



## **CONSOLIDATED FINANCIAL STATEMENTS**

**for the years ended**

**December 31, 2008**

**and**

**December 31, 2007**



**Cinnamon Jang Willoughby & Company**

Chartered Accountants

*A Partnership of Incorporated Professionals*

## AUDITORS' REPORT

To the Shareholders of **Kootenay Gold Inc.:**

We have audited the consolidated balance sheets of Kootenay Gold Inc. as at December 31, 2008 and 2007 and the consolidated statements of loss and deficit, and cash flows for the years then ended. These consolidated financial statements are the responsibility of the company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the company as at December 31, 2008 and 2007 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

/s/ "Cinnamon Jang Willoughby & Company"

Chartered Accountants

Burnaby, BC

April 23, 2009

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**KOOTENAY GOLD INC.**  
(An Exploration Stage Company)  
**CONSOLIDATED BALANCE SHEETS**

Exhibit 1

	<b>December 31 2008</b>	<b>December 31 2007</b>
<b>ASSETS</b>		
<b>Current</b>		
Cash and cash equivalents	\$ 15,911,376	\$ 1,566,191
Accounts receivable and advances	995,324	193,060
Share subscriptions receivable	-	35,500
Prepaid expenses	108,030	107,756
Marketable securities (Note 4)	267,238	365,750
<b>Total current assets</b>	<b>17,281,968</b>	<b>2,268,257</b>
<b>Equipment</b> (Note 5)	<b>91,447</b>	<b>48,494</b>
<b>Exploration advances</b>	<b>22,572</b>	<b>74,921</b>
<b>Exploration deposits</b>	<b>-</b>	<b>36,644</b>
<b>Mineral properties</b> (Note 6)	<b>12,173,648</b>	<b>4,776,655</b>
	<b>\$ 29,569,635</b>	<b>\$ 7,204,971</b>

**LIABILITIES**

<b>Current</b>		
Accounts payable and accrued liabilities	\$ 683,909	\$ 472,244
Investor deposits	37,500	96,700
Exploration advances	-	249,450
<b>Total current liabilities</b>	<b>721,409</b>	<b>818,394</b>

**SHAREHOLDERS' EQUITY**

<b>Share capital</b> (Note 7)	<b>23,258,809</b>	<b>4,934,521</b>
<b>Contributed surplus</b> (Note 7)	<b>10,845,151</b>	<b>4,014,397</b>
<b>Accumulated other comprehensive income (loss)</b> (Exhibit 3)	<b>(460,355)</b>	<b>47,000</b>
<b>Deficit</b>	<b>(4,795,379)</b>	<b>(2,609,341)</b>
	<b>28,848,226</b>	<b>6,386,577</b>
	<b>\$ 29,569,635</b>	<b>\$ 7,204,971</b>

**Continued Operations and Going Concern** (Note 2)

Approved on Behalf of the Board:

"James McDonald"  
Director

"Kenneth Berry"  
Director

- see accompanying notes -

# KOOTENAY GOLD INC.

(An Exploration Stage Company)

## CONSOLIDATED STATEMENTS OF OPERATIONS

Exhibit 2

	For the year ended	
	December 31 2008	December 31 2007
<b>Administrative Expenses</b>		
Amortization	\$ 19,801	\$ 12,300
Foreign exchange loss	191,123	(49,418)
General and administrative	632,570	620,021
Management fees	349,705	171,251
Stock-based compensation (Note 8)	1,164,423	408,927
Professional fees	110,861	181,032
Regulatory and filing fees	72,909	42,541
Rent	47,620	24,449
<b>Loss before Other Items</b>	<b>2,589,012</b>	<b>1,411,103</b>
<b>Other Items</b>		
Loss on sale of marketable securities	(16,097)	-
Gain on sale of mineral property interest	-	30,200
Administration income	142,572	153,979
Interest income	276,499	22,363
	<b>402,974</b>	<b>206,542</b>
<b>Loss before income taxes</b>	<b>2,186,038</b>	<b>1,204,561</b>
<b>Income tax recovery</b>	<b>-</b>	<b>153,881</b>
<b>Loss for the Period</b>	<b>2,186,038</b>	<b>1,050,680</b>
<b>Deficit, Beginning</b>	<b>2,609,341</b>	<b>1,558,661</b>
<b>Deficit, Ending</b>	<b>\$ 4,795,379</b>	<b>\$ 2,609,341</b>
<b>Basic and Diluted Earnings (Loss) per Share</b>	<b>\$ (0.069)</b>	<b>\$ (0.056)</b>
<b>Weighted Average Number of Shares Outstanding</b>	<b>31,583,700</b>	<b>18,792,403</b>
<b>Fully Diluted Weighted Average Number of Shares Outstanding</b>	<b>41,715,502</b>	<b>20,513,251</b>

- see accompanying notes -

# KOOTENAY GOLD INC.

(An Exploration Stage Company)

## CONSOLIDATED STATEMENTS OF ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS)

Exhibit 3

	For the year ended	
	December 31 2008	December 31 2007
<b>Accumulated other comprehensive income, beginning of year</b>	\$ 47,000	\$ -
Other comprehensive loss	(507,355)	47,000
<b>Accumulated other comprehensive loss, end of year</b>	\$ (460,355)	\$ 47,000

## CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS

Exhibit 4

	For the year ended	
	December 31 2008	December 31 2007
<b>Net loss</b>	\$ (2,186,038)	\$ (1,050,680)
Other comprehensive income		
Transitional adjustment to accumulated other comprehensive income	-	5,500
Unrealized loss on available-for-sale financial assets arising during the period	(507,355)	41,500
Total other comprehensive loss	(507,355)	47,000
<b>Comprehensive loss</b>	\$ (2,693,393)	\$ (1,003,680)

- see accompanying notes -

# KOOTENAY GOLD INC.

(An Exploration Stage Company)

## CONSOLIDATED STATEMENTS OF CASH FLOWS

Exhibit 5

	For the year ended	
	December 31 2008	December 31 2007
<b>Cash Flows from Operating Activities</b>		
Net loss for the period	\$ (2,186,038)	\$ (1,050,680)
Add items not involving any outlay of cash:		
Income tax recovery	-	(153,881)
Stock-based compensation	1,164,423	408,927
Loss from the sale of marketable securities	16,097	-
Amortization	19,801	12,300
	(985,717)	(783,344)
Changes in non-cash working capital balances:		
Accounts receivable and advances	(802,264)	(97,658)
Prepaid expenses	(274)	(105,644)
Exploration advances received	(249,450)	(550)
Accounts payable and accrued liabilities	211,665	124,773
	\$ (1,734,222)	\$ (862,413)
<b>Cash Flows from Financing Activities</b>		
Share subscriptions receivable	\$ 35,500	\$ -
Issuance of share capital	22,591,669	3,429,179
	\$ 22,627,169	\$ 3,429,179
<b>Cash Flows from Investing Activities</b>		
Proceed from the sale of marketable securities	\$ 10,935	\$ -
Investment in equipment	(62,754)	(25,118)
Investment in mineral properties	(6,404,125)	(2,746,527)
	\$ (6,455,944)	\$ (2,771,645)
<b>Increase (Decrease) in Cash and Cash Equivalents During the Period</b>	<b>14,345,185</b>	<b>(204,879)</b>
<b>Cash and Cash Equivalents, Beginning of the Period</b>	<b>1,566,191</b>	<b>1,771,070</b>
<b>Cash and Cash Equivalents, End of the Period</b>	<b>\$ 15,911,376</b>	<b>\$ 1,566,191</b>

Supplemental Disclosure of Cash and Non-Cash Activities (Note 10)

- see accompanying notes -

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

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**December 31, 2008 and December 31, 2007**

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**1 Nature of Operations:**

The Company's main business is acquiring and exploring mineral properties principally located in the North America, with the objective of identifying mineralized deposits economically worthy of subsequent development, mining or sale.

**2 Continued Operations and Going Concern:**

These consolidated financial statements have been prepared on a going concern basis which assumes that the Company will be able to realize its assets and discharge its liabilities in the normal course of business for the foreseeable future. During the years ended December 31, 2008 and 2007, the Company experienced operating losses and negative operating cash flows, operations of the Company having been primarily funded by the issuance of share capital. Continued operations are dependent on the Company's ability to complete public equity financing or generate profitable operations in the future.

The consolidated financial statements do not reflect adjustments that would be necessary if the going concern assumption were not appropriate. If the going concern basis was not appropriate for these consolidated financial statements, then adjustments would be necessary to the carrying values of assets and liabilities.

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	<b>December 31 2008</b>	December 31 2007
Deficit	\$ 4,795,379	\$ 2,609,341
Working capital	\$ 16,560,559	\$ 1,449,863

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**3 Significant Accounting Policies:**

These consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles ("Canadian GAAP"). The significant accounting policies adopted by the Company are as follows:

**Consolidation**

These consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries, Kootenay Resources Inc. (formerly Kootenay Gold Corp), Minera JM S.A. de C.V. (a company incorporated in Mexico) and Kootenay Gold (US) Corp. All significant inter-company transactions have been eliminated upon consolidation.

**Use of estimates**

The preparation of financial statements in accordance with Canadian GAAP requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amount of revenues and expenses during the period. Actual results could differ from these estimates. The most significant estimates

**KOOTENAY GOLD INC.**  
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**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**December 31, 2008 and December 31, 2007**

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**3 Significant Accounting Policies (continued):**

made by management relate to amounts recorded for the depreciation of capital assets, measurement of stock-based compensation, and the recoverability of mineral properties. By their nature, these estimates are subject to measurement uncertainty and actual results may differ from those estimates.

**Foreign currency translation**

The Company's foreign subsidiary is considered an integrated foreign operation and is translated using the temporal method. Under this method, monetary assets and liabilities are translated at the rate of exchange at the balance sheet date and non-monetary assets and liabilities are translated at historical rates. Revenues and expenses are translated at the exchange rates approximating those in effect on the date of the transactions. Exchange gains and losses arising on translation are included in the consolidated statements of operations.

**Cash and cash equivalents**

Cash is comprised of cash on hand. Cash equivalents are short-term, highly liquid investments with original maturities of three months or less that are readily convertible to known amounts of cash and which are subject to an insignificant risk of change in value.

**Marketable securities**

Marketable securities are recorded at market value by reference to published price quotations in an active market, and are written down when the value is impaired on an other-than-temporary basis, or when no other means exist to independently confirm the recorded value is reasonable. Realized gains or losses on the sale of securities are determined based on specific cost basis.

**Mineral property interests**

All costs related to the acquisition, exploration and development of mineral properties are capitalized by property. If economically recoverable ore reserves are developed, capitalized costs of the related property are reclassified as mining assets and amortized using the unit of production method. When a property is abandoned, all related costs are written off to operations. If, after management review, it is determined that the carrying amount of a mineral property is impaired, that property is written down to its estimated net realizable value. A mineral property is reviewed for impairment whenever events or changes in circumstances indicate that its carrying amount may not be recoverable.

The amounts shown for mineral properties do not necessarily represent present or future values. The recoverability of mineral properties is dependent upon the discovery of economically recoverable reserves, the ability of the Company to obtain the necessary financing and permits necessary to complete the development and future profitable production, or proceeds from the disposition thereof.

Although the Company has taken steps to verify title to mineral properties in which it has an interest, according to usual industry standards for the stage of exploration of such properties, these procedures do not guarantee the Company's title. Such properties may be subject to prior agreements or transfers and title may be affected by undetected defects.

**KOOTENAY GOLD INC.**  
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**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**December 31, 2008 and December 31, 2007**

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**3 Significant Accounting Policies (continued):**

**Stock-based compensation**

In connection with incentive stock options granted by the Company to its officers, directors, employees and consultants, an expense is recognized over the vesting period based on the estimated fair value of the options on the date of the grant as determined using the Black -Scholes option pricing model. The expense is charged to stock-based compensation and the offset is credited to contributed surplus. Cash received on exercise of incentive stock options is credited to the then issued and outstanding capital stock of the Company.

**Equipment**

Equipment is recorded at cost less accumulated amortization. Amortization is recognized using the declining balance method at the following annual rates:

Computer equipment	30%
Computer software	100%
Vehicles	30%

For the year of acquisition, the rate is one-half of the above.

**Asset retirement obligation**

The Company recognizes the fair value of a liability for an asset retirement obligation in the period in which it is incurred or when a reasonable estimate of fair value can be made. The fair value of an asset retirement obligation is recorded as a liability and a corresponding increase in mineral properties. Changes in the liability for an asset retirement obligation due to the passage of time will be measured by applying an interest method of allocation. The amount will be recognized as an increase in the liability and an accretion expense in the statement of operations. Changes resulting from revisions to the timing or the amount of the original estimate of undiscounted cash flows are recognized as an increase or a decrease to the carrying amount of the liability and the related long-lived asset. Actual costs incurred upon settlement are charged against the asset retirement obligation. Any difference between the actual costs and the recorded liability is recognized as a gain or loss in earnings in the period in which the settlement occurs. At present, estimated future site restoration costs for the Company's mineral property interests are considered minimal.

**Flow-through shares**

Canadian tax legislation permits a company to issue flow-through shares whereby the deduction for tax purposes relating to qualified resource expenditures is claimed by the investors rather than the Company. Recording these expenditures for accounting purposes gives rise to taxable temporary differences.

When flow-through expenditures are renounced to the investors, a portion of the future income tax assets that were not recognized in previous years, due to the recording of a valuation allowance, are recognized as a recovery of income taxes in the statement of operations.

**Share capital**

The Company records proceeds from share issuances net of share issuance costs. Share capital issued for non-monetary consideration is recorded at the fair market value of the shares on the date the shares are issued.

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**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**December 31, 2008 and December 31, 2007**

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**3 Significant Accounting Policies (continued):**

**Loss per share**

The Company uses the treasury stock method to compute the dilutive effect of options, warrants and similar instruments. Under this method the dilutive effect on loss per share is recognized on the use of the proceeds that could be obtained upon exercise of options, warrants and similar instruments. It assumes that the proceeds would be used to purchase common shares at the average market price during the period. For the periods presented, this calculation proved to be anti-dilutive. Basic loss per common share is calculated using the weighted-average number of shares outstanding during the period.

**Income taxes**

Income taxes are recorded using the asset and liability method. Under the asset and liability method, future tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Future tax assets and liabilities are measured using the enacted or substantively enacted tax rates expected to apply when the asset is realized or the liability settled. The effect on future tax assets and liabilities of a change in tax rates is recognized in income in the period that substantive enactment or enactment occurs. To the extent that the Company does not consider it more likely than not that a future tax asset will be recovered, it provides a valuation allowance against the excess.

**Financial instruments – Recognition and Measurement – Section 3855**

The Company classifies financial instruments as either available-for-sale, held-for-trading, or loans and receivables. Financial assets, loans and receivables and financial liabilities other than those held for trading, are measured at amortized cost using the effective interest method. Available-for-sale instruments are measured at fair value with unrealized gains and losses recognized in comprehensive income, unless an unrealized loss is considered to be other than temporary in which case the loss is recorded on the consolidated statement of operations for the period. Instruments classified as held-for-trading are measured at fair value with unrealized gains and losses recognized on the statement of operations. Transaction costs on financial assets and liabilities classified other than as held-for-trading are treated as part of the investment cost.

The Company has classified its financial assets and liabilities as follows:

<u>Held-for-trading</u>	<u>Loans and receivables</u>	<u>Available-for-sale</u>	<u>Other liabilities</u>
Cash and cash equivalents	Receivables Subscriptions receivable Exploration deposits Exploration advances	Marketable securities	Exploration advances Accounts payable Accrued liabilities

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

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**December 31, 2008 and December 31, 2007**

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**3 Significant Accounting Policies (continued):**

**Comprehensive income**

Other comprehensive income represents the change in net equity for the period that arises from unrealized gains and losses on available-for-sale financial instruments, and changes in the fair market value of derivative instruments designated as cash flow hedges. Amounts included in other comprehensive income are shown net of tax. Cumulative changes in other comprehensive income are included in accumulated other comprehensive income which is presented (if applicable) as a new category in shareholders' equity.

**Risk management**

The Company's activities expose it to a variety of financial risks: market risk (foreign exchange risk), credit risk and liquidity risk. The Company's risk management program focuses on ensuring liquidity is available to the Company in order to fund its exploration efforts. Risk management is the responsibility of Kootenay's management who identifies and evaluates financial risks.

**Hedges – Sections 3865**

This Section establishes standards for how hedge accounting may be applied. The Company currently does not have any hedges in place, and therefore this standard has no impact on the financial statements.

**Capital Disclosures – Section 1535**

This Section which specifies the disclosure of information that enables users of an entity's financial statements to evaluate management's objectives, policies and processes for managing capital including qualitative information about its objectives, policies and processes for managing capital, summary quantitative data about what the entity manages as capital, whether it has complied with any capital requirements and, if it has not complied, the consequences on non-compliance.

**Section 1400, General Standards of Financial Statement Presentation**

In June 2007, the CICA amended Handbook Section 1400, Going Concern, to assess an entity's ability to continue as a going concern and disclose any material uncertainties that cast doubt on its ability to continue as a going concern. The amendments to Section 1400 are effective for interim and annual reporting periods beginning on or after January 1, 2008. The application of this new standard had no impact on the Company's operating results or financial position.

**Recent accounting pronouncements issued by the CICA, which have not yet been adopted by the Company.**

**Transition to International Financial Reporting Standards**

In 2006, Canada's Accounting Standards Board (AcSB) ratified a strategic plan that will result in the convergence of Canadian GAAP, as used by public companies, with International Financial Reporting Standards over a transitional period. The AcSB has developed and published a detailed implementation plan, with a changeover date for fiscal years beginning on or after January 1, 2011. The Company has not assessed the impact of the initiative on its financial statements.

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

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**December 31, 2008 and December 31, 2007**

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**4 Marketable Securities:**

Marketable securities are classified as available for sale financial instruments, which are adjusted to market value at the end of the reporting period. Market value as at December 31, 2008 is \$267,238 (2007 – \$365,750), resulting in other comprehensive loss of \$507,355 (2007 – \$47,000 gain).

**5 Equipment:**

	<b>Cost</b>		<b>Accumulated Amortization</b>		<b>2008 Net</b>		<b>2007 Net</b>
Vehicles	\$	58,411	\$	23,459	\$	34,952	21,193
Computer		72,946		16,451		56,495	27,301
	\$	131,357	\$	39,910	\$	91,447	48,494

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# KOOTENAY GOLD INC.

(An Exploration Stage Company)

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2008 and December 31, 2007

### 6 Mineral Properties:

	Canada		Santa	Sonora	Los		El		Mexico	United	2008	2007	
	Total	Promontorio	Lucia	Anomalies	Chinos	Opochi	Cuervo	Espiritu*	Other	Total	States	Total	Total
	\$	\$	\$	\$	\$				\$	\$	\$	\$	\$
<b>Acquisition Costs</b>													
Balance, beginning	341,399	967,326	55,724	29,823	47,375	-	-	-	4,728	1,104,976	65,102	1,511,477	262,718
Incurred	364,973	1,645,068	31,500	472,398	1,037	-	-	-	330	2,150,333	-	2,515,604	1,248,759
Balance, ending	706,372	2,612,394	87,224	502,221	48,412	-	-	-	5,356	3,255,309	65,102	4,027,081	1,511,477
<b>Exploration Expenditures</b>													
Balance, beginning	1,715,602	1,247,443	331,065	794,530	19,190	-	150,000	150,000	14,709	2,706,937	204,326	4,626,865	1,013,168
Assaying and Lab	161,119	443,552	1,304	61,800	-	-	-	-	-	506,656	999	668,774	111,554
Camp Costs	18	326,803	5,554	285,390	-	-	-	-	-	617,747	878	618,643	58,228
Drafting	4,420	-	-	-	-	-	-	-	-	-	-	4,420	78,966
Drilling	494,634	1,930,455	-	-	-	-	-	-	-	1,958,455	-	2,425,089	1,077,264
Geological mapping	110,970	113,649	13,645	72,647	394	236	-	236	-	200,807	-	311,777	180,490
Geophysics	225,509	471,418	3,884	-	-	-	-	-	-	475,302	(90)	700,721	862,316
Maintenance	52,814	92,587	52,380	373,552	28,036	2,289	38,441	51,651	-	638,936	10,600	702,350	67,758
Miscellaneous	109,361	3,741	28,748	18,136	-	-	-	-	-	50,625	-	159,986	181,060
Prospecting	202,809	374,052	5,595	225,080	64,865	32,597	6,281	11,551	-	720,021	-	982,829	856,815
Rock Sampling	47,143	64,609	17,280	-	4,060	-	-	-	-	85,949	-	133,092	139,246
Incurred	1,408,796	3,820,866	128,390	1,096,142	97,355	35,122	44,722	63,438	-	5,226,498	12,387	6,647,681	3,613,697
Balance, ending	3,124,398	5,096,309	459,455	1,831,135	116,545	35,122	194,722	213,438	14,411	7,933,435	216,713	11,274,546	4,626,865
Total property balance	3,830,770	7,680,703	546,679	2,333,356	164,957	35,122	194,722	213,438	19,767	11,188,744	281,815	15,301,329	6,138,342
Recovery of costs	(1,058,841))	-	(595,057)	(1,145,442)	-	-	(163,397)	(164,944)	-	(2,068,840)	-	(3,127,681)	(1,361,687)
Abandoned	-	-	-	-	-	-	-	-	-	-	-	-	-
Cumulative mineral property costs	2,771,929	7,680,703	(48,378)	1,187,914	164,957	35,122	31,325	48,494	19,767	9,119,904	281,815	12,173,648	4,776,655

\*Joint Venture Project

# KOOTENAY GOLD INC.

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December 31, 2008 and December 31, 2007

### 6 Mineral Properties (Canada):

	Alisa Lake	Chapleau*	Chenier	Conner Creek	CP Midas	Deer Creek	Monashee	Jumping Josephine*	Murphy	Sunrise	Rosetta*	Other	2008 Total	2007 Total
	\$	\$	\$	\$	\$	\$	\$	\$	\$	\$	\$	\$	\$	\$
<b>Acquisition Costs</b>														
Balance, beginning	50,000	-	50,800	24,250	50,000	42	-	24,250	50,000	77,500	-	14,557	341,399	62,491
Incurred	32,000	-	32,000	-	32,000	48,997	46,250	55,000	32,000	32,000	51,093	3,633	364,973	278,908
Balance, ending	82,000	-	82,800	24,250	82,000	49,039	46,250	79,250	82,000	109,500	51,093	18,190	706,372	341,399
<b>Exploration Expenditures</b>														
Balance, beginning	4,685	29,333	199,424	439,640	55,538	81,930	-	97,667	188,375	54,430	-	564,580	1,715,602	557,329
Assaying and Lab	10,206	12,043	-	15,478	-	13,361	52,827	36	91	-	10,231	46,846	161,119	43,126
Camp Costs	-	18	-	-	-	-	-	-	-	-	-	-	18	697
Drafting	-	-	-	-	-	-	-	-	-	-	1,200	3,220	4,420	11,054
Drilling	-	-	-	13,695	-	-	-	480,939	-	-	-	-	494,634	440,535
Geological mapping	984	52,776	-	5,777	158	2,190	-	(942)	1,685	325	1,200	46,817	110,970	27,688
Geophysics	3,618	666	-	5,935	-	550	85,180	-	-	-	122,478	7,082	225,509	285,005
Maintenance	1,372	316	-	5,219	445	1,200	9,027	114	1,375	-	15,589	18,157	52,814	30,250
Miscellaneous	-	282	-	-	-	-	-	104,043	1,925	-	800	2,311	109,361	12,026
Prospecting	7,788	3,294	550	1,951	4,950	1,176	7,423	2,276	1,451	844	11,404	159,701	202,808	204,054
Rock Sampling	-	-	-	1,388	424	2,667	-	-	2,618	-	2,842	37,204	47,143	103,838
Incurred	23,968	69,395	550	49,443	5,977	21,144	154,457	586,466	9,145	1,169	165,744	321,338	1,408,796	1,158,273
Balance, ending	28,653	98,728	199,975	493,372	61,515	103,074	154,457	684,133	197,520	55,599	165,744	885,918	3,124,128	1,715,602
Total property balance	110,653	98,728	275,775	513,333	143,515	152,113	200,707	763,383	279,520	165,099	216,837	904,108	3,830,770	2,057,001
Recovery of costs	-	-	(254,959)	(485,872)	-	-	-	(145,950)	(172,060)	-	-	-	(1,058,841)	(864,114)
Abandoned	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Cumulative mineral property costs	110,653	98,728	20,815	27,461	143,515	152,113	200,707	617,433	107,460	165,099	216,837	904,108	2,771,929	1,192,887

\*Joint Venture Project

**KOOTENAY GOLD INC.**  
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**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**December 31, 2008 and December 31, 2007**

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**6 Mineral Properties (continued):**

**Details of Mineral Properties - Canada**

**Connor Creek Property** - Trail Creek Mining Division, British Columbia

The Company exercised its right under a Grubstake Agreement dated March 20, 2003 granting the Company the option to purchase a 100% interest in thirty-six mineral claims covering sixty-eight units in the Connor Creek area of Trail, British Columbia.

In order to exercise its option the Company must issue 100,000 shares of the Company to the vendor, and incur an aggregate of \$40,000 in expenditures on or before July 23, 2007. The Company expended \$49,443 on the property for the year ended December 31, 2008 (2007 - \$404,333). The Company issued 25,000 shares valued at \$0.25, 25,000 shares valued at \$0.10, 25,000 shares valued at \$0.37, and 25,000 shares valued at \$0.75 per share each, pursuant to this agreement. With expenditure commitments being fulfilled and the issuance of common stock to the vendor under the agreement, the claims have been transferred to the Company.

The Company entered into an option agreement with Amador Gold Inc., whereby the Company granted the right to Amador to earn a 50% undivided interest in the Connor Creek property. The option calls for Amador to expend \$1,000,000 in exploration and issue 400,000 shares to the Company over 4 years. If commercial production is reached, an additional 250,000 shares of Amador are payable to the Company. The Company received accumulative reimbursements in the amount of \$485,872 for costs incurred up to the period ended December 31, 2008 (2007 - \$431,037). During the year ended December 31, 2008, the Company received notice of termination of the option agreement from Amador .

**Jumping Josephine Property** - Nelson Mining Division, British Columbia

The Company exercised its right under a Grubstake Agreement dated March 20, 2003 granting the Company the option to purchase a 100% interest in twenty mineral claims comprised of fifty-eight units in the Jumping Josephine area of Nelson, British Columbia.

In order to exercise its option the Company must issue 100,000 shares of the Company to the vendor and incur an aggregate of \$40,000 in expenditures on or before July 23, 2007. The Company issued 25,000 shares valued at \$0.25, 25,000 shares valued at \$0.10, 25,000 shares valued at \$0.37 and 25,000 shares valued at \$0.75 per share each, pursuant to this agreement. With expenditure commitments being fulfilled and the issuance of common stock to the vendor under the agreement the claims have been transferred to the Company.

The Company entered into an additional agreement dated June 30, 2005, which grants the Company the option to purchase a 100% interest in additional seven mineral claims in the Jumping Josephine area of Nelson, British Columbia. In order to exercise its option the Company must pay \$97,000 to the vendor and incur an aggregate of \$500,000 in expenditures on or before the October 31, 2009.

The Company entered into an option agreement with Astral Mining Corporation, ("Astral") on April 11, 2006, whereby the Company will grant to Astral the right to earn up to 60% undivided interest in the Jumping Josephine Property. Astral have fulfilled its obligations under the option agreement by spending \$2,100,000 in exploration on the property and issuing to the Company 400,000 common shares. Under the joint venture agreement the Company is carrying a 40% interest and incurred \$586,466 to the period ending December 31, 2008.

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December 31, 2008 and December 31, 2007

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### 6 Mineral Properties (continued):

#### **Chapleau Property** – Sault Ste. Marie Mining Division, Ontario

The Company entered into a 50/50 joint venture agreement with Golden Chalice Resources Inc. (formerly International Chalice Resources Inc.) to further explore the Kimberlite dike with large diamond potential on the Chapleau property. Cost will be shared equally on March 1, 2006. The Company expended \$69,395 in exploration during the period ended December 31, 2008 (2007 - \$29,333).

#### **Other Properties – Southern British Columbia**

On September 27, 2006, the Company exercised its right under a Grubstake Agreement granting the Company the option to purchase a 100% interest in five mineral claims comprising of twenty-eight units. The properties are known as the Sunrise, Midas, Chenier, Murphy and Alisa Lake Properties. Four (Sunrise, Chenier, Murphy and Midas) are located in the Rossland-Republic trend and Alisa Lake is in the Sullivan District in south eastern British Columbia.

The agreement requires issuance of 25,000 shares per property on September 27, 2006 and 25,000 shares in the next three anniversaries (September 27, 2007; September 27, 2008; September 27, 2009) for a total of 100,000 for each property, being a total of 500,000 shares. The Company must also make expenditures of \$40,000 on each property by April 1, 2011. The Company expended a total of \$40,809 (Sunrise \$1,169; Chenier \$550; Murphy \$9,145; Midas \$5,977; and Alisa \$23,968) on the properties during the year ended December 31, 2008 (2007 - \$410,491). The Company issued 150,000 shares valued at \$1.10; 125,000 shares valued at \$0.90; 125,000 shares valued at \$1.00 and 125,000 shares valued at \$1.28 per share pursuant to this agreement.

A bonus payment of 200,000 common shares is payable upon commencement of Commercial Production on any given property. The Company has the right to terminate the property agreements at anytime.

On April 17, 2007, the Company entered into an option agreement with Astral Mining Corporation (“Astral”), whereby the Company gave the right to Astral to earn a 60% undivided interest in the Chenier property located in the West Kootenay region of in south eastern British Columbia. In order to exercise its option, Astral must issue 500,000 common shares to the Company and incur an aggregate of \$2,500,000 in expenditures for each mineral property on or before May 4, 2011. The Company received accumulative reimbursements in the amount of \$254,959 for costs to the period ended December 31, 2008 (2007 - \$237,532). During the year ended December 31, 2008, Astral exercised its right to terminate the option agreement.

During the year ended December 31, 2008, the option agreement on the Murphy Property with Abitibi Mining Corp (“Abitibi”) was terminated by the optionee. The Company received 100,000 shares of Abitibi for total accumulative reimbursements in the amount of \$172,060 for costs incurred up to the period ended December 31, 2008 (2007 - \$nil).

# KOOTENAY GOLD INC.

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## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2008 and December 31, 2007

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### 6 Mineral Properties (continued):

Under the terms of the Kennedy Grubstake Agreement dated March 20, 2003, on July 2, 2008, Kootenay Gold Inc. elected to option three additional properties namely, Deer Park, Rosetta Creek and Monashee. All projects are located in the West Kootenay region of British Columbia. Deer Park covers 10,573 hectares in 24 claims, Monashee covers 11,459 hectares in 24 claims and Mc Donald Creek covers 11,588 hectares in 26 claims. The Company expended a total of \$341,345 (Deer Park \$21,144; Monashee \$154,457 and Rosetta \$165,744)

Under the terms of the Grubstake Agreement each property requires a work commitment of \$40,000 over three years and share payments of 25,000 shares on election of the option and 25,000 shares on each of years one, two and three to maintain the option in good standing. If production is achieved on a specific property a bonus of 200,000 shares would be paid. The Company issued 75,000 common shares valued at \$1.85 per share pursuant to the terms of the agreement.

On November 24, 2008, the Company entered into an option agreement with Theia Resources ("Theia"), whereby the Company gave the right to Theia to earn a 60% undivided interest in the Rosetta Creek property. In order to exercise its option, Theia must issue 400,000 common shares to the Company with 100,000 issuable on the fifth day after the regulatory approval and the remaining shares issued in equal amounts on the anniversary of the agreement for the following three years. An aggregate of \$1,000,000 in exploration expenditures must be expended by Theia on the mineral property within a five year period commencing regulatory approval.

Additional properties have been staked and are currently being evaluated to determine the viability of further exploration or development. Once the Company has made its evaluations the properties will be either be abandoned or acquired under the terms of the Grubstake Agreements.

### Details of Mineral Properties - Mexico

#### Promontorio - Sonora State, Mexico

The Company entered into an agreement on October 20, 2006 with Siete Companas de Plata, S.A de C.V. ("Siete"), Exploration Canada De Oro, SA de CV ("ECO") and the Mexican Government Agency ("FIFOMI") to acquire an unencumbered 100% registered and beneficial interest in the former producing Promontorio Mine Site and the surrounding properties and mineral rights known as the Promontorio Concession. The claims cover approximately 37,000 hectares, and are located in the historic silver and gold producing Sierra Madre Region of Northwest Mexico. The Company expended \$3,820,866 on exploration for the year ended December 31, 2008 (2007 - \$1,119,496).

The agreement calls for the Company to pay up to \$1,375,000 U.S. in cash, issue up to 850,000 shares of Kootenay to ECO and Siete, and to pay a debt owing to FIFOMI in connection with the Promontorio Concession. The Company issued 300,000 shares valued at \$1.15 per share; 150,000 shares valued at \$1.05 per share; 200,000 shares with a average value of \$1.93 per share; 50,000 shares valued at \$1.68 per share and 150,000 shares valued at \$2.11 per share pursuant to this agreement.

In addition, there is a 2 per-cent net smelter return relating to the acquisition. The Company may upon commencement of commercial production or sooner purchase 50 per cent of the net smelter return for \$1,000,000 U.S. in order to reduce the total net smelter return to 1 per cent. The Company also has the right of first refusal on the remaining 1 per cent in the event that the ECO and Siete decide to sell it. The Company has also negotiated a settlement with FIFOMI on the properties outstanding debt; under the terms of the agreement the Company will pay FIFOMI 4,218,935 pesos (\$400,000 U.S.) over a five- year period.

# KOOTENAY GOLD INC.

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## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2008 and December 31, 2007

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### 6 Mineral Properties (continued):

#### **Santa Lucia** - Southern Sonora State, Mexico

On May 1, 2006, amended September 27, 2006, the Company entered into an agreement which grants the Company the option to purchase a 100% interest in two mineral claims comprised of 9,350 hectares in the southern Sonora State region located between Navajoa and Alamos, Mexico.

In order to exercise its option the Company must issue 100,000 shares of the Company to the vendor. The Company expended \$128,390 on exploration during the year ended December 31, 2008 (2007 - \$227,786). The Company under a grubstaking agreement dated June 15, 2005 issued a total of 75,000 shares, with three tranches of 25,000 shares valued at \$0.74; \$1.00 and \$1.35 per share respectively pursuant to this agreement. In addition, there is a 2.5-per-cent net smelter return relating to the acquisition. The Company may upon commencement of commercial production or sooner purchase 50 per cent of the net smelter return for \$1,000,000 U.S. in order to reduce the total net smelter return to 1.25 per cent. The Company also has the right of first refusal on the remaining 1.25 per cent in the event that the Cross group decides to sell it.

The Company entered into a letter agreement dated June 6, 2006 with Klondike Silver Corp. ("Klondike"), whereby the Company will grant to Klondike the right to earn up to a 50% interest in the Santa Lucia property located in Sonora State, Mexico. In order to earn their interest, Klondike must spend \$1,000,000 U.S. in exploration on the property; pay \$25,000 U.S. in cash and issue to the Company 500,000 common shares in its capital by June 14, 2009. The Company received 500,000 shares of Klondike pursuant to this agreement. The Company received accumulative reimbursements in the amount of \$595,057 for costs incurred up to the year ended December 31, 2008 (2007 - \$252,940). Subsequent to the year end, the Company received notice of termination on the Santa Lucia option agreement from Klondike.

#### **Sonora Anomalies** - Northwest Mexico

The Company entered into an agreement dated June 21, 2006 with Klondike Silver Corp. ("Klondike"), whereby the Company granted to Klondike the right to earn up to a 50% interest in three mineral properties in Mexico. In order to earn their interest, Klondike must reimburse the Company \$250,000 U.S., and for each property optioned, spend \$1,000,000 U.S. on exploration and issue to the Company 500,000 common shares within two years of the exchange approval date which is yet to be determined. In June 2007, under the same terms as the initial agreement, Klondike agreed to increase the number of properties by three. The Company expended \$1,096,142 on exploration during the year ended December 31, 2008 (2007 - \$1,056,042). The Company received accumulative reimbursements in the amount of \$1,145,442 for costs incurred to the year ended December 31, 2008 (2007 - \$127,133).

# KOOTENAY GOLD INC.

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## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2008 and December 31, 2007

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### 6 Mineral Properties (continued):

On March 31, 2008, the Company announced the completion of six option agreements with Klondike Silver Corp. ("Klondike") on six of the Company's 100% owned mineral concessions in the Sierra Madre Region of Northwest Mexico. The six concessions selected by Klondike include two epithermal precious metal settings (Suzanne and Ofelia), three porphyry settings (Los Alamos, Cerro Colorado and Espiritu) and one skarn (Cuervo). Under the terms of each option agreement, Klondike can earn a 50% undivided interest in the mineral concession by incurring or funding a minimum of US\$1,000,000 in exploration expenditures in stages over three years and issuing 500,000 shares to the Company in stages over two years. In order for Klondike to earn an undivided interest in all six mineral concessions, Klondike must incur or fund minimum exploration expenditures totaling in the aggregate \$6,000,000 (US\$1,000,000 on each mineral concession) and issue to the Company an aggregate of 3,000,000 shares (500,000 shares per mineral concession).

On August 18, 2008, Klondike received regulatory approval and issued the Company 1,800,000 common shares being the initial commitment of 300,000 common shares per each optioned property. Subsequent to the year end, the Company received notice of termination on all but the Espiritu option agreement from Klondike.

The Company continues to advance the remaining properties from the Staking activities originally funded by Klondike.

#### **Details of Mineral Properties - United States**

##### **Elephant Mountain Property - Rampart Mining District, Alaska, U.S.A.**

On December 12, 2003, the Company acquired seventy-one mineral claims in the Rampart mining district located eighty kilometres northwest of Fairbanks, Alaska. The property is subject to a 1.5% net returns royalty to the vendors. The Company purchased the property for \$65,102 and has expended a total of \$216,713 since acquisition.

##### **Title to Mineral Property Interests**

Although the Company has taken steps to verify the title to mineral properties in which it has an interest, in accordance with industry standards for the current stage of exploration of such properties, these procedures do not guarantee the Company's title. Property title may be subject to unregistered prior agreements or transfers and title may be affected by undetected defects.

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**7 Share Capital:**

**Authorized:**

Unlimited common shares without par value

Unlimited preferred shares

**Issued and Fully Paid:**

	Number of Shares		Share Capital		Contributed Surplus
Balance, December 31, 2005	9,851,800	\$	1,247,031	\$	8,260
For cash:					
Exercise of stock options	280,000		49,000		-
Private placements	793,500		357,075		-
Exercise of warrants	3,200,000		1,312,000		129,099
Acquisition of mineral properties	75,000		56,000		-
Share issuance costs	-		(129,100)		-
Stock-based compensation	-		-		501,838
<b>Balance, December 31, 2006</b>	<b>14,200,300</b>	<b>\$</b>	<b>2,892,006</b>	<b>\$</b>	<b>639,197</b>
For cash:					
Private placement, net of issuance cost of \$90,317	5,298,925		761,361		3,238,440
Exercise of warrants	914,500		713,978		(220,427)
Exercise of stock options	100,000		122,740		(51,740)
Acquisition of mineral properties	750,000		805,000		-
Future income tax effect on renunciation of flow-through share expenditures	-		(153,881)		-
Share issuance costs	-		(206,683)		-
Stock-based compensation	-		-		408,927
<b>Balance, December 31, 2007</b>	<b>21,263,725</b>	<b>\$</b>	<b>4,934,521</b>	<b>\$</b>	<b>4,014,397</b>
For cash:					
Private placement, net of issuance cost of \$2,428,145	11,401,200		11,583,877		8,069,626
Exercise of warrants	3,410,925		5,316,975		(2,367,735)
Exercise of stock options	63,750		83,685		(35,560)
Acquisition of mineral properties	725,000		1,339,750		-
Stock-based compensation	-		-		1,164,423
<b>Balance, December 31, 2008</b>	<b>36,864,600</b>	<b>\$</b>	<b>23,258,808</b>	<b>\$</b>	<b>10,845,151</b>

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**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**December 31, 2008 and December 31, 2007**

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**7 Share Capital (continued):**

2008 Private Placements

On February 29, 2008, the Company issued 5,500,000 units at \$1.50 per unit for total gross proceeds of \$8,250,000. Each unit consisted of one common share and one-half share purchase warrant. One whole warrant is exercisable into an additional common share for \$1.80 expiring August 29, 2009. The Company paid a finder's fee of \$369,285 in cash, 94,500 finder's units and 340,690 share purchase warrants. Each warrant is exercisable into one common share at \$1.70 per share expiring on August 29, 2009.

On June 19, 2008, the Company issued 5,648,000 units at \$2.20 per unit, by way of brokered private placement for total gross proceeds of \$12,425,600. Each unit consisted of one common share of the Company and one-half of one transferable common share purchase warrant. Each whole Warrant will entitles the holder to acquire, at any time within 24 months from the date of closing of the Private Placement, one additional common share of the Company at an exercise price of \$2.75 per share. A total of 2,824,000 Warrants were issued to investors under the Private Placement. A commission equal to 6.5% of the gross proceeds of the Private Placement, consisting of \$458,524 paid in cash and 158,700 units (the "Agent's Units"), having the same terms as the Units sold under the Private Placement, except that the common share purchase warrants comprising part of the Agent's Units are non-transferable. The Agent also received 367,120 options (the "Agent's Options"), equal to 6.5% of the number of Units sold under the Private Placement. Each Agent's Option is exercisable at any time up to 24 months following the Closing to acquire one common share of the Company at an exercise price of \$2.50 per share.

2007 Private Placements

On January 12, 2007, the Company completed a private placement of 3,076,925 units at a price of \$0.65 per unit consisting of one common share and one common share purchase warrant, for gross proceeds of \$2,000,001. The warrant entitles the holder to acquire one common share at a price of \$0.80 per share for a period of eighteen months from the date the warrant is issued. The warrants were valued at \$2,324,309. Issuance costs of \$90,317 were netted against the proceeds.

On October 23, 2007, the Company completed a private placement of 2,222,000 units at a price of \$0.90 per unit consisting of one common share and one common share purchase warrant, for gross proceeds of \$1,999,800. Each warrant entitles the holder to purchase one common share at a price of \$1.25 per share for a period of eighteen months from the date of issuance of the warrant. Subsequent to four months from closing, the Company has a right upon 30 days notice to holders, to accelerate conversion of warrants by warrant holders if the share price of the Company remains equal to or greater than \$2.25 per common share for a period of twenty consecutive trading days. The warrants were valued at \$914,131. Issuance costs of \$89,106 were netted against the proceeds.

In February 2007, the Company renounced \$451,000 of flow-through share expenditures to investors for Canadian Income Tax purposes. As a result, \$153,881 has been charged to share capital to reflect the future income tax effect of the renouncement.

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**8 Options and Warrants:**

Stock option and share purchase warrant transactions are summarized as follows:

	Warrants		Options	
	Number	Weighted Average Exercise Price	Number	Weighted Average Exercise Price
<b>Outstanding, December 31, 2006</b>	<b>793,500</b>	<b>0.50</b>	<b>1,425,000</b>	<b>0.746</b>
Granted	5,298,925	0.99	625,000	0.914
Exercised	(914,500)	0.54	(100,000)	0.710
Expired/Cancelled	-	-	-	-
<b>Outstanding, December 31, 2007</b>	<b>5,177,925</b>	<b>1.18</b>	<b>1,950,000</b>	<b>0.802</b>
Granted	6,408,410	2.25	890,000	1.950
Exercised	(3,410,925)	0.90	(63,750)	0.738
Expired/Cancelled	(35,000)	0.80	-	-
<b>Outstanding, December 31, 2008</b>	<b>8,140,410</b>	<b>\$ 2.05</b>	<b>2,776,250</b>	<b>\$ 1.171</b>

**Warrants**

As at December 31, 2008, the Company had outstanding share purchase warrants, enabling holders to acquire common shares as follows:

Number of Shares	Exercise Price	Expiry Date
1,732,000	1.25	April 22, 2009
2,797,250	1.80	August 29, 2009
340,690	1.70	August 29, 2009
2,903,350	2.75	June 19, 2010
367,120	2.50	June 19, 2010
<b>8,140,410</b>		

The fair value of warrants is estimated using the Black Scholes option-pricing model. Warrants are included in contributed surplus until exercised, at which time they are transferred into share capital.

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**8 Options and Warrants (continued):**

The following assumptions were used for the Black-Scholes valuation of warrants issued during 2008 and 2007:

	<b>2008</b>	<b>2007</b>
Risk-free interest rate	<b>3.10% - 3.35%</b>	4.20% - 4.33%
Expected life of warrants	<b>18 – 24 months</b>	1.5 years
Fair value per warrant issued	<b>\$1.12 - \$1.44</b>	\$0.41 - \$0.75
Annualized volatility	<b>95% - 105%</b>	80% - 98%
Dividend rate	<b>0.00%</b>	0.00%

**Options**

The Company has adopted an incentive stock option plan under the rules of the TSX Venture Exchange ("TSXV") pursuant to which it is authorized to grant options to executive officers, directors, employees and consultants, enabling them to acquire up to 10% of the issued and outstanding common shares of the Company. Under the plan, the exercise price of each option is equal to the market price of the Company's shares on the date of grant. The options can be granted for a maximum term of 5 years and generally vest 25% in specified increments. No individual may hold options to purchase common shares of the Company exceeding 5% of the total number of common shares outstanding from time to time. Pursuant to the policies of the TSX Venture Exchange, shares issued on exercise of options are restricted from trading during the four month period subsequent to the date of grant.

As at December 31, 2008, the Company had outstanding stock options enabling holders to acquire common share of the Company as follows:

	Number of Shares	Exercise Price	Expiry Date
	875,000	\$ 0.71	April 12, 2011
	400,000	0.84	December 5, 2011
	436,250	0.90	September 18, 2011
	175,000	0.95	October 23, 2011
	890,000	1.95	March 31, 2013
	<b>2,776,250</b>		

For stock options granted to employees, officers, directors and consultants, the Company recognizes stock-based compensation expense based on the estimated fair value of the stock options granted as calculated using the Black-Scholes option-pricing model on the date of the grant.

The following assumptions were used for the Black-Scholes valuation of stock options granted during 2008 and 2007:

	<b>2008</b>	<b>2007</b>
Risk-free interest rate	<b>2.67%</b>	4.22 % - 4.23 %
Expected life of options	<b>5 years</b>	5 years
Fair value per option granted	<b>\$1.60</b>	\$0.72 - \$0.80
Annualized volatility	<b>108.7%</b>	109.9% - 111.07%
Dividend rate	<b>0.00%</b>	0.00%

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**8 Options and Warrants (continued):**

During the year ended December 31, 2008, the Company granted 890,000 (2007 – 625,000) stock options with a exercise price of \$1.95 per option (2007 - \$0.91). Stock-based compensation totalling \$1,164,423 (2007 - \$408,927) was expensed during the year. As at December 31, 2008, 2,178,437 options with a weighted average exercised price of \$1.03 per option were vested and exercisable.

Option pricing models require the input of highly subjective assumptions, particularly as to the expected price volatility of the stock. Changes in these assumptions can materially affect the fair value estimate and therefore it is management's view that the existing models do not necessarily provide a single reliable measure of the fair value of the Company's stock option and warrant grants.

**9 Income Taxes:**

A reconciliation of current income taxes at statutory rates with the reported taxes is as follows:

	<b>2008</b>	<b>2007</b>
Loss before income taxes	<b>\$ 2,186,038</b>	\$ 1,050,680
Statutory rates	<b>30.00%</b>	31.50%
Expected income tax recovery at statutory rates	<b>(655,811)</b>	(330,964)
Effect of reduction in tax rates	<b>(7,577)</b>	19,913
Tax benefit from share issuance costs not recognized	<b>(728,443)</b>	(65,106)
Stock based compensation not deductible for tax purposes	<b>349,327</b>	128,614
Other deductible items for tax purposes	<b>-</b>	(9,513)
Non-deductible items for tax purposes	<b>4,724</b>	1,142
Increase (decrease) in valuation allowance	<b>1,037,780</b>	102,033
Future income tax recovery	<b>\$ -</b>	\$ (153,881)

Details of future income tax assets are as follows:

	<b>2008</b>	<b>2007</b>
Future income tax assets:		
Non-capital losses carried forward	<b>\$ 992,469</b>	\$ 557,431
Tax value of mineral properties in excess of book value	<b>(113,875)</b>	22,403
Tax value of share issuance costs in excess of book value	<b>667,222</b>	76,484
Tax value of equipment in excess of book value	<b>12,309</b>	6,092
	<b>1,558,125</b>	662,410
Flow through share renunciation	<b>-</b>	(142,065)
Valuation allowance	<b>(1,558,125)</b>	(520,345)
Future income tax assets	<b>\$ -</b>	\$ -

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**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

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**9 Income Taxes (continued):**

Estimated taxable income for the period is \$nil. Based upon the level of historical taxable income, it cannot be reasonably estimated at this time if it is more likely than not that the Company will realize the benefits from future income tax assets. The estimated taxable temporary difference valuation allowance will be adjusted in the period it is determined that it is more likely than not that some portion or all of the future tax assets will be realized.

As at December 31, 2008, the Company has non-capital losses of approximately \$3,308,230 (2007 - \$1,748,204) which may be carried forward to apply against future years income tax for Canadian income tax purposes, subject to final determination by taxation authorities and expiring as follows:

2009	\$	2,646
2009		26,700
2010		78,801
2014		167,304
2015		287,469
2026		481,860
2027		724,842
2028		1,538,608
		\$ 3,308,230

**10 Supplemental Disclosure of Cash and Non-Cash Activities:**

The following transactions incurred during the period did not include cash:

	<b>2008</b>	2007
Acquisition of marketable securities as proceeds on the optioning of mineral property interests	\$ <b>435,875</b>	\$ 147,500
Issuance of share capital for acquisition of mineral property interests	<b>1,339,750</b>	805,000

**11 Related Party Transactions and Balances:**

Except as disclosed elsewhere in these financial statements related party transactions are as follows:

The following related party transactions were incurred in the normal course of business and are non-interest bearing, unsecured, due on demand and were measured at their fair value as determined by management.

	<b>2008</b>	2007
Management fees charged by a company controlled by a director and officers	\$ <b>434,000</b>	\$ 118,600
Consulting, administrative and management fees charged by a company controlled by common directors	<b>134,161</b>	20,000
Consulting and accounting fees charged by a company controlled by an officer	-	47,883
Consulting and management fees charged by a director and officer	-	96,000

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**11 Related Party Transactions and Balances (continued):**

The Company has entered into a consulting agreement with Makwa Exploration Ltd. for the services of James McDonald to act as the Company's President and CEO, and with Manly Capital Corp. for the services of Kenneth Berry to act as the Company's Chairman. The consulting agreement is effective as of January 1, 2008 and expires on December 31, 2009 and will unless otherwise terminated extend for an additional 24 months.

Effective September 1, 2008, the Company entered into a administrative services agreement with Touchstone Capital Corp. a private company owned by two directors of the Company. Touchstone provides services to the Company including assisting in professional analysis and planning of exploration programs, promotional materials; providing access to secretarial services and providing such other additional instructions and directions as the Company may require. For the year ended December 31, 2008 the Company incurred expenses of \$134,161 under the administrative services contract. The agreement is effective as of September 1, 2008 and expires on August 31, 2010 and will unless otherwise terminated extend on an annual basis.

Included in accounts receivable as at December 31, 2008, is \$421,338 receivable from company's controlled by a common director. The amounts are related to exploration costs incurred by the Company on behalf of projects were a earn-in option agreement exists.

In addition to the above:

- a) Included in accounts payable and accrued liabilities as at December 31, 2008 is \$117,995.11 (December 31, 2007-\$2,758) due to a director or companies controlled by directors or officers.
- b) Included in marketable securities as at December 31, 2008 is \$238,550 (December 31, 2007-\$20,750) are market value of shares received from a company with a director in common.
- c) Included in mineral properties as at December 31, 2008 is \$2,726,772 (December 31, 2007-\$476,823) which are funds received as recoveries from joint venture partners whose companies are controlled by common directors.

The Company received notice of termination from three of its joint venture partners whose companies are controlled by common directors terminated their option agreements. The cost recoveries from the terminated joint venture partners accounted for \$796,798 of the Company's 2008 cost recoveries.

- d) Included in mineral properties as at December 31, 2008 is \$9,781 (December 31, 2007-\$6,855) paid as consulting fees to a director's immediate family.
- e) Included in administration fee income as at December 31, 2008 is \$132,276 (December 31, 2007-\$71,070) which are funds received from companies controlled by a common director.
- f) Included in exploration deposits as at December 31, 2008 is \$nil (December 31, 2007-\$249,450) are funds received to be applied to future exploration services from a company controlled by a common director.
- g) Included in share subscription receivable as at December 31, 2008 is \$nil (December 31, 2007-\$35,500) due from an officer.

**12 Contingent Liabilities:**

The Company's mineral properties are affected by the laws and regulations concerning environmental protection that exist in the various jurisdictions. It is not possible to estimate the future impact on operating results, if any, as a result of, future changes in regulations or developments.

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**13 Segmented Information:**

The Company has one reportable operating segment, being the acquisition and exploration and future development of mineral properties.

The Company's mineral properties and deferred costs by geographic location are as follows:

	2008	2007
Mineral properties:		
Canada	\$ 2,771,929	\$ 1,192,887
USA	281,815	269,428
Mexico	9,119,904	3,314,340
	\$ 12,173,648	\$ 4,776,655

**14 Commitments:**

During the year, the company entered into a contract for office rent which expires July 2012. The following table summarizes the company's total annual obligations under this agreement:

2009	\$	48,441
2010		49,497
2011		50,554
2012		25,277
		\$ 173,769

See Note 11 for commitments with related parties.

**15 Financial instruments and financial risk management:**

The Company's financial instruments include cash, accounts receivable, share subscriptions receivable, exploration deposits and advances, marketable securities, accounts payable and accrued liabilities. The carrying values of these financial instruments approximate their fair values due to their relatively short periods to maturity.

The Company's risk management policies are established to identify and analyze the risks faced by the Company, to set appropriate risk limits and controls, and to monitor risks and adherence to market conditions and the Company's activities. The Company has exposure to credit risk, liquidity risk and market risk as a result of its use of financial instruments.

This note presents information about the Company's exposure to each of the above risks and the Company's objectives, policies and processes for measuring and managing these risks. Further quantitative disclosures are included throughout these financial statements. The Board of Directors has overall responsibility for the establishment and oversight of the Company's risk management framework. The Board has implemented and monitors compliance with risk management policies.

(a) Credit risk:

Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its contractual obligations. The Company's accounts receivable relates to receivables from exploration partners who are earning a right to the Company's property via earn-in option agreements, Goods and Services Tax input tax credits and IVA credits (Mexican Value added Tax refunds) from the Mexican Government. Accordingly, the Company views credit risk on accounts receivable as minimal, being the refund of tax credits in Canada and Mexico to moderate being receivables from exploration partners.

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**15 Financial instruments and financial risk management (continued):**

(b) Liquidity risk:

Liquidity risk is the risk that the Company will incur difficulties meeting its financial obligations as they are due. The Company's approach to managing liquidity is to ensure, as far as possible, that it will have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions without incurring unacceptable losses or risking harm to the Company's reputation.

The Company prepares annual expenditure budgets, which are regularly monitored and updated as considered necessary. To facilitate its expenditure program, the Company raises funds through private equity placements. The Company anticipates it will have adequate liquidity to fund its financial liabilities through future equity contributions.

As at December 31, 2008, the Company's financial liabilities were comprised of accounts payable accrued liabilities and investor deposits which have a maturity of less than one year.

(c) Market risk:

Market risk consists of currency risk, commodity price risk and interest rate risk. The objective of market risk management is to manage and control market risk exposures within acceptable limits while maximizing returns.

(i) Currency risk:

Foreign currency exchange rate risk is the risk that the fair value or future cash flows will fluctuate as a result of changes in foreign exchange rates. Although the Company is considered to be in the exploration stage and has not yet developed commercial mineral interests, the underlying market prices in Canada for minerals are impacted by changes in the exchange rate between the Canadian, the United States dollar and the Mexican Peso. The Company's transactions are denominated in Canadian dollars, United States dollars and the Mexican Peso, the Company has not entered into any arrangements to hedge currency risk but does maintain cash balances within each currency with a predominate balance held in Canadian Dollars. Canadian dollars are exchanged when needed to meet foreign denominated liabilities.

(ii) Commodity price risk:

Commodity price risk is the risk that the fair value or future cash flows will fluctuate as a result of changes in commodity prices. Commodity prices for minerals are impacted by world economic events that dictate the levels of supply and demand as well as the relationship between the Canadian and United States dollar, as outlined above. As the Company has not yet developed commercial mineral interests, it is not exposed to commodity price risk at this time.

(iii) Interest rate risk:

Interest rate risk is the risk that future cash flows will fluctuate as a result of changes in market interest rates. The risk that the Company will realize a loss as a result of a decline in the fair value of cash and cash equivalents is limited because of their short-term investment nature. A variable rate of interest is earned on cash and cash equivalents, changes in market interest rates at the year end would not have a material impact on the Company's financial statements.

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**16. Capital management:**

The Company's objectives when managing capital are to safeguard the Company's ability to continue as a going concern and to maintain a flexible capital structure which will allow it to pursue the development of its mineral properties. Therefore, the Company monitors the level of risk incurred in its mineral property expenditures relative to its capital structure.

The Company considers its capital structure to include working capital and shareholders' equity. The Company monitors its capital structure and makes adjustments in light of changes in economic conditions and the risk characteristics of the underlying assets. In order to facilitate the management of capital and the development of its mineral properties, the Company prepares annual expenditure budgets which are regularly monitored and updated as considered necessary.

To maintain or adjust the capital structure, the Company may issue new equity if available on favourable terms, option its mineral properties for cash and/or expenditure commitments from optionees, enter into joint venture arrangements, or dispose of mineral properties.

The Company's investment policy is to hold cash in interest bearing bank accounts and highly liquid short-term interest bearing investments with maturities of one year or less which can be liquidated at any time without penalties.

The Company is not subject to externally imposed capital requirements. There has been no change in the Company's approach to capital management during the year ended December 31, 2008.

**17 Comparative Figures:**

Certain of the comparative figures have been reclassified to conform to the presentation adopted in the current period.