



## **AURCANA CORPORATION**

### **Consolidated Financial Statements**

**December 31, 2011**

**(Audited)**

Expressed in United States dollars unless otherwise stated

1750 - 1188 West Georgia Street, Vancouver BC V6E 4A2 CANADA

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## **Independent Auditor's Report**

### **To the Shareholders of Aurcana Corporation**

We have audited the accompanying consolidated financial statements of **Aurcana Corporation** (the "Company"), which comprise the consolidated statements of financial position as at December 31, 2011, December 31, 2010 and January 1, 2010 and the consolidated statements of operations, comprehensive income (loss), changes in equity and cash flows for the years ended December 31, 2011 and 2010, and the related notes, which comprise 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 the Company as at December 31, 2011, December 31, 2010 and January 1, 2010 and its financial performance and its cash flows for the years ended December 31, 2011 and 2010 in accordance with International Financial Reporting Standards.

*PricewaterhouseCoopers LLP*

**Chartered Accountants**

April 12, 2012

Vancouver, British Columbia

*PricewaterhouseCoopers LLP Chartered Accountants*

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**Aurcana Corporation**  
**Consolidated Statements of Financial Position**  
**(Expressed in United States dollars, unless otherwise stated)**

	Notes	December 31 2011	December 31 2010	January 1 2010
<b>Assets</b>				
<b>Current assets</b>				
Cash and cash equivalents	20	\$ 36,560,380	\$ 22,176,481	\$ 2,713,843
Trade and other receivable	4	3,451,158	1,795,700	1,246,299
Inventories	5	2,359,605	1,616,874	1,295,869
Short-term investments	6	383,481	975,238	1,088,800
Amounts receivable	7	942,616	-	-
Prepaid expenses and advances		403,999	89,514	265,517
		<b>44,101,239</b>	<b>26,653,807</b>	<b>6,610,328</b>
<b>Non Current assets</b>				
Amounts receivable	7	-	820,079	732,235
Property, plant and equipment	8	52,728,808	11,895,943	7,532,568
Mineral Properties	9	55,116,656	46,742,066	46,625,280
Deferred tax asset	10	1,304,810	1,239,324	-
Long term deposits		936,196	-	-
		<b>\$ 154,187,709</b>	<b>\$ 87,351,219</b>	<b>\$ 61,500,411</b>
<b>Liabilities</b>				
<b>Current liabilities</b>				
Accounts payable and accrued liabilities	11	\$ 9,193,574	\$ 4,318,474	\$ 4,150,315
Income tax	10	119,635	688,298	-
Convertible debentures	12	-	7,401,717	-
Current portion of long-term debt	13	1,150,164	236,661	1,323,893
		<b>10,463,373</b>	<b>12,645,150</b>	<b>5,474,208</b>
Deferred revenue	14	-	-	21,109,691
Convertible debentures	12	-	1,999,510	7,875,945
Long-term debt	13	1,668,123	-	2,277,252
Provision for environmental rehabilitation	15	2,738,587	1,396,514	1,273,141
		<b>14,870,083</b>	<b>16,041,174</b>	<b>38,010,237</b>
<b>Equity</b>				
Share capital	16	146,556,711	90,861,167	47,358,524
Contributed Surplus		28,440,706	23,075,899	8,388,348
Accumulated other comprehensive income (loss)		(2,262,183)	(1,552,567)	250,669
Deficit		(34,845,299)	(41,828,429)	(33,076,656)
<b>Total equity attributable to equity holders of the parent</b>		<b>137,889,935</b>	<b>70,556,070</b>	<b>22,920,885</b>
<b>Non-controlling interest</b>	17	<b>1,427,691</b>	<b>753,975</b>	<b>569,289</b>
<b>Total equity</b>		<b>139,317,626</b>	<b>71,310,045</b>	<b>23,490,174</b>
		<b>\$ 154,187,709</b>	<b>\$ 87,351,219</b>	<b>\$ 61,500,411</b>

Commitments (Note 19)

Subsequent event (Notes 28)

See accompanying notes to these consolidated financial statements.

Approved on behalf of the Board of Directors:

\_\_\_\_\_  
Director

\_\_\_\_\_  
Director

**Aurcana Corporation**  
**Consolidated Statements of Operations**  
(Expressed in United States dollars, unless otherwise stated)

	Notes	Years ended December 31,	
		2011	2010
<b>Revenues</b>			
Mining operations	22	\$ 45,882,178	\$ 26,144,936
<b>Costs of sales</b>			
Mining operating expenses	23	22,700,366	24,550,310
<b>Earnings from mine operations</b>		<b>23,181,812</b>	<b>1,594,626</b>
<b>Other items</b>			
Administrative costs	24	4,563,379	2,913,237
Financing expense and others	25	143,955	680,361
Stock-based compensation	16	7,811,935	264,588
Foreign exchange (gain) loss		271,200	(1,338,786)
Loss on termination of silver sale contract	14	-	7,570,872
Other expenses (income)		747,875	592,207
		<b>13,538,344</b>	<b>10,682,479</b>
<b>Income (loss) before income taxes</b>		<b>9,643,468</b>	<b>(9,087,853)</b>
Current Income tax expense	10	2,052,107	718,558
Deferred income tax (recovery) expense	10	(65,486)	(1,239,324)
<b>Net income (loss) for the year</b>		<b>\$ 7,656,846</b>	<b>\$ (8,567,087)</b>
<b>Attributable to:</b>			
Non-controlling interest		673,716	184,686
Equity holders of the Company		6,983,130	(8,751,773)
		<b>\$ 7,656,846</b>	<b>\$ (8,567,087)</b>
Weighted average number of shares – basic		351,308,109	137,836,536
Weighted average number of shares – diluted		421,434,690	137,836,536
<b>Net income (loss) per share – basic &amp; diluted</b>			
Basic		\$ 0.02	\$ (0.06)
Diluted		\$ 0.02	\$ (0.06)

See accompanying notes to these consolidated financial statements.

Aurcana Corporation  
**Consolidated Statements of Comprehensive Income (Loss)**  
**(Expressed in United States dollars, unless otherwise stated)**

	Notes	Years ended December 31,	
		2011	2010
<b>Net income (loss) for the year</b>		\$ 7,656,846	\$ (8,567,087)
Currency translation adjustment		(117,859)	(2,078,644)
Unrealized gain (loss) on Short-term investments	6	(591,757)	444,961
Effect of sale of short-term investments	6	-	(169,553)
<b>Comprehensive income (loss) for the year</b>		<b>6,947,231</b>	<b>(10,370,323)</b>
<b>Attributable to:</b>			
Non-controlling interest		673,716	184,686
Equity holders of the Company		6,273,515	(10,555,009)
		<b>\$ 6,947,231</b>	<b>\$ (10,370,323)</b>

*See accompanying notes to these consolidated financial statements.*

**Aurcana Corporation**  
**Consolidated Statements of Changes in Equity**  
**(Expressed in United States dollars, unless otherwise stated)**

	Share Capital	Contributed Surplus	Accumulated Other Comprehensive Income (Loss)	Deficit	Total Equity Attributable to Shareholders of the Company	Non-controlling Interest	Total Equity
<b>Balance, January 1, 2010</b>	\$ 47,358,524	\$ 8,388,348	\$ 250,669	\$ (33,076,656)	\$ 22,920,885	\$ 569,289	\$ 23,490,174
Currency translation adjustment	-	-	(2,078,644)	-	(2,078,644)	-	(2,078,644)
Unrealized gain (loss) on available for sale investments	-	-	444,961	-	444,961	-	444,961
Effect of sale of market securities	-	-	(169,553)	-	(169,553)	-	(169,553)
Net income (loss) for the year	-	-	-	(8,751,773)	(8,751,773)	184,686	(8,567,087)
Shares issued for:							
Private placement	46,789,623	14,133,525	-	-	60,923,148	-	60,923,148
Issuance of warrants (Trafigura)	-	380,783	-	-	380,783	-	380,783
Exercise of options	340,303	(97,244)	-	-	243,059	-	243,059
Exercise of warrants	587,294	(59,259)	-	-	528,035	-	528,035
Fair value of warrants issued	-	53,243	-	-	53,243	-	53,243
Fair value of finder fee warrants	-	11,915	-	-	11,915	-	11,915
Share issue costs	(4,214,577)	-	-	-	(4,214,577)	-	(4,214,577)
Stock-based compensation	-	264,588	-	-	264,588	-	264,588
<b>Balance, December 31, 2010</b>	90,861,167	23,075,899	(1,552,567)	(41,828,429)	70,556,070	753,975	71,310,045
Currency translation adjustment	-	-	(117,859)	-	(117,859)	-	(117,859)
Unrealized gain (loss) on available for sale investments	-	-	(591,757)	-	(591,757)	-	(591,757)
Net income (loss) for the year	-	-	-	6,983,130	6,983,130	673,716	7,656,846
Shares issued for:							
Private placement	29,126,036	4,455,440	-	-	33,581,476	-	33,581,476
Exercise of warrants	26,927,452	(6,156,764)	-	-	20,770,688	-	20,770,688
Exercise of options	1,858,459	(745,804)	-	-	1,112,655	-	1,112,655
Share issue costs	(2,216,403)	-	-	-	(2,216,403)	-	(2,216,403)
Stock-based compensation	-	7,811,935	-	-	7,811,935	-	7,811,935
<b>Balance, December 31, 2011</b>	\$ 146,556,711	\$ 28,440,706	\$ (2,262,183)	\$ (34,845,299)	\$ 137,889,935	\$ 1,427,691	\$ 139,317,626

See accompanying notes to these consolidated financial statements.

**Aurcana Corporation**  
**Consolidated Statements of Cash Flows**  
(Expressed in United States dollars, unless otherwise stated)

	Years ended	
	December 31, 2011	December 31, 2010
<b>Cash flows from operating activities</b>		
Net income (loss) for the year	\$ 7,656,846	\$ (8,567,087)
Items not involving cash:		
Depreciation, depletion and amortization	3,479,244	2,990,512
Accretion of amounts receivable	(122,537)	(87,844)
Financing expense and others	143,955	680,361
Stock-based compensation	7,811,935	264,588
Unrealized foreign exchange (gain) loss	582,236	(1,899,394)
Recognition of deferred revenue	-	(3,447,627)
Deferred Income Tax (recovery) expense	(65,486)	(1,239,324)
Loss on termination of silver sale contract	-	7,570,872
<b>Operating Cash Flow before movements in working capital items</b>	<b>19,486,193</b>	<b>(3,734,943)</b>
<b>Net change to non-cash working capital balances</b>		
Trade and other receivables	(1,655,458)	(549,401)
Inventories	(742,731)	(321,005)
Income Taxes Payable	(568,663)	688,298
Prepaid expenses and advances	(314,485)	176,003
Accounts payable and accrued liabilities	872,572	168,159
<b>Cash provided by operating activities</b>	<b>17,077,429</b>	<b>(3,572,889)</b>
<b>Cash flows from investing activities</b>		
Purchase of property, plant and equipment	(39,755,102)	(5,388,594)
Expenditures on mineral properties	(6,643,549)	(1,509,107)
Long term deposits	(936,196)	-
<b>Cash used in investing activities</b>	<b>(47,334,847)</b>	<b>(6,897,701)</b>
<b>Cash flows from financing activities</b>		
Share capital issued, net of share issue costs	53,248,416	57,925,606
Silver sale contract termination payment	-	(25,232,936)
Repayment of convertible debenture	(10,280,932)	-
Financing cost	(73,291)	(556,988)
Advances of notes payable, net	2,581,626	(3,364,484)
<b>Cash provided by (used in) financing activities</b>	<b>45,475,819</b>	<b>28,771,198</b>
<b>Increase in cash and cash equivalents</b>	<b>15,218,400</b>	<b>18,300,608</b>
<b>Effect of exchange rate changes on cash</b>	<b>(834,501)</b>	<b>1,162,030</b>
<b>Cash and cash equivalents, beginning of the year</b>	<b>22,176,481</b>	<b>2,713,843</b>
<b>Cash and cash equivalents, end of the year</b>	<b>\$ 36,560,380</b>	<b>\$ 22,176,481</b>

See accompanying notes to these consolidated financial statements

## **AURCANA CORPORATION**

### **Notes to Consolidated Financial Statements**

**(Expressed in United States dollars, unless otherwise stated)**

#### **1. Governing Statutes and Purpose of the Organization**

Aurcana Corporation (the "Company") was originally incorporated in Canada under the laws of Ontario in 1917 and on September 14, 1998 was continued under the *Canada Business Corporations Act* ("CBCA"). The Company is currently engaged in the production and sale of copper, silver, lead and zinc concentrates and the exploration, development and operation of natural resource properties. The Company's principal operating unit is the La Negra Mine, located in Queretaro State, Mexico and the Company's main developing property is the Shafter Silver Properties located in Presidio County, S.W. Texas.

The Company's shares are listed on the TSX Venture Exchange and the head office, principal address, and registered office is located at Suite 1750-1188 West Georgia Street, Vancouver, B.C., V6E 4A2, Canada.

#### **2. Basis of Preparation and adoption of International Financial Reporting Standards ("IFRS")**

The Company prepares its financial statements in accordance with Canadian generally accepted accounting principles as set out in the Handbook of the Canadian Institute of Chartered Accountants ("CICA Handbook"). In 2010, the CICA Handbook was revised to incorporate IFRS, and requires publicly accountable enterprises to apply such standards effective for years beginning on or after January 1, 2011. Accordingly, the Company has reported on this basis in these consolidated financial statements. In these financial statements, the term "Canadian GAAP" refers to Canadian GAAP before the adoption of IFRS.

These consolidated financial statements have been prepared in accordance with IFRS applicable to the preparation of financial statements, including IFRS 1. Subject to certain transition elections disclosed in Note 29 the Company has consistently applied the same accounting policies in its opening IFRS statements of financial position at January 1, 2010 and throughout all periods presented, as if these policies had always been in effect. Note 29 discloses the impact of the transition to IFRS on the Company's reported financial position, financial performance and cash flows, including the nature and effect of significant changes in accounting policies from those used in the Company's consolidated financial statements for the year ended December 31, 2010. Comparative figures for 2010 in these financial statements have been restated to give effect to these changes.

The policies applied in these condensed consolidated financial statements are based on IFRS issued and current as of December 31, 2011. The Audit Committee approved the statements on behalf of the Board of Directors on April 12, 2012.

#### **3. Summary of Significant Accounting Policies**

The consolidated financial statements have been prepared under the historical cost convention, except for the revaluation of certain financial instruments. The Company's principal accounting policies are outlined below:

##### *Basis of Consolidation*

The consolidated financial statements include the accounts of Aurcana Corporation and entities controlled by the Company ("its subsidiaries"). Control is achieved where the Company has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities.



## AURCANA CORPORATION

### Notes to Consolidated Financial Statements

(Expressed in United States dollars, unless otherwise stated)

#### 3. Summary of Significant Accounting Policies (continued)

These financial statements include the accounts of: Aurcana Corporation and its wholly-owned subsidiaries, Silver Assets Inc., a U.S. corporation, Cane Silver Inc., a Barbados corporation and Minera Aurcana S.A. de C.V., a Mexican corporation.

Real de Maconi S.A. de C.V. ("Maconi"), a Mexican corporation, is fully consolidated with the Company at 100% of profit or loss and assets and liabilities of Maconi, and recognizes an 8% non-controlling interest in the results of Maconi. Maconi substantively owns 100% of Minera La Negra S.A. de C.V. ("La Negra"), a Mexican Corporation, subject to one nominal share held by a second shareholder in order to comply with Mexican Company Law.

All significant intra-group balances and transactions are eliminated in full on consolidation.

#### Foreign Currency

The Company changed its presentation currency from Canadian dollars to US dollars effective January 1, 2011 (Note 29). In accordance with IAS 1 *Presentation of financial statements*, comparative information is also presented in US dollars.

##### *(i) Functional and Presentation Currency*

The financial statements of each entity in the Company group are measured using the currency of the primary economic environment in which each entity operates (the "functional currency"). The consolidated financial statements are presented in United States dollars.

The functional currency of Aurcana Corporation is the Canadian dollar, the functional currency of Silver Assets Inc. is the United States dollar and the functional currency of its Mexican subsidiaries is the United States dollar. The financial statements of the parent company are translated into the U.S. dollar presentation currency as follows:

- Assets and liabilities – at the closing rate at the date of the statement of financial position.
- Income and expenses – at the average rate of the period (as this is considered a reasonable approximation to actual rates).
- All resulting foreign exchange gains or losses are recognized in other comprehensive income as cumulative translation adjustments.

When the settlement of a monetary item receivable from or payable to a foreign operation is neither planned nor likely in the foreseeable future, foreign exchange gains and losses arising from the item are considered to form part of the net investment in a foreign operation and are recognized in other comprehensive income.

## AURCANA CORPORATION

### Notes to Consolidated Financial Statements

(Expressed in United States dollars, unless otherwise stated)

#### 3. Summary of Significant Accounting Policies (continued)

When an entity disposes of its entire interest in a foreign operation, or loses control, joint control, or significant influence over a foreign operation, the foreign currency gains or losses accumulated in other comprehensive income related to the foreign operation are recognized in profit or loss. If an entity disposes of part of an interest in a foreign operation which remains a subsidiary, a proportionate amount of foreign currency gains or losses accumulated in other comprehensive income related to the subsidiary are reallocated between controlling and non-controlling interests.

##### *(ii) Transactions and balances*

Foreign currency transactions are translated into the functional currency of an entity using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of foreign currency transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in currencies other than an operation's functional currency are recognized in the statement of income.

##### Stock-based Compensation

The Company grants stock options to buy common shares of the Company to directors, officers and employees. The Company records compensation expense under the plan for all options issued. The fair value of all stock-based awards is estimated using the Black-Scholes option pricing model at the grant date. The share-based compensation expense is recognized over the tranche's vesting period, in earnings or capitalized as appropriate, based on the number of options expected to vest. None of the Company's awards call for settlement in cash or other assets. Upon the exercise of the stock options, consideration paid together with the amount previously recognized in contributed surplus is recorded as an increase in share capital.

##### Mineral Properties

Mineral properties are stated at cost on a property-by-property basis. The recorded cost of mineral properties is based on acquisition costs incurred to date, less recoveries and write-offs.

Title to mineral properties, concessions, and shareholdings in Canada, U.S.A., Mexico, and Barbados involves certain inherent risks due to the difficulties of determining the validity of certain claims, as well as the potential for problems arising from the frequently ambiguous conveyance history and unregistered prior agreements. Management has investigated the titles to all of its concessions and shareholdings, and, to the best of its knowledge, believes they are in good standing.

##### *(i) Capitalization*

All direct and indirect costs relating to the acquisition and exploration of mineral properties are capitalized on a basis of specific claim blocks or areas of geological interest until the properties to which they relate are placed into production, sold, or when management has determined that there is impairment in the carrying values of those mineral properties. The Company capitalizes costs if it has the legal right to the mineral claim or the right to explore the area. Capitalized costs, net of any recoveries, are deferred until commercial production is achieved.

## AURCANA CORPORATION

### Notes to Consolidated Financial Statements

(Expressed in United States dollars, unless otherwise stated)

#### 3. Summary of Significant Accounting Policies (continued)

Costs associated with commissioning new assets, in the period before they are capable of operating in the manner intended by management, are capitalized. Development costs incurred on borrowings related to construction or development projects is capitalized until the point when substantially all the activities that are necessary to make the asset ready for its intended use are complete.

The application of the Company's accounting policy for exploration and evaluation expenditure requires judgment in determining whether it is likely that future economic benefit either from future exploration or sale or where activities have not reached a stage which permits a reasonable assessment of the existence of reserves. Management makes certain estimates and assumptions about future events or circumstances, in particular when an economically viable extraction operation can be established. Estimates and assumptions made may change if new information becomes available. If, after expenditure is capitalized, information becomes available suggesting that the recovery of expenditure is unlikely, the amount capitalized is written off in profit or loss in the period when the new information becomes available.

##### *(ii) Depreciation*

Amortization of mineral properties is based on the units-of-production basis, using estimated proven and probable reserves and the measured and indicated resources expected to be converted to proven and probable reserves, not to exceed the assets useful life. Properties are abandoned either when the lease expires or when management determines that no further work will be performed on the property since it has no value to the Company. When significant properties in an area of interest are abandoned, the costs related thereto are charged to income on a pro-rata basis to the total costs to date included in the area, in the year of abandonment.

Management's calculation of proven and probable reserves is based upon engineering and geological estimates and financial estimates including mineral prices and operating and development costs. The Company depreciates some of its assets over proven and probable mineral reserves. Changes in geological interpretations of the Company's ore bodies and changes in mineral prices and operating costs may change the Company's estimate of proven and probable reserves. It is possible that the Company's estimate of proven and probable reserves could change in the near term and that could result in revised charges for depreciation and depletion in future periods.

##### Property, Plant and Equipment

Property, plant and equipment are stated at cost less accumulated amortization and impairment losses. The cost capitalized is determined by the fair value of consideration given to acquire the asset at the time of acquisition or construction, the direct cost of bringing the asset to the condition necessary for operation, and the estimated future cost of dismantling and removing the asset.

##### *(i) Depreciation*

Mining machinery, plant and property are depleted on a unit of production basis, based on estimated recoverable reserves. Estimated recoverable reserves include proven and probable reserves and the portion of mineralized zones expected to be classified as reserves.

## AURCANA CORPORATION

### Notes to Consolidated Financial Statements

(Expressed in United States dollars, unless otherwise stated)

#### 3. Summary of Significant Accounting Policies (continued)

Other equipment is amortized on a straight-line basis over their estimated useful lives. Amortization begins when plant and equipment are put into use. The rates of amortization used are as follows:

Plant and equipment	Based on depletion over 5 years
Vehicles	25%
Computer Equipment	30%
Other	10-12%

The depreciation method, useful life and residual values are reviewed annually.

#### Impairment

##### *(i) Impairment for Mineral Properties*

The carrying values of mineral properties are reviewed by management for impairment annually, on a property-by-property basis. If indication of impairment exists, the asset's recoverable amount is estimated.

An impairment loss is recognized when the carrying amount of an asset, or its cash-generating unit, exceeds its recoverable amount. A cash-generating unit is the smallest identifiable group of assets that generates cash inflows that are largely independent of cash inflows from other assets or groups of assets. Impairment losses recognized in respects to cash-generating units are allocated to cash generating units, and then to reduce the carrying amount of the other assets in the unit on a pro-rata basis. Impairment losses are recognized in profit and loss for the period it is identified.

From time-to-time, the Company may acquire or dispose of a mineral property interest pursuant to the terms of an option agreement. As the options are exercisable entirely at the discretion of the optionee, the amounts payable or receivable are not recorded. Option payments are recorded as property costs or recoveries when the payments are made or received. When the amount of recoveries exceeds the total amount of capitalized costs of the property, the amount in excess of costs is credited to income.

##### *(ii) Impairment for Exploration and Evaluation Assets*

Management reviews the carrying amount of exploration and evaluation assets on an annual basis and recognizes impairment based on current exploitation results, and management's assessment of the probability of profitable exploitation at each property or realizable value from disposal of such property. If a project does not prove to be viable, all irrecoverable costs associated with the project net of any related impairment provisions are written off in the year.

Management's assessment of each property's estimated fair value is based on review of other mineral property transactions that have occurred in the same geographic area as that of the properties under review.

**AURCANA CORPORATION**  
**Notes to Consolidated Financial Statements**  
**(Expressed in United States dollars, unless otherwise stated)**

**3. Summary of Significant Accounting Policies (continued)**

*(iii) Reversal of Impairment*

An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. 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 or amortization, if no impairment loss has been recognized.

Inventories

Mine stores and finished concentrates are valued at the lower of average cost and net realizable value. Cost of finished concentrates inventory includes direct mining and production costs, direct mine overhead costs, amortization and depletion. Cost of sales includes costs of finished concentrates plus shipping costs less amortization and depletion, which is disclosed separately in the statement of operations.

Consumables and supplies, which consist of spare parts and consumable goods used for general repairs and maintenance, are recorded at the lower of cost and net realizable value.

Provisions

*(i) General*

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 a reliable estimate of the amount of the obligation can be made.

The expense relating to any provision is presented in profit or loss net of any reimbursement. Provisions are discounted using a current pre-tax rate that reflects where appropriate, the risks specific to the liability. Where discounting is used, the increase in the provision due to the passage of time is recognized as a finance cost.

*(ii) Environmental Rehabilitation*

The Company recognizes liabilities for statutory, contractual, constructive or legal obligations associated with the retirement of property, plant and equipment, when those obligations result from the acquisition, construction, development or normal operation of the assets. Such costs are discounted to their net present value and are provided for and capitalized at the start of each project, as soon as the obligation to incur such costs arises. These costs are charged against profits over the life of the operation, through the depreciation of the asset and the unwinding of the discount on the provision.

**AURCANA CORPORATION**  
**Notes to Consolidated Financial Statements**  
**(Expressed in United States dollars, unless otherwise stated)**

**3. Summary of Significant Accounting Policies (continued)**

Revenue

*(i) Revenue Recognition*

Revenue from the sale of precious metals is recognized upon delivery when significant risks and rewards of ownership of metal or metal-bearing concentrate passes to the buyer, probable that the economic benefits will flow to the Company, revenue can be reliably measured, and collection is reasonably assured. Revenue is measured at the fair value of the consideration received, excluding discounts, rebates, royalties and sales taxes or duty.

*(ii) Deferred Revenue*

Deferred revenue has been recognized to earnings over the estimated silver reserves on a per ounce of silver delivered basis.

Financial Assets

The Company classifies its financial assets in the following categories: fair value through profit or loss, held to maturity investments, available-for-sale financial assets, and loans and receivables. The classification depends on the nature and purpose for which the financial assets were acquired. Management determines the classification of financial assets at initial recognition.

*(i) Financial assets at fair value through profit or loss ("FVTPL")*

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 when it is purchased and incurred with the intention of generating profits in the near term, part of an identified portfolio of financial instruments that the Company manages and has actual pattern of short-term profit-taking; or 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 in the year in which the costs are incurred. The Company does not have any assets classified as FVTPL investments.

*(ii) Held to Maturity Investments*

Investments are measured at amortized cost using the effective interest rate method. Transaction costs are added and amortized to the statement of operations over the life of the financial instrument on an effective yield basis. The Company does not have any assets classified as held to maturity investments.

**AURCANA CORPORATION**  
**Notes to Consolidated Financial Statements**  
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**3. Summary of Significant Accounting Policies (continued)**

*(iii) Available-for-sale Financial Assets*

Financial assets classified as available-for-sale are carried at fair value (where determinable based on market prices of actively traded securities) with changes in fair value recorded in other comprehensive income. Available-for-sale securities are written down to fair value through earnings when there is objective evidence that a financial asset is impaired. The Company classifies short-term investments as available-for-sale financial assets.

*(iv) Loans and Receivables*

Loans and receivables are measured at amortized cost using the effective interest rate method. The Company has cash and cash equivalents, trade and other receivables classified as loans and receivables.

*(v) 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.

*(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.

Evidence of impairment may include indicators that the issuer or counterparty is experiencing significant financial difficulty, default or delinquency in interest or principal payments, or it has become probable that the borrower will enter bankruptcy or other financial reorganization.

Impairment for financial assets carried at amortized cost, is the difference between the asset's carrying amount 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. Uncollectible amounts in trade receivables are written off against the allowance account.

Available-for-sale financial assets are impaired if the cost (net of any principal payment and amortizations) is greater than the current fair value, less any impairment previously recognized in profit or loss. The impairment amount is transferred from equity to the income statement.

## AURCANA CORPORATION

### Notes to Consolidated Financial Statements

(Expressed in United States dollars, unless otherwise stated)

#### 3. Summary of Significant Accounting Policies (continued)

For all other financial assets carried at amortized cost in which impairment was previously recognized, if subsequent measurement indicates that the recorded impairment has decreased, and the decrease can be related objectively to an event occurring after the impairment was recognized, then the reversal of the impairment is recognized in the income statement. On the date of the impairment reversal, the carrying value of the financial asset cannot exceed its amortized cost had impairment not been recognized.

##### Financial Liabilities

Financial liabilities are classified as either financial liabilities at fair value through profit or loss ("FVTPL") or other financial liabilities. The Company does not have any financial liabilities at FVTPL.

##### *(i) Other Financial Liabilities*

Other financial liabilities are initially measured at fair value, net of transaction costs, and subsequently measured at amortized cost, with any resulting premium or discount from the face value being amortized to income or expense using the effective interest rate method.

The Company has classified short-term notes, convertible debentures, long-term debt, and accounts payable, and accrued liabilities as other financial liabilities.

##### *(ii) Derecognition of Financial Liabilities*

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

##### Derivatives

All derivative instruments are recorded on the balance sheet at fair value with changes in fair value recorded in the Statement of Operations.

Derivatives may be embedded in other financial instruments (host instruments). Embedded derivatives are treated as separate derivatives when their economic characteristics and risks are not closely related to those of the host instrument, the terms of the embedded derivative are the same as those of a stand-alone derivative, and the combined contract is not classified as held for trading. These embedded derivatives are measured at fair value on the balance sheet with subsequent changes in fair value recognized in income. The Company has not identified any embedded derivatives that are required to be accounted for separately from the host contract.

##### Cash and cash equivalents

Cash and cash equivalents include cash on hand, term deposits and short term highly liquid investments with the original term to maturity of three months or less, which are readily convertible to known amounts of cash and which, in the opinion of management, are subject to an insignificant risk of changes in value.



**AURCANA CORPORATION**  
**Notes to Consolidated Financial Statements**  
**(Expressed in United States dollars, unless otherwise stated)**

**3. Summary of Significant Accounting Policies (continued)**

Short-Term Investments

Short-term investments are classified as “available for sale”, and consist of highly liquid equity securities. These equity securities are initially recorded at fair value. Changes in the market value of these equity securities are recorded as changes to other comprehensive income or loss.

Income (Loss) Per Share

Basic income (loss) per share is computed by dividing the net income (loss) available to common shareholders by the weighted average number of shares outstanding during the reporting year. Diluted income (loss) per share is computed similar to basic income (loss) per share except that the weighted average shares outstanding are increased to include additional shares for the assumed conversion of debt and exercise of stock options and warrants, if dilutive. The number of additional shares is calculated by assuming that outstanding stock options and warrants were exercised and that the proceeds from such exercises were used to acquire common stock at the average market price during the reporting periods.

Income Taxes

Income tax expense comprises current and deferred tax. Current tax and deferred tax are recognized in profit or loss except to the extent that it relates to a business combination, or items recognized directly in equity or in other comprehensive income.

Current tax is the expected tax payable or receivable on the taxable income or loss for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax is recognized in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognized for the following temporary differences:

- the initial recognition of assets or liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable profit or loss; and

A deferred tax asset is recognized for unused tax losses, tax credits and deductible temporary differences, to the extent that it is probable that future taxable profits will be available against which they can be utilized. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realized.

Equity Instruments

The Company records proceeds from share issuances net of issue costs.

## AURCANA CORPORATION

### Notes to Consolidated Financial Statements

(Expressed in United States dollars, unless otherwise stated)

#### 3. Summary of Significant Accounting Policies (continued)

##### Use of Estimates and Judgments

The preparation of the condensed consolidated financial statements requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected.

Critical accounting estimates are estimates and assumptions made by management that may result in a material adjustment to the carrying amount of assets and liabilities within the next financial year and are as follows:

##### *(i) Environmental Rehabilitation Provision*

The Company's estimate on reclamation costs could change as a result of contractual requirements, laws or regulation, the extent of environmental remediation required or completed, and the means of reclamation or changes in cost estimate. These changes are recorded directly to mining assets with a corresponding entry to the rehabilitation provision. The Company's estimates are reviewed annually for changes in regulatory requirements, effects of inflation and changes in estimates.

##### *(i) Exploration and Evaluation Assets*

The application of the Company's accounting policy for exploration and evaluation expenditure requires judgment in determining whether future economic benefits are likely, which may be based on assumptions about future events or circumstances. Estimates and assumptions made may change if new information becomes available. If, after expenditure is capitalized, information becomes available suggesting that the recovery of expenditure is unlikely, the amount capitalized is recognized in loss in the period that the new information becomes available.

##### *(ii) Determination of Functional Currency*

In accordance with IAS 21, The Effects of Changes in Foreign Exchange Rates, management has determined that the functional currency of Aurcana Corporation is the Canadian dollar and its subsidiaries are the United States dollar.

##### *(iii) Units of Production Depreciation and Useful Life*

Estimated recoverable reserves are used in determining the amortization of mine specific assets. This results in an amortization charge proportional to the depletion of the anticipated remaining life of mine production.

## AURCANA CORPORATION

### Notes to Consolidated Financial Statements

(Expressed in United States dollars, unless otherwise stated)

#### 3. Summary of Significant Accounting Policies (continued)

Each asset's life is assessed annually and considerations are made in regards to both its physical life limitations and present assessments of economically recoverable reserves of the mine properties. Such calculations require the use of estimates and assumptions, including the amount of recoverable reserves and estimates of future capital expenditure. Changes are accounted for prospectively.

##### *(ii) Recovery of Deferred Tax Assets*

Judgment is required in determining whether deferred tax assets are recognized in the statement of financial position. Deferred tax assets, including those arising from un-utilized tax losses, require management to assess the likelihood that the Company will generate taxable earnings in future periods, in order to utilize recognized deferred tax assets. Estimates of future taxable income are based on forecast cash flows from operations and the application of existing tax laws in each jurisdiction. To the extent that future cash flows and taxable income differ significantly from estimates, the ability of the Company to realize the net deferred tax assets recorded at the date of the statement of financial position could be impacted.

Additionally, future changes in tax laws in the jurisdictions in which the Company operates could limit the ability of the Company to obtain tax deductions in future periods.

##### Recent Accounting Announcements

In May 2011, the IASB issued the following standards which have not yet been adopted by the Company: IFRS 9, *Financial instruments - Classification and Measurement*, IFRS 10, *Consolidated Financial Statements*, IFRS 11, *Joint Arrangements*, IFRS 12, *Disclosure of Interests in Other Entities*, IAS 27, *Separate Financial Statements*, IFRS 13, *Fair Value Measurement* and amended IAS 28, *Investments in Associates and Joint Ventures*. Each of the new standards is effective for annual periods beginning on or after January 1, 2013 with early adoption permitted, except IFRS 9, which is effective January 1, 2015. The Company has not yet begun the process of assessing the impact that the new and amended standards will have on its consolidated financial statements or whether to early adopt any of the new requirements.

The following is a brief summary of the new standards:

##### *IFRS 9, Financial Instruments: Classification and Measurement*

This is the first part of a new standard on classification and measurement of financial assets that will replace IAS 39, *Financial Instruments: Recognition and Measurement*. IFRS 9 has two measurement categories: amortized cost and fair value. All equity instruments are measured at fair value. A debt instrument is recorded at amortized cost only if the entity is holding the instrument to collect contractual cash flows and the cash flows represent principal and interest. Otherwise it is recorded at fair value through profit or loss.

##### *IFRS 10, Consolidated Financial Statements*

IFRS 10 requires an entity to consolidate an investee when it is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its control over the investee. Under existing IFRS, consolidation is required when an entity has the power to govern the

**AURCANA CORPORATION**  
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**3. Summary of Significant Accounting Policies (continued)**

financial and operating policies of an entity so as to obtain benefits from its activities. IFRS 10 replaces SIC-12 *Consolidation—Special Purpose Entities* and parts of IAS 27 *Consolidated and Separate Financial Statements*.

*IFRS 11, Joint Arrangements*

IFRS 11 requires a venturer to classify its interest in a joint arrangement as a joint venture or joint operation. Joint ventures will be accounted for using the equity method of accounting whereas for a joint operation the venture will recognize its share of the assets, liabilities, revenue and expenses of the joint operation. Under existing IFRS, entities have the choice to proportionately consolidate or equity account for interests in joint ventures. IFRS 11 supersedes IAS 31, *Interests in Joint Ventures*, and SIC-13, *Jointly Controlled Entities—Non-monetary Contributions by Venturers*.

*IFRS 12, Disclosure of Interests in Other Entities*

IFRS 12 establishes disclosure requirements for interests in other entities, such as joint arrangements, associates, special purpose vehicles and off balance sheet vehicles. The standard carries forward existing disclosures and also introduces significant additional disclosure requirements that address the nature of, and risks associated with, an entity's interests in other entities.

*IFRS 13 Fair Value Measurement*

IFRS 13 is a comprehensive standard for fair value measurement and disclosure requirements for use across all IFRS standards. The new standard clarifies that fair value is 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. It also establishes disclosures about fair value measurement. Under existing IFRS, guidance on measuring and disclosing fair value is dispersed among the specific standards requiring fair value measurements and in many cases does not reflect a clear measurement basis or consistent disclosures.

*IAS 19 – Employee Benefits*

In June 2011, the IASB issued an amended version of IAS 19, *Employee Benefits* ("IAS 19"). The amendments to IAS 19 are meant to improve the quality, transparency and comparability of information presented for post-employment benefits. For defined benefit plans, the amendments eliminate the option to defer actuarial gains and losses on the balance sheet through the "corridor method". The amendments also require any remeasurement gains or losses, including actuarial gains and losses, to be recognized immediately and presented in other comprehensive income, eliminating the option to recognize and present these through the income statement. Additional disclosures will also be required to present better information about the characteristics, amounts recognized, and risks related to defined benefit plans. The amendments to IAS 19 are effective for financial years beginning on or after January 1, 2013 with earlier adoption permitted. The Company has not yet begun the process of assessing the impact that the amended standard will have on its consolidated financial statements or whether to early adopt any of the new requirements.

**AURCANA CORPORATION**  
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**4. Trade and Other Receivable**

	<u>December 31</u> <u>2011</u>	<u>December 31</u> <u>2010</u>	<u>January 1</u> <u>2010</u>
Trade receivables	\$ 2,869,636	\$ 1,587,613	1,001,470
Other receivables	581,522	208,087	244,829
	<u>\$ 3,451,158</u>	<u>\$ 1,795,700</u>	<u>1,246,299</u>

**5. Inventories**

	<u>December 31</u> <u>2011</u>	<u>December 31</u> <u>2010</u>	<u>January 1</u> <u>2010</u>
Supplies inventory	\$ 1,540,244	\$ 1,045,367	\$ 1,091,611
Stockpile inventory	763,732	536,975	169,377
Concentrates and in-process	55,629	34,532	34,881
	<u>\$ 2,359,605</u>	<u>\$ 1,616,874</u>	<u>\$ 1,295,869</u>

During the year \$7,723,455 (2010 - \$6,951,965) of inventory was expensed in cost of sales.

**6. Short-term investments**

As partial consideration for the sale of Rosario (Note 7), Silvermex issued 1,000,000 common shares to the Company.

The 1,000,000 Silvermex shares are carried at fair market value based on quoted market prices as follows:

	<u>December 31,</u> <u>2011</u>	<u>December 31,</u> <u>2010</u>	<u>January 1</u> <u>2010</u>
Current portion:			
Balance beginning of the year	\$ 975,238	\$ 1,088,800	\$ 861,250
Proceeds from sale	-	(388,970)	-
Loss on sale of short-term investments	-	(169,553)	-
Unrealized (loss)gain	(591,757)	444,961	227,550
Balance end of the year	<u>\$ 383,481</u>	<u>\$ 975,238</u>	<u>\$ 1,088,800</u>

The unrealized loss on these securities has been recorded in other comprehensive income.

**7. Amounts Receivable**

On November 30, 2009, the Company sold its Rosario exploration and development project located in Sinaloa State, Mexico ("Rosario") to Silvermex Resources Inc. ("Silvermex") for cash and share consideration (Note 6) and recorded a loss of \$1,295,063 in the year ended December 31, 2009.

**AURCANA CORPORATION**  
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**7. Amount Receivable (continued)**

As part of the required cash consideration, the Company is to receive approximately \$1 million USD in two payments of \$500,000. The first payment is due by April 9, 2012 and the second payment is due by October 9, 2012. The carrying value of this receivable is calculated using a 12% discount rate and will be accreted up to its principal balance over the term of the receivable using the effective interest method. A summary of changes in accounts receivable is presented below:

	<u>December 31, 2011</u>	<u>December 31, 2010</u>	<u>January 1 2010</u>
Carrying value, January 1,	\$ 820,079	\$ 732,235	\$ 732,235
Accretion for the Period	<u>122,537</u>	<u>87,844</u>	<u>-</u>
Carrying value, December 31,	<u>\$ 942,616</u>	<u>\$ 820,079</u>	<u>\$ 732,235</u>

	<u>December 31, 2011</u>	<u>December 31, 2010</u>	<u>December 31, 2010</u>
Current	\$ 942,616	\$ -	\$ -
Non - Current	<u>-</u>	<u>820,079</u>	<u>732,335</u>
Carrying value, December 31,	<u>\$ 942,616</u>	<u>\$ 820,079</u>	<u>\$ 732,335</u>

**AURCANA CORPORATION**  
**Notes to Consolidated Financial Statements**  
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**8. Property, Plant and Equipment**

	Buildings	Plant and Equipment	Mine Development Cost	Exploration Properties	Vehicles	Computer Equipment	Other Assets under construction	Total
<b>Cost</b>								
Balance at January 1, 2010	\$ 425,467	\$ 7,872,178	\$ 242,646	\$ 183,384	\$ 438,425	\$ 318,646	\$ 47,064	\$ 9,527,810
Additions	241,776	2,463,441	2,449,759	138,289	155,240	48,654	63,807	5,388,593
Impairment	-	(172,373)	-	-	-	-	-	(172,373)
<b>Balance at December 31, 2010</b>	<b>667,243</b>	<b>10,163,246</b>	<b>2,692,405</b>	<b>321,673</b>	<b>593,665</b>	<b>367,300</b>	<b>110,871</b>	<b>14,916,403</b>
Additions	808,037	14,428,498	4,904,561	682,159	1,411,142	99,006	45,336	43,357,854
<b>Balance at December 31, 2011</b>	<b>\$ 1,475,280</b>	<b>\$ 24,591,744</b>	<b>\$ 7,596,966</b>	<b>\$ 1,003,832</b>	<b>\$ 2,004,807</b>	<b>\$ 466,306</b>	<b>\$ 156,207</b>	<b>\$ 20,979,115</b>
<b>Accumulated depreciation</b>								
Balance at January 1, 2010	\$ 5,307	\$ 1,676,197	\$ -	\$ -	\$ 154,908	\$ 153,422	\$ 5,409	\$ 1,995,242
Charge for the year	19,624	808,055	-	-	80,750	104,879	11,911	1,025,219
Balance at December 31, 2010	24,931	2,484,251	-	-	235,657	258,301	17,320	3,020,460
Charge for the year	-	2,100,709	207,232	-	124,127	52,165	12,618	2,524,990
<b>Balance at December 31, 2011</b>	<b>\$ 53,070</b>	<b>\$ 4,584,960</b>	<b>\$ 207,232</b>	<b>\$ -</b>	<b>\$ 359,784</b>	<b>\$ 310,466</b>	<b>\$ 29,938</b>	<b>\$ 5,545,450</b>
<b>Net book value</b>								
Balance at January 1, 2010	\$ 420,160	\$ 6,195,982	\$ 242,646	\$ 183,384	\$ 283,518	\$ 165,224	\$ 41,655	\$ 7,532,568
Balance at December 31, 2010	\$ 642,312	\$ 7,678,995	\$ 2,692,405	\$ 321,673	\$ 358,008	\$ 108,999	\$ 93,551	\$ 11,895,943
Balance at December 31, 2011	\$ 1,422,210	\$ 20,006,784	\$ 7,389,734	\$ 1,003,832	\$ 1,645,023	\$ 155,840	\$ 126,269	\$ 20,979,115

Mining and plant equipment and assets under construction, which are not in production, are not subject to amortization.

**AURCANA CORPORATION**  
**Notes to Consolidated Financial Statements**  
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**9. Mineral Properties**

<b>Cost</b>	La Negra	Shafter	<b>Total</b>
	Mexico	Texas	
	Producing mine	Mine under construction	
<b>Balance as at January 1, 2010</b>	\$ 12,717,017	\$ 39,080,658	\$ 51,797,675
Expenditures	-	195,335	195,335
Capitalized accretion (Note 12)	-	1,525,282	1,525,282
Capitalized interest expense	-	361,462	361,462
<b>Balance as at December 31, 2010</b>	12,717,017	41,162,737	53,879,754
Expenditures	-	6,643,549	6,643,549
Capitalized accretion and ARO (Note 12 & 15)	-	2,285,520	2,285,520
Capitalized interest expense	-	399,775	399,775
<b>Balance as at December 31, 2011</b>	\$ 12,717,017	\$ 50,491,581	\$ 63,208,598
<b>Accumulated depletion</b>			
<b>Balance as at January 1, 2010</b>	\$ 5,172,395	\$ -	\$ 5,172,395
Charge for the year	1,965,293	-	1,965,293
<b>Balance as at December 31, 2010</b>	7,137,688	-	7,137,688
Charge for the period	954,254	-	954,254
<b>Balance as at December 31, 2011</b>	\$ 8,091,942	\$ -	\$ 8,091,942
<b>Net book value</b>			
<b>Balance as at January 1, 2010</b>	\$ 7,544,622	\$ 39,080,658	\$ 46,625,280
<b>Balance as at December 31, 2010</b>	\$ 5,579,329	\$ 41,162,737	\$ 46,742,066
<b>Balance as at December 31, 2011</b>	\$ 4,625,075	\$ 50,491,581	\$ 55,116,656

La Negra Mine, Queretaro State, Mexico

In March 2006, the Company entered into an agreement with Reyna Mining & Engineering S.A. de C.V. ("Reyna") to operate the La Negra mine. The agreement was initially on the basis of an 80% held by the Company and 20% held by Reyna. During the year ended December 31, 2009, the Reyna's ownership interest was diluted to 8%. See also Note 28.

Shafter Silver Mine, Texas USA

On July 15, 2008, the Company closed the acquisition of 100% of the Shafter silver mine ("Shafter") from Silver Standard Resources Inc. ("Silver Standard"). Shafter is located in Presidio County, southwest Texas.



**AURCANA CORPORATION**

**Notes to Consolidated Financial Statements**

**(Expressed in United States dollars, unless otherwise stated)**

**9. Mineral Properties (continued)**

To acquire Shafter, Aurcana paid Silver Standard US\$23 million in cash; issued 15 million Aurcana common shares (fair value \$6,900,000); and issued a \$10 million convertible debenture paying a 3% coupon with a three year term and convertible into 6.62 million Aurcana common shares at \$1.51 per share (Note 12).

**10. Income Taxes**

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

	<u>2011</u>	<u>2010</u>
Earnings (loss) before income taxes	\$ 9,643,468	\$ (9,087,853)
Canadian federal and provincial income tax rates	26.5%	28.5%
Income tax expense (recovery) based on above rates	<u>2,555,519</u>	<u>(2,590,038)</u>
Increase (decrease) due to:		
Non-deductible (taxable) items and other items	2,466,974	(449,190)
Foreign exchange	1,204,678	-
Change in tax rate	-	64,724
Previously unrecognized tax losses	(3,822,760)	(1,239,324)
Other	62,342	-
Differences between foreign and Canadian tax rates	(1,420,079)	3,243,303
Losses and other deductions for which no benefit has been recognized	<u>939,947</u>	<u>449,760</u>
<b>Income tax (expense) recovery</b>	<u>\$ 1,986,621</u>	<u>\$ (520,765)</u>
The income tax (expense) recovery is comprised of:		
Current income tax expense	2,052,107	718,558
Future income tax recovery	(65,486)	(1,239,324)
<b>Income tax (expense) recovery</b>	<u>\$ 1,986,621</u>	<u>\$ (520,766)</u>
Income tax expense (recovery) by country:		
Mexico	\$ 4,190,249	\$ (520,766)
Canada	(2,203,628)	-
<b>Income tax (expense) recovery</b>	<u>\$ 1,986,621</u>	<u>\$ (520,766)</u>

**AURCANA CORPORATION****Notes to Consolidated Financial Statements****(Expressed in United States dollars, unless otherwise stated)****10. Income Taxes (continued)**

Significant components of deferred income tax assets (liabilities) are as follows:

	December 31, 2011	December 31, 2010
Non-capital losses	\$ 2,203,628	\$ -
Mineral properties	499,282	390,685
Asset retirement obligations	315,552	229,342
Accruals and other items	825,402	411,585
Property, plant and equipment	(2,539,054)	207,712
<b>Deferred income tax assets (liabilities)</b>	<b>\$ 1,304,810</b>	<b>\$ 1,239,324</b>
Represented on the balance sheet as:		
Deferred income tax assets, non-current	\$ 1,304,810	\$ 1,239,324
Deferred income tax liabilities, non-current	-	-
	<b>\$ 1,304,810</b>	<b>\$ 1,239,324</b>

The components of unrecognized deferred income tax assets are as follows:

Non-capital losses	\$ 2,294,858	\$ 4,793,355
Capital losses	1,243,074	1,271,050
Property, plant and equipment	4,118	44,640
Mineral property	1,936,038	1,979,609
Share issuance costs	1,114,839	996,076
Other items	14,750	-
	<b>\$ 6,607,677</b>	<b>\$ 9,084,730</b>

**AURCANA CORPORATION**

**Notes to Consolidated Financial Statements**

**(Expressed in United States dollars, unless otherwise stated)**

**10. Income Taxes (continued)**

As at December 31, 2011, the Company has tax losses for income tax purposes, which may be used to reduce future taxable income. The income tax benefit, if any, of these losses have not been recorded in these consolidated financial statements because of the uncertainty of their recovery. The future expiration and potential tax benefit of these losses is as follows:

<b>YEAR</b>	<b>USA</b>	<b>Canada</b>	<b>Barbados</b>	<b>Mexico</b>	<b>Total</b>
2012	\$ 601,936	\$ -	\$ -	\$ -	601,936
2018	541,863	-	-	-	541,863
2019	222,039	-	7,057,013	-	7,279,052
2020	33,069	-	-	312,054	345,123
2022	14,334	-	-	-	14,334
2023	11,956	-	-	-	11,956
2024	193,820	-	-	-	193,820
2025	100,952	-	-	-	100,952
2026	164,165	-	-	-	164,165
2027	148,444	-	-	-	148,444
2028	168,559	-	-	-	168,559
2029	414,262	-	-	-	414,262
2030	247,948	-	-	-	247,948
2031	2,921,844	-	-	-	2,921,844
Capital losses - no expiry	-	9,944,592	-	-	9,944,592
	<b>\$ 5,785,191</b>	<b>\$ 9,944,592</b>	<b>\$ 7,057,013</b>	<b>\$ 312,054</b>	<b>\$ 23,098,850</b>

Current income taxes payable:

	<b>December 31, 2011</b>	<b>December 31, 2010</b>
Current Income tax expense	\$ 2,052,107	\$ 718,558
Instalments	1,932,472	30,260
Income tax payable	<b>\$ 119,635</b>	<b>\$ 688,298</b>

**AURCANA CORPORATION**  
**Notes to Consolidated Financial Statements**  
**(Expressed in United States dollars, unless otherwise stated)**

**11. Accounts Payable and Accrued Liabilities**

	<b>December 31, 2011</b>	December 31, 2010	January 1, 2010
Silver arrears *	\$ -	\$ 185,295	\$ 1,290,234
Convertible debenture interest (Note 12)	-	186,205	175,832
Royalties	<b>1,236,338</b>	844,983	629,893
Salaries, source deductions and employee benefits	<b>904,420</b>	381,567	264,403
Employees' statutory profit sharing	<b>708,662</b>	642,763	315,061
Mine suppliers	<b>1,472,890</b>	1,209,404	548,680
Construction in progress suppliers	<b>3,602,753</b>	428,525	-
Other	<b>1,268,511</b>	439,732	926,212
	<b><u>\$ 9,193,574</u></b>	<b><u>\$ 4,318,474</u></b>	<b><u>\$ 4,150,315</u></b>

\*Represents 6,017 ounces of silver owed to Silver Wheaton at December 31, 2010 (paid in January 2011)

**12. Convertible Debenture**

In July 2008, the Company issued a convertible debenture to Silver Standard as part of the purchase price to acquire Shafter (Note 9). The convertible debenture was unsecured, had a CDN\$10 million face value, bore interest at 1.5% per annum for the first year and 4% per annum for the 2 following years, was convertible into common shares of the Company at CDN\$1.51 per share and was due in full on July 15, 2011.

Under IFRS, the Company recorded the fair value of the conversion option on the residual basis at \$2,864,729 and recorded this amount in "contributed surplus". The convertible liability was discounted by 12% to yield an effective interest rate of 12% on the debt portion of the instrument. The Company capitalized the interest and the accretion expense to Shafter, the purchase of which was financed by the convertible debenture.

In April 2011, the terms of the debenture were amended. Under the terms of the amended Convertible Debenture:

- The maturity date of the Debenture was extended from July 15, 2011 to July 15, 2012;
- The Company agreed to repay an aggregate of CDN\$7,000,000 of the principal owing under the Debenture on or before July 15, 2011 (paid \$7,335,220); the remaining CDN\$3,000,000 principal balance was to be repaid in equal quarterly instalments of CDN\$750,000 per quarter commencing on October 15, 2011 (paid \$742,207);
- The rate of interest on the principal outstanding after July 15, 2011 was 9% per annum; and
- The Company could prepay the Debenture at any time prior to maturity without penalty.

On December 22, 2011 the Company paid out in advance the final balance in the amount of CDN\$2,250,000 (\$2,203,506).

**AURCANA CORPORATION**  
**Notes to Consolidated Financial Statements**  
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**12. Convertible Debenture (continued)**

Details are as follows:

Balance, January 1, 2010	\$ 7,875,945
Accretion for the year	<u>1,525,282</u>
Balance, December 31, 2010	9,401,227
Payment July 15, 2011	(7,335,220)
Payment October 15, 2011	(742,207)
Payment December 22, 2011	(2,203,506)
Realized foreign exchange loss	280,932
Accretion to December 22, 2011	<u>598,773</u>
Balance, December 31, 2011	<u>-</u>
Current portion	\$ 7,401,717
Non - current	<u>1,999,510</u>
Balance, December 31, 2010	<u>\$ 9,401,227</u>
Current portion	-
Non - current	<u>-</u>
Balance, December 31, 2011	<u>-</u>

**AURCANA CORPORATION**  
**Notes to Consolidated Financial Statements**  
**(Expressed in United States dollars, unless otherwise stated)**

**13. Current and Long-term Debt**

	<u>December 31 2011</u>	<u>December 31 2010</u>	<u>January 1 2010</u>
Atlas Copco - Capital equipment contracts, repayable in quarterly payments totalling US\$60,000 at 8.78% per annum, maturing December 2011 and secured by the	\$ -	\$ 236,661	\$ 588,645
Notes payables to the Company's principal customer, repayable in monthly instalments totalling US\$80,000; bearing interest at LIBOR plus 2% per annum	-	-	3,012,499
Sandvik - Capital equipment contracts, repayable in monthly payments totalling US\$20,098 at 7.9% per annum, maturing December 2014	<b>743,196</b>	-	-
Sandvik - Capital equipment contracts, repayable in monthly payments totalling US\$74,111 at 8.9% per annum, maturing April 2014	<b>2,075,091</b>	-	-
<b>Total</b>	<b><u>\$ 2,818,287</u></b>	<b><u>\$ 236,661</u></b>	<b><u>\$ 3,601,145</u></b>
Current portion	<b>\$ 1,150,164</b>	\$ 236,661	\$ 1,323,893
Long-term debt	<b><u>1,668,123</u></b>	<u>-</u>	<u>2,277,252</u>
	<b><u>\$ 2,818,287</u></b>	<b><u>\$ 236,661</u></b>	<b><u>\$ 3,601,145</u></b>

Schedule principal repayments are as follows:

2012	<b>\$ 1,150,164</b>
2013	<b>1,130,503</b>
2014	<b>537,620</b>
	<b><u>\$ 2,818,287</u></b>

The net book value of the assets in note 8 under capital lease is \$4,186,185

**14. Deferred Revenue**

In June 2008, the Company agreed to sell to Silver Wheaton (Caymans) Ltd. ("Silver Wheaton") 50% of the silver metal produced from ore extracted during the mine-life at La Negra under a Silver Stream Purchase Agreement ("SPA"). The SPA was made in consideration of a prepayment to Cane Silver Inc., a 100% owned subsidiary of the Company, of US\$25 million in cash. A fee per ounce of silver of US\$3.90 was also payable to Cane.

**AURCANA CORPORATION**  
**Notes to Consolidated Financial Statements**  
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**14. Deferred Revenue (continued)**

During the year ended December 31, 2010 the Company negotiated the termination of the SPA in consideration of a \$US 25 million payment (paid) and recorded a loss on termination of \$7,570,872. The Company also agreed to deliver sufficient silver to repay the amount accrued for silver deliveries in arrears to Silver Wheaton in the amount of 212,017 ounces, of which 206,000 ounces were delivered in December 2010 and 6,017 ounces were delivered in January 2011 (Note 10). The termination of the SPA eliminated the Company's obligation to deliver 50% of its future silver production to Silver Wheaton.

Details are as follows:

Balance, January 1, 2010	\$ 21,109,691
Recognized	(3,447,627)
Contract termination	<u>(17,662,064)</u>
Balance, December 31, 2010	\$ -
<b>Balance, December 31, 2011</b>	<b><u>\$ -</u></b>

Loss on termination of silver sale agreement:	
Termination payment	\$ 25,000,000
Deferred revenue balance at termination	(17,662,064)
Legal fees	<u>232,936</u>
Loss on termination	<b><u>\$ 7,570,872</u></b>

Loss for trading activity, net	<u>2010</u>
--------------------------------	-------------

Sales earned from Silver Wheaton (US\$3.90/ounce)	\$ 1,674,825
Recognition of deferred revenue (Note 11)	<u>3,641,671</u>
	5,316,496
Cost of sales (at market price)	(10,512,311)
Loss from trading activity in CDN	<u>\$ (5,195,815)</u>
Loss from trading activity in USD	<b><u>\$ (5,043,058)</u></b>

**AURCANA CORPORATION****Notes to Consolidated Financial Statements****(Expressed in United States dollars, unless otherwise stated)****15. Provision for Environmental Rehabilitation**

The Company has accrued an estimated liability related to reclamation and closure costs at the La Negra Mine based on the total future remediation cost, discounted to December 31, 2011 using a 6.35% discount factor (December 31, 2010 - 5.0% and January 1, 2010 - 5.0%) and a 3.41% inflation factor (December 31, 2010: 2.5% and January 1, 2010: 2.5%), in the amount of \$1,467,178 (December 31, 2010 - \$1,396,514 and January 1, 2010 - \$1,273,141).

The Company has accrued an initial estimated liability related to reclamation and closure costs at the Shafter mine based on the total future remediation cost, discounted to December 31, 2011 using a 2.0% discount factor and a 3.2% inflation factor, in the amount of \$1,271,409 (December 31, 2010 - \$nil and January 1, 2010 - \$nil).

The liability is subject to revision based on future mine resource realization, and other factors which affect the costs incurred at future dates.

The provision for environment rehabilitation for the years ended December 31, 2010 and 2011 are as follows:

	<b>December 31 2011</b>	December 31 2010
Environmental rehabilitation, beginning of the year	\$ 1,396,514	\$ 1,273,141
Addition	1,271,409	-
Accretion	70,664	123,373
Environmental rehabilitation, end of the year	<u>\$ 2,738,587</u>	<u>\$ 1,396,514</u>

**16. Equity**

Authorized - An unlimited number of common shares

Share issuance details:

	Number of Shares	Amount
<b>Balance, January 1, 2010</b>	120,171,660	\$ 47,358,524
Issued pursuant to private placement	200,033,380	46,789,623
Share issuance costs	-	(4,214,577)
Exercised warrants	1,574,908	587,294
Exercised options	1,075,000	340,303
<b>Balance, December 31, 2010</b>	322,854,948	\$ 90,861,167
Issued pursuant to private placement	52,853,000	29,126,036
Share issuance costs	-	(2,216,403)
Exercised warrants	51,713,455	26,927,452
Exercised options	3,345,000	1,858,459
<b>Balance, December 31, 2011</b>	<u>430,766,403</u>	<u>\$ 146,556,711</u>



## AURCANA CORPORATION

### Notes to Consolidated Financial Statements

(Expressed in United States dollars, unless otherwise stated)

#### 16. Equity (continued)

On November 15, 2011, Aurcana completed its private placement financing. The private placement offering (the "Offering") of units ("Units") was conducted through a syndicate of agents led by RBC Capital Markets and included, BMO Capital Markets, Dundee Securities Ltd. and Stonecap Securities Inc. (the "Agents"). Pursuant to the Offering, Aurcana sold an aggregate 52,853,000 Units at a price of CDN\$0.65 per Unit for aggregate gross proceeds of approximately CDN\$34.4 million (\$33.6 million).

Each Unit consists of one common share in the capital of the Company (the "Unit Shares") and one half of one common share purchase warrant (each whole warrant, a "Warrant"). Each full Warrant will entitle the holder, on exercise, to purchase one additional common share of the Company (a "Warrant Share"), at a price of CDN\$1.00 at any time until the close of business on the day which is 24 months from the date of issue of the Warrant. All securities issued in connection with the Offering are subject to a hold period in Canada expiring on March 30, 2012.

On December 7, 2010, the Company completed a fully subscribed Equity Offering (the "Offering"). The Company has issued 193,548,387 units (the "Units") at a purchase price of CDN\$0.31 per Unit for gross proceeds of CDN\$60,000,000. Each Unit consists of one common share (a "Share") of the Company and one half of one common share purchase warrant. Each whole common share purchase warrant (a "Warrant") permits the holder thereof to purchase a further common share (a "Warrant Share") of the Company for a period of 36 months from the closing of the Offering at a purchase price of CDN\$0.41 per Warrant Share. Sunel Securities Inc., its US placement agent, Sunrise Securities Corp. and its sub-agents (collectively, the "Agent") acted as lead agent on the Offering. The Company paid to the Agent a cash commission of CDN\$3,969,674, representing 7% of the gross proceeds of the Offering generated by the Agent, and issued to the Agent 12,805,262 compensation options (the "Compensation Options"), which is equal to 7% of the number of Units sold by the Agent pursuant to the Offering. Each Compensation Option is exercisable into one broker's unit (a "Broker's Unit") at a price of CDN\$0.41 per Broker's Unit for a period of 24 months from the closing date of the Offering. Each Broker's Unit consists of one common share in the capital of the Company and one-half of one common share purchase warrant (each whole common share purchase warrant, a "Broker's Warrant"). Each Broker's Warrant entitles the holder to purchase one common share in the capital of the Company (a "Broker's Warrant Share") for a period of 24 months from the closing of the Offering at a purchase price of CDN\$0.41 per Broker's Warrant Share. In addition, the Company paid commissions of CDN\$13,020 cash and issued 42,000 warrants ("Compensation Warrant") Each Compensation Warrant entitles the holder to purchase one common share in the capital of the Company (a "Compensation Share") for a period of 24 months from the closing of the Offering at a purchase price of CDN\$0.41 per Compensation Warrant Share.

On July 5, 2010 and July 26, 2010, the Company completed the second and third tranches of the Financing by issuing 720,000 and 340,000 units, respectively, for gross proceeds of CDN\$265,000. The units issued were under the same terms as the Units.

On June 30, 2010, the Company completed the first tranche of a non-brokered private placement by issuing 5,425,000 units (each a "Unit") at a price of CDN\$0.25 per Unit, for gross proceeds of CDN\$1,356,250 (the "Financing"). Each Unit consisted of one common share of the Company and one common share purchase warrant (each a "Warrant"), with each warrant entitling the holder to purchase one common share of the Company at a price of CDN\$0.40 per share expiring on June 30, 2013. Cash of CDN\$12,600 was accrued and 50,400 warrants on the same terms as the Warrants were issued as Finders' fees.

**AURCANA CORPORATION**  
**Notes to Consolidated Financial Statements**  
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**16. Equity (continued)**

Stock options

On June 29, 2011, the Company adopted a new fixed option plan (the "New Plan"), pursuant to which the Company may grant up to 34,698,803 stock options to directors, officers, employees and consultants. The exercise price, term and vesting period of each option are determined by the board of directors within regulatory guidelines.

<u>Stock options</u>	Number of Share Options	Weighted Average Exercise Price per Share
<b>Balance, January 1, 2010</b>	12,012,500	\$ 0.45
Granted	1,500,000	0.29
Forfeited	-	-
Exercised	(1,075,000)	0.23
Expired or cancelled	(1,400,000)	1.02
	<hr/>	
<b>Balance, December 31, 2010</b>	11,037,500	0.38
Granted	21,925,000	0.72
Exercised	(3,345,000)	0.30
Forfeited, expired or cancelled	(1,750,000)	0.88
<b>Balance, December 31, 2011</b>	<hr/> <hr/>	<hr/> <hr/>
	27,867,500	\$ 0.62

**AURCANA CORPORATION****Notes to Consolidated Financial Statements****(Expressed in United States dollars, unless otherwise stated)****16. Equity (continued)**

The Company's weighted average share price on the date the options were exercised during the year ended December 31, 2011 is as follow:

<b>Date of exercise</b>	<b>Number of options</b>	<b>Share price CDN\$ on date of exercise</b>
February 22, 2011	100,000	0.85
August 15, 2011	200,000	0.71
August 23, 2011	500,000	0.70
July 19, 2011	300,000	0.74
January 12, 2011	150,000	0.68
February 22, 2011	200,000	0.85
January 14, 2011	200,000	0.62
January 21, 2011	50,000	0.56
November 10, 2011	150,000	0.76
November 10, 2011	20,000	0.76
July 7, 2011	300,000	0.73
March 3, 2011	25,000	0.98
January 12, 2011	150,000	0.68
April 7, 2011	150,000	0.86
July 19, 2011	225,000	0.74
January 12, 2011	200,000	0.68
January 5, 2011	50,000	0.74
February 3, 2011	25,000	0.70
February 15, 2011	100,000	0.72
January 27, 2011	200,000	0.63
February 3, 2011	50,000	0.70
<b>Total/weighted average for the year ended December 31, 2011</b>	<b>3,345,000</b>	<b>\$ 0.72</b>

**AURCANA CORPORATION****Notes to Consolidated Financial Statements****(Expressed in United States dollars, unless otherwise stated)****16. Equity (continued)**

As determined by the "Black - Scholes Model", the weighted average fair value of the stock options granted during 2011 was CDN\$0.39 per share.

As of December 31, 2011 details of outstanding stock options are as follows:

Outstanding	Vested	Exercise Price (CDN\$)	Expiry Date
462,500	462,500	\$ 1.5000	March 22, 2012
150,000	150,000	\$ 1.6500	March 30, 2012
100,000	100,000	\$ 0.6400	December 12, 2012
150,000	150,000	\$ 0.5800	May 15, 2013
725,000	725,000	\$ 0.3100	September 9, 2013
350,000	350,000	\$ 0.1300	January 16, 2014
2,780,000	2,780,000	\$ 0.1000	August 13, 2014
1,025,000	1,025,000	\$ 0.2850	December 18, 2014
700,000	700,000	\$ 0.2750	February 12, 2012
350,000	350,000	\$ 0.2500	July 5, 2015
350,000	350,000	\$ 0.6100	January 14, 2016
150,000	150,000	\$ 0.6900	May 30, 2016
8,250,000	7,000,000	\$ 0.7600	February 22, 2016
250,000	187,500	\$ 0.8600	March 18, 2012
75,000	56,250	\$ 0.7600	May 4, 2016
10,300,000	5,150,000	\$ 0.6900	May 30, 2016
150,000	150,000	\$ 0.7900	September 12, 2016
1,100,000	137,500	\$ 0.6700	September 27, 2016
450,000	-	\$ 0.7000	December 5, 2016
<u>27,867,500</u>	<u>19,973,750</u>		

The weighted average exercise price of vested options at December 31, 2011 is \$0.59 per option. The above options expiring on March 22 and 30, 2012 expired unexercised.

**AURCANA CORPORATION**  
**Notes to Consolidated Financial Statements**  
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**16. Equity (continued)**

Stock-based compensation

For the year ended December 31, 2011 the stock-based compensation expense was \$7,811,935 (December 31, 2010 - \$264,588) . The fair value of share options issued as per above is calculated using "Black - Scholes model" following weighted average assumptions:

	<u>December 31, 2011</u>	<u>December 31, 2010</u>
Risk-free interest rate	2.14%	1.91%
Expected stock price volatility	86.79%	85.08%
Expected dividend yield	0.00%	0.00%
Expected option life in years	4.3	3.7

<u>Share purchase warrants</u>	Number of Share Warrants
<b>Balance, January 1, 2010</b>	6,208,560
Issued pursuant to private placements	103,259,172
Issued to Auramet (i)	300,000
Issued as finders' fee	108,000
Issued to Trafigura (ii)	2,125,203
Issued as agents' fee (iii)	12,847,402
Exercised	<u>(1,574,908)</u>
<b>Balance, December 31, 2010</b>	123,273,429
Issued pursuant to private placements	28,133,877
Exercised	(51,713,455)
Expired	<u>(364,181)</u>
<b>Balance, December 31, 2011</b>	<u>99,329,670</u>

- (i) During the year ended December 31, 2010, and pursuant to an advisory agreement, the Company issued 300,000 share purchase warrants to Auramet Trading, LLC ("Auramet") at a fair value of \$55,375. Each warrant is exercisable into one common share of the Company at an exercise price of \$0.35 per share. The warrants expire on March 2, 2013.
- (ii) During the year ended December 31, 2010, the Company extended the original due date of the note payable to Trafigura Beheer B.V. ("Trafigura") and issued 2,125,203 share purchase warrants to Trafigura at a fair value of \$ 392,317 as compensation for the extension. The remaining balance of the loan was fully repaid in the year ended December 31, 2010 (Note 13).
- (iii) In this total are 12,805,262, which allow the holder to acquire one common share and one-half of a share purchase warrant for a period of 24 months from the closing date of the Offering at CDN \$0.41.

**AURCANA CORPORATION****Notes to Consolidated Financial Statements****(Expressed in United States dollars, unless otherwise stated)****16. Equity (continued)**

As of December 31, 2011 details of outstanding warrants are as follows:

Number of Warrants	Exercise Price (CDN)	Expiry Date
4,511,000	\$ 0.40	June 30, 2013
24,960	\$ 0.35	June 30, 2013
58,326,566	\$ 0.41	December 12, 2013
10,040,644	\$ 0.41	December 12, 2012
<u>26,426,500</u>	\$ 1.00	November 29, 2013
<u><u>99,329,670</u></u>		

The fair value of share purchase warrants issued as per above is calculated using "Black - Scholes model" following weighted average assumptions:

	<u>December 31, 2011</u>	<u>December 31, 2010</u>
Risk-free interest rate	1.02%	1.27%
Expected stock price volatility	75.92%	115.92%
Expected dividend yield	n/a	0.00%
Expected warrant life in years	1.9	1.9

**Capital management**

The Company's objectives when managing capital are to safeguard its ability to continue as a going concern in order to pursue the development of its mineral properties and to maintain a flexible capital structure which optimizes the cost of capital at an acceptable risk.

In the management of capital, the Company includes the components of shareholders' equity.

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 its capital structure, the Company may attempt to issue new shares, issue debt and acquire or dispose of assets.

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

In order to maximize ongoing development efforts, the Company does not pay dividends.

The Company's investment policy is to limit investments to guaranteed investment certificates, banker's acceptance notes, investment savings accounts or money market funds with high quality financial institutions in Canada and treasury bills, selected with regards to the expected timing of expenditures from operations.

**AURCANA CORPORATION**  
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**17. Non-Controlling Interest**

The non-controlling interest is comprised of the following:

<b>Balance, January 1, 2010</b>	\$ 569,289
Non-controlling interest's share of profit in La Negra Mine	<u>184,686</u>
<b>Balance, December 31, 2010</b>	753,975
Non-controlling interest's share of profit in La Negra Mine	<u>673,716</u>
<b>Balance, December 31, 2011</b>	<u><u>\$1,427,691</u></u>

**18. Related Party Transactions**

Except as noted elsewhere in these condensed consolidated financial statements, the Company conducted the following related party transactions:

a) Trading transactions

The Company's related parties consist of companies owned by executive officers and directors and payments to these parties are as follows:

	Note	December 31 2011	December 31 2010
Technical and consulting fees	(i)	\$ 535,533	\$ 376,399
General and administrative expenses	(ii)	121,204	129,562
Management fees	(iii)	849,235	414,563
Related party transactions fees		<u>\$ 1,505,972</u>	<u>\$ 920,524</u>

(i) To companies controlled by officers or directors.

(ii) To a company controlled by corporate secretary for management services performed as an officer.

(iii) To a company controlled by President & CEO for management services performed.

b) Compensation of key management personnel

	December 31 2011	December 31 2010
Related party transactions fees	\$ 1,505,972	\$ 920,524
Directors' fees	159,236	-
Officer salaries	\$ 187,680	\$ 211,833
Share-based payment	5,440,260	172,980
	<u>\$ 7,293,148</u>	<u>\$ 1,305,338</u>

**AURCANA CORPORATION****Notes to Consolidated Financial Statements****(Expressed in United States dollars, unless otherwise stated)****19. Commitments****Supply agreement**

On November 14, 2006, La Negra signed a purchase contract with Trafigura Beheer B.V. ("Trafigura") whereby Trafigura agreed to purchase 100%, evenly spread from January to December, of copper concentrate to be produced during the years 2007, 2008 and 2009 by the La Negra Mine. Prices are based on the published prices in the Metal Bulletin in London in US dollars of the following month of shipment is made. In August 2010 the copper purchase contract was extended till the end of 2012.

On March 2011, La Negra signed a purchase contract with Glencore, whereby Glencore's Mexican subsidiary (Metagri), agreed to purchase 100% of lead concentrate to be produced during the years 2011 and 2012. Prices are based on the published prices in the Metal Bulletin in London in US dollars no later than within five days of the monthly lot.

**Office Lease**

Effective May 1, 2010, the Company executed a lease for new office space for a period of 60 months, expiring on April 30, 2015. The minimum annual payments are \$86,160 (May 1, 2010 to April 30, 2012), \$89,750 (May 1, 2012 to April 30, 2013) and \$93,340 (May 1, 2013 to April 30, 2015).

**20. Supplemental Cash Flow Information**

Cash and cash equivalents of the Company are comprised of bank balances and short-term investments, which are convertible to cash, with a term of 90 days or less as follows:

	<u>December 31 2011</u>	<u>December 31 2010</u>	<u>January 1 2010</u>
Cash	\$ 21,243,815	\$ 8,634,145	\$ 2,636,892
Short-term investments	<u>15,316,565</u>	<u>13,542,336</u>	<u>76,951</u>
Cash and cash equivalents	<u>\$ 36,560,380</u>	<u>\$ 22,176,481</u>	<u>\$ 2,713,843</u>

Supplemental disclosures of cash flow information:

	<u>December 31 2011</u>	<u>December 31 2010</u>
Cash interest paid	\$ 73,290	\$ 556,988
Income taxes paid	<u>2,052,107</u>	<u>718,558</u>

The short-term investments were made on overnight basis and at rates from 0.2% to 1.1% per annum.



**AURCANA CORPORATION**

**Notes to Consolidated Financial Statements**

**(Expressed in United States dollars, unless otherwise stated)**

**20. Supplemental Cash Flow Information (continued)**

Supplemental disclosures of non-cash investing

Accounts payable related to construction in progress	<b>3,602,753</b>	428,525
Accrued interest on convertible debt capitalized to mineral property (Note 9)	<b>399,775</b>	361,462

**21. Segmented Information**

The reportable operating segments have been identified as the La Negra mine, the Shafter mine and Corporate, while all other projects and properties have been aggregated into the category "All Other Segments". The Company manages its business, including the allocation of resources and assessment of performance, on a project by project basis, except where the Company's projects are substantially connected and share resources and administrative functions.

December 31, 2011	La Negra	Shafter	Corporate	All other segments	Total
Sales to external customers	\$ 45,882,178	\$ -	\$ -	\$ -	\$ 45,882,178
Mining operating expenses	19,221,122	-	-	-	19,221,122
Depreciation and amortization	2,524,990	-	-	-	2,524,990
Depletion of mineral properties	954,254	-	-	-	954,254
Gross income (loss)	23,181,812	-	-	-	23,181,812
Expenses	1,737,891	(24,769)	11,359,632	465,590	13,538,344
Income (loss) before income taxes	21,443,921	24,769	(11,359,632)	(465,590)	9,643,468
Income tax expense (recovery)	4,190,249	-	(2,203,628)	-	1,986,621
Property, plant and equipment	24,848,086	27,475,358	405,364	-	52,728,808
Segment Mineral properties	4,625,076	50,491,581	-	-	55,116,656
Total capital assets	29,473,162	77,966,939	405,364	-	107,845,464
Total segment assets	36,889,125	79,764,504	37,515,909	18,173	154,187,710
Total liabilities	8,298,103	6,028,344	527,556	16,079	14,870,083

**AURCANA CORPORATION**  
**Notes to Consolidated Financial Statements**  
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**21. Segmented Information (continued)**

December 31, 2010	La Negra	Shafter	Corporate	All other segments	Total
Sales to external customers	\$ 26,144,936	\$ -	\$ -	\$ -	\$ 26,144,936
Mining operating expenses	16,344,367	-	-	-	16,344,367
Depreciation and amortization	1,025,219	-	-	-	1,025,219
Depletion of mineral properties	1,965,293	-	-	-	1,965,293
Loss from trading activity, net	-	-	-	5,043,058	5,043,058
Impairment of property, plant & equipment	-	-	172,373	-	172,373
Gross income (loss)	6,810,056	-	(172,373)	(5,043,058)	1,594,626
Expenses	834,571	115,505	2,759,077	6,973,326	10,682,479
income (loss) before income taxes	5,975,486	(115,505)	(2,931,450)	(12,016,384)	(9,087,853)
Income tax expense (recovery)	(520,766)	-	-	-	(520,766)
Property, plant and equipment	10,809,593	836,198	250,152	-	11,895,943
Segment Mineral properties	5,579,329	41,162,737	-	-	46,742,066
Total capital assets	16,388,922	41,998,935	250,152	-	58,638,009
Total segment assets	5,430,194	3,065,224	78,623,957	231,844	87,351,219
Total liabilities	5,843,423	59,650	9,931,776	206,325	16,041,174

**22. Revenues**

	Years ended December 31,	
	2011	2010
<b>Revenues from mining operations:</b>		
Mining operations	<b>\$ 45,882,178</b>	<b>\$ 26,144,936</b>
	Years ended December 31,	
	2011	2010
Gross revenues from Mining operations (\$million)	<b>\$ 57.8</b>	<b>\$ 33.0</b>
Deductions T.C., refining and smelting charges deducted by the customers	<b>10.2</b>	<b>5.9</b>
Net Revenues before Royalties	<b>47.6</b>	<b>27.1</b>
Royalties	<b>1.7</b>	<b>1.0</b>
Revenues from mining operations	<b>45.9</b>	<b>26.1</b>
<b>Net Revenues by customer:</b>		
Trafigura (Corminmex)	<b>\$ 28.3</b>	<b>\$ 27.1</b>
Glencore (Metagri)	<b>19.3</b>	<b>-</b>
	<b>47.6</b>	<b>27.1</b>

**AURCANA CORPORATION**

**Notes to Consolidated Financial Statements**

**(Expressed in United States dollars, unless otherwise stated)**

**23. Mining operating expenses**

	Notes	Years ended December 31,	
		2011	2010
Mine and Mill supplies		\$ 7,723,455	\$ 6,951,965
Power		1,620,862	1,447,195
Salaries and benefits		8,908,690	7,170,447
Freight and delivery		968,115	774,760
Depreciation and amortization		2,524,990	1,025,219
Depletion of mineral properties		954,254	1,965,293
Loss from trading activity, net	14	-	5,043,058
Impairment of property, plant & equipment		-	172,373
		<u>\$ 22,700,366</u>	<u>\$ 24,550,310</u>

**24. Administrative costs**

	Years ended December 31,	
	2011	2010
Administrative costs[1]	\$ 2,990,345	\$ 2,049,362
Professional fees	774,583	566,385
Investor relations	669,820	243,104
Listing and filing fees	128,632	54,386
	<u>\$ 4,563,379</u>	<u>\$ 2,913,237</u>

[1] Administrative costs break down:

[1] Administrative costs break down:	Years ended December 31,	
	2011	2010
Management fees	\$ 849,235	\$ 414,563
Rent and overhead	145,853	117,258
Travel and accommodation	361,457	258,177
Office	185,817	170,181
Insurance	25,265	39,474
Salaries and Consulting fees	989,584	897,586
Directors Fees	159,236	-
Other	273,898	152,123
	<u>\$ 2,990,345</u>	<u>\$ 2,049,362</u>

**AURCANA CORPORATION****Notes to Consolidated Financial Statements****(Expressed in United States dollars, unless otherwise stated)****25. Financing expense**

	<u>Years ended December 31,</u>	
	<u>2011</u>	<u>2010</u>
Accretion of provision of environmental rehabilitation (note 15)	\$ 70,664	\$ 123,373
Financing expense and bank charges	<u>73,290</u>	<u>556,988</u>
	<u>\$ 143,955</u>	<u>\$ 680,361</u>

**26 Earnings per Share**

	<u>Years ended December 31,</u>	
	<u>2011</u>	<u>2010</u>
Net income (loss) for the year attributable to equity holders of the Company	<u>\$ 6,983,130</u>	<u>\$ (8,751,773)</u>
Weighted average number of shares – basic	351,308,109	137,836,536
Adjustment for:		
Share options	5,212,458	-
Warrants	<u>64,914,123</u>	<u>-</u>
Weighted average number of shares – diluted	421,434,690	137,836,536

**27 Financial Instruments**

The Company's is exposed to certain financial risks, including foreign exchange risk and price risk.

(a) Foreign exchange risk:

The Company is exposed to the financial risk related to the fluctuation of foreign exchange rates in currencies other than the functional currency of the parent, which is the Canadian dollar. The Company operates in Canada, the United States and Mexico and a portion of its expenses are incurred in US dollars and Mexican Pesos. A significant change in the currency exchange rates between the CDN dollar relative to the US dollar or Mexican Peso could have an effect on the Company's results of operations, financial position or cash flows. The Company has not hedged its exposure to currency fluctuations.

**AURCANA CORPORATION****Notes to Consolidated Financial Statements****(Expressed in United States dollars, unless otherwise stated)****27 Financial Instruments (continued)**

At December 31, 2011, the Company's Canadian operations, which have a Canadian dollar functional currency, are exposed to currency risk through the following assets and liabilities denominated in US dollars:

	<u>December 31, 2011</u>
Cash and cash equivalents	USD\$ 20,474,265
Accounts payable	(1,383,602)
Convertible debenture	<u>(2,798,626)</u>
	USD\$ <u>16,292,036</u>
<b>CDN\$ Equivalent</b>	<b>16,114,453</b>

At December 31, 2011, the Company is exposed to currency risk through the following assets and liabilities denominated in Mexican Pesos:

	<u>December 31, 2011</u>
Cash and cash equivalents	MXP\$ 100,001
Other receivable	2,246,160
Accounts payable	<u>(31,246,712)</u>
	MXP\$ <u>(28,900,551)</u>
<b>CDN\$ Equivalent</b>	<b>(2,305,108)</b>

Based on the above net exposures as at December 31, 2011, and assuming that all other variables remain constant, a 10% depreciation or appreciation of the CDN Dollar against the US dollar and the Mexican Peso would result in a \$1,380,935 change to the Company's loss in terms of unrealized exchange gains or losses recognized in earnings or loss for the year.

(b) Credit risk:

The Company's credit risk is primarily attributable to cash and bank balances, short-term deposits, accounts receivable and amounts receivable.

The Company limits its credit exposure on cash held in bank accounts by holding its key transactional bank accounts with banks of investment grade. As the Company has its operations in developing countries, it is unavoidable that some cash is held with regional banks in areas where the banking system does not operate as efficiently as in major financial centres. In these circumstances, the Company attempts to keep only minimal balances with such banks.

## **AURCANA CORPORATION**

### **Notes to Consolidated Financial Statements**

**(Expressed in United States dollars, unless otherwise stated)**

#### **27 Financial Instruments (continued)**

The Company manages its credit risk on short-term deposits by only investing with counterparties that carry investment grade ratings as assessed by external rating agencies and spreading the investments across these counterparties. Under the Company's risk management policy, allowable counterparty exposure limits are determined by the level of the rating unless exceptional circumstances apply. A rating of "A-" grade or equivalent is the minimum allowable rating required as assessed by international credit rating agencies. Likewise, it is the Company's policy to deal with banking counterparties for derivatives who are rated "A-" grade or above by international credit rating agencies and graduated counterparty limits are applied depending upon the rating.

Exceptions to the policy for dealing with relationship banks with ratings below "A-" are reported to, and approved by, the Audit Committee. As at December 31, 2010 substantially all cash and short-term deposits are with counterparties with ratings "A-" or higher.

The Company's credit risk associated with trade accounts receivable is managed through establishing long-term contractual relationships with international trading companies using industry-standard contract terms. 100% of the Company's product sales and trade accounts receivable are generated from two customers representing 100% of the total sales for the year. Other accounts receivable consist of amounts owing from government authorities in relation to the refund of value-added taxes applying to inputs for the production process and property, plant and equipment expenditures.

The carrying amount of financial assets recorded in the financial statements, net of any allowances for losses, represents the Company's maximum exposure to credit risk.

#### **(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 by maintaining cash and cash equivalent balances and available credit facilities to ensure that it is able to meet its short-term and long-term obligations as and when they fall due. Company-wide cash projections are managed centrally and regularly updated to reflect the dynamic nature of the business and fluctuations caused by commodity price and exchange rate movements.

Accounts payable and accrued liabilities are due within the current operating period.

The Company's expected source of cash flow in the upcoming year will be through its operations from both at La Negra and Shafter; equity financing; loans, leasing financing and entering into joint venture agreements, or a combination thereof.

**AURCANA CORPORATION**  
**Notes to Consolidated Financial Statements**  
**(Expressed in United States dollars, unless otherwise stated)**

**27 Financial Instruments (continued)**

The following table summarizes the Company's undiscounted financial liabilities:

	Payments due by period (000's)				
	Total	Less than 1 year	1-3 years	3-5 years	More than 5 years
Accounts payable	9,194	\$9,194	\$ Nil	\$ Nil	\$ Nil
Notes payable	2,818	1,150	1,668	Nil	Nil
Total	\$12,012	\$10,344	\$1,668	\$0	\$0

(d) Price risk

Metal content	2011			10% variance on:				Sensitivity effect on		
	Average sales price	Price as at December 31, 2011	Unit	Average sales price	Price as at December 31, 2011	volume on sales 2011	Unit	Average sales price	Price as at December 31, 2011	
Silver	\$ 35.25	\$ 27.88	oz	\$ 3.53	\$ 2.79	953,850	oz	\$ 3,362,320	\$ 2,659,333	
Copper	4.04	3.43	lb	0.40	0.34	1,482	tn	1,319,969	1,120,667	
Zinc	0.97	0.83	lb	0.10	0.08	3,584	tn	766,433	655,814	
Lead	1.03	0.90	lb	0.10	0.09	1,346	tn	305,644	267,068	
								5,754,366	4,702,881	
								T.C. refining and smelting charges	999,736	817,056
								Revenues before royalties	4,754,630	3,885,825
								Royalties (3.5%) on Revenues	166,412	136,004
								Net revenues	4,588,218	3,749,821

The impact of a 10% variance on 2011 average price, represents an increase or decrease of \$4,588,218 in revenues from mining operations

The impact of a 10% variance on price at December 31, 2011, represents an increase or decrease of \$3,749,821 in revenues from mining operations

The Company is subject to revenue price risk from fluctuations in the market prices of copper, silver, lead and zinc. The Company is also exposed to commodity price risk on diesel fuel through its mining operations. The Company's risk management policy does not currently provide for the management of these exposures through the use of derivative financial instruments. Commodity price risk is also the risk that metal prices will move adversely during the time period between shipment of the concentrate and final payment for the concentrate. The Company's commodity price risk related to financial instruments primarily relates to changes in fair value of embedded derivatives in accounts receivable reflecting commodity sales provisionally priced based on the forward price curve at the end of each quarter.

Based on the gross revenues generated from sales of copper, silver, lead and zinc for the year ended December 31, 2011, and assuming that all other variables remain constant, a 10% depreciation or appreciation in the prices of these commodities would result in a \$4.6 million decrease or increase, respectively, to the Company's reported in earnings or loss for the year.

**AURCANA CORPORATION**

**Notes to Consolidated Financial Statements**

**(Expressed in United States dollars, unless otherwise stated)**

**27 Financial Instruments (continued)**

(e) Fair value estimation

The Company's financial instruments include cash and cash equivalents, trade and other receivables, short-term investments, amounts receivable, advances, accounts payable and accrued liabilities and other long-term debt. The carrying values of cash and cash equivalents, trade and other receivables, advances and accounts payable and accrued liabilities, approximate their fair values due to the relatively short-term nature of these amounts.

The Company classifies the fair value of financial instruments within a hierarchy that prioritizes the inputs to fair value measurement. The three levels of the fair value hierarchy are: Level 1, which are inputs that are unadjusted quoted prices in active markets for identical assets or liabilities; Level 2, which are inputs other than Level 1 quoted prices that are observable for the asset or liability, either directly or indirectly; and Level 3, which are inputs for the asset or liability that are not based on observable market data.

The following table summarizes the fair value hierarchy, as of December 31, 2011:

	Fair value through profit or loss \$	Loans and receivables \$	Other financial assets and liabilities \$	Total \$	fair value hierarchy
<b>Financial Assets</b>					
Cash and cash equivalents	-	36,560,380	-	36,560,380	n/a
Trade and other receivable	-	3,451,158	-	3,451,158	n/a
Short-term investments	383,481	-	-	383,481	Level 1
Amounts receivable	-	942,616	-	942,616	n/a
	<b>383,481</b>	<b>40,954,154</b>	<b>-</b>	<b>41,337,635</b>	
<b>Financial Liabilities</b>					
Accounts payable and accrued liabilities	-	-	(9,193,574)	(9,193,574)	n/a
Long Term Debt	-	-	(2,818,287)	(2,818,287)	n/a
	<b>383,481</b>	<b>40,954,154</b>	<b>(12,011,861)</b>	<b>29,325,774</b>	



**AURCANA CORPORATION**  
**Notes to Consolidated Financial Statements**  
**(Expressed in United States dollars, unless otherwise stated)**

**27 Financial Instruments (continued)**

The following table summarizes the fair value hierarchy, as of December 31, 2010:

	Fair value through profit or loss \$	Loans and receivables \$	Other financial assets and liabilities \$	Total \$	fair value hierarchy
<b>Financial Assets</b>					
Cash and cash equivalents	-	22,176,481	-	22,176,481	n/a
Trade and other receivable	-	1,795,700	-	1,795,700	n/a
Short-term investments	975,238	-	-	975,238	Level 1
Amounts receivable	-	-	-	-	n/a
	<b>975,238</b>	<b>23,972,181</b>	<b>-</b>	<b>24,947,419</b>	
<b>Financial Liabilities</b>					
Accounts payable and accrued liabilities	-	-	(4,318,474)	(4,318,474)	n/a
Long Term Debt	-	-	(236,661)	(236,661)	n/a
	<b>975,238</b>	<b>23,972,181</b>	<b>(4,555,135)</b>	<b>20,392,284</b>	

There were no material differences between the carrying value and fair value of long-term assets and liabilities as of December 31, 2011. The Company assesses its financial instruments and non-financial contracts on a regular basis to determine the existence of any embedded derivatives which would be required to be accounted for separately at fair value and to ensure that any embedded derivatives are accounted for in accordance with the Company's policy.

**28. Subsequent event:**

On February 17, 2012, the Company increased its ownership in Real de Maconi S.A. de C.V. ("Real Maconi") from 92% to 99.86 % as a result of a recent capital restructure of Real de Maconi . Real Maconi holds a 99.99% interest (one share representing a .00002% interest is held by a third party) in Minera La Negra S.A. de C.V. which has a 100% interest in the La Negra Mine.

The capital restructure was the result of Real De Maconi's 2010 tax audit wherein the Mexican Tax Authorities required Real de Maconi to reclassify certain accounting transactions resulting in a reclassification and roll back of the capitalization of the equity accounts. The result of the roll back increased Aurcana's ownership of Real de Maconi to 99.86% leaving a non-controlling interest of 0.14% to a third party (Note 17).

## AURCANA CORPORATION

### Notes to Consolidated Financial Statements

(Expressed in United States dollars, unless otherwise stated)

#### 29. First-Time Adoption of IFRS

The Company adopted IFRS on January 1, 2011 with a transition date of January 1, 2010. IFRS 1, *First-Time Adoption of International Financial Reporting Standards*, provides guidance for the initial adoption of IFRS. IFRS 1 requires retrospective application of the standards in the transition statement of financial position, with all adjustments to assets and liabilities taken to retained earnings unless certain exemptions are applied.

The Company changed its presentation currency from Canadian dollars to US dollars effective January 1, 2011. Under IFRS, the change in presentation currency was applied retrospectively and the changes resulted in a translation adjustment of \$1,805,733 at January 1, 2010. The effects of the change in presentation currency are included as part of the IFRS reconciliations below.

The Company has applied the following exemptions and specific guidelines:

##### a) *Cumulative Translation Differences*

IFRS 1 allows the Company to set the currency translation adjustment, which is included in accumulated other comprehensive income, to zero at January 1, 2010 and adjust deficit by the same amount. If, subsequent to adoption, a foreign operation is disposed of the translation differences that arose before the date of transition to IFRS will not affect the gain or loss on disposal.

Upon the change to IFRS, the Company reversed the currency translation balance of \$1,805,733 at January 1, 2010 and recorded a decrease in the deficit of \$1,805,733.

At December 31, 2010, the Company reclassified \$2,078,644 of cumulative translation adjustments occurring in the year ended December 31, 2001 to accumulated other comprehensive income for presentation purposes.

##### b) *Estimates*

In accordance with IFRS 1, an entity's estimates at the date of transition to IFRS must be consistent with estimates made for the same date under previous GAAP, unless there is objective evidence that those estimates were in error. The Company's IFRS estimates as of January 1, 2010 and December 31, 2010 and for the year then ended are consistent with the Canadian GAAP estimates for the same dates.

##### c) *Deferred income taxes*

Under Canadian GAAP, the Company recognized a deferred income tax liability on asset acquisitions where the accounting basis is greater than the tax basis. Under IFRS, the initial recognition exemption does not allow for the recognition of a deferred income tax liability on asset acquisitions.

On July 15, 2008, the Company acquired the Shafter silver mine ("Shafter") from Silver Standard Resources Inc., which resulted in a deferred income tax liability and an increase in the corresponding asset of \$14,249,903 (CDN\$16,197,191).

## AURCANA CORPORATION

### Notes to Consolidated Financial Statements

(Expressed in United States dollars, unless otherwise stated)

#### 29. First-Time Adoption of IFRS (continued)

As a result of this deferred income tax liability in the United States, under Canadian GAAP, the Company was able to recognize the benefit of its United States non-capital loss carry-forwards, which generated a tax asset of \$1,695,685 (CDN\$1,779,452) as at December 31, 2009. This tax asset was netted against the deferred tax liability for Canadian GAAP purposes. On transition to IFRS, upon elimination of the deferred tax liability, as discussed further below, the Company also reversed this tax asset by increasing the deferred tax liability and the deficit at January 1, 2010 by \$1,695,685. During the year ended December 31, 2010, under Canadian GAAP, the Company also recognized an additional tax asset of \$411,427 to bring the total tax asset recognized to \$2,107,112 at December 31, 2010.

From the acquisition of Shafter to December 31, 2009, the deferred income tax liability, related to Shafter, increased by \$3,387,540 to \$17,637,443 (C\$18,533,796) as a result of the liability being denominated in US dollars when the functional currency under Canadian GAAP was the Canadian dollar.

During the year ended December 31, 2010, the deferred income tax liability, related to Shafter, decreased by \$1,857,848 to \$15,779,595 (CDN\$15,694,843).

Upon the change to IFRS, the Company eliminated the deferred income tax liability related to the acquisition of Shafter at January 1, 2010 in the amount of \$17,637,443, decreased the related mining property asset by \$14,249,903 and recorded a decrease of \$3,387,540 to the deficit. The Company also eliminated the tax asset, in the amount of \$1,695,685 related to its United States non-capital loss carry-forwards, which do not meet the more likely than not test, by an offsetting increase to the opening deficit at January 1, 2010.

Under IFRS, as at and for the year ended December 31, 2010, the Company reversed the foreign exchange gain recorded under Canadian GAAP in the amount of \$1,857,848, reversed the deferred income tax liability in the amount of \$15,779,595, decreased the related mining property asset by \$14,249,903 and recorded a cumulative decrease in deficit of \$1,529,692. The Company also eliminated the tax asset, in the amount of \$2,107,112 related to its United States non-capital loss carry-forwards, which do not meet the more likely than not test and reversed the recognition of future income tax recovery of \$411,427 recorded on the U.S. tax losses under Canadian GAAP and recorded a cumulative increase in deficit of \$2,107,112.

The Company also reclassified a Canadian GAAP foreign exchange loss on its tax basis in Mexico of \$1,723,140 from foreign exchange (gain) loss for Canadian GAAP purposes to deferred income tax recovery for the year ended December 31, 2011 in accordance with IFRS.

**AURCANA CORPORATION**

**Notes to Consolidated Financial Statements**

**(Expressed in United States dollars, unless otherwise stated)**

**29. First-Time Adoption of IFRS (continued)**

*d) Convertible debt*

As required, the Company has changed the method of determining the fair value of the debt and equity components from a relative fair value approach to the required residual approach. Under the residual approach, the debt is fair valued and the residual is assigned as the fair value of the equity component.

Upon the change to IFRS, the Company decreased the debt portion of the convertible debt at January 1, 2010 in the amount of \$610,486, increased contributed surplus by \$1,969,310 and increased the deficit by \$1,358,824 representing the increased accretion of the debt required under IFRS prior to January 1, 2010.

Under IFRS, for the year ended December 31, 2010, the Company increased the accretion of the debt portion of the convertible debt recorded under Canadian GAAP in the amount of \$304,051 and the adjustment to the December 31, 2010 debt portion of the convertible debt decreased to \$306,435 and the deficit increased by \$1,662,875.

The changes made to the consolidated statements of operations and the consolidated statements of financial position have resulted in the reclassification of various amounts on the statements of cash flows, however as there have been no changes to the net cash flows, and accordingly no reconciliations have been prepared.

Reconciliations of assets, liabilities, equity, and comprehensive income of the Company at December 31, 2010 from those reported under Canadian GAAP to IFRS are as follows:

**AURCANA CORPORATION**  
**Notes to Consolidated Financial Statements**  
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**29. First-Time Adoption of IFRS (continued)**

a) The January 1, 2010 Canadian GAAP statement of financial position has been reconciled to IFRS as follows:

	Canadian GAAP January 1, 2010 CDN\$	Canadian GAAP January 1, 2010 USD\$	Note	Effect of Transition to IFRS January 1, 2010 USD\$	IFRS January 1, 2010 USD \$
<b>Assets</b>					
<b>Current assets</b>					
Cash and cash equivalents	2,852,174	2,713,843		-	<b>2,713,843</b>
Trade and other receivables	1,309,825	1,246,299		-	<b>1,246,299</b>
Inventories	1,361,922	1,295,869		-	<b>1,295,869</b>
Short-term investments	1,147,500	1,088,800		-	<b>1,088,800</b>
Prepaid expenses and advances	279,051	265,517		-	<b>265,517</b>
	6,950,472	6,610,328		-	<b>6,610,328</b>
<b>Non Current assets</b>					
Trade and other receivables	766,357	732,235		-	<b>732,235</b>
Property, plant and equipment	7,916,519	7,532,568		-	<b>7,532,568</b>
Mineral Properties	63,978,122	60,875,183	c	(14,249,903)	<b>46,625,280</b>
Deferred tax asset	-	-		-	-
Long term deposits	-	-		-	-
<b>Total assets</b>	<b>79,611,470</b>	<b>75,750,314</b>		<b>(14,249,903)</b>	<b>61,500,411</b>
<b>Liabilities</b>					
<b>Current liabilities</b>					
Accounts payable and accrued liabilities	4,361,865	4,150,315		-	<b>4,150,315</b>
Notes Payable current portion	1,391,375	1,323,893		-	<b>1,323,893</b>
	5,753,240	5,474,208		-	<b>5,474,208</b>
Deferred revenue	22,185,697	21,109,691		-	<b>21,109,691</b>
Convertible debentures	8,919,003	8,486,431	d	(610,486)	<b>7,875,945</b>
Notes payable Long-term	2,393,328	2,277,252		-	<b>2,277,252</b>
Provision for environmental rehabilitation	1,338,036	1,273,141		-	<b>1,273,141</b>
Deferred tax liability	16,754,344	15,941,758	c	1,695,685	
			c	(17,637,443)	-
<b>Total liabilities</b>	<b>57,343,648</b>	<b>54,562,481</b>		<b>(16,552,244)</b>	<b>38,010,237</b>
<b>Shareholders' Equity</b>					
Issued capital	55,684,504	47,358,524		-	<b>47,358,524</b>
Contributed Surplus	7,077,058	6,419,038	d	1,969,310	<b>8,388,348</b>
Translation adjustment on change in presentation currency	-	1,805,733	a	(1,805,733)	-
Other comprehensive income	286,250	250,669		-	<b>250,669</b>
Deficit	(41,378,297)	(35,215,420)	c	3,387,540	
			c	(1,695,685)	
			a	1,805,733	
			d	(1,358,824)	<b>(33,076,656)</b>
<b>Total equity attributable to equity holders of the parent</b>	<b>21,669,515</b>	<b>20,618,544</b>		<b>2,302,341</b>	<b>22,920,885</b>
<b>Non-controlling interest</b>	<b>598,307</b>	<b>569,289</b>		-	<b>569,289</b>
<b>Total liabilities and equity</b>	<b>79,611,470</b>	<b>75,750,314</b>		<b>(14,249,903)</b>	<b>61,500,411</b>

**AURCANA CORPORATION**  
**Notes to Consolidated Financial Statements**  
**(Expressed in United States dollars, unless otherwise stated)**

**29. First-Time Adoption of IFRS (continued)**

- b) The Company's Canadian GAAP statement of operations and statement of comprehensive (loss) income for the year ended December 31, 2010 has been reconciled to IFRS as follows:

	Year Ended December 31, 2010				
	Canadian GAAP CDN\$	Canadian GAAP USD\$	Note	Effect of transition to IFRS USD\$	IFRS USD\$
<b>Revenues</b>					
Mining operations	\$ 26,936,880	\$ 26,144,936		\$ -	\$ 26,144,936
<b>Costs of sales</b>					
Mining operating expenses	25,291,687	24,550,310		-	24,550,310
<b>Earnings from mine operations</b>	<b>1,645,193</b>	<b>1,594,626</b>		<b>-</b>	<b>1,594,626</b>
<b>Other items</b>					
Administrative costs	3,001,481	2,913,237		-	2,913,237
Bank Charges/Interest and Financing	387,708	376,309	d	304,051	680,361
Stock-based compensation	272,602	264,588		-	264,588
Foreign exchange (gain) loss	(1,518,127)	(1,473,494)	c	1,857,848	(1,338,786)
			c	(1,723,140)	(1,338,786)
Loss on termination of silver sale contract	7,681,310	7,570,872		-	7,570,872
Other expenses (income)	610,145	592,207		-	592,207
	10,435,119	10,243,719		438,759	10,682,479
<b>Loss before income taxes</b>	<b>(8,789,926)</b>	<b>(8,649,094)</b>		<b>(438,759)</b>	<b>(9,087,853)</b>
Income tax recovery (expense)	(740,324)	(718,558)			(718,558)
Deferred income tax recovery (expense)	3,476,088	3,373,891	c	(411,427)	1,239,324
			c	(1,723,140)	1,239,324
<b>Loss for the year</b>	<b>\$ (6,054,162)</b>	<b>\$ (5,993,761)</b>		<b>\$ (2,573,326)</b>	<b>\$ (8,567,087)</b>
<b>Attributable to:</b>					
Non-controlling interest	190,280	184,686		-	184,686
Equity holders of the Company	(6,244,442)	(6,178,447)		(2,573,326)	(8,751,773)
	\$ (6,054,162)	\$ (5,993,761)		\$ (2,573,326)	\$ (8,567,087)

Condensed Interim Consolidated Statements of Comprehensive Income (Loss)	Year Ended December 31, 2010				
	Canadian GAAP CDN\$	Canadian GAAP USD\$	Note	Effect of transition to IFRS USD\$	IFRS USD\$
<b>Net income (loss) for the year</b>	<b>\$ (6,054,162)</b>	<b>\$ (5,993,761)</b>		<b>\$ (2,573,326)</b>	<b>\$ (8,567,087)</b>
Currency translation adjustment		(272,911)		(1,805,733)	(2,078,644)
Unrealized gain (loss) on available-for-sale investments	460,000	444,961		-	444,961
Effect of sale of short-term investments	(176,250)	(169,553)		-	(169,553)
<b>Comprehensive income (loss) for the year</b>	<b>(5,770,412)</b>	<b>(5,991,264)</b>		<b>(4,379,059)</b>	<b>(10,370,323)</b>
<b>Attributable to:</b>					
Non-controlling interest	190,280	184,686			184,686
Equity holders of the Company	(5,960,692)	(6,175,950)		(4,379,059)	(10,555,009)
	\$ (5,770,412)	\$ (5,991,264)		\$ (4,379,059)	\$ (10,370,323)

**AURCANA CORPORATION**  
**Notes to Consolidated Financial Statements**  
**(Expressed in United States dollars, unless otherwise stated)**

**29. First-Time Adoption of IFRS (continued)**

c) The Company's Canadian GAAP statement of financial position at December 31, 2010 has been reconciled to IFRS as follows:

	Canadian GAAP December 31, 2010 CDN\$	Canadian GAAP December 31, 2010 USD\$	Note	Effect of Transition to IFRS December 31, 2010 USD\$	IFRS December 31, 2010 USD \$
<b>Assets</b>					
<b>Current assets</b>					
Cash and cash equivalents	\$ 22,057,371	\$ 22,176,481		\$ -	<b>22,176,481</b>
Trade and other receivables	1,786,055	1,795,700		-	<b>1,795,700</b>
Inventories	1,608,190	1,616,874		-	<b>1,616,874</b>
Short-term investments	970,000	975,238		-	<b>975,238</b>
Prepaid expenses and advances	89,033	89,514		-	<b>89,514</b>
	<b>26,510,649</b>	<b>26,653,807</b>		<b>-</b>	<b>26,653,807</b>
<b>Non Current assets</b>					
Trade and other receivables	815,674	820,079		-	<b>820,079</b>
Property, plant and equipment	12,362,789	11,895,943		-	<b>11,895,943</b>
Mineral Properties	64,250,514	60,991,969	c	(14,249,903)	<b>46,742,066</b>
Deferred tax asset	1,232,668	1,239,324		-	<b>1,239,324</b>
Long term deposits	-	-		-	<b>-</b>
<b>Total assets</b>	<b>\$ 105,172,294</b>	<b>\$ 101,601,122</b>		<b>\$ (14,249,903)</b>	<b>87,351,219</b>
<b>Liabilities</b>					
<b>Current liabilities</b>					
Accounts payable and accrued liabilities	\$ 4,295,279	\$ 4,318,474		\$ -	<b>4,318,474</b>
Income tax payable	684,601	688,298		-	<b>688,298</b>
Convertible debt current portion	7,666,752	7,708,152	d	(306,435)	<b>7,401,717</b>
Notes Payable current portion	235,390	236,661		-	<b>236,661</b>
	<b>12,882,022</b>	<b>12,951,585</b>		<b>(306,435)</b>	<b>12,645,150</b>
Convertible debentures	1,988,771	1,999,510		-	<b>1,999,510</b>
Provision for environmental rehabilitation	1,385,480	1,396,514		-	<b>1,396,514</b>
Deferred tax liability	13,599,048	13,672,483	c	(15,779,595)	<b>-</b>
			c	2,107,112	<b>-</b>
<b>Total liabilities</b>	<b>29,855,321</b>	<b>30,020,092</b>		<b>(13,978,918)</b>	<b>16,041,174</b>
<b>Shareholders' Equity</b>					
Issued capital	99,657,659	90,861,167		-	<b>90,861,167</b>
Contributed Surplus	21,923,466	21,106,589	d	1,969,310	<b>23,075,899</b>
Currency translation adjustment	-	(272,911)	a	(1,805,733)	<b>-</b>
			a	2,078,644	<b>-</b>
Accumulated other comprehensive income	570,000	526,077	a	(2,078,644)	<b>(1,552,567)</b>
Deficit	(47,622,739)	(41,393,867)	c	1,529,692	<b>-</b>
			c	(2,107,112)	<b>-</b>
			a	1,805,733	<b>-</b>
			d	(1,662,875)	<b>(41,828,429)</b>
<b>Total equity attributable to equity holders of the parent</b>	<b>74,528,386</b>	<b>70,827,055</b>		<b>(270,985)</b>	<b>70,556,070</b>
<b>Non-controlling Interest</b>	<b>788,587</b>	<b>753,975</b>		<b>-</b>	<b>753,975</b>
<b>Total liabilities and equity</b>	<b>\$ 105,172,294</b>	<b>\$ 101,601,122</b>		<b>\$ (14,249,903)</b>	<b>87,351,219</b>