# SONORA GOLD & SILVER CORP.

Consolidated Financial Statements

Years Ended January 31, 2012 and 2011

(Expressed in Canadian dollars)

SATURNA GROUP
CHARTERED ACCOUNTANTS LLP

1066 West Hastings Street, Suite 1250
Vancouver, BC Canada V6E 3X1

## INDEPENDENT AUDITORS' REPORT

**To the Shareholders of Sonora Gold & Silver Corp.**

We have audited the accompanying consolidated financial statements of Sonora Gold & Silver Corp., which comprise the statements of financial position as at January 31, 2012, January 31, 2011, and February 1, 2010 and the consolidated statements of comprehensive loss, changes in equity, and cash flows for the years ended January 31, 2012 and 2011, and the related notes comprising a summary of significant accounting policies and other explanatory information.

**Management's Responsibility for the 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 financial statements that are free from material misstatement, whether due to fraud or error.

**Auditors' 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 financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the 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 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 involves evaluating the appropriateness of the accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

**Opinion**

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of Sonora Gold & Silver Corp. as at January 31, 2012, January 31, 2011, and February 1, 2010 and its financial performance and its cash flows for the years then ended, in accordance with International Financial Reporting Standards.

**Emphasis of Matter**

Without qualifying our opinion, we draw attention to Note 1 of the consolidated financial statements which indicates the existence of a material uncertainty that may cast significant doubt on the ability of Sonora Gold & Silver Corp. to continue as a going concern.

Saturna Group Chartered Accountants LLP

Vancouver, Canada

May 24, 2012

**SONORA GOLD & SILVER CORP.**
Consolidated statements of financial position
(Expressed in Canadian dollars)

| | January 31, 2012 $ | January 31, 2011 $ | February 1, 2010 $ (Note 14) |
|---|---|---|---|
| Assets | | | |
| Current assets | | | |
| Cash and cash equivalents | 638,580 | 1,225,194 | 52,855 |
| Amounts receivable | 5,686 | 20,011 | 1,825 |
| Prepaid expenses | 12,719 | 15,946 | – |
| Total current assets | 656,985 | 1,261,151 | 54,680 |
| Non-current assets | | | |
| Restricted cash (Note 3) | 11,500 | 11,500 | 11,500 |
| Exploration and evaluation assets (Note 4) | 968,700 | 846,306 | 574,965 |
| Total non-current assets | 980,200 | 857,806 | 586,465 |
| Total assets | 1,637,185 | 2,118,957 | 641,145 |
| Liabilities | | | |
| Current liabilities | | | |
| Accounts payable and accrued liabilities | 30,898 | 77,517 | 39,705 |
| Notes payable (Note 5) | – | 150,000 | – |
| Total liabilities | 30,898 | 227,517 | 39,705 |
| Equity | | | |
| Share capital | 11,542,225 | 11,512,225 | 8,967,865 |
| Share-based payment reserve | 1,075,715 | 920,365 | 234,698 |
| Deficit | (11,011,653) | (10,541,150) | (8,601,123) |
| Total equity | 1,601,287 | 1,891,440 | 601,440 |
| Total liabilities and equity | 1,637,185 | 2,118,957 | 641,145 |

Nature of operations and continuance of business (Note 1)
Contingency (Note 11)

Approved and authorized for issue by the Board of Directors on May 24, 2012:

*/s/ "Kenneth Churchill"*

Kenneth Churchill, Director

*/s/ "Michael Resendes"*

Michael Resendes, Director

(The accompanying notes are an integral part of these consolidated financial statements)

**SONORA GOLD & SILVER CORP.**
Consolidated statements of operations and comprehensive loss
(Expressed in Canadian dollars)

| | Year ended January 31, 2012 $ | Year ended January 31, 2011 $ |
|---|---|---|
| Revenue | – | – |
| Expenses | | |
| Consulting fees (Note 9) | 37,110 | 40,745 |
| Foreign exchange loss | 27,231 | 14,545 |
| Impairment of mineral property costs (Note 4) | – | 560,217 |
| Insurance | 18,414 | – |
| Management fees (Note 9) | 58,800 | 58,800 |
| Office and miscellaneous | 16,015 | 18,078 |
| Professional fees | 92,061 | 154,239 |
| Project evaluation costs | – | 29,737 |
| Rent (Note 9) | 17,200 | 16,206 |
| Stock-based compensation (Note 8) | 155,350 | 848,929 |
| Transfer agent and regulatory fees | 26,997 | 53,568 |
| Travel and promotion | 9,095 | 101,545 |
| Total expenses | 458,273 | 1,896,609 |
| Loss before other expense | (458,273) | (1,896,609) |
| Other expense | | |
| Interest expense | (12,230) | (43,418) |
| Net loss and comprehensive loss for the year | (470,503) | (1,940,027) |
| Loss per share, basic and diluted | (0.01) | (0.07) |
| Weighted average shares outstanding | 35,856,104 | 29,640,404 |

(The accompanying notes are an integral part of these consolidated financial statements)

**SONORA GOLD & SILVER CORP.**
Consolidated statements of changes in equity
(Expressed in Canadian dollars)

| | Share capital | | Share-based payment | | |
|---|---|---|---|---|---|
| | Number of shares | Amount $ | reserve $ | Deficit $ | Total equity $ |
| Balance, February 1, 2010 | 25,196,348 | 8,967,865 | 234,698 | (8,601,123) | 601,440 |
| Issued pursuant to private placements | 7,500,000 | 1,500,000 | – | – | 1,500,000 |
| Issued pursuant to exercise of stock options | 1,396,000 | 189,200 | – | – | 189,200 |
| Fair value of stock options exercised transferred from contributed surplus | – | 163,262 | – | – | 163,262 |
| Issued pursuant to exercise of share purchase warrants | 575,000 | 86,250 | – | – | 86,250 |
| Issued pursuant to mineral property option agreements | 1,000,000 | 568,000 | – | – | 568,000 |
| Issued pursuant to notes payable proceeds received | 58,824 | 37,648 | – | – | 37,648 |
| Fair value of stock options granted | – | – | 848,929 | – | 848,929 |
| Fair value of stock options exercised transferred to share capital | – | – | (163,262) | – | (163,262) |
| Net loss for the year | – | – | – | (1,940,027) | (1,940,027) |
| Balance, January 31, 2011 | 35,726,172 | 11,512,225 | 920,365 | (10,541,150) | 1,891,440 |
| Issued pursuant to exercise of share purchase warrants | 200,000 | 30,000 | – | – | 30,000 |
| Fair value of stock options granted | – | – | 155,350 | – | 155,350 |
| Net loss for the year | – | – | – | (470,503) | (470,503) |
| Balance, January 31, 2012 | 35,926,172 | 11,542,225 | 1,075,715 | (11,011,653) | 1,606,287 |

(The accompanying notes are an integral part of these consolidated financial statements)

**SONORA GOLD & SILVER CORP.**
Consolidated statements of cash flows
(Expressed in Canadian dollars)

| | Year ended January 31, 2012 $ | Year ended January 31, 2011 $ |
|---|---|---|
| Cash provided by (used in): | | |
| Operating activities | | |
| Net loss for the year | (470,503) | (1,940,027) |
| Items not involving cash: | | |
| Impairment of mineral property costs | – | 560,217 |
| Stock-based compensation | 155,350 | 886,577 |
| Changes in non-cash operating working capital: | | |
| Amounts receivable | 14,325 | (18,186) |
| Prepaid expenses | 3,227 | (15,946) |
| Accounts payable and accrued liabilities | (46,619) | 52,560 |
| Net cash used in operating activities | (344,220) | (474,805) |
| Investing activities | | |
| Exploration and evaluation asset expenditures | (122,394) | (278,306) |
| Net cash used in investing activities | (122,394) | (278,306) |
| Financing activities | | |
| Proceeds from notes payable | – | 150,000 |
| Repayment of notes payable | (150,000) | – |
| Proceeds from shares issued | 30,000 | 1,775,450 |
| Net cash provided by (used in) financing activities | (120,000) | 1,925,450 |
| Increase (decrease) in cash and cash equivalents | (586,614) | 1,172,339 |
| Cash and cash equivalents, beginning of year | 1,225,194 | 52,855 |
| Cash and cash equivalents, end of year | 638,580 | 1,225,194 |
| Cash and cash equivalents consists of : | | |
| Cash | 638,580 | 423,393 |
| Funds held in legal trust | – | 801,801 |
| Total cash and cash equivalents | 638,580 | 1,225,194 |
| Non-cash investing and financing activities: | | |
| Shares issued pursuant to mineral property option agreement | – | 568,000 |
| Supplemental disclosures: | | |
| Interest paid | 18,000 | – |
| Income taxes paid | – | – |

(The accompanying notes are an integral part of these consolidated financial statements)

**1. Nature of Operations and Continuance of Business**

The Company is an exploration stage company currently focussed on exploration and development of precious and base metal projects in Tanzania.

These financial statements have been prepared on the going concern basis, which assumes that the Company will be able to realize its assets and discharge its liabilities in the normal course of business. As at January 31, 2012, the Company has not generated any revenues from operations and has an accumulated deficit of $11,011,653. The continued operations of the Company are dependent on its ability to generate future cash flows or obtain additional financing. Management is pursuing equity financing. Management is of the opinion that sufficient working capital will be obtained from external financing to meet the Company's liabilities and commitments as they become due, although there is a risk that additional financing will not be available on a timely basis or on terms acceptable to the Company. These financial statements do not reflect any adjustments that may be necessary if the Company is unable to continue as a going concern.

**2. Significant Accounting Policies**

(a) Basis of Preparation

The accompanying financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS"), as issued by the International Accounting Standards Board ("IASB") on a going concern basis. Effective January 1, 2011, Canadian generally accepted accounting principles ("GAAP") were revised to incorporate IFRS, and required publicly accountable companies to apply IFRS standards. Therefore, the Company has begun reporting on the IFRS basis for these financial statements. Within these financial statements, the term Canadian GAAP refers to Canadian GAAP prior to the adoption of IFRS.

An explanation of how the transition to IFRS has affected the reported financial position, financial performance and cash flows of the Company is provided in Note 14.

The financial statements have been prepared on a historical cost basis. The financial statements are presented in Canadian dollars, which is the Company's functional currency.

These consolidated financial statements include the accounts of the Company and its inactive wholly-owned subsidiary, DJ Mines Limited, a Company incorporated in Tanzania. All inter-company balances and transactions have been eliminated on consolidation.

(b) Use of Estimates and Judgments

The preparation of the financial statements in conformity with IFRS requires the Company's management to make judgments, estimates and assumptions that affect the application of accounting policies and reported amounts of assets, liabilities, revenues 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 estimate is revised and in any future periods affected.

Significant areas requiring the use of estimates include the valuation of exploration and evaluation assets, measurement of share-based payments, and deferred income tax asset valuation allowances.

**2. Significant Accounting Policies** (continued)

(c) Cash and Cash Equivalents

The Company considers all highly liquid instruments with a maturity of three months or less at the time of issuance to be cash equivalents.

(d) Exploration and Evaluation Expenditures

Exploration and evaluation expenditures include the costs of acquiring licenses, costs associated with exploration and evaluation activity, and the fair value (at acquisition date) of exploration and evaluation assets acquired in a business combination. Exploration and evaluation expenditures are capitalized. Costs incurred before the Company has obtained the legal rights to explore an area are charged to operations.

Exploration and evaluation assets are assessed for impairment if (i) sufficient data exists to determine technical feasibility and commercial viability, and (ii) facts and circumstances suggest that the carrying amount exceeds the recoverable amount.

Once the technical feasibility and commercial viability of the extraction of mineral resources in an area of interest are demonstrable, exploration and evaluation assets attributable to that area of interest are first tested for impairment and then reclassified to mining property and development assets within property, plant and equipment.

Recoverability of the carrying amount of any exploration and evaluation assets is dependent on successful development and commercial exploitation, or alternatively, sale of the respective areas of interest.

*Mineral Property Options*

The Company does not record any expenditures made by the optionee in its accounts. It also does not recognize any gain or loss on its exploration and evaluation option arrangements but re-designates any costs previously capitalized in relation to the whole interest as relating to the partial interest retained and any consideration received directly from the optionee is credited against costs previously capitalized.

(e) Impairment of Non-Current Assets

At each reporting date, the Company reviews the carrying amounts of its tangible assets to determine whether there are any indications of impairment. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment, if any.

Where the asset does not generate cash flows that are independent from other assets, the Company estimates the recoverable amount of the cash generating unit ("CGU") to which the asset belongs. The recoverable amount is determined as the higher of fair value less direct costs to sell and the asset's value in use. In assessing value in use, the estimated future cash flows are discounted to their present value. Estimated future cash flows are calculated using estimated recoverable reserves, estimated future commodity prices and the expected future operating and capital costs. The pre-tax discount rate applied to the estimated future cash flows reflects current market assessments of the time value of money and the risks specific to the asset for which the future cash flow estimates have not been adjusted.

If the carrying amount of an asset or CGU exceeds its recoverable amount, the carrying amount of the asset or CGU is reduced to its recoverable amount through an impairment charge to the statement of income.

**2. Significant Accounting Policies** (continued)

(e) Impairment of Non-Current Assets (continued)

Assets that have been impaired are tested for possible reversal of the impairment whenever events or changes in circumstance indicate that the impairment may have reversed. When an impairment subsequently reverses, the carrying amount of the asset or CGU is increased to the revised estimate of its recoverable amount, but only so that the increased carrying amount does not exceed the carrying amount that would have been determined (net of depreciation, depletion and amortization) had no impairment loss been recognized for the asset or CGU in prior periods. A reversal of impairment is recognized as a gain in the statement of income.

(f) Reclamation and Remediation Provisions

The Company recognizes a provision for statutory, contractual, constructive or legal obligations associated with decommissioning of mining operations and reclamation and rehabilitation costs arising when environmental disturbance is caused by the exploration or development of mineral properties, plant and equipment. Provisions for site closure and reclamation are recognized in the period in which the obligation is incurred or acquired, and are measured based on expected future cash flows to settle the obligation, discounted to their present value. The discount rate used is a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the liability including risks specific to the countries in which the related operation is located.

When an obligation is initially recognized, the corresponding cost is capitalized to the carrying amount of the related asset in mineral properties, plant and equipment. These costs are depreciated using either the unit of production or straight line method depending on the asset to which the obligation relates.

The obligation is increased for the accretion and the corresponding amount is recognized as a finance expense. The obligation is also adjusted for changes in the estimated timing, amount of expected future cash flows, and changes in the discount rate. Such changes in estimates are added to or deducted from the related asset except where deductions are greater than the carrying value of the related asset in which case, the amount of the excess is recognized in the statements of comprehensive income/loss.

Due to uncertainties concerning environmental remediation, the ultimate cost to the Company of future site restoration could differ from the amounts provided. The estimate of the total provision for future site closure and reclamation costs is subject to change based on amendments to laws and regulations, changes in technology, price increases and changes in interest rates, and as new information concerning the Company's closure and reclamation obligations becomes available.

(g) Financial Instruments

(i) Non-derivative financial assets

The Company initially recognizes loans and receivables and deposits on the date that they are originated. All other financial assets (including assets designated at fair value through profit or loss) are recognized initially on the trade date at which the Company becomes a party to the contractual provisions of the instrument.

The Company derecognizes a financial asset when the contractual rights to the cash flows from the asset expire, or it transfers the rights to receive the contractual cash flows on the financial asset in a transaction in which substantially all the risk and rewards of ownership of the financial asset are transferred. Any interest in transferred financial assets that is created or retained by the Company is recognized as a separate asset or liability.

**2. Significant Accounting Policies** (continued)

(g) Financial Instruments (continued)

(i) Non-derivative financial assets (continued)

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

*Financial assets at fair value through profit or loss*

Financial assets are classified as fair value through profit or loss when the financial asset is held for trading or it is designated as fair value through profit or loss. A financial asset is classified as held for trading if: (i) it has been acquired principally for the purpose of selling in the near future; (ii) it is a part of an identified portfolio of financial instruments that the Company manages and has an actual pattern of short-term profit taking; or (iii) it is a derivative that is not designated and effective as a hedging instrument.

Financial assets classified as fair value through profit or loss are stated at fair value with any gain or loss recognized in profit or loss. The net gain or loss recognized incorporates any dividend or interest earned on the financial asset. The Company does not have any assets classified as fair value through profit or loss.

*Held-to-maturity investments*

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

*Available-for-sale financial assets*

Available-for-sale financial assets are non-derivative financial assets that are designated as available-for-sale and that are not classified in any of the previous categories. Subsequent to initial recognition, they are measured at fair value and changes therein, other than impairment losses and foreign currency differences on available-for-sale equity instruments, are recognized in other comprehensive income and presented within equity in the fair value reserve. When an investment is derecognized, the cumulative gain or loss in other comprehensive income is transferred to profit or loss. Available-for-sale financial assets are comprised of marketable securities. The Company does not have any assets classified as available-for-sale.

*Loans and receivables*

Loans and receivables are financial assets with fixed or determinable payments that are not quoted in an active market are classified as loans and receivables. Such assets are initially recognized at fair value plus any directly attributable transaction costs. Subsequent to initial recognition loans and receivables are measured at amortized cost using the effective interest method, less any impairment losses. Loans and receivables are comprised of cash and amounts receivable.

**2. Significant accounting policies** (continued)

(g) Financial instruments (continued)

(i) Non-derivative financial assets (continued)

*Impairment of financial assets*

When an available-for-sale financial asset is considered to be impaired, cumulative gains or losses previously recognized in other comprehensive income or loss are reclassified to profit or loss in the period. Financial assets are assessed for indicators of impairment at the end of each reporting period. 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 assets, the estimated future cash flows of the investments have been impacted. For marketable securities classified as available-for-sale, a significant or prolonged decline in the fair value of the securities below their cost is considered to be objective evidence of impairment.

For all other financial assets objective evidence of impairment could include:

- significant financial difficulty of the issuer or counterparty; or
- default or delinquency in interest or principal payments; or
- it becoming probable that the borrower will enter bankruptcy or financial re-organization.

For certain categories of financial assets, such as amounts receivable, assets that are assessed not to be impaired individually are subsequently assessed for impairment on a collective basis. The carrying amount of financial assets is reduced by the impairment loss directly for all financial assets with the exception of amounts receivable, where the carrying amount is reduced through the use of an allowance account. When an amount receivable is considered uncollectible, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited against the allowance account. Changes in the carrying amount of the allowance account are recognized in profit or loss.

With the exception of available-for-sale equity instruments, if, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized, the previously recognized impairment loss is reversed through profit or loss to the extent that the carrying amount of the investment at the date the impairment is reversed does not exceed what the amortized cost would have been had the impairment not been recognized. In respect of available-for-sale equity securities, impairment losses previously recognized through profit or loss are not reversed through profit or loss. Any increase in fair value subsequent to an impairment loss is recognized directly in equity.

(ii) Non-derivative financial liabilities

The Company initially recognizes debt securities issued and subordinated liabilities on the date that they are originated. All other financial liabilities (including liabilities designated at fair value through profit or loss) are recognized initially on the trade at which the Company becomes a party to the contractual provisions of the instrument.

The Company derecognizes a financial liability when its contractual obligations are discharged or cancelled or expire.

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

**2. Significant accounting policies** (continued)

(g) Financial instruments (continued)

(ii) Non-derivative financial liabilities

The Company has the following non-derivative financial liabilities: accounts payable and accrued liabilities and notes payable.

Such financial liabilities are recognized initially at fair value plus any directly attributable transaction costs. Subsequent to initial recognition these financial liabilities are measured at amortized cost using the effective interest method.

(iii) Share capital

Common shares are classified as equity. Transaction costs directly attributable to the issue of common shares and stock options are recognized as a deduction from equity, net of any tax effects.

(h) Income Taxes

*Current income tax*

Current income tax assets and liabilities for the current period are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted, at the reporting date. Current income tax relating to items recognized directly in other comprehensive income or equity is recognized in other comprehensive income or equity and not in profit or loss. Management periodically evaluates positions taken in the tax returns with respect to situations in which applicable tax regulations are subject to interpretation and establishes provisions where appropriate.

*Deferred income tax*

Deferred income tax is provided using the balance sheet method on temporary differences at the reporting date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. The carrying amount of deferred income tax assets is reviewed at the end of each reporting period and recognized only to the extent that it is probable that sufficient taxable profit will be available to allow all or part of the deferred income tax asset to be utilized. Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realized or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted by the end of the reporting period. Deferred income tax assets and deferred income tax liabilities are offset, if a legally enforceable right exists to set off current tax assets against current income tax liabilities and the deferred income taxes relate to the same taxable entity and the same taxation authority.

(i) Flow-through Shares

The resource expenditure deductions for income tax purposes related to exploration and development activities funded by flow-through share arrangements are renounced to investors in accordance with Canadian tax legislation. On issuance, the premium recorded on the flow-through share, being the difference in price over a common share with no tax attributes, is recognized as a liability. As expenditures are incurred, the deferred income tax liability associated with the renounced tax deductions is recognized through profit and loss with a pro-rata portion of the deferred premium.

**2. Significant Accounting Policies** (continued)

(j) Foreign Currency Translation

The functional and reporting currency is the Canadian dollar. Transactions denominated in foreign currencies are translated using the exchange rate in effect on the transaction date or at an average rate. Monetary assets and liabilities denominated in foreign currencies are translated at the rate of exchange in effect at the statement of financial position date. Non-monetary items are translated using the historical rate on the date of the transaction. Foreign exchange gains and losses are included in profit or loss.

(k) Loss Per Share

Basic loss per share is computed using the weighted average number of common shares outstanding during the period. The treasury stock method is used for the calculation of diluted loss per share, whereby all "in the money" stock options and share purchase warrants are assumed to have been exercised at the beginning of the period and the proceeds from their exercise are assumed to have been used to purchase common shares at the average market price during the period. When a loss is incurred during the period, basic and diluted loss per share are the same as the exercise of stock options and share purchase warrants is considered to be anti-dilutive.

(l) Comprehensive Loss

Comprehensive income (loss) is the change in the Company's net assets that results from transactions, events and circumstances from sources other than the Company's shareholders and includes items that are not included in profit or loss.

(m) Stock-based Compensation

The Company grants share-based awards to employees, directors and consultants as an element of compensation. The fair value of the awards is recognized over the vesting period as share-based compensation expense and contributed surplus. The fair value of share-based payments is determined using the Black-Scholes option pricing model using estimates at the date of the grant. At each reporting date prior to vesting, the cumulative expense representing the extent to which the vesting period has expired and management's best estimate of the awards that are ultimately expected to vest is computed. The movement in cumulative expense is recognized in the statement of income with a corresponding entry within equity, against contributed surplus. No expense is recognized for awards that do not ultimately vest. When stock options are exercised, the proceeds received, together with any related amount in contributed surplus, are credited to share capital.

Share-based payments arrangements in which the Company receives goods or services as consideration for its own equity instruments are accounted for as equity-settled share-based payment transactions, unless the fair value cannot be estimated reliably. If the Company cannot reliably estimate the fair value of the goods or services received, the Company will measure their value by reference to the fair value of the equity instruments granted.

**2. Significant Accounting Policies** (continued)

(n) Accounting Standards Issued But Not Yet Effective

A number of new standards, and amendments to standards and interpretations, are not yet effective for the year ended January 31, 2012, and have not been applied in preparing these financial statements.

(i) Effective for annual periods beginning on or after July 1, 2011:

*Amendments to IFRS 7, "Financial Instruments: Disclosures"*

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

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

*Amendments to IAS 1 "Presentation of Financial Statements"*

In June 2011, the IASB issued amendments to IAS 1 to require companies to group together items within other comprehensive income ("OCI") that may be reclassified to the statement of income. The amendments also reaffirm existing requirements that items in OCI and profit or loss should be presented as either a single statement or two separate statements. The amendments are to be applied retrospectively.

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

*New standard IFRS 9, "Financial Instruments"*

Partial replacement of IAS 39, "Financial Instruments: Recognition and Measurement". IFRS 9 introduces new requirements for how an entity should classify and measure financial assets that are in the scope of IAS 39. The standard requires all financial assets to be classified on the basis of the entity's business model for managing the financial assets, and the contractual cash flow characteristics of the financial asset. A financial asset is measured at amortized cost if two criteria are met: (a) the objective of the business model is to hold the financial asset for the collection of the contractual cash flows, and (b) the contractual cash flows under

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

*New Standard IFRS 10, "Consolidated Financial Statements"*

In May 2011, the IASB issued IFRS 10 to replace portions of IAS 27, "Consolidated and Separate Financial Statements" and interpretation SIC-12, "Consolidated - Special Purpose Entities". IFRS 10 incorporates a single model for consolidating all entities that are controlled and revises the definition of control to be "An investor controls an investee when it is exposed, or has rights, to variable returns from its involvement with the investee and has the current ability to affect those returns through its power over the investee". Along with control, the new standard also focuses on the concept of power, both of which will include a use of judgment and a continuous reassessment as facts and circumstances change.

**2. Significant Accounting Policies** (continued)

(n) Accounting Standards Issued But Not Yet Effective (continued)

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

*New standard IFRS 11, "Joint Arrangements"*

In May 2011, the IASB issued IFRS 11 to replace IAS 31, "Interest in Joint Ventures". The new standard will apply to the accounting for interest in joint arrangements where there is joint control. Joint arrangements will be separated into joint ventures and joint operations. The structure of the joint arrangement will no longer be the most significant factor on classifying a joint arrangement as either a joint operation or a joint venture. Proportionate consolidations will be removed and replaced with equity accounting.

*New standard IFRS 12 "Disclosure of Interest in Other Entities"*

In May 2011, the IASB issued IFRS 12. The new standard includes disclosure requirements about subsidiaries, joint ventures and associates, as well as unconsolidated structured entities and replaces existing disclosure requirements.

*New standard IFRS 13, "Fair Value Measurement"*

In May 2011, the IASB issued IFRS 13. The new standard converges IFRS and US GAAP on how to measure fair value and the related fair value disclosures. The new standard creates a single source of guidance for fair value measurements, where fair value is required or permitted under IFRS, by not changing how fair value is used but how it is measured. The focus will be on an exit price.

The Company has not early adopted these new and revised standards and is currently assessing the impact that these standards will have on its consolidated financial statements.

Other accounting standards or amendments to existing accounting standards that have been issued but have future effective dates are either not applicable or are not expected to have a significant impact on the Company's consolidated financial statements.

**3. Restricted Cash**

The Company has pledged a guaranteed investment certificate ("GIC") as collateral for the Company's credit cards. The GIC earns interest of prime minus 2.05% and has a maturity date of January 16, 2013.

## 4. Exploration and Evaluation Assets

| 2012 | Handeni<br>$ | Negese<br>$ | Total<br>$ |
|---|---|---|---|
| *Acquisition Costs:* | | | |
| Balance, January 31, 2011 | 731,642 | 114,664 | 846,306 |
| Additions | – | 49,689 | 49,689 |
| Balance, January 31, 2012 | 731,642 | 164,353 | 895,995 |
| *Exploration Costs:* | | | |
| Balance, January 31, 2011 | – | – | – |
| Geological | – | 45,940 | 45,940 |
| Assays | – | 26,765 | 26,765 |
| Balance, January 31, 2012 | – | 72,705 | 72,705 |
| | 731,642 | 237,058 | 968,700 |

| 2011 | Los Pavitos<br>$ | Handeni<br>$ | Negese<br>$ | Total<br>$ |
|---|---|---|---|---|
| *Acquisition Costs:* | | | | |
| Balance, January 31, 2010 | 514,675 | – | – | 514,675 |
| Additions | – | 731,642 | 114,664 | 846,306 |
| Impairment | (514,675) | – | – | (514,675) |
| Balance, January 31, 2011 | – | 731,642 | 114,664 | 846,306 |
| *Exploration Costs:* | | | | |
| Balance, January 31, 2010 | 60,290 | – | – | 60,290 |
| Impairment | (60,290) | – | – | (60,290) |
| Balance, January 31, 2011 | – | – | – | – |
| | – | 731,642 | 114,664 | 846,306 |

| 2010 | Los Pavitos<br>$ | Brenda<br>$ | Christina<br>$ | Total<br>$ |
|---|---|---|---|---|
| *Acquisition Costs:* | | | | |
| Balance, January 31, 2009 | 514,675 | 19,501 | 19,501 | 553,677 |
| Impairment | – | (19,501) | (19,501) | (39,002) |
| Balance, February 1, 2010 | 514,675 | – | – | 514,675 |
| *Exploration Costs:* | | | | |
| Balance, January 31, 2009 | 60,290 | 7,315 | 7,315 | 74,920 |
| Impairment | – | (7,315) | (7,315) | (14,630) |
| Balance, February 1, 2010 | 60,290 | – | – | 60,290 |
| | 574,965 | – | – | 574,965 |

**4. Exploration and Evaluation Assets** (continued)

(a) Los Pavitos, Christina, and Brenda, Mexico

On September 11, 2007, the Company entered into an option agreement to purchase three separate mineral claims (Los Pavitos, Christina, and Brenda) in the state of Sonora, Mexico. The Company paid US$50,000 to purchase a two year option on the three separate mining claims. Under the agreement, the Company had the right to earn a 100% interest in the three properties. In order to exercise the options relating to Los Pavitos and Christina, the Company must, for each property, make payments of US$50,000 and issue 1,500,000 common shares of the Company. To exercise the option on Brenda, the Company must issue 3,500,000 common shares of the Company. All three properties were subject to a 2% net smelter return.

On November 27, 2007, the Company exercised its option to acquire 100% of the Los Pavitos mining claim in Sonora, Mexico, by making a cash payment of US$50,000 and by issuing 1,500,000 common shares at a fair value of $442,500 to the vendors.

During the year ended January 31, 2010, the Company decided not to exercise the options on the Christina and Brenda properties and therefore recognized an impairment loss of $53,632 on these two properties.

During the year ended January 31, 2011, the Company decided not to pursue exploration on the Los Pavitos property and therefore recognized an impairment loss of $560,217 on the property.

(b) Handeni Property, Tanzania

On July 24, 2010 (amended on October 6, 2010), the Company entered into an option agreement to acquire the mineral licence for the Handeni property located in Tanzania.

To earn this interest, the Company must issue 700,000 common shares (issued) and make the following cash payments:

- initial payment of US$20,000 into an escrow account within 10 days of the execution of the agreement (paid and released to the optionor upon completion of due diligence);
- a further US$22,500 every 90 days for a total of US$90,000 until July 24, 2011. ($45,000 has been paid)

The initial term is for one year. The Company has the right of extending the option for up to two further one year periods and then one further six month period by notice in writing to the optionor and a further payment of US$45,000 at the beginning of the each new extension option period. If the purchase option is exercised prior to the expiry of the initial term or any extension option period, then no further instalment payments or extension payments will be required to be paid.

The Company can exercise the option at any time by paying the optionor US$1,000,000. The optionor retains a 2% net smelter royalty. The US$1,000,000 option exercise payment will be treated as an advance payment of the royalty.

Refer to Note 11.

**4. Exploration and Evaluation Assets** (continued)

(c) Negese Property, Tanzania

On September 9, 2010, the Company entered into an option agreement to acquire the mineral licence to the Negese property located in Tanzania.

To earn this interest, the Company must issue 300,000 common shares (issued) and make the following cash payments:

- US$5,000 to be paid on execution of the agreement (paid);
- A further US$25,000 to be paid within 30 days on execution of the agreement (paid);
- Monthly payment of US$2,000 on the 1st day of each proceeding month from November 9, 2010 to September 9, 2011 (prorated for first month). ($5,400 has been paid);

The initial term is for one year. The Company has the right of extending the option for up to four further one year periods by notice in writing to the optionor and further monthly payments of US$5,000. If the purchase option is exercised prior to the expire of any one year option period then the value of any unexpired option period will be deducted from the purchase price

The Company can exercise the option at any time by paying the optionor US$1,300,000. The optionor retains a 2% net smelter royalty. The US$1,300,000 option exercise payment will be treated as an advance payment of the royalty.

**5. Notes Payable**

In fiscal 2011, the Company entered into promissory note agreements with three directors of the Company whereby each of the three directors advanced the Company $50,000, for a total of $150,000. The notes payable bear interest at 12% per annum, are unsecured, and due on October 6, 2011. The Company issued a total of 58,824 common shares with a fair value of $37,648 to the three directors as a bonus for lending the funds which was recorded as interest expense. On October 6, 2011, the Company repaid the full balance of $150,000 plus accrued interest of $18,000 to the directors of the Company.

**6. Share Capital**

Authorized: 100,000,000 common shares without par value

(a) On April 22, 2010, the Company issued 2,500,000 units at $0.10 per unit for proceeds of $250,000. Each unit consisted of one common share and one-half of one share purchase warrant. Each whole share purchase warrant entitles the holder to acquire an additional common share at an exercise price of $0.15 per share expiring on April 22, 2011.

(b) On September 9, 2010, the Company issued 300,000 common shares with a fair value of $78,000 pursuant to the Negese mineral property option agreement. Refer to Note 4(c).

(c) On September 22, 2010, the Company issued 5,000,000 units at $0.25 per unit for proceeds of $1,250,000. Each unit consisted of one common share and one-half of one share purchase warrant. Each whole share purchase warrant entitles the holder to acquire an additional common share at an exercise price of $0.50 per share expiring on September 22, 2012.

(d) On October 6, 2010, the Company issued 700,000 common shares with a fair value of $490,000 pursuant to the Handeni mineral property option agreement. Refer to Note 4(b).

(e) On October 6, 2010, the Company also issued 58,824 common shares with a fair value of $37,648 pursuant to the promissory notes payable executed with three directors of the Company. Refer to Note 5.

## 7. Share Purchase Warrants

The following table summarizes the continuity of share purchase warrants:

| | Number of warrants | Weighted average exercise price $ |
|---|---|---|
| Balance, January 31, 2010 | – | – |
| Issued | 3,750,000 | 0.38 |
| Exercised | (575,000) | 0.20 |
| Balance, January 31, 2011 | 3,175,000 | 0.43 |
| Exercised | (200,000) | 0.15 |
| Expired | (475,000) | 0.15 |
| Balance, January 31, 2012 | 2,500,000 | 0.50 |

As at January 31, 2012, the following share purchase warrants were outstanding:

| Number of warrants outstanding | Exercise price $ | Expiry date |
|---|---|---|
| 2,500,000 | 0.50 | September 22, 2012 |

## 8. Stock Options

The Company has adopted a fixed stock option plan pursuant to which options may be granted to directors, officers, employees and consultants of the Company to a maximum of 10% of the issued and outstanding common shares. Stock options granted under this plan vest immediately.

The following table summarizes the continuity of the Company's stock options:

| | Number of options | Weighted average exercise price $ |
|---|---|---|
| Outstanding, January 31, 2010 | 1,000,000 | 0.18 |
| Granted | 2,700,000 | 0.40 |
| Exercised | (1,396,000) | 0.14 |
| Expired | (104,000) | 0.20 |
| Outstanding, January 31, 2011 | 2,200,000 | 0.48 |
| Granted | 1,400,000 | 0.16 |
| Cancelled | (50,000) | 0.50 |
| Expired | (50,000) | 0.50 |
| Outstanding, January 31, 2012 | 3,500,000 | 0.35 |

**8. Stock Options** (continued)

Additional information regarding stock options outstanding as at January 31, 2012 is as follows:

| | Outstanding and exercisable | | |
|---|---|---|---|
| Range of exercise prices $ | Number of shares | Weighted average remaining contractual life (years) | Weighted average exercise price $ |
| 0.10 | 350,000 | 3.4 | 0.10 |
| 0.16 | 1,400,000 | 4.6 | 0.16 |
| 0.50 | 850,000 | 1.6 | 0.50 |
| 0.60 | 900,000 | 1.7 | 0.60 |
| | 3,500,000 | 3.0 | 0.35 |

The fair values for stock options granted have been estimated using the Black-Scholes option pricing model assuming no expected dividends and the following weighted average assumptions:

| | 2012 | 2011 |
|---|---|---|
| Risk-free interest rate | 1.42% | 2.35% |
| Expected life (in years) | 5 | 5 |
| Expected volatility | 133% | 112% |

The weighted average fair value of the stock options granted was $0.11 (2011 – $0.32) per option. The total fair value of the stock options granted in 2012 was $155,350 (2011 – $848,929) which was recorded as share-based payment reserve and charged to operations.

**9. Related Party Transactions**

(a) During the year ended January 31, 2012, the Company incurred consulting fees of $37,110 (2011 - $23,710) to the Chief Financial Officer of the Company and a company controlled by the Chief Financial Officer of the Company.

(b) During the year ended January 31, 2012, the Company incurred consulting fees of $nil (2011 - $17,035) to a former director of the Company.

(c) During the year ended January 31, 2012, the Company incurred management fees of $40,800 (2011 - $40,800) to the President of the Company and a company controlled by the President of the Company.

(d) During the year ended January 31, 2012, the Company incurred rent of $14,400 (2011 - $14,400) to the President of the Company and a company controlled by the President of the Company.

## 10. Financial Instruments and Risks

(a) Fair Values

Assets and liabilities measured at fair value on a recurring basis were presented on the Company's balance sheet as at January 31, 2012 as follows:

| | Fair Value Measurements Using | | | |
|---|---|---|---|---|
| | Quoted prices in active markets for identical instruments (Level 1) $ | Significant other observable inputs (Level 2) $ | Significant unobservable inputs (Level 3) $ | Balance, January 31, 2012 $ |
| Cash | 638,580 | – | – | 638,580 |
| Restricted cash | 11,500 | – | – | 11,500 |

The fair values of other financial instruments, which include amounts receivable, accounts payable and accrued liabilities, and notes payable, approximate their carrying values due to the relatively short-term maturity of these instruments.

(b) Credit Risk

Financial instruments that potentially subject the Company to a concentration of credit risk consist primarily of cash. The Company limits its exposure to credit loss by placing its cash with high credit quality financial institutions. Amounts receivable consist of GST/HST refunds due from the Government of Canada. The carrying amount of financial assets represents the maximum credit exposure.

(c) Foreign Exchange Rate and Interest Rate Risk

The Company is not exposed to any significant foreign exchange rate or interest rate risk.

(d) 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 currently settles its financial obligations out of cash. The ability to do this relies on the Company raising equity financing in a timely manner and by maintaining sufficient cash in excess of anticipated needs.

(e) Price Risk

The Company is exposed to price risk with respect to commodity prices. The Company's ability to raise capital to fund exploration and development activities is subject to risks associated with fluctuations in the market price of commodities.

## 11. Contingency

On February 11, 2011, the Minister for Energy and Minerals for Tanzania cancelled the mineral licence underlying the Handeni Property option agreement. The Company believes that it has a valid agreement and that the Minister for Energy and Minerals erred in law when it cancelled the mineral licence. The Company has appealed to the High Court of Tanzania to have the mineral licence reinstated. The appeal was heard on March 27, 2012 and the Company is awaiting the decision. The outcome cannot be reasonably determined at this time.

## 12. Capital Management

The Company manages its capital to maintain its ability to continue as a going concern and to provide returns to shareholders and benefits to other stakeholders. The capital structure of the Company consists of cash and equity comprised of issued share capital, share-based payment reserve and deficit.

The Company manages its capital structure and makes adjustments to it in light of economic conditions. The Company, upon approval from its Board of Directors, will balance its overall capital structure through new share issues or by undertaking other activities as deemed appropriate under the specific circumstances.

The Company is not subject to externally imposed capital requirements and the Company's overall strategy with respect to capital risk management remains unchanged from the year ended January 31, 2011.

## 13. Income Taxes

The tax effect (computed by applying the Canadian federal and provincial statutory rate) of the significant temporary differences, which comprise deferred tax assets and liabilities, are as follows:

| | 2012<br>$ | 2011<br>$ |
|---|---|---|
| Canadian statutory income tax rate | 26.37% | 28.33% |
| Income tax recovery at statutory rate | (124,072) | (549,610) |
| Tax effect of: | | |
| Permanent differences and other | 41,458 | 230,672 |
| Expiry of non-capital loss | – | 17,476 |
| Change in enacted tax rates | 4,292 | 35,435 |
| Change in valuation allowance | 78,322 | 266,027 |
| Income tax provision | – | – |

The significant components of deferred income tax assets and liabilities are as follows:

| | 2012<br>$ | 2011<br>$ |
|---|---|---|
| Deferred income tax assets | | |
| Non-capital losses carried forward | 563,723 | 446,619 |
| Property and equipment | 99 | 179 |
| Resource pools | 302,203 | 335,761 |
| Share issuance costs | – | 5,144 |
| Total gross deferred income tax assets | 866,025 | 787,703 |
| Valuation allowance | (866,025) | (787,703) |
| Net deferred income tax asset | – | – |

**13. Income Taxes** (continued)

As at January 31, 2012, the Company has non-capital losses carried forward of $2,254,892, which are available to offset deferred years' taxable income. These losses expire as follows:

| | $ |
|---|---|
| 2026 | 108,450 |
| 2027 | 204,837 |
| 2028 | 222,157 |
| 2029 | 335,930 |
| 2030 | 227,511 |
| 2031 | 687,590 |
| 2032 | 468,417 |
| | 2,254,892 |

The Company also has available mineral resource related expenditure pools totalling $2,177,513 which may be deducted against future taxable income on a discretionary basis.

**14. Transition to IFRS**

As stated in Note 2, these are the Company's first annual financial statements prepared in accordance with IFRS.

The accounting policies set out in Note 2 have been applied in preparing the financial statements for the year ended January 31, 2012, the comparative information presented in these financial statements for the year ended January 31, 2011, and in the preparation of an opening IFRS statement of financial position as at February 1, 2010 (the Company's date of transition).

*First Time Adoption of IFRS*

The Company has adopted IFRS on February 1, 2011 with a transition date of February 1, 2010. Under IFRS 1, "First Time Adoption of International Financial Reporting Standards ("IFRS 1"), the IFRS standards are applied retrospectively at the transition date with all adjustments to assets and liabilities as stated under GAAP taken to deficit, with IFRS providing certain optional and mandatory exemptions to this principle.

The Company has elected to apply the following optional exemptions:

Share-based payment transactions

IFRS 1 encourages, but does not require, first-time adopters to apply IFRS 2, "Share-based Payment to equity instruments that were granted on or before November 7, 2002, or equity instruments that were granted subsequent to November 7, 2002 and vested before the later of the date of transition to IFRS and January 1, 2005. The Company has elected not to apply IFRS 2 to awards that vested prior to February 1, 2010.

Fair value as deemed cost

The Company may elect among two options when measuring the value of its assets under IFRS. It may elect, on an asset by asset basis, to use either historical cost as measured under retrospective application of IFRS or fair value of an asset at the opening balance sheet date. The Company has elected to use historical cost for its exploration and evaluation assets.

**14. Transition to IFRS** (continued)

*Reconciliation to previously reported financial statements*

Flow-through shares

Under IFRS, the proceeds from flow-through shares are allocated between the offering of the share and the sale of the tax benefits. The allocation is based on the difference between the amount the investor pays for the flow-through shares and the share prices as of the date the transaction is approved. A liability is recognized for the premium, and extinguished when the tax effect of the temporary differences, resulting from incurring the relevant expenditure, is recorded.

Under Canadian GAAP, the Company recorded the gross proceeds relating to the flow-through shares to share capital at the time of issuance. The Company then recorded a charge (reduction) to share capital at the time the tax benefits of the flow-through shares were renounced to the investors. The charge was calculated by multiplying the amount of the renounced tax benefits (which are equal to the proceeds of the flow-through share issue) by the effective tax rate at the time. The offset would go to the deferred tax liability to reflect the fact that the Company could no longer use the tax attributes for its benefit.

Impact on statement of financial position:

As at February 1, 2010

| | Previous Canadian GAAP $ | Effect of transition to IFRS $ | IFRS $ |
|---|---|---|---|
| Share capital | 8,929,432 | 38,433 | 8,967,865 |
| Share-based payment reserve | 234,698 | – | 234,698 |
| Deficit | (8,562,690) | (38,433) | (8,601,123) |
| Total equity | 601,440 | – | 601,440 |

The transition from Canadian GAAP to IFRS had no material impact on the statement of financial position as at January 31, 2011 and the statements of operations and comprehensive loss and cash flows for the year then ended.