

Condensed Interim Financial Statements

**Quest Rare Minerals Ltd.**

(An Exploration & Development Stage Corporation)

For the Quarter ended January 31, 2016

(Unaudited)

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**NOTICE TO READER**

Management has compiled the unaudited condensed interim financial statements of Quest Rare Minerals Ltd. as at January 31, 2016 and for the three month period then ended. These condensed interim financial statements have not been audited or reviewed by the Corporation's independent auditors.

**Quest Rare Minerals Ltd.**

**STATEMENTS  
OF FINANCIAL POSITION  
(UNAUDITED)**

	<b>January 31, 2016</b>	<b>October 31, 2015</b>
	<u>\$</u>	<u>\$</u>
<b>ASSETS</b>		
<b>Current assets</b>		
Cash <i>[notes 1 and 12]</i>	142,863	208,925
Investments <i>[note 12]</i>	800	650
Prepaid expenses and deposits	235,499	294,187
Commodity taxes and other receivables	94,338	189,971
Tax credits receivable	1,031,107	685,320
	<u>1,504,607</u>	<u>1,379,053</u>
<b>Non-current assets</b>		
Tax credits receivable	1,367,000	1,812,500
Other non-current assets <i>[note 6]</i>	511,371	441,655
<b>Total assets</b>	<u>3,382,978</u>	<u>3,633,208</u>
<b>EQUITY AND LIABILITIES</b>		
<b>Current liabilities</b>		
Accounts payable and accrued liabilities <i>[note 11]</i>	2,430,594	1,947,650
Loans payable <i>[note 8]</i>	105,955	—
Convertible debentures <i>[note 9]</i>	2,091,852	—
<b>Total current liabilities</b>	<u>4,628,401</u>	<u>1,947,650</u>
<b>Non-Current liabilities</b>		
Convertible debentures <i>[note 9]</i>	—	1,987,238
<b>Total non-current liabilities</b>	<u>—</u>	<u>1,987,238</u>
<b>Deficiency</b>		
Share capital <i>[note 10]</i>	81,613,013	81,543,188
Warrants <i>[note 10]</i>	927,890	927,890
Equity component of convertible debentures <i>[note 9]</i>	232,957	232,957
Contributed surplus <i>[note 10]</i>	21,810,211	21,808,066
Deficit	(105,829,494)	(104,813,781)
<b>Total deficiency</b>	<u>(1,245,423)</u>	<u>(301,680)</u>
<b>Total equity and liabilities</b>	<u>3,382,978</u>	<u>3,633,208</u>
Going concern uncertainty <i>[note 1]</i>		

*See accompanying notes*

**Quest Rare Minerals Ltd.**

**STATEMENTS OF  
COMPREHENSIVE LOSS  
(UNAUDITED)**

	<b>Quarter ended</b>	
	<b>January 31</b>	
	<b>2016</b>	<b>2015</b>
		<b>Restated - see Note 3</b>
	<b>\$</b>	<b>\$</b>
<b>REVENUES</b>	<b>—</b>	<b>—</b>
<b>EXPENSES</b>		
Exploration and evaluation expenditures <i>[note 5]</i>	<b>461,356</b>	835,974
Administration expenses <i>[notes 7 and 11]</i>	<b>256,394</b>	352,939
Investor relations <i>[notes 7 and 11]</i>	<b>36,643</b>	171,110
Professional fees <i>[note 11]</i>	<b>112,262</b>	88,457
	<b>866,655</b>	1,448,480
<b>Operating loss</b>	<b>(866,655)</b>	(1,448,480)
Finance income	<b>470</b>	5,400
Finance expense <i>[notes 7, 8 and 9]</i>	<b>(149,678)</b>	(27,321)
Unrealized loss on investments held for trading <i>[note 12]</i>	<b>150</b>	(300)
	<b>(149,058)</b>	(22,221)
<b>Net loss and comprehensive loss for the quarter</b>	<b>(1,015,713)</b>	(1,470,701)
<b>Net loss per share</b>		
Basic and fully diluted	<b>(0.01)</b>	(0.02)
<b>Weighted average number of outstanding shares</b>		
Basic and fully diluted	<b>85,064,500</b>	78,829,196

Going concern uncertainty *[note 1]*

*See accompanying notes*

Quest Rare Minerals Ltd.

**STATEMENTS OF CHANGES IN EQUITY  
(UNAUDITED)**

	Share capital		Warrants		Equity Component of Convertible Debentures	Contributed surplus	Deficit (Restated - see Note 3)	Total
	#	\$	#	\$	\$	\$	\$	\$
<b>Balance – November 1, 2014</b>	78,829,196	80,935,251	11,531,485	601,543	—	21,530,007	(97,501,420)	5,565,381
Issuance of shares and warrants <i>[note 10]</i>	—	—	(506,000)	(72,286)	—	72,286	—	—
Issuance of shares for exploration and evaluation expenditures <i>[note 10]</i>	—	—	—	—	—	109,514	—	109,514
Net loss and comprehensive loss for the quarter	—	—	—	—	—	—	(1,470,701)	(1,470,701)
<b>Balance – January 31, 2015</b>	<b>78,829,196</b>	<b>80,935,251</b>	<b>11,025,485</b>	<b>529,257</b>	<b>—</b>	<b>21,711,807</b>	<b>(98,972,121)</b>	<b>4,204,194</b>
<b>Balance – November 1, 2015</b>	<b>85,034,011</b>	<b>81,543,188</b>	<b>18,105,300</b>	<b>927,890</b>	<b>232,957</b>	<b>21,808,066</b>	<b>(104,813,781)</b>	<b>(301,680)</b>
Settlement of RSUs	<b>255,000</b>	<b>69,825</b>	—	—	—	(69,825)	—	—
Stock-based compensation <i>[note 10]</i>	—	—	—	—	—	<b>71,970</b>	—	<b>71,970</b>
Net loss and comprehensive loss for the quarter	—	—	—	—	—	—	(1,015,713)	(1,015,713)
<b>Balance – January 31, 2016</b>	<b>85,289,011</b>	<b>81,613,013</b>	<b>18,105,300</b>	<b>927,890</b>	<b>232,957</b>	<b>21,810,211</b>	<b>(105,829,494)</b>	<b>(1,245,423)</b>

Going concern uncertainty *[note 1]*

See accompanying notes

**Quest Rare Minerals Ltd.****STATEMENTS OF CASH FLOWS  
(UNAUDITED)**

Quarter ended January 31,

	2015	2014
	\$	Restated - see Note 3 \$
<b>OPERATING ACTIVITIES</b>		
Net loss	(1,015,713)	(1,470,701)
Items not impacting cash:		
Accretion of convertible debentures <i>[notes 7 and 9]</i>	104,614	—
Interest payable <i>[notes 7 and 8]</i>	45,064	—
Unrealized (gain) loss on investments held for trading	(150)	300
Stock-based compensation <i>[note 10]</i>	71,970	109,514
	<u>(794,215)</u>	<u>(1,360,887)</u>
Net change in non-cash working capital items	637,580	311,388
<b>Net cash flows from operating activities</b>	<u>(156,635)</u>	<u>(1,049,499)</u>
<b>INVESTING ACTIVITIES</b>		
Increase in non-current assets <i>[note 6]</i>	(10,715)	(1,486)
<b>Net cash flows from investing activities</b>	<u>(10,715)</u>	<u>(1,486)</u>
<b>FINANCING ACTIVITIES</b>		
Decrease in loan facility	—	(169,932)
Increase in loans payable <i>[note 8]</i>	105,000	—
Share issue costs <i>[note 9]</i>	(3,712)	—
Interest paid	—	(27,281)
<b>Net cash flows from financing activities</b>	<u>101,288</u>	<u>(197,213)</u>
<b>Net decrease in cash</b>	(66,062)	(1,248,198)
Cash, beginning of period	208,925	1,281,706
<b>Cash, end of period</b>	<u>142,863</u>	<u>33,508</u>

Going concern uncertainty *[note 1]**See accompanying notes*

## **Quest Rare Minerals Ltd.**

### **NOTES TO CONDENSED INTERIM FINANCIAL STATEMENTS (UNAUDITED)**

January 31, 2016

#### **1. NATURE OF OPERATIONS AND GOING CONCERN UNCERTAINTY**

Quest Rare Minerals Ltd. [“Quest” or the “Corporation”] was incorporated under the *Canada Business Corporations Act* on June 6, 2007. The registered office of Quest is located at 1155 University Street, Suite 906, Montreal, Québec, H3B 3A7. Quest is a publicly-listed Corporation and its shares are listed on the Toronto Stock Exchange under the symbol “QRM”. On January 29, 2015, Quest advised the NYSE MKT that it wished to voluntarily delist from the NYSE MKT. The voluntary delisting from the NYSE MKT became effective on February 18, 2015.

Quest is a Canadian-based exploration and evaluation company which is focused on the development of its Strange Lake rare earth deposit in northeastern Québec as described in note 5. The development of this Strange Lake deposit is now the key focus of the Corporation.

#### **Going Concern Uncertainty**

These condensed interim financial statements have been prepared on the basis of accounting principles applicable to a going concern, which assume that the Corporation will continue in operation for the foreseeable future and will be able to realize its assets and discharge its obligations in the normal course of operations. In assessing whether the going concern assumption is appropriate, management takes into account all available information about the future, which is at least, but not limited to twelve months from the end of the reporting period. The use of these principles may not be appropriate.

To date, the Corporation has not earned significant revenue and is considered to be in the exploration and development stage. Exploration and evaluation expenditures comprise a significant portion of the Corporation’s activities. Mineral exploration and development is highly speculative and involves inherent risks.

The Corporation’s current committed cash resources are insufficient to cover expected expenditures for the next 12 months and its planned Pre-feasibility study on Strange Lake. The Corporation’s ability to continue as a going concern is dependent on being able to obtain the necessary financing to satisfy its liabilities as they become due. There can be no assurance that management will be successful in securing adequate financing. In addition, while the Corporation’s Preliminary Economic Assessment (“PEA”) and future development activities in relation to its Strange Lake project look promising, there can be no assurance that the results of its planned Pre-feasibility study will confirm the existence of economically viable quantities of ore or that the project will ultimately go into production.

**Quest Rare Minerals Ltd.**

**NOTES TO CONDENSED INTERIM FINANCIAL STATEMENTS  
(UNAUDITED)**

January 31, 2016

**1. NATURE OF OPERATIONS AND GOING CONCERN UNCERTAINTY  
[Cont'd]**

The Corporation reported a net loss and total comprehensive loss in the quarter ended January 31, 2016 and the year ended October 31, 2015 of \$1,015,713 and \$7,312,361, respectively. As at January 31, 2016, the Corporation's current liabilities exceeded its current assets by \$3,123,794 [October 31, 2015 – \$568,597]. These recurring losses and the need for continued financing to further successful exploration and development activities indicate the existence of a material uncertainty that may cast significant doubt as to the Corporation's ability to continue as a going concern.

These condensed interim financial statements do not give effect to any adjustments to the carrying values and classifications of assets and liabilities that might be necessary, if the Corporation is unable to continue as a going concern. Such adjustments could be material.

**2. BASIS OF PREPARATION**

**Statement of Compliance**

The condensed interim financial statements of the Corporation for the quarter ended January 31, 2016 have been prepared in accordance with International Accounting Standard 34, Interim Financial Reporting. The same accounting policies and methods of computation were followed in the preparation of these condensed interim financial statements as were followed in the preparation of the financial statements for the year ended October 31, 2015. These condensed interim financial statements do not include all of the information required for full annual financial statements and should be read in conjunction with the financial statements for the year ended October 31, 2015 which have been prepared in accordance with IFRS.

The Board of Directors approved these condensed interim financial statements effective March 8, 2016.

## Quest Rare Minerals Ltd.

### NOTES TO CONDENSED INTERIM FINANCIAL STATEMENTS (UNAUDITED)

January 31, 2016

#### 3. CHANGE IN ACCOUNTING POLICY

During the year ended October 31, 2015, the Corporation voluntarily changed its policy for accounting for exploration and evaluation expenditures considered under IFRS 6 - *Exploration for and Evaluation of Mineral Resources*. The Corporation previously elected to capitalize all costs relating to the exploration and evaluation on its properties, net of tax credits. During the year ended October 31, 2015, the Corporation changed its policy under IFRS 6 to expense all costs relating to the exploration and evaluation on its properties (including the cost of acquisition of exploration rights), net of tax credits, as it concluded that this policy provided more useful information to the users.

The Corporation has applied the change in accounting policy on a retrospective basis and has therefore restated its 2015 comparatives as follows:

#### Statement of Comprehensive Loss

For the quarter ended January 31, 2015	Note	As previously Reported \$	Effect of Change \$	Restated \$
<b>Revenues</b>		—	—	—
<b>Expenses</b>				
Impairment of exploration and evaluation assets	(i)	12,670	(12,670)	—
Exploration and evaluation expenditures	(ii)	—	835,974	835,974
Administration expenses		352,939	—	352,939
Investor relations		171,110	—	171,110
Professional fees		88,457	—	88,457
		<b>625,176</b>	<b>823,304</b>	<b>1,448,480</b>
<b>Operating loss</b>		<b>(625,176)</b>	<b>(823,304)</b>	<b>(1,448,480)</b>
Finance income		5,400	—	5,400
Finance expense		(27,321)	—	(27,321)
Unrealized loss on investments held for trading		(300)	—	(300)
		<b>(22,221)</b>	<b>—</b>	<b>(22,221)</b>
<b>Net loss and comprehensive loss for the year</b>		<b>(647,397)</b>	<b>—</b>	<b>(1,470,701)</b>
<b>Net loss per share - basic and fully diluted</b>		<b>(0.01)</b>	<b>—</b>	<b>(0.02)</b>

(i) Impairment of exploration and evaluation expenditures is reversed with a corresponding offset to deficit.

(ii) Expensing of exploration and evaluation expenditures as incurred, net of tax credits, with a corresponding offset to deficit.



**Quest Rare Minerals Ltd.**

**NOTES TO CONDENSED INTERIM FINANCIAL STATEMENTS  
(UNAUDITED)**

January 31, 2016

**3. CHANGE IN ACCOUNTING POLICY [Cont'd]**

**Statement of Cash Flows**

For the quarter ended January 31, 2015	Note	As previously Reported \$	Effect of Change \$	Restated \$
<b>OPERATING ACTIVITIES</b>				
<b>Net loss</b>		(647,397)	(823,304)	<b>(1,470,701)</b>
<b>Items not impacting cash:</b>				
Impairment of exploration and evaluation assets	(i)	12,670	(12,670)	—
Unrealized loss on investments held for trading		300	—	<b>300</b>
Stock-based compensation	(ii)	100,066	9,448	<b>109,514</b>
		(534,361)	(826,526)	<b>(1,360,887)</b>
Net change in non-cash working capital items	(iii)	205,555	105,833	<b>311,388</b>
<b>Net cash flows used in operating activities</b>		<b>(328,806)</b>	<b>(720,693)</b>	<b>(1,049,499)</b>
<b>INVESTING ACTIVITIES</b>				
Investment in exploration and evaluation assets	(iii)	(720,693)	720,693	—
Increase in non-current assets		(1,486)	—	<b>(1,486)</b>
<b>Net cash flows used in investing activities</b>		<b>(722,179)</b>	—	<b>(1,486)</b>
<b>FINANCING ACTIVITIES</b>				
Decrease in loan facility		(169,932)	—	<b>(169,932)</b>
Interest paid		(27,281)	—	<b>(27,281)</b>
<b>Net cash flows used in financing activities</b>		<b>(197,213)</b>	—	<b>(197,213)</b>
<b>Net decrease in cash</b>		<b>(1,248,198)</b>	—	<b>(1,248,198)</b>
Cash, beginning of quarter		1,281,706	—	<b>1,281,706</b>
<b>Cash, end of quarter</b>		<b>33,508</b>	—	<b>33,508</b>

- (i) Impairment of exploration and evaluation expenditures recognized in accounting period is reversed.
- (ii) Expensing of share-based payments qualifying as exploration and evaluation expenditures which were capitalized as exploration and evaluation assets in the statements of financial position under the previous accounting policy.
- (iii) As a result of the change in accounting policy, changes in accounts payable and accrued liabilities and exploration and evaluation expenditures are no longer investing activities and are now considered operating activities.

## Quest Rare Minerals Ltd.

### NOTES TO CONDENSED INTERIM FINANCIAL STATEMENTS (UNAUDITED)

January 31, 2016

#### 3. CHANGE IN ACCOUNTING POLICY [Cont'd]

##### Standards issued but not yet effective

The following pronouncements are issued but not yet effective for the quarter ended January 31, 2016:

##### a) IFRS 16 Leases

IFRS 16 Leases In January 2016, the IASB issued IFRS 16, Leases, to set out the principles for the recognition, measurement, presentation and disclosure of leases for both parties to a lease contract. The standard requires lessees to recognize asset and liabilities for most leases. The standard supersedes IAS 17, Leases and other lease related interpretations. The standard will be effective on November 1, 2019 for the Corporation with earlier application permitted only if IFRS 15 Revenue from Contracts with Customers is also applied. The Corporation is currently assessing the impact of IFRS 16.

#### 4. INCOME TAXES

A reconciliation of income tax charge applicable to accounting loss before income tax at the weighted average statutory income tax rate to income tax charge at the Corporation's effective income tax rate for the quarters ended January 31 is as follows:

	2016 \$	2015 \$
Loss before income tax	<u>(1,015,713)</u>	<u>(1,470,701)</u>
Income tax recovery at the combined Federal and Provincial tax rate 26.87% [2015 – 26.98%]	(272,962)	(396,790)
Stock-based compensation	19,341	29,547
Other non-deductible expenses or non-taxable revenues	(13,902)	1,522
Other	—	(1,861)
Changes in valuation allowance	267,523	367,582
Tax recovery at an effective income tax rate	<u>—</u>	<u>—</u>

## Quest Rare Minerals Ltd.

### NOTES TO CONDENSED INTERIM FINANCIAL STATEMENTS (UNAUDITED)

January 31, 2016

#### 4. INCOME TAXES [Cont'd]

The deferred tax assets and liabilities of the Corporation consist of the following:

	January 31, 2016 \$	October 31, 2015 \$
<b>Future income tax assets</b>		
Exploration and evaluation expenditures	15,445,285	15,308,139
Non-capital loss carry-forwards	5,950,696	5,823,045
Share issue costs	239,611	253,953
Investments	5,670	5,691
	<b>21,641,262</b>	21,390,828
<b>Future income tax liabilities</b>		
Convertible debentures	(69,660)	(86,749)
Net future income tax assets	21,571,602	21,304,079
Unrecognized deferred tax assets	(21,571,602)	(21,304,079)
<b>Net future income tax liabilities</b>	—	—

#### 5. EXPLORATION AND EVALUATION EXPENDITURES

The following is a breakdown by project of the exploration and evaluation expenditures incurred, net of tax credits, for the quarter ended January 31:

	2016 \$	2015 \$
Strange Lake (Québec)	458,056	813,856
Misery Lake (Québec)	—	11,148
Other projects (Canada)	—	1,522
Total exploration and evaluation expenditures before stock-based compensation	458,056	826,526
Stock-based compensation [note 10[ff]]	3,300	9,448
<b>Total expenditures incurred</b>	<b>461,356</b>	835,974

## Quest Rare Minerals Ltd.

### NOTES TO CONDENSED INTERIM FINANCIAL STATEMENTS (UNAUDITED)

January 31, 2016

#### 5. EXPLORATION AND EVALUATION EXPENDITURES [Cont'd]

During the three-month period ended January 31, 2016, significant changes occurred in the following properties:

##### Strange Lake Property, (Québec)

The Corporation's 100%-owned Strange Lake property is located adjacent to Lac Brisson situated within the George River belt located 220 km northeast of Schefferville, Québec and 125 km west of the Voisey's Bay Nickel-Copper-Cobalt Mine, and covers an area of approximately 9,367 hectares. The property is a rare earth mineralized zone and consists of 211 mining claims, all of which are in Québec.

A breakdown of exploration and evaluation expenditures incurred on the Strange Lake project are set out below:

	Quarter Ended January 31, 2016 \$	Quarter Ended January 31, 2015 \$	From Inception \$
Acquisition costs	—	11,064	201,135
Geochemical Surveys	—	—	42,027
Geophysical Surveys	—	—	288,651
Geological Surveys	18,750	7,472	13,002,742
Drilling	9,375	8,054	15,076,292
Prospecting	—	718	264,174
Prefeasibility Studies	105,694	477,667	31,377,313
Feasibility Studies	—	—	5,110,525
Metallurgical Work	—	(5,533)	2,851,112
Environmental & Permitting	118,427	—	2,610,701
Project Management & Support	260,310	246,856	1,586,734
Other	—	79,676	2,425,205
Government Tax Credits	(54,500)	(12,118)	(14,147,988)
<b>Total expenditures incurred</b>	<b>458,056</b>	<b>813,856</b>	<b>60,688,623</b>

## Quest Rare Minerals Ltd.

### NOTES TO CONDENSED INTERIM FINANCIAL STATEMENTS (UNAUDITED)

January 31, 2016

#### 6. OTHER NON-CURRENT ASSETS

A breakdown of other non-current assets as at January 31, 2016 and October 31, 2015 are as follows:

	January 31, 2016	October 31, 2015
	\$	\$
SPIP Agreement – lease payments	333,936	296,364
Fraenkel Agreement – option payments	177,435	145,291
<b>Total</b>	<b>511,371</b>	<b>441,655</b>

#### 7. EXPENSES BY NATURE

The following is a breakdown of the nature of expenses included in investor relations and administration expenses for the quarters ended January 31:

	2016	2015
	\$	\$
<b>Investor relations:</b>		
Advertising	3,902	2,702
Conferences	—	10,835
Consulting services	—	20,883
Dues and subscriptions	255	1,238
Investor relations fees	4,575	48,628
Listing and stock transfer fees	26,920	67,392
Printing and filing	564	1,004
Salaries and other employee benefits	—	483
Travel related costs	427	17,360
Other	—	585
<b>Total</b>	<b>36,643</b>	<b>171,110</b>

## Quest Rare Minerals Ltd.

### NOTES TO CONDENSED INTERIM FINANCIAL STATEMENTS (UNAUDITED)

January 31, 2016

#### 7. EXPENSES BY NATURE [Cont'd]

	2016	2015
	\$	\$
<b>Administration expenses:</b>		
Office Expenses:		
Salaries and other employee benefits	48,748	125,191
Directors' fees	61,250	27,524
Directors' and Officers' Insurance	26,226	26,090
Rent	14,045	47,436
Travel costs	12,636	7,286
Telephone and internet	4,206	5,233
IT Services	6,984	6,725
Repairs and maintenance	—	99
Other office expenses	6,159	5,303
Bank charges	1,612	1,935
Foreign exchange (gain) loss	(321)	51
Stock-based compensation [note 10(f)]	68,670	100,066
Other	6,179	—
<b>Total</b>	<b>256,394</b>	<b>352,939</b>
	2016	2015
	\$	\$
<b>Finance expense:</b>		
Interest on loan facility	—	27,280
Interest on loans payable [note 8]	955	—
Interest on convertible debentures [note 9]	44,109	—
Accretion of convertible debentures [note 9]	104,614	—
Other	—	41
<b>Total</b>	<b>149,678</b>	<b>27,321</b>

As at January 31, 2016 the expenditures incurred on separation and termination benefits and onerous lease that were unpaid and included in accounts payable and accrued liabilities amounted to \$153,828 and \$98,243 respectively [January 31, 2015 – nil and nil].

## Quest Rare Minerals Ltd.

### NOTES TO CONDENSED INTERIM FINANCIAL STATEMENTS (UNAUDITED)

January 31, 2016

#### 8. LOANS PAYABLE

On December 15, 2015, the Corporation entered into loan agreements with a number Directors, Officers or their related parties and others (collectively “the Lenders”) under which the Lenders agreed to loan to the Corporation a total of \$105,000 for the purposes of providing working capital. The loaned amounts are repayable at the earlier of receipt of certain commodity taxes receivables, future private placements, future government grants, or one year from the date of the loan and bear interest at a rate of 8.5% per annum, compounded monthly. The Corporation provided security to each Lender by way of a hypothec, in the amount 120% of the principal loan amount, over all input tax credits or input tax refunds, due from the Government of Québec, present or future, including those related to its quarter ended January 31, 2016.

During the quarter ended January 31, 2016, interest expense pursuant to these loans amounted to \$955 [January 31, 2015 – nil] [note 7].

#### 9. CONVERTIBLE DEBENTURES

A breakdown of convertible debentures as at January 31, 2016 and October 31, 2015 are as follows:

	Host Debt Component \$	Common Share Purchase Warrants \$	Equity Component of Convertible debentures feature \$	Total \$
<b>Balance, November 1, 2015</b>	—	—	—	—
Debentures issued during the year	2,025,932	201,379	272,689	2,500,000
Issue costs	(295,192)	(29,343)	(39,732)	(364,267)
Accretion	256,498	—	—	256,498
<b>Balance, October 31, 2015</b>	<b>1,987,238</b>	<b>172,036</b>	<b>232,957</b>	<b>2,392,231</b>
Accretion (Note 7)	104,614	—	—	104,614
<b>Balance, January 31, 2016</b>	<b>2,091,852</b>	<b>172,036</b>	<b>232,957</b>	<b>2,496,845</b>

## Quest Rare Minerals Ltd.

### NOTES TO CONDENSED INTERIM FINANCIAL STATEMENTS (UNAUDITED)

January 31, 2016

#### 10. SHARE CAPITAL

##### Authorized

###### Common

An unlimited number of no par value shares.

###### Preferred

An unlimited number of shares issuable in series, non-voting, conditions to be determined by the Board of Directors.

##### [a] Common shares

##### Issuances during the quarter ended January 31, 2016

[i] On January 20, 2016, the Corporation issued 255,000 common shares in relation to the exercise of 255,000 RSUs [note 10 [e]].

##### Issuances during the quarter ended January 31, 2015

[ii] There were no issuances of common shares during the quarter ended January 31, 2015.

##### [b] Stock options

The outstanding options as at January 31, 2016 and October 31, 2015 and the respective changes during the quarter and the year then ended are summarized as follows:

	Quarter ended January 31, 2016		Year ended October 31, 2015	
	Number of options #	Weighted average exercise price \$	Number of options #	Weighted average exercise price \$
Outstanding, beginning of period	5,301,000	2.42	4,167,499	3.31
Granted	1,920,000	0.07	1,736,000	0.18
Exercised	—	—	—	—
Expired/cancelled	—	—	(602,499)	(2.14)
Outstanding, end of period	7,221,000	1.79	5,301,000	2.42



**Quest Rare Minerals Ltd.**

**NOTES TO CONDENSED INTERIM FINANCIAL STATEMENTS  
(UNAUDITED)**

January 31, 2016

**10. SHARE CAPITAL [Cont'd]**

The following options are outstanding and exercisable as at January 31, 2016.

<b>Options outstanding</b>					
<b>Range of exercise price</b>	<b>Number outstanding</b>	<b>Weighted average remaining contractual life</b>	<b>Weighted average exercise price</b>	<b>Number exercisable</b>	<b>Weighted average exercise price</b>
\$	#	(in years)	\$	#	\$
0.00 to 0.749	4,181,000	4.30	0.16	3,413,998	0.18
0.75 to 1.499	0	0	0	0	0
1.50 to 2.249	205,000	4.54	2.11	205,000	2.11
2.25 to 2.999	695,000	4.86	2.71	695,000	2.71
3.75 to 4.499	1,390,000	4.76	4.44	1,390,000	4.44
4.50 to 5.249	500,000	4.72	4.69	500,000	4.69
5.25 to 5.999	250,000	4.94	5.72	250,000	5.72
<b>0.00 to 5.999</b>	<b>7,221,000</b>	<b>4.50</b>	<b>1.79</b>	<b>6,453,998</b>	<b>1.99</b>

The fair value of stock options granted during the quarter ended January 31, 2016 and 2015 were estimated at their respective grant dates using the Black-Scholes option pricing model, using the following weighted average assumptions.

	<b>2016</b>	2015
Risk-free interest rate	<b>0.72%</b>	1.32%
Forfeiture rate	<b>6.44%</b>	5.46%
Expected volatility	<b>90%</b>	82%
Dividend yield	<b>Nil</b>	Nil
Expected life [in years]	<b>5</b>	5
<b>Fair value at grant date</b>	<b>\$0.05</b>	\$0.09

## Quest Rare Minerals Ltd.

### NOTES TO CONDENSED INTERIM FINANCIAL STATEMENTS (UNAUDITED)

January 31, 2016

#### 10. SHARE CAPITAL [Cont'd]

##### [c] Broker Compensation Units

As at January 31, 2016 and October 31, 2015, the Corporation had outstanding 613,008 broker compensation units, entitling holders to purchase units of the Corporation at a price of \$0.27 per unit at any time until July 17, 2016. Each unit entitles its holder to one common share of the Corporation and one common share purchase warrant. Each common share purchase warrant would entitle its holder to purchase one additional common share of the Corporation at a price of \$0.40 per share until July 17, 2017.

##### [d] Warrants

The outstanding warrants as at January 31, 2016 and October 31, 2015 and the respective changes during the quarter and year then ended are summarized as follows:

	Quarter ended January 31, 2016		Year ended October 31, 2015	
	Number of warrants #	Weighted average exercise price \$	Number of warrants #	Weighted average exercise price \$
Outstanding balance, beginning of year	18,105,300	0.30	11,531,485	0.42
Granted	—	—	7,079,815	0.15
Exercised	—	—	—	—
Expired	—	—	(506,000)	0.80
Outstanding balance, end of year	18,105,300	0.30	18,105,300	0.30

##### [e] Restricted and Deferred Share Unit Plans

On March 9, 2012, the Board of Directors adopted the Restricted Share Unit ["RSU"] Plan and the Deferred Share Unit ["DSU"] Plan to complement the 2012 Stock Option Plan. Under these plans, RSUs may be granted to executives and key employees, and DSUs may be granted to directors and key executives, as part of their long-term compensation packages.

RSUs vest over the period of a "Performance Cycle", defined as the period from the date of grant of the unit to the end of the Corporation's second fiscal year after the fiscal year in which the unit was granted [a period of up to three years]. DSUs vest immediately, and DSU awards can be settled only when the holder ceases to be an employee of the Corporation.

## Quest Rare Minerals Ltd.

### NOTES TO CONDENSED INTERIM FINANCIAL STATEMENTS (UNAUDITED)

January 31, 2016

#### 10. SHARE CAPITAL [Cont'd]

RSUs and DSUs entitle the holder to receive a payout, at the Corporation's discretion in either: [i] common shares, on the basis of one common share per RSU or DSU vested in the holder's account or [ii] cash, based on the Corporation's share price at the relevant time. The value of the cash payout, if elected by the Corporation, is determined by multiplying the RSUs and DSUs vested at the payout date by the average closing price of the Corporation's shares over the last ten days prior to the payout date. DSU awards can be settled only when the holder ceases to be an employee of the Corporation.

Each of the RSU and DSU Plans provides that a maximum of 750,000 common shares can be issued thereunder. All RSUs and DSUs granted are classified as equity instruments in accordance with IFRS as their terms provide for settlement in either equity or cash at the sole discretion of the Corporation.

The outstanding RSUs and DSUs as at January 31, 2016 and October 31, 2015 and the respective changes during the quarter and the year then ended are summarized as follows:

	Restricted Share Units			
	Number of units #	Fair value at grant date \$	Number of units #	Fair value at grant date \$
	Quarter ended January 31, 2016		Year ended October 31, 2015	
Outstanding, beginning of year	530,000	0.21	110,000	0.48
Granted	—	—	430,000	0.14
Exercised	(255,000)	0.24	—	—
Expired/cancelled	—	—	(10,000)	0.48
Outstanding, end of period	275,000	0.18	530,000	0.21
Units exercisable	—	—	255,000	0.24

## Quest Rare Minerals Ltd.

### NOTES TO CONDENSED INTERIM FINANCIAL STATEMENTS (UNAUDITED)

January 31, 2016

#### 10. SHARE CAPITAL [Cont'd]

	Deferred Share Units			
	Number of units #	Fair value at grant date \$	Number of units #	Fair value at grant date \$
	Quarter ended January 31, 2015		Year ended October 31, 2014	
Outstanding, beginning of year	620,000	0.48	325,000	1.06
Granted	—	—	420,000	0.16
Exercised	—	—	(125,000)	(0.91)
Expired/cancelled	—	—	—	—
Outstanding, end of period	620,000	0.48	620,000	0.48
Units exercisable	140,000	0.48	140,000	0.48

#### [f] Stock-based compensation

For the quarter ended January 31, 2016, the amount of stock-based compensation expenditures from all sources, included in administration expenses and exploration and evaluation expenditures in the statements of comprehensive loss, were \$68,670 and \$3,300 respectively [2015 – \$100,066 and \$9,448].

#### 11. RELATED PARTY TRANSACTIONS

In addition to the related party transaction disclosed in note 8, the following related party transactions occurred in the normal course of operations.

- [a] The Corporation retains the services of certain directors of the Corporation to carry out professional services. For the quarter ended January 31, 2016, the total amount charged for professional services by directors of the Corporation and recorded in exploration and evaluation assets was nil [2015 – \$10,000].
- [b] During the quarter ended January 31, 2016, the Corporation incurred fees to a law firm in which a director of the Corporation is a partner. In addition, during the quarter ended January 31, 2016, the Corporation incurred fees to a second law firm, to which a Director of the Corporation has a related party association. During the quarter ended January 31, 2016, the total amount for such services provided was \$33,551, all of which was recorded in professional fees [2015 – \$19,515 in professional fees, \$1,328 in prepaid expenses and \$4,411 in exploration and evaluation expenses]. As at January 31, 2016 an amount of \$359,354 [October 31, 2015 – \$288,333] owing to these law firms was included in accounts payable and accrued liabilities in respect of these fees.

## Quest Rare Minerals Ltd.

### NOTES TO CONDENSED INTERIM FINANCIAL STATEMENTS (UNAUDITED)

January 31, 2016

#### 11. RELATED PARTY TRANSACTIONS [Cont'd]

[c] During the quarter ended January 31, 2016, the Corporation incurred fees to a private investment firm of which a director of the Corporation has a related party association. During the quarter ended January 31, 2016, the total amount recorded in professional fees for such services provided was \$34,500 [2015 – nil]. As at January 31, 2016, an amount of \$58,400 [October 31, 2015 – nil] owing to this firm was included in accounts payable and accrued liabilities in respect of these fees.

[d] During the quarter ended January 31, 2016, the Corporation incurred fees to a number of management entities of which certain officers or directors of the Corporation have a related party association. For the quarter ended January 31, 2016, the total amount for such services provided was \$87,516, of which \$12,500 was recorded in directors fees and \$75,017 was recorded in exploration and evaluation expenditures [2015 – \$25,000 and \$278,578 respectively]. As at January 31, 2016, an amount of \$93,608 [October 31, 2015 – \$52,534] owing to these firms was included in accounts payable and accrued liabilities in respect of these fees.

#### [e] Compensation of key management personnel and Board of Directors

Excluding the amounts reported above, during the quarters ended January 31, 2016 and 2015, the Corporation recorded the following compensation for key management personnel and the Board of Directors:

	2016	2015
	\$	\$
Salaries, employee benefits	74,685	225,131
Directors' fees	61,250	26,875
Stock compensation	44,341	96,703
Total compensation paid or accrued to key management personnel and Board of Directors	<u>180,276</u>	<u>348,709</u>

## Quest Rare Minerals Ltd.

### NOTES TO CONDENSED INTERIM FINANCIAL STATEMENTS (UNAUDITED)

January 31, 2016

#### 12. FINANCIAL INSTRUMENTS

##### Principles of risk management

The Corporation's objectives when managing capital are to safeguard its ability to continue its operations as well as its exploration programs. As such, the Corporation relies primarily on the equity markets to fund its activities. In order to carry out planned exploration and to pay for administrative costs, the Corporation will spend its existing working capital and raise additional funds as needed. The Corporation has not used term debt financing and has not paid any dividends. As well, the Corporation does not have any externally-imposed capital requirements, either regulatory or contractual to which it is subject.

The prices of minerals fluctuate widely and are affected by many factors outside of the Corporation's control. The prices of minerals and future expectation of such prices may have a significant impact on the market sentiment for investment in mining and mineral exploration companies. This in turn may impact on the Corporation's ability to raise equity financing for its capital requirements.

The fair value of the convertible debentures is determined using the discounted cash flow method using a discount rate that reflects rates currently available for debt on similar terms, considering the Corporation's credit risk and remaining maturity.

Below is a comparison of the carrying amount of the financial instruments and their respective fair values as at January 31:

Classification	Fair value level	2016		2015		
		Carrying value \$	Fair value \$	Carrying value \$	Fair value \$	
<b>Financial assets</b>						
Investments –						
Canadian stocks	Held-for-trading	I	800	800	650	650
<b>Financial liabilities</b>						
Convertible						
debentures	Other liabilities	I	2,091,852	2,343,870	1,987,238	2,236,171

The Corporation does not enter into financial instrument agreements, including derivative financial instruments, for speculative purposes.

**Quest Rare Minerals Ltd.**

**NOTES TO CONDENSED INTERIM FINANCIAL STATEMENTS  
(UNAUDITED)**

January 31, 2016

**12. FINANCIAL INSTRUMENTS [Cont'd]**

**Credit risk**

Credit risk is the risk of financial loss to the Corporation if a counter-party to a financial instrument fails to meet its contractual obligations; the Corporation's maximum exposure to credit loss is the book value of its financial instruments.

The Corporation is not exposed to any significant credit risk as at January 31, 2016. The Corporation's cash is deposited with a major Canadian chartered bank and is held in highly-liquid investments.

**Liquidity risk**

Liquidity risk is the risk that the Corporation will not be able to meet its financial obligations as they come due. All of the Corporation's financial liabilities are due within one year.

As at January 31, 2016, the Corporation had a total of \$142,863 in cash. The Corporation manages liquidity risk through the management of its capital structure. Accounts payable and accrued liabilities have contractual maturities of 30 – 90 days or less and are subject to normal trade terms, and amounts due to related parties are due on demand.

**Market risk analysis**

Market risk is the risk that the fair value of the future cash flows of a financial instrument will fluctuate because of changes in market prices. The Corporation's primary market exposures are to interest rate risk

**Interest rate risk**

Interest rate risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate due to changes in market interest rates. The Corporation does not carry any significant interest rate exposure on its cash balances.