

**ENTRÉE GOLD INC.**  
**(An Exploration Stage Company)**

**CONSOLIDATED FINANCIAL STATEMENTS**  
**(Expressed in United States dollars)**  
**(Unaudited)**

June 30, 2006

# ENTRÉE GOLD INC.

(An Exploration Stage Company)

## CONSOLIDATED BALANCE SHEETS

(Expressed in United States Dollars)

	June 30, 2006 (Unaudited)	December 31, 2005
<b>ASSETS</b>		
<b>Current</b>		
Cash and cash equivalents	\$ 19,683,175	\$ 21,687,487
Receivables	120,359	310,888
Prepaid expenses	<u>461,815</u>	<u>169,133</u>
Total current assets	20,265,349	22,167,508
Equipment (Note 4)	<u>812,658</u>	<u>742,560</u>
<b>Total assets</b>	<u>\$ 21,078,007</u>	<u>\$ 22,910,068</u>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
<b>Current</b>		
Accounts payable and accrued liabilities	<u>\$ 122,342</u>	<u>\$ 502,449</u>
<b>Commitments (Note 10)</b>		
<b>Stockholders' equity</b>		
Common stock, no par value, unlimited number authorized, (Note 6) 70,708,093 (December 31, 2005 - 69,638,926) issued and outstanding	47,106,265	45,423,077
Additional paid-in capital	8,527,136	9,003,859
Accumulated other comprehensive income:	2,261,317	1,280,436
Foreign currency cumulative translation adjustment		
Accumulated deficit during exploration stage	<u>(36,939,053)</u>	<u>(33,299,753)</u>
Total stockholders' equity	<u>20,955,665</u>	<u>22,407,619</u>
<b>Total liabilities and stockholders' equity</b>	<u>\$ 21,078,007</u>	<u>\$ 22,910,068</u>

### Nature of operations (Note 2)

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

# ENTRÉE GOLD INC.

(An Exploration Stage Company)

## CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE LOSS

(Unaudited)

(Expressed in United States Dollars)

	Three Months Ended June 30, 2006	Three Months Ended June 30, 2005	Six Months Ended June 30, 2006	Six Months Ended June 30, 2005	Cumulative Period from Inception (July 19, 1995) to March 31, 2006
<b>EXPENSES</b>					
Audit and accounting	\$ 31,116	\$ 32,936	\$ 37,206	\$ 41,224	\$ 208,806
Consulting fees (Note 6)	7,876	280,336	106,934	1,113,904	1,519,492
Depreciation	45,404	24,554	89,859	41,446	250,769
Escrow shares compensation (Notes 6 and 7)	-	39,473	-	(435,583)	1,790,959
Foreign exchange loss	10,430	(487)	7,702	3,151	24,615
Legal (Note 6)	47,821	157,027	54,696	268,370	1,126,563
Loss on settlement of debt (Note 6)	-	-	-	-	5,252
Management fees (Notes 6 and 7)	11,975	1,005,081	21,762	1,854,807	2,837,311
Mineral property interests (Note 5 and 6)	1,209,454	2,032,805	1,724,270	3,203,819	23,740,777
Office and administration (Note 6)	349,241	549,575	706,794	1,031,059	3,049,705
Regulatory and transfer agent fees	155,780	13,827	222,525	36,792	392,064
Shareholder communications and investor relations (Note 6)	154,101	140,719	921,473	310,604	2,348,426
Travel	37,836	35,845	91,308	68,713	451,931
<b>Loss from operations</b>	<b>(2,061,034)</b>	<b>(4,311,691)</b>	<b>(3,984,529)</b>	<b>(7,538,306)</b>	<b>(37,746,670)</b>
Interest income	153,510	23,339	345,229	52,931	807,617
<b>Net loss</b>	<b>\$ (1,907,524)</b>	<b>\$ (4,288,352)</b>	<b>\$ (3,639,300)</b>	<b>\$ (7,485,375)</b>	<b>\$ (36,939,053)</b>
Comprehensive loss:					
Net loss	\$ (1,907,524)	\$ (4,288,352)	\$ (3,639,300)	\$ (7,485,375)	\$ (36,939,053)
Foreign currency translation adjustment	992,489	9,400	980,881	(16,783)	2,261,317
<b>Comprehensive loss</b>	<b>\$ (915,035)</b>	<b>\$ (4,278,952)</b>	<b>\$ (2,658,419)</b>	<b>\$ (7,502,158)</b>	<b>\$ (34,677,736)</b>
<b>Basic and diluted loss per share</b>	<b>\$ (0.03)</b>	<b>\$ (0.08)</b>	<b>\$ (0.05)</b>	<b>\$ (0.15)</b>	
<b>Weighted average number of shares outstanding</b>	<b>70,598,771</b>	<b>51,481,697</b>	<b>70,332,826</b>	<b>50,568,683</b>	

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

# ENTREE GOLD INC.

(An Exploration Stage Company)

## CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY

(Unaudited)

(Expressed in United States Dollars)

	Number of Shares	Common Stock	Additional Paid-in Capital	Accumulated Other Comprehensive Income	Accumulated Deficit During the Exploration Stage	Total Stockholders' Equity
<b>Balance, July 19, 1995 (date of inception)</b>	-	\$ -	\$ -	\$ -	\$ -	\$ -
Shares issued:						
Private placements	4,200,000	60,852	-	-	-	60,852
Acquisition of mineral property interests	3,200,000	147,520	-	-	-	147,520
Foreign currency translation adjustment	-	-	-	(756)	-	(756)
Net loss	-	-	-	-	(175,714)	(175,714)
<b>Balance, April 30, 1996</b>	<u>7,400,000</u>	<u>208,372</u>	<u>-</u>	<u>(756)</u>	<u>(175,714)</u>	<u>31,902</u>
Shares issued:						
Private placements	3,880,000	274,718	-	-	-	274,718
Foreign currency translation adjustment	-	-	-	(8,568)	-	(8,568)
Net loss	-	-	-	-	(56,250)	(56,250)
<b>Balance, April 30, 1997</b>	<u>11,280,000</u>	<u>483,090</u>	<u>-</u>	<u>(9,324)</u>	<u>(231,964)</u>	<u>241,802</u>
Foreign currency translation adjustment	-	-	-	(5,216)	-	(5,216)
Net loss	-	-	-	-	(33,381)	(33,381)
<b>Balance, April 30, 1998</b>	<u>11,280,000</u>	<u>483,090</u>	<u>-</u>	<u>(14,540)</u>	<u>(265,345)</u>	<u>203,205</u>
Foreign currency translation adjustment	-	-	-	(3,425)	-	(3,425)
Net loss	-	-	-	-	(40,341)	(40,341)
<b>Balance, April 30, 1999</b>	<u>11,280,000</u>	<u>483,090</u>	<u>-</u>	<u>(17,965)</u>	<u>(305,686)</u>	<u>159,439</u>
Escrow shares compensation	-	-	41,593	-	-	41,593
Exercise of stock options	1,128,000	113,922	-	-	-	113,922
Foreign currency translation adjustment	-	-	-	(896)	-	(896)
Net loss	-	-	-	-	(154,218)	(154,218)
<b>Balance, April 30, 2000</b>	<u>12,408,000</u>	<u>597,012</u>	<u>41,593</u>	<u>(18,861)</u>	<u>(459,904)</u>	<u>159,840</u>
Foreign currency translation adjustment	-	-	-	(5,627)	-	(5,627)
Net loss	-	-	-	-	(18,399)	(18,399)
<b>Balance, April 30, 2001</b>	<u>12,408,000</u>	<u>\$ 597,012</u>	<u>\$ 41,593</u>	<u>\$ (24,488)</u>	<u>\$ (478,303)</u>	<u>\$ 135,814</u>

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# ENTRÉE GOLD INC.

(An Exploration Stage Company)

## CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY

(Unaudited)

(Expressed in United States Dollars)

	Number of Shares	Common Stock	Additional Paid-in Capital	Accumulated Other Comprehensive Income	Accumulated Deficit During the Exploration Stage	Total Stockholders' Equity
- continued -						
<b>Balance, April 30, 2001</b>	12,408,000	\$ 597,012	\$ 41,593	\$ (24,488)	\$ (478,303)	\$ 135,814
Foreign currency translation adjustment	-	-	-	(2,561)	-	(2,561)
Net loss	-	-	-	-	(22,490)	(22,490)
<b>Balance, April 30, 2002</b>	12,408,000	597,012	41,593	(27,049)	(500,793)	110,763
Shares issued:						
Private placements	7,500,000	1,351,055	-	-	-	1,351,055
Exercise of warrants	12,500	3,288	-	-	-	3,288
Agent's finder fee	310,000	39,178	-	-	-	39,178
Finder's fee for mineral property interests	100,000	35,827	-	-	-	35,827
Debt settlement	135,416	45,839	5,252	-	-	51,091
Agent's warrants	-	-	16,877	-	-	16,877
Escrow shares compensation	-	-	40,205	-	-	40,205
Stock-based compensation	-	-	16,660	-	-	16,660
Share issue costs	-	(211,207)	-	-	-	(211,207)
Foreign currency translation adjustment	-	-	-	73,080	-	73,080
Net loss	-	-	-	-	(1,073,320)	(1,073,320)
<b>Balance, April 30, 2003</b>	20,465,916	1,860,992	120,587	46,031	(1,574,113)	453,497
Shares issued:						
Private placements and offerings	16,352,942	10,891,160	-	-	-	10,891,160
Exercise of warrants	3,730,372	1,316,664	(6,443)	-	-	1,310,221
Exercise of stock options	35,000	18,730	(4,026)	-	-	14,704
Agent's corporate finance fee	100,000	64,192	8,384	-	-	72,576
Acquisition of mineral property interests (Note 5)	5,000,000	3,806,000	-	-	-	3,806,000
Agent's warrants	-	-	370,741	-	-	370,741
Escrow shares compensation	-	-	1,949,878	-	-	1,949,878
Stock-based compensation	-	-	414,847	-	-	414,847
Share issue costs	-	(1,302,715)	-	-	-	(1,302,715)
Foreign currency translation adjustment	-	-	-	1,950	-	1,950
Net loss	-	-	-	-	(12,505,759)	(12,505,759)
<b>Balance, December 31, 2003</b>	45,684,230	\$ 16,655,023	\$ 2,853,968	\$ 47,981	\$ (14,079,872)	\$ 5,477,100

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# ENTRÉE GOLD INC.

(An Exploration Stage Company)

## CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY

(Unaudited)

(Expressed in United States Dollars)

	Number of Shares	Common Stock	Additional Paid-in Capital	Accumulated Other Comprehensive Income	Accumulated Deficit During the Exploration Stage	Total Stockholders' Equity
- continued -						
<b>Balance, December 31, 2003</b>	45,684,230	\$ 16,655,023	\$ 2,853,968	\$ 47,981	\$ (14,079,872)	\$ 5,477,100
Shares issued:						
Private placement	4,600,000	3,846,521	-	-	-	3,846,521
Exercise of warrants	533,836	186,208	(13,197)	-	-	173,011
Exercise of stock options	50,000	26,180	(8,238)	-	-	17,942
Warrants issued for cancellation	-	-	-	-	-	-
of price guarantee ( Note 5)	-	-	129,266	-	-	129,266
Escrow shares compensation	-	-	405,739	-	-	405,739
Share issue costs	-	(21,026)	-	-	-	(21,026)
Stock-based compensation	-	-	1,530,712	-	-	1,530,712
Foreign currency translation adjustment	-	-	-	132,501	-	132,501
Net loss	-	-	-	-	(5,528,114)	(5,528,114)
<b>Balance, December 31, 2004</b>	50,868,066	20,692,906	4,898,250	180,482	(19,607,986)	6,163,652
Shares issued:						
Private placement	7,542,410	13,538,097	0	0	0	13,538,097
Exercise of warrants	10,456,450	10,475,291	0	0	0	10,475,291
Exercise of stock options	772,000	1,238,581	(532,908)	0	0	705,673
Escrow shares compensation	0	0	(435,583)	0	0	(435,583)
Share issue costs	0	(521,798)	0	0	0	(521,798)
Stock-based compensation	0	0	5,074,100	0	0	5,074,100
Foreign currency translation adjustment	0	0	0	1,099,954	0	1,099,954
Net loss	0	0	0	0	(13,691,767)	(13,691,767)
<b>Balance, December 31, 2005</b>	69,638,926	\$ 45,423,077	\$ 9,003,859	\$ 1,280,436	\$ (33,299,753)	\$ 22,407,619

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# ENTRÉE GOLD INC.

(An Exploration Stage Company)

## CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY

(Unaudited)

(Expressed in United States Dollars)

	Number of Shares	Common Stock	Additional Paid-in Capital	Accumulated Other Comprehensive Income	Accumulated Deficit During the Exploration Stage	Total Stockholders' Equity
- continued -						
<b>Balance, December 31, 2005</b>	69,638,926	\$ 45,423,077	\$ 9,003,859	\$ 1,280,436	\$ (33,299,753)	\$ 22,407,619
Shares issued:						
Exercise of stock options	850,000	1,279,219	(545,320)	-	-	733,899
Stock-based compensation	-	-	240,393	-	-	240,393
Foreign currency translation adjustment	-	-	-	(11,608)	-	(11,608)
Net loss	-	-	-	-	(1,731,776)	(1,731,776)
<b>Balance, March 31, 2006</b>	70,488,926	46,702,296	8,698,932	1,268,828	(35,031,529)	21,638,527
Shares issued:						
Membership paid in stock	4,167	8,870	-	-	-	8,870
Exercise of stock options	215,000	395,099	(171,796)	-	-	223,303
Foreign currency translation adjustment	-	-	-	992,489	-	992,489
Net loss	-	-	-	-	(1,907,524)	(1,907,524)
<b>Balance, June 30, 2006</b>	70,708,093	\$ 47,106,265	\$ 8,527,136	\$ 2,261,317	\$ (36,939,053)	\$ 20,955,665

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

# ENTRÉE GOLD INC.

(An Exploration Stage Company)

## CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

(Expressed in United States dollars)

	Three Months Ended June 30, 2006	Three Months Ended June 30, 2005	Six Months Ended June 30, 2006	Six Months Ended June 30, 2005	Cumulative Period from Inception (July 19, 1995) to June 30, 2006
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>					
Net loss	\$ (1,907,524)	\$ (4,288,352)	\$ (3,639,300)	\$ (7,485,375)	\$ (36,939,053)
Items not affecting cash:					
Depreciation	45,404	24,554	89,859	41,446	250,769
Stock-based compensation	-	2,337,510	240,393	4,855,564	7,276,712
Escrow shares compensation	-	39,473	-	(435,583)	2,001,832
Loss on settlement of debt	-	-	-	-	5,252
Warrants issued for cancellation of price guarantee	-	-	-	-	129,266
Finder's fee paid in stock	-	-	-	-	35,827
Mineral property interest paid in stock	-	-	-	-	3,806,000
Membership fees paid in stock	8,870	-	8,870	-	8,870
Changes in assets and liabilities:					
Receivables	689	(4,905)	202,473	(57,559)	(97,530)
Prepaid expenses	16,949	8,210	(281,830)	(203,199)	(445,087)
Accounts payable and accrued liabilities	(84,843)	582,675	(398,620)	659,190	132,284
Net cash used in operating activities	<u>(1,920,455)</u>	<u>(1,300,835)</u>	<u>(3,778,155)</u>	<u>(2,625,516)</u>	<u>(23,834,858)</u>
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>					
Proceeds from issuance of capital stock	223,303	16,149,412	957,202	16,162,622	43,881,177
Share issue costs	-	(521,798)	-	(521,798)	(1,557,374)
Net cash provided by financing activities	<u>223,303</u>	<u>15,627,614</u>	<u>957,202</u>	<u>15,640,824</u>	<u>42,323,803</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>					
Acquisition of equipment	<u>(119,475)</u>	<u>(214,567)</u>	<u>(159,957)</u>	<u>(478,338)</u>	<u>(1,063,427)</u>
Net cash used in investing activities	<u>(119,475)</u>	<u>(214,567)</u>	<u>(159,957)</u>	<u>(478,338)</u>	<u>(1,063,427)</u>
<b>Effect of foreign currency translation on cash and cash equivalents</b>	<u>982,023</u>	<u>9,400</u>	<u>976,598</u>	<u>(16,783)</u>	<u>2,257,657</u>
<b>Change in cash and cash equivalents during the period</b>	<u>(834,604)</u>	<u>14,121,612</u>	<u>(2,004,312)</u>	<u>12,520,187</u>	<u>19,683,175</u>
<b>Cash and cash equivalents, beginning of period</b>	<u>20,517,779</u>	<u>4,458,946</u>	<u>21,687,487</u>	<u>6,060,371</u>	<u>-</u>
<b>Cash and cash equivalents, end of period</b>	<u>\$ 19,683,175</u>	<u>\$ 18,580,558</u>	<u>\$ 19,683,175</u>	<u>\$ 18,580,558</u>	<u>\$ 19,683,175</u>
<b>Cash paid for interest during the period</b>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>
<b>Cash paid for income taxes during the period</b>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>

Supplemental disclosure with respect to cash flows. (Note 9)

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



**ENTRÉE GOLD INC.**

(An Exploration Stage Company)

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

June 30, 2006

(Unaudited)

(Expressed in United States dollars)

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**1. BASIS OF PRESENTATION**

The interim period financial statements have been prepared by the Company in conformity with generally accepted accounting principles in the United States of America. The preparation of financial data is based on accounting principles and practices consistent with those used in the preparation of annual financial statements, and in the opinion of management these financial statements contain all adjustments necessary (consisting of normally recurring adjustments) to present fairly the financial information contained therein. Certain information and footnote disclosure normally included in the financial statements prepared in conformity with generally accepted accounting principles in the United States of America have been condensed or omitted. These interim period statements should be read together with the most recent audited financial statements and the accompanying notes for the year ended December 31, 2005. The results of operations for the three and six month periods ended June 30, 2006 are not necessarily indicative of the results to be expected for the year ending December 31, 2006.

**2. NATURE OF OPERATIONS**

The Company was incorporated under the laws of the Province of British Columbia and continued under the laws of the Yukon Territory. On May 27, 2005, the Company changed the governing jurisdiction from the Yukon Territory to British Columbia by continuing into British Columbia under the British Columbia *Business Corporation Act*. The Company's principal business activity is the exploration of mineral property interests. Effective October 10, 2002, pursuant to a special resolution passed by the shareholders of the Company, the Company changed its name from Entrée Resources Inc. to Entrée Gold Inc. and consolidated its share capital on a 2:1 basis. In December 2003, the Company changed its fiscal year end from April 30 to December 31. To date, the Company has not generated significant revenues from its operations and is considered to be in the exploration stage.

All amounts are expressed in United States dollars, except for certain per share amounts denoted in Canadian dollars ("C\$").

**3. SIGNIFICANT ACCOUNTING POLICIES**

These consolidated financial statements follow the same significant accounting principles as those outlined in the notes to the audited consolidated financial statements for the year ended December 31, 2005.

**Escrow shares**

Shares placed in escrow in connection with an initial public offering which are to be released upon achievement of certain performance criteria are considered to be contingently issueable and compensatory in nature. Accordingly, the difference between the fair value of these shares, being the trading price of the Company's publicly traded common shares, at the time they are released from escrow and their original issue price is accounted for as compensation expense in the period of release.

As described in Note 6, certain of the Company's escrow shares were transferred to a Trustee for the benefit of future employees, officers and directors of the Company. As these performance escrow shares are considered compensatory in nature, the Company records a compensation benefit at fair value, being the trading price of the Company's publicly traded common shares, when a portion or all of the these performance escrow shares are allocated to specific individuals and adjusts this compensation benefit to fair value at the end of each respective reporting period until the performance escrow shares are released from escrow.

**ENTRÉE GOLD INC.**

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**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

June 30, 2006

(Unaudited)

(Expressed in United States dollars)

**3. SIGNIFICANT ACCOUNTING POLICIES (cont'd... )****Stock-based compensation**

Effective January 1, 2006, the Company adopted SFAS No. 123(revised), "Share-Based Payment" [SFAS 123(R)] utilizing the modified prospective approach. The impact of adoption of the standard did not materially affect the Company's financial position, results of operations, or cash flows because the Company adopted the fair value based method of accounting for stock options prescribed by SFAS 123, "Accounting for Stock-Based Compensation", on May 1, 2003.

Under Statements of Financial Accounting Standards No. 123, "Accounting for Stock-Based Compensation" the Company used the fair value based method of accounting for stock-based employee compensation.

The Company's results for the three and six month periods ended June 30, 2006 were not significantly affected as a result of adopting SFAS 123(R) on January 1, 2006.

In May 2005, FASB issued Statement of Financial Accounting Standards No. 154 Accounting Changes and Error Corrections – A Replacement of APB Opinion No. 20 and FASB Statement No. 3 ("SFAS 154"), which is effective for fiscal years ending after December 15, 2005. SFAS 154 requires that changes in accounting policy be accounted for on a retroactive basis.

The adoption of these new pronouncements are not expected to have a material effect on the Company's consolidated financial position or results of operations.

**Comparative figures**

Certain comparative figures have been revised to reflect adjustments recorded at December 31, 2005.

**4. EQUIPMENT**

	June 30, 2006			December 31, 2005		
	Cost	Accumulated Depreciation	Net Book Value	Cost	Accumulated Depreciation	Net Book Value
Office equipment	\$ 75,116	\$ 16,497	\$ 58,619	\$ 57,453	\$ 10,836	\$ 46,617
Computer equipment	291,825	147,066	144,759	214,621	92,297	122,324
Field equipment	362,125	25,022	337,103	309,133	17,238	291,895
Buildings	345,968	73,791	272,177	322,264	40,540	281,724
	<u>\$ 1,075,034</u>	<u>\$ 262,376</u>	<u>\$ 812,658</u>	<u>\$ 903,471</u>	<u>\$ 160,911</u>	<u>\$ 742,560</u>

**5. MINERAL PROPERTY INTERESTS**

Title to mineral property interests involves certain inherent risks due to the difficulties of determining the validity of certain claims as well as the potential for problems arising from the frequently ambiguous conveyancing history characteristic of many mineral property interests. The Company has investigated title

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**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

June 30, 2006

(Unaudited)

(Expressed in United States dollars)

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**5. MINERAL PROPERTY INTERESTS (cont'd... )**

to its mineral property interests and, to the best of its knowledge, title to the mineral property interests are in good standing.

Each of our exploration licenses was granted by the Mineral Resources and Petroleum Authority of Mongolia for an initial term of three years, subject to a right to renew for two successive 2-year renewals (for a cumulative total of seven years). Mongolian exploration licenses are maintained in good standing by payment to the Mineral Resources and Petroleum Authority of Mongolia of set annual fees escalating from \$0.05 to \$1.50 per hectare over the course of the potential seven year tenure.

Two of the three licenses that comprise Lookout Hill were issued April 3, 2001 and were renewed for the second of their two year renewals in March, 2006. The third Lookout Hill license was issued March 30, 2001 and was renewed for the second of its two-year renewals in March, 2006. The Manlai license was issued March 9, 2001 and renewed for the second of its two-year renewals in March, 2006. The Khatsavch license was issued to the original owner on October 31, 2003 and transferred to the Company in August, 2004.

In October, 2004, the Company granted to Ivanhoe Mines Ltd. ("Ivanhoe") the right to earn, over an eight year period, a participating interest in a certain portion of its Lookout Hill Property (the "Project Property"). Under the agreement, Ivanhoe must spend a minimum of \$3 million in order to earn surface rights in the Project Property and a minimum of \$20 million in order to earn any mineral rights interest in the Project Property and may acquire up to an 80% interest in mineralization below a depth of 560 metres and a 70% interest in mineralization above a depth of 560 metres by spending \$35 million. Thereafter, the Company has the right to require Ivanhoe to fund its share of subsequent project costs through to production, to be recovered from production cash flow. The agreement with Ivanhoe also provided for Ivanhoe to subscribe for 4,600,000 units of the Company at a price of C\$1.00 per unit (completed in November 2004).

The Company's exploration licenses begin to expire in March 2008 through to October 2010. The total estimated annual fees in order to maintain these licenses in good standing is approximately \$240,000.

In February 2006, the Company acquired an option to purchase the Oyut Tolgoi copper property along with two other licenses (Asgat Uul and Onts Uul) in Western Mongolia. The terms of the option include an initial US\$50,000 payment to the Mongolian Property Owner (paid). The agreement was amended in April 2006. After a due diligence period of 6 months from April 2006, the Company, should it wish to maintain its option, will be required to pay an additional US\$100,000 and issue 100,000 shares. The Company will then have one year from the end of the due diligence period to explore the property. A final payment of US\$250,000 and the issuance of an additional 250,000 shares on or before the anniversary date will earn the Company a 100% interest in the three properties. A finder's fee of 5% plus 10,000 shares is payable.

In May 2006, the Company secured an option to acquire the Sol Dos copper prospect, located in the Safford district, of south-eastern Arizona. Under the terms of the agreement, the Company may earn a 100% interest in the Sol Dos property by spending \$4 million on exploration over four years and by making staged payments totalling \$1 million cash and issuing 250,000 shares. The Company's interest would be subject to a 2% NSR royalty, one half of which it may purchase for \$1 million cash and issuing 250,000 shares.

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**5. MINERAL PROPERTY INTERESTS (cont'd... )**

Mineral property interest costs incurred are summarized as follows:

	Three Month Period Ended June 30, 2006	Three Month Period Ended June 30, 2005	Six Month Period Ended June 30, 2006	Six Month Period Ended June 30, 2005	Cumulative Period Ended June 30, 2006
<b>Lookout Hill:</b>					
Acquisition	\$ 86,151	\$ 43,382	\$ 133,863	\$ 92,592	\$10,181,558
Assaying, testing and analysis	17,773	61,277	30,023	70,354	810,467
Camp and field supplies	71,743	347,341	122,234	579,745	2,321,418
Drilling	239,061	314,616	239,061	314,616	2,842,696
Geological and geophysical	341,399	717,932	481,636	1,559,290	4,384,890
Travel and accommodation	65,124	77,658	102,401	113,399	570,050
	<u>821,251</u>	<u>1,562,206</u>	<u>1,109,218</u>	<u>2,729,996</u>	<u>21,111,079</u>
<b>Manlai:</b>					
Acquisition	3,334	1,630	5,221	3,476	17,562
Assaying, testing and analysis	7,310	13,341	10,980	13,341	130,741
Camp and field supplies	28,755	182,003	88,593	183,364	635,294
Drilling	-	-	-	-	416,037
Geological and geophysical	170,061	273,625	252,338	273,625	875,491
Travel and accommodation	28,201	-	32,347	-	66,442
	<u>237,661</u>	<u>470,599</u>	<u>389,479</u>	<u>473,806</u>	<u>2,141,567</u>
<b>Khatsavch:</b>					
Acquisition	-	-	-	17	66
	<u>-</u>	<u>-</u>	<u>-</u>	<u>17</u>	<u>66</u>
<b>Oyut Tolgoi</b>					
Acquisition	17,659	-	73,086	-	73,086
	<u>17,659</u>	<u>-</u>	<u>73,086</u>	<u>-</u>	<u>73,086</u>
<b>Sol Dos</b>					
Acquisition	25,725	-	25,725	-	25,725
Assaying, testing and analysis	99	-	99	-	99
Geological and geophysical	5,985	-	5,985	-	5,985
Travel and accommodation	1,240	-	1,240	-	1,240
	<u>33,049</u>	<u>-</u>	<u>33,049</u>	<u>-</u>	<u>33,049</u>
<b>Other</b>					
Geological and geophysical	99,834	-	119,438	-	381,930
	<u>99,834</u>	<u>-</u>	<u>119,438</u>	<u>-</u>	<u>381,930</u>
	<u>\$ 1,209,454</u>	<u>\$ 2,032,805</u>	<u>\$ 1,724,270</u>	<u>\$ 3,203,819</u>	<u>\$23,740,777</u>

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**6. COMMON STOCK****Share issuances**

In June 2005, the Company completed a non-brokered private placement consisting of 5,665,730 units at a price of C\$2.20 per unit for gross proceeds of \$10,170,207. Each unit consisted of one common share, one non-transferable share purchase A warrant and one non-transferable share purchase B warrant. Two A warrants entitle the holder to purchase one common share of the Company at a price of C\$2.75 for a period of 2 years. Two B warrants entitle the holder to purchase one common share of the Company at a price of C\$3.00 for a period of two years. Pursuant to an agreement with the Company, the placee, Kennecott Canada Exploration Inc. (indirect wholly-owned subsidiary of Rio Tinto plc) has the right to acquire additional securities and participate in future financings by the Company so as to maintain its proportional equity in the Company. Related share issue costs were comprised of cash costs totalling \$521,798.

In July 2005, the Company completed a non-brokered private placement consisting of 1,876,680 units at a price of C\$2.20 per unit for gross proceeds of \$3,367,890. Each unit consisted of one common share, one non-transferable share purchase A warrant and one non-transferable share purchase B warrant. Two A warrants entitle the holder to purchase one common share of the Company at a price of C\$2.75 for a period of 2 years. Two B warrants entitle the holder to purchase one common share of the Company at a price of C\$3.00 for a period of two years.

During the year ended December 31, 2005, the Company issued 10,456,450 common shares for cash proceeds of \$10,475,291 on the exercise of warrants.

During the year ended December 31, 2005, the Company issued 772,000 common shares for cash proceeds of \$705,673 on the exercise of stock options. The fair value recorded when the options were granted of \$532,908 has been transferred from additional paid-in capital to common stock on the exercise of the options.

During the three months ended March 31, 2006, the Company issued 850,000 common shares for cash proceeds of \$733,899 on the exercise of stock options. The fair value recorded when the options were granted of \$545,320 has been transferred from additional paid-in capital to common stock on the exercise of the options.

During the three months ended June 30, 2006, the Company issued 215,000 common shares for cash proceeds of \$223,303 on the exercise of stock options. The fair value recorded when the options were granted of \$171,796 has been transferred from additional paid-in capital to common stock on the exercise of the options.

During the three months ended June 30, 2006, the Company issued 4,167 common shares to the University of British Columbia as a donation to become a member of the Mineral Deposit Research Unit. The fair value recorded when the shares were issued of \$8,870 has been recorded as a donation expense.

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**6. COMMON STOCK (cont'd ... )****Escrow shares**

At December 31, 2005, all performance escrow shares had been released from escrow.

The total escrow compensation expense (recovery) has been recorded in the consolidated financial statements as follows with corresponding additional paid-in capital recorded in stockholders' equity:

	Three Month Period Ended June 30, 2006	Three Month Period Ended June 30, 2005	Six Month Period Ended June 30, 2006	Six Month Period Ended June 30, 2005	Cumulative Period Ended June 30, 2006
<b>Escrow shares allocated to president pursuant to employment agreement:</b>					
Mineral property interests expense (recovery)	\$ -	\$ -	\$ -	\$ -	\$ 169,280
Escrow shares compensation expense (recovery)	-	136	-	(1,453)	211,394
	-	136	-	(1,453)	380,674
<b>Escrow shares allocated to directors, officers, and employees:</b>					
Escrow shares compensation expense (recovery)	-	39,337	-	(434,130)	1,579,565
	\$ -	\$ 39,473	\$ -	\$ (435,583)	\$ 1,960,239

**Share purchase warrants**

Share purchase warrant transactions are summarized as follows:

	Number of Shares	Weighted Average Exercise Price (C\$)
Balance as at December 31, 2004	12,914,270	1.22
Issued	7,542,410	2.88
Expired	(2,207,820)	1.26
Exercised	(10,456,450)	0.77
Balance as at December 31, 2005 and March 31, 2006	7,792,410	2.82
Expired	(250,000)	1.05
Balance as at June 30, 2006	7,542,410	\$ 2.88

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**6. COMMON STOCK** (cont'd ... )**Share purchase warrants** (cont'd ... )

As at June 30, 2006, the following share purchase warrants were outstanding and exercisable:

Number of Shares	Exercise Price (C\$)	Expiry Date
2,832,865	2.75	June 29, 2007
2,832,865	3.00	June 29, 2007
938,340	2.75	July 7, 2007
<u>938,340</u>	3.00	July 7, 2007
<u>7,542,410</u>		

**Stock options**

During the year ended April 30, 2003, the Company adopted a stock option plan (the "Plan") to grant options to directors, officers, employees and consultants. Under the Plan, as amended in May 2005, the Company may grant options to acquire up to 10,176,613 common shares of the Company. Options granted can have a term up to ten years and an exercise price typically not less than the Company's closing stock price at the date of grant.

On March 3, 2005, the Company became a Tier 1 Issuer on the TSX Venture Exchange and, as a result, all previously issued stock options became fully vested except those granted to investor relations consultants, which included a twelve month vesting period. As a Tier 1 Issuer, future stock options granted may vest upon grant except those granted to investor relations consultants which must have a minimum 12 month vesting period.

Stock option transactions are summarized as follows:

	Number of Shares	Weighted Average Exercise Price (C\$)
Balance as at December 31, 2004	5,915,000	\$ 1.03
Granted	3,340,000	1.67
Exercised	<u>(772,000)</u>	1.09
Balance as at December 31, 2005	8,483,000	1.28
Granted	245,000	2.01
Exercised	<u>(850,000)</u>	0.99
Balance as at March 31, 2006	7,878,000	1.33
Exercised	<u>(215,000)</u>	1.17
Balance as at June 30, 2006	<u>7,663,000</u>	\$ 1.33

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**6. COMMON STOCK** (cont'd ... )**Stock options** (cont'd ... )

The weighted average fair value per stock option granted during the six months ended June 30, 2006 was C\$1.06 (June 30, 2005 - C\$0.94). The number of stock options exercisable at June 30, 2006 was 7,663,000 (December 31, 2005 - 8,464,250).

At June 30, 2006, the following stock options were outstanding:

Number of Shares	Exercise Price (C\$)	Expiry Date
100,000	\$ 1.15	November 1, 2006
475,000	0.46	August 26, 2007
360,000	0.60	January 30, 2008
100,000	1.19	March 3, 2008
735,000	1.00	September 18, 2008
175,000	2.32	November 13, 2008
560,000	1.24	February 11, 2009
1,425,000	1.15	November 12, 2009
600,000	1.25	December 17, 2009
400,000	1.28	January 7, 2010
75,000	1.19	March 3, 2010
63,000	1.48	May 24, 2010
2,205,000	1.75	June 9, 2010
100,000	2.00	August 15, 2010
25,000	1.66	August 25, 2010
20,000	1.85	September 28, 2010
125,000	1.80	January 23, 2011
100,000	2.20	February 8, 2011
20,000	2.34	March 28, 2011
<hr/> 7,663,000		

**Stock-based compensation**

The fair value of stock options granted during the six months ended June 30, 2006 was \$225,075 (June 30, 2005 - \$2,380,679) which is being recognized over the options vesting periods. Total stock-based compensation recognized during the six months ended June 30, 2006 was \$240,393 (June 30, 2005 - \$4,855,564) which has been recorded in the consolidated statements of operations as follows with corresponding additional paid-in capital recorded in stockholders' equity:



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**6. COMMON STOCK** (cont'd ... )

**Stock-based compensation** (cont'd ... )

	Three Month Period Ended June 30, 2006	Three Month Period Ended June 30, 2005	Six Month Period Ended June 30, 2006	Six Month Period Ended June 30, 2005	Cumulative Period Ended June 30, 2006
Consulting fees	\$ -	\$ 234,365	\$ 102,579	\$ 1,056,441	1,360,123
Legal	-	90,140	-	152,092	250,796
Management fees	-	1,014,077	-	1,831,464	2,547,549
Mineral property interests	-	563,378	91,236	918,075	1,358,848
Office and administration	-	392,110	31,275	732,776	1,079,412
Stockholder communications and investor relations	-	43,440	15,303	164,716	679,984
	\$ -	\$ 2,337,510	\$ 240,393	\$ 4,855,564	\$ 7,276,712

The following weighted-average assumptions were used for the Black-Scholes valuation of stock options granted:

	Six Month Period Ended June 30, 2006	Six Month Period Ended June 30, 2005
Risk-free interest rate	3.58%	2.84%
Expected life of options (years)	5.0	5.0
Annualized volatility	57%	81%
Dividend rate	0.00%	0.00%

**7. RELATED PARTY TRANSACTIONS**

The Company entered into the following transactions with related parties during the six months ended June 30, 2006:

- a) Recognized an expense (recovery) of \$Nil. (June 30, 2005 - \$(1,453)) from certain performance escrow shares allocated to the president of the Company (Note 6) which have been recorded as escrow shares compensation expense (recovery) of \$Nil (June 30, 2005 - \$(1,453)). In addition, compensation expense (recovery) of \$Nil (June 30, 2005 - \$(434,130)) was recognized during the current period from certain performance escrow shares allocated to directors, officers and employees of the Company (Note 6) which has been recorded as escrow shares compensation expense (recovery) of \$Nil (June 30, 2005 - \$(434,130)).

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**7. RELATED PARTY TRANSACTIONS (cont'd... )**

b) Paid or accrued management fees of \$21,762 (June 30, 2005 - \$25,821) to directors and officers of the Company.

These transactions were in the normal course of operations and were measured at the exchange amount which represented the amount of consideration established and agreed to by the related parties.

**8. SEGMENT INFORMATION**

The Company operates in one business segment being the exploration of mineral property interests.

Geographic information is as follows:

	June 30, 2006	December 31, 2005
Identifiable assets		
Canada	\$20,184,190	\$ 22,167,229
Mongolia	893,817	742,839
	<u>\$21,078,007</u>	<u>\$ 22,910,068</u>

	Three Month Period Ended June 30, 2006	Three Month Period Ended June 30, 2005	Six Month Period Ended June 30, 2006	Six Month Period Ended June 30, 2005
Loss for the period				
Canada	\$ (583,192)	\$ (2,434,867)	\$ (1,757,652)	\$ (4,184,690)
Mongolia	<u>(1,324,332)</u>	<u>(1,853,485)</u>	<u>(1,881,648)</u>	<u>(3,300,685)</u>
	<u>\$(1,907,524)</u>	<u>\$ (4,288,352)</u>	<u>\$(3,639,300)</u>	<u>\$ (7,485,375)</u>

**9. SUPPLEMENTAL DISCLOSURE WITH RESPECT TO CASH FLOWS**

The significant non-cash transaction for the six months ended June 30, 2006 consisted of the issuance of 4,167 common shares in payment of membership fees in the amount of \$8,870 (Note 6).

Significant non-cash transactions for the six months ended June 30, 2005 consisted of:

- The recognition of compensation expense (recovery) from the allocation of certain performance escrow shares to the president of the Company which has been recorded as escrow shares compensation (recovery) of (\$1,453).
- The recognition of compensation expense (recovery) from the allocation of certain performance escrow shares to directors, officers and employees of the Company which has been recorded as escrow shares compensation expense (recovery) of \$(434,130).

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**10. COMMITMENTS**

The Company is committed to make lease payments for the rental of office space as follows:

2006	\$ 30,860
2007	74,064
2008	75,414
2009	77,728
2010	78,693
<u>2011</u>	<u>32,789</u>
<u>Total</u>	<u>\$ 369,548</u>

**11. SUBSEQUENT EVENTS**

Subsequent to June 30, 2006, the Company issued 1,085,000 stock options with an exercise price of C\$1.32. The term of the options was five years except for 20,000 options whose term was two years.