Independent Expert's Report and Financial Service Guide

Poseidon Nickel Limited – New Convertible Note Issue and Amendment to Existing Convertible Notes

21 January 2011

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PART 1 – INDEPENDENT EXPERT'S REPORT

The Directors
Poseidon Nickel Limited
Unit 8, 331-335 Hay Street
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21 January 2011

Dear Sirs

New Convertible Note Issue and Amendment to Existing Convertible Notes

On 23 December 2010, Poseidon Nickel Limited ("Poseidon" or the "Company") announced that to assist with the funding of the continued development of the Windarra Nickel Project and its other exploration activities, it had secured a US$20 million convertible note facility (the "New Notes") from two private investment funds managed by US based Harbinger Capital Partners LLC ("Harbinger"). The New Notes have a six year term, are interest free for the first three years and are convertible, subject to a number of conditions, into fully paid Poseidon ordinary shares at 30 cents per share (the "New Note Shares").

The New Notes are to be issued to the Credit Distressed Blue Line Master Fund Ltd (the "Harbinger Blue Line Master Fund") and to Global Opportunities Breakaway Ltd (the "Harbinger Breakaway Fund"), with both entities taking up US$10 million each. Reference in this report to "Harbinger" incorporates reference to the Harbinger Blue Line Master Fund and the Harbinger Breakaway Fund.

In June 2008, Poseidon issued convertible notes with a face value of US$15 million to two funds managed by Harbinger as the first tranche ("Tranche 1") of a US$50 million convertible note facility (the "Existing Notes"). The second tranche (Tranche 2") of US$35 million was to be issued by Poseidon at a time agreed to by the Company and the two Harbinger funds. Because of the onset of the global financial crisis (the "GFC") and the significant deterioration of world financial markets, Tranche 2 of the Existing Notes has never been drawn down. The Existing Notes have a six year term, are interest free for the first three years and are convertible, subject to a number of conditions, into fully paid Poseidon ordinary shares at A$1.00 per share (the "Existing Note Shares"). Poseidon shareholders approved the issue of the Existing Notes and the possible future issue of the Existing Note Shares at the Company's annual general meeting held in November 2008 (the "2008 AGM").

Of the Existing Notes issued under Tranche 1, US$7.5 million are held by the Harbinger Capital Partners Master Fund I (the "Harbinger Master Fund") and US$7.5 million are held by the Harbinger Capital Partners Special Situations Fund (the "Harbinger Special Situations Fund"). Both funds were going to contribute US$17.5 million each as part of Tranche 2. Reference in this report to "Harbinger" also incorporates reference to the Harbinger Master Fund and the Harbinger Special Situations Fund.

In negotiating the New Notes, Poseidon and Harbinger have agreed to amend the terms of the Existing Notes, with the period of the Existing Notes issued under Tranche 1 being reset to six years from the date of the New Notes with an interest free period of three years and the conversion price being reset from A$1.00 to 40 cents. The US$35 million Existing Notes that were to be issued under Tranche 2 are to be cancelled. Reference in this report to the New Notes and Existing Notes in conjunction with each other will be referred to collectively as the "Convertible Notes".

At a general meeting of the Company to be held on or about 4 March 2011 (the "Meeting"), those Poseidon shareholders not associated with Harbinger (the "Non-Associated Shareholders") are to consider resolutions seeking approval for the issue of the New Notes and the New Note Shares and for the amendment of the terms of the Existing Notes, including the termination of the Tranche 2 Existing Notes, and the issue of the Existing Note Shares with respect to those Existing Notes issued under Tranche 1.

Under Section 606 of the Corporations Act (the "Act"), an entity is prohibited from acquiring a greater than 20% interest in the voting shares of a listed company. An exception to the prohibition is item 7 of Section 611 of the Act, which allows for the acquisition or relevant transaction to be approved by shareholders. Once over 20%, the entity can only increase its voting interest by no greater than 3% every six months. Again, an exception to this is for the acquisition or transaction to be approved by shareholders under item 7 of Section 611.

Because they carry no ordinary voting rights, the issue of the New Notes and the amendment to the Existing Notes has no immediate Section 606 consequences. However as at the date of this report, Harbinger holds 17,375,459 shares in Poseidon which equates to an 8.9% voting interest. It is highly likely that if all of the New Notes and all of the Existing Notes issued under Tranche 1, separately or together, are converted Harbinger's voting interest in Poseidon would increase to above the 20% allowed under Section 606. On this basis, shareholder approval is being sought pursuant to item 7 of Section 611 for the issue by Poseidon of the New Note Shares and the Existing Note Shares to Harbinger on the possible conversion of the Convertible Notes.

Unless the directors themselves provide such a report, under the Australian Securities and Investments Commission, Regulatory Guide 111: Content of expert reports ("RG 111"), resolutions proposed for item 7 of Section 611 purposes are required to be accompanied by an independent expert's report which is to provide an opinion as to whether or not the proposed transaction is fair and reasonable to the non-associated shareholders of the company.

As such, the purpose of this report is to address, as independent expert, whether or not, in our opinion, the issue of the New Note Shares and the Existing Note Shares to Harbinger on the possible conversion of the Convertible Notes is fair and reasonable to the Non-Associated Shareholders.

RG 111 also requires us to consider whether or not Harbinger, Poseidon or any other party is paying or receiving a premium for control as a result of the issue of the New Note Shares and the Existing Note Shares on the possible conversion of the Convertible Notes.

The issue of the New Notes and the amendment of the Existing Notes are subject to both being approved by the Non-Associated Shareholders. If either proposal is not approved then the issue of the New Notes and the amendment of the Existing Notes will not proceed.

Summary of Opinion

Our detailed summary and conclusion is contained in section 6 of this report. It is recommended that our opinion be read in conjunction with the whole of this report, including the appendices.

Based on the detailed discussion and analysis throughout this report, the issue of the New Note Shares and the Existing Notes to Harbinger on the possible conversion of the New Notes and Tranche 1 of the Existing Notes are, in our opinion, fair and reasonable to the Non-Associated Shareholders. In stating this, it is our view that the advantages which may accrue if the issue of the New Note Shares and Existing Note Shares are approved outweigh the disadvantages.

In relation to the possible issue of the New Note Shares and the Existing Note Shares, because the future fair value of the shares to be issued cannot be determined at this time, an assessment of whether or not Harbinger would be paying a premium for control is, at the date of this report, not possible. It is however relevant to note that the respective 30 cent and 40 cent conversion prices of the New Notes and Existing Notes were at a premium of 25% and 67% to the closing price of a Poseidon share on the Australian Securities Exchange on 20 January 2011. It is also relevant that when comparing the 5 day, 20 day, 30 day and 60 day volume weighted average prices prior to the date the New Notes facility and the amendment to the Existing Notes were announced on 23 December 2010 with the conversion prices, there was a premium ranging from 20.0% to 45.6% on the 30 cent conversion price and a premium ranging from 60.0% to 94.2% on the 40 cent conversion price. The existence of the premium is to the benefit of the Non-Associated Shareholders.

Other Matters

This independent expert's report has been prepared specifically for the Non-Associated Shareholders. Neither Ernst & Young Transaction Advisory Services, Ernst & Young nor any employee thereof undertakes responsibility to any person, other than the Non-Associated Shareholders, in respect of this report, including any errors or omissions howsoever caused.

This independent expert's report constitutes general financial product advice only and has been prepared without taking into consideration the individual circumstances of shareholders. The decision as to whether to approve or not approve the New Notes and the amendment to the Existing Notes, together with the future possible issue of the New Note Shares and the Existing Note Shares is a matter for individual Poseidon shareholders. Poseidon shareholders should have regard to the Notice of Meeting and Explanatory Memorandum prepared by the Directors and management of the Company in relation to the transactions. Poseidon shareholders who are in doubt as to the action they should take in relation to the transactions should consult their own professional adviser.

Ernst & Young Transaction Advisory Services has prepared a Financial Services Guide in accordance with the Act. The Financial Services Guide is included as Part 2 of this report.

Yours faithfully
Ernst & Young Transaction Advisory Services Limited

Brenda J Moore
Representative

Ken Pendergast
Director and Representative

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1. Introduction

1.1 Background

On 23 December 2010, Poseidon Nickel Limited ("Poseidon" or the "Company") announced that it had secured a US$20 million convertible note facility (the "New Notes") from two private investment funds managed by US based Harbinger Capital Partners LLC ("Harbinger"). The funding is to be used to help finance the continued development of the Windarra Nickel Project and the Company's other ongoing exploration activities.

With the recovery in commodity prices and stronger demand for nickel, Poseidon plans to complete the rehabilitation and redevelopment of the Windarra mine, which is located in the mid-eastern region of Western Australia. Management's short term objective is to re-establish Windarra as a world class nickel sulphide operation. The sourcing of the US$20 million under the New Notes is a major step towards achieving this.

The New Notes are to be issued to the Credit Distressed Blue Line Master Fund Ltd (the "Harbinger Blue Line Master Fund") and Global Opportunities Breakaway Ltd (the "Harbinger Breakaway Fund"), with each entity taking up a US$10 million obligation. Reference in this report to "Harbinger" incorporates reference to the Harbinger Blue Line Master Fund and the Harbinger Breakaway Fund.

Two other funds managed by Harbinger, the Harbinger Capital Partners Master Fund I (the "Harbinger Master Fund") and the Harbinger Capital Partners Special Situations Fund (the "Harbinger Special Situations Fund"), already hold US$15 million of convertible notes that were issued by Poseidon as the first tranche ("Tranche 1") of a US$50 million convertible note facility in June 2008 (the "Existing Notes"). Each entity holds US$7.5 million Existing Notes under Tranche 1. Reference in this report to "Harbinger" also incorporates reference to the Harbinger Master Fund and the Harbinger Special Situations Fund.

The US$35 million second tranche ("Tranche 2") of the Existing Notes has not been drawn down.

In negotiating the New Notes, Poseidon and Harbinger have agreed to amend the terms of the Existing Notes issued under Tranche 1 and to cancel the US$35 million Existing Notes that were to be issued under Tranche 2. Reference in this report to the New Notes and Existing Notes in conjunction with each other will be referred to collectively as the "Convertible Notes".

At the date of this report, Harbinger has an 8.9% interest in Poseidon.

Unless otherwise stated, all amounts referred to in this report are stated in Australian dollars ("A$").

1.2 The New Notes

The terms and conditions of the New Notes are detailed in the convertible note certificates issued by Poseidon to the Harbinger Blue Line Master Fund and the Harbinger Breakaway Fund, dated 22 December 2010 (the "Note Certificates"). The major terms are summarised as follows:

- the New Notes have a principal amount of US$10 million each;
- the New Notes are unsecured;
- the New Notes have a maturity date of six years from their issue date;
- interest is payable at a rate of 0% per annum for the initial three year period following the date of issue and 5% per annum on the principal amount thereafter, payable quarterly in arrears until maturity or the date of conversion;
- interest payable may be satisfied, at the discretion of Poseidon, and subject to the provisions of the Act, by the issue of shares. The number of shares to be issued will be determined at the lesser of the conversion price or the average volume weighted average price ("VWAP") for the Company's shares on the Australian Securities Exchange ("ASX") for the five trading days prior to the relevant interest payment date;
- the conversion price of the New Notes is 30 cents (in $A's) per share (the "Conversion Price"), subject to any adjustment caused by the issue of other securities at prices below the Conversion Price or any dividend payments made within in the 180 days of 22 December 2010 (the "Dilution Factor");
- the New Notes are convertible at any time after the closing price of a Poseidon share on the ASX has exceeded the Conversion Price for five consecutive trading days;
- conversion is at the discretion of the holder;
- conversions are to be based on a US$ to A$ exchange rate (or vice versa) calculated by reference to the Australian and New Zealand Banking Group Limited's ("ANZ") average spot buying rate for the five business days prior to the relevant conversion date;
- the New Notes are transferable; and
- if at the date of maturity the New Notes have not been converted, then Poseidon is required to repay the US$20 million plus any interest outstanding.

With respect to the Conversion Price of 30 cents, Poseidon has on issue 16,742,436 options with an exercise price of 25 cents. If any of these options are exercised within 180 days of 22 December 2010, the shares issued on exercise will not be included in the calculation of the Dilution Factor. All of the other options that the Company has on issue have exercise prices greater than the Conversion Price.

The underlying terms and conditions of the New Notes are essentially the same as those of the Existing Notes save for the different conversion prices.

1.3 The Amendments to the Existing Notes

The US$50 million Existing Notes facility was agreed to between Poseidon and Harbinger on 25 June 2008. The US$15 million Tranche 1 amount was received by the Company in June 2008 and the Existing Notes relevant to that amount were issued.

The US$35 million Tranche 2 amount was to be paid and the corresponding Existing Notes issued at a subsequent time that was to be agreed between Poseidon and Harbinger. Because of the receipt of the US$15 million under Tranche 1 there was no immediate need for the Company to drawdown this amount.

The Existing Notes have a six year term, are interest free for the first three years and are convertible, subject to a number of conditions, into fully paid Poseidon shares at $1.00 per share (the "Existing Note Shares"). Poseidon shareholders approved the issue of the Existing Notes and the possible future issue of the Existing Note Shares at the Company's annual general meeting held in November 2008 (the "2008 AGM").

Based on their terms, the Existing Notes issued under Tranche 1 mature on 24 June 2014. If not converted at that date, the US$15 million is repayable by Poseidon together with any outstanding interest due. The interest free period on the Existing Notes expires on 24 June 2011. Thereafter the Company is required to pay interest at a rate of 5% per annum.

With the onset of the global financial crisis (the "GFC") and the deterioration of world financial markets, by early 2009, the Company's share price had fallen from around 75 cents at the time the Existing Notes facility was announced in June 2008 to levels of around 25 cents. The worsening US economy and the fall in equity markets had a negative impact on the value and liquidity of Harbinger and its underlying funds. While Tranche 2 remained 'technically' available, with the change in circumstances for both Poseidon and Harbinger it became increasingly difficult for the funds to be provided under the original terms of the Existing Notes. Accordingly, the US$35 million Tranche 2 of the Existing Notes has not been drawn down.

As part of negotiating the New Notes, Poseidon and Harbinger have agreed, subject to a number of conditions, to amend some of the terms of the Existing Notes issued under Tranche 1 and to cancel Tranche 2. The amendments and cancellation are detailed in the Convertible Note Amendment Deeds and the Convertible Note Termination Deeds entered into with the Harbinger Master Fund and the Harbinger Special Situations Fund on 22 December 2010.

The key amendments to be made to the Existing Notes issued under Tranche 1 are summarised as follows:

- the conversion price is to be reduced from $1.00 to 40 cents;
- the maturity date of the Existing Notes issued under Tranche 1 will be reset to a date which is six years from the date of the New Notes;
- the interest free period will be reset to a date which is three years from the date of the New Notes (the interest rate thereafter will remain at 5%);
- the new conversion price of 40 cents (in $A's) per share will be subject to any adjustment caused by the issue of other securities at prices below that price or any dividend payments made within in the 180 days of 22 December 2010; and
- the Tranche 1 Existing Notes will be transferable.

The effect of the cancellation of Tranche 2 of the Existing Notes will be to terminate all rights and obligations of both Poseidon and Harbinger with respect to Tranche 2.

The resetting of the period of the Existing Notes, including the interest free period, aligns those terms with the period of the New Notes.

1.4 Conditions precedent

The issue of the New Notes and the amendment of the Existing Notes issued under Tranche 1 are subject to a number of conditions precedent being:

- the execution of the Convertible Note Amendment Deeds and the Convertible Note Termination Deeds entered into by Poseidon separately with the Harbinger Master Fund and the Harbinger Special Situations Fund;
- the execution of the New Note agreements between Poseidon and, separately, the Harbinger Blue Line Master Fund and the Harbinger Breakaway Fund; and
- shareholders approving the issue and the possible conversion of the New Notes and the amendment and conversion of the Existing Notes and any of the underlying transactions contemplated by the New Notes and the amended Existing Notes.

Accordingly, the issue of the New Notes and the amendments to the Existing Notes, including the cancellation of Tranche 2 of the Existing Notes, will not proceed unless both transactions are approved by shareholders. If the issue of the New Notes or the amendments to the Existing Notes are not approved, neither of the transactions contemplated will proceed.

The conditions under the first two bullet points have been met.

2. Scope of the Report

2.1 Purpose of the Report

Under Section 606 of the Corporations Act ("the Act") an entity is prohibited from acquiring a greater than 20% interest in the voting shares of a listed company. An exception to the prohibition is item 7 of Section 611 of the Act, which allows for the acquisition or relevant transaction to be approved by shareholders. Once over 20%, the entity can only increase its voting interest by no greater than 3% every six months. Again, an exception to this is for the acquisition or transaction to be approved by shareholders under item 7 of Section 611.

Because they carry no ordinary voting rights, the issue of the New Notes and the amendment to the Existing Notes has no immediate Section 606 consequences. However at the date of this report, Harbinger held 17,375,459 shares in Poseidon which equates to an 8.9% voting interest. It is highly likely that if all of the Existing Notes issued under Tranche 1 and all of the New Notes, separately or together, are converted Harbinger's voting interest in Poseidon would increase to above the 20% allowed under Section 606. On this basis, shareholder approval is being sought pursuant to item 7 of Section 611 for the issue by Poseidon of the New Note Shares and the Existing Note Shares to Harbinger on the possible conversion of the Convertible Notes.

While shareholder approval for the issue of the Existing Note Shares to Harbinger for item 7 of Section 611 purposes was obtained at the Company's 2008 AGM, given the impact of the proposed amendments to the Existing Notes on the number of Existing Note Shares that would be issued if the Existing Notes were converted, the Directors consider it prudent to have shareholders approve the amended terms.

Unless the directors themselves provide such a report, under the Australian Securities and Investments Commission, Regulatory Guide 111: Content of expert reports ("RG 111"), resolutions proposed for item 7 of Section 611 purposes are required to be accompanied by an independent expert's report which is to provide an opinion as to whether or not the proposed transaction is fair and reasonable to the non-associated shareholders of the company.

As such, the purpose of this report is to address, as independent expert, whether or not, in our opinion, the issue of the New Note Shares and the Existing Note Shares to Harbinger on the possible conversion of the Convertible Notes is fair and reasonable to the non-associated shareholders of Poseidon. The "non-associated shareholders" of Poseidon are those not associated with Harbinger (the "Non-Associated Shareholders").

RG 111 also requires us to consider whether or not Harbinger, Poseidon or any other party is paying or receiving a premium for control as a result of the issue of the New Note Shares and the Existing Note Shares on the possible conversion of the Convertible Notes.

At a general meeting of the Company to be held on or about 4 March 2011 (the "Meeting"), those Poseidon shareholders not associated with Harbinger (the "Non-Associated Shareholders") are to consider resolutions seeking approval for the issue of the New Notes and the New Note Shares and for the amendment of the terms of the Existing Notes, including the issue of the Existing Note Shares.

This report is to be included in the Notice of Meeting and Explanatory Memorandum being sent to Poseidon shareholders in regards to the Meeting.

2.2 Basis of assessment

The Act does not specifically define the term "fair and reasonable". In assessing whether the issue of the New Note Shares and the Existing Note Shares to Harbinger on the possible conversion of the Convertible Notes is fair and reasonable to the Non-Associated Shareholders we have had regard to the contents of RG 111.

RG 111 provides guidance in relation to the preparation of independent expert reports for the purposes of the Act and to the term "fair and reasonable". RG 111 states that in deciding on the appropriate form of analysis, the expert needs to keep in mind that the main purpose of the report is to adequately deal with the reasonably anticipated concerns of those persons affected by the proposed transaction (i.e. the shareholders not involved in the transaction). The form of analysis an expert uses to evaluate a transaction should address the issues faced by shareholders.

In the circumstances of a takeover bid or a "control transaction", RG 111 suggests that "*an offer is 'fair' if the value of the offer price or consideration is equal to or greater than the value of the securities the subject of the offer*". A "control transaction" is a transaction where an entity acquires or increases a controlling interest in a company. In regards to "control", Section 608 (4) of the Act states that an entity has control of a company if that entity has the capacity to determine the outcome of decisions about the company's financial and operating policies.

A concern expressed within RG 111 is where an entity is looking to use a transaction that is being approved by shareholders under item 7 of Section 611 to avoid making a takeover bid for the company. As detailed in section 4, if the New Notes and the Existing Notes are converted it is estimated that Harbinger's interest in Poseidon would increase to 28.3%. Under this scenario, it is assumed that because of the 40 cent exercise price, the options held by The Australian Children's Trust (the "ACT") will be exercised, with the ACT obtaining 26.8%. Given the near equivalent shareholders between Harbinger and the ACT it is unlikely that Harbinger would be able to control the Company.

If Poseidon's share price trades above 30 cents but below 40 cents there is the possibility that the Existing Notes issued under the US$15 million Tranche 1 will be converted while the New Notes remain unconverted. If this was to occur, the analysis in section 4 indicates that Harbinger's interest in Poseidon would increase to 30.7%, with no other shareholder having greater than 5% interest. While Harbinger has been major supporter of the current Board and management of Poseidon in the almost four years it has been a substantial shareholder of the Company it has never sought Board representation. Without the ability to control the Board, it is unlikely that Harbinger would have the capacity to control the financial and operating activities of Poseidon. In stating that, with a 30.7% interest Harbinger would be in a position to exert significant influence on the Company as the dominant shareholder.

A key consideration of the shareholders of a company entering into a substantial transaction is generally whether or not they will be better or worse off as a result of the transaction. Part of the rationale of the prohibition contained in Section 606 of the Act is to ensure, as far as practicable, that the non-associated shareholders are no worse off because of a substantial transaction.

Accordingly, in assessing whether or not the issue of the New Note Shares and the Existing Note Shares to Harbinger on the possible conversion of the Convertible Notes is fair and reasonable to the Non-Associated Shareholders we have considered the likely advantages and disadvantages, if any, which may accrue if the issue of the New Note Shares and Existing Note Shares are approved. Part of this analysis will be consideration of the issue of the New Notes and the receipt by Poseidon of the US$20 million and the amended terms of the Existing Notes. Under this assessment, the issue of the New Note Shares and the Existing Note Shares would be considered "fair and reasonable" if the Non-Associated Shareholders are considered to be better off, or at least no worse off, as a result of their issue. The Non-Associated Shareholders would be better off if the expected advantages outweigh the possible disadvantages.

The matters considered in our analysis include the following:

- the nature of the Convertible Notes and their conversion terms;
- comparison of the previous terms of the Existing Notes with the new terms, and consequences of their conversion;
- the trading price on the ASX of Poseidon's shares prior to the announcement of the New Notes facility and the amendment to the Existing Notes;
- comparison of the trading price of a Poseidon share with the conversion price of the New Notes and the Existing Notes;
- the trading price of Poseidon's shares since the announcement of the New Notes facility and the amendment to the Existing Notes;
- the overall terms of the New Notes and the amended Existing Notes;
- the level of control likely to be gained by Harbinger from the issue of the New Note Shares and the Existing Note Shares;
- consideration of Harbinger's track record in investing in other ASX listed resource companies;
- Poseidon's need for funding and alternative sources; and
- other significant matters.

Issues of valuation are considered in section 5.1 and the relevant commercial and qualitative factors are considered in section 5.2. Whether Harbinger, Poseidon or any other party is paying or receiving a premium for control is considered in section 5.3. Our summary and conclusion is detailed in section 6.

Our assessment is based on the economic, political, social, market and other conditions prevailing at the date of this report. These conditions can change significantly over relatively short periods of time.

2.3 Shareholders' decisions

This independent expert's report has been prepared specifically for the Non-Associated Shareholders at the request of the Directors with respect to the issue of New Notes and the amendment to the Existing Notes, with particular emphasis on consideration of the issue of the New Note Shares and the Existing Note Shares on the possible conversion of the Convertible Notes at some future date. As such, Ernst & Young Transaction Advisory Services, Ernst & Young and any member or employee thereof, take no responsibility to any entity other than Poseidon shareholders, in respect of this report, including any errors or omissions howsoever caused.

This report constitutes general financial product advice only and has been prepared without taking into consideration the individual circumstances of the Non-Associated Shareholders. The decision to approve or not approve the issue of New Note Shares and the Existing Note Shares is a matter for individual shareholders. Poseidon shareholders should consider the advice in the context of their own circumstances, preferences and risk profiles. Poseidon shareholders should have regard to the Notice of Meeting and Explanatory Memorandum prepared by the Directors and management of the Company. Poseidon shareholders who are in doubt as to the action they should take in relation to the Convertible Notes, including the New Note Shares and the Existing Note Shares, should consult their own professional adviser.

Ernst & Young Transaction Advisory Services has prepared a Financial Services Guide in accordance with the Act. The Financial Services Guide is included as Part 2 of this report.

2.4 Limitations and reliance on information

In the preparation of this independent expert's report, Ernst & Young Transaction Advisory Services was provided with information in respect of Poseidon and obtained additional information from public sources, as set out in Appendix B.

We have had discussions with the Directors and management of Poseidon in relation to the issue of the New Notes, the amendment of the Existing Notes and the operations, financial position, operating results and outlook of Poseidon.

This independent expert's report is also based upon financial and other information provided by Poseidon. Ernst & Young Transaction Advisory Services has considered and relied upon this information.

The information provided to Ernst & Young Transaction Advisory Services has been evaluated through analysis, enquiry and review for the purposes of forming an opinion as to whether the issue of the New Note Shares and the Existing Note Shares to Harbinger on the possible conversion of the Convertible Notes is fair and reasonable to the Non-Associated Shareholders of Poseidon. However, Ernst & Young Transaction Advisory Services does not warrant that its enquiries have identified all of the matters that an audit, an extensive examination or 'due diligence' and/or tax investigation might disclose.

Preparation of this report does not imply that we have, in any way, audited the accounts or records of Poseidon. It is understood that the accounting information that was provided was prepared in accordance with generally accepted accounting principles including the Australian equivalents to International Financial Reporting Standards and International Financial Reporting Standards, as applicable.

In forming our opinion we have also assumed that:

- matters such as title, compliance with laws and regulations and contracts in place are in good standing and will remain so, and that there are no material legal proceedings, other than as publicly disclosed;
- the information set out in the Notice of Meeting and Explanatory Memorandum to be sent to Poseidon shareholders is complete, accurate and fairly presented in all material respects; and
- the publicly available information relied upon by Ernst & Young Transaction Advisory Services in its analysis was accurate and not misleading.

To the extent that there are legal issues relating to assets, properties, or business interests or issues relating to compliance with applicable laws, regulations and policies, we assume no responsibility and offer no legal opinion or interpretation on any issue.

The statements and opinions given in this independent expert's report are given in good faith and in the belief that such statements and opinions are not false or misleading.

Ernst & Young Transaction Advisory Services provided draft copies of this report to the Directors and management of Poseidon for their comments as to factual accuracy, as opposed to opinions, which are the responsibility of Ernst & Young Transaction Advisory Services alone. Amendments made to this report as a result of this review have not changed the methodology or conclusions reached by Ernst & Young Transaction Advisory Services.

This report should be read in the context of the full qualifications, limitations and consents set out in Appendix A of this independent expert's report.

This report has been prepared in accordance with APES 225: *Valuation Services* issued by the Accounting Professional & Ethical Standards Board Limited in July 2008.

3. Overview of Poseidon

3.1 Background

In December 2005, Poseidon, under its former name of "Niagara Mining Limited", acquired the Windarra Nickel Project from BHP Billiton Pty Ltd for a consideration of $7 million plus a deferred amount of $1 million and a 1% revenue royalty. The Windarra Nickel Project is located near Laverton in the mid-eastern region of Western Australia, approximately 250 kilometres north east of Kalgoorlie.

Windarra has historical significance to the Australian resource sector in that its discovery in the late 1960's underpinned the nickel boom of the early 1970's. Between 1974 and 1994 mining operations at Windarra produced over 8 million tonnes of ore, recovering approximately 815,000 tonnes of nickel concentrate which contained 84,000 tonnes of nickel metal. The mine was closed in 1994 in response to lower nickel prices.

In July 2007, the Company was renamed "Poseidon Nickel Limited" to reflect the clear focus of re-establishing a viable nickel mining operation at Windarra.

At the time of securing the US$50 million Existing Notes facility with Harbinger in June 2008, Poseidon was intending to complete a feasibility study into the construction of a concentrator at Windarra, with the view of becoming a 20,000 tonne per annum nickel metal producer. Dewatering and rehabilitation of the Windarra decline and mine had commenced in March 2008, with further in-mine drilling being planned as access to previously worked areas was obtained.

In the three months prior to the announcement of Poseidon securing the Existing Notes facility with Harbinger, the Company's shares traded on the ASX in the range of 51 cents to 95 cents, closing on 25 June 2008, the day prior to the announcement of the facility, at a price of 74 cents. On 29 June 2008 the Company's share price had increased to a high of $1.51. With the onset of the GFC and the deterioration of world financial markets over the period from July 2008 to 31 December 2008, the Company's share price declined from the $1.51 at the end of June 2008 to a low in October 2008 of 16 cents to close at 31 December 2008 at 34 cents. In December 2008, Poseidon shares traded in the range of 18 cents to 37 cents.

Through the GFC commodity prices decreased significantly as demand weakened and the level of economic uncertainty increased. After reaching an historical high of around US$55,000 per tonne ("/t") in May 2007, by June 2008 nickel had traded down to around US$20,000/t and then down to US$10,000/t by October 2008. The price reached a low of just under US$9,000/t in December 2008.

In October 2008 Poseidon announced that given the economic uncertainty brought about by the GFC, in order to conserve cash it was suspending the rehabilitation of the Windarra mine. Exploration drilling at Denny Bore, located 12 kilometres south of Windarra, continued and in January 2009 the Company announced the discovery of the Cerberus nickel sulphide deposit with an Inferred Resource of approximately 25,000 tonnes of contained nickel at an average grade of 2.45%. Reflecting the suspension of rehabilitation work at Windarra, evaluation and exploration expenditure for the six months to 30 June 2009 totalled approximately $1.0 million compared to the $7.9 million incurred for the previous six months to 31 December 2008.

Since early 2009, Poseidon's exploration activities have concentrated on gaining a better understanding of the characteristics of the Cerberus deposit, extending resources at South Windarra and identifying through geochemical analysis and re-interpretation of historical data new exploration targets at Windarra. Indicated and Inferred Resources at Windarra and Cerberus have increased to approximately 97,000 tonnes of contained nickel, with an average grade of 1.71%, making Windarra one of the largest undeveloped nickel sulphide deposits in Australia.

Dewatering of the Windarra decline recommenced in April 2010 with the water level being lowered and maintained to approximately 165 metres below surface. Equipment has been installed in the decline and delivered to site so that the rehabilitation and refurbishment of the decline and mine will be able to be recommenced with a short lead time. Poseidon management has estimated around 20% of the necessary refurbishment work at Windarra has been completed, with the remaining work to be undertaken once sufficient funding is secured. Evaluation and exploration expenditure for the year ended 30 June 2010 totalled approximately $2.9 million.

Subject to sourcing the necessary funding, Poseidon hopes to bring Windarra back into production within a two year time frame. The cost of reopening Windarra, including mine refurbishment, underground drilling, feasibility study and construction of a concentrator is estimated by management to be US$55 million. Initial mining rate is forecast at 350,000 tonnes per annum, producing 4,500 tonnes of nickel in concentrate. In the medium term it is proposed to increase production to 10,000 tonnes of nickel in concentrate per annum.

Over 2009, and into 2010 the nickel price steadily recovered to reach a two year high in April 2010 of just over US$27,000/t. Since then the price drifted back to around US$18,000/t by July 2010 and then increased to levels of just under US$25,000/t in December 2010. The higher prices reflect a more positive outlook as world economies recover from the GFC.

Over the period since October 2008, Poseidon management has been active in investigating the possible acquisition of a number of other nickel projects based in Western Australia. While discussions on some of these opportunities were advanced, ultimately none progressed.

In March 2009, the Company sold the gold rights on its West Australian tenements to Triton Gold Limited ("Triton") for a consideration satisfied by the issue of 9,000,000 shares in Triton plus a cash amount of $300,000. Triton listed on the ASX in August 2009. With a 9.6% interest, Poseidon is Triton's largest shareholder. The shares held by the Company in Triton are escrowed for two years.

In May 2010 Poseidon reached agreement to sell its shares and interests in the Salman South and Mame gold prospects located in South Ghana to Hodges Resources Limited for $750,000 plus 1,250,000 shares in the company. The sales remains contingent on the Company obtaining approval to transfer the prospecting licence in Ghana. The $750,000 cash amount is being held in escrow subject to the completion of the sale.

At 31 December 2010, Poseidon had cash on hand of approximately $736,000.

3.2 Capital structure

As at the date of this report, Poseidon had on issue 194,876,072 fully paid ordinary shares, 425,000 partly paid shares, 313,131 special bonus employee shares and 143,932,839 options. The Company also had 15,906,681 Existing Notes on issue, representing the Tranche 1 amount of US$15 million received from Harbinger in June 2008 converted at the then A$:US$ exchange rate of 94.3 cents. Based on the conversion price of $1.00, if converted this equates to 15,906,681 ordinary shares.

The partly paid shares were issued at a price of 10.2 cents per share, of which 375,000 have been paid up to 8.2 cents each and the remaining 50,000 paid up to 0.2 cents each.

Details of the options Poseidon has on issue are as follows:

Options on Issue	Expiry Date	Exercise Price	Number
Exercisable anytime up to	2 July 2011	$1.96	1,000,000
Exercisable anytime up to	5 December 2011	$0.92	6,157,403
Exercisable anytime up to	31 July 2012	$0.40	2,500,000
Exercisable anytime up to	31 August 2012	$0.25	9,267,436
Exercisable anytime up to	19 September 2012	$0.40	115,000,000
Exercisable anytime up to	22 October 2012	$1.41	533,000
Exercisable anytime up to	19 December 2012	$0.80	2,000,000
Exercisable subject to conditions up to	31 August 2016	$0.25	2,975,000
Exercisable subject to conditions up to	23 November 2016	$0.25	4,500,000
			143,932,839

Source: Poseidon's records

While exercisable at 25 cents each, the August and November 2016 options are subject to, amongst other conditions, Poseidon's share price trading above 50 cents on the ASX for five consecutive days.

At 20 December 2010, the Company had approximately 7,300 shareholders with the top 20 shareholders holding approximately 34% of the shares on issue. The Company's largest shareholder is Harbinger, holding an 8.9% interest. Other major shareholders include Contango Asset Management Limited (5.7%), Technical Investing Pty Ltd (4.2%) and Mr Andrew Forrest (2.6%), Poseidon's Chairman.

In the period 21 July 2010 to 3 November 2010 Harbinger reduced its shareholding in Poseidon through the on-market disposal of 10,172,686 shares. Before the sell down of these shares Harbinger had a 15.8% interest in the Company, which prior to the capital raising undertaken by Poseidon in March 2010, equated to a 17.3% interest. Harbinger had previously increased its interest to 17.6% in July 2008.

The holder of the 115,000,000 September 2012 40 cent options is Leaping Joey Pty Ltd as trustee for The Australian Children's Trust (the "ACT"), which is a charitable trust that was set up in 2001 by Mr Forrest and his wife. The primary objective of the ACT is to assist underprivileged children throughout Australia. While chaired by Mr Forrest, the ACT has an independent Board of Directors and an independent Executive Committee. The options were vested to the ACT by Mr Forrest. Shareholder approval under item 7 of Section 611 for the issue of shares to Mr Forrest or his nominee (i.e. the ACT) on the exercise of the options was obtained at a general meeting held by the Company in July 2007.

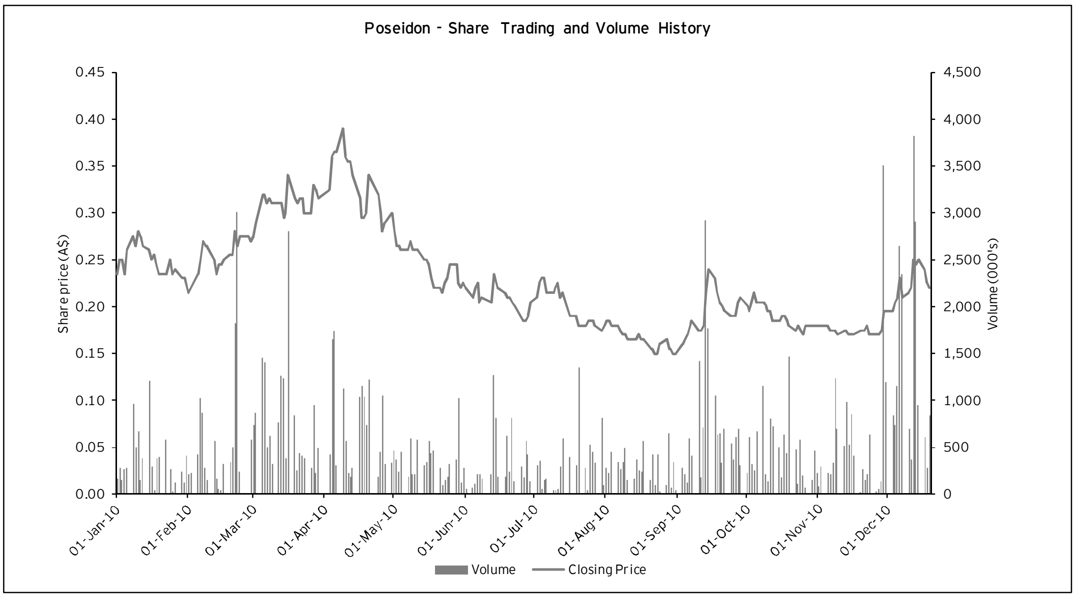
3.3 Share price performance

The table below summarises the trading history of Poseidon shares on the ASX over the period 4 January 2010 to 22 December 2010, the last trading day prior to the ASX announcement of the New Notes facility with Harbinger.

Poseidon - Share Trading History	High $	Low $	Close $	Monthly VWAP	Volume 000's	Liquidity % of Shares on Issue
January 2010	0.29	0.23	0.24	0.259	7,110	4.4%
February 2010	0.32	0.21	0.28	0.266	11,070	6.8%
March 2010	0.35	0.26	0.33	0.312	16,705	9.8%
April 2010	0.39	0.28	0.29	0.330	14,230	8.3%
May 2010	0.30	0.20	0.25	0.252	7,184	4.1%
June 2010	0.24	0.18	0.19	0.216	7,785	4.4%
July 2010	0.25	0.18	0.18	0.198	6,291	3.6%
August 2010	0.19	0.15	0.16	0.169	6,922	3.7%
September 2010	0.26	0.15	0.21	0.204	14,668	7.8%
October 2010	0.22	0.17	0.18	0.193	10,090	5.2%
November 2010	0.19	0.17	0.17	0.176	8,592	4.4%
to 22 December 2010	0.27	0.17	0.22	0.222	23,025	11.8%

Source: Bloomberg, E&Y analysis

The following chart is a summary of Poseidon's share trading history on the ASX for the same period. The trading price is based on the daily closing price.



Source: Bloomberg, E&Y analysis

The analysis shows that over the period considered, Poseidon's shares traded up from levels of around 25 cents at the beginning of 2010 to a high of 39 cents in mid-April 2010, then gradually down to a low of 14.5 cents in early September 2010. From there the shares traded up to levels of above 20 cents prior to the announcement of the New Notes facility on 23 December 2010. The closing price of the Company's shares on 22 December 2010 was 22 cents. The VWAP across the period 4 January 2010 to 22 December 2010 was 24.1 cents.

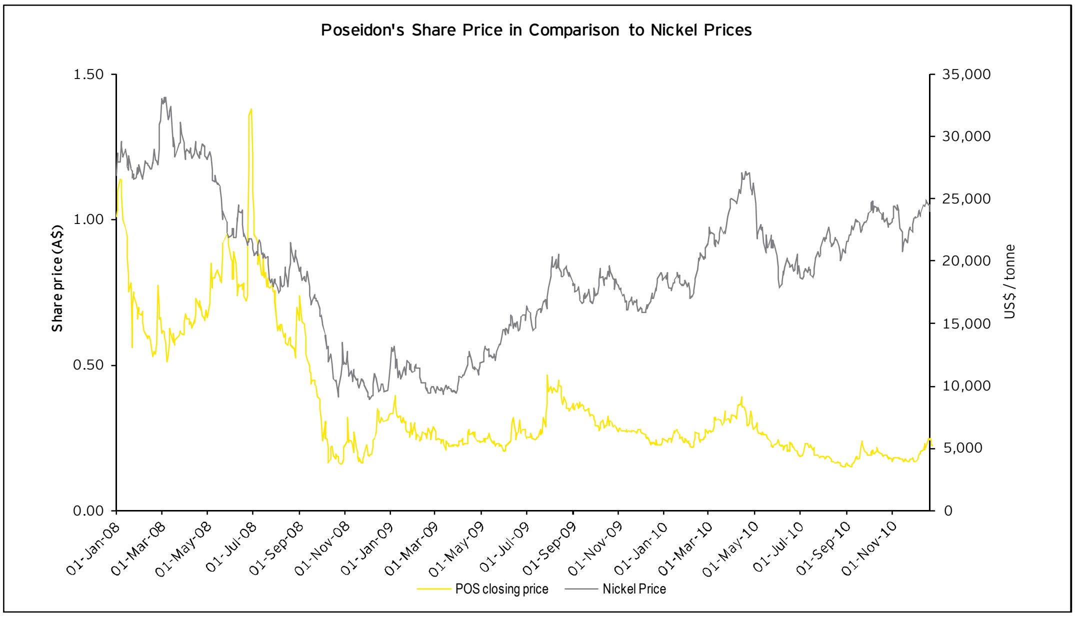
With respect to announcements made by the Company over the period considered to 22 December 2010 that may have had an impact on underlying trading prices, in addition to the required quarterly, half yearly and annual lodgements, we note the following:

- in January 2010, the Company announced the next stage of its exploration program at Windarra, highlighting its intention to conduct additional work to gain a better understanding of the Cerberus deposit;
- in March 2010, Poseidon advised that it was to raise $2 million through the issue of 8,000,000 shares at a price of 25 cents per share to assist with financing the ongoing evaluation of its mineral projects and to provide working capital;
- in April 2010, the Company announced the recommencement of the dewatering of the decline at Windarra with the plan of recommencing the rehabilitation and refurbishment of the decline and mine once the funds became available;
- in June 2010, Poseidon announced that it had identified several new prospective targets at Windarra;
- in July 2010, the Company announced that it would commence evaluation of the new targets in order to determine drilling priorities;
- in July 2010, the Company announced a capital raising of approximately $3.2 million through the issue of approximately 17.9 million shares at 18 cents per share to assist with its proposed work program;
- in August 2010, Poseidon announced the results of the first stage of its drilling program at Windarra, and that the surface electromagnetic work completed revealed important sub-surface anomalies;
- in September 2010, the Company announced that two nickel sulphide intersections at Cerberus had exceeded expectations, with the visible sulphide intersections being thicker than previously estimated; and
- in October 2010, the Company announced that further assay results for the first two nickel sulphide drill holes at Cerberus exceeded expectations in both grade and width. The work completed had confirmed the real potential for increasing the Cerberus resource nearer to surface than the geological modelling estimated.

The monthly volume of Poseidon's shares traded over the period 4 January 2010 to 22 December 2010 fluctuated between 3.6% of the shares on issue in July 2010 to 11.8% for the month to date to 22 December 2010. Not surprisingly, the volume of shares traded increased when there was an upward movement in Poseidon's share price, as shareholders took advantage of higher prices.

Given the nature of the Company's activities, while at an early stage of development it would be expected that there would be some correlation between Poseidon's share price and the price of nickel. In this regard, after recovering from levels of around US$9,000/t in December 2008, over 2009 and into 2010 the nickel price steadily increased to a two year high in April 2010 of over US$27,000/t, to drift back down to around US$18,000/t by July 2010, subsequently increasing to levels of just under US$25,000/t in December 2010.

The following chart details Poseidon's share price and the nickel price over the period from 2 January 2008 through to 22 December 2010.



Source: Bloomberg, E&Y analysis

While there has been a general correlation between Poseidon's share price and the nickel price, since June/July 2010 this correlation appears to have been less evident, in that while the nickel price has improved the Company's share price has remained flat. The capital raising completed by Poseidon through the issue of approximately 17.9 million shares in two tranches in August and October 2010 at 18 cents may have impacted the Company's share price as investors looked to sell shares whenever the price was at a reasonable premium to that price. In addition, over this period Harbinger was selling down its interest from 15.8% to 8.9%.

Consideration of broker forecasts indicates that the nickel price is expected to be maintained at levels of around US$25,000/t through to 2013, increasing to around US$30,000/t in 2014. The longer term estimate is for a nickel price of around US$16,000/t, which is higher than the historical average price.

4. Impact on the Non-Associated Shareholders

With respect to the US$15 million Tranche 1 of the Existing Notes, if the conversion price is reduced from $1.00 to 40 cents, assuming a A$:US$ exchange rate at parity, the number of Poseidon shares issued to Harbinger on conversion would increase from 15,000,000 to 37,500,000.

The table below summarises the position of the Non-Associated Shareholders if the Tranche 1 Existing Notes are converted, all of the options with an exercise price of 40 cents or less are exercised (excluding the August and November 2016 options which, while having a 25 cent exercise price, have a 50 cents trading price hurdle), the special bonus employee shares vest and the partly paid shares become fully paid.

Conversion of Tranche 1 of Existing Notes at 40 cents	Total Shares	Non-Associated Shareholders	Harbinger	The ACT
Current	194,876,072	177,500,613	17,375,459	-
Interest	*100.0%*	*91.1%*	*8.9%*	*0.0%*
Exercise of Options	126,767,436	11,767,436		115,000,000
Special bonus employee shares vest	313,131	313,131		
Partly paids become fully paid	425,000	425,000		
Conversion of Existing Notes	37,500,000		37,500,000	
	359,881,639	190,006,180	54,875,459	115,000,000
Interest	*100.0%*	*52.8%*	*15.2%*	*32.0%*

Source: E&Y analysis

This shows that the ACT would become Poseidon's largest shareholder with a 32.0% interest. The Non-Associated Shareholders interest would decrease from 91.1% to 52.8% and Harbinger's shareholding would increase from 8.9% to 15.2%.

Based on the Conversion Price of 30 cents, the number of shares that would need to be issued to Harbinger with respect to the $US20 million New Notes, assuming a A$:US$ exchange rate at parity, would be 66,666,667.

With respect to the proposed transactions, Poseidon has agreed, subject to shareholder approval, to issue 2,608,863 shares in lieu of a cash fee to the individual who assisted the Company with brokering the issue of the Convertible Notes with Harbinger (the "Broker Shares").

If the Existing Notes are converted at 40 cents it is highly likely that the New Notes would also be converted. The table below summarises the position of the existing Non-Associated Shareholders if the Tranche 1 Existing Notes and the New Notes are converted, the Broker Shares are issued, all of the options with an exercise price of 40 cents or less are exercised (excluding the August and November 2016 options), the special bonus employee shares vest and the partly paid shares become fully paid.

Conversion of Tranche 1 of Existing Notes and New Notes	Total Shares	Non-Associated Shareholders	Harbinger	The ACT	Broker Shares
Current	194,876,072	177,500,613	17,375,459	-	-
Interest	*100.0%*	*91.1%*	*8.9%*	*0.0%*	*0.0%*
Exercise of Options	126,767,436	11,767,436		115,000,000	
Special bonus employee shares vest	313,131	313,131			
Partly paids become fully paid	425,000	425,000			
Broker Shares issued	2,608,863				2,608,863
Conversion of Existing Notes	37,500,000		37,500,000		
Conversion of New Notes	66,666,667		66,666,667		
	429,157,169	190,006,180	121,542,126	115,000,000	2,608,863
Interest	*100.0%*	*44.3%*	*28.3%*	*26.8%*	*0.6%*

Source: E&Y analysis

This shows that Harbinger's interest in the Company would increase to 28.3% with the ACT's interest being 26.8%. The Non-Associated Shareholders interest would be 44.3%.

With the Conversion Price of the New Notes being lower than the conversion price of the Tranche 1 Existing Notes, the New Notes may be converted before the Existing Notes. The table below summarises the position of the Non-Associated Shareholders if only the New Notes are converted, the Broker Shares are issued, all of the options with an exercise price of 30 cents or less are exercised (excluding the August and November 2016 options), the special bonus employee shares vest and the partly paids become fully paid.

Conversion of New Notes at 30 cents	Total Shares	Non-Associated Shareholders	Harbinger	The ACT	Broker Shares
Current	194,876,072	177,500,613	17,375,459	-	-
Interest	*100.0%*	*91.1%*	*8.9%*	*0.0%*	*0.0%*
Exercise of Options	9,267,436	9,267,436		-	
Special bonus employee shares vest	313,131	313,131			
Partly paids become fully paid	425,000	425,000			
Broker Shares issued	2,608,863				2,608,863
Conversion of New Notes	66,666,667		66,666,667		
	274,157,169	187,506,180	84,042,126	-	2,608,863
Interest	*100.0%*	*68.4%*	*30.7%*	*0.0%*	*1.0%*

Source: E&Y analysis

This analysis shows that Harbinger would become Poseidon's major shareholder with a 30.7% interest, while the Non-Associated Shareholders' collective interest would reduce to 68.4%.

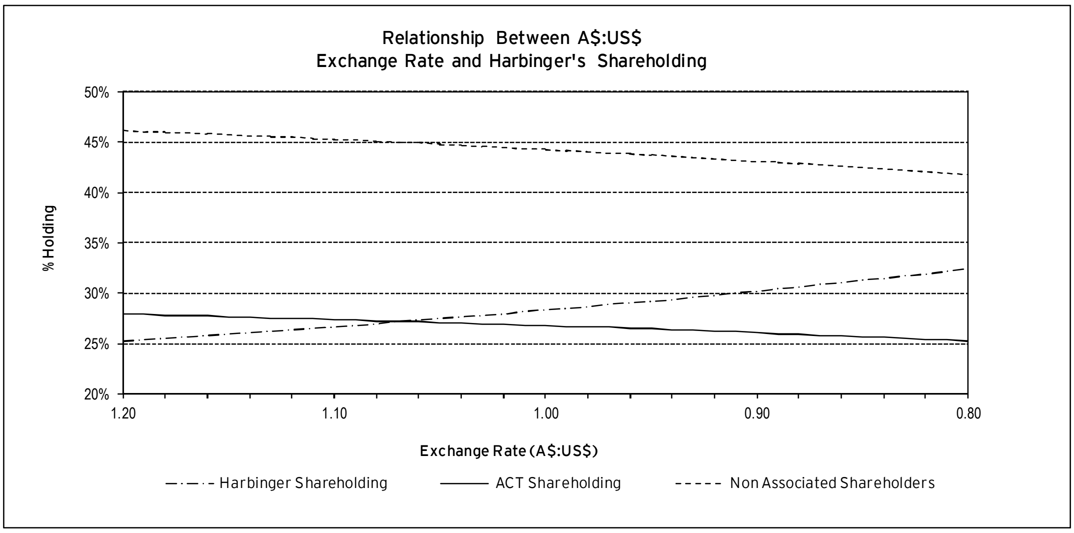
In the unlikely scenario that only the Existing Notes issued under Tranche 1 and the New Notes are converted, the Broker Shares issued and none of the options are exercised, the special bonus employee shares do not vest and the partly paid shares do not become fully paid, then Harbinger's interest in Poseidon would increase to 40.3%, with the Non-Associated Shareholders having a collective interest of 58.8%.

The scenarios considered above assume that no Dilution Factor adjustment is required to the Conversion Price on the New Notes. The Dilution Factor will only apply if Poseidon, in the 180 days after 22 December 2010, issues shares at a price less than 30 cents or if the Company pays a dividend.

The ultimate conversion of the Existing Notes and the New Notes will be impacted by movements in the A$:US$ exchange rate, in that conversion of the face value of the Convertible Notes is required to be calculated based on the exchange rate at the date of conversion. Recently the A$:US$ exchange rate has been at or close to parity, however over time the rate is likely to fluctuate.

If the A$:US$ exchange rate reduces to 90 cents then the number of shares that Poseidon would need to issue on conversion of both Tranche 1 of the Existing Notes and the New Notes would increase from 104,166,667 to 115,740,741. Under this scenario Harbinger's interest in the Company would be restated from 28.3% to 30.2%. The ACT's shareholding would reduce from 26.8% to 26.1%. The Non-Associated Shareholders collective interest would reduce from 44.3% to 43.1%.

The following chart summarises the relationship between the A$:US$ exchange rate and what Harbinger's interest in the Company would be if the Convertible Notes were converted, the Broker Shares issued, all of the options with an exercise price of less than 40 cents were exercised (except the August and November 2016 options), the bonus shares vest and the partly paid shares become fully paid.



Source: E&Y analysis

The following table summarises the possible impact of the conversion of Tranche 1 of the Existing Notes and the New Notes:

Summary of Shareholdings Under Different Scenarios	Non-Associated Shareholders	Harbinger	The ACT	Broker Shares
Present position	91.1%	8.9%	-	-
Convertible Notes converted (using a US$:A$ exchange rate at parity), Options priced at 40 cents or less exercised*, Broker Shares issued, bonus shares vest and partly paids are paid up	44.3%	28.3%	26.8%	0.6%
Convertible Notes converted (using a 90 cent exchange rate), Options priced at 40 cents or less exercised*, Broker Shares issued, bonus shares vest and partly paids are paid up	43.1%	30.2%	26.1%	0.6%
New Notes are converted only (using a US$:A$ exchange rate at parity), Options priced at 30 cents or less exercised*, Broker Shares issued, bonus shares vest and partly paids are paid up	68.4%	30.7%	-	1.0%
New Notes are converted only (using a 90 cent exchange rate), Options priced at 30 cents or less exercised*, Broker Shares issued, bonus shares vest and partly paids are paid up	66.6%	32.5%	-	0.9%

* excluding the August and November 2016 options which have a 50 cents price hurdle

The analysis shows that, regardless of whether both the Existing Notes issued under Tranche 1 and the New Notes are converted, or just the New Notes are converted, Harbinger's shareholding interest in Poseidon will increase to around 30%. The difference is that under the scenario whereby both the Existing Notes and the New Notes are converted, the options held by the ACT are assumed to be exercised, which would result in the ACT gaining an interest in the Company similar to Harbinger's interest at around 26%. If just the New Notes are converted then Harbinger would be Poseidon's largest shareholder by a significant margin.

With regards to Poseidon being able to elect to pay interest charged on the Convertible Notes through the issue of shares to Harbinger, given the three year interest free period no attempt has been made to quantify the number of shares that may be issued in satisfaction of any future interest payments due on the Convertible Notes.

Over the last two years, to conserve cash the Directors of the Company have accepted shares in payment for their directors' fees. While this is expected to continue, the number of shares issued is unlikely to have a material impact on the analysis contained in this section.

Of the 143,932,839 options that Poseidon has on issue, 17,165,403 have exercise prices or price hurdles greater than 40 cents. Because these options are 'out of the money' in comparison to the 40 cent amended conversion price of the Existing Notes and the 30 cents conversion price of the New Notes, they have not been included in our analysis.

It is of note that at the Company's 2008 AGM, pursuant to item 7 of Section 611 of the Act Poseidon shareholders approved the issue of shares to Harbinger on the possible conversion of the full US$50 million Existing Notes facility. Ernst & Young Transaction Advisory Services prepared an independent expert's report, dated 6 October 2008, in which an analysis of the potential impact of the issue of shares on conversion of the Existing Notes would have on the shareholders of Poseidon was detailed. Based on a A$:US$ exchange rate of 94.3 cents and the $1.00 conversion price, assuming that the relevant broker shares were issued, all options with an exercise price of less than $1.00 were exercised, the bonus shares vest and the partly paid shares paid up, the analysis indicated that Harbinger's shareholding in the Company would increase to 23.1%, with the ACT being Poseidon's largest shareholder with a 33.0% interest (at an 80 cent exchange rate Harbinger's interest increased to 25.1%).

The analysis for the amendment to the conversion terms of the Tranche 1 Existing Notes and the New Notes indicates an increase in Harbinger's shareholding interest above what already has been approved of approximately 7%, albeit Harbinger's interest would be greater than the ACT's interest.

5. Evaluation of the amendments and the New Notes

5.1 Issues of valuation

5.1.1 The nature of convertible notes

The issue of the New Note Shares and the Existing Note Shares will only occur if Harbinger elects to convert the New Notes and the Existing Notes issued under Tranche 1. If Harbinger does not convert the New Notes and the Existing Notes, Poseidon will be required to repay the US$35 million owing to Harbinger.

The New Notes have a six year life and are convertible at any time after the closing price of a Poseidon share on the ASX has exceeded the Conversion Price of 30 cents (assuming that there is no dilution) for five consecutive trading days. A review of the Company's trading price on the ASX shows that the last time Poseidon's shares closed above 30 cents for at least five consecutive days was in April 2010. Without Poseidon's share price meeting the price hurdles there is no certainty as to whether Harbinger will be able to convert the New Notes.

Under the amendments to the Existing Notes, the original six year life of the Existing Notes, which have been on issue for approximately 2.5 years, is to be reset to six years from the issue of the New Notes. With respect to the trading price hurdle applicable to the Existing Notes, the closing price of Poseidon's shares exceeded the $1.00 conversion for at least five consecutive days was met in June/July 2008 not long after the funds were received from Harbinger. Accordingly, the Existing Notes are eligible to be converted. While the trading hurdle on the Existing Notes is not being reset, the last time Poseidon's shares traded above 40 cents was in August 2009.

In considering the possible conversion of the Convertible Notes and the issue of the New Note Shares and the Existing Note Shares, the relevant date to assess the value of the New Note Shares and the Existing Note Shares is at or around the time the shares are issued and Harbinger's voting interest in Poseidon increases.

At the date of this report, no assessment of the value of the New Note Shares and the Existing Note Shares can reasonably be made as the possible date of conversion cannot be predicted and the value of a Poseidon share at any future date cannot be determined. Because of this, at the date of their issue the conversion price and the wider terms of the New Notes and the Existing Notes are more important than the underlying value of the Company's assets and liabilities. This is especially so in the circumstances of a transaction which does not reflect a change of control.

On this basis, in considering the possible issue of the New Note Shares and the Existing Note Shares we have considered the following matters:

- the nature of convertible debt securities; and
- the prices at which the Convertible Notes are to be converted compared to Poseidon's share trading prices on the ASX.

The nature of the convertible debt securities is such that it provides the holder with a right to convert the face value of the debt to shares in the issuer at a particular price at some time in the future. A key feature of the conversion right is that it generally provides the holder with the right but not the obligation to convert the debt to equity. Accordingly, while Harbinger has the right to convert the Convertible Notes there is no guarantee that it will.

It follows that, in most circumstances, a rational investor would only exercise the right to convert if the conversion price was at or less than the trading price of the company's underlying shares at the time of conversion. Accordingly, it would be expected that for the New Notes and the Existing Notes to be converted, at the time of conversion Poseidon's shares would have to be trading at prices equal to or above the respective conversion prices of 30 cents and 40 cents (assuming no dilution) or there was a strong likelihood of that occurring on a sustainable basis.

While future trading prices may be important to the holder's decision as to whether or not to convert the convertible debt security, an important consideration for the shareholders of the company issuing the security is the conversion price in comparison to the prices at which the company's shares have recently traded at the time the security is issued. The existence of a premium between recent trading prices and the conversion price is to the benefit of shareholders.

The prices at which Poseidon shares traded at over the period 4 January 2010 to 22 December 2010, the day before the announcement of the New Note issue and the amendment to the Existing Notes, is detailed in section 3.3. The comparison of recent trading prices with the conversion price is detailed in section 5.1.2. Section 5.1.3 considers Poseidon's share trading performance following the announcement of the New Note sfacility and the amendment to the Existing Notes on 23 December 2010.

5.1.2 Comparison of Poseidon's trading price and the conversion prices

The table in section 3.3 summarising the prices at which Poseidon's shares traded at on the ASX over the period 4 January 2010 to 22 December 2010 shows that over the period the Company's shares traded up from levels of around 25 cents to a high of 39 cents in mid-April 2010 then gradually down to a low of 14.5 cents by early September 2010. From there the shares traded up to levels of above 20 cents prior to the announcement of the New Notes facility on 23 December 2010. The closing price of the Company's shares on 22 December 2010 was 22 cents. The VWAP across the whole period was 24.1 cents.

Over the six months prior to the announcement of the issue of the New Notes to Harbinger, and the amendment to the Existing Notes, Poseidon's shares on the ASX generally traded in the range of 17 cents and 22 cents.

The VWAP for Poseidon shares for the 5, 20, 40 and 60 trading days prior to the announcement on 23 December 2010, together with the closing price on 22 December 2010, in comparison to the respective 30 cent and 40 cent conversion prices are detailed below.

Comparison of Trading Prices to Conversion Prices		Premium / (Discount) over Trading Price	
	$	New Notes	Existing Notes
Conversion price ($)		0.300	0.400
Closing price on 22 December 2010	0.220	36.4%	81.8%
5 day VWAP	0.250	20.0%	60.0%
20 day VWAP	0.220	36.4%	81.8%
30 day VWAP	0.211	42.2%	89.6%
60 day VWAP	0.206	45.6%	94.2%

Source: E&Y analysis

The analysis indicates that at the time of the announcement of the issue of the New Notes to Harbinger, and the amendment to the Existing Notes, the respective conversion prices of 30 cents and 40 cents were at significant premiums to the prices at which Poseidon's shares had traded on the ASX over the preceding three months. Based on the closing price of the Company's shares on the day prior to the announcement, the premium was 36.4% for the New Notes and 81.8% for the Existing Notes.

It is of note that when the Existing Notes facility was announced on 26 June 2008 the conversion price of $1.00 was at a premium to the closing price of Poseidon shares on 25 June of 35.1%, a 20.2% premium to the 20 day VWAP and a 26.4% premium to the 60 day VWAP. As detailed in the table above, the premium of the Conversion Price on the New Notes and the amended conversion price on the Existing Notes are at greater premiums to those evident at the time the Existing Notes facility was announced.

On the premise that the New Notes and the Existing Notes will only be converted if the trading price of a Poseidon share is at or above their conversion price, having a conversion price which is at a premium to the trading prices at the time of issue is to the advantage of the Non-Associated Shareholders on the basis that the Company's trading price will need to increase substantially before conversion is likely. Any increase in Poseidon's underlying trading price on the ASX would be to the benefit of the Non-Associated Shareholders.

5.1.3 Trading price since the announcement

The table below summarises the market trading performance of Poseidon shares for the 12 trading days following the announcement of the issue of the New Notes to Harbinger and the amendment of the Existing Notes prior to trading commencing on 23 December 2010.

Poseidon - Share Price Post Announcement of the New Notes and Amendment to Existing Notes

	High $	Low $	Close $	VWAP $	Volume	Liquidity
23-Dec-10	0.25	0.23	0.24	0.242	695,934	0.4%
24-Dec-10	0.26	0.24	0.25	0.249	368,200	0.2%
29-Dec-10	0.27	0.26	0.26	0.260	3,820,480	2.0%
30-Dec-10	0.27	0.25	0.25	0.259	2,906,271	1.5%
31-Dec-10	0.27	0.25	0.27	0.259	950,022	0.5%
04-Jan-11	0.27	0.25	0.26	0.257	602,880	0.3%
05-Jan-11	0.26	0.25	0.26	0.253	278,804	0.1%
06-Jan-11	0.26	0.23	0.23	0.249	836,395	0.4%
07-Jan-11	0.26	0.24	0.25	0.247	1,044,777	0.5%
10-Jan-11	0.25	0.24	0.24	0.243	1,996,700	1.0%
11-Jan-11	0.26	0.24	0.24	0.248	2,981,065	1.5%
12-Jan-11	0.24	0.22	0.23	0.232	753,043	0.4%
Max				**0.260**	**3,820,480**	**2.0%**
Min				**0.232**	**278,804**	**0.1%**
12 day average prior to announcement				**0.227**	**1,445,271**	**0.9%**
12 day average post announcement				**0.250**	**1,436,214**	**0.7%**
12 day VWAP prior to announcement				**0.230**		
12 day VWAP post announcement				**0.252**		

Source: E&Y analysis

Based on the movement in share price since the announcement of the New Notes and the amendment to the Existing Notes, it appears that the announcement has had a positive impact on the share price of Poseidon. The VWAP for the 12 days considered pre and post the announcement increased by 9.6%. Over the 12 trading days the total shares traded equated to 8.9% of the number of shares Poseidon has on issue, representing a liquidity higher than the Company's recent history.

The respective conversion prices of 30 cents and 40 cents are at a 30% and 74% premium to the closing price of a Poseidon share on 12 January 2011 of 23 cents. On the assumption that the Company's share price would need to increase to the 30 cent and 40 cent levels before conversion is likely, any increase in Poseidon's underlying trading price on the ASX would be to the benefit of the existing Non-Associated Shareholders.

In the six trading days between 13 January 2011 and 20 January 2011, Poseidon's shares traded in the range of 22.5 cents and 25 cents, closing on 20 January at 24 cents. The volume of shares traded averaged around 290,000 per day.

5.2 Commercial and qualitative factors

5.2.1 The terms of the New Notes and the amendments to the Existing Notes

Included in the table below are details of convertible note issues undertaken by Australian resource companies over the last six months. This list is not meant to be exhaustive; its purpose is to provide recent examples of the terms that convertible notes have been issued on. In providing the list it is recognised that the circumstances and operations of each company are different.

Company	Share Price at Time	Premium / (Discount) Conversion Price to Share Price	Market Cap. (m's)	Amount Raised (m's)	Summary of Terms	Use of Funds
Galaxy Resources *November 2010*	$1.16	35%	$220.1	$61.5	Approx. Term: 5 years Interest Rate: 8% p.a Conversion Price: A$1.56 Other terms: The conversion price may be reset downwards to the market price 12 months after the settlement date, subject to a floor price equal to 80% of the conversion price	Capital to fund the final stages of development of its current projects and also provide the Company with funds for the potential acquisition of additional lithium-related projects
Continental Coal *October 2010*	$0.08	1%	$105.9	$10.0	Approx. Term: 3 Years Interest Rate: 10% p.a. paid six monthly in arrears Conversion Price: A$0.08 Other terms: If the noteholder elects to convert the note prior to one year from the commitment date, the noteholder will be issued with one option for every five shares issued with an exercise price of 8 cents and expiry on 15 September 2013	Capital to fund the acquisition of unlisted South African thermal coal mining and export coal producing company Mashala Resources ("Mashala") and the development of the Company's third coal mine at the Penumbra Project in South Africa
Kangaroo Resources *July 2010*	$0.12	16%	$89.4	US$14.0	Approx. Term: 2 years Interest Rate: 10% p.a Conversion Price: $0.133 Other terms: At the time of the issue of the notes, each noteholder will be entitled to receive one warrant exercisable at A$0.133 per share for each share to which the noteholder would become entitled to upon conversion of the notes. The warrants will expire five years after the first closing date	Capital to fund the progress the Company's key Indonesian coal projects, in particular the ramp-up of production and exploration at the Mamahak Coking Coal Project, and to advance exploration across the balance of the Company's key properties

Source: E&Y analysis

The key differences between the convertible notes listed and the New Notes facility and the amended Existing Notes issued under Tranche 1 are the six year term, the three year interest free period and the interest rate of 5% per annum thereafter. With respect to US$15 million received under Tranche 1, this amount has been interest free since June 2008. The proposed amendments to these notes effectively extend their term from six years to approximately 8.5 years and the interest free period from three years to 5.5 years.

Under both facilities, Harbinger is providing Poseidon with US$35 million on an interest-free basis for three years. At an interest rate of 8% to 12% per annum this is a saving to the Company of US$8 million to US$13 million across the three years (an additional US$4 million to US$5 million on the extra 2.5 years interest free period on the US$15 million Tranche 1 Existing Notes). At the 5% being charged for the final three years, the three year interest free period represents a saving of over US$5 million.

In regards to the reduction of the conversion price on the Existing Notes from $1.00 to 40 cents, Poseidon's shares last traded at prices above $1.00 in July 2008 prior to the full impact of the GFC being felt across world equity markets. The ability of the Company's shares to trade at levels of around $1.00 will be dependent on, amongst many other factors, the successful development of Windarra. Without securing the necessary funding to develop Windarra, all other things being equal, the likelihood of Poseidon's shares trading at $1.00 is low. In these circumstances, it is unlikely that the Existing Notes with a $1.00 conversion price would be converted and Poseidon would need to source funding to repay the US$15 million. The reduction of the conversion price to 40 cents, together with the provision of the US$20 million funding by Harbinger, will increase the possibility of Poseidon's share price reaching a level where the Existing Notes will be converted.

The saving of interest will enable Poseidon to redirect funds that otherwise would be required to meet interest payments towards Windarra and its other mineral projects. Alternatively, if Poseidon was to elect to meet interest payments through the issue of shares, the interest free period means that there is no dilution through the issue of shares. The interest free period is a significant benefit to the Non-Associated Shareholders.

The 5% per annum interest rate for the final three years is low when compared to the other convertible notes and interest rates in general. Securing funds at a 5% interest rate is a benefit to the Non-Associated Shareholders.

If the amendments to the Existing Notes are not approved or are not implemented because the issue of the New Notes and New Note Shares are not approved, Poseidon will be required to pay interest on the US$15 million from 26 June 2011. At an interest rate of 5% per annum, the quarterly charge would be approximately US$190,000. Without the Company having the cash flows to meet these payments they would need to be met by the issue of shares. The reset of the interest free period on the Existing Notes is a significant benefit to the Non-Associated Shareholders.

In the case of the Existing Notes, without the amendments and in the absence of conversion, the US$15 million would become repayable in June 2014. If the New Notes are issued in March 2011, the maturity date of the Existing Notes will be extended to March 2017. The extension is a significant benefit to the Non-Associated Shareholders.

It is assumed that the willingness of Harbinger to provide the funds to Poseidon on an interest free basis reflects the expected capital appreciation in the Company's share price as the development of Windarra progresses. The expectation is that, all other things being equal (i.e. nickel prices, demand, etc) the spending of the US$20 million by Poseidon should add substantial value to the Windarra Nickel Project and, in turn, have a positive impact on the Company's underlying share price. If this is the case then the Non-Associated Shareholders will benefit.

In the circumstances that the development does not occur or is not successful, it is unlikely that the New Notes or the Existing Notes will be converted on the basis that the Company's share price will continue to trade below the respective conversion prices. Under this scenario, it would be unlikely that the Company would have the financial capacity to repay the US$35 million. The existence of this risk and Harbinger's willingness to provide the funding reflects the expectations that Harbinger has in Windarra being successfully developed.

The convertible notes considered in the table above generally have conversion prices that were at a premium to the company's share price around the date the issues were announced, however the premiums were substantially less than the premium on the New Notes and the amended Existing Notes, as detailed in section 5.1.2.

The terms of the New Notes and the Existing Notes are attractive when compared to other convertible note issues and when compared to normal terms on which debt facilities are generally provided. Securing funding under these terms is a significant benefit to the Non-Associated Shareholders.

Included in the following table is a summary of the terms of the Convertible Notes in comparison to other sources of funding:

Type of Financing	Interest Free Period	Interest Rate at 5%	Available to Developing Resource Companies	Dilutionary on Issue	Issued at Premium to Market Price	Secured
Bond market	no	higher	no	no	n/a	varied
Equity market	n/a	n/a	yes	yes	n/a	n/a
Debt financing	no	higher	no	no	n/a	yes
Recent convertible note issues	no	higher	yes	no	varied	varied
The Convertible Notes	yes	yes	yes	no	yes	no

Source: E&Y analysis

On each measure, the terms of the New Notes and the Existing Notes are more attractive than the other sources referred to, with the benefits to the Non-Associated Shareholders being substantial. The ability of Poseidon to source alternative funding is considered in section 5.2.5.

5.2.2 Control issues

As at the date of this report, Poseidon had on issue 194,876,072 fully paid ordinary shares, 425,000 partly paid shares, 313,131 special bonus employee shares and 143,932,839 options. Harbinger is the Company's largest shareholder with an 8.9% interest. As at 20 December 2010, Poseidon's second largest shareholder had a 5.7% interest, with the top 20 shareholders holding approximately 34% of the shares on issue.

With the US$20 million New Notes having a Conversion Price of 30 cents, assuming a A$:US$ exchange rate at parity and no Dilution Factor, if the New Notes were converted Poseidon would need to issue to Harbinger 66,666,667 New Note Shares.

With the conversion price on the Existing Notes issued under the US$15 million Tranche 1 being reduced to 40 cents, under the same assumptions as for the New Notes, the number of Existing Notes Shares that would need to be issued on conversion would be 37,500,000.

Of the options Poseidon has on issue, 9,267,436 have an exercise price of less than 30 cents. Excluded from this number are 7,475,000 options which, although having an exercise price of 25 cents, have a 50 cents price hurdle which is yet to be achieved. If the New Notes were converted, the options with an exercise price of less than 30 cents that could be exercised were exercised, the special bonus employee shares vested, the partly paid shares were paid up and the Broker Shares issued, Harbinger's interest in the Company would increase to 30.7%. Assuming the second largest shareholder holds no options, that entity's 5.7% interest would reduce to 4.1%.

In addition to those eligible options with an exercise price of less than 30 cents, Poseidon has 117,500,000 options which are exercisable at 40 cents, of which 115,000,000 are held by the ACT. If the New Notes were converted, the Existing Notes converted, the options with an exercise price of 40 cents or less that could be exercised were exercised, the special bonus employee shares vested, the partly paid shares were paid up and the Broker Shares issued, Harbinger's interest in the Company would increase to 28.3%. With the exercise of the options, the ACT's interest in the Company would be 26.8%.

As a maximum scenario, if only the New Notes and Existing Notes are converted, the Broker Shares issued and none of the options are exercised, the special bonus employee shares do not vest and the partly paid shares do not become fully paid, then Harbinger's interest in Poseidon would increase to 40.3% (assuming an A$:US$ exchange rate at parity). The second largest shareholder's 5.7% interest would reduce to 3.7%.

Under the Act, an entity is considered to have control of a company if it has the capacity to determine the outcome of decisions about the company's financial and operating policies. Section 608 (5) states that the determination of whether an entity has the capacity to control a company is based on the "*practical influence*" that the entity can exert on a company as opposed to the "*rights they can enforce*".

In April 2007, Poseidon (then known as Niagara Mining Limited) announced that it was to undergo a reorganisation whereby the majority of directors and management would stand down and be replaced by a team led by Mr Andrew Forrest, as non-executive Chairman. The reorganisation was completed and approved by shareholders at a general meeting held on 2 July 2007. With the exception of Mr Geoff Brayshaw, who was appointed a Director in February 2008, the Board of Directors and the senior management of Poseidon have essentially been in place since the reorganisation.

In support of the 'reorganised' Poseidon and its reconstituted Board and management team, Harbinger became a substantial shareholder of Poseidon in April 2007 and has remained a substantial shareholder since that time, maintaining a greater than 15% interest across most of that period. Harbinger's support of the Company, the Board and its management was reflected in agreeing to provide Poseidon with the US$50 million Existing Notes facility in June 2008. While Harbinger sold down its interest in the Company to 8.9% between July 2010 and November 2010, its agreeing to provide the US$20 million New Notes facility again signals its continued confidence in the Board and its management to achieve the Company's objective of re-establishing Windarra as a viable nickel mining operation.

In the announcement of the provision of the New Notes facility, Mr Philip Falcone, Harbinger's Chief Executive Officer, stated that "*Poseidon has a first class Board and management team and is well poised to develop Windarra into an effective and profitable sulphide nickel project. We* (i.e. Harbinger) *are pleased to be able to reaffirm our commitment to this project. The Windarra Nickel Project has surpassed all of our investment criteria fundamentals and delivers an excellent entry point in the strengthening nickel industry*".

In supporting the Board and the management team over the period it has been a substantial shareholder, Harbinger has not had and has not acted to obtain representation on Poseidon's Board of Directors. While it is not known what Harbinger's intentions may be, it is not unreasonable to suggest that as long as Harbinger supports the current Board and management team it will not look to seek Board representation.

Being the largest shareholder with a 30.7% shareholding in the Company, in the event that only the Tranche 1 of the Existing Notes are converted, even if Harbinger sought a position on the Board it is unlikely that it would be able to gain majority representation. Without Board representation or the ability to control the Board, it is unlikely that Harbinger would have the capacity to control the financial and operating activities of Poseidon. In stating that, Harbinger would be in a position to exert significant influence on the Company as the dominant shareholder.

In the situation where the New Notes and the Existing Notes issued under Tranche 1 are converted and the ACT exercised its options, Harbinger's 28.3% interest would be matched by the ACT's 26.8% interest. Harbinger's ability to exert significant influence on Poseidon in this circumstance would be less likely.

In considering the exercise of the 115,000,000 options held by the ACT, these expire in September 2012 whereas the New Notes and the Existing Notes at that time will have an approximate 4.5 years to maturity. The longer conversion period may mean that the options held by the ACT may not be exercised, but the New Notes and Existing Notes are ultimately converted at a later date. Given the intention of the Company to develop Windarra over the short term, it is anticipated that any success at Windarra would have a positive impact on Poseidon's share price, and that the ACT options will be 'in the money' before September 2012.

The nature of Harbinger as a hedge fund and consideration of Harbinger's investment activity in ASX listed companies is detailed in Section 5.2.3. Consistent with its nature, our analysis indicates that Harbinger has primarily acted as an investor as opposed to seeking to control an investee company.

If Harbinger was looking to dispose of a greater than 20% interest to a single purchaser or a number of related entities, shareholder approval would need to be obtained under item 7 of Section 611 of the Act. Similarly if the ACT was looking to dispose a greater than 20% interest in the same circumstances it would also need to obtain shareholder approval.

Having a greater than 20% interest in Poseidon may enable Harbinger to influence the Company in general meetings. However, this may not be to the detriment of the Non-Associated Shareholders. With a shareholding of around 30%, as long as greater than 43% of the remaining shares are voted, then Harbinger will not be in the majority.

While being the largest shareholder without having Board representation, it is unlikely that Harbinger will be in a position to control the Company's financial and operating policies. Harbinger not looking to control the Company reflects, in part, its confidence in Poseidon's current Board and management team. This confidence in the current Board and management team to be able to bring Windarra to production should be to the advantage of the Non-Associated Shareholders.

5.2.3 Harbinger

Harbinger is a US based hedge fund which as at December 2010 was reported to be managing investments valued at over US$8 billion, down from a reported peak of approximately US$26 billion in mid 2008. Commencing in 2001, Harbinger has followed a strategy of identifying and investing in undervalued assets, special situation assets and assets that are distressed. As with the investment in Poseidon, it is not unusual for the funds managed by Harbinger to co-invest in opportunities.

Prior to the GFC, Harbinger was an active investor in Western Australian resource stock; however over the past 18 months the group has sold the majority of its key interests in various high profile Western Australian listed companies, including Fortescue Metals Group Ltd ("FMG") and Murchison Metals Ltd ("Murchison"). Harbinger has decreased its shareholding in FMG and Murchison over the past year from holdings of approximately 15% to 20% in each company, to levels to where it has ceased to be a substantial shareholder in either company (i.e. reduced shareholding to less than 5%).

Historically, as a substantial shareholder in listed Australian resource companies, Harbinger has consistently not had or not looked to obtain any board representation and has had no involvement in the management of any of the companies. In general Harbinger has taken a passive role as an investor and does not act to influence the management of its investee companies.

However, it is clear that if Harbinger believes the investee company is underperforming or is contemplating a transaction that Harbinger believes is not necessarily in the best interest of shareholders then it will take action to protect its position. While this action, to date, has not appeared to have included acting to gain control of an investee company it has included obtaining a minority position on the board of directors and using its shareholding interest to influence the outcome of proposed transactions. Given the nature of Harbinger as a hedge fund, it is likely that any action taken by Harbinger would, in the first instance, be to protect its position rather than the position of all shareholders as a whole, albeit any improved performance of an investee company would be to the benefit of all shareholders.

While Harbinger's intentions for its investment in Poseidon are not known, its track record with its investment in ASX listed resource companies shows that it is supportive of management and their endeavours to bring mineral projects into production. For Poseidon, which is looking to re-establish its development of the Windarra Nickel Project, having Harbinger's support should be to the advantage of all shareholders.

5.2.4 Poseidon's need for funding

Poseidon's focus is on the development of Windarra as a world class nickel operation. The cost of reopening Windarra, including mine refurbishment, underground drilling, feasibility study and construction of a concentrator is estimated by management at US$55 million. The initial mining rate is forecast at 350,000 tonnes per annum, producing 4,500 tonnes of nickel in concentrate. In the medium term it is proposed to increase production to 10,000 tonnes of nickel in concentrate per annum.

The funds provided by Harbinger are to be applied to assist in financing the following activities:

- complete the dewatering and refurbishment works at the Windarra mine with commencement of the program to take place in early 2011;
- expand the drilling program at the Mt Windarra, Cerberus and South Windarra prospects to increase the JORC complaint resources and reserves; and
- complete the feasibility study with respect to the construction of a concentrator at Windarra.

At 31 December 2010, Poseidon had cash on hand of approximately $736,000.

Throughout 2010 Poseidon has funded the work conducted at Windarra and its other projects by way of share placements. Since March 2010 the Company has conducted two capital raisings, issuing approximately 25.9 million shares at an average price of approximately 20 cents per share, raising total cash of about $5.2 million. Details of the two capital raisings are contained in section 5.2.5.

The provision of the US$20 million by Harbinger under the issue of the New Notes on the attractive terms negotiated is a significant step for Poseidon being able to continue the redevelopment of Windarra and work towards achieving its objectives.

5.2.5 Alternative sources of funding

By securing the US$20 million through the New Notes facility it is anticipated that Windarra will be progressed to the stage where a final decision on its development will be made. Currently, management estimate that the total costs to develop Windarra will be around US$55 million. It is anticipated that funding beyond the US$20 million will be sourced through debt. Until a decision is made on the development of Windarra securing funding through more conventional debt sources is not a viable option for Poseidon.

Poseidon successfully completed two separate share placements during 2010, raising approximately $5.2 million through the issue of approximately 25.9 million shares. As detailed in the following table the placements were done at a discount to the share price of a Poseidon share as at the announcement date (based on the closing price on the day before the announcement).

Poseidon - Capital Raisings Undertaken in 2010						
Date Announced	Share Price $	Amount Raised $000's	Issue Price $	Discount to Share Price	5 day VWAP $	Discount to Share Price
3 March 2010	0.265	2,000	0.25	5.7%	0.283	11.7%
22 July 2010	0.190	3,216	0.18	5.3%	0.207	13.1%

Source: E&Y analysis

The capital raising announced on 22 July 2010 was conducted through two tranches and had a free attaching option on a one-for-two basis, exercisable at 25 cents.

If Poseidon were to continue funding its operations through periodical share placements it is likely that the need to offer shares at a discount would continue. Based on a share price of 25 cents, the Company's market capitalisation totals approximately $49 million. Without significant market support it is unlikely that Poseidon would be able to raise an amount equivalent to the SU$20 million being provided by Harbinger under the New Notes facility. Without having access to sufficient capital it would be difficult for the Directors to commit to recommencing the redevelopment of Windarra.

Raising funds through placements would be significantly more dilutionary than the proposed funding arrangement with Harbinger. At a share price of 25 cents less a discount of 5%, to raise A$20 million, Poseidon would have to issue approximately 84 million shares (representing approximately 30% of the Company's expanded share capital). While it is recognised that the full amount may not have to be raised at once, the continued need for ongoing funding would expose the Company to potential uncertainty in financial markets.

Given these matters, the offer of shares as an alternative source of funding for Poseidon at this time would be to the disadvantage of the Non-Associated Shareholders.

Prior to negotiating the New Notes with Harbinger, Poseidon management confirmed that they were in advanced discussions with another overseas group with respect to the provision of funding. While no formal offer was made, management confirmed that the terms of the New Notes are more attractive than those being discussed with the other party.

Regardless of whether or not Poseidon has available alternative sources, it is unlikely that any funding would be on as attractive terms as the terms on which Harbinger has provided the Convertible Notes.

5.3 Premium for control

A "premium for control" generally represents the difference between the price per share which one party would be prepared to pay to obtain a controlling interest in a company and the price at which a share that does not carry with it control of that company could be acquired. In the case of the issue of shares, the entity receiving the shares is paying a premium if the value of the shares being issued is less than the value of the consideration being paid. The greater the premium the better off the shareholders not involved in the transaction will be.

In relation to the possible issue of the New Note Shares and the Existing Note Shares, because the future fair value of the shares to be issued cannot be determined at this time, an assessment of whether or not Harbinger would be paying a premium for control is, at the date of this report, not possible. It is however relevant to note that the respective 30 cent and 40 cent conversion prices of the Convertible Notes were at a premium of 25% and 67% to the closing price of a Poseidon share on the ASX of 24 cents on 20 January 2011. . It is also relevant that when comparing the 5 day, 20 day, 30 day and 60 day volume weighted average prices prior to the date the New Notes facility and the amendment to the Existing Notes were announced on 23 December 2010 with the conversion prices, there was a premium ranging from 20.0% to 45.6% on the 30 cent conversion price and a premium ranging from 60.0% to 94.2% on the 40 cent conversion price. The existence of the premium is to the benefit of the Non-Associated Shareholders.

6. Summary and conclusion

In forming our opinion as to whether the issue of the New Note Shares to Harbinger on the possible conversion of the Convertible Notes is fair and reasonable to the Non-Associated Shareholders of Poseidon, we have considered the following matters:

The Nature of Convertible Securities

- In considering the possible conversion of the Convertible Notes and the issue of the New Note Shares and the Existing Note Shares, the relevant date to assess the value of the New Note Shares and the Existing Note Shares is at or around the time the shares are issued and Harbinger's voting interest in Poseidon increases. At the date of this report, no assessment of the value of the New Note Shares and the Existing Note Shares can reasonably be made as the possible date of conversion cannot be predicted and the value of a Poseidon share at any future date cannot be determined. Because of this, at the date of their issue the conversion price and the wider terms of the New Notes and the Existing Notes are more important than the underlying value of the Company's assets and liabilities.

- The nature of the convertible debt securities is such that it provides the holder with a right to convert the face value of the debt to shares in the issuer at a particular price at some time in the future. A key feature of the conversion right is that it generally provides the holder with the right but not the obligation to convert the debt to equity. Accordingly, while Harbinger has the right to convert the New Notes and the Existing Notes issued under Tranche 1 there is no guarantee that it will. If the Convertible Notes are not converted, Harbinger's interest in the Company does not increase.

- Because of this right but not the obligation to convert, it follows that in most circumstances, a rational investor would only exercise the right to convert if the conversion price was less than the market trading price of the company's underlying shares at the time of conversion. Accordingly, it would be expected that for the New Notes and the Existing Notes to be converted, at the time of conversion Poseidon's shares would have to be trading at prices equal to or above the respective conversion prices of 30 cents and 40 cents (assuming there has been no dilution) or there was a strong likelihood of that occurring on a sustainable basis.

Comparison of the Trading Price of a Poseidon Share with the Conversion Prices

- The table below compares Poseidon's VWAP's for various periods up until the announcement of the US$20 million New Notes facility with Harbinger and the amendment to the Existing Notes and closing price on 22 December 2010, being the date before the announcement:

Comparison of Trading Prices to Conversion Prices		Premium / (Discount) over Trading Price	
	$	New Notes	Existing Notes
Conversion price ($)		0.300	0.400
Closing price on 22 December 2010	0.220	36.4%	81.8%
5 day VWAP	0.250	20.0%	60.0%
20 day VWAP	0.220	36.4%	81.8%
30 day VWAP	0.211	42.2%	89.6%
60 day VWAP	0.206	45.6%	94.2%

Source: E&Y analysis

- Accordingly, across all periods considered the 30 cents conversion price of the New Notes and the amended 40 cent conversion price on the Existing Notes are at a substantial premium to the prices at which Poseidon's shares had been trading at on the ASX.

- On the premise that the New Notes and Existing Notes will only be converted if the trading price of a Poseidon share is at or above the conversion price, having a conversion price which is at a premium to trading price at the time of issue is to the advantage of the Non-Associated Shareholders on the basis that the Company's trading price will need to increase substantially before conversion is likely. Any increase in Poseidon's underlying trading price on the ASX would be to the benefit of the Non-Associated Shareholders.

- In considering the prices at which Poseidon's shares traded at on the ASX there has been an increase in the Company's share price post the announcement of the intended issue of the New Notes and the amendments to the Existing Notes, in that the VWAP for the 12 trading days post the announcement was 9.6% higher than the VWAP for the 12 trading days pre the announcement. The market appears to reacted positively to the New Notes facility.

The Attractive Terms of the New Notes and the Amendments to the Existing Notes

- With an interest free period of three years and an interest rate of 5% per annum thereafter, the terms of the New Notes are extremely attractive when compared to other convertible note issues and to normal terms on which debt facilities are generally provided. Accordingly, being able to secure funding under the terms of the New Notes is a significant benefit to the Non-Associated Shareholders.

- The amendments to the terms of the Existing Notes effectively extend the period of the Existing Notes from six years to approximately 8.5 years and the interest free period from three years to approximately 5.5 years. Without the amendments, interest will become payable on the US$15 million of Tranche 1 of the Existing Notes from 26 June 2011 and repayment would be due in June 2014. The reduction of the conversion price from $1.00 to 40 cents should increase the possibility of the Existing Notes being converted. Under the original terms of the Existing Notes it would have been likely that Poseidon would have to source US$15 million to redeem that Existing Notes. The amendment of the terms of the Exiting Notes is of significant benefit to the Non-Associated Shareholders.

Matters of Control

- If the New Notes are converted, the Existing Notes are converted, the options with an exercise price of 40 cents or less that could be exercised are exercised, the special bonus employee shares vested, the partly paid shares were paid up and the Broker Shares issued, Harbinger's interest in the Company would increase to 28.3% (assuming an A$:US$ exchange rate at parity). The ACT's interest in the Company on the exercise of the 40 cent option it holds would be 26.8%. In this circumstance, Harbinger would not be in a position to control Poseidon.

- If the New Notes are converted, the options with an exercise price of 30 cents or less that could be exercised are exercised, the special bonus employee shares vested, the partly paid shares were paid up and the Broker Shares issued (i.e. the Existing Notes are not converted and the ACT options not exercised), Harbinger's interest in the Company would increase to 30.7% (assuming an A$:US$ exchange rate at parity). The second largest shareholder would hold a less than 5% interest. Even if Harbinger sought a position on the Board it is unlikely that it would be able to gain majority representation. Without Board representation or the ability to control the Board, it is unlikely that Harbinger would have the capacity to control the financial and operating activities of Poseidon. In stating that, Harbinger would be in a position to exert significant influence on the Company as the dominant shareholder.

- Harbinger not looking to control the Company reflects, in part, its confidence in Poseidon's current Board and management team. This confidence in the current Board and management team to be able to bring Windarra to production should be to the advantage of the Non-Associated Shareholders.

Harbinger

- While Harbinger's intentions for its investment in Poseidon are not known, its track record with its investment in Poseidon as well as other ASX listed resource companies shows that it is supportive of management and their endeavours to bring mineral projects into production. For Poseidon, which is looking to develop the Windarra Nickel Project, having Harbinger's support should be to the advantage of all shareholders.

- Harbinger's significant investment in Poseidon without having Board representation indicates that it has confidence in the Company's current management team, this should be to the advantage of the Non-Associated Shareholders.

Poseidon's Need for Funding and Alternative Sources

- The provision of the US$20 million by Harbinger under the issue of the New Notes on the attractive terms negotiated is a significant step for Poseidon being able to continue the development of Windarra.

- With a share price less than the conversion price, raising capital through the issue of shares would be more dilutionary to the Non-Associated Shareholders than the issue of the Convertible Notes.

- Regardless of whether or not Poseidon has available alternative sources, it is unlikely that any funding would be on as attractive terms as the terms on which Harbinger has provided the Convertible Notes.

Based on the matters summarised above and detailed discussion and analysis throughout this report, the issue of the New Note Shares and the Existing Notes to Harbinger on the possible conversion of the New Notes and Tranche 1 of the Existing Notes is, in our opinion, fair and reasonable to the Non-Associated Shareholders. In stating this, it is our view that the advantages which may accrue if the issue of the New Note Shares and Existing Note Shares are approved outweigh the disadvantages.

In relation to the possible issue of the New Note Shares and the Existing Note Shares, because the future fair value of the shares to be issued cannot be determined at this time, an assessment of whether or not Harbinger would be paying a premium for control is, at the date of this report, not possible. It is however relevant to note that the respective 30 cent and 40 cent conversion prices of the New Notes and Existing Notes are at a premium of 25% and 67% to the closing price of a Poseidon share on the ASX on 20 January 2011. It is also relevant that when using the 20 day, 30 day and 60 day VWAPs prior to the date the New Notes facility and the amendment to the Existing Notes was announced on 23 December 2010, a premium ranged from 20.0% to 45.6% on the 30 cent conversion price and 60.0% to 94.2% on the 40 cent conversion price. The existence of the premium is to the benefit of the Non-Associated Shareholders.

Appendix A Statement of qualifications and declarations

Ernst & Young Transaction Advisory Services, which is wholly owned by Ernst & Young, holds an Australian Financial Services Licence under the Act and its representatives are qualified to provide this report. The directors of Ernst & Young Transaction Advisory Services responsible for this report have not provided financial advice to Poseidon.

Prior to accepting this engagement, Ernst & Young Transaction Advisory Services considered its independence with respect to Poseidon with reference to Regulatory Guide 112, *Independence of experts*.

This report has been prepared specifically for the shareholders of Poseidon in relation to the issue of New Notes and the amendment to the Existing Notes. Neither Ernst & Young Transaction Advisory Services, Ernst & Young and any employee thereof undertakes responsibility to any person, other than the Poseidon Shareholders, in respect of this report, including any errors or omissions howsoever caused.

The statements and opinions given in this report are given in good faith and the belief that such statements and opinions are not false or misleading. In the preparation of this report Ernst & Young Transaction Advisory Services has relied upon and considered information believed after due inquiry to be reliable and accurate. Ernst & Young Transaction Advisory Services has no reason to believe that any information supplied to it was false or that any material information has been withheld from it. Ernst & Young Transaction Advisory Services has evaluated the information provided to it by Poseidon, its advisors, as well as other parties, through inquiry, analysis and review, and nothing has come to its attention to indicate the information provided was materially mis-stated or would not afford reasonable grounds upon which to base its report. Ernst & Young Transaction Advisory Services does not imply and it should not be construed that it has audited or in any way verified any of the information provided to it, or that its inquiries could have verified any matter which a more extensive examination might disclose.

The information relied upon in the preparation of this report is set out in Appendix B to this report.

Poseidon has provided an indemnity to Ernst & Young Transaction Advisory Services for any claims arising out of any mis-statement or omission in any material or information provided to it in the preparation of this report.

Ernst & Young Transaction Advisory Services provided draft copies of this report to the directors and management of Poseidon for their comments as to factual accuracy, as opposed to opinions, which are the responsibility of Ernst & Young Transaction Advisory Services alone. Changes made to this report as a result of this review by the directors and management have not changed the methodology or conclusions reached by Ernst & Young Transaction Advisory Services.

Ernst & Young Transaction Advisory Services will receive a professional fee based on time spent in the preparation of this report estimated at approximately $35,000 (exclusive of GST). Ernst & Young Transaction Advisory Services will not be entitled to any other pecuniary or other benefit whether direct or indirect, in connection with the making of this report.

Ms Brenda Moore, a representative of Ernst & Young Transaction Advisory Services and an executive director of Ernst & Young and Mr Ken Pendergast, a director and representative of Ernst & Young Transaction Advisory Services and a partner of Ernst & Young have assumed overall responsibility for this report. Both have the necessary experience and professional qualifications appropriate to the advice being offered. Other Ernst & Young Transaction Advisory Services staff have been consulted in the preparation of this report where appropriate.

It is not intended that the report should be used for any other purpose other than to be included in the Notice of Meeting and Explanatory Memorandum to be sent to Poseidon shareholders with respect to the New Notes and the amendment of the Existing Notes. In particular, it is not intended that this report should be used for any other purpose other than as an expression of its opinion as to whether or not the of the New Note Shares and the Existing Notes to Harbinger on the possible conversion of the New Notes and Tranche 1 of the Existing Notes is fair and reasonable to the Non-Associated Shareholders.

Ernst & Young Transaction Advisory Services consents to the issue of this report in the form and context in which it is included in the Notice of Meeting and Explanatory Memorandum.

Appendix B Sources of information

In preparing this report, Ernst & Young Transaction Advisory Services had regard to the following sources of information:

- Various presentations prepared by Poseidon in relation to its operations and the Windarra Nickel Project;
- Poseidon shareholder information at various dates, as provided by the Company's share registry and share register analysis provided by Thomson Reuters;
- various schedules of all Poseidon securities on issue provided by the Company;
- Poseidon's convertible note certificates issued to the Harbinger Blue Line Master Fund and the Harbinger Breakaway Fund relating to the New Notes;
- Harbinger Master Fund and Harbinger Special Situations Fund convertible note amendment deeds and subsequent termination deeds relating to the Existing Notes;
- Discussions with Poseidon management;
- Various public disclosure documents lodged by Poseidon with the ASX, including Poseidon's annual reports for the years ended 30 June 1009 and 2010 and public announcement in relation to the issue of the Convertible Notes to Harbinger;
- Information from Poseidon' website, http://www.poseidon-nickel.com.au/;
- ASIC Regulatory Guides;
- Bloomberg;
- Capital IQ;
- Reuters;
- Thompson Research;
- DatAnalysis;
- Various broker reports from late 2010 to January 2011 used as a source of nickel price forecasts;
- The Corporations Act;
- Independent Expert's Report prepared by Ernst & Young Transaction Advisory Services to Poseidon Shareholders dated 6 October 2008, in relation to Poseidon' proposed issue of the Existing Notes to Harbinger; and
- Other publicly available information.

Appendix C Glossary

Abbreviation	Full Title / Description
2008 AGM	Poseidon's Annual General Meeting held in November 2008
A$	Australian dollar
ASIC	The Australian Securities & Investments Commission
Broker Shares	Shares issued to the individual who assisted with the negotiation of the Convertible Notes with Harbinger
Dilution Factor	The issue of other securities at prices below the conversion price or any dividend payments made within in the 180 days following the date of the Note Certificates
Ernst & Young Transaction Advisory Services" or "we," or "us" or "our"	Ernst & Young Transaction Advisory Services Limited
FSG	Financial Services Guide
GFC	The global financial crisis
Harbinger	Harbinger Capital Partners LLC
Harbinger Blue Line Master Fund	The Credit Distressed Blue Line Master Fund Ltd
Harbinger Breakaway Fund	The Global Opportunities Breakaway Ltd
Harbinger Master Fund	The Harbinger Capital Partners Master Fund I
Harbinger Special Situations Fund	The Harbinger Capital Partners Special Situations Fund
JORC Code	Code for Reporting of Mineral Resources and Ore Reserves as prescribed by the Australasian Joint Ore Reserves Committee
m	Million
Non-Associated Shareholders	Those Poseidon shareholders not associated with Harbinger
Poseidon	Poseidon Nickel Limited
Report	Independent Expert's Report
RG 111	ASIC Regulatory Guide 111: Content of expert reports
t	Tonne
/t	Per tonne
the Act	The Corporations Act
the ACT	The Australian Children's Trust
the Company	Poseidon Nickel Limited
the Existing Notes	The US$50 million convertible note facility with Harbinger, agreed to in June 2008
the Existing Note Shares	The shares issued on the conversion of the Existing Notes issued under Tranche 1
the Meeting	General meeting of the Company to be held on or about 4 March 2011
the New Notes	The new US$20 million convertible note facility

the Non-Associated Shareholders	Shareholders of Poseidon are those not associated with Harbinger
the Note Certificates	The Convertible Note Certificates entered into for the New Notes, dated 22 December 2010
the New Note Shares	The issue by Poseidon of fully paid ordinary shares to Harbinger
Tranche 1	The first US$15 million tranche of the Existing Notes
Tranche 2	The second US$35 million tranche of the Existing Notes
US$	United States dollars
VWAP	Volume weighted average price

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THIS FINANCIAL SERVICES GUIDE FORMS PART OF THE INDEPENDENT EXPERT'S REPORT

21 January 2011

PART 2 - FINANCIAL SERVICES GUIDE

1. Ernst & Young Transaction Advisory Services

Ernst & Young Transaction Advisory Services Limited ("Ernst & Young Transaction Advisory Services" or "we," or "us" or "our") has been engaged to provide general financial product advice in the form of an Independent Expert's Report ("Report") in connection with a financial product of another person. The Report is set out in Part 1.

2. Financial Services Guide

This Financial Services Guide ("FSG") provides important information to help retail clients make a decision as to their use of the general financial product advice in a Report, information about us, the financial services we offer, our dispute resolution process and how we are remunerated.

3. Financial services we offer

We hold an Australian Financial Services Licence which authorises us to provide the following services:

► Financial product advice in relation to securities, derivatives, general insurance, life insurance, managed investments, superannuation, and government debentures, stocks and bonds; and

► Arranging to deal in securities.

4. General financial product advice

In our Report we provide general financial product advice. The advice in a Report does not take into account your personal objectives, financial situation or needs.

You should consider the appropriateness of a Report having regard to your own objectives, financial situation and needs before you act on the advice in a Report. Where the advice relates to the acquisition or possible acquisition of a financial product, you should also obtain an offer document relating to the financial product and consider that document before making any decision about whether to acquire the financial product.

We have been engaged to issue a Report in connection with a financial product of another person. Our Report will include a description of the circumstances of our engagement and identify the person who has engaged us. Although you have not engaged us directly, a copy of the Report will be provided to you as a retail client because of your connection to the matters on which we have been engaged to report.

5. Remuneration for our services

We charge fees for providing Reports. These fees have been agreed with, and will be paid by, the person who engaged us to provide a Report. Our fees for Reports are based on a time cost or fixed fee basis. Our directors and employees providing financial services receive an annual salary, a performance bonus or profit share depending on their level of seniority.

Ernst & Young Transaction Advisory Services is ultimately owned by Ernst & Young, which is a professional advisory and accounting practice. Ernst & Young may provide professional services, including audit, tax and financial advisory services, to the person who engaged us and receive fees for those services.

Except for the fees and benefits referred to above, Ernst & Young Transaction Advisory Services, including any of its directors, employees or associated entities should not receive any fees or other benefits, directly or indirectly, for or in connection with the provision of a Report.

6. Associations with product issuers

Ernst & Young Transaction Advisory Services and any of its associated entities may at any time provide professional services to financial product issuers in the ordinary course of business.

7. Responsibility

The liability of Ernst & Young Transaction Advisory Services, if any, is limited to the contents of this Financial Services Guide and the Report.

8. Complaints process

As the holder of an Australian Financial Services Licence, we are required to have a system for handling complaints from persons to whom we provide financial services. All complaints must be in writing and addressed to the AFS Compliance Manager or Chief Complaints Officer and sent to the address below. We will make every effort to resolve a complaint within 30 days of receiving the complaint. If the complaint has not been satisfactorily dealt with, the complaint can be referred to the Financial Ombudsman Service Limited.

9. Compensation Arrangements

The Company and its related entities hold Professional Indemnity insurance for the purpose of compensation should this become relevant. Representatives who have left the Company's employment are covered by our insurances in respect of events occurring during their employment. These arrangements and the level of cover held by the Company satisfy the requirements of Section 912B of the Corporations Act 2001.

Contacting Ernst & Young Transaction Advisory Services	**Contacting the Independent Dispute Resolution Scheme:**
AFS Compliance Manager Ernst & Young 680 George Street Sydney NSW 2000 Telephone: (02) 9248 5555	Financial Ombudsman Service Limited PO Box 3 Melbourne VIC 3001 Telephone: 1300 78 08 08

This Financial Services Guide has been issued in accordance with ASIC Class Order CO 04/1572.