# Excellon Resources Inc.

Condensed Interim Consolidated Financial Statements

June 30, 2015
in thousands of U.S. dollars
(unaudited)

NOTICE OF NO AUDITOR REVIEW OF CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

Under National Instrument 51-102, Part 4, subsection 4.3(3) (a), if an auditor has not performed a review of the interim financial statements; they must be accompanied by a notice indicating that the financial statements have not been reviewed by an auditor. The accompanying unaudited condensed interim consolidated financial statements of the Company have been prepared by management and approved by the Audit Committee and Board of Directors of the Company. The Company's independent auditors have not performed a review of these financial statements in accordance with the standards established by the Chartered Professional Accountants of Canada for a review of interim financial statements by an entity's auditors.

August 12, 2015

# Excellon Resources Inc.

## Condensed Interim Consolidated Statements of Financial Position

(unaudited) (in thousands of U.S. dollars)

| | Notes | June 30, 2015 $ | December 31, 2014 $ |
|---|---|---|---|
| **Assets** | | | |
| **Current assets** | | | |
| Cash and cash equivalents | | 1,333 | 3,467 |
| Trade receivables | | 1,652 | 1,778 |
| Income taxes receivable | | 2,659 | 2,556 |
| Inventories | *3* | 1,766 | 2,364 |
| Other current assets | | 1,894 | 1,552 |
| | | 9,304 | 11,717 |
| | | | |
| **Non-current assets** | | | |
| Property, plant and equipment | *4* | 16,464 | 18,384 |
| Mineral rights | *5* | 5,451 | 5,975 |
| Deferred income tax assets | *10* | 8,707 | 7,735 |
| **Total assets** | | 39,926 | 43,811 |
| | | | |
| **Liabilities** | | | |
| **Current liabilities** | | | |
| Trade payables | | 5,288 | 5,541 |
| | | | |
| **Non-current liabilities** | | | |
| Provisions | *6* | 1,991 | 1,984 |
| **Total liabilities** | | 7,279 | 7,525 |
| | | | |
| **Equity** | | | |
| Share capital | *7* | 77,352 | 77,323 |
| Contributed surplus | | 11,844 | 11,504 |
| Accumulated other comprehensive income | | (8,695) | (6,745) |
| Deficit | | (47,854) | (45,796) |
| **Total equity** | | 32,647 | 36,286 |
| | | | |
| **Total liabilities and equity** | | 39,926 | 43,811 |
| | | | |
| *Going Concern* | *2b* | | |

The accompanying notes are an integral part of these condensed interim consolidated financial statements.

| **Approved by the Board** | **Director** | **Director** |
|---|---|---|
| | *"Timothy J. Ryan"* | *"Alan R. McFarland"* |

# Excellon Resources Inc.

## Condensed Interim Consolidated Statements of Income (loss) and Comprehensive Income (loss)

## For the three and six months ended June 30, 2015 and 2014

(unaudited)(in thousands of U.S. dollars, except per share data)

| | | Three months ended | | Six months ended | |
|---|---|---|---|---|---|
| | | **June 30, 2015** | **June 30, 2014** | **June 30, 2015** | **June 30, 2014** |
| | *Notes* | **$** | **$** | **$** | **$** |
| Revenues | *12* | 4,036 | 8,792 | 9,091 | 19,328 |
| Production Costs | | (4,013) | (5,615) | (8,573) | (12,419) |
| Depletion and amortization | | (815) | (1,047) | (1,662) | (2,040) |
| Cost of Sales | *8a* | (4,828) | (6,662) | (10,235) | (14,459) |
| **Gross profit** | | (792) | 2,130 | (1,144) | 4,869 |
| Administrative expenses | | (548) | (864) | (1,162) | (1,712) |
| Share based payments | *7* | (264) | (202) | (392) | (469) |
| Depletion and amortization | | (50) | (76) | (100) | (146) |
| General and administrative expenses | *8b* | (862) | (1,142) | (1,654) | (2,327) |
| Exploration | | (188) | (181) | (414) | (518) |
| Other income (expense) | *8c* | (722) | (881) | (172) | 219 |
| Finance costs | | (18) | (22) | (44) | (44) |
| **Income (loss) before income tax** | | (2,582) | (96) | (3,428) | 2,199 |
| Income tax recovery (expense) | *10* | 761 | (615) | 1,370 | (1,035) |
| **Net income (loss)** | | (1,821) | (711) | (2,058) | 1,164 |
| **Other comprehensive income (loss)** | | | | | |
| Foreign currency translation differences | | 43 | 2,036 | (1,950) | (59) |
| **Total other comprehensive income (loss)** | | 43 | 2,036 | (1,950) | (59) |
| **Total comprehensive income (loss)** | | (1,778) | 1,325 | (4,008) | 1,105 |

| | | | | |
|---|---|---|---|---|
| **Income (loss) per share** | | | | |
| Basic | $ (0.03) | $ (0.01) | $ (0.04) | $ 0.02 |
| Diluted | $ (0.03) | $ (0.01) | $ (0.04) | $ 0.02 |
| **Weighted average number of shares** | | | | |
| Basic | 54,958,121 | 54,970,613 | 54,946,836 | 54,979,149 |
| Diluted | 55,032,766 | 55,042,540 | 55,032,766 | 55,049,682 |

The accompanying notes are an integral part of these condensed interim consolidated financial statements.

# Excellon Resources Inc.

## Condensed Interim Consolidated Statements of Changes in Equity

## For the Six months ended June 30, 2015 and 2014

(unaudited) (in thousands of U.S. dollars)

| | Share capital $ | Contributed surplus $ | Accumulated other comprehensive income (loss) $ | Deficit $ | Total equity $ |
|---|---|---|---|---|---|
| **Balance - January 1, 2014** | 77,434 | 10,676 | (1,955) | (26,504) | 59,651 |
| Net income (loss) for the period | - | - | - | 1,164 | 1,164 |
| Total other comprehensive income (loss) | - | - | (59) | - | (59) |
| Total comprehensive income (loss) | - | - | (59) | 1,164 | 1,105 |
| Employee share options: | | | | | |
| Value of services recognized | 2 | 311 | - | - | 313 |
| Proceeds on issuing shares | 3 | - | - | - | 3 |
| Repurchased shares under normal course issuer bid | (50) | 3 | - | - | (47) |
| **Balance - June 30, 2014** | 77,389 | 10,990 | (2,014) | (25,340) | 61,025 |
| | | | | | |
| **Balance - January 1, 2015** | 77,323 | 11,504 | (6,745) | (45,796) | 36,286 |
| Net income (loss) for the period | - | - | - | (2,058) | (2,058) |
| Total other comprehensive income (loss) | - | - | (1,950) | - | (1,950) |
| Total comprehensive income (loss) | - | - | (1,950) | (2,058) | (4,008) |
| Employee share options: | | | | | |
| Value of services recognized | - | 135 | - | - | 135 |
| Deferred and Restricted share units | | | | | |
| Value of units recognized | 29 | 205 | - | - | 234 |
| **Balance - June 30, 2015** | 77,352 | 11,844 | (8,695) | (47,854) | 32,647 |

The accompanying notes are an integral part of these condensed interim consolidated financial statements.

# Excellon Resources Inc.

## Condensed Interim Consolidated Statements of Cash Flow

## For the three and six months ended June 30, 2015 and 2014

(in thousands of U.S. dollars)

| | Three months ended | | Six months ended | |
|---|---|---|---|---|
| | **June 30, 2015** | **June 30, 2014** | **June 30, 2015** | **June 30, 2014** |
| | **$** | **$** | **$** | **$** |
| **Cash flow provided by (used in)** | | | | |
| **Operating activities** | | | | |
| Net income (loss) for the period | (1,821) | (711) | (2,058) | 1,164 |
| Adjustments for: | | | | |
| Depletion and amortization | 865 | 1,123 | 1,762 | 2,186 |
| Deferred income tax | (555) | 333 | (972) | 325 |
| Share-based compensation | 264 | 200 | 392 | 469 |
| Post-employment benefits | 43 | 21 | 84 | 41 |
| Rehabilitation provision - accretion | 17 | 21 | 35 | 43 |
| Unrealized loss (gain) on marketable securities | - | (99) | - | (354) |
| Unrealized loss (gain) on foreign intercompany loans | - | 732 | - | (116) |
| Operating cash flows before changes in working capital | (1,187) | 1,620 | (757) | 3,758 |
| Changes in items of working capital: | | | | |
| Trade receivables | 205 | 275 | 126 | (157) |
| Income taxes receivable | 5 | 141 | (103) | 466 |
| Inventories | 203 | (624) | 598 | 121 |
| Other current assets | (131) | 38 | (342) | (227) |
| Trade payables | 894 | 503 | (253) | 319 |
| **Net cash provided by (used in) operating activities** | (11) | 1,953 | (731) | 4,280 |
| **Investing activities** | | | | |
| Purchase of property, plant and equipment | (267) | (381) | (659) | (912) |
| Purchase of mineral rights | 1 | - | (10) | - |
| **Net cash used in investing activities** | (266) | (381) | (669) | (912) |
| **Financing activities** | | | | |
| Proceeds on issuance of shares | - | - | - | 3 |
| Repurchased shares under normal course issuer bid | - | (38) | - | (47) |
| **Net cash used in financing activities** | - | (38) | - | (44) |
| **Effect of exchange rate changes on cash and cash equivalents** | 337 | 405 | (734) | 20 |
| **Increase (decrease) in cash and cash equivalents** | 60 | 1,939 | (2,134) | 3,344 |
| **Cash and cash equivalents - Beginning of the period** | 1,273 | 3,996 | 3,467 | 2,591 |
| **Cash and cash equivalents - End of the period** | 1,333 | 5,935 | 1,333 | 5,935 |
| Interest | 9 | - | 9 | - |
| Cash paid for income tax | 185 | 33 | 185 | 71 |

The accompanying notes are an integral part of these condensed interim consolidated financial statements.

## 1. GENERAL INFORMATION

Excellon Resources Inc. and its subsidiaries (together the Company or Excellon) are involved in the exploration, development and extraction of high-grade silver-lead-zinc metals in Mexico.

Excellon is domiciled in Canada and incorporated under the laws of the province of Ontario. The address of its principal office is 20 Victoria Street, Suite 900, Toronto, Ontario, M5C 2N8, Canada.

## 2. BASIS OF PRESENTATION AND GOING CONCERN

### *a. Statement of compliance*

These unaudited condensed interim consolidated financial statements have been prepared in compliance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB") and Interpretations of the International Financial Reporting Interpretations Committee ("IFRIC") which the Canadian Accounting Standards Board has approved for incorporation into Part 1 of the Chartered Professional Accountants of Canada including IAS 34 Interim Financial Reporting. The condensed interim consolidated financial statements should be read in conjunction with the annual consolidated financial statements for the year ended December 31, 2014.

The accounting policies and the application adopted are consistent with those disclosed in Note 3 to the Company's consolidated financial statements for the year ended December 31, 2014.

Areas of critical accounting estimates and judgments that have the most significant effect on the amounts recognized in the condensed interim consolidated financial statements are disclosed in Note 4 of the Company's consolidated financial statements as at and for the year ended December 31, 2014.

All financial information presented in USD has been rounded to the nearest thousand unless otherwise stated.

These condensed interim consolidated financial statements were approved by the Board of Directors for issue on August 12, 2015.

### *b. Going Concern*

These condensed interim consolidated financial statements have been prepared in accordance with IFRS applicable to a going concern which contemplates the realization of assets and settlement of liabilities in the normal course of business as they become due. For the three and six months ended June 30, 2015, the Company reported a net loss of $1,821 and $2,058 respectively and the Company's working capital has also declined during the three and six month period to $4,016 as at June 30, 2015. The Company must secure sufficient funding to cover continued reductions on margins should silver price remain at current price levels in order to meet current liabilities and capital expenditure requirements at its operating mine in Mexico. These circumstances lend significant doubt as to the ability of the Company to meet its obligations as they come due and, accordingly, the appropriateness of the use of accounting principles applicable to a going concern. Management is pursuing financing alternatives to fund the Company's operations so it can continue as a going concern. Management plans to secure the necessary financing through a combination of equity and debt instrument arrangements. Nevertheless, there is no assurance that these initiatives will be successful.

The Company's ability to continue as a going concern is dependent upon its ability to generate positive cash flows from operations. These financial statements do not reflect the adjustments to the carrying values of assets and liabilities and the reported expenses and balance sheet classifications that would be necessary if the company were unable to realize its assets and settle its liabilities as a going concern in the normal course of operations. Such adjustments could be material.

(Unaudited) (in thousands of U.S. dollars, except share data)

## 3. INVENTORIES

| | June 30, 2015 $ | December 31, 2014 $ |
|---|---|---|
| Ore | 198 | 165 |
| Concentrate | - | 275 |
| Production spares | 1,568 | 1,924 |
| | 1,766 | 2,364 |

As at June 30, 2015, the Company delivered the entire concentrate production at the mill leaving a nil balance.

(Unaudited) (in thousands of U.S. dollars, except share data)

## 4. PROPERTY, PLANT AND EQUIPMENT

| | Mining properties $ | Mining equipment $ | Processing equipment $ | Assets under construction $ | Total $ |
|---|---|---|---|---|---|
| At January 1, 2014 | | | | | |
| Cost | 25,293 | 12,055 | 7,829 | 30 | 45,207 |
| Accumulated amortization | (14,189) | (5,676) | (4,182) | - | (24,047) |
| | 11,104 | 6,379 | 3,647 | 30 | 21,160 |
| **Year ended December 31, 2014** | | | | | |
| Opening net book value | 11,104 | 6,379 | 3,647 | 30 | 21,160 |
| Additions | 1,973 | 883 | 21 | 463 | 3,340 |
| Reclassification | - | - | 132 | (132) | - |
| Amortization | (1,441) | (1,394) | (849) | - | (3,684) |
| Write-down | - | (153) | - | (8) | (161) |
| Exchange differences | (1,251) | (647) | (340) | (33) | (2,271) |
| Closing net book value | 10,385 | 5,068 | 2,611 | 320 | 18,384 |
| At December 31, 2014 | | | | | |
| Cost | 24,482 | 11,072 | 7,094 | 320 | 42,968 |
| Accumulated amortization | (14,097) | (6,004) | (4,483) | - | (24,584) |
| | 10,385 | 5,068 | 2,611 | 320 | 18,384 |
| **Period ended June 30, 2015** | | | | | |
| Opening net book value | 10,385 | 5,068 | 2,611 | 320 | 18,384 |
| Additions | 543 | - | - | 116 | 659 |
| Amortization | (663) | (573) | (356) | - | (1,592) |
| Exchange differences | (573) | (259) | (132) | (23) | (987) |
| Closing net book value | 9,692 | 4,236 | 2,123 | 413 | 16,464 |
| At June 30, 2015 | | | | | |
| Cost | 23,608 | 10,463 | 6,707 | 413 | 41,191 |
| Accumulated amortization | (13,916) | (6,227) | (4,584) | - | (24,727) |
| | 9,692 | 4,236 | 2,123 | 413 | 16,464 |

(Unaudited) (in thousands of U.S. dollars, except share data)

## 5. MINERAL RIGHTS

| | Platosa (Mexico) $ | Beschefer (Canada) $ | DeSantis (Canada) $ | Total $ |
|---|---|---|---|---|
| At January 1, 2014 | | | | |
| Cost | 4,755 | 8,176 | 11,116 | 24,047 |
| Accumulated amortization | (1,320) | - | - | (1,320) |
| | 3,435 | 8,176 | 11,116 | 22,727 |
| **Year ended December 31, 2014** | | | | |
| Opening net book value | 3,435 | 8,176 | 11,116 | 22,727 |
| Amortization | (422) | - | - | (422) |
| Impairments (1) | - | (6,084) | (9,379) | (15,463) |
| Exchange differences | (53) | (369) | (445) | (867) |
| Closing net book value | 2,960 | 1,723 | 1,292 | 5,975 |
| At December 31, 2014 | | | | |
| Cost | 4,534 | 1,723 | 1,292 | 7,549 |
| Accumulated amortization | (1,574) | - | - | (1,574) |
| | 2,960 | 1,723 | 1,292 | 5,975 |
| **Period ended June 30, 2015** | | | | |
| Opening net book value | 2,960 | 1,723 | 1,292 | 5,975 |
| Additions | 10 | - | - | 10 |
| Amortization | (170) | - | - | (170) |
| Exchange differences | (174) | (109) | (81) | (364) |
| Closing net book value | 2,626 | 1,614 | 1,211 | 5,451 |
| At June 30, 2015 | | | | |
| Cost | 4,277 | 1,614 | 1,211 | 7,102 |
| Accumulated amortization | (1,651) | - | - | (1,651) |
| | 2,626 | 1,614 | 1,211 | 5,451 |

(1) At September 30, 2014, the Company wrote down the value of its Beschefer and DeSantis exploration properties in Canada following a review of the Company's portfolio of mineral property assets. The impairment consideration was based on current valuations attributable to similar stage projects in similar jurisdictions, which valuations are related, in part, to current commodity prices, equity market conditions and the availability of exploration financing for such projects. The recoverable amounts of each property have been estimated to be less than its carrying value, resulting in an impairment of $15,463 being recognized in 2014.

(Unaudited) (in thousands of U.S. dollars, except share data)

## 6. PROVISIONS

| | Post-retirement benefits (1) | Rehabilitation provision | DSU and RSU | Total |
|---|---|---|---|---|
| | $ | $ | $ | $ |
| **Year ended December 31, 2014** | | | | |
| Opening balance | 323 | 1,276 | 184 | 1,783 |
| Change in estimate | 423 | 104 | - | 527 |
| Accretion for the year | - | 86 | - | 86 |
| Reclassified to contributed surplus (2) | - | - | (161) | (161) |
| Exchange differences | (77) | (151) | (23) | (251) |
| Closing Balance | 669 | 1,315 | - | 1,984 |
| **Period ended June 30, 2015** | | | | |
| Opening balance | 669 | 1,315 | - | 1,984 |
| Change in estimate | 84 | - | - | 84 |
| Accretion for the period | - | 35 | - | 35 |
| Exchange differences | (39) | (73) | - | (112) |
| Closing Balance | 714 | 1,277 | - | 1,991 |

(1) Post-retirement benefits: The Company provides post retirement benefits supplements as well as leaving indemnities to employees at the Mexican operations. Under Mexican Labour Law, the Company provides statutorily mandated severance benefits to its employees terminated under certain circumstances. Such benefits consist of a one-time payment of three months wages plus 20 days wages for each year of service payable upon involuntary termination without just cause.

Key financial assumptions used in the above estimate include an annual discount rate of 6.5% (December 31, 2014 – 6.5%) based on the yield curve from short and long term Mexican government bonds, annual salary and minimum wage increase rate of 3.6% (December 31, 2014 – 3.6%) and the life of mine of five years.

(2) Prior to the amendment of the DSU and RSU Plans in April 2014, the expense related to DSUs and RSUs granted in 2013 was credited to liabilities since the payment method was in cash. Upon the adoption of the amended DSU and RSU Plans in 2014, the balance was reclassified from provisions to equity under contributed surplus since the payment in cash or common shares is at the option of the Company.

(Unaudited) (in thousands of U.S. dollars, except share data)

## 7. SHARE CAPITAL

| | Number of shares (000's) | $ |
|---|---|---|
| **Year ended December 31, 2014** | | |
| Opening balance | 54,989 | 77,434 |
| Shares issued on exercise of stock options | 3 | 5 |
| Shares purchased under normal course issuer bid | (88) | (116) |
| Balance at December 31, 2014 | 54,904 | 77,323 |
| **Period ended June 30, 2015** | | |
| Opening balance | 54,904 | 77,323 |
| Exercise of DSU shares | 55 | 29 |
| Balance at June 30, 2015 | 54,959 | 77,352 |

*SHARE OPTION PROGRAM (EQUITY-SETTLED)*

The Company has a share option program that entitles directors, officers, employees and consultants to purchase shares in the Company. Under the program, the Company may grant options for up to 10% of the common shares issued and outstanding. The exercise price of each option may not be less than the market price of the Company's common shares on the date of grant, and an option's maximum term is five years. Options may be granted by the board of directors at any time with varying vesting conditions.

(Unaudited) (in thousands of U.S. dollars, except share data)

*Disclosure of share option program*

The number and weighted average exercise prices of share options are as follows:

| | Weighted Average Exercise Price (CAD) | Options |
|---|---|---|
| Outstanding at January 1, 2014 | $ 2.70 | 3,144,500 |
| Granted | $ 1.38 | 100,000 |
| Exercised | $ 1.14 | (2,500) |
| Expired | $ 2.81 | (470,000) |
| Forfeited | $ 1.87 | (20,000) |
| Outstanding at December 31, 2014 | $ 2.65 | 2,752,000 |
| Exercisable at December 31, 2014 | $ 2.88 | 2,216,160 |

| | | |
|---|---|---|
| Outstanding at January 1, 2015 | 2.65 | 2,752,000 |
| Granted | $ 0.58 | 665,000 |
| Expired | $ 4.95 | (20,000) |
| Forfeited | $ 0.82 | (88,333) |
| Outstanding at June 30, 2015 | $ 2.27 | 3,308,667 |
| Exercisable at June 30, 2015 | $ 2.63 | 2,636,168 |

As at June 30, 2015, the following stock options were outstanding and exercisable:

| CAD | Stock Options Outstanding | Weighted Average Remaining Contractual Life (years) | Stock Options Exercisable | Weighted Average Exercise Price (CAD) |
|---|---|---|---|---|
| $0.50 to $0.99 | 615,001 | 4.76 | 221,676 | $ 0.58 |
| $1.14 to $1.49 | 831,666 | 3.52 | 562,492 | $ 1.16 |
| $1.50 to $1.99 | 130,000 | 2.92 | 120,000 | $ 1.72 |
| $2.00 to $5.21 | 1,732,000 | 1.61 | 1,732,000 | $ 3.43 |
| | 3,308,667 | 2.73 | 2,636,168 | $ 2.63 |

(Unaudited) (in thousands of U.S. dollars, except share data)

*Inputs for measurement of grant date fair values*

The grant date fair value of the share option program was measured based on the Black-Scholes formula. Expected volatility is estimated by considering historic average share price volatility. The inputs used in the measurement of the fair values at grant date of the share option program were the following:

| | Six months ended June 30, 2015 | 2014 |
|---|---|---|
| Fair value at grant date | $0.35 | $0.84 |
| Share price at grant date | $0.58 | $1.38 |
| Exercise price | $0.58 | $1.38 |
| Risk free interest rate | 0.61% | 1.47% |
| Expected life of options in years | 5.00 | 5.00 |
| Expected volatility | 73.89% | 73.97% |
| Expected dividend yield | 0.00% | 0.00% |
| Estimated forfeiture rate | 3.57% | 4.09% |

*Share-based compensation expense*

Compensation expense is recognized over the vesting period of the grant with the corresponding equity impact recorded in contributed surplus. Share-based compensation expense is comprised of the following costs:

| | Three months ended | | Six months ended | |
|---|---|---|---|---|
| | June 30, 2015 $ (CAD) | June 30, 2014 $ (CAD) | June 30, 2015 $ (CAD) | June 30, 2014 $ (CAD) |
| Share options granted in 2012 | - | 37 | - | 67 |
| Share options granted in 2013 | 8 | 120 | 46 | 258 |
| Share options granted in 2014 | 7 | 18 | 17 | 18 |
| Share options granted in 2015 | 97 | - | 103 | - |
| | 112 | 175 | 166 | 343 |

*DEFERRED SHARE UNITS ("DSU")*

During 2013, the Company implemented a DSU plan for directors of the Corporation, which was subsequently amended and approved by the Company's shareholders on April 29, 2014. Pursuant to the new plan, DSUs can be paid in cash or in awards of common shares either from treasury or from market purchases based on the five-day volume weighted average price ("Market Price") of the Company's publicly traded common shares on settlement dates elected by a director between the retirement date and December 15th of the calendar year subsequent to the year of the director's retirement. All grants under the plan are fully vested upon credit to an eligible directors' account. The value of the cash payout is determined by multiplying the number of DSUs vested at the payout date by the Market Price of the Company's shares. The expense is recorded in the consolidated statement of loss and comprehensive loss in share based payments and credited to equity under contributed surplus since the payment in cash or common shares is at the option of the Company.

Prior to the amendment of the DSU Plan in 2014, the expense related to DSUs granted was credited to provisions since the settlement method was in cash. Upon the adoption of the amended DSU Plan, the balance was reclassified from provisions to equity under contributed surplus.

During the six months ended June 30, 2015, the Company granted 320,383 DSUs (six months ended June 30, 2014 – 62,874 DSUs) with a market value of CAD$183 (six months ended June 30, 2014 - CAD$83) at the date of grant to non-executive directors as compensation in lieu of cash director fees. During the six months ended June 30, 2015, there were 55,124 DSUs settled for common shares (six months ended June 30, 2014 – nil).

Total share based compensation expensed in the six months ended June 30, 2015 related to vested DSUs was CAD$263 (six months ended June 30, 2014 – CAD$101). As at June 30, 2015, the Company has 636,685 outstanding DSUs.

*RESTRICTED SHARE UNITS ("RSU")*

During 2013, the Company implemented a RSU plan for officers and employees of the Corporation, which was subsequently amended and approved by the Company's shareholders on April 29, 2014. The RSU Plan entitles officers or employees to either a cash payment or an award of common shares from treasury or from market purchases at the end of a term or performance period of up to three years following the date of the award. The value of the cash payout is determined by multiplying the number of RSUs vested at the payout date by the Market Price of the Company's shares prior to a payout date with settlement in cash. The expense is recorded in the consolidated statement of loss and comprehensive loss in share based payments and credited to equity under contributed surplus since the payment in cash or common shares is at the option of the Company.

Prior to the amendment of the RSU Plan in 2014, the expense related to RSUs granted was credited to provisions since the payment method was in cash. Upon the adoption of the amended RSU Plan, the balance was reclassified from provisions to equity under contributed surplus.

During the six months ended June 30, 2015 the Company granted 425,000 RSUs subject to performance vesting conditions (six months ended June 30, 2014 – 15,000 RSUs subject to non-performance vesting conditions) with market value of CAD$242 (six months ended June 30, 2014 - CAD$22) at the date of grant to officers and employees.

During the six months ended June 30, 2015, there were no RSU settlements (six months ended June 30, 2014 – nil).

Total share based compensation expensed in the six months ended June 30, 2015 related to vested RSUs was CAD$54 (six months ended June 30, 2014 – CAD$55). As at June 30, 2015, the Company has 718,507 outstanding RSUs.

(Unaudited) (in thousands of U.S. dollars, except share data)

## 8. EXPENSE BY NATURE

(a) Cost of sales comprises the following:

| | Three months ended | | Six months ended | |
|---|---|---|---|---|
| | **June 30, 2015** | **June 30, 2014** | **June 30, 2015** | **June 30, 2014** |
| | **$** | **$** | **$** | **$** |
| Direct mining and milling costs (1) | 3,995 | 6,109 | 8,357 | 11,988 |
| Changes in inventories | 18 | (494) | 216 | 431 |
| Depletion, depreciation and amortization | 815 | 1,047 | 1,662 | 2,040 |
| **Cost of sales** | 4,828 | 6,662 | 10,235 | 14,459 |

(1) Direct mining and milling costs include personnel, general and administrative, fuel and electricity, maintenance and repair costs as well as operating supplies, external services, third party smelting, refining and transport fees.

(b) General and administrative expenses consist of the following:

| | Three months ended | | Six months ended | |
|---|---|---|---|---|
| | **June 30, 2015** | **June 30, 2014** | **June 30, 2015** | **June 30, 2014** |
| | **$** | **$** | **$** | **$** |
| Office and overhead costs | 250 | 439 | 546 | 885 |
| Salaries and wages | 298 | 425 | 616 | 827 |
| Share based compensation | 264 | 202 | 392 | 469 |
| Depletion and amortization | 50 | 76 | 100 | 146 |
| **General and administrative expenses** | 862 | 1,142 | 1,654 | 2,327 |

(c) Other expense (income) consist of the following:

| | Three months ended | | Six months ended | |
|---|---|---|---|---|
| | **June 30, 2015** | **June 30, 2014** | **June 30, 2015** | **June 30, 2014** |
| | **$** | **$** | **$** | **$** |
| Unrealized loss (gain) on marketable securities | - | (99) | - | (354) |
| Foreign exchange loss (gain) | 722 | 980 | 172 | 135 |
| **Other expense (income)** | 722 | 881 | 172 | (219) |

(Unaudited) (in thousands of U.S. dollars, except share data)

## 9. RELATED PARTIES

The corporate secretary of the Company is a partner in a firm that provides legal services to the Company. During the three month ended June 30, 2015, the Company incurred legal services of $8 (three months ended June 30, 2014 - $12). During the six months ended June 30, 2015, the Company incurred legal services of $32 (six months ended June 30, 2014 – $32) with an outstanding payable balance of $33 at June 30, 2015 (June 30, 2014 – $nil).

## 10. INCOME TAX

Income tax expense is recognized based on management's best estimate of the weighted average annual income tax rate expected for the full financial year. The estimated average annual rate used for the year ended December 31, 2014 was 26.5% and the six months ended June 30, 2015 was 26.5%.

In 2013, the Mexican tax authority (Servicio de Administración Tributaria – "SAT") in the state of Zacatecas completed an income tax audit of the 2008 and 2009 years in respect of one of the Company's Mexican subsidiaries. As a result of this audit, on February 24, 2014 and March 13, 2014 the Company received notice of reassessments from SAT for 2009 and 2008 respectively, denying deductions in the amount of 115.2 million pesos ($7,400) and 72.9 million pesos ($4,700) respectively that relate primarily to foreign exchange losses. The combined impact of the 2009 and 2008 reassessments is a reduction in the available non-capital loss balance totaling 188.1 million pesos ($12,100), which, consequently, would result in a reduction in the deferred tax asset balance of $3,600 and a corresponding increase in deferred income tax expense. Management was of the view that there was a strong case to support the Company's position, particularly because the SAT has only made adjustments to foreign exchange losses but has not made offsetting adjustments to foreign exchange gains recognized in the same period. Accordingly, the Company appealed the 2008 and 2009 reassessments through the SAT's appeal procedures.

In December 2014, the Company was notified by SAT that a favourable resolution had been issued, confirming the Company's tax treatment of the foreign exchange losses in its 2009 annual tax return. This resolution should also support the tax treatment that was previously denied in the 2008 tax return, for which the appeal remained outstanding at the end of the period. Accordingly, management believes, based on the tax advice from its tax advisors that it is more likely than not that that the Company's position will be sustained and no amounts related to this issue has been recorded in the financial statements as of June 30, 2015 and December 31, 2014

## 11. SEGMENT REPORTING

| | MEXICO | | CANADA | | TOTAL | |
|---|---|---|---|---|---|---|
| | June 30, 2015 $ | Dec 31, 2014 $ | June 30, 2015 $ | Dec 31, 2014 $ | June 30, 2015 $ | Dec 31, 2014 $ |
| Property, plant and equipment | 16,464 | 18,384 | - | - | 16,464 | 18,384 |
| Capital expenditures | (659) | (3,340) | - | - | (659) | (3,340) |
| Mineral rights | 2,626 | 2,960 | 2,825 | 3,015 | 5,451 | 5,975 |
| Total assets | 35,660 | 38,655 | 4,266 | 5,156 | 39,926 | 43,811 |

(Unaudited) (in thousands of U.S. dollars, except share data)

| | Three months ended | | Six months ended | |
|---|---|---|---|---|
| | **June 30, 2015** | **June 30, 2014** | **June 30, 2015** | **June 30, 2014** |
| | **$** | **$** | **$** | **$** |
| **MEXICO** | | | | |
| Revenue | 4,036 | 8,792 | 9,091 | 19,328 |
| Cost of sales | (4,828) | (6,662) | (10,235) | (14,459) |
| Exploration | (175) | (181) | (383) | (404) |
| Other expenses | (826) | (881) | 118 | (1,095) |
| Net finance costs | (18) | (22) | (44) | (44) |
| Income tax | 761 | (615) | 1,370 | (1,035) |
| Net income (loss) | (1,050) | 431 | (83) | 2,291 |
| **CANADA** | | | | |
| General and administrative expenses | (862) | (1,142) | (1,654) | (2,327) |
| Exploration | (13) | - | (31) | (114) |
| Other expenses | 104 | - | (290) | 1,314 |
| Net income (loss) | (771) | (1,142) | (1,975) | (1,127) |
| **Net income (loss)** | **(1,821)** | **(711)** | **(2,058)** | **1,164** |

## 12. REVENUES

Under the terms of the Company's concentrate sales contracts, lead–silver and zinc-silver concentrates are sold on a provisional pricing basis whereby sales are recognized at prevailing metal prices when the revenue recognition criteria have been met, namely when title, and risks and rewards of ownership have transferred to the customer. Revenue is recorded net of treatment and refining charges. Final pricing of each delivery is not determined until one or two months post-delivery. The price recorded at the time of sale may differ from the actual final price received from the customer due to changes in market prices for metals. The price volatility is considered an embedded derivative in accounts receivable. The embedded derivative is recorded at fair value at each reporting period until settlement occurs, with the changes in fair value recorded to revenues.

During the three months ended June 30, 2015, the Company recognized positive adjustment to revenues of $243 related to sales made prior to April 1, 2015 as receivables were ultimately settled at higher values during the quarter (three months ended June 30, 2014 – negative adjustment of $130).

During the six months ended June 30, 2015, the Company recognized positive adjustment to revenues of $136 primarily related to the reversal of the mark to market taken at the end of 2014 as receivables were ultimately settled at higher values in 2015 (six months ended June 30, 2014 – positive adjustment of $893).

As at June 30, 2015, unsettled provisionally priced sales totalled $2,570. A 10% increase or decrease in the price of silver, lead and zinc will result in a corresponding increase or decrease in revenues of $257 during the third quarter of 2015.