

# **NETCO SILVER INC.**

## **Unaudited Condensed Interim Consolidated Financial Statements** (Expressed in Canadian dollars)

**For the Six Months Ended June 30, 2012 and 2011**

### **Index**

#### **Notice of No Auditor Review of Interim Financial Statements**

#### **Condensed Interim Consolidated Financial Statements**

Condensed Interim Consolidated Statements of Financial Position

Condensed Interim Consolidated Statements of Comprehensive Loss

Condensed Interim Consolidated Statement of Changes in Shareholders' Equity

Condensed Interim Consolidated Statements of Cash Flows

Notes to the Condensed Interim Consolidated Financial Statements

## **NOTICE OF NO AUDITOR REVIEW OF INTERIM FINANCIAL STATEMENTS**

In accordance with National Instrument 51-102, Part 4, subsection 4.3(3) released by the Canadian Securities Administrators, the Company discloses that its auditors have not reviewed these unaudited condensed interim consolidated financial statements as at and for the six months ended June 30, 2012 and 2011.



## Netco Silver Inc.

### Condensed Interim Consolidated Statements of Comprehensive Loss For the period ended June 30, 2012, with comparative figures for 2011

(Unaudited - Prepared by Management)

(Expressed in Canadian dollars)

	Notes	For the six months ended June 30 2012	For the three months ended June 30 2012	For the six months ended June 30 2011	For the three months ended June 30 2011
<b>GENERAL AND ADMINISTRATION EXPENSES</b>					
Director and officer fees	11	\$ -	-	\$ 12,000	\$ 6,000
Office and general		72,693	40,823	30,063	14,710
Professional fees		91,108	58,558	32,671	24,476
Management fees	11	93,900	46,669	13,440	13,440
Transfer agent and filing		14,275	2,434	23,138	15,802
Share-based compensation	9	23,630	23,630	106,385	36,648
		<b>295,606</b>	<b>172,114</b>	<b>217,697</b>	<b>111,076</b>
<b>Loss before other items</b>		<b>(295,606)</b>	<b>(172,114)</b>	<b>(217,697)</b>	<b>(111,076)</b>
<b>OTHER ITEMS</b>					
Foreign exchange gain (loss)		1,135	(7,942)	(820)	116
Interest and miscellaneous income		658	426	-	-
		<b>1,793</b>	<b>(7,516)</b>	<b>(820)</b>	<b>(61)</b>
<b>Loss before income tax</b>		<b>(293,813)</b>	<b>(179,630)</b>	<b>(218,517)</b>	<b>(111,137)</b>
<b>Comprehensive loss for the period</b>		<b>\$ (293,813)</b>	<b>(179,630)</b>	<b>\$ (218,517)</b>	<b>\$ (111,137)</b>
<b>Basic and diluted loss per share</b>		<b>\$ (0.01)</b>	<b>\$ (0.00)</b>	<b>\$ (0.01)</b>	<b>\$ (0.00)</b>
<b>Weighted average shares outstanding</b>		<b>42,563,070</b>	<b>42,563,070</b>	<b>33,823,330</b>	<b>33,823,330</b>

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

## Netco Silver Inc.

### Condensed Interim Consolidated Statement of Changes in Shareholders' Equity For the period ended June 30, 2012 and 2011

(Unaudited - Prepared by Management)

(Expressed in Canadian dollars)

	Number of Shares	Share Capital	Contributed Surplus	Deficit	Total
<b>Balance as at January 1, 2012</b>	40,323,275	\$ 18,041,108	\$ 717,380	\$(18,348,896)	\$ 409,592
Share-based compensation	-	-	36,454	-	36,454
Issue of share capital	6,685,000	792,929	-	-	792,929
Total comprehensive loss for the period	-	-	-	(293,813)	(293,813)
<b>Balance as at June 30, 2012</b>	<b>47,008,275</b>	<b>\$ 18,834,037</b>	<b>\$ 753,834</b>	<b>\$(18,642,709)</b>	<b>\$ 945,162</b>

	Number of Shares	Share Capital	Contributed Surplus	Deficit	Total
<b>Balance as at January 1, 2011</b>	33,683,275	\$ 17,276,465	\$ 495,807	\$(17,642,017)	\$ 130,255
Share-based compensation	-	-	106,386	-	106,386
Issue of share capital	140,055	756,160	-	-	756,160
Total comprehensive loss for the period	-	-	-	(218,517)	(218,517)
<b>Balance as at June 30, 2011</b>	<b>33,823,330</b>	<b>\$ 18,032,625</b>	<b>\$ 602,193</b>	<b>\$(17,860,534)</b>	<b>\$ 774,284</b>

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

## Netco Silver Inc.

### Consolidated Statements of Cash Flows

For the period ended June 30, 2012, with comparative figures for 2011

(Unaudited - Prepared by Management)

(Expressed in Canadian dollars)

	For the six months ended June 30, 2012	For the six months ended June 30, 2011
<b>CASH FLOWS PROVIDED BY (USED IN):</b>		
<b>Operating activities</b>		
Net loss for the period from continuing operations	\$ (293,813)	\$ (218,517)
Adjustment for items not involving cash:		
Foreign exchange loss	(1,135)	(820)
Share based compensation	-	106,386
	<b>(294,948)</b>	<b>(112,951)</b>
Changes in non-cash working capital:		
Increase in accounts receivable	(33,204)	(50,348)
Increase in accounts payable	22,613	(6,477)
Increase in harmonized sales tax recoverable	(5,218)	(4,320)
Increase in prepaid expenses	(11,635)	-
	<b>(322,392)</b>	<b>(174,096)</b>
<b>Investing activities</b>		
Acquisition of exploration and evaluation assets	(556,646)	(59,847)
Increase (decrease) in loans receivable	-	174
	<b>(556,646)</b>	<b>(59,673)</b>
<b>Financing activities</b>		
Issuance of common shares	829,383	756,160
	<b>829,383</b>	<b>756,160</b>
<b>Effect of foreign currency translation on cash and cash equivalents</b>	<b>1,135</b>	<b>820</b>
<b>Increase (decrease) in cash and cash equivalents</b>	<b>(48,520)</b>	<b>523,211</b>
<b>Cash and cash equivalents, beginning of period</b>	<b>249,036</b>	<b>63,861</b>
<b>Cash and cash equivalents, end of period</b>	<b>\$ 200,516</b>	<b>\$ 587,072</b>

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

# NETCO SILVER INC.

Notes to the Unaudited Condensed Interim Consolidated Financial Statements  
(Expressed in Canadian Dollars)

For the Six Months Ended June 30, 2012 and 2011

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## 1. NATURE AND CONTINUANCE OF OPERATIONS

Netco Silver Inc. (the "Company") is a publicly listed company incorporated in Canada with limited liability under the legislation of the Provinces of British Columbia and Alberta. The Company's shares are listed on the TSX Venture Exchange. The head office, principal address is 609 Granville Street, Suite 880, Vancouver, British Columbia, Canada, V7Y 1G5.

The unaudited condensed interim consolidated financial statements ("interim financial statements") of the Company as at and for the six months ended June 30, 2012 comprise the Company and its subsidiaries (together referred to as the "Group"). The Group primarily is involved in the mining and petroleum and natural gas industries.

These interim financial statements have been prepared on the basis of accounting principles applicable to a going concern, which assumes that the Group will be able to continue in operation for the foreseeable future and will be able to realize its assets and discharge its liabilities and commitments in the normal course of business.

The Group currently has no source of revenues, has working capital of \$160,730 (December 31, 2011 - \$181,806) and a deficit of \$18,642,709 (December 31, 2011 - \$18,348,896). 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. The Group's ability to continue as a going concern is dependent upon achieving profitable operations and upon obtaining additional financing. The outcome of these matters cannot be predicted at this time. These financial statements do not include any adjustments to the amounts and classification of assets and liabilities that might be necessary should the Company be unable to continue in business.

## 2. BASIS OF PREPARATION

### (a) Statement of compliance:

These interim financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS").

These interim financial statements have been prepared in accordance with International Accounting Standard 34 Interim Financial Reporting. They do not include all the information required for full annual financial statements.

These interim financial statements were approved by the Board of Directors on August 29, 2012.

# NETCO SILVER INC.

Notes to the Unaudited Condensed Interim Consolidated Financial Statements  
(Expressed in Canadian Dollars)

For the Six Months Ended June 30, 2012 and 2011

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## 2. BASIS OF PREPARATION (continued)

(b) Functional and presentation currency:

These consolidated financial statements are presented in Canadian dollars, which is the Group's functional currency.

(c) Basis of measurement:

The interim financial statements have been prepared on the historical cost basis except for financial assets classified as fair value through profit or loss which are stated at their fair value.

In addition, these interim financial statements have been prepared using the accrual basis of accounting, except for cash flow information.

(d) Use of estimates and judgments:

The preparation of financial statements in compliance with IFRS requires management to make certain judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results may differ from these estimates and assumptions.

The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgments about carrying values of assets and liabilities that are not readily apparent from other sources.

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 years affected.

### Significant accounting estimates

- a. The inputs used in accounting for share-based payments in profit or loss;
- b. The assessment of indications of impairment of each property and related determination of the net realizable value and write-down of those properties where applicable;
- c. The tax basis of assets and liabilities and related deferred income tax assets and liabilities;
- d. Amounts of provisions, if any, for decommissioning obligations; and
- e. Rates of depletion and accretion of petroleum and natural gas interests.



# NETCO SILVER INC.

Notes to the Unaudited Condensed Interim Consolidated Financial Statements  
(Expressed in Canadian Dollars)

For the Six Months Ended June 30, 2012 and 2011

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## 2. BASIS OF PREPARATION (continued)

(d) Use of estimates and judgments (continued):

Significant accounting judgments

- a. The determination of categories of financial assets and financial liabilities has been identified as an accounting policy which involves judgments or assessments made by management; and
- b. The analysis of the functional currency for each entity of the Group. In concluding that the Canadian dollar is the functional currency of the parent and its subsidiary companies, management considered the currency that mainly influences the cost of providing goods and services in each jurisdiction in which the Company operates. As no single currency was clearly dominant, management also considered secondary indicators including the currency in which funds from financing activities are denominated and the currency in which funds are retained.

## 3. SIGNIFICANT ACCOUNTING POLICIES

The accounting policies set out below have been applied consistently to all periods presented in these interim financial statements, and have been applied consistently by the Group.

(a) Basis of consolidation

(i) Subsidiaries:

The interim financial statements of the Company include its wholly-owned subsidiaries, Green River Petroleum (USA) Inc., incorporated in the State of Wyoming and in the State of Washington, USA and Netco Argentina S.A., incorporated in Argentina. All inter-company transactions and balances have been eliminated on consolidation.

Subsidiaries are entities controlled by the Company. Control exists when the Company has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, potential voting rights that currently are exercisable are taken into account. The financial statements of a subsidiary are included in the consolidated financial statements from the date that control commences until the date that control ceases.

(ii) Jointly controlled operations and jointly controlled assets:

Many of the Group's resource activities and oil and natural gas activities involve jointly controlled assets. The interim financial statements include the Group's share of these jointly controlled assets and a proportionate share of the relevant revenue and related costs.

# NETCO SILVER INC.

Notes to the Unaudited Condensed Interim Consolidated Financial Statements  
(Expressed in Canadian Dollars)

For the Six Months Ended June 30, 2012 and 2011

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## 3. SIGNIFICANT ACCOUNTING POLICIES (continued)

### (a) Basis of consolidation (continued)

#### (iii) Transactions eliminated on consolidation:

Intercompany balances and transactions, and any unrealized income and expenses arising from intercompany transactions, are eliminated in preparing the consolidated financial statements.

### (b) Foreign Currency

Transactions in currencies other than the functional currency are recorded at the rates of exchange prevailing on dates of transactions. At each financial position reporting date, monetary assets and liabilities that are denominated in foreign currencies are translated at the rates prevailing at the date when the fair value was determined. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated.

### (c) Financial instruments

#### Financial Assets

All financial assets are initially recorded at fair value and designated upon inception into one of the following four categories: held-to-maturity, available-for-sale, loans-and-receivables or at fair value through profit or loss ("FVTPL").

Financial assets classified as FVTPL are measured at fair value with unrealized gains and losses recognized through profit and loss. Regular way purchases and sales of FVTPL financial assets are accounted for at trade date, as opposed to settlement date. The Group has classified its cash and cash equivalents as FVTPL.

Financial assets classified as loans-and-receivables and held-to-maturity are measured at amortized cost. The Group's accounts and loan receivables are classified as loans-and-receivables.

Financial assets classified as available-for-sale are measured at fair value with unrealized gains and losses recognized in other comprehensive income (loss) except for losses in value that are considered other than temporary. The Group has not classified any financial asset as available-for-sale.

# NETCO SILVER INC.

Notes to the Unaudited Condensed Interim Consolidated Financial Statements  
(Expressed in Canadian Dollars)

For the Six Months Ended June 30, 2012 and 2011

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## 3. SIGNIFICANT ACCOUNTING POLICIES (continued)

### (c) Financial instruments (continued)

#### Financial Assets (continued)

Transactions costs associated with FVTPL and available-for-sale financial assets are expensed as incurred, while transaction costs associated with all other financial assets are included in the initial carrying amount of the asset.

#### Financial liabilities

All financial liabilities are initially recorded at fair value and designated upon inception as FVTPL or other-financial-liabilities.

Financial liabilities classified as other-financial-liabilities are initially recognized at fair value less directly attributable transaction costs. After initial recognition, other-financial-liabilities are subsequently measured at amortized cost using the effective interest method. The effective interest method is a method of calculating the amortized cost of a financial liability and of allocating interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments through the expected life of the financial liability, or, where appropriate, a shorter period. The Group's accounts payable and accrued liabilities and loan are classified as other-financial-liabilities.

Financial liabilities classified as FVTPL include financial liabilities held for trading and financial liabilities designated upon initial recognition as FVTPL. Derivatives, including separated embedded derivatives are also classified as held for trading unless they are designated as effective hedging instruments. Fair value changes on financial liabilities classified as FVTPL are recognized through profit and loss. The Group has not classified any financial liabilities as FVTPL.

The Group is not engaged in any financial derivative contracts.

### (d) Cash and cash equivalents:

Cash and cash equivalents comprise cash on hand, and cash equivalents with original maturities of three months or less that are readily convertible into cash and which are subject to insignificant risk of changes in value.

# NETCO SILVER INC.

Notes to the Unaudited Condensed Interim Consolidated Financial Statements  
(Expressed in Canadian Dollars)

For the Six Months Ended June 30, 2012 and 2011

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## 3. SIGNIFICANT ACCOUNTING POLICIES (continued)

### (e) Exploration and evaluation assets

Exploration and evaluation (“E&E”) costs are those expenditures incurred on properties for which technical feasibility and commercial viability have not been determined. Exploration and evaluation costs, including the costs of acquiring licenses, acquisition of rights to explore, geological and geophysical, drilling, sampling, trenching and survey costs, decommissioning and often directly attributable internal costs, initially are capitalized as exploration and evaluation assets. The costs are accumulated in cost centres by well, field or exploration area and not depreciated pending determination of technical feasibility and commercial viability.

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. For purposes of impairment testing, exploration and evaluation assets are allocated to cash-generating units.

The technical feasibility and commercial viability of extracting a mineral resource is considered to be determinable when proven and/or probable reserves are determined to exist. A review of each exploration license or field is carried out, at least annually, to ascertain whether proven and/or probable reserves have been discovered. Upon determination of proven and/or probable reserves, exploration and evaluation assets attributable to those reserves are first tested for impairment and then reclassified from exploration and evaluation assets to property, plant and equipment or expensed to exploration and evaluation impairments.

### (f) Property, plant and equipment

Items of property, plant and equipment, which include oil and natural gas development and production assets, are measured at cost less accumulated depletion and depreciation and accumulated impairment losses. Development and production assets are grouped into Cash Generating Units (“CGU’s”) for impairment testing.

Gains and losses on disposal of an item of property, plant and equipment, including oil and natural gas interests, are determined by comparing the proceeds from disposal with the carrying amount of property, plant and equipment and are recognized net within “other income” or “other expenses” in profit or loss.

Costs incurred subsequent to the determination of technical feasibility and commercial viability and the costs of replacing parts of property, plant and equipment are recognized as oil and natural gas interests only when they increase the future economic benefits embodied in the specific asset to which they relate. All other expenditures are recognized in profit or loss as incurred. Such capitalized oil and natural gas interests generally represent costs incurred in developing proved and/or probable reserves and bringing in or enhancing production from such reserves, and are accumulated on a field or geotechnical area basis. The carrying amount of any replaced or sold component is derecognized.

# NETCO SILVER INC.

Notes to the Unaudited Condensed Interim Consolidated Financial Statements  
(Expressed in Canadian Dollars)

For the Six Months Ended June 30, 2012 and 2011

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## 3. SIGNIFICANT ACCOUNTING POLICIES (continued)

### (f) Property, plant and equipment (continued)

The costs of the day-to-day servicing of property, plant and equipment are recognized in profit or loss as incurred.

Depletion and depreciation:

The net carrying value of development or production assets is depleted using the unit of production method by reference to the ratio of production in the year to the related proven reserves. These estimates are reviewed by independent reserve engineers at least annually.

Proven reserves are estimated using independent reserve engineer reports and represent the estimated quantities of crude oil, natural gas and natural gas liquids which geological, geophysical and engineering data demonstrate with a specified degree of certainty to be recoverable in future years from known reservoirs and which are considered commercially producible. There should be a minimum 90 percent statistical probability that the actual quantity of recoverable reserves will be more than the amount estimated as proven and a maximum 10 percent statistical probability that it will be less. Such reserves may be considered commercially producible if management has the intention of developing and producing them and such intention is based upon:

- a reasonable assessment of the future economics of such production;
- a reasonable expectation that there is a market for all or substantially all the expected oil and natural gas production; and
- evidence that the necessary production, transmission and transportation facilities are available or can be made available.

Reserves may only be considered proven if future economic feasibility is supported by either actual production or conclusive formation test. The area of reservoir considered proven includes (a) that portion delineated by drilling and defined by gas-oil and/or oil-water contacts, if any, or both, and (b) the immediately adjoining portions not yet drilled, but which can be reasonably judged as economically productive on the basis of available geophysical, geological and engineering data. In the absence of information on fluid contacts, the lowest known structural occurrence of oil and natural gas controls the lower proved limit of the reservoir.

# NETCO SILVER INC.

Notes to the Unaudited Condensed Interim Consolidated Financial Statements  
(Expressed in Canadian Dollars)

For the Six Months Ended June 30, 2012 and 2011

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## 3. SIGNIFICANT ACCOUNTING POLICIES (continued)

### (g) Impairment

#### (i) Financial assets:

A financial asset, other than those designated as FVTPL is assessed at each reporting date to determine whether there is any objective evidence that it is impaired. A financial asset is considered to be impaired if objective evidence indicates that one or more events have had a negative effect on the estimated future cash flows of that asset.

An impairment loss in respect of a financial asset measured at amortized cost is calculated as the difference between its carrying amount and the present value of the estimated future cash flows discounted at the original effective interest rate. Individually significant financial assets are tested for impairment on an individual basis. The remaining financial assets are assessed collectively in groups that share similar characteristics.

All impairment losses are recognized in profit or loss. An impairment loss is reversed if the reversal can be related objectively to an event occurring after the impairment loss was recognized.

#### (ii) Non-financial assets:

For the purpose of impairment testing, assets are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups of assets (the CGU). The recoverable amount of an asset or a CGU is the greater of its value in use and its fair value less costs to sell.

In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. Value in use is generally computed by reference to the present value of the future cash flows expected to be derived from production of proven and probable reserves. An impairment loss is recognized if the carrying amount of an asset or its CGU exceeds its estimated recoverable amount. Impairment losses are recognized in profit or loss. Impairment losses recognized in respect of CGU's are allocated first to reduce the carrying amount of any goodwill allocated to the units and then to reduce the carrying amounts of the other assets in the unit (group of units) on a pro rata basis.

Impairment losses recognized in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. 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 depletion and depreciation or amortization, if no impairment loss had been recognized.

# NETCO SILVER INC.

Notes to the Unaudited Condensed Interim Consolidated Financial Statements  
(Expressed in Canadian Dollars)

For the Six Months Ended June 30, 2012 and 2011

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## 3. SIGNIFICANT ACCOUNTING POLICIES (continued)

### (h) Decommissioning obligations

When the Group's activities give rise to dismantling, decommissioning and site disturbance remediation activities, provision is made for the estimated cost of site restoration and capitalized in the relevant asset category.

Decommissioning obligations are measured at the present value of management's best estimate of expenditure required to settle the present obligation at the statement of financial position date. Subsequent to the initial measurement, the obligation is adjusted at the end of each period to reflect the passage of time and changes in the estimated future cash flows underlying the obligation. The increase in the provision due to the passage of time is recognized as finance costs whereas increases/decreases due to changes in the estimated future cash flows are capitalized. Actual costs incurred upon settlement of the asset retirement obligations are charged against the provision.

### (i) Income taxes

Income tax expense comprises current and deferred tax. Income tax expense is recognized in profit or loss except to the extent that if the income tax expense related to items recognized directly in equity, the income tax expense would also be recognized in equity. Current tax is the expected tax payable on the taxable income for the period, 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 using the statement of financial position liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date. Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset, and they relate to income taxes levied by the same tax authority on the same taxable entity, or on different tax entities, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realized simultaneously.

A deferred tax asset is recognized to the extent that it is probable that future taxable profits will be available against which the temporary difference 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.

# NETCO SILVER INC.

Notes to the Unaudited Condensed Interim Consolidated Financial Statements  
(Expressed in Canadian Dollars)

For the Six Months Ended June 30, 2012 and 2011

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## 3. SIGNIFICANT ACCOUNTING POLICIES (continued)

### (j) Share capital

Financial instruments issued by the Company are classified as equity only to the extent that they do not meet the definition of a financial liability or financial asset. The Company's common shares, share warrants and options are classified as equity instruments.

Incremental costs directly attributable to the issue of new shares or options are recognized as a deduction from equity.

#### Valuation of equity units issued in private placements

The Company has adopted a residual value method with respect to the measurement of shares and warrants issued as private placement units. The residual value method first allocates value to the more easily measurable component based on fair value and then the residual value, if any, to the less easily measurable component.

The fair value of the common shares issued in the private placements was determined to be the more easily measurable component and were valued at their fair value, as determined by the closing quoted bid price on the announcement date. The balance, if any, was allocated to the attached warrants. Any fair value attributed to the warrants is recorded in contributed surplus.

### (k) Share-based payments

Where equity-settled share options are awarded to employees, the fair value of the options at the date of grant is charged to the statement of comprehensive loss/income over the vesting period. Performance vesting conditions are taken into account by adjusting the number of equity instruments expected to vest at each reporting date so that, ultimately, the cumulative amount recognized over the vesting period is based on the number of options that eventually vest. Non-vesting conditions and market vesting conditions are factored into the fair value of the options granted. As long as all other vesting conditions are satisfied, a charge is made irrespective of whether these vesting conditions are satisfied. The cumulative expense is not adjusted for failure to achieve a market vesting condition or where a non-vesting condition is not satisfied.

Where the terms and conditions of options are modified before they vest, the increase in the fair value of the options, measured immediately before and after the modification, is also charged to the statement of comprehensive loss over the remaining vesting period.

Where equity instruments are granted to non-employees, they are recorded at the fair value of the goods or services received in the statement of comprehensive loss/income, unless they are related to the issuance of shares. Amounts related to the issuance of shares are recorded as a reduction of share capital.



# NETCO SILVER INC.

Notes to the Unaudited Condensed Interim Consolidated Financial Statements  
(Expressed in Canadian Dollars)

For the Six Months Ended June 30, 2012 and 2011

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## 3. SIGNIFICANT ACCOUNTING POLICIES (continued)

### (k) Share-based payments (continued)

When the value of goods or services received in exchange for the share-based payment cannot be reliably estimated, the fair value is measured by use of a valuation model. The expected life used in the model is adjusted, based on management's best estimate, for the effects of non-transferability, exercise restrictions, and behavioral considerations.

All equity-settled share-based payments are reflected in contributed surplus, until exercised. Upon exercise, shares are issued from treasury and the amount reflected in contributed surplus is credited to share capital, adjusted for any consideration paid.

Where a grant of options is cancelled or settled during the vesting period, excluding forfeitures when vesting conditions are not satisfied, the Company immediately accounts for the cancellation as an acceleration of vesting and recognizes the amount that otherwise would have been recognized for services received over the remainder of the vesting period. Any payment made to the employee on the cancellation is accounted for as the repurchase of an equity interest except to the extent the payment exceeds the fair value of the equity instrument granted, measured at the repurchase date. Any such excess is recognized as an expense.

### (l) Earnings (loss) per share

Basic earnings per share is calculated by dividing the profit or loss attributable to common shareholders of the Company by the weighted average number of common shares outstanding during the period. Diluted earnings per share is computed similar to basic earnings (loss) per share except that the weighted average shares outstanding are increased to include additional shares for the assumed exercise of stock options and warrants, if dilutive.

### (m) Revenue recognition

Revenue from the sale of minerals, petroleum and natural gas is recorded when title passes to an external party and is based on volumes delivered to customers at contractual delivery points, and rates and collectability are reasonably assured. The costs associated with the delivery, including operating and maintenance costs, transportation and production-based royalty expenses, are recognized during the same period in which the related revenue is earned and recorded.

# NETCO SILVER INC.

Notes to the Unaudited Condensed Interim Consolidated Financial Statements  
(Expressed in Canadian Dollars)

For the Six Months Ended June 30, 2012 and 2011

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## 3. SIGNIFICANT ACCOUNTING POLICIES (continued)

- (n) New accounting standards and interpretations not yet adopted

Amendments to IFRS 7, Financial Instruments: Disclosures are effective for annual periods beginning on or after July 1, 2011. These amendments increase the 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.

### IFRS 9 – Financial Instruments

In an effort to reduce the complexity of accounting for financial instruments, the IASB is engaged in a project to replace IAS 39, Financial Instruments: Recognition and Measurement. IFRS 9 introduces new requirements for classifying and measuring financial assets and liabilities, which may affect the Company's accounting for its financial assets. Under this guidance, entities have the option to recognize financial liabilities at fair value through earnings. If this option is elected, entities would be required to reverse the portion of the fair value change due to a company's own credit risk out of earnings and recognized the change in other comprehensive income. The standard is not applicable until January 1, 2015 but is available for early adoption.

### IFRS 10 – Consolidation

IFRS 10 was issued on May 12, 2011. This standard 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 power over the investee. Under existing IFRS, consolidation is required when an entity has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. IFRS 10 replaces SIC12, Consolidation – Special Purpose Entities, and parts of IAS 27, Consolidated and Separate Financial Statements. The standard is not applicable until January 1, 2013 but is available for early adoption.

### IFRS 13 – Fair Value Measurement

IFRS 13 was issued on May 12, 2011. This 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. The standard is not applicable until January 1, 2013 but is available for early adoption.

# NETCO SILVER INC.

Notes to the Unaudited Condensed Interim Consolidated Financial Statements  
(Expressed in Canadian Dollars)

For the Six Months Ended June 30, 2012 and 2011

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## 3. SIGNIFICANT ACCOUNTING POLICIES (continued)

(n) New accounting standards and interpretations not yet adopted (continued)

IAS 12 – ‘Income Taxes’ – Amendments Regarding Deferred Tax: Recovery of Underlying Assets

These amendments are applicable to annual reporting periods beginning on or after January 1, 2012 and a practical approach for the measurement of deferred tax relating to investment properties measured at fair value, property, plant and equipment and intangible assets measured using the revaluation model. The measurement of deferred tax for these specified assets is based on the presumption that the carrying amount of the underlying asset will be recovered entirely through sale, unless the entity has clear evidence that economic benefits of the underlying asset will be consumed during its economic life.

IFRS 11 - ‘Joints Arrangements’

This standard replaces IAS 31: ‘Interest in Joint Ventures’ and applies for annual periods beginning on or after January 1, 2013. This new standard introduces new rules which classify joint arrangements as either a joint operation or joint venture. Under the new standard, proportionate consolidation is not allowed and all joint ventures must be equity accounted. All joint arrangements held by the Company will need to be reassessed to determine whether the joint operation or joint venture classification is appropriate, and the potential impacts of a change on the presentation of the Financial Statements.

IFRS 12 - ‘Disclosure of Interests in other Entities’

This new standard is applicable for annual reporting periods beginning on or after January 1, 2013. This standard clarifies the disclosure requirements for all forms of interests in other entities including joint arrangements, associates, special purpose vehicles and other off balance sheet vehicles.

IFRIC 20 – ‘Stripping Costs in the Production Phase of a Surface Mine’

The Interpretation is effective for annual periods beginning on or after January 1, 2013 with earlier application permitted. The Interpretation clarifies when production stripping should lead to the recognition of an asset and how that asset should be measured, both initially and in subsequent periods.

The Group is currently assessing the impact that these revised or new standards will have on the financial statements.

# NETCO SILVER INC.

Notes to the Unaudited Condensed Interim Consolidated Financial Statements  
(Expressed in Canadian Dollars)

For the Six Months Ended June 30, 2012 and 2011

## 4. DETERMINATION OF FAIR VALUES

Estimates of the fair value of financial instruments are made at a specific point in time, based on relevant information about financial markets and specific financial instruments. As these estimates are subjective in nature, involving uncertainties and matters of significant judgement, they cannot be determined with precision. Changes in assumptions can significantly affect estimated fair values. At June 30, 2012, the Group's financial instruments include cash and cash equivalents, accounts receivable, and accounts payable and accrued liabilities. These items are recognized on the statement of financial position at their carrying value which approximated their fair value due to their short-term nature.

All financial instruments measured at fair value are categorized into a hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets (Level 1 measurement) and the lowest priority to unobservable inputs (Level 3 measurement). The three levels of the fair value hierarchy are described below:

Level 1 – quoted prices (unadjusted) in active markets for identical assets or liabilities;

Level 2 – inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (i.e., as prices) or indirectly (i.e., derived from prices); and

Level 3 – inputs for the asset or liability that are not based on observable market data (unobservable inputs).

The following table sets forth the Group's financial assets measured at fair value by level within the fair value hierarchy.

<b>June 30, 2012</b>	Level 1	Level 2	Level 3	Total
Assets:				
Cash	\$ 200,516	\$ -	\$ -	\$ 200,516

December 31, 2011	Level 1	Level 2	Level 3	Total
Assets:				
Cash	\$ 249,036	\$ -	\$ -	\$ 249,036

# NETCO SILVER INC.

Notes to the Unaudited Condensed Interim Consolidated Financial Statements  
(Expressed in Canadian Dollars)

For the Six Months Ended June 30, 2012 and 2011

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## 5. FINANCIAL RISK MANGEMENT

### (a) Overview

The Group's activities expose it to a variety of financial risks that arise as a result of its exploration, development, production, and financing activities such as:

- market risk
- credit risk
- liquidity risk

This note presents information about the Group's exposure to each of the above risks, the Group's objectives, policies and processes for measuring and managing risk.

The Board of Directors oversees management's establishment and execution of the Group's risk management framework. Management has implemented and monitors compliance with risk management policies. The Group's risk management policies are established to identify and analyze the risks faced by the Group, to set appropriate risk limits and controls, and to monitor risks and adherence to market conditions and the Group's activities.

### (b) Market risk

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risk comprises three types of risk: interest rate risk, foreign currency risk and other price risk.

#### (i) Interest rate risk

The Group's cash and cash equivalents is held in bank accounts and due to the short-term nature of these financial instruments fluctuations in market interest rates do not have an impact on the fair value as at June 30, 2012.

The Group's sensitivity to interest rates is currently immaterial due to the short term maturity of its monetary assets and liabilities.

# NETCO SILVER INC.

Notes to the Unaudited Condensed Interim Consolidated Financial Statements  
(Expressed in Canadian Dollars)

For the Six Months Ended June 30, 2012 and 2011

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## 5. FINANCIAL RISK MANGEMENT (continued)

### (b) Market risk (continued)

#### (ii) Foreign currency risk

Currency risk is the risk to the Group's earnings that arises from fluctuations of foreign exchange rates and the degree of volatility of these rates. The Group does not use derivative instruments to reduce its exposure to foreign currency risk.

At June 30, 2012, the Group had the following financial assets and liabilities:

	<u>US Dollars</u>	<u>Argentine Pesos</u>
Cash	\$ 208	64,333
Accounts receivable	\$ -	396,770
Accounts payable	\$ 19,725	197,573

At June 30, 2012 US dollar amounts were converted at a rate of \$1.00 US dollars to \$1.0181 Canadian dollars and Argentine pesos amounts were converted at a rate of 1.00 Argentine pesos to \$0.2253 Canadian dollars.

#### (iii) Other price risk

Other price risk is the risk that the fair or future cash flows of a financial instrument will fluctuate because of changes in market prices, other than those arising from interest rate risk. The Group is not exposed to significant other price risk.

### (c) Credit risk

Credit risk is the risk that one party to a financial instrument will cause a loss for the other party by failing to discharge an obligation. The Group's cash and cash equivalents and accounts receivable are exposed to credit risk. The credit risk on cash and cash equivalents is considered small because the funds have been placed with major Canadian and Argentinean financial institutions. Management believes that the credit risk related to its accounts receivable is remote.

### (d) Liquidity risk

Liquidity risk is the risk that an entity will encounter difficulty in meeting obligations associated with financial liabilities. The Group's approach to managing liquidity risk is to ensure, as far as possible, that it will have sufficient liquidity to meet liabilities when due.

At June 20, 2012, the Group had a cash balance of \$200,516, accounts receivable of \$43,656 and harmonized sales tax receivable of \$12,370. The Group has accounts payable and accrued liabilities of \$111,018.

# NETCO SILVER INC.

Notes to the Unaudited Condensed Interim Consolidated Financial Statements  
(Expressed in Canadian Dollars)

For the Six Months Ended June 30, 2012 and 2011

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## 6. CAPITAL MANAGEMENT

The Group considers its capital structure to include working capital and shareholders' equity. Management's objective is to ensure that there is sufficient capital to minimize liquidity risk and to continue as a going concern. Management reviews its capital management approach on an ongoing basis and believes that its approach, given the relative size of the Group is reasonable.

The Group is not subject to any external capital restrictions and the Group did not change its approach to capital management during the period.

## 7. EXPLORATION AND EVALUATION ASSETS

Exploration and evaluation (E&E) assets consist of the Group's exploration projects which are pending the determination of proven and/or probable reserves, commercial viability or to be technically feasible.

	June 30, 2012	December 31, 2011
Argentina, Toruel property		
Mineral resource interest	\$ 784,432	227,786
United States, Columbia River Basin		
Oil and natural gas interest	-	-
Net carrying amount	\$ 784,432	\$227,786

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### Reconciliation of activity during the periods:

Balance, December 31, 2010	\$ 126,118
Additions	240,133
Write down	(138,465)
Balance, December 31, 2011	227,786
Additions	556,646
Balance, June 30, 2012	\$ 784,432

# NETCO SILVER INC.

Notes to the Unaudited Condensed Interim Consolidated Financial Statements  
(Expressed in Canadian Dollars)

For the Six Months Ended June 30, 2012 and 2011

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## 7. EXPLORATION AND EVALUATION ASSETS (continued)

Argentina, Toruel property:

In March 2011, the Company entered into an option agreement (the "Agreement") with Marifil Mines Ltd. ("Marifil") whereby Marifil granted the Company an option (the "Option") to acquire up to a 75% interest in Marifil's Toruel property located in the Rio Negro Province of the Republic of Argentina (the "Property"). Under the terms of the Agreement, the Company can earn a 50% interest in the Property during the period of March 3, 2011 to March 3, 2014 by paying Marifil an aggregate of US\$200,000 in cash (US\$100,000 paid) issuing Marifil 3,150,000 of its common shares (650,000 common shares issued), and expending US\$2,800,000 on the Property. The Company can earn a further 10% interest during the period from March 3, 2014 to March 3, 2015 by providing Marifil with a pre-feasibility study on the Property and paying Marifil US\$100,000 on each of the fourth and fifth anniversaries of the Agreement date. The Company can earn a further 10% interest in the Property during the period from March 3, 2016 to March 3, 2017 by providing Marifil with a feasibility study on the Property. Upon completion of the feasibility study, all further expenditures relating to the Property will be shared by the Company and Marifil, with 70% covered by the Company and 30% by Marifil. However, at Marifil's sole option, it can elect to be carried through to the commencement of commercial production on the Property, in which case the Company will earn an additional 5% interest, bringing its total interest in the Property to 75%. In the event the Company fails to provide Marifil with a feasibility study by March 3, 2017, the Company's interest in the Property may be reduced to 49% at Marifil's sole option.

During the period ended June 30, 2012, there were no indications, events or changes in circumstance which would cause the Company to question whether the carrying amount of the Toruel assets may not be recoverable, as such there is no provision for impairment recorded.

United States - Columbia River Basin (unproven):

In 2007, we acquired a 7.5% working interest in undeveloped leases in the Columbia River Basin of south central Washington with the intent of exploring for and developing natural gas reserves. The Company currently retains an interest in approximately 136,000 undeveloped gross mineral acres. As a consequence of negative results from two unsuccessful exploratory gas wells, the Company has written off the value of the Columbia River Basin properties.

Ownership in petroleum and natural gas interests involve certain inherent risks due to the difficulties in determining the validity of certain interests as well as the potential for problems arising from the frequently ambiguous conveyancing history characteristic of many petroleum and natural gas interests. The Company has investigated the ownership of its interests and, to the best of its knowledge, they are in good standing.



# NETCO SILVER INC.

Notes to the Unaudited Condensed Interim Consolidated Financial Statements  
(Expressed in Canadian Dollars)

For the Six Months Ended June 30, 2012 and 2011

## 8. DECOMMISSIONING OBLIGATIONS

No decommissioning liability has been accrued at June 30, 2012 for the Group's properties as there has been no activity on the properties that would obligate the Group to do so.

## 9. SHARE CAPITAL

### (a) Authorized

Unlimited number of common shares without par value.  
Unlimited number of preferred shares without par value.

### (b) Issued:

	Period ended June 30, 2012		Year ended December 31, 2011	
	Number of Shares	Amount	Number of Shares	Amount
Common shares:				
Balance, beginning of period	40,323,275	\$ 18,041,108	33,683,275	\$ 17,276,465
Transactions during the year:				
Private placement, net of share issue costs	6,435,000	750,429	6,240,000	718,393
Marifil option agreement	250,000	42,500	400,000	46,250
Shares for debt (Note 12)	-	-	-	-
<b>Balance, end of period</b>	<b>47,008,275</b>	<b>\$18,834,037</b>	<b>40,323,275</b>	<b>\$ 18,041,108</b>

On June 22, 2011, the Company closed a non-brokered private placement financing (the "Financing") of units (each, a "Unit"). The Company has issued 6,240,000 Units, at a price of \$0.125 per Unit, for aggregate gross proceeds of \$780,000. Each Unit consists of one common share and one-half of one share purchase warrant (each, a "Warrant"), with each whole Warrant entitling the holder to acquire one common share at an exercise price of \$0.22 for a period of two years from the closing of the Financing.

In connection with the Financing, the Company paid aggregate finder's fee of \$46,778 and issued a total of 370,720 finder's warrants. The finder's warrants entitle the holder to acquire one common share at an exercise price of \$0.125 for a period of two years. A total fair value cost of \$14,830 has been recognized as share issuance costs and has been recorded in contributed surplus in recognition of the fair value of the finder's warrants.

# NETCO SILVER INC.

Notes to the Unaudited Condensed Interim Consolidated Financial Statements  
(Expressed in Canadian Dollars)

For the Six Months Ended June 30, 2012 and 2011

## 9. SHARE CAPITAL (continued)

### (b) Issued (continued):

Also, on June 22, 2011, in connection with the closing of the Transaction (described above in Note 7), the Company issued a total of 150,000 common shares of the Company to Marifil in accordance to the terms of the Option Agreement. On October 18, 2011, the Company issued an additional 250,000 common shares to Marifil as required under the terms of the Option Agreement with Marifil with respect to the Toruel Property. The price per share was based on the closing price on date of issuance, for a total value of \$46,250.

On February 20, 2012, the Company issued an additional 250,000 common shares to Marifil as required under the terms of the Option Agreement with Marifil with respect to the Toruel Property. The price per share was based on the closing price on date of issuance, for a total value of \$42,500.

On February 29, 2012, the Company closed the first tranche of the non-brokered private placement financing, pursuant to which the Company issued 4,775,000 units at a price of \$0.125 per unit for gross proceeds of \$596,875. In connection the closing of the first tranche, the Company paid aggregate cash commissions of \$35,700 and issued an aggregate of 285,600 finder's warrants, with each finder's warrant exercisable into one common share at a price of \$0.125 per share for a period of 18 months.

On March 2, 2012, the Company closed the final tranche of the non-brokered private placement financing, pursuant to which the Company issued 1,660,000 units at a price of \$0.125 per unit for gross proceeds of \$207,500. In connection with the closing of the final tranche, the Company paid aggregate cash commissions of \$4,375 and issued an aggregate of 35,000 finder's warrants, with each finder's warrant exercisable into one common share at a price of \$0.125 per share for a period of 18 months.

A total fair value cost of \$12,824 has been recognized as share issuance costs and has been recorded in contributed surplus in recognition of the fair value of the finder's warrants issued in the first and second tranches of the private placements described above.

### (c) Contributed surplus:

	<b>Period ended June 30, 2012</b>	Year ended December 31, 2011
Balance, beginning of year	\$ 717,380	\$ 495,807
Share-based compensation	23,630	206,743
Finder's warrants	12,824	14,830
Balance, end of year	\$ 753,834	\$ 717,380

# NETCO SILVER INC.

Notes to the Unaudited Condensed Interim Consolidated Financial Statements  
(Expressed in Canadian Dollars)

For the Six Months Ended June 30, 2012 and 2011

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## 9. SHARE CAPITAL (continued)

### (d) Stock Options

The Company has a stock option plan in accordance with the policies on the TSX Venture Exchange whereby, from time to time at the discretion of the board of directors, stock options are granted to directors, officers and certain consultants.

Under the plan up to 6,415,600 common shares are reserved for the issuance of stock options. The exercise price of each option is based on the market price of the Company's common stock at the date of the grant less an applicable discount. The options can be granted for a maximum term of 10 years. The maximum number of options that may be granted to any one person must not exceed 5% of the common shares issued and outstanding at the time of grant unless disinterested shareholder approval is obtained. Any options granted to Consultants or persons performing Investor Relations under the Amended Stock Option Plan shall vest to the optionee as follows: 25% at date of grant, 25% six months from date of grant, 25% nine months from date of grant and the remaining 25% twelve months from the date of grant. All other options granted under the Amended Stock Option Plan shall have vesting terms set at the discretion of the Board of Directors.

On March 4, 2011, the Company granted a total of 525,000 stock options to officers, directors and consultants of the Company. Each option is exercisable into one common share at a price of \$0.12 for a period of five years.

On April 28, 2011, the Company granted 200,000 stock options to a director and a consultant of the Company. Each option is exercisable into one common share of the Company at a price of \$0.165 per shares for a period of five years.

On October 18, 2011, the Company granted a total of 1,125,000 stock options to directors and advisors/consultants at an exercise price of \$0.15 per share for a period of 5 years.

On December 8, 2011, the Company granted a total of 50,000 stock options to a consultant at an exercise price of \$0.15 per share for a period of 5 years.

On April 12, 2012, the Company granted a total of 240,000 stock options to an officer and consultants at an exercise price of \$0.15 per share for a period of 5 years.

For the period ended June 30, 2012, \$23,630 (2011 - \$106,385) has been recorded as share-based compensation relating to options issued and fully vested during the period. The fair value of stock options was estimated using the Black-Scholes option-pricing model with the following weighted average assumptions: Dividend yield 0%, expected annual volatility 124%; risk-free interest rate 1.16%; market share price of \$0.15; forfeiture rate of 0% and expected life of 5 years. The weighted average fair value of options granted was \$0.12 per option. Expected volatility was based on the historical share price volatility over the past 5 years. The expected life of the option was calculated based on the history of option exercises.

# NETCO SILVER INC.

Notes to the Unaudited Condensed Interim Consolidated Financial Statements  
(Expressed in Canadian Dollars)

For the Six Months Ended June 30, 2012 and 2011

## 9. SHARE CAPITAL (continued)

### (d) Stock Options (continued)

A summary of the stock option activity is as follows:

	June 30, 2012		December 31, 2011	
	Number	Weighted Average Exercise Price	Number	Weighted Average Exercise Price
Balance, beginning of period	1,900,000	\$0.14	750,000	\$0.40
Issued	240,000	\$0.15	1,900,00	0.14
Expired/Cancelled	-	-	(750,000)	(0.40)
Balance, end of period	<u>2,140,000</u>	<u>\$0.14</u>	<u>1,900,00</u>	<u>\$0.14</u>

As at June 30, 2012, the Company has outstanding directors' and employees' incentive stock options enabling the holders to acquire additional common shares as follows:

Number of options outstanding	Number of options exercisable	Exercise Price	Expiry Date
525,000	525,000	\$ 0.12	March 4, 2016
200,000	200,000	\$0.165	April 28, 2016
1,125,000	1,125,000	\$0.15	October 18, 2016
50,000	50,000	\$0.15	December 9, 2016
240,000	240,000	\$0.15	April 12, 2017
<u>2,140,000</u>	<u>2,140,000</u>		

### (e) Warrants

	June 30, 2012		December 31, 2011	
	Number	Weighted Average Exercise Price	Number	Weighted Average Exercise Price
Balance, beginning of period	12,490,720	\$0.34	13,395,000	\$0.40
Issued	3,538,100	\$0.21	3,490,720	\$0.21
Expired/Cancelled	(5,000,000)	(\$0.28)	(4,395,000)	(\$0.43)
Balance, end of period	<u>11,028,820</u>	<u>\$0.28</u>	<u>12,490,720</u>	<u>\$0.34</u>

# NETCO SILVER INC.

Notes to the Unaudited Condensed Interim Consolidated Financial Statements  
(Expressed in Canadian Dollars)

For the Six Months Ended June 30, 2012 and 2011

## 9. SHARE CAPITAL (continued)

### (e) Warrants (continued)

As at June 30, 2012, the Company has outstanding share purchase warrants entitling the holders to acquire additional common shares, as follows:

Number of Warrants	Exercise Price	Expiry Date
4,000,000	\$0.52	September 4, 2012
3,120,000	\$0.22	June 22, 2013
370,720	\$0.125	June 22, 2013
285,600	\$0.125	August 29, 2013
35,000	\$0.125	September 2, 2014
2,387,500	\$0.22	February 28, 2014
830,000	\$0.22	March 2, 2014
11,028,820		

## 10. SEGMENTED REPORTING

The Group's activities are in two industry segments comprised of exploration, development and production of petroleum, natural gas reserves and mineral exploration.

Petroleum and natural gas and mineral resource interests (exploration and evaluation assets) by geographical segment are as follows:

June 30, 2012	United States	Argentina	Total
Petroleum and natural gas	\$ -	\$ -	\$ -
Mineral resource	\$ -	\$ 784,432	\$ 784,432

December 31, 2011	United States	Argentina	Total
Petroleum and natural gas	\$ -	\$ -	\$ -
Mineral resource	\$ -	\$ 227,786	\$ 227,786

# NETCO SILVER INC.

Notes to the Unaudited Condensed Interim Consolidated Financial Statements  
(Expressed in Canadian Dollars)

For the Six Months Ended June 30, 2012 and 2011

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## 11. RELATED PARTY TRANSACTIONS

The aggregate amount of expenditures made to parties not at arm's length to the Group for the periods ending June 30, 2012 and 2011:

<b>June 30,</b>	<b>2012</b>	<b>2011</b>
Compensation of key management:		
Directors fees	\$ -	\$ 12,000
Management fees	93,900	13,440
Share-based compensation	23,630	106,385

These transactions are in the normal course of operations and are measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties, unless otherwise noted.

## 12. SUBSEQUENT EVENTS

The Company does not have any proposed transactions or subsequent events.