 3.2</b>	<b>\$ 1.7</b>	<b>\$ 4.9</b>

*Mining related obligations*

Obligations are related to site restoration and closure for inactive iron ore mines located in northern Ontario. As there is no associated tangible long-lived asset, changes in the obligation are expensed.

*Site restoration and decommissioning provision / Asset retirement obligations*

This liability represents the Company's obligations associated with site restoration and decommissioning determined based on the Company's best estimate of the costs to be incurred, discounted at risk free rate adjusted for the risk specific to the liabilities. Changes in future conditions could require a change in this liability.

**19. OTHER LONG TERM LIABILITIES**

The other long term liabilities represent the Company's obligation under finance leases.

	<b>June 30, 2011</b>	March 31, 2011	April 1, 2010
Current portion of other long term liabilities	\$ 0.9	\$ 0.9	\$ 0.9
Non-current portion of long term liabilities	1.4	1.6	2.4
	<b>\$ 2.3</b>	<b>\$ 2.5</b>	<b>\$ 3.3</b>

**20. TAX MATTERS**

The components of income tax expense are as follows:

	<b>Three months ended June 30, 2011</b>	Three months ended June 30, 2010
Current tax expense	\$ 2.1	\$ 8.1
Deferred income tax expense	6.8	12.4
<b>Income tax expense</b>	<b>\$ 8.9</b>	<b>\$ 20.5</b>

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**20. TAX MATTERS** *(continued)*

The composition of the deferred income tax expense is as follows:

	<b>Three months ended June 30, 2011</b>	<b>Three months ended June 30, 2010</b>
Initiating and reversing temporary differences:		
Accounting reserves and book-tax basis differences on inventories	\$ 1.0	\$ 0.6
Pension and post-employment benefit expense	(0.5)	0.1
Tax depreciation less than book depreciation	(9.2)	(10.2)
Unrealized gain (loss) on foreign exchange translation on US dollar debt	0.5	(4.8)
Tax loss carry-forward	15.2	2.1
Foreign exchange (loss) gain on translation to presentation currency	(1.5)	24.3
Financing expenses	0.3	-
Other	1.0	0.3
	<b>\$ 6.8</b>	<b>\$ 12.4</b>

**21. COMMITMENTS AND CONTINGENCIES**

*Operating leases*

Under operating leases for premises and equipment, the Company is obligated to make aggregate payments of \$8.5 million, comprised of:

2012	\$ 5.2
2013	2.2
2014	0.5
2015	0.3
2016 and thereafter	0.3
	<b>\$ 8.5</b>

*Key inputs to production*

The Company requires large quantities of iron ore, coal, oxygen, electricity and natural gas in order to satisfy the demands of the steel manufacturing operation. The Company makes most of its purchases of these principal raw materials at negotiated prices under annual and multi-year agreements. These agreements provide the Company with comfort that an adequate supply of these key raw materials will be available to the Company at a price acceptable to the Company. The pricing of the iron ore purchased under these contracts is based on certain published benchmark pricing factors.

*Legal Matters*

From time to time, in the ordinary course of business, the Company is a defendant or party to a number of pending or threatened legal actions and proceedings. Although such matters cannot be predicted with certainty, management currently considers the Company's exposure to such claims and litigation, to the extent not covered by the Company's insurance policies or otherwise provided for, not to have a material adverse effect on these consolidated financial statements. In addition, the Company is involved in and potentially subject to regular audits from federal and provincial tax authorities relating to income, capital and commodity taxes and, as a result of these audits, may receive assessments and reassessments.

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**22. CAPITAL STOCK**

Authorized – Unlimited common shares

	<b>Common shares Issued and Outstanding</b>	
	<b>Number of Shares</b>	<b>Stated Capital</b>
Common shares issued on incorporation	10,000	\$ -
Common shares issued during the period from April 12, 2007 to December 31, 2007	500,000,000	531.8
Balance at March 31, 2008	500,010,000	531.8
Return of capital during fiscal year 2009		41.4
Balance at April 1, 2010, March 31, 2011 and June 30, 2011	500,010,000	\$ 490.4

**23. CONTRIBUTED SURPLUS**

<b>Components of Contributed Surplus:</b>	<b>June 30, 2011</b>	<b>March 31, 2011</b>	<b>April 1, 2010</b>
Algoma Energy Limited Partnership (“AELP”) sale of 49.9% Net gain on the sale of 50.1% interest in AELP	\$ 55.5	\$ 55.5	\$ 55.5
	2.7	2.7	2.7
Contributed surplus at end of period	\$ 58.2	\$ 58.2	\$ 58.2

**24. NET CHANGE IN NON-CASH OPERATING WORKING CAPITAL**

	<b>Three months ended June 30, 2011</b>	<b>Three months ended June 30, 2010</b>
Accounts receivable	\$ (64.9)	\$ 27.1
Income and other taxes payable	(2.4)	0.2
Inventories	(8.6)	9.1
Prepaid expenses and other current assets	(2.2)	2.0
Accounts payable and accrued liabilities	15.6	(38.0)
Loan receivable from related party	3.0	(0.3)
	\$ (59.5)	\$ 0.1

**ESSAR STEEL ALGOMA INC.**  
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**25. RELATED PARTY TRANSACTIONS AND BALANCES**

The Company's shareholder, ESSAR Steel Holdings Limited and its commonly controlled affiliates are related parties. Related party transactions which occur in the ordinary course of business are measured at the exchange amount, which is the amount of consideration agreed to between the parties.

The following transactions are reflected in the condensed interim consolidated statement of comprehensive income:

	<b>Three months ended June 30, 2011</b>	<b>Three months ended June 30, 2010</b>
Purchases of raw materials from Essar Steel Holdings Limited, the Company's shareholder	\$ 15.1	\$ 3.3
Fees received for services provided to affiliated companies under common control	0.6	\$ 0.6
Interest income earned from an affiliated company under common control	0.1	0.1
Fees paid for services purchased from affiliated companies under common control	(3.6)	(4.8)

The following balances are reflected in the condensed interim consolidated statement of financial position:

	<b>June 30, 2011</b>	<b>March 31, 2011</b>	<b>April 1, 2010</b>
The following balances with affiliated companies under common control were outstanding at the end of the reporting period:			
Accounts receivable	<i>a</i> \$ 0.7	\$ 3.8	\$ 1.9
Loan receivable from related party	<i>b</i> 10.6	10.7	-
Interest receivable	<i>c</i> 0.5	0.3	-
Accounts payable	<i>a</i> 0.7	0.7	1.2

The following balances with the Company's shareholder were outstanding at the end of the reporting period:

Prepaid expenses	<i>a</i> 0.9	0.3	-
Accounts payable	<i>a</i> 2.2	-	-

*a* Trade balances, bearing no interest due within 30 and 60 days.

*b* Promissory Note bearing interest at a rate of 3.29% per annum, due on demand.

*c* Interest receivable under promissory note "b" due on demand.

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**25. RELATED PARTY TRANSACTIONS AND BALANCES (continued)**

**Contractual relationships with related parties:**

The Company holds a promissory note in the amount of US dollar 11 million. The note is due from Essar Minerals Canada Limited. The note is due on demand, and bears interest at a rate of 3.29% per annum.

In November 2009, the Company entered into 20-year agreements with Essar Power Canada Limited as follows:

- [i] Energy Supply Agreement to purchase electricity at the Hourly Ontario Energy Price.
- [ii] A Shared Services Agreement to provide employees and other services.
- [iii] A Lease Agreement for the land on which the facility is built is for a nominal amount annually.

The Company's purchases and income under this agreement are reflected above.

The Company has entered into agreements with a related party to source its coal requirements until June 30, 2012 at predetermined prices. The Company's purchases under these agreements are reflected above.

**26. FINANCIAL INSTRUMENTS**

**Financial risk management**

The Company's activities expose it to a variety of financial risks including credit risk, liquidity risk and market risk. The Company may use derivative financial instruments to hedge certain of these risk exposures. The use of derivatives is based on established practices and parameters, which are subject to the oversight of the Board of Directors. The Company does not utilize derivative financial instruments for trading or speculative purposes.

**Fair value of financial instruments**

The fair value of cash, accounts receivable, loan receivable from related party, bank indebtedness and accounts payable and accrued liabilities approximates their carrying value due to the short-term nature of these instruments. At June 30, 2011, the fair value of the Senior Notes, including the embedded call options, was approximately \$345.1 million (March 31, 2011 - \$351.6 million; April 1, 2010 - \$359.8 million) based on market pricing for the Senior Notes on or about that date. At June 30, 2011, the fair value of the Secured Notes, including the embedded call options, was approximately \$386.8 million (March 31, 2011 - \$393.7 million; April 1, 2010 - \$410.4 million) based on market pricing for the Secured Notes on or about that date.

The following table represents the fair value hierarchy of derivative financial instruments by level:

Reporting Period	Measurement	Total Carrying Value	Level One	Level Two	Level Three
June 30, 2011	Fair value	\$ -	\$ -	\$ -	\$ -
March 31, 2011	Fair value	(0.5)	-	(0.5)	-
April 1, 2010	Fair value	(2.8)	-	(2.8)	-

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**26. FINANCIAL INSTRUMENTS** *(continued)*

**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, and arises primarily from the Company's receivables from customers. The Company has an established credit policy under which each new customer is analyzed individually for creditworthiness before the Company's standard payment and delivery terms and conditions are offered. The Company's review includes a review of the potential customer's financial information, external credit ratings and bank and supplier references. Credit limits are established for each new customer and customers that fail to meet the Company's credit requirements may transact with the Company only on a prepayment basis.

The maximum credit exposure at June 30, 2011 is the carrying amount of accounts receivable of \$221.7 million (March 31, 2011 - \$160.4 million; April 1, 2010 - \$203.5 million). At June 30, 2011 there was no one customer account that represented 10% of this amount (March 31, 2011 - one customer greater than 10%; April 1, 2010 - one customer greater than 10%). As at June 30, 2011 \$5.1 million or 2.3% of accounts receivable were more than 90 days overdue (March 31, 2011 - \$7.3 million or 4.5%; April 1, 2010 - \$11.8 million, or 5.8%).

The Company establishes an allowance for doubtful accounts that represents its estimate of incurred losses in respect of accounts receivable. The main components of this allowance are a specific provision that relates to individual exposures and a provision for expected losses that have been incurred but not yet identified. The allowance for doubtful accounts at June 30, 2011 was \$1.6 million (March 31, 2011 - \$1.6 million; April 1, 2010 - \$2.2 million).

The Company may be exposed to certain losses in the event of non-performance by counterparties to derivative financial instruments such as commodity price contracts and foreign exchange contracts. The Company mitigates this risk by entering into transactions with highly rated major financial institutions.

**Liquidity risk**

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they come due. The Company manages liquidity risk by maintaining adequate cash balances and by appropriately utilizing the Revolving Facility to ensure that there is sufficient availability under the facility. The details of the Revolving Facility are described in Note 13. The Company continuously monitors and reviews actual and forecasted cash flows to ensure adequate liquidity and anticipate liquidity requirements. The Company's objectives and processes for capital management, including the management of long term debt, are described in Note 15.

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**26. FINANCIAL INSTRUMENTS (continued)**

The following table shows the Company's contractually agreed (undiscounted) cash flows payable under financial liabilities and derivative financial instruments as at the reporting period end:

**June 30, 2011**

<b>Undiscounted Cash Flows</b>	<b>Carrying Amount</b>	<b>Contractual Cash Flows</b>	<b>Less Than 1 year</b>	<b>1-2 years</b>	<b>2-5 years</b>	<b>More Than 5 years</b>
<b>Non-derivative financial liabilities</b>						
Senior Notes	\$ 371.0	\$ (371.0)	\$ -	\$ -	\$(371.0)	\$ -
Interest on Senior Notes	1.5	(146.4)	(36.6)	(36.6)	(73.2)	-
Secured Notes	385.8	(385.8)	-	-	(385.8)	-
Interest on Secured Notes	10.5	(144.7)	(36.2)	(36.2)	(72.3)	-
Revolving Facility	168.2	(168.2)	(168.2)	-	-	-
Accounts payable and accrued liabilities	185.5	(185.5)	(185.5)	-	-	-
	<b>\$ 1,122.5</b>	<b>\$ (1,401.6)</b>	<b>\$ (426.5)</b>	<b>\$ (72.8)</b>	<b>\$(902.3)</b>	<b>\$ -</b>

**March 31, 2011**

<b>Undiscounted Cash Flows</b>	<b>Carrying Amount</b>	<b>Contractual Cash Flows</b>	<b>Less Than 1 year</b>	<b>1-2 years</b>	<b>2-5 years</b>	<b>More Than 5 years</b>
<b>Non-derivative financial liabilities</b>						
Senior Notes	\$ 373.0	\$ (373.0)	\$ -	\$ -	\$(373.0)	\$ -
Interest on Senior Notes	10.7	(184.2)	(36.8)	(36.8)	(110.6)	-
Secured Notes	387.8	(387.8)	-	-	(387.8)	-
Interest on Secured Notes	1.5	(145.4)	(36.4)	(36.4)	(72.6)	-
Revolving Facility	184.5	(184.5)	(184.5)	-	-	-
Accounts payable and accrued liabilities	169.2	(169.2)	(169.2)	-	-	-
Derivative financial instruments (a)						
Gas purchase swap	0.5	(0.5)	(0.5)	-	-	-
	<b>\$ 1,127.2</b>	<b>\$ (1,444.6)</b>	<b>\$ (427.4)</b>	<b>\$ (73.2)</b>	<b>\$ (944.0)</b>	<b>\$ -</b>

**April 1, 2010**

<b>Undiscounted Cash Flows</b>	<b>Carrying Amount</b>	<b>Contractual Cash Flows</b>	<b>Less Than 1 year</b>	<b>1-2 years</b>	<b>2-5 years</b>	<b>More Than 5 years</b>
<b>Non-derivative financial liabilities</b>						
Senior Notes	\$ 390.8	\$ (390.8)	\$ -	\$ -	\$ -	\$ (390.8)
Interest on Senior Notes	11.3	(204.2)	(38.6)	(38.6)	(115.8)	(11.2)
Secured Notes	406.1	(406.1)	-	-	(406.1)	-
Interest on Secured Notes	1.7	(193.2)	(38.6)	(38.7)	(115.9)	-
Revolving Facility	92.2	(92.2)	(92.2)	-	-	-
Accounts payable and accrued liabilities	181.1	(181.1)	(181.1)	-	-	-
Derivative financial instruments (a)						
Interest rate swap	2.7	(2.7)	(2.7)	-	-	-
	<b>\$ 1,085.9</b>	<b>\$ (1,470.3)</b>	<b>\$ (353.2)</b>	<b>\$ (77.3)</b>	<b>\$(637.8)</b>	<b>\$ (402.0)</b>

(a) – The derivative financial instruments cash outflows represent the net contractual obligation

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**26. FINANCIAL INSTRUMENTS** *(continued)*

**Market risk**

Market risk is the risk that changes in market prices, such as foreign exchange rates, interest rates and commodity 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.

The Company occasionally buys and sells derivatives in order to manage market risks. These activities are carried out under the oversight of the Board of Directors.

**Currency risk**

The Company is exposed to currency risk on purchases, labour costs and pension (Note 16) and other post retirement employment benefits (Note 17) liabilities that are denominated in Canadian dollars. The prices for steel products sold in Canada are derived mainly from price levels in the US market in US dollars converted into Canadian dollars at the prevailing exchange rates. As a result, a stronger US dollar relative to the Canadian dollar increases the Company's Canadian dollar selling prices for sales within Canada.

The Company's Canadian dollar denominated financial instruments were as follows:

	<u>June 30, 2011</u>	<u>March 31, 2011</u>	<u>April 1, 2010</u>
Cash	\$ 9.8	\$ 2.1	\$ -
Accounts receivable	111.1	77.5	102.9
Bank indebtedness	-	(5.2)	(92.2)
Accounts payable and accrued liabilities	(165.5)	(157.3)	(158.9)
Other long-term liabilities	<u>(2.3)</u>	<u>(2.5)</u>	<u>(3.3)</u>
<b>Net Canadian dollar liability</b>	<b><u>\$ (46.9)</u></b>	<b><u>\$ (85.4)</u></b>	<b><u>\$ (151.5)</u></b>

A \$0.01 decrease (or increase) in the US dollar relative to the Canadian dollar at June 30, 2011 would have increased (or decreased) income from operations by \$1.1 million (June 30, 2010 - \$0.4 million).

**Interest rate risk**

Interest rate risk is the risk that the value of the Company's assets and liabilities will be affected by a change in interest rates. The Company's interest rate risk mainly arises from the interest rate impact on its debt. The Company may manage interest rate risk through the periodic use of interest rate swaps.

For the periods ended June 30, 2011 and June 30, 2010 one percent increase (or decrease) in interest rates would have had a negligible effect on net earnings.

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**26. FINANCIAL INSTRUMENTS** *(continued)*

**Commodity price risk**

The Company is subject to price risk from fluctuations in the market prices of commodities, including natural gas, iron ore and coal. The Company enters into supply agreements for certain of these commodities as disclosed in Note 21. To manage risks associated with future variability in cash flows attributable to certain commodity purchases, the Company may use derivative instruments with maturities of 12 months or less. At June 30, 2011 the company did not have any natural gas swap contracts in place. At March 31, 2011, the fair value of natural gas swap contracts was a liability of \$0.5 million, which was included in accounts payable and accrued liabilities (April 1, 2010 - nil).

**27. TRANSITION TO INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS)**

**27.1 First-time Adoption of IFRS**

The Company has adopted IFRS effective April 1, 2011. Prior to the adoption of IFRS, the Company presented its consolidated financial statements in accordance with previous CGAAP.

IFRS 1 – First-time Adoption of International Financial Reporting Standards (“IFRS 1”) requires first-time adopters to apply IFRS retrospectively as if IFRS had been in effect from the date of the Company’s inception. The Company’s first annual consolidated financial statements prepared in accordance with IFRS will be for the fiscal year ending March 31, 2012. Accordingly, the Company will make an unreserved statement of compliance with IFRS beginning with its 2012 annual financial statements. The Company’s transition date is April 1, 2010 and an opening condensed interim consolidated statement of financial position has been prepared as at that date.

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**27. TRANSITION TO INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS) (continued)**

The condensed interim consolidated financial statements for the period ended June 30, 2011 are prepared in accordance with IAS 34 – Interim Financial Statements. These consolidated financial statements have been presented in accordance with the IFRS accounting policies discussed in Note 3. The Company will ultimately prepare its opening condensed consolidated statement of financial position as at April 1, 2010 and financial statements for the year ended March 31, 2012 by applying IFRS that are in effect as at March 31, 2012. The IFRS standards and IFRIC interpretations applicable at March 31, 2012, including those applicable on an optional basis, were not known with certainty at the time of preparing these condensed interim consolidated financial statements.

**27.2 Presentation of Consolidated Financial Statements**

*Consolidated Statement of Comprehensive Income*

A full reconciliation of the condensed consolidated statements of comprehensive income previously reported under previous CGAAP to that prepared under IFRS is presented in Note 27.7.

*Condensed Interim Consolidated Statement of Financial Position*

IFRS requires certain items, some of which the Company previously grouped together, to be presented separately on the face of the condensed interim consolidated statement of financial position. As part of the transition to IFRS, the term “future income taxes” has been replaced with “deferred income taxes”. Under IFRS all deferred income tax assets or liabilities are classified as non-current. These reclassifications for presentation under IFRS are shown in the restated statement of financial position under IFRS as “IFRS Reclassifications”.

**27.3 Elected exemptions from full retrospective application**

IFRS 1 provides entities preparing their first IFRS compliant financial statements with several optional exemptions from full retrospective application of IFRS. The Company has applied certain of these optional exemptions as described below.

*Business combinations*

This exemption allows the Company to not apply IFRS 3 - *Business Combinations* retrospectively to past business combinations. The Company has elected to apply this exemption and therefore has not restated business combinations that took place prior to the Transition Date. The Company does not have goodwill arising on business combinations that occurred before the Transition Date.

*Employee benefits*

This exemption permits the Company to reset its cumulative unamortized actuarial gains and losses to zero by recognizing the full amount in opening retained earnings as at April 1, 2010. The Company has elected to apply this exemption.

*Cumulative translation differences*

This exemption permits the Company to reset its cumulative translation differences to zero by recognizing the full amount in opening retained earnings as at April 1, 2010 after adjusting for the change in the functional currency as determined under IFRS. The Company has elected to apply this exemption.

**ESSAR STEEL ALGOMA INC.**  
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**27. TRANSITION TO INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS) (continued)**

*Borrowing costs*

This exemption allows the Company to adopt IAS 23 - *Borrowing Costs*, which requires the capitalization of borrowing costs on all qualifying assets, prospectively from the Transition Date. The Company has elected to apply this exemption.

*Leases*

This exemption applies to first-time adopters who have made a determination of whether an arrangement contained a lease in accordance with a previous CGAAP. The Company has elected to apply this exemption.

**27.4 Mandatory exception to retrospective application of IFRS**

In preparing these condensed interim consolidated financial statements in accordance with IFRS 1, the following mandatory exception from full retrospective application of IFRS is applicable to the Company.

*Estimates*

Estimates made by the Company under previous CGAAP are consistent with their application under IFRS.

**27.5 Reconciliation of shareholder's equity from previous CGAAP to IFRS**

The following is a reconciliation of the Company's total shareholder's equity reported in accordance with previous CGAAP to its shareholder's equity reported in accordance with IFRS for the following dates:

	Note	March 31, 2011	June 30, 2010	April 1, 2010
Total shareholder's equity as reported under previous CGAAP		\$ 95.5	\$ 449.5	\$ 389.9
Transitional adjustments:				
Property, plant and equipment	<i>a</i>	(58.0)	(42.5)	(38.5)
Provisions	<i>b</i>	3.2	2.4	2.4
Employee benefits	<i>c</i>	(165.3)	(104.1)	(108.3)
Foreign exchange gains (losses)	<i>d</i>	(31.7)	(44.8)	(43.4)
Income taxes	<i>e</i>	88.6	32.7	56.9
Total transitional adjustments		\$ (163.2)	\$ (156.3)	\$ (130.9)
Total as reported under IFRS		\$ (67.7)	\$ 293.2	\$ 259.0

*a Property, plant and equipment*

IAS 16 – Property, Plant and Equipment requires the Company to componentize the amount initially recognized in respect of an item of property, plant and equipment to its significant parts and depreciate each part separately over its useful life. The Company determined that certain of its equipment assets have additional separable parts or “components”. These components were separately depreciated over their useful lives, which are usually less than the equipment to which the components belong, resulting in a higher depreciation charge.

**ESSAR STEEL ALGOMA INC.**  
**Notes to the Condensed Interim Consolidated Financial Statements (Unaudited)**  
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**27. TRANSITION TO INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS) (continued)**

*b Provisions*

Under IFRS, reserves and/or accruals for which there is a significant degree of uncertainty about the amount or timing of the payment are classified as provisions. In addition, a provision must be discounted when the time-value of money is material. Therefore, the Company reclassified certain accruals to provisions and has discounted these provisions where applicable.

Furthermore, IFRS specifies that the discount rate applied to the provision must be the rate that reflects the risks associated with the obligation. Under previous CGAAP, the Company measured its provisions for asset retirement obligations using the credit adjusted risk-free rate. As a result, the Company has re-measured its provisions for asset retirement obligations, which are now referred to as site restoration and decommissioning provisions under IFRS.

Under previous CGAAP, reserves and accruals are only recorded when a legal obligation exists. Under IFRS provisions are recorded for both legal and constructive obligations. A constructive obligation exists when an action by the Company indicates to a third party that it will accept certain responsibilities, and creates a valid expectation on the part of that third party that it will discharge those responsibilities.

*c Employee Benefits*

Under previous CGAAP the Company was using the corridor method to amortize gains and losses. On transition to IFRS, the Company elected to reset all cumulative unamortized actuarial gains and losses to zero as at the Transition Date. Cumulative actuarial gains and losses that existed at the Transition Date were recognized in opening retained earnings for the Company's employee benefit plans. The Company recognized all actuarial gains and losses that arose subsequent to the Transition Date immediately in OCI.

*d Foreign exchange gains (losses)*

The Company elected to reset all cumulative translation differences to zero as at the Transition Date. Cumulative translation differences that existed at the Transition Date were fully recognized in opening retained earnings. This adjustment also reflects foreign exchange translation impact of changes in the value of non-monetary items resulting from IFRS adjustments.

*e Income taxes*

This adjustment reflects the change in current or deferred income taxes resulting from the effect of the IFRS adjustments described as allowed under IAS 12 - Income Taxes. This adjustment also includes the impact of recognition of deferred income taxes on temporary differences on non-monetary items due to the change in the exchange rate as the Company's taxable earnings are determined in a different currency from its functional currency.

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**27. TRANSITION TO INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS) (continued)**

**27.6 Reconciliation of Comprehensive Income from previous CGAAP to IFRS**

The following is a reconciliation of the Company's net income (loss) reported in accordance with previous CGAAP to its net loss in accordance with IFRS for the following periods:

	Note	Three months ended June 30, 2010	Year ended March 31, 2011
<b>Total net income (loss) as reported under previous CGAAP</b>		\$ 39.7	\$ (285.9)
Transitional adjustments:			
Property, plant and equipment	<i>a</i>	(4.0)	(19.5)
Provisions	<i>b</i>	-	0.8
Employee benefits	<i>c</i>	4.2	(26.2)
Foreign exchange translation	<i>d</i>	5.4	2.8
Income taxes	<i>e</i>	(24.2)	24.0
Total transitional adjustments		<u>\$ (18.6)</u>	<u>\$ (18.1)</u>
<b>Total net income (loss) as reported under IFRS</b>		<u>\$ 21.1</u>	<u>\$ (304.0)</u>
<b>Comprehensive income (loss) as reported under previous CGAAP</b>		\$ 59.6	\$ (294.4)
Transitional adjustments:			
Adjustments to net loss		(18.6)	(18.1)
Employee benefit revaluation losses (net of tax of \$7.7 million at March 31, 2011)	<i>c</i>	-	(23.1)
Foreign exchange (gain) loss on translation to presentation currency	<i>f</i>	(6.8)	8.9
Total transitional adjustments		<u>\$ (25.4)</u>	<u>\$ (32.3)</u>
<b>Total comprehensive income (loss) as reported under IFRS</b>		<u>\$ 34.2</u>	<u>\$ (326.7)</u>

*a Property, plant and equipment*

Additional significant components of certain assets are depreciated separately over a shorter useful life. As a result, higher depreciation was charged on these components.

*b Provisions*

The fair value of the site restoration and decommissioning provision is estimated using the expected cash flow approach that reflects a range of possible outcomes discounted at the risk-free interest rate adjusted for the risks specific to the liabilities at the end of the reporting period.

**ESSAR STEEL ALGOMA INC.**  
**Notes to the Condensed Interim Consolidated Financial Statements (Unaudited)**  
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**27. TRANSITION TO INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS) (continued)**

*c Employee benefit revaluation losses*

The Company elected to recognize all cumulative actuarial gains and losses as at the Transition Date. As a result, the Company adjusted its pension and other post-employment benefits expenses to remove the amortization of actuarial gains and losses. Furthermore, the Company's policy under IFRS is to record revaluation gains and losses into OCI. Under previous CGAAP, the Company was recognizing revaluation gains and losses into net earnings using the corridor approach.

*d Foreign exchange translation*

This adjustment reflects the foreign exchange impact of changes in the carrying value of items resulting from the effect of the IFRS adjustments described.

*e Income taxes*

This adjustment reflects the change in current or deferred income taxes resulting from the effect of the IFRS adjustments described as allowed under IAS 12 - Income Taxes. This adjustment also includes the impact of recognition of deferred income taxes on temporary differences due to the change in the exchange rate as the Company's taxable earnings are determined in a different currency.

*f Foreign exchange loss (gain) on translation to presentation currency*

This adjustment reflects exchange translation differences resulting from the use of a presentation currency other than the functional currency on amounts as determined under IFRS. This adjustment also includes incremental foreign exchange differences on non-current non-monetary items resulting from the change in functional currency as determined under IFRS.

**27.7 Restated Financial Statements**

The following are reconciliations of the financial statements reported under previous CGAAP to amended financial statements prepared under IFRS.

**ESSAR STEEL ALGOMA INC.**  
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**27. TRANSITION TO INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS) (continued)**

**27.7.1 Restated Condensed Consolidated Statement of Financial Position under IFRS - As at April 1, 2010:**

	Previous CGAAP	Reclass- ifications	IFRS Adjustments	IFRS	
<b>Assets</b>					
Cash	\$ 40.2			\$ 40.2	
Accounts receivable	203.5			203.5	
Income taxes receivable	21.4			21.4	
Inventories	289.3			289.3	
Prepaid expenses	7.4			7.4	
Future income tax assets	1.5	\$ (1.5)		-	
<b>Total current assets</b>	<b>\$ 563.3</b>			<b>\$ 561.8</b>	
Property, plant and equipment, net	\$ 1,552.8		\$ (76.9)	\$ 1,475.9	
Intangible assets, net	116.5		(5.4)	111.1	
Other assets	2.5		(0.5)	2.0	
		1.5		1.5	Deferred income tax assets
	<u>\$ 2,235.1</u>			<u>\$ 2,152.3</u>	
<b>Liabilities and shareholder's equity</b>					
<b>Current</b>					
Bank indebtedness	\$ 92.2			\$ 92.2	
Accounts payable and accrued liabilities	194.1	0.3		194.4	
Income taxes payable	0.3	(0.3)			
Accrued post-employment benefit obligation	18.2	(18.2)			
		1.3		1.3	Current portion of provisions
		0.9		0.9	Current portion of other long term liabilities
Current portion of capital leases and other long term liabilities	2.2	(2.2)			
Future income tax liabilities	3.5	(3.5)			
<b>Total current liabilities</b>	<b>\$ 310.5</b>			<b>\$ 288.8</b>	
Long term provisions					
Long term debt	\$ 776.5			\$ 776.5	
Accrued pension liability	135.5		126.7	262.2	
Accrued post-employment benefit obligation	405.0	18.2	(18.4)	404.8	
		6.8	(3.3)	3.5	Provisions
		2.4		2.4	Other long term liabilities
Other long term liabilities	9.2	(9.2)			
Future income tax liabilities	208.5	3.5	(56.9)	155.1	Deferred income tax liabilities
<b>Total Liabilities</b>	<b>\$ 1,845.2</b>			<b>\$ 1,893.3</b>	
<b>Shareholder's Equity</b>					
Capital Stock	\$ 490.4			\$ 490.4	
Contributed surplus	58.2			58.2	
Accumulated other comprehensive income (loss)	34.3		(34.3)	-	
Deficit	(193.0)		(96.6)	(289.6)	
<b>Total Shareholder's equity</b>	<b>\$ 389.9</b>			<b>\$ 259.0</b>	
<b>Total liabilities and shareholder's equity</b>	<b>\$ 2,235.1</b>			<b>\$ 2,152.3</b>	

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**27. TRANSITION TO INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS) (continued)**

**27.7.2 Restated Condensed Consolidated Statement of Financial Position under IFRS – as at March 31, 2011:**

	Previous CGAAP	Reclass- ifications	IFRS Adjustments	IFRS	
<b>Assets</b>					
Cash	\$ 5.7			\$ 5.7	
Accounts receivable	160.4			160.4	
Income taxes receivable	2.5			2.5	
Loan receivable from related party	11.0			11.0	
Inventories	278.2		\$ 0.2	278.4	
Prepaid expenses	4.5			4.5	
Future income tax assets	1.5	\$ (1.5)			
	<u>\$ 463.8</u>			<u>\$ 462.5</u>	
Property, plant and equipment, net	\$ 1,363.0		(85.2)	\$ 1,277.8	
Intangible assets, net	95.0		(4.4)	90.6	
Other assets	1.4		(0.2)	1.2	
		1.5	(0.1)	1.4	Deferred income tax assets
	<u>\$ 1,923.2</u>			<u>\$ 1,833.5</u>	
<b>Liabilities and shareholder's equity</b>					
<b>Current</b>					
Bank indebtedness	\$ 184.5			\$ 184.5	
Accounts payable and accrued liabilities	181.4			181.4	
Accrued post-employment benefit obligation	20.5	(20.5)			
		1.1		1.1	Current portion of provisions
		0.9		0.9	Current portion of other long term liabilities
Current portion of capital lease and other long term liabilities	2.0	(2.0)			
Future income tax liabilities	2.2	(2.2)			
<b>Total current liabilities</b>	<u>\$ 390.6</u>			<u>\$ 367.9</u>	
Long term debt	\$ 742.8			\$ 742.8	
Accrued pension liability	144.6		163.5	308.1	
Accrued post-employment benefit obligation	418.6	20.5	1.8	440.9	
		7.0	(3.2)	3.8	Provisions
		1.6		1.6	Other long-term liabilities
Other long term liabilities	8.6	(8.6)			
Future income tax liabilities	122.5	2.2	(88.6)	36.1	Deferred income tax liabilities
<b>Total Liabilities</b>	<u>\$ 1,827.7</u>			<u>\$ 1,901.2</u>	
<b>Shareholder's Equity</b>					
Capital Stock	\$ 490.4			\$ 490.4	
Contributed surplus	58.2			58.2	
Accumulated other comprehensive income (loss)	25.8		(48.5)	(22.7)	
Deficit	(478.9)		(114.7)	(593.6)	
<b>Total Shareholder's equity</b>	<u>\$ 95.5</u>			<u>\$ (67.7)</u>	
<b>Total liabilities and shareholder's equity</b>	<u>\$ 1,923.2</u>			<u>\$ 1,833.5</u>	

**ESSAR STEEL ALGOMA INC.**

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**27. TRANSITION TO INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS) (continued)**

**27.7.3 Restated Condensed Consolidated Statement of Comprehensive Income - Function of Expense format under previous CGAAP - for the period ended June 30, 2010:**

	Previous CGAAP	Adjustments for New Format	Function of Expense Format under previous CGAAP	
Sales	\$ 475.7		\$ 475.7	Revenue
Operating Expenses				Operating Expenses
		\$ 436.2	\$ 436.2	Cost of sales
Cost of sales excluding amortization	\$ 390.0	(390.0)		
Amortization	46.2	(46.2)		
	<u>\$ 436.2</u>			
Administrative and selling Amortization of intangible assets and non-productive assets	14.1	5.8	19.9	Administrative and selling
	<u>5.8</u>	<u>(5.8)</u>		
Income from operations	\$ 19.6		\$ 19.6	Income from operations
Interest on long-term liabilities, net	\$ 19.4	(19.4)		
Interest on short-term liabilities	1.9	(1.9)		
		21.3	\$ 21.3	Finance cost
Foreign exchange loss	(37.6)		(37.6)	
Investment income	<u>(0.1)</u>		<u>(0.1)</u>	Finance income
	\$ (16.4)		\$ (16.4)	
Income before income taxes	\$ 36.0		\$ 36.0	Income before income taxes
Income taxes				
Current Expense	\$ 8.0	(8.0)		
Future recovery	<u>(11.7)</u>	11.7		
	\$ (3.7)	<u>(3.7)</u>	<u>(3.7)</u>	Income taxes
Net income for the period	\$ 39.7		\$ 39.7	Net income
Unrealized gain on foreign exchange translation	<u>19.9</u>		<u>19.9</u>	Foreign exchange gain on translation to presentation currency
Comprehensive Income	<u>\$ 59.6</u>		<u>\$ 59.6</u>	Total comprehensive income

**ESSAR STEEL ALGOMA INC.****Notes to the Condensed Interim Consolidated Financial Statements (Unaudited)**

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**27. TRANSITION TO INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS) (continued)****27.7.4 Restated Condensed Consolidated Statement of Comprehensive Income under IFRS - for the period ended June 30, 2010:**

	Function of Expense Format under Previous CGAAP	IFRS Adjustments	IFRS
Revenue	\$ 475.7		\$ 475.7
Operating expenses			
Cost of sales	436.2	\$ (1.8)	434.4
Administrative and selling	19.9	(0.8)	19.1
Income from operations	\$ 19.6		\$ 22.2
Finance cost	\$ 21.3	-	\$ 21.3
Foreign exchange gain	(37.6)	(3.1)	(40.7)
Finance income	(0.1)	0.1	-
	\$ (16.4)		\$ (19.4)
Income before income taxes	\$ 36.0		\$ 41.6
Income taxes	(3.7)	24.2	20.5
Net income	\$ 39.7	(18.6)	\$ 21.1
Foreign exchange (loss) gain on translation to presentation currency	19.9	(6.8)	13.1
Total comprehensive income	\$ 59.6		\$ 34.2

**27.8 Reconciliation of cash flows from previous CGAAP to IFRS**

All adjustments to the Company's consolidated statements of cash flows reported in accordance with IFRS relate to non cash movements. Significant adjustments have been made to depreciation and amortization, pension expense in excess of current funding and deferred income tax expense recovery as a result of the transitional adjustments described above.

Net finance cost and income tax expense are included in "operating activities" and interest paid, interest received and income taxes paid are included in "cash generated from operating activities" in the consolidated statements of cash flows under IFRS.

**28. SELECTED ANNUAL DISCLOSURES**

These condensed interim consolidated financial statements are the Company's first consolidated financial statements prepared using IFRS. Certain disclosures required by IFRS were disclosed in a different way, or were not required under previous CGAAP. The Company has included unaudited annual IFRS disclosures for the year ended March 31, 2011 to assist the user in understanding these condensed interim consolidated financial statements.

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**28. SELECTED ANNUAL DISCLOSURES** *(continued)*

**28.1 Taxation**

**Audit by tax authorities**

In the ordinary course of business, the Company is subject to ongoing audits by tax authorities. While the Company believes that its tax filing positions are appropriate and supportable, from time to time, certain matters are reviewed and challenged by the tax authorities.

In the second quarter of fiscal 2010, the Canada Revenue Agency (“CRA”) concluded its review of the Company’s assignment of \$160.0 million as the fair market value of the 16 million common shares issued as consideration in discharging debts under the 2002 financial reorganization. The CRA reduced the fair market value assigned to the common shares to \$126.4 million and, as a result, reassessed the Company’s , 2002 to 2006 taxation years to reflect a reduced amount of available non-capital loss carryforwards. The Company had filed an objection to the CRA reassessments and no provision had been made in the condensed interim consolidated statement of comprehensive income for the income taxes or interest associated with the reassessments. The Company paid the reassessments, which totalled \$2.0 million including \$0.5 million of interest, and had reflected this amount as a recoverable netted with income and other taxes payable in the statement of financial position. In October 2010 the CRA issued notices of reassessment which accepted the objection filed by the Company and refunded the amounts previously paid in addition to refund interest.

There have been no material changes in ongoing audits by tax authorities.

The Company regularly reviews the potential for adverse outcomes in respect of tax matters. The Company believes that the ultimate disposition of any tax matters in dispute with tax authorities will not have a material adverse effect on its liquidity, consolidated financial position or results of operations because the Company believes that it has adequate provision for these tax matters. Should the ultimate tax liability materially differ from the provision, the Company’s effective tax rate and its earnings could be affected positively or negatively in the period in which the matters are resolved.

*Scientific research and experimental development claims*

For the fiscal years 2002-2010, the Company has filed, or intends to file, scientific research and experimental development (“SR&ED”) claims with the CRA totalling \$366.7 million. The potential tax benefit on these claims is 20% to 24% of the claims or \$74.6 million. To date, \$31.9 million of the potential tax benefit, the portion that management believes meets the threshold of “reasonable assurance” of realization, has been recognized. The determination of the amount of tax benefit to recognize requires judgement, and is subject to change based on the CRA’s audit of the claims which may result in adjustments to net earnings.

The CRA has assessed \$3.4 million of tax credits in respect of 2002 to which the Company has objected. In August and September 2010, the Company reached agreements with the CRA on \$19.6 million of tax credits for the years 2003-2006.

**Deferred income tax assets**

Deferred income tax assets are recognized to the extent that it is determined to be more likely than not that sufficient taxable income will be available within the carryforward periods to allow the asset to be realized. The determination is made at the statement of financial position dates by assessing all positive and negative evidence regarding the future sources of taxable income.

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**28. SELECTED ANNUAL DISCLOSURES**

**28.1 Taxation (continued)**

**Loss carryforwards**

The Company has non-capital losses available of \$232.4 million of which \$29.7 million expire in 2030 and \$202.7 million in 2031.

The Company's subsidiary, Cannelton Iron Ore Company, has non-capital losses available on a calendar year basis, which are limited to use under Internal Revenue Code 382, of approximately US \$38.3 million, of which US \$1.9 million expire in 2021 and US \$36.4 million in 2022.

Income taxes in the condensed consolidated statement of comprehensive income vary from amounts that would be computed by applying statutory income tax rates for the following reasons:

	<b>Year ended March 31, 2011</b>
Loss before income taxes	<u>\$ (415.2)</u>
Income taxes based on the applicable tax rate of 28.4%	(117.9)
Add / (deduct):	
Non taxable portion of exchange gain on US dollar currency	(1.5)
Initiating future tax asset recognized at tax rates lower than statutory rate	6.9
Other	<u>1.3</u>
Recovery of income taxes	<u>\$ (111.2)</u>

The applicable tax rate is the aggregate of the Canadian federal income tax rate of 17.6% and the Canadian provincial income tax rate of 10.8%.

The tax-effected temporary differences which result in deferred income tax assets and (liabilities) and the amount of deferred income taxes recognized in the consolidated statement of comprehensive income are as follows:

<b>Undiscounted Cash Flows</b>	<b>Balance at April 1, 2010</b>	<b>Recognized in Deferred Income Tax Expense</b>	<b>Recognized in Other Comprehensive Income</b>	<b>Balance at March 31, 2011</b>
Accounting reserves	1.4	-	-	1.4
Defined pension benefit	101.3	8.9	-	110.2
Other post-employment benefits	65.5	3.9	7.7	77.1
Loss carryforward	8.5	49.8	-	58.3
Financial instruments	9.2	(1.3)	-	7.9
Property, plant and equipment and intangible assets	(331.2)	54.4	-	(276.8)
Unrealized exchange gains on US dollar debt	(4.9)	(4.6)	-	(9.5)
Inventory reserve	(3.4)	1.0	-	(2.4)
Other	-	(0.9)	-	(0.9)
Net deferred tax liability	<u>(153.6)</u>	<u>111.2</u>	<u>7.7</u>	<u>(34.7)</u>

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**28. SELECTED ANNUAL DISCLOSURES** *(continued)*

**28.2 Defined Pension Benefit Plans**

The principal assumptions used for the purposes of the actuarial valuations at March 31, 2011 were as follows

Accrued benefit obligation:	
Discount rate	5.86%
Rate of compensation increase	3.50%
Net periodic pension costs:	
Discount rate	5.60%
Expected long-term rate of return on plan assets	6.34%
Rate of compensation increase	2.74%

Amounts immediately recognized in other comprehensive income, net of income tax in respect of these defined benefit plans for the year ended March 31, 2011 are as follows:

Actuarial losses on defined benefit obligation	\$	(24.0)
Actuarial gain on plan assets		15.6
Change in effect of ceiling limit		(4.3)
Less tax effect		3.2
Total defined benefit cost recognized immediately in OCI	\$	<u>(9.5)</u>

Movements in the present value of the plan assets for the year ended March 31, 2011 were as follows.

Fair value of plan assets at beginning of period	\$	681.9
Actual return (net of investment management expenses)		59.3
Administration expenses		
Employer contribution		47.2
Benefits paid		(45.7)
Fair value of plan assets at end of period	\$	<u>742.7</u>

Movements in the present value of the defined benefit obligation for the year ended March 31, 2011 were as follows:

Opening defined benefit obligation	\$	944.1
Current service cost		22.3
Interest cost		57.2
Past service costs		44.6
Actuarial losses		24.0
Benefits paid		(45.7)
Benefit obligation at end of period	\$	<u>1,046.5</u>

The amount included in the consolidated statement of financial position at March 31, 2011 arising from the entity's obligation in respect of its defined benefit plans is as follows:

Present value of funded defined benefit obligation	\$	1,046.5
Fair value of plan assets		742.7
Deficit	\$	303.8
Effect of IFRIC14 limit at beginning of year		4.3
	\$	<u>308.1</u>

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**28. SELECTED ANNUAL DISCLOSURES**

**28.2 Defined pension benefit plans (continued)**

The major categories of plan assets at March 31, 2011 for each category are as follows:

Equities	44 %
Bonds	55 %
Other (predominantly cash)	1 %

**Cash flow information**

Contributions for the year ended March 31, 2011 were based on actuarial valuations at August 1, 2007.

The actuarially estimated funding contributions expected for the year ended March 31, 2012 are \$69.4 million based on actuarial valuations at August 1, 2010.

The actuarially estimated future pension benefit payments to retirees for the next 10 years based on the August 1, 2010 valuation are as follows:

2012	\$ 59.9
2013	64.6
2014	67.1
2015	68.3
2016	69.7
2017 – 2021	374.4

**28.3 Other post-retirement benefit plans**

The principal assumptions used for the purposes of the actuarial valuations at March 31, 2011 were as follows:

Accrued benefit obligation:	
Discount rate	5.65%
Rate of compensation increase	3.00%
Initial health care rate	7.41%
Ultimate health care rate	4.50%
Year ultimate rate reached	2030
Net periodic benefit costs:	
Discount rate	5.90%
Rate of compensation increase	3.00%
Initial health care rate	7.54%
Ultimate health care rate	4.50%
Year ultimate rate reached	2030

Amounts immediately recognized in other comprehensive income, net of income tax in respect of these other post-retirement benefit plans for the year ended March 31, 2011 were as follows:

Actuarial losses on defined benefit obligation	\$ (18.0)
Less tax effect	4.5
	<u>\$ (13.5)</u>

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**28. SELECTED ANNUAL DISCLOSURES**

**28.3 Other Post-Retirement Benefit Plans** *(continued)*

Movements in the present value of the plan assets for the year ended March 31, 2011 were as follows.

Fair value of plan assets at the beginning of the period	\$	-
Employer contribution		14.3
Benefits paid		(14.3)
Benefit obligation at end of period	<u>\$</u>	<u>-</u>

Movements in the present value of the defined benefit obligation in the year ended March 31, 2011 were as follows:

Opening defined benefit obligation	\$	404.8
Current service cost		4.4
Interest cost		24.3
Past service costs		3.7
Actuarial losses		18.0
Benefits paid		(14.3)
Benefit obligation at end of period	<u>\$</u>	<u>440.9</u>

The amount included in the consolidated statement of financial position arising from the entity's obligation in respect of its other post-retirement benefit plans for the year ended March 31, 2011 was as follows.

Present value of funded defined benefit obligation	\$	440.9
Fair value of plan assets		-
	<u>\$</u>	<u>440.9</u>

**Cash flow information**

The actuarially estimated future benefit payments for the next 10 years are as follows:

2012	\$	20.5
2013		21.9
2014		22.8
2015		24.1
2016		25.3
2017 – 2021		143.9

**29. APPROVAL OF CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS**

These condensed interim consolidated financial statements were approved and authorized for issue by the Audit Committee on August 10, 2011.