Consolidated financial statements of

Mandalay Resources Corporation

December 31, 2012 and 2011

Mandalay Resources Corporation
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Independent Auditor's Report

To the Shareholders of Mandalay Resources Corporation

We have audited the accompanying consolidated financial statements of Mandalay Resources Corporation, which comprise the consolidated statements of financial position as at December 31, 2012 and December 31, 2011, and the consolidated statements of income, consolidated statements of comprehensive income, consolidated statements of changes in equity and consolidated statements of cash flows for the years ended December 31, 2012 and December 31, 2011, and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained in our audits is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Mandalay Resources Corporation as at December 31, 2012 and December 31, 2011, and its financial performance and its cash flows for the years ended December 31, 2012 and December 31, 2011 in accordance with International Financial Reporting Standards.

(Signed) Deloitte LLP

Chartered Accountants
February 20, 2013
Vancouver, British Columbia

Mandalay Resources Corporation
Consolidated statements of income
years ended December 31, 2012 and 2011
(Expressed in U.S. dollars)

	2012	2011
	$	$
Revenues	**171,805,623**	92,163,852
Cost of operations		
Cost of sales excluding depletion and depreciation	**76,540,792**	50,872,196
Depletion and depreciation	**19,339,436**	11,872,581
	95,880,228	62,744,777
Income from mine operations	**75,925,395**	29,419,075
Expenses		
Administration expense (Note 13)	**15,329,765**	9,278,068
Share-based compensation (Note 11)	**1,777,915**	1,642,407
(Gain) loss on disposal of property, plant and equipment	**(11,399)**	337,437
Write-off of exploration and evaluation (Note 5)	**1,587,791**	-
	18,684,072	11,257,912
Income from operations	**57,241,323**	18,161,163
Other income (expenses)		
Finance costs (Note 14)	**(3,418,217)**	(4,532,409)
(Loss) gain on derivative financial instruments (Note 15)	**(13,560,421)**	676,138
Interest and other income	**470,114**	160,816
Foreign exchange loss	**(318,769)**	(439,256)
	(16,827,293)	(4,134,711)
Income before income taxes	**40,414,030**	14,026,452
Income taxes expense (recovery) (Note 12)		
Current	**5,290,064**	-
Deferred	**(6,588,391)**	(4,450,865)
	(1,298,327)	(4,450,865)
Net income for the year	**41,712,357**	18,477,317
Income per share (Note 16)		
Basic	**0.14**	0.07
Diluted	**0.11**	0.06
Weighted average number of common shares outstanding (Note 16)		
Basic	**296,964,020**	251,213,123
Diluted	**368,597,541**	300,946,478

See accompanying notes to the consolidated financial statements.

Mandalay Resources Corporation

Consolidated statements of comprehensive income
years ended December 31, 2012 and 2011
(Expressed in U.S. dollars)

	2012	2011
	$	$
Net income for the year	**41,712,357**	18,477,317
Other comprehensive loss		
Foreign currency translation	**493,270**	(1,808,273)
Total comprehensive income	**42,205,627**	16,669,044

See accompanying notes to the consolidated financial statements.

Mandalay Resources Corporation

Consolidated statements of financial position
as at December 31, 2012 and 2011

(Expressed in U.S. dollars)

	2012	2011
	$	$
Assets		
Current assets		
Cash and cash equivalents	**17,264,446**	12,741,454
Trade and other receivables (Note 3)	**29,175,603**	11,225,321
Inventories (Note 4)	**14,177,346**	12,401,401
Prepaid expenses and other	**585,639**	290,657
Derivative financial instruments (Note 15)	**-**	16,253,768
	61,203,034	52,912,601
Non-current assets		
Reclamation and other deposits (Note 9)	**2,666,249**	2,431,941
Property, plant and equipment (Note 5)	**108,945,171**	79,099,451
Intangible asset (Note 6)	**1,246,984**	-
Deferred tax asset (Note 12)	**11,229,246**	4,450,865
	124,087,650	85,982,257
	185,290,684	138,894,858
Liabilities		
Current liabilities		
Trade and other payables (Note 7)	**18,218,862**	13,320,759
Current portion of borrowings (Note 8)	**-**	10,004,691
Provisions (Note 10)	**2,284,229**	1,408,666
Derivative financial instruments (Note 15(b))	**2,219,707**	-
	22,722,798	24,734,116
Non-current liabilities		
Borrowings (Note 8)	**-**	254,333
Reclamation and site closure costs (Note 9)	**17,145,695**	13,830,271
Provisions (Note 10)	**2,343,293**	1,105,172
	19,488,988	15,189,776
	42,211,786	39,923,892
Equity		
Share capital (Note 11)	**88,634,701**	79,665,838
Share option reserve (Note 11)	**7,332,054**	6,796,248
Warrants reserve (Note 11)	**1,251,752**	4,543,207
Foreign currency translation reserve	**2,167,685**	1,674,415
Retained earnings	**43,692,706**	6,291,258
	143,078,898	98,970,966
	185,290,684	138,894,858

Approved and authorized for issue by the Board on February 20, 2013.

(Signed) Bradford A. Mills

Bradford A. Mills, Director

(Signed) Robert Doyle

Robert Doyle, Director

See accompanying notes to the consolidated financial statements.

Mandalay Resources Corporation

Consolidated statements of changes in equity
years ended December 31, 2012 and 2011

(Expressed in U.S. dollars)

	Number of shares issued	Share capital	Share option reserve	Warrants reserve	Foreign currency translation reserve	Retained earnings (deficit)	Total equity
		$	$	$	$	$	$
Balance, December 31, 2010	215,178,788	59,233,056	5,573,759	6,019,794	3,482,688	(12,024,086)	62,285,211
Stock options exercised (Note 11 (b))	1,487,500	817,048	(419,918)	-	-	-	397,130
Share-based compensation (Note 11 (c))	-	-	1,642,407	-	-	-	1,642,407
Warrants exercised (Note 11 (d)(i))	53,960,287	19,748,064	-	(1,476,587)	-	-	18,271,477
Normal course issuer bid (Note 11 (e))	(449,500)	(132,330)	-	-	-	(161,973)	(294,303)
Total comprehensive (loss) income for the year	-	-	-	-	(1,808,273)	18,477,317	16,669,044
Balance, December 31, 2011	270,177,075	79,665,838	6,796,248	4,543,207	1,674,415	6,291,258	98,970,966
Stock options exercised (Note 11 (b))	3,929,086	2,283,903	(1,242,109)	-	-	-	1,041,794
Share-based compensation (Note 11 (c))	-	-	1,777,915	-	-	-	1,777,915
Warrants exercised (Note 11 (d)(i))	14,471,600	5,579,161	-	(642,126)	-	-	4,937,035
Warrant exchange offer (Note 11 (d)(ii))	-	-	-	(940,884)	-	-	(940,884)
Issuance of common shares in exchange for warrants (Note 11 (d)(ii))	35,795,052	1,708,445	-	(1,708,445)	-	-	-
Normal course issuer bid (Note 11 (e))	(2,185,660)	(602,646)	-	-	-	(1,110,365)	(1,713,011)
Dividends paid (Note 11 (f))	-	-	-	-	-	(3,200,544)	(3,200,544)
Total comprehensive (loss) income for the year	-	-	-	-	493,270	41,712,357	42,205,627
Balance, December 31, 2012	**322,187,153**	**88,634,701**	**7,332,054**	**1,251,752**	**2,167,685**	**43,692,706**	**143,078,898**

See accompanying notes to the consolidated financial statements.

Mandalay Resources Corporation

Consolidated statements of cash flows
years ended December 31, 2012 and 2011
(Expressed in U.S. dollars)

	2012	2011
	$	$
Operating activities		
Net income for the year	**41,712,357**	18,477,317
Adjustments to reconcile loss to net cash used by operating activities		
Depletion and depreciation	**19,370,520**	11,905,926
Amortization of intangible asset	**167,098**	-
(Gain) loss on disposal of property, plant and equipment	**(11,399)**	337,437
Write-off of exploration and evaluation	**1,587,791**	-
Share-based compensation	**1,777,915**	1,642,407
Foreign exchange (gain) loss	**187,495**	176,347
Interest and other income	**(470,114)**	(160,816)
Finance costs	**3,418,217**	4,532,409
Loss (gain) on derivative financial instruments	**13,560,421**	(676,138)
Deferred tax	**(6,588,391)**	(4,450,865)
Change in non-cash operating working capital items		
Trade and other receivables	**(17,971,575)**	617,695
Inventories	**(1,738,858)**	(5,057,867)
Prepaid expenses and other	**(295,782)**	442,187
Trade and other payables	**4,300,118**	1,558,689
Provisions	**2,234,342**	1,262,904
Cash generated from (used in) operations	**61,240,155**	30,607,632
Interest received	**470,138**	122,963
Interest paid	**(1,119,851)**	(1,071,869)
	60,590,442	29,658,726
Investing activities		
Expenditure for property, plant and equipment	**(44,410,537)**	(33,735,882)
Payment for reclamation and other deposits	**(194,843)**	(1,275,117)
Expenditure for reclamation	**(564,687)**	(1,548,775)
Proceeds on disposal of property, plant and equipment	**68,770**	944,324
Payment for derivative financial instruments	**-**	(16,053,450)
Proceeds from derivative financial instruments	**4,931,700**	475,820
Intangible assets	**(1,414,082)**	-
	(41,583,679)	(51,193,080)
Financing activities		
Proceeds from borrowings	**10,998,300**	4,993,888
Repayment of borrowings	**(26,287,273)**	(3,860,385)
Purchase of common shares for cancellation	**(1,713,011)**	(294,303)
Warrants and stock options exercised	**5,978,829**	18,668,607
Dividends paid	**(3,200,544)**	-
	(14,223,699)	19,507,807
Effects of exchange rate changes on the balance of cash held in foreign currencies	**(260,072)**	(155,105)
Increase (decrease) in cash and cash equivalents	**4,522,992**	(2,181,652)
Cash and cash equivalents, beginning of year	**12,741,454**	14,923,106
Cash and cash equivalents, end of year	**17,264,446**	12,741,454
Cash and cash equivalents are comprised of		
Cash	**8,400,446**	9,297,602
Cash equivalents	**8,864,000**	3,443,852
	17,264,446	12,741,454
Supplemental cash flow information		
Non-cash financing and investing activities		
Purchase of plant and equipment with equipment loans	**3,032,602**	637,589
Issuance of common shares in exchange for warrants	**1,708,445**	-
Purchase of building in exchange for other asset	**107,451**	-

See accompanying notes to the consolidated financial statements.

(Expressed in U.S. dollars)

1. Description of business and nature of operations

Mandalay Resources Corporation ("Mandalay" or the "Company") and its wholly-owned subsidiaries is a gold, silver and antimony producer engaged in mining and related activities including acquisition, exploration, extraction, processing and reclamation. Mandalay's assets are comprised of the Costerfield gold and antimony mine in Australia, the Cerro Bayo silver and gold mine in Chile as well as other exploration projects in Chile.

Mandalay is incorporated in British Columbia, Canada. The Company's shares are listed on the Toronto Stock Exchange ("TSX"). The head office and principal address of the Company is 76 Richmond Street East, Suite 330, Toronto, Canada, M5C 1P1. The Company's registered office is located at 1900-355 Burrard Street, Vancouver, British Columbia, V6C 2G8.

2. Summary of significant accounting policies

These consolidated financial statements, including comparatives, have been prepared using accounting policies in compliance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB") effective for the year ended December 31, 2012, using the significant accounting policies outlined below.

These financial statements have been prepared on a historical cost basis except for certain financial instruments, which are measured at fair values, as explained in the accounting policies set out below. In addition, these consolidated financial statements have been prepared using the accrual basis of accounting, except for cash flow information.

(a) Basis of consolidation

These consolidated financial statements include the financial statements of the Company and all of its controlled subsidiaries. Control exists when the Company has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. Subsidiaries are included in the consolidated financial statements from the date control commences until the date control ceases.

The principal subsidiaries of the Company as of December 31, 2012 are as follows:

Subsidiary	Interest
	%
AGD Mining Pty Ltd.[1]	100
Compania Minera Cerro Bayo Ltda[2]	100

[1] AGD Mining Pty Ltd. ("AGD") was acquired on November 30, 2009. AGD owns the Costerfield gold and antimony mine in Australia.

[2] Compania Minera Cerro Bayo Ltda ("Cerro Bayo") was acquired on August 10, 2010. Cerro Bayo owns the Cerro Bayo silver and gold mine and exploration projects in Chile.

All intercompany transactions, balances, income and expenses are eliminated.

2. Summary of significant accounting policies (continued)

(b) Foreign currencies

The Company's functional currency is the Canadian dollar as this is the principal currency of the economic environment in which it operates. AGD and Cerro Bayo have functional currencies of the Australian dollar and U.S. dollar, respectively.

Transactions in foreign currencies are initially recorded in the respective entity's functional currency at the exchange rate at the date of the transaction. Monetary assets and liabilities that are denominated in foreign currencies are translated at the rates prevailing at each reporting date. The translation gain/loss is recognized in the statement of income (loss). Non-monetary items that are measured in terms of historical cost in a foreign currency are translated at the exchange rate on the date of the transaction. On consolidation, each respective entity's financial statements are translated into the presentation currency as outlined below.

The financial statements are presented in U.S. dollars. For presentation purposes the assets and liabilities of the Company and its subsidiaries, including fair value adjustments arising on acquisition, are translated to U.S. dollars at exchange rates at the reporting date. The income and expenses of foreign operations are translated to U.S. dollars at the average exchange rate for the period in which the transaction arose. Exchange differences arising are recognized as a separate component of equity titled "foreign currency translation reserve". The financial statements have been presented in a currency other than the parent's functional currency as management has determined that the U.S. dollar is the common currency in which the Company's peers, being multi jurisdictional mining companies, present their financial statements.

(c) Business combinations

Acquisitions of subsidiaries and businesses are accounted for using the acquisition method. The consideration for each acquisition is measured at the aggregate of the fair values at the date of exchange of assets given, liabilities incurred or assumed, and equity instruments issued by the Company in exchange for control of the acquiree. Acquisition-related costs are recognized in profit or loss as incurred (unless they related to issue of debt/equity instruments).

Where applicable, the consideration for the acquisition includes any asset or liability resulting from a contingent consideration arrangement, measured at its acquisition-date fair value. Subsequent changes in such fair values are adjusted against the cost of acquisition where they qualify as measurement period adjustments. All other subsequent changes in the fair value of contingent consideration classified as an asset or liability are accounted for in accordance with relevant IFRS. Changes in the fair value of contingent consideration classified as equity are not recognized.

Goodwill arising in a business combination is recognized as an asset at the date that control is acquired (the "acquisition date"). Goodwill is measured as the excess of the sum of the consideration transferred, the amount of any non-controlling interests in the acquiree, and the fair value of the acquirer's previously held equity interest in the acquiree, if any, over the net of the acquisition-date amounts of the identifiable assets acquired and the liabilities assumed.

If the Company's interest in the fair value of the acquiree's identifiable net assets exceeds the sum of the consideration transferred, the amount of any non-controlling interests in the acquiree and the fair value of the acquirer's previously held equity interest in the acquiree, if any, the excess is recognized immediately in profit or loss as a bargain purchase gain.

2. Summary of significant accounting policies (continued)

(c) Business combinations (continued)

Goodwill is not amortized but is reviewed for impairment at least annually. For the purpose of impairment testing, goodwill is allocated to each of the Company's cash-generating units expected to benefit from the synergies of the combination. Cash generating units to which goodwill has been allocated are tested for impairment annually, or more frequently when there is an indication that the unit may be impaired. If the recoverable amount of the cash-generating unit is less than its carrying amount, the impairment loss is allocated first to reduce the carrying amount of any goodwill allocated to the unit and then to the other assets of the unit pro rata on the basis of the carrying amount of each asset in the unit. An impairment loss recognized for goodwill is not reversed in a subsequent period.

On disposal of a subsidiary, the attributable amount of goodwill is included in the determination of the profit or loss on disposal.

(d) Cash and cash equivalents

The Company considers all highly liquid investments with original maturities of three months or less at the date of acquisition to be cash equivalents.

(e) Inventories

Finished goods, work-in-process and stockpiled ore are valued at the lower of average production cost or net realizable value. Production costs include the cost of raw materials, direct labour, mine-site overhead expenses and depreciation and depletion of mining interests. Net realizable value is calculated as the estimated price at the time of sale based on prevailing and long-term metal prices less estimated future production costs to convert the inventories into saleable form and costs necessary to make the sale.

In-process inventory represents materials that are currently in the process of being converted into finished goods. The average production cost of finished goods represents the average cost of in-process inventories incurred prior to the refining process, plus applicable refining costs and associated royalties.

Supplies are valued at the lower of average cost and net realizable value.

(f) Property, plant and equipment

(i) <u>Exploration and evaluation</u>

Once a license to explore an area has been secured, expenditures on exploration and evaluation activities are capitalized within property, plant and equipment.

The Company records its capitalized exploration and evaluation at cost. The capitalized cost is based on cash paid, the value of share consideration and exploration costs incurred. The recoverable values are not always readily determinable and are dependent on the development program, the nature of the mineral deposit, commodity prices, adequate funding and the ability of the Company to bring its projects into production.

All costs related to the acquisition, exploration and evaluation of these interests are capitalized on the basis of specific claim blocks or areas of geological interest until the properties to which they relate are moved into development or production, sold or management has determined there to be an impairment of the value.

2. Summary of significant accounting policies (continued)

(f) Property, plant and equipment (continued)

(i) Exploration and evaluation (continued)

Management reviews the carrying value of capitalized exploration and evaluation costs at least annually. In the case of undeveloped projects, there may be only inferred resources to form a basis for the impairment review. The review is based on a status report regarding the Company's intentions for development of the undeveloped property. In some cases, the undeveloped properties are regarded as successors to ore bodies currently in production. Where this is the case, it is intended that these will be developed and go into production when the current source of ore is exhausted or to replace the reduced output.

Once an economically viable reserve has been determined for an area and the decision to proceed with development has been approved, exploration and evaluation assets attributable to that area are first tested for impairment and then reclassified to mining interests within property, plant and equipment.

(ii) Mining interests

Mining interests represent capitalized expenditures related to the development of mining properties, acquisition costs, capitalized borrowing costs (Note 2 (h)), expenditures related to exploration and evaluation transferred in and estimated site closure and reclamation costs.

Capitalized costs are depleted using the unit of production method over the estimated economic life of the mine to which they relate.

(iii) Plant and equipment

Plant and equipment are recorded at cost less accumulated depreciation, depletion and impairment charges.

Where an item of plant and equipment comprises major components with different useful lives, the components are accounted for as separate items of plant and equipment.

Expenditures incurred to replace a component of an item of plant and equipment that is accounted for separately, including major inspection and overhaul expenditures, are capitalized. Any remaining book value associated with the component being replaced is derecognized upon its replacement. Directly attributable expenses incurred for major capital projects and site preparation are capitalized until the asset is brought to a working condition for its intended use. These costs include dismantling and site restoration costs to the extent these are recognized as a provision.

(iv) Depreciation

Mining interests are depreciated to estimated residual value using the unit-of-production method based on the estimated total recoverable metal ounces contained in proven and probable reserves at the related mine when the production level intended by management has been reached ("commencement of commercial production").

The production level intended by management is considered to be reached when operational commissioning of major mine and plant components is completed, operating results are being achieved consistently for a period of time and there are indicators that these operating results will be sustained. Other factors include one or more of the following:

- A significant utilization rate of plant capacity has been achieved;
- A significant portion of available funding is directed towards operating activities;
- A pre-determined, reasonable period of time of stable operation has passed; and
- A development project significant to the primary business objective of the Company has been completed and significant milestones have been achieved.

2. Summary of significant accounting policies (continued)

(f) Property, plant and equipment (continued)

(iv) Depreciation (continued)

Management reviews the estimated useful lives, residual values and depreciation methods of the Company's property, plant and equipment at the end of each reporting period and when events and circumstances indicate that such a review should be made. Changes to estimated useful lives, residual values or depreciation methods resulting from such review are accounted for prospectively.

Plant and equipment cost is depreciated, using the straight-line method over their estimated useful lives, if shorter than the mine life, otherwise they are depreciated on the unit-of-production basis.

Plant and equipment includes building, plant and equipment, vehicles, furniture and fixtures and computer equipment and their estimated useful lives ranges from 2.5 years to 10 years.

Assets under construction are depreciated when they are complete and available for their intended use, over their estimated useful lives.

(g) Impairment of non-financial assets

The Company reviews and evaluates its property, plant and equipment for indicators of impairment when events or changes in circumstances indicate that the related carrying amounts may not be recoverable or at least at the end of each reporting period. If an indication of impairment exists, the asset's recoverable amount is estimated.

An impairment loss is recognized when the carrying amount of an asset exceeds its recoverable amount. For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which the asset belongs. A cash-generating unit is the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other assets or groups of assets. Future cash flows are estimated based on expected future production, commodity prices, operating costs and capital costs.

The recoverable amount is the greater of the asset's fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

Impairment losses are recognized in profit or loss.

An impairment loss is reversed if there is an indication that there has been a change in the original conditions that resulted in the impairment being recognized. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation, if no impairment loss had been recognized.

(h) Borrowing costs

Borrowing costs related to the costs of developing mining properties and constructing new facilities are capitalized and included in the carrying amounts of the related assets until mining properties reach commercial production and facilities are ready for their intended use.

The amount of borrowing costs capitalized (before effects of income tax) for the period is determined by applying the interest rate applicable to appropriate borrowings outstanding during the period to the average amount of capitalized expenditure for the qualifying assets during the period. Where any borrowing costs are incurred specifically in relation to a qualifying asset, they are allocated directly to the asset to which they relate and are excluded from the afore-mentioned calculation.

All other borrowing costs are recognized in profit or loss in the period in which they incurred.

2. Summary of significant accounting policies (continued)

(i) Intangible asset

Intangible assets with a finite useful lives that are acquired separately are carried at cost less accumulated amortization and accumulated impairment losses. Amortization is recognized on a straight-line basis over their estimated useful lives. The estimated useful life and amortization method are reviewed at the end of each reporting period, with the effect of any changes in estimate being accounted for on a prospective basis. Intangible assets with infinite useful lives that are acquired separately are carried at cost less accumulated impairment losses.

(j) Site closure and reclamation cost obligations

The Company records a liability based on the best estimate of costs for site closure and reclamation activities that the Company is legally or constructively required to remediate. The liability is recognized at the time the environmental disturbance occurs and the resulting costs are capitalized to the corresponding asset. The provision for site closure and reclamation liabilities is estimated using expected cash flows based on engineering and environmental reports prepared by third party industry specialists and discounted at a pre-tax rate specific to the liability. The capitalized amount is amortized on the same basis as the related asset. The liability is adjusted for the accretion of the discounted obligation and any changes in the amount or timing of the underlying future cash flows or the discount rate. Significant judgments and estimates are involved in forming expectations of the amounts and timing of future closure and reclamation cash flows.

Changes in site closure and reclamation estimates are accounted for as a change in the corresponding capitalized cost.

Costs of site closure and reclamation projects for which a provision has been recorded are recorded directly against the provision as incurred, most of which are incurred at the end of the life of mine.

(k) Income taxes

The Company uses the liability method of accounting for income taxes. Deferred tax is recognized on temporary differences between the carrying amounts of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable income and on the carryforward of tax losses and tax credits. Deferred tax liabilities are generally recognized for all taxable temporary differences except to the extent that the deferred tax liability arises from the initial recognition of an asset or liability in a transaction which affects neither accounting nor taxable profit at the time of the transaction. Deferred tax assets are generally recognized for all deductible temporary differences to the extent that it is probable that taxable profits will be available against which those deductible temporary differences can be utilized.

The Company recognizes a deferred tax asset for deductible temporary differences arising from investments in subsidiaries only to the extent that it is probable that the temporary difference will reverse in the foreseeable future and taxable profit will be available against which the temporary difference can be utilized. The Company recognizes a deferred tax liability for taxable temporary differences associated with investments in subsidiaries, except to the extent that the Company is able to control the timing of the reversal of the temporary difference and it is probable that the temporary difference will not reverse in the foreseeable future.

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

2. Summary of significant accounting policies (continued)

(k) Income taxes (continued)

Deferred tax assets and liabilities are measured using enacted or substantively enacted tax rates expected to apply when the asset is realized or the liability settled.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to set off current tax assets against current tax liabilities and when they relate to income taxes levied by the same taxation authority and the Company intends to settle its current tax assets and liabilities on a net basis.

Current and deferred tax are recognized as an expense or income in profit or loss, except when they relate to items that are recognized outside profit or loss (whether in other comprehensive income or directly in equity), in which case the tax is also recognized outside profit or loss, or where they arise from the initial accounting for a business combination. In the case of a business combination, the tax effect is included in the accounting for the business combination.

(l) Employee benefits

A liability is recognized for benefits accruing to employees in respect of wages and salaries, annual leave and long service leave when it is probable that settlement will be required and it is capable of being measured reliably. Liabilities recognized in respect of employee benefits due to be settled within 12 months are measured at their nominal values using the remuneration rate expected to apply at the time of settlement.

Liabilities recognized in respect of employee benefits which are not due to be settled within one year are measured at the present value of the estimated future cash outflows to be made by the Company in respect of services provided by employees up to reporting date.

(m) Revenue recognition

Revenue is measured at the fair value of the consideration received or receivable.

Revenue from the sale of metals is recognized when all of the following conditions are satisfied:

- the significant risks and rewards of ownership have been transferred to the purchaser;
- the Company does not retain continuing managerial involvement to the degree usually associated with ownership or effective control over the metals sold;
- the amount of revenue can be measured reliably;
- it is probable that the economic benefits associated with the transaction will flow to the Company; and
- the costs incurred or to be incurred in respect of the sale can be measured reliably.

Sales of certain commodities are provisionally priced such that the price is not settled until a predetermined future date based on the market price at that time. Revenue on these sales is initially recognized (when the above criteria are met) at the current market price. Provisionally priced sales are marked to market at each reporting date using the forward price for the period equivalent to that outlined in the contract. This mark to market adjustment is recognized in revenue.

2. Summary of significant accounting policies (continued)

(n) Share-based payment

Equity-settled share-based payments to employees and others providing similar services are measured at the fair value of the equity instruments at the grant date. Details regarding the determination of the fair value of equity-settled share-based transactions are set out in Note 11 (c).

The fair value determined using a valuation technique (e.g. Black-Scholes option pricing model) at the grant date of the equity-settled share-based payments is expensed on a straight-line basis over the vesting period, based on the Company's estimate of equity instruments that will eventually vest. At the end of each reporting period, the Company revises its estimate of the number of equity instruments expected to vest. The impact of the revision of the original estimates, if any, is recognized in profit or loss such that the cumulative expense reflects the revised estimate, with a corresponding adjustment to the share option reserve.

Equity-settled share-based payment transactions with parties other than employees are measured at the fair value of the goods or services received, except where that fair value cannot be estimated reliably, in which case they are measured at the fair value of the equity instruments granted, measured at the date the entity obtains the goods or the counterparty renders the service.

(o) Financial assets

Financial assets are classified into one of four categories:

- fair value through profit or loss ("FVTPL");
- held-to-maturity ("HTM");
- available for sale ("AFS"); and
- loans and receivables.

The classification is determined at initial recognition and depends on the nature and purpose of the financial asset.

(i) *<u>FVTPL financial assets</u>*

Financial assets are classified as FVTPL when the financial asset is held for trading or is designated as FVTPL.

A financial asset is classified as held for trading if:

- it has been acquired principally for the purpose of selling in the near future;
- it is a part of an identified portfolio of financial instruments that the Company manages and has an actual pattern of short-term profit-taking; or
- it is a derivative that is not designated and effective as a hedging instrument.

Financial assets classified as FVTPL are stated at fair value with any resultant gain or loss recognized in profit or loss. Transaction costs are expensed when incurred. The net gain or loss recognized incorporates any dividend or interest earned on the financial asset (Note 19).

2. Summary of significant accounting policies (continued)

(o) Financial assets (continued)

(ii) HTM investments

HTM investments are recognized on a trade-date basis and are initially measured at fair value, including transaction costs. The Company does not have any assets classified as HTM investments.

(iii) AFS financial assets

AFS financial assets are initially recognized at fair value. Subsequently, gains and losses arising from changes in fair value are recognized in other comprehensive income and accumulated in the accumulated other comprehensive income. When an investment is disposed of or is determined to be impaired, the cumulative gain or loss previously recognized in the other comprehensive income is included in profit or loss for the period. The fair value of AFS monetary assets denominated in a foreign currency is translated at the spot rate at the statement of financial position date. The change in fair value attributable to translation differences on amortized cost of the asset is recognized in profit or loss, while other changes are recognized in equity. The Company does not have any assets classified as AFS financial assets.

(iv) Loans and receivables

Trade receivables, loans, and other receivables that have fixed or determinable payments that are not quoted in an active market are classified as loans and receivables.

Loans and receivables are initially recognized at the transaction value and subsequently carried at amortized cost less impairment losses. The impairment loss of receivables is based on a review of all outstanding amounts at period end. Bad debts are written off during the year in which they are identified. Interest income is recognized by applying the effective interest rate, except for short-term receivables when the recognition of interest would be immaterial (Note 19).

(v) Effective interest method

The effective interest method calculates the amortized cost of a financial asset and allocates interest income over the corresponding period. The effective interest rate is the rate that discounts estimated future cash receipts over the expected life of the financial asset, or, where appropriate, a shorter period, to the net carrying amount on initial recognition.

Income is recognized on an effective interest basis for financial instruments other than those financial assets classified as FVTPL.

2. Summary of significant accounting policies (continued)

(o) Financial assets (continued)

(vi) *Impairment of financial assets*

Financial assets, other than those at FVTPL, are assessed for indicators of impairment at each period end. Financial assets are impaired when there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows of the investment have been impacted.

For financial assets carried at amortized cost, the amount of the impairment is the difference between the asset's carrying amount and the present value of the estimated future cash flows, discounted at the financial asset's original effective interest rate.

The carrying amount of all financial assets, excluding trade receivables, is directly reduced by the impairment loss. The carrying amount of trade receivables is reduced through the use of an allowance account. When a trade receivable is considered uncollectible, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited against the allowance account. Changes in the carrying amount of the allowance account are recognized in profit or loss.

With the exception of AFS equity instruments, if, in a subsequent period, the amount of the impairment loss decreases and the decrease relates to an event occurring after the impairment was recognized, the previously recognized impairment loss is reversed through profit or loss. On the date of impairment reversal, the carrying amount of the financial asset cannot exceed its amortized cost had impairment not been recognized.

(vii) *Derecognition of financial assets*

A financial asset is derecognized when:

- the contractual right to the asset's cash flows expire; or
- if the Company transfers the financial asset and substantially all risks and rewards of ownership to another entity.

2. Summary of significant accounting policies (continued)

(p) Financial liabilities and equity

Debt and equity instruments are classified as either financial liabilities or as equity in accordance with the substance of the contractual arrangement.

An equity instrument is any contract that evidences a residual interest in the assets of an entity after deducting all of its liabilities. Equity instruments issued by the Company are recorded at the proceeds received, net of direct issue costs.

Financial liabilities are classified as either financial liabilities at FVTPL or other financial liabilities.

(i) Other financial liabilities

Other financial liabilities are initially measured at fair value, net of transaction costs, and are subsequently measured at amortized cost using the effective interest method, with interest expense recognized on an effective yield basis.

The effective interest method is a method of calculating the amortized cost of a financial liability and of allocating interest expenses over the corresponding period. The effective interest rate is the rate that exactly discounts estimated future cash payments over the expected life of the financial liability, or, where appropriate, a shorter period, to the net carrying amount on initial recognition (Note 19).

(ii) Derecognition of financial liabilities

The Company derecognizes financial liabilities when, and only when, the Company's obligations are discharged, cancelled or they expire.

(q) Income per share

Basic income per share is computed by dividing the net income attributable to common shareholders by the weighted average number of shares outstanding during the reporting period.

Diluted income per share is computed similar to basic income per share except that (i) net income attributable to common shareholders are adjusted for fair value gains or losses of warrants (if dilutive) and (ii) the weighted average shares outstanding are increased to include additional shares for the assumed exercise of stock options and warrants (if dilutive).

The number of additional shares is calculated by assuming that outstanding dilutive stock options and warrants were exercised and that the proceeds from such exercises (after adjustment of any unvested portion of stock options) were used to acquire common stock at the average market price during the reporting periods.

(r) Provisions

Provisions are recorded when a present legal or constructive obligation exists as a result of past events, where it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and when a reliable estimate of the amount of the obligation can be made.

The amount recognized as a provision is the best estimate of the consideration required to settle the present obligation estimated at the end of each reporting period, taking into account the risks and uncertainties surrounding the obligation. Where a provision is measured using the cash flows estimated to settle the present obligation, its carrying amount is the present value of those cash flows. When some or all of the economic benefits required to settle a provision are expected to be recovered from a third party, the receivable is recognized as an asset if it is virtually certain that reimbursement will be received and the amount receivable can be measured reliably.

2. Summary of significant accounting policies (continued)

(s) Critical judgments and accounting estimates

In the application of the Company's accounting policies, management is required to make judgments, estimates and assumptions about the carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and assumptions are based on historical experience and other factors that are considered to be relevant. Actual results may differ from these estimates.

Following are the items involving significant judgments:

- determination of functional currency; and
- classification of financial instruments.

Following are the items involving significant estimates:

- measurement of revenue and accounts receivable;
- the assumptions used in the accounting for share-based compensation (Note 11 (c));
- the provision for income taxes and composition of deferred income tax assets and liabilities (Note 12);
- the recoverability of accounts receivable;
- the recoverability of inventory;
- the fair value of FVTPL financial assets and liabilities;
- the fair value of assets and liabilities acquired in business combinations;
- reserve estimates (see below);
- the anticipated costs of reclamation and closure cost obligations (Notes 2 (i) and 9); and
- valuation of warrants (Note 11 (d)).

Reserve estimates

The Company estimates its ore reserves and mineral resources based on information compiled by Qualified Persons as defined in accordance with Canadian Securities Administrators National Instrument 43-101 *Standards for Disclosure of Mineral Projects* ("NI 43-101"). Reserves are used in the calculation of depreciation and amortization, impairment assessment, assessment of life of mine stripping ratios and for forecasting the timing of payment of mine closure, reclamation and rehabilitation costs.

There are numerous uncertainties inherent in estimating ore reserves, and assumptions that are valid at the time of estimation may change significantly when new information becomes available. Changes in the forecast prices of commodities, exchange rates, production costs or recovery rates may change the economic status of reserves and may, ultimately, result in the reserves being restated.

2. Summary of significant accounting policies (continued)

(t) New accounting pronouncement

(a) *Application of new and revised International Financial Reporting Standards*

Effective January 1, 2012, the Company adopted revised International Financial Reporting Standards that were issued by the International Accounting Standards Board ("IASB"). The application of this new and revised IFRSs have not had any impact on the amounts reported for the current and prior years but may affect the accounting for future transactions or arrangements.

(i) Amendments to IFRS 7 *Financial Instruments: Disclosures*

Increase in disclosure with regards to the transfer of financial assets, especially if there is a disproportionate amount of transfer transactions that take place around the end of a reporting period.

(ii) Amendments to IAS 12 *Income Taxes*

The amendment provides a practical solution to the application of IAS 12 in relation to investment property under IAS 40 Investment Property.

(b) *Accounting standards issued but not yet effective*

(i) Effective for annual periods beginning on or after July 1, 2012

- Amended standard IAS 1 Presentation of Financial Statements

  The amendment to IAS 1 revises the presentation of other comprehensive income.

(ii) Effective for annual periods beginning on or after January 1, 2013

- Amended standard IFRS 7 *Financial Instruments: Disclosures*

  The amendment to IFRS 7 enhances the disclosure required when offsetting financial assets and liabilities.

- New standard IFRS 10 *Consolidated Financial Statements*

  IFRS 10 outlines the principles for the presentation and preparation of consolidated financial statements.

- New standard IFRS 11 *Joint Arrangements*

  IFRS 11 defines the two types of joint arrangements (joint operations and joint ventures) and outlines how to determine the type of joint arrangement entered into and the principles for accounting for each type of joint arrangement.

- New standard IFRS 12 *Disclosure of Interests in Other Entities*

  IFRS 12 outlines the disclosures required in order to provide users of financial statements with the information necessary to evaluate an entity's interest in other entities, the corresponding risks related to those interests and the effects of those interests on the entity's financial position, financial performance and cash flows.

2. Summary of significant accounting policies (continued)

(t) New accounting pronouncement (continued)

(b) Accounting standards issued but not yet effective (continued)

(ii) Effective for annual periods beginning on or after January 1, 2013 (continued)

- New standard IFRS 13 *Fair Value Measurement*

  IFRS 13 defines fair value, summarizes the methods of determining fair value and outlines the required fair value disclosures. IFRS 13 is utilized when another IFRS standard requires or allows fair value measurements or disclosures about fair value measurements.

- New interpretation IFRIC Interpretation 20 *Stripping Costs in the Production Phase of a Surface Mine*

  IFRIC Interpretation 20 summarizes the method of accounting for waste removal costs incurred as a result of surface mining activity during the production phase of a mine.

- Amended standard IAS 19 *Employee Benefits*

  IAS 19 outlines the accounting treatment and required disclosures for employee benefits. The amendments applicable to the Company consist of modification of the accounting treatment for termination benefits and the clarification of miscellaneous issues including the classification of employee benefits.

- Amended standard IAS 27 *Separate Financial Statements*

  IAS 27 outlines the accounting principles to be applied with regards to investments in subsidiaries, joint ventures and associates when an entity elects or is required by local regulations to present separate, non-consolidated, financial statements. The previous standard was titled IAS 27 Consolidated and Separate Financial Statements.

- Amended standard IAS 28 *Investments in Associates and Joint Ventures*

  IAS 28 outlines the accounting treatment and corresponding application of the equity method of accounting in investments in associates and joint ventures. The previous standard was titled IAS 28 Investments in Associates.

(iii) Effective for annual periods beginning on or after January 1, 2014

- Amended standard IAS 32 *Financial Instruments: Presentation*

  The amendments to IAS 32 pertained to the application guidance on the offsetting of financial assets and financial liabilities.

(iv) Effective for annual periods beginning on or after January 1, 2015

- Amended standard IFRS 7 *Financial Instruments: Disclosures*

  The amendments to IFRS 7 outlines the disclosures required when initially applying IFRS 9 Financial Instruments.

- New standard IFRS 9 *Financial Instruments*

  Partial replacement of IAS 39 Financial Instruments: Recognition and Measurement

The Company has not early adopted these new and amended standards. No material impact is expected as a result of the adoptions of these new and amended standards.

(Expressed in U.S. dollars)

3. Trade and other receivables

Trade and other receivables are comprised of the following:

	2012	2011
	$	$
Trade receivables (Note 19 (b))	**25,834,771**	7,720,331
VAT and other indirect tax receivables	**2,856,547**	3,172,674
Other receivables	**484,285**	332,316
	29,175,603	11,225,321

The allowance for doubtful accounts was $Nil at December 31, 2012 and 2011, respectively.

During the year ended December 31, 2012, the Company received $1.0 million value added tax ("VAT") refund from the Chilean tax authority, which was acquired as part of the Cerro Bayo acquisition in 2010. With this receipt, the Company has collected all VAT refunds acquired as part of the Cerro Bayo acquisition. The $1.0 million VAT is payable to the vendor of Cerro Bayo in accordance with the acquisition agreement. The Company completed the payment in June 2012.

4. Inventories

	2012	2011
	$	$
Finished goods	**6,370,235**	5,315,421
Work-in-progress and stockpiled ore	**808,842**	870,558
Consumables	**6,998,269**	6,215,422
	14,177,346	12,401,401

The amount of inventories recognized in cost of sales for the year ended December 31, 2012 is $95,880,228 (2011 - $62,744,777).

During the year ended December 31, 2012, the Company recorded a provision of $Nil (2011 -$237,419) to write down the value of the consumables to net realizable value.

(Expressed in U.S. dollars)

5. Property, plant and equipment

Property, plant and equipment consist of the following:

	Mining interests			Plant and equipment			Exploration and evaluation			
	Costerfield	Cerro Bayo	Others	Costerfield	Cerro Bayo	Others	Costerfield	Cerro Bayo	Others	Total
	$	$	$	$	$	$	$	$	$	$
Cost										
As at January 1, 2011	15,127,566	13,326,943	-	13,693,863	10,247,799	92,862	1,120,578	584,847	9,888,012	64,082,470
Additions	6,160,012	14,481,736	-	5,491,977	3,880,364	88,236	2,774,475	506,179	1,754,268	35,137,247
Disposals	-	(2,433)	-	(1,681,419)	(522,958)	(65,838)	-	-	-	(2,272,648)
Reclassification to mining interest	-	577,625	-	-	-	-	-	(577,625)	-	-
Foreign exchange	(1,128,585)	-	-	(285,025)	-	68,515	(32,368)	-	(192,645)	(1,570,108)
As at December 31, 2011	20,158,993	28,383,871	-	17,219,396	13,605,205	183,775	3,862,685	513,401	11,449,635	95,376,961
Additions	7,964,203	14,631,990	-	7,870,833	7,908,693	408,072	5,132,931	4,793,105	2,298,167	51,007,994
Disposals	-	-	-	(278,213)	(2,094,215)	(2,874)	-	-	-	(2,375,302)
Reclassification to mining interest	1,473,923	-	-	-	-	-	(1,473,923)	-	-	-
Impairment	-	-	-	-	-	-	(271,390)	(1,316,401)	-	(1,587,791)
Foreign exchange	115,481	-	-	289,715	-	3,688	114,986	-	217,815	741,685
As at December 31, 2012	**29,712,600**	**43,015,861**	**-**	**25,101,731**	**19,419,683**	**592,661**	**7,365,289**	**3,990,105**	**13,965,617**	**143,163,547**
Accumulated depreciation										
As at January 1, 2011	1,839,641	-	-	1,921,139	377,188	20,806	-	-	-	4,158,774
Expense	2,976,699	4,381,186	-	1,673,530	4,213,845	48,486	-	-	-	13,293,746
Disposals	-	-	-	(426,361)	(493,756)	(10,343)	-	-	-	(930,460)
Foreign exchange	(139,840)	-	-	(103,435)	-	(1,275)	-	-	-	(244,550)
As at December 31, 2011	4,676,500	4,381,186	-	3,064,873	4,097,277	57,674	-	-	-	16,277,510
Expense	3,307,814	9,525,977	-	2,736,291	4,424,845	41,256	-	-	-	20,036,183
Disposals	-	-	-	(120,323)	(2,087,345)	(1,232)	-	-	-	(2,208,900)
Foreign exchange	61,944	-	-	50,325	-	1,314	-	-	-	113,583
As at December 31, 2012	**8,046,258**	**13,907,163**	**-**	**5,731,166**	**6,434,777**	**99,012**	**-**	**-**	**-**	**34,218,376**
Carrying value										
As at December 31, 2011	15,482,493	24,002,685	-	14,154,523	9,507,928	126,101	3,862,685	513,401	11,449,635	79,099,451
As at December 31, 2012	21,666,342	29,108,698	-	19,370,565	12,984,906	493,649	7,365,289	3,990,105	13,965,617	108,945,171

For the year ended December 31, 2012, Cerro Bayo's plant and equipment depreciation of $664,599 is capitalized in mining interest (2011 - $1,387,820).

(Expressed in U.S. dollars)

5. Property, plant and equipment (continued)

(a) Exploration and evaluation - others

(i) La Quebrada

During the year ended December 31, 2001, the Company entered into an option agreement with Inversiones Y Mineria Andale Ltda. ("Andale") and Exploraciones Rio Bravo Ltda. ("Rio Bravo") subject to a 2% net smelter return royalty ("NSR") (amended November 25, 2001 and February 27, 2004) to earn up to a 100% undivided, right, title and interest in certain mining claims located in Northern Chile (known as the "La Quebrada Property").

(ii) Leoncita

During the year ended December 31, 2005, the Company entered into an option agreement with Andale subject to a 2% NSR (amended March 31, 2009). The agreement allowed the Company to earn up to a 100% undivided, right, title and interest in the property located contiguous to the Company's La Quebrada copper-silver property in North Central Chile (the "Leoncita Property").

(b) Royalties

For its Costerfield mine, the Company is required to pay a 2.75% NSR to the government in Australia.

For its Cerro Bayo mine, the Company is required to pay to the former owner a 2% NSR on production in excess of 50,000 ounces of gold and 5,000,000 ounces of silver. As of December 31, 2012, 23,767 ounces of gold and 4,230,260 ounces of silver has been produced.

6. Intangible asset

In June 2012, the Company reached an agreement with its union workers in Chile and paid a lump-sum cash payment of $1,414,082 to secure the contract. This payment is recorded as an intangible asset and amortized over the contractual life of the union agreement being three years. The carrying amount of the union payment as at December 31, 2012 is $1,246,984 (2011 - $Nil). Amortization expense of $167,098 (2011 - $Nil) is recorded as part of cost of sales.

7. Trade and other payables

	2012	2011
	$	$
Trade payables	**5,149,999**	7,752,970
Accrued liabilities	**7,108,259**	3,851,276
Income, payroll and other taxes payable	**5,960,604**	772,841
Payable to vendor for VAT refund (Note 3)	**-**	943,672
	18,218,862	13,320,759

The average credit period of purchases is one month. The Company has financial risk management policies in place to ensure that all payables are paid within the pre-agreed credit terms.

(Expressed in U.S. dollars)

8. Borrowings

Borrowings consist of the following:

	Effective interest rate	Maturity	**2012**	2011
	%		**$**	$
Current				
Equipment loan (a)	7.35 to 9.32	2012	**-**	718,377
Sprott loan (b)	17.00	2012	**-**	7,183,811
Silver contract (c)	-	2012	**-**	2,102,503
			-	10,004,691
Non-current				
Equipment loan (a)	7.35 to 9.32	2013 - 2014	**-**	254,333
			-	10,259,024

(a) AGD leased certain equipment under finance leases. Equipment loans bear interest at rates from 7.86% to 9.93% and are secured by the applicable equipment they are financing. During the year ended December 31, 2012, the Company repaid the entire equipment loan.

(b) In December 2010, the Company entered into a loan agreement with Sprott Resource Lending Partnership (“Sprott”) in the amount of $10,054,000 (C$10,000,000) bearing interest at a rate of 11% and maturing on December 17, 2012. The loan was secured by certain assets of the Company. The Company drew down the first tranche of the loan of C$5,000,000 by December 31, 2010, net of the arrangement fee of $100,540 (C$100,000). The Company also issued 1,885,938 common shares to Sprott and incurred $467,266 (C$463,230) in loan issue costs. These transaction costs were netted against the loan balance. The Company was required to prepay portions of the loan upon certain financing transactions occurring prior to maturity of the loan. In February 2011 the Company drew down the second tranche of the loan of $5,027,000 (C$5,000,000). On this second finance loan, the Company incurred $757,086 (C$734,038) in loan issue costs. The loan was fully repaid in June 2012.

(c) The Company was required to pay cash in an aggregate amount equal to the U.S. dollar equivalent of 125,000 ounces of silver to be paid in six quarterly installments from Q3 2011 to Q4 2012 to the vendor of Cerro Bayo in accordance with the acquisition agreement. For the year ended December 31, 2012, the Company paid the last four instalments (2011 – first two installments) of the silver contract totalling $2,555,916 based on the silver market price (2011 - $1,258,313). As at December 31, 2012, the Company settled the liability. During the year ended December 31, 2012, the Company recorded a fair value measurement loss of $453,413 (2011 - $1,708,638) (Note 14).

(d) In March 2012, Cerro Bayo borrowed $1,000,100 from Banco Credito Inversiones (“BCI”). The loan was non-secured, bearing interest at a rate of 3.68% and matured on May 29, 2012. The Company fully repaid the loan at maturity.

(Expressed in U.S. dollars)

8. Borrowings (continued)

(e) On May 30, 2012, the Company and the Bank of Montreal ("BMO") entered into a one year revolving corporate loan facility (the "Corporate Facility") for $20 million. The Corporate Facility is for general corporate purposes, including working capital, capital expenditures and any acquisition of an entity in the mining industry in Australia, Canada, Chile or the United States of America. It is subject to an interest rate of the lender's borrowing cost (LIBOR etc.) plus a variable margin of between 2.25% and 3.25%. Unused credit facility balances are subject to a standby fee at the rate of 0.8%. The Corporate Facility is secured by all assets held by the Company.

The Company incurred transaction costs of $157,828 (C$162,341) for the arrangement of the Corporate Facility, which is recorded in finance costs.

In June and July 2012, the Company drew down a total of $8 million of the credit facility to repay the equipment loan (Note 8 (a)) and the Sprott loan (Note 8 (b)). Subsequently, in September 2012, the Company repaid the loan fully.

9. Reclamation and site closure costs

Site closure and reclamation cost obligations arise from the acquisition, development, construction and normal operation of mining property, plant and equipment, due to government controls and regulations that protect the environment on the closure and reclamation of mining properties. The Company has future obligations to retire its mining assets including dismantling, remediation and ongoing treatment and monitoring of sites. The exact nature of environmental issues and costs, if any, which the Company may encounter in the future are subject to change, primarily because of the changing character of environmental requirements that may be enacted by governmental agencies.

The Company's site closure reclamation obligations consist of costs for the Costerfield Mine and the Cerro Bayo Mine (including Furioso). Significant site closure and reclamation activities include land rehabilitation, demolition of buildings and mine facilities, ongoing care and maintenance and other costs.

Changes to the site closure and reclamation cost balance are as follows:

	$
Balance, December 31, 2010	14,391,089
Expenditure for reclamations	(1,548,775)
Accretion (Note 14)	986,225
Foreign exchange	1,732
Balance, December 31, 2011	13,830,271
Expenditure for reclamations	(564,687)
Change in estimated cash outflows	2,792,573
Accretion (Note 14)	1,062,357
Foreign exchange	25,181
Balance, December 31, 2012	17,145,695

Each period the Company reviews cost estimates and other assumptions used in the valuation of reclamation and closure cost's to reflect events, changes in circumstances and new information available. Changes in these cost estimates and assumptions have a corresponding impact on the best estimate of the site closure and reclamation obligation.

(Expressed in U.S. dollars)

9. Reclamation and site closure costs (continued)

The best estimate of site closure and reclamation obligation costs is measured by discounting the expected cash flows using a discount factor that reflects a pre-tax rate specific to the liability. The Company prepares estimates of the timing and amount of expected cash flows when site closure and reclamation costs are incurred. Expected cash flows are updated to reflect changes in facts and circumstances. The principal factors that can cause expected cash flows to change are: the construction of new processing facilities; changes in the quantities of material in reserves and a corresponding change in the life-of-mine plan; changing ore characteristics that impact required environmental protection measures and related costs; changes in water quality that impact the extent of water treatment required; and changes in laws and regulations governing the protection of the environment. The best estimate of site closure and reclamation costs is recorded when it is incurred.

The total undiscounted amount of estimated cash flows required to settle the retirement obligations is $19,539,284 (2011 - $15,960,680).

The present value of the site closure and reclamation cost obligations for the Costerfield mine at December 31, 2012 is $1,923,098 (2011 - $1,793,291), calculated using a discount rate of 7% (2011 - 7%). The obligations are expected to be settled primarily in the years 2017 through 2018. The regulatory body in Australia requires reclamation deposits from the Company. As at December 31, 2012, the deposit amounted to $2,666,249 (2011 - $2,431,941) and is recorded in reclamation and other deposits.

The present value of the site closure and reclamation cost obligations for the Cerro Bayo Mine at December 31, 2012 is $15,222,597 (2011 - $12,036,980), calculated using a discount rate of 2.63% (2011 – 7.00%). The obligations are expected to be settled in the years 2013 through 2022.

10. Provisions

	Employee benefit (i)	Severence payment (ii)	Total
	$	$	$
Balance, December 31, 2011	1,480,381	1,033,457	2,513,838
Additions	2,431,354	1,209,419	3,640,773
Amounts paid	(1,497,439)	(40,522)	(1,537,961)
Foreign exchange	10,872	-	10,872
Balance, December 31, 2012	2,425,168	2,202,354	4,627,522
Less: current portion	2,284,229	-	2,284,229
Long-term portion	140,939	2,202,354	2,343,293

(i) AGD and Cerro Bayo provide for vacation provision for their current employees, in accordance with statutory requirements.

(ii) Cerro Bayo provides for certain severance payments in accordance with statutory requirements.

(Expressed in U.S. dollars)

11. Share capital

At December 31, 2012, the Company had unlimited number of authorized common shares without par value and 322,187,153 common shares outstanding (2011 - 270,177,075 common shares). All outstanding shares are fully paid.

(a) Shares issued for cash

For the years ended December 31, 2012 and 2011, the Company issued its common shares upon exercise of share options and warrants by their holders and pursuant to the Company's warrant exchange offer (Note 11 (b) and (d)).

(b) Stock options

The Company has established a "rolling" stock option plan (the "Plan") in compliance with the TSX's policy for granting stock options. Under the Plan, the maximum number of shares reserved for issuance may not exceed 10% of the total number of issued and outstanding common shares. The exercise price of each option shall not be less than the market price of the Company's stock at the date of grant. Options generally vest over three years and have a maximum term of seven years from date of grant.

	Number of options	Weighted average exercise price
		C$
Balance, December 31, 2010	10,100,946	0.27
Granted	5,748,750	0.58
Forfeited	(463,750)	0.24
Expired	(187,480)	0.50
Exercised	(1,487,500)	0.27
Balance, December 31, 2011	13,710,966	0.40
Granted	4,092,500	0.83
Forfeited	(130,000)	0.55
Expired	(114,380)	0.50
Exercised	(3,929,086)	0.26
Balance, December 31, 2012	13,630,000	0.57

(Expressed in U.S. dollars)

11. Share capital (continued)

(b) Stock options (continued)

The following table summarizes information about the stock options outstanding at December 31, 2012:

Options outstanding			Options exercisable	
Number of stock options outstanding	Weighted average remaining contractual life (years)	Weighted average exercise price	Number of options exercisable	Weighted average exercise price
		C$		C$
2,130,000	1.94	0.26	2,130,000	0.26
1,402,500	2.66	0.26	1,390,000	0.26
50,000	2.69	0.31	37,500	0.31
300,000	2.77	0.33	225,000	0.33
100,000	2.71	0.34	75,000	0.34
70,000	3.07	0.42	70,000	0.42
150,000	0.64	0.50	150,000	0.50
3,965,000	3.20	0.56	-	0.56
470,000	3.28	0.58	-	0.58
490,000	3.92	0.70	-	0.70
450,000	3.51	0.76	-	0.76
4,052,500	4.19	0.83	-	0.83
13,630,000	3.24	0.57	4,077,500	0.27

(c) Share-based compensation

For the year ended December 31, 2012, the Company recorded $1,777,915 (2011 - $1,642,407) as share-based compensation expense and recorded this amount in share option reserve. The value was determined using the Black-Scholes option pricing model. A weighted average grant-date fair value of C$0.59 (2011 - C$0.51) was calculated using the following weighted average assumption. Expected stock price volatility is based on the Company's historical share price volatility.

	2012	2011
Risk free interest rate	**1.49%**	2.53%
Expected dividend yield	**Nil**	Nil
Expected option life (years)	**5.00**	5.00
Expected stock price volatility	**91%**	116%
Expected forfeiture rate	**5%**	5%

(Expressed in U.S. dollars)

11. Share capital (continued)

(d) Share purchase warrants

(i) A summary of the changes in share purchase warrants is presented below:

	Number of warrants	Weighted average exercise price
		C$
Balance, December 31, 2010	159,489,599	0.36
Exercised	(53,960,287)	0.33
Expired	(150,000)	0.25
Balance, December 31, 2011	105,379,312	0.38
Exercised	(14,471,600)	0.34
Exchanged for common shares	(67,297,777)	0.39
Expired	(9,935)	0.33
Balance, December 31, 2012	**23,600,000**	**0.37**

The following table summarizes information about outstanding and exercisable share purchase warrants at December 31, 2012:

Number of warrants	Exercise price	Expiry date
	C$	
8,950,000	0.47	November 30, 2014
14,650,000	0.31	November 30, 2014
23,600,000	0.37	

(ii) On May 24, 2012, the Company commenced an exchange offer to its warrant holders to exchange all or a portion of their common share purchase warrants of the Company for common shares of the Company at the rates set out below:

Warrant series	Exercise price	Expiry date	Exchange price for each warrant
	C$		
Series 2	0.33	August 6, 2012	0.58 common shares
Series 3	0.20	April 22, 2014	0.79 common shares
Series 4	0.20	July 22, 2014	0.79 common shares
Series 5	0.47	October 15, 2014	0.47 common shares
Series 6	0.31	November 30, 2014	0.63 common shares
Series 7	0.47	November 30, 2014	0.47 common shares

11. Share capital (continued)

(d) Share purchase warrants (continued)

(ii) (continued)

The offer expired on July 3, 2012. Warrants that were not tendered to the exchange offer remain outstanding in accordance with their terms and are not affected by the exchange offer.

The Company has determined that the fair value of the consideration given up approximated the fair value of the warrants reacquired, accordingly no adjustment was recorded to warrants reserve.

The related transaction costs of $940,884 were recorded as a decrease to warrants reserve.

As of July 4, 2012, 67,297,777 warrants were tendered to the exchange offer. The Company issued 35,795,052 common shares in exchange for the tendered warrants. Upon the issuance, $1,708,445 was reclassified from warrants reserve to share capital.

(e) Normal Course Issuer Bid ("NCIB")

On October 13, 2011, the Company entered into an NCIB ("2011 NCIB"). The 2011 NCIB covered the period of October 17, 2011 to October 16, 2012. Pursuant to the 2011 NCIB, the Company was authorized by the TSX to purchase up to 13,501,078 common shares and 1,970,965 common share purchase warrants. Purchases were made at the discretion of the Company at prevailing market prices, commencing October 17, 2011 and ending October 16, 2012. Pursuant to TSX policies, daily purchases made by the Company did not exceed 53,433 common shares and 6,084 common share purchase warrants. The shares acquired under the NCIB were cancelled upon their purchases. The funding for any purchase pursuant to the NCIB was financed out of working capital of the Company.

On October 15, 2012, the TSX approved the Company's notice of intention to make an NCIB ("2012 NCIB"). Pursuant to the 2012 NCIB, the Company may purchase up to 15,856,786 common shares, issued and outstanding as of October 3, 2012. Purchases will be made, at the discretion of the Company at prevailing market prices, commencing October 17, 2012 and ending October 16, 2013. Pursuant to TSX policies, daily purchases made by the Company will not exceed 57,089 common shares. The shares acquired under the NCIB will be cancelled upon their purchase. The funding for any purchase pursuant to the NCIB will be financed out of the working capital of the Company.

Under the 2011 NCIB and the 2012 NCIB, the Company repurchased 2,185,660 common shares (2011 – 449,500) at an average price of C$0.78 (2011 – C$0.69) at a cost of $1,713,011 (2011 - $294,303) during the year ended December 31, 2012. The excess of the purchase price over the average stated value of shares purchased for cancellation of $1,110,365 (2011 - $161,973) was charged to retained earnings. The Company ceases to consider shares as outstanding on the date of the Company's purchase of its shares although the actual cancellation of the shares by the transfer agent and register occurs on a date shortly thereafter.

(f) Dividends

On November 7, 2012, the Board of Directors declared a dividend in the amount of $0.01 per common share, based on the Company's operating results for the three month period ended September 30, 2012, payable to shareholders of record on November 20, 2012. Total payment of $3,200,544 was made during the year ended December 31, 2012 (2011 - $Nil).

(Expressed in U.S. dollars)

12. Income taxes

Income tax expense (recovery) consists of the following:

	2012	2011
	$	$
Current tax		
Income tax	5,290,064	-
	-	-
Deferred tax		
Origination and reversal of temporary differences	2,651,952	-
Previously unrecognized tax loss or temporary difference used to reduce current tax expense	2,966,872	2,517,860
Previously unrecognized tax loss or temporary difference used to reduce deferred tax expense	(12,207,215)	(6,968,725)
	(6,588,391)	(4,450,865)
	(1,298,327)	(4,450,865)

Income tax expense differs from the amount that would result from applying the Canadian federal and provincial income tax rates to income before taxes. These differences result from the following items:

	2012	2011
	$	$
Income before income taxes	40,414,030	14,026,452
Canadian federal and provincial income tax rates	26.5%	28.3%
Income tax expense based on above rates	10,709,718	3,962,472
Increase (decrease) due to		
Non-deductible expenditures	273,757	460,095
Rate difference in other jurisdictions	(2,117,683)	(1,662,319)
Impact of lower tax rates on deferred income taxes	(731,362)	(1,777,380)
Benefit of losses not previously recognized	(10,022,197)	(6,101,980)
Others	589,440	668,247
	(1,298,327)	(4,450,865)

The tax rates used for the 2012 and 2011 reconciliations above are the corporate tax rates applicable to Mandalay in the Canadian jurisdictions. The applicable tax rate changed from 28.3% in 2011 to 26.5% in 2012 due to a change in the substantively enacted rate.

Current taxes payable of $5,290,064 have been included in trade and other payables on the consolidated statements of financial position.

(Expressed in U.S. dollars)

12. Income taxes (continued)

The components of deferred income taxes are as follows:

	2012	2011
	$	$
Deferred income tax assets (a)		
Tax loss carryforwards	**13,860,940**	5,622,962
Deductible temporary differences and other:		
Reclamation and site closure costs	**3,044,520**	2,046,287
Provisions and accruals	**973,432**	408,936
Other	**835,505**	-
Deferred income tax assets	**18,714,397**	8,078,185
Deferred income tax liabilities		
Property, plant and equipment	**(7,485,151)**	(3,627,320)
Deferred income tax, net	**11,229,246**	4,450,865

(a) The Company believes that it is probable that future operations will generate sufficient taxable income to realize the above-noted deferred tax assets.

The changes in the Company's net deferred income tax asset/liability for the year ended December 31 are as follows:

	2012	2011
	$	$
Opening net deferred income tax asset/liability	**4,450,865**	-
Income tax expense charged to earnings during the year	**6,588,391**	4,450,865
Foreign exchange	**189,990**	-
Ending net deferred income tax asset/liability	**11,229,246**	4,450,865

Deferred tax assets not recognized at the reporting date are summarized as follows:

	2012	2011
	$	$
Deferred income tax assets		
Tax loss carryforwards	**4,308,340**	19,163,298
Deductible temporary differences:		
Derivative financial instrument (financing warrants)	**588,222**	-
Financing costs	**679,656**	530,138
Other	**24,773**	263,541
	5,600,991	19,956,977

(Expressed in U.S. dollars)

12. Income taxes (continued)

At December 31, 2012, the Company has:

- Canadian income tax losses of approximately US$15,690,999 (2011 - US$12,048,000) that expire from 2015 through 2032;
- Australian loss carryforward of approximately US$45,008,518 (2011 - US$48,750,000) that can be carried forward indefinitely; and
- Chile loss carryforward of approximately US$2,004,418 (2011 - US$15,595,000) that can be carried forward indefinitely.

13. Administration expense

The administration expenses for the Company are broken down as follows:

	2012	2011
	$	$
Accounting and legal	**1,505,036**	1,043,697
Administrative and office	**10,029,828**	5,575,839
Consulting fee	**760,613**	347,912
Depreciation	**31,083**	33,346
Investor relations	**489,894**	337,639
Management fee	**1,459,106**	1,262,294
Travel and entertainment	**1,054,205**	677,341
	15,329,765	9,278,068

Included in cost of sales and administrative and office are the employee salary and benefit expenses of $27,557,335 and $3,400,893 (2011 - $20,462,897 and $1,867,874), respectively.

14. Finance costs

	2012	2011
	$	$
Interest on borrowings (Note 8 (a)(b)(d)(e))	**1,902,447**	1,837,546
Fair value adjustment on silver contract (Note 8 (c))	**453,413**	1,708,638
Accretion of reclamation and site closure costs (Note 9)	**1,062,357**	986,225
	3,418,217	4,532,409

15. Derivative financial instruments

(a) Silver and gold put options

The Company enters into certain silver put options and gold put options to hedge commodity price risks from time to time. The Company recorded a fair value measurement loss of $11,322,069 for the year ended December 31, 2012 (2011 – gain of $676,138).

The following table presents the costs and fair value of outstanding derivative financial instruments held by the Company as at December 31, 2011. As at December 31, 2012, no silver or gold put options were outstanding.

(Expressed in U.S. dollars)

15. Derivative financial instruments (continued)

(a) Silver and gold put options (continued)

		December 31, 2011	
	Maturity period	**Cost**	**Fair value**
		$	**$**
Silver			
50,000 ounces silver put option/month (450,000 ounces in total) at the price of $25 per ounce	April 2012 through to December 2012	**1,262,500**	**1,158,200**
100,000 ounces silver put option/month (1,200,000 ounces in total) at the price of $35 per ounce	January 2012 through to December 2012	**7,344,000**	**9,916,300**
70,000 ounces silver put option/month (840,000 ounces in total) at the price of $30 per ounce	January 2012 through to December 2012	**3,358,950**	**3,771,670**
Gold			
2,400 ounces gold put option/month (21,600 ounces in total) at the price of $1,400 per ounce	April 2012 through to December 2012	**2,469,600**	**1,407,598**
		14,435,050	**16,253,768**
Less: current portion			**16,253,768**
Non-current portion			**-**

(b) Financing warrants

During the year ended December 31, 2012, the Company reached an agreement to issue 3,050,000 warrants to specific service providers as consideration for financing and other services the Company received in prior years (“financing warrants”).

These financing warrants have an exercise price of $0.31 and expire on November 30, 2014. The service providers have the ability to require the Company to settle in cash, based on the Company’s share price at the date of settlement.

These financing warrants are accounted for as a liability and are marked to market at each period end until they are exercised or expire.

During the year ended December 31, 2012, 420,900 financing warrants were exercised with a cash settlement of $139,578, which is included in administration expense. As at December 31, 2012, 2,629,100 financing warrants valued at $2,219,707 (2011 - $Nil) are outstanding. The Company recorded a fair value measurement loss of $2,238,352 for the year ended December 31, 2012 (2011 - $Nil), which is reported in loss on derivative financial instruments.

(Expressed in U.S. dollars)

16. Income per share

As at December 31, 2012, the weighted average number of common shares for the purpose of calculating diluted income per share reconciles to the weighted average number of common shares used in the calculation of basic income per share as follows:

	2012	2011
Basic weighted average number of shares outstanding	**296,964,020**	251,213,123
Effective of dilutive securities		
Stock options	**8,906,486**	5,464,649
Warrants	**62,727,035**	44,268,706
Diluted weighted average number of shares outstanding	**368,597,541**	300,946,478

The following potential common shares, outstanding at December 31, 2012, are anti-dilutive and are therefore excluded from the weighted average number of common shares for the purposes of diluted income per share because the exercise price exceeded the daily weighted average market values of the common shares for the year ended December 31, 2012 of C$0.83 (2011 - C$0.73):

	2012	2011
Stock options	**4,052,000**	940,000

(Expressed in U.S. dollars)

17. Segmented information

The Company manages its operations by geographical location. These reportable operating segments are summarized in the table below:

	Year ended December 31, 2012			
	Australia	Canada	Chile	Total
	$	$	$	$
Revenue	59,137,784	-	112,667,839	171,805,623
Depletion and depreciation (including corporate office depreciation)	(6,044,275)	(31,084)	(13,295,161)	(19,370,520)
Income (loss) from operations	11,574,890	(5,194,380)	50,860,813	57,241,323
Other income (expense), except for fair value adjustment on silver contract and derivative financial instruments	(1,015,945)	(181,447)	(1,616,067)	(2,813,459)
Income (loss) for underlying operations	10,558,945	(5,375,827)	49,244,746	54,427,864
Income (loss) for underlying operations per share				
Basic				0.18
Diluted				0.15
Fair value adjustments				
Gain on derivative financial instruments (Note 15 (a))	(510,742)	-	(10,811,327)	(11,322,069)
Fair value adjustment on silver contract (Note 14)	-	-	(453,413)	(453,413)
Financing warrants (Note 15 (b))	-	(2,238,352)	-	(2,238,352)
Total fair value adjustment	(510,742)	(2,238,352)	(11,264,740)	(14,013,834)
Net income (loss) before income tax	10,048,203	(7,614,179)	37,980,006	40,414,030
Current tax expense	-	-	(5,290,064)	(5,290,064)
Deferred tax recovery (expense)	9,240,342	-	(2,651,951)	6,588,391
Net income (loss)	19,288,545	(7,614,179)	30,037,991	41,712,357
Income (loss) per share				
Basic				0.14
Diluted				0.11
Expenditures for property, plant and equipment	17,828,146	-	26,582,391	44,410,537
Total non-current assets as at December 31, 2012	60,498,104	10,124,343	53,465,203	124,087,650
Total assets as at December 31, 2012	67,775,143	14,855,980	102,659,561	185,290,684
Total liabilities as at December 31, 2012	8,684,116	3,787,557	29,740,113	42,211,786

(Expressed in U.S. dollars)

17. Segmented information (continued)

	Year ended December 31, 2011			
	Australia	Canada	Chile	Total
	$	$	$	$
Revenue	44,160,290	-	48,003,562	92,163,852
Depletion and depreciation (including corporate office depreciation)	(4,650,228)	(33,345)	(7,222,353)	(11,905,926)
Income (loss) from operations	7,482,388	(5,083,814)	15,762,589	18,161,163
Other income (expense), except for fair value adjustment on silver contract and derivative financial instruments	(917,378)	(1,197,036)	(987,797)	(3,102,211)
Income (loss) for underlying operations	6,565,010	(6,280,850)	14,774,792	15,058,952
Income (loss) for underlying operations per share				
Basic				0.06
Diluted				0.05
Fair value adjustments				
Gain on derivative financial instruments (Note 15 (a))	(125,258)	-	801,396	676,138
Fair value adjustment on silver contract (Note 14)	-	-	(1,708,638)	(1,708,638)
Total fair value adjustment	(125,258)	-	(907,242)	(1,032,500)
Net income (loss) before income tax	6,439,752	(6,280,850)	13,867,550	14,026,452
Deferred tax recovery	-	-	4,450,865	4,450,865
Net income (loss)	6,439,752	(6,280,850)	18,318,415	18,477,317
Income (loss) per share				
Basic				0.07
Diluted				0.06
Cash expenditures for property, plant and equipment	13,701,650	342,956	19,691,276	33,735,882
Total non-current assets as at December 31, 2011	35,930,967	113,489	49,937,801	85,982,257
Total assets as at December 31, 2011	42,930,340	5,765,576	90,198,942	138,894,858
Total liabilities as at December 31, 2011	10,163,642	8,595,715	21,164,535	39,923,892

For the year ended December 31, 2012, the Company had four customers from whom it earned more than 10% of its total revenue (2011 - three). Revenue from these customers is summarized as follows:

	2012	2011
	$	$
AGD (antimony and gold)		
Customer 1	**57,664,292**	44,092,992
	57,664,292	44,092,992
Cerro bayo (silver and gold)		
Customer 1	**38,169,250**	41,924,645
Customer 2	**24,151,158**	-
Customer 3	**50,344,788**	-
Customer 4	**-**	4,961,523
	112,665,196	46,886,168
Total	**170,329,488**	90,979,160

(Expressed in U.S. dollars)

18. Capital risk management

The Company manages its capital to ensure that it will be able to continue as a going concern while maximizing the return to stakeholders through the optimization of the debt and equity balance.

In the management of capital, the Company includes the components of shareholders' equity, long-term debt and net of the cash and cash equivalents.

Capital, as defined above, at December 31, 2012 and December 31, 2011 is summarized in the following table.

	2012	2011
	$	$
Shareholders' equity	**143,078,898**	98,970,966
Long-term debt	**-**	10,259,024
	143,078,898	109,229,990
Cash and cash equivalents	**(17,264,446)**	(12,741,454)
	125,814,452	96,488,536

The Company manages the capital structure and makes adjustments to it in light of changes in economic conditions and the risk characteristics of the underlying assets. To maintain or adjust the capital structure, the Company may attempt to issue new shares or purchase existing shares under the NCIB arrangements, issue new debt or pay down existing debt, or acquire or dispose of assets.

In order to facilitate the management of its capital requirements, the Company prepares annual budgets that are updated as necessary depending on various factors, including successful capital deployment and general industry conditions. The annual budget and quarterly updated forecasts are approved by the Board of Directors.

19. Financial risk management

The Company thoroughly examines the various financial instrument risks to which it is exposed and assesses the impact and likelihood of those risks. These risks may include credit risk, liquidity risk, currency risk, interest risk and commodity price risks. Where material, these risks are reviewed and monitored by the Board of Directors.

(a) Credit risk

Credit risk is the risk of an unexpected loss if a party to its financial instrument fails to meet its contractual obligations.

The Company's financial assets are primarily composed of cash and cash equivalents, reclamation deposits, derivative financial instrument and trade and other receivables. Credit risk is primarily associated with trade receivables and investments; however it also arises on cash and cash equivalents.

To mitigate exposure to credit risk, the Company has established policies to limit the concentration of credit risk, to ensure counterparties demonstrate minimum acceptable credit worthiness, and to ensure liquidity of available funds.

The Company closely monitors its financial assets and does not have any significant concentration of credit risk. The Company sells its antimony, silver and gold exclusively to large international organizations with strong credit ratings.

The historical level of customer defaults is minimal and, as a result, the credit risk associated with gold, silver and antimony trade receivables at December 31, 2012 is not considered to be high.

(Expressed in U.S. dollars)

19. Financial risk management (continued)

(a) Credit risk (continued)

The Company's maximum exposure to credit risk at December 31, 2012 and December 31, 2011, is as follows:

	2012	2011
	$	$
Cash and cash equivalents	**17,264,446**	12,741,454
Trade and other receivables	**29,175,603**	11,225,321
Reclamation and other deposits	**2,666,249**	2,431,941
	49,106,298	26,398,716

A significant portion of the Company's cash and cash equivalents is held in large Canadian financial institutions.

(b) Aging of past due, but not impaired receivables

The Company receives 90-95% of the estimated sales revenue of gold, silver, and antimony upon delivery. Final selling price is determined approximately 90-180 days after the delivery when smelting is complete. The remaining receivable balance is settled with an adjustment once the final selling price is determined which may be after 180 days. The Company has financial risk management policies in place to ensure that all receivables are received within the pre-agreed credit terms.

For the year ended December 31, 2012, substantially all of the Company's silver/gold/antimony production was sold to four customers (2011 - three) and there was no significant change in the credit quality of these customers over that time. Below is the information on the aging of the accounts receivable. There are neither past due amounts nor impaired trade receivables as at December 31, 2012 and 2011.

	2012	2011
	$	$
Less than 6 months	**23,862,301**	6,902,424
6 months or more	**1,972,470**	817,907
	25,834,771	7,720,331

(Expressed in U.S. dollars)

19. Financial risk management (continued)

(c) Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due. The Company manages liquidity risk through the management of its capital structure and has financial leverage as outlined in Note 18.

The following are the contractual maturities of commitments. The amounts presented represent the future undiscounted principal and interest cash flows and therefore do not equate to the carrying amounts on the consolidated statement of financial position.

					2012	2011
	Less than 1 year	**1-3 years**	**4-5 years**	**After 5 years**	**Total**	Total
	$	**$**	**$**	**$**	**$**	$
Trade and other payables	**18,218,862**	**-**	**-**	**-**	**18,218,862**	13,320,759
Borrowings	**-**	**-**	**-**	**-**	**-**	10,259,024
Interest payable on borrowings	**-**	**-**	**-**	**-**	**-**	677,975
	18,218,862	**-**	**-**	**-**	**18,218,862**	24,257,758

In the opinion of management, the working capital of $38,480,236 at December 31, 2012, which is the current assets, net of the current liabilities, together with expected positive cash flows from operations, are sufficient to support the Company's normal operating requirements through its current reporting period. However, taking into consideration the Company's current cash position, volatile equity markets, global uncertainty in the capital markets and increasing cost pressures, the Company is continuing to review expenditures in order to ensure adequate liquidity and flexibility to support its growth strategy while maintaining production levels at its current operations.

19. Financial risk management (continued)

(d) Currency risk

The Company operates in Canada, Australia, and Chile. As a result, the Company has foreign currency exposure with respect to items not denominated in U.S. dollars. The three main types of foreign exchange risk of the Company can be categorized as follows:

(i) *Exposure to currency risk*

The Company is exposed to currency risk through the following assets and liabilities denominated in currencies other than the U.S. dollar: cash and cash equivalents, trade and other receivables, trade and other payables, reclamation and other deposits and long-term debt. The currencies of the Company's financial instruments denominated in currencies other than U.S. dollars were as follows:

			2012
	Australian dollar	**Canadian dollar**	**Chilean peso**
Cash and cash equivalents	**3,075,805**	**1,023,168**	**605,415**
Trade and other receivables	**330,621**	**-**	**3,083,028**
Reclamation and other deposits	**2,666,249**	**-**	**-**
Trade and other payables	**(5,982,300)**	**(1,567,850)**	**(11,396,331)**
Long-term debt	**-**	**-**	**-**
Gross statement of financial position exposure	**90,375**	**(544,682)**	**(7,707,888)**

			2011
	Australian dollar	Canadian dollar	Chilean peso
Cash and cash equivalents	1,087,175	2,757,817	1,730,996
Trade and other receivables	339,885	367,086	2,639,856
Reclamation and other deposits	2,431,941	-	-
Trade and other payables	(5,705,907)	(468,233)	(5,279,488)
Long-term debt	(972,710)	(7,183,811)	-
Gross statement of financial position exposure	(2,819,616)	(4,527,141)	(908,636)

A 10% strengthening of the U.S. dollar against the Australian dollar, Canadian dollar and Chilean peso would have increased (decreased) the Company's net monetary assets (liabilities) by the amount of ($71,389) (2011 - $281,962) for the Australian dollar, $54,468 (2011 - $452,714) for the Canadian dollar and $770,789 (2011 - $90,864) for the Chilean peso. A weakening of the U.S. dollar would have an opposite impact of the same degree.

(ii) *Translation exposure*

The Company's presentation currency is U.S. dollars. The Company's operations translate their operating results from the functional currencies to U.S. dollars. Therefore, exchange rate movements in the Australian dollar, Canadian dollar and Chilean peso can have a significant impact on the Company's consolidated operating results.

19. Financial risk management (continued)

(e) Interest rate risk

Interest rate risk is the risk that the fair value or the future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The Company's exposure to interest rate changes is limited since its long-term debt instruments are based on fixed percentage interest rates and it has no long-term debt instruments as at December 31, 2012.

(f) Commodity price risk

The Company's earnings and cash flows are subject to price risk due to fluctuations in the market price of gold, silver, and antimony. World metal prices have historically fluctuated widely. World gold prices are affected by numerous factors beyond the Company's control, including:

- the strength of the U.S. economy and the economies of other industrialized and developing nations;
- global or regional political or economic crises;
- the relative strength of the U.S. dollar and other currencies;
- expectations with respect to the rate of inflation;
- interest rates;
- purchases and sales of gold by central banks and other holders;
- demand for jewelry containing gold, and/or silver;
- changes in industrial demand for silver and/or antimony;
- changes in supply of gold, silver, and/or antimony due to new mines being commissioned and existing minds being exhausted; and
- investment activity, including speculation, in gold, silver, and antimony as a commodities.

The Company is subject to price risk for fluctuations in the cost of energy, principally electricity and purchased petroleum products. The Company's production costs are also affected by the prices of materials it consumes or uses in its operations, such as lime, reagents and explosives. The prices of such commodities are influenced by supply and demand trends affecting the mining industry in general and other factors outside the Company's control.

20. Fair value measurement

The Company defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. In assessing the fair value of a particular contract, the market participant would consider the credit risk of the counterparty to the contract. Consequently, when it is appropriate to do so, the Company adjusts the valuation models to incorporate a measure of credit risk. Fair value represents management's estimates of the current market value at a given point in time.

(Expressed in U.S. dollars)

20. Fair value measurement (continued)

At December 31, 2012 and December 31, 2011, the Company's financial assets and liabilities are categorized as follows:

2012	**FVTPL**	**Loans and receivables**	**Other financial liability**	**Total**
	$	**$**	**$**	**$**
Financial assets				
Cash and cash equivalents	**-**	**17,264,446**	**-**	**17,264,446**
Trade receivables	**2,384,986**	**23,449,785**	**-**	**25,834,771**
Other receivables	**-**	**3,340,832**	**-**	**3,340,832**
Reclamation and other deposits	**-**	**2,666,249**	**-**	**2,666,249**
Financial liabilities				
Trade and other payables	**-**	**-**	**18,218,862**	**18,218,862**
Borrowings other than silver contract	**-**	**-**	**-**	**-**
Derivative financial instrument	**2,219,707**	**-**	**-**	**2,219,707**

2011	FVTPL	Loans and receivables	Other financial liability	Total
	$	$	$	$
Financial assets				
Cash and cash equivalents	-	12,741,454	-	12,741,454
Trade receivables	-	7,720,331	-	7,720,331
Other receivables	-	3,504,990	-	3,504,990
Reclamation and other deposits	-	2,431,941	-	2,431,941
Derivative financial instrument	16,253,768	-	-	16,253,768
Financial liabilities				
Trade and other payables	-	-	13,320,759	13,320,759
Silver contract	2,102,503	-	-	2,102,503
Borrowings other than silver contract	-	-	8,156,521	8,156,521

(Expressed in U.S. dollars)

20. Fair value measurement (continued)

At December 31, 2012 and December 31, 2011, the carrying values and the fair values of the Company's financial instruments are shown in the following table.

	2012			2011
	Carrying value	**Fair value**	Carrying value	Fair value
	$	**$**	$	$
Financial assets				
Cash and cash equivalents	**17,264,446**	**17,264,446**	12,741,454	12,741,454
Trade receivables	**23,449,785**	**23,449,785**	7,720,331	7,720,331
Other receivables	**3,340,832**	**3,340,832**	3,504,990	3,504,990
Reclamation and other deposits	**2,666,249**	**2,666,249**	2,431,941	2,431,941
Financial liabilities				
Trade and other payables	**18,218,862**	**18,218,862**	13,320,759	13,320,759
Borrowings other than silver contract	**-**	**-**	8,156,521	8,156,521

The Company has certain financial assets and liabilities that are measured at fair value. The fair value hierarchy establishes three levels to classify the inputs to valuation techniques used to measure fair value. Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities. Level 2 inputs are quoted prices in markets that are not active, quoted prices for similar assets or liabilities in active markets, inputs other than quoted prices that are observable for the asset or liability (for example, interest rate and yield curves observable at commonly quoted intervals, forward pricing curves used to value currency and commodity contracts and volatility measurements used to value option contracts), or inputs that are derived principally from or corroborated by observable market data or other means. Level 3 inputs are unobservable (supported by little or no market activity). The fair value hierarchy gives the highest priority to Level 1 inputs and the lowest priority to Level 3 inputs.

As at December 31, 2012, provisional pricing feature of trade receivables, derivative financial instruments and silver contract are based on Level 2 inputs.

The fair values of cash and cash equivalents, trade and other receivables (non-provisional pricing portion), reclamation and other deposits, and trade and other payables approximate their carrying value due to the nature of these items. Due to the nature of the liabilities, the fair values of borrowings other than silver contract are indeterminable.

21. Related party transactions

Key management personnel compensation

The remuneration of directors and other members of key management personnel during the year was as follows:

	2012	2011
	$	$
Salaries and short-term benefits	**1,409,939**	1,282,978
Share-based payments	**929,005**	456,477
	2,338,944	1,739,455

22. Commitments and contingencies

The Company is involved in legal proceedings from time to time, arising in the ordinary course of business. Typically, the amount of the ultimate liability with respect to these actions will not materially affect the Company's financial position, financial performance or cash flows.

23. Subsequent events

From January 1, 2013 to February 20, 2013.

On January 7, 2013, 1,647,000 financing warrants were exercised and the Company settled with a cash payment of $1,339,340.

On January 9, 2013, and January 14, 2013, 600,000 and 2,000,000 warrants were exercised, respectively, with an exercise price of C$0.47 and the total proceeds received was $1,227,833 (C$1,209,000).

On February 20, 2013, the Board of Directors declared a dividend in the amount of C$0.01 per share, payable on March 14, 2013 to shareholders of record as of March 7, 2013.