

GOLD RESERVE INC  
Form 10-Q  
August 11, 2010

**United States**  
**SECURITIES AND EXCHANGE COMMISSION**  
**Washington, D.C. 20549**

**FORM 10-Q**

**(Mark One)**

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

**For the quarterly period ended June 30, 2010**

**OR**

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

**For the transition period from \_\_\_\_\_ to \_\_\_\_\_**

Commission file number: **001-31819**

**GOLD RESERVE INC.**

(Exact name of Registrant as specified in its charter)

**Yukon Territory, Canada**

**NA**

(Jurisdiction of incorporation or organization  
Identification No.)

(I.R.S. Employer

**926 West Sprague Avenue, Suite 200, Spokane, Washington**

**99201**

(Address of principal executive offices)

Zip Code

**(509) 623-1500**

(Registrant's Telephone, including area code)

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Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.  Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See definitions of “large accelerated filer,” “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act. Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).  Yes  No

As of August 11, 2010, 57,798,163 Class A common shares, no par value per share, and 961 Class B common shares, no par value per share, were issued and outstanding.

**Item 1. Financial Statements**  
**(Unaudited)**

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**CONSOLIDATED BALANCE SHEETS****June 30, 2010 (unaudited)**

	<b>June 30,</b>	<b>December 31,</b>
<b>U.S. Dollars</b>		<b>2010</b>
<b>2009</b>		
<b>ASSETS</b>		
<b>Current Assets:</b>		
Cash and cash equivalents (Note 4) 60,962,813		\$ 59,298,629 \$
Marketable debt securities (Note 5) 10,175,020		10,080,457
Marketable equity securities (Note 6) 598,825		1,376,945
Deposits, advances and other 566,483		775,979
Total current assets 72,303,141		71,532,010
Property, plant and equipment, net (Note 9) 38,122,102		30,063,783
Restricted cash (Note 13) 9,489,777		8,995,701
Total assets 119,915,020		\$ 110,591,494 \$
<b>LIABILITIES</b>		
<b>Current Liabilities:</b>		
Accounts payable and accrued expenses 3,790,003		\$ 1,845,903 \$
Accrued interest 234,550		234,550
Total current liabilities 4,024,553		2,080,453

June 30, 2010 (unaudited)

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Convertible notes (Note 16) 93,693,168	95,286,586	
Other 2,279,699	2,266,743	
Total liabilities 99,997,420	99,633,782	
Measurement uncertainty (Note 1)		
Commitments and contingencies (Notes 11, 13)		
<b>SHAREHOLDERS' EQUITY</b>		
Serial preferred stock, without par value, none issued		
Common shares and equity units, without par value (Note 15) 247,905,231	248,212,543	
Equity component of convertible notes (Note 16) 28,652,785	28,652,785	
Less common shares held by affiliates (636,267)	(636,267)	
Stock options (Note 11) 10,014,136	10,067,220	
Accumulated deficit (265,630,369)	(275,341,372)	
Accumulated other comprehensive income (loss) (277,225)	113,494	
KSOP debt (Note 10) (110,691)	(110,691)	
Total shareholders' equity 19,917,600	10,957,712	
Total liabilities and shareholders' equity 119,915,020	\$ 110,591,494	\$

Current Liabilities:

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

**Approved by the Board of Directors:**

**s/ Chris D. Mikkelsen**

**s/**

**Patrick D. McChesney**

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# CONSOLIDATED STATEMENTS OF OPERATIONS

For the Three and Six Months Ended June 30, 2010 and 2009 (unaudited)

	<u>Three Months Ended</u>		<u>Six Months Ended</u>	
U.S. Dollars 2009	2010	2009	2010	
<b>OTHER INCOME</b>				
Interest 147,252	\$ 64,018	\$ 67,310	\$ 128,537	\$
Gain on extinguishment of debt 601,936				
Gain on disposition of marketable securities 1,853,983		1,853,983	106,551	
Gain on sale of equipment 370,044	314,170			
Foreign currency gain (loss) 144,286 (50,921)	62,042	(28,971)		
	440,230	1,892,322	749,418	
2,552,250				
<b>EXPENSES</b>				
Corporate general and administrative 2,520,968	808,080	1,332,625	1,781,517	
Venezuelan expenses 1,466,821	426,534	684,351	876,651	
Equipment holding costs 478,989 62,958	138,235	27,500		
Corporate communications 404,451	132,177	210,182	262,291	
Legal and accounting 1,069,939	164,511	282,870	291,662	
Arbitration (Note 3) 2,423,938	1,344,669			



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Takeover defense (Note 17)		(94,457)	
1,359,198			
	3,014,206	2,443,071	6,115,048
6,884,335			
Loss before interest expense			
and income tax	(2,573,976)	(550,749)	(5,365,630)
(4,332,085)			
Interest expense	(2,208,138)		
(4,408,015)			
Loss before income tax	(4,782,114)	(550,749)	(9,773,645)
(4,332,085)			
Income tax benefit (expense)	60,948	(236,807)	62,642
(166,677)			
Net loss for the period	\$ (4,721,166)	\$ (787,556)	\$ (9,711,003)
\$(4,498,762)			
Net loss per share, basic and diluted	\$ (0.08)	\$ (0.01)	\$ (0.17)
\$ (0.08)			
Weighted average common			
shares outstanding	57,763,646	57,421,516	57,647,029
57,191,673			

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

## CONSOLIDATED STATEMENTS OF DEFICIT

For the Six Months Ended June 30, 2010 and 2009 *(unaudited)*

### U.S. Dollars

Deficit, December 31, 2009 (265,630,369)	\$
Net loss for the period (9,711,003)	
Deficit, June 30, 2010 (275,341,372)	\$
Deficit, December 31, 2008 (100,180,541)	\$
Net loss for the period (4,498,762)	
Deficit, June 30, 2009 (104,679,303)	\$

## CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS

For the Three and Six Months Ended June 30, 2010 and 2009 *(unaudited)*

U.S. Dollars	<u>Three Months Ended</u>		<u>Six Months Ended</u>	
	2010	2009	2010	2009

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Net loss for the period (4,498,762)	\$ (4,721,166)	\$ (787,556)	\$ (9,711,003)	\$
Other comprehensive income, net of tax:				
Unrealized gain on marketable securities 951,422	275,508	816,597	497,270	
Adjustment for realized gains included in net loss (1,853,983)		(1,853,983)	(106,551)	
Other comprehensive income (loss) (902,561)	275,508	(1,037,386)	390,719	
Comprehensive loss for the period (5,401,323)	\$ (4,445,658)	\$ (1,824,942)	\$ (9,320,284)	\$

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

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# CONSOLIDATED STATEMENTS OF CASH FLOWS

For the Three and Six Months Ended June 30, 2010 and 2009 (unaudited)

<u>Ended</u>	<u>Three Months Ended</u>		<u>Six Months</u>	
U.S. Dollars 2009	2010	2009	2010	
<b>Cash Flows from Operating Activities:</b>				
Net loss for the period (4,498,762)	\$ (4,721,166)	\$ (787,556)	\$ (9,711,003)	\$
Adjustments to reconcile net loss to net cash used by operating activities:				
Stock option compensation 81,172      384,742	10,573	199,906		
Depreciation 75,719      108,047	35,576	53,954		
Gain on extinguishment of debt (601,936)				
Gain on sale of equipment (370,044)	(314,170)			
Amortization of premium on marketable debt securities 94,563      13,584	47,543	13,584		
Accretion of convertible notes 1,593,418	800,839			
Foreign currency loss 108,078		35,586		
Other (12,956)      (4,964)	(7,700)	(7,645)		
Net gain on disposition of marketable securities (1,853,983)		(1,853,983)	(106,551)	

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Future income tax (benefit) expense (58,466)      169,815	(58,466)	239,270	
Shares issued for compensation 238,140      392,025	181,140		
Changes in non-cash working capital:			
Net decrease (increase) in deposits and advances (209,496)      (207,288)	140,714	413,623	
Net decrease in accounts payable and accrued expenses (3,706,225)	(2,383,306)	(1,702,128)	(1,944,100)
Net cash used in operating activities (9,696,867)	(6,268,423)	(3,395,389)	(10,329,604)
<b>Cash Flows from Investing Activities:</b>			
Proceeds from disposition of marketable securities 609,592      3,074,279		2,574,279	
Purchase of marketable securities (13,420,028)	(410,441)	(12,920,028)	(831,976)
Purchase of property, plant and equipment (5,755,898)		(2,851,248)	(498,440)
Proceeds from sales of equipment 8,851,084	4,985,443		
Decrease in restricted cash 494,076      748,808		748,808	
Interest paid on convertible notes (2,828,841)		(2,828,841)	
Other (28,469)		2,896	
Net cash provided by (used in) investing activities (18,210,149)	4,575,002	(15,274,134)	8,624,336
<b>Cash Flows from Financing Activities:</b>			
Net proceeds from the issuance of common shares 41,084	8,700		

Cash Flows from Operating Activities:

Extinguishment of convertible notes  
(415,254)

Net cash provided by (used in) financing activities 8,700  
41,084 (415,254)

**Change in Cash and Cash Equivalents:**

Net decrease in cash and cash equivalents (1,684,721) (18,669,523)  
(1,664,184) (28,322,270)

Cash and cash equivalents - beginning of period 60,983,350 81,897,420 60,962,813  
91,550,167

Cash and cash equivalents - end of period \$ 59,298,629 \$ 63,227,897 \$ 59,298,629  
\$ 63,227,897

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

## 1. The Company and Significant Accounting Policies

**The Company.** Gold Reserve Inc. (the “Company”) is an exploration stage company incorporated in 1998 under the laws of the Yukon Territory, Canada, and is the successor issuer to Gold Reserve Corporation which was incorporated in 1956. The Company is engaged in the business of acquiring, exploring and developing mining projects. From 1992 to 2009 the Company focused substantially all of its management and financial resources on the development of the Brisas gold and copper project located in the Kilometre 88 mining district of the State of Bolivar in south-eastern Venezuela (which we refer to as the “Brisas Project” or “Brisas”). As further detailed in Note 3, we discontinued development of the Brisas Project after it was expropriated by the Venezuelan government and while we are pursuing our arbitration claim we are also seeking to invest in or acquire alternative mining projects. The Company has no revenue producing mining operations at this time. All amounts shown herein are expressed in U.S. dollars unless otherwise noted. The expense categories shown in the consolidated statements of operations have been revised on a comparative basis to better present the current operations of the Company. The revisions had no effect on previously reported results of operations.

In February 1999, the shareholders of Gold Reserve Corporation approved a plan of reorganization whereby Gold Reserve Corporation became a subsidiary of Gold Reserve Inc., the successor issuer (the “Reorganization”). Generally, each shareholder of Gold Reserve Corporation received one Gold Reserve Inc. Class A common share for each common share owned of Gold Reserve Corporation.

Certain U.S. holders of Gold Reserve Corporation elected, for tax reasons, to receive equity units in lieu of Gold Reserve Inc. Class A common shares. An equity unit is comprised of one Gold Reserve Inc. Class B common share and one Gold Reserve Corporation Class B common share. Each equity unit is substantially equivalent to a Class A common share and is immediately convertible into a Gold Reserve Inc. Class A common share, upon compliance with certain procedures. Equity units are not listed for trading on any stock exchange, but, subject to compliance with applicable federal, provincial and state securities laws, may be transferred. Unless otherwise noted, general references to common shares of the Company include Class A common shares and Class B common shares as a combined group.

**Principles of Consolidation.** The consolidated financial statements contained herein have been prepared in accordance with accounting principles generally accepted in Canada, which as described in Note 18, differ in certain material respects from accounting principles generally accepted in the U.S.

These consolidated financial statements include the accounts of the Company, Gold Reserve Corporation, two domestic subsidiaries, Great Basin Energies, Inc. (“Great Basin”) and MGC Ventures Inc. (“MGC Ventures”), four Venezuelan subsidiaries, two Barbadian subsidiaries and one Aruban subsidiary which were formed to hold the Company’s interest in its foreign subsidiaries or for future transactions. All subsidiaries are wholly owned with the exception of Great Basin and MGC Ventures which are 45% and 44% owned, respectively. All intercompany accounts and transactions have been eliminated on consolidation. The Company’s policy is to consolidate those subsidiaries where control exists. See Note 12.

**Cash and Cash Equivalents.** The Company considers short-term, highly liquid investments purchased with an original maturity of three months or less to be cash equivalents for purposes of reporting cash equivalents and cash flows. Cash and cash equivalents are designated as held-for-trading and recorded at fair value. The Company manages the exposure of its cash and cash equivalents to credit risk by diversifying its holdings into major Canadian and U.S. financial institutions and corporations

**Exploration and Development Costs.** Exploration costs incurred in locating areas of potential mineralization are expensed as incurred. Exploration costs of properties or working interests with specific areas of potential mineralization are capitalized at cost pending the determination of a property’s economic viability. Development costs of proven mining properties not yet producing are capitalized at cost and classified as capitalized exploration costs under property, plant and equipment. Costs related to staffing and maintenance of offices and facilities in Venezuela

are charged to operations. Property holding costs are charged to operations during the period if no significant exploration or development activities are being conducted on the related properties. Upon commencement of production, capitalized exploration and development costs would be amortized based on the estimated proven and probable reserves benefited. Properties determined to be impaired or that are abandoned are written-down to the estimated fair value. Carrying values do not necessarily reflect present or future values.

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**Property, Plant and Equipment.** Property, plant and equipment are recorded at cost less accumulated depreciation. Replacements and major improvements are capitalized. Maintenance and repairs are charged to expense as incurred. The cost and accumulated depreciation of assets retired or sold are removed from the accounts and any resulting gain or loss is reflected in operations. Depreciation is provided using straight-line and accelerated methods over the lesser of the useful life or lease term of the related asset. Interest and financing costs incurred during the construction and development of qualifying assets are capitalized on an interest avoidance basis. The amount capitalized during an accounting period is determined by applying an interest rate to the average amount of accumulated qualifying assets during the period. Adjustments increasing the carrying value of convertible notes upon remeasurement due to a change in estimated life are considered interest costs and are therefore eligible for capitalization. The Company's qualifying assets include its costs of developing mining properties and constructing new facilities.

**Impairment of Long Lived Assets.** The Company reviews long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of the assets may not be recoverable. If the sum of the expected future net cash flows to be generated from the use or disposition of a long-lived asset (undiscounted and without interest charges) is less than the carrying amount of the asset, an impairment loss is recognized and the asset is written down to fair value. Fair value is generally determined by discounting estimated cash flows, using quoted market prices where available or making estimates based on the best information available.

**Foreign Currency.** The U.S. dollar is the Company's functional currency. The Company's foreign subsidiaries are integrated foreign operations and accordingly foreign currency amounts are translated into U.S. dollars using the temporal method. Non-monetary assets and liabilities are translated at historical rates, monetary assets and liabilities are translated at current rates and revenue and expense items are translated at average exchange rates during the reporting period, except for depreciation which is translated at historical rates. Translation gains and losses are included in operating expenses. Since the Company has discontinued development of the Brisas project, the financial statement impact of transactions in the Venezuelan currency is expected to be reduced in the future.

**Stock Based Compensation.** The Company uses the fair value method of accounting for stock options. The fair value of options granted to employees is computed using the Black-Scholes method as described in Note 11 and is expensed over the vesting period of the option. For non-employees, the fair value of stock based compensation is recorded as an expense over the vesting period or, if earlier, upon completion of performance. Consideration paid for shares on exercise of share options, in addition to the fair value attributable to stock options granted, is credited to capital stock. Fair value of restricted stock issued as compensation is based on the grant date market value and expensed over the vesting period. The Company also maintains the Gold Reserve Director and Employee Retention Plan. Units granted under the plan become fully vested and payable upon a change of control. Each Unit granted to a participant entitles such person to receive a cash payment equal to the fair market value of one Gold Reserve Class A Common Share (1) on the date the Unit was granted or (2) on the date any such participant becomes entitled to payment, whichever is greater.

**Income Taxes.** The Company uses the liability method of accounting for income taxes. Future tax assets and liabilities are determined based on the differences between the tax basis of assets and liabilities and those amounts reported in the financial statements. The future tax assets or liabilities are calculated using the substantively enacted tax rates expected to apply in the periods in which the differences are expected to be settled. Future tax assets are recognized to the extent that they are considered more likely than not to be realized.

**Use of Estimates.** The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

**Measurement Uncertainty.** Any operations we may have are subject to the effects of changes in legal, tax and regulatory regimes, political, labor and economic developments, social and political unrest, currency and exchange

controls, import/export restrictions and government bureaucracy in the countries in which we may operate. In 2009, subsequent to the expropriation and the resulting loss of control and physical access to the Brisas project, we recorded a \$150.7 million non-cash write-off of the carrying value of the expropriated assets including an adjustment for the estimated net realizable value of certain processing and related equipment purchased for the Brisas Project of approximately \$14.5 million. The realizable value of the remaining processing and related equipment may be different than management's current estimate. See Notes 3, 9 and 13. The Company operates and files tax returns in a number of jurisdictions. The preparation of such tax filings requires considerable judgment and the use of assumptions. Accordingly, the amounts reported could vary in the future.

**Net Loss Per Share.** Net loss per share is computed by dividing net loss by the combined weighted average number of Class A and B common shares outstanding during each year, which is reduced by the common shares owned by Great Basin and MGC Ventures. In periods in which a loss is incurred, the effect of potential issuances of shares under options and convertible notes would be anti-dilutive, and therefore basic and diluted losses per share are the same.

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**Asset Retirement Obligations.** The fair value of a liability for an asset retirement obligation is recognized in the period in which it is incurred if a reasonable estimate of fair value can be made. The associated asset retirement costs are capitalized as part of the carrying amount of the long-lived asset and amortized over the same period as the underlying asset.

**Convertible Notes.** Convertible notes are initially recorded at fair value and subsequently measured at amortized cost. The fair value is allocated between the equity and debt component parts based on their respective fair values at the time of issuance and recorded net of transaction costs. The equity portion of the notes is estimated using the residual value method. The fair value of the debt component is accreted to the face value of the notes using the effective interest rate method over the expected life of the notes, with the resulting charge recorded as interest expense. Interest expense allocable to the qualifying cost of developing mining properties and to constructing new facilities is capitalized until assets are ready for their intended use.

**Comprehensive Income.** Comprehensive income includes net income or loss and other comprehensive income. Other comprehensive income may include unrealized gains and losses on available-for-sale securities, gains and losses on certain derivative instruments and foreign currency gains and losses from self sustaining foreign operations. The Company presents comprehensive income and its components in the consolidated statements of comprehensive loss.

**Financial Instruments.** The Company's financial instruments consist of cash and cash equivalents, marketable securities, accounts payable, accrued expenses and convertible notes. Cash and cash equivalents are classified as held for trading and any changes in fair value are charged to the statement of operations. Marketable equity securities are classified as available for sale with any unrealized gain or loss recorded in other comprehensive income. Marketable debt securities are classified as held-to-maturity and are measured at amortized cost using the effective interest rate method. Other financial liabilities are accounted for at cost or amortized cost.

**Disposal of Long-Lived Assets.** Long-Lived assets are classified as held for sale in the period in which certain criteria are met. Assets held for sale are measured at the lower of carrying amount or fair value less cost to sell and are not depreciated as long as they remain classified as held for sale.

## 2. New Accounting Policies

### Future Accounting Policies:

CICA Section 1582, Business Combinations. This Section replaces Section 1581 and applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after January 1, 2011.

CICA Section 1601, Consolidated Financial Statements. This section establishes standards for the preparation of consolidated financial statements and applies to financial reporting periods beginning on or after January 1, 2011. The Company is currently evaluating the impact of this Section on its financial statements.

CICA Section 1602, Non-Controlling Interests. This section establishes standards for accounting for a non-controlling interest in a subsidiary in consolidated financial statements subsequent to a business combination and applies to financial reporting periods beginning on or after January 1, 2011. The Company is currently evaluating the impact of this Section on its financial statements.

## 3. Expropriation of Brisas Project by Venezuelan Government and Arbitration

From 1992 to 2009 we focused substantially all of our management and financial resources on the development of the Brisas gold and copper project located in the Kilometre 88 mining district of the State of Bolivar in south-eastern Venezuela. After approval of the Brisas operating plan and the Environmental and Social Impact Study in 2003 and

2007, respectively, the Ministry of Environment issued in March 2007, the Authorization to Affect for the Brisas Project. In April 2008, the Ministry of Environment revoked the Authorization to Affect without prior notification.

After months of continuous efforts to meet with representatives of the Venezuelan government to resolve the issues related to the revocation of the Authorization to Affect, on April 21, 2009 the Company notified the Venezuelan government of the existence of a dispute under the Agreement between the Government of Canada and the Government of the Republic of Venezuela for the Promotion and Protection of Investments (“Canada – Venezuela Treaty”).

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After additional months of efforts to meet with representatives of the Venezuelan government to resolve the issues related to the revocation of the Authorization to Affect, on October 21, 2009 we filed a Request for Arbitration under the Additional Facility Rules of ICSID, against the Bolivarian Republic of Venezuela ("Respondent"). On October 26, 2009, Venezuelan government personnel arrived at the Brisas Project camp site, claimed ownership of the Brisas Alluvial Concession, seized assets, expelled our personnel and took physical possession of the property. Subsequently, on November 4, 2009, the Venezuelan government notified the Company through the issuance of an Administrative Act, dated October 20, 2009, of its intent to cancel the Company's underlying hard rock concession which was formally cancelled in June 2010. In November 2009 our Request for Arbitration was registered by ICSID (Gold Reserve Inc. v. Bolivarian Republic of Venezuela (ICSID Case No. ARB(AF)/09/1)).

As a result of the expropriation of the Brisas Project by the Venezuelan government we no longer have control or physical access to the project which has caused the Company to discontinue the development of its Venezuelan properties, including Brisas and Choco 5 (which was a grass-roots exploration property also located in the State of Bolivar) and discontinue reporting mineral reserves for Brisas. In 2009 we recorded a \$150.7 million non-cash write-off of the carrying value of the expropriated assets including an adjustment for the estimated net realizable value of certain processing and related equipment purchased for the Brisas Project of approximately \$14.5 million.

The Company is seeking compensation in the arbitration for all of the loss and damage resulting from Venezuela's wrongful conduct which includes the full market value of the legal rights to develop the Brisas Project. Our current arbitration efforts consist of engaging and assisting technical, legal, and financial experts and developing and filing our initial pleadings. The first session was held with the Tribunal on April 23, 2010 with several procedural matters agreed to, including the tentative time schedule for the Arbitration. The filing of our initial written submission, known as the Memorial, is planned for September 2010.

The Canada-Venezuela Treaty requires as a precondition to bringing an arbitration claim under the Treaty that an investor and any enterprise the investor owns directly or indirectly that has suffered losses that form the basis of a claim by the investor to "waive[ ] its right to initiate or continue any other proceedings in relation to the measure that is alleged to be in breach of [the Treaty] before the courts or tribunals of the Contracting Party concerned or in a dispute settlement procedure of any kind." As a result, the Company and its relevant subsidiaries waived their right to commence or continue before Venezuelan courts or tribunals with other legal or administrative challenges to the conduct that forms the basis of the ICSID claim, including the revocation of the Authorization to Affect and the denial of the extension of the Brisas Alluvial and El Pauji Concessions.

#### 4. Cash and Cash Equivalents

		June 30,	
December 31,			
2010	2009		
Bank deposits 53,900,646		\$ 52,118,577	\$
Money market funds 7,062,167		7,180,052	
Total 60,962,813		\$ 59,298,629	\$

The above amounts exclude restricted cash of approximately \$9 million and \$9.5 million as at June 30, 2010 and December 31, 2009, respectively. See Note 13, Commitments. At June 30, 2010 and December 31, 2009, the

Company had approximately \$217,000 and \$59,000 respectively, in Venezuela and banks outside Canada and the U.S.

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**5. Marketable Debt Securities**

December 31,		June 30,	
2010	2009		
Amortized cost		\$ 10,080,457	\$
10,175,020			

The Company's marketable debt securities are classified as held-to-maturity and are measured at amortized cost using the effective interest rate method.

**6. Marketable Equity Securities**

December 31,		June 30,	
2010	2009		
Fair value at beginning of year		\$ 598,825	\$
1,342,760			
Acquisitions		581,977	
2,135,293			
Dispositions, at cost		(253,041)	
(2,102,548)			
Realized (gain) loss on sale		(106,551)	
(2,274,848)			
Unrealized gain (loss)		555,735	
1,498,168			
Fair value at balance sheet date		\$ 1,376,945	\$
598,825			

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The Company's marketable equity securities are classified as available-for-sale and are recorded at quoted market value with gains and losses recorded within other comprehensive income until realized. As of June 30, 2010 and December 31, 2009 marketable securities had a cost basis of \$1,204,985 and \$876,049, respectively.

**7. Financial Instruments**

The fair values as at June 30, 2010 and December 31, 2009 along with the carrying amounts shown on the consolidated balance sheets for each classification of financial instrument are as follows:

<u>2009</u>			<u>June 30, 2010</u>		<u>December 31,</u>	
Carrying	Fair	Classification	Carrying	Fair	Amount	Amount
Value			Amount	Value		
Cash and cash equivalents 60,962,813		held for trading	\$ 59,298,629	\$ 59,298,629	\$ 60,962,813	\$
Restricted cash 9,489,777		held for trading	8,995,701	8,995,701	9,489,777	
Marketable debt securities 10,208,950		held to maturity	10,080,457	10,097,000	10,175,020	
Marketable equity securities 598,825	598,825	available for sale	1,376,945	1,376,945		
Deposits advances and other 566,483	566,483	held to maturity	775,979	775,979		
A/P and accruals 3,790,003	3,790,003	other financial liabilities	1,845,903	1,845,903		
Accrued interest 234,550	234,550	other financial liabilities	234,550	234,550		
Convertible notes 52,540,530		other financial liabilities	95,286,586	63,544,849	93,693,168	

Fair value estimates for marketable securities are made at the balance sheet date by reference to recent market transactions. The convertible notes are not listed on an exchange and the market for them is not active. Fair value estimates for convertible notes are made at the balance sheet date by reference to weighted average transaction prices



over the preceding twelve months.

CICA 3862 establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value into three broad levels: Level 1 inputs are quoted prices in active markets for identical assets or liabilities, Level 2 inputs are inputs other than quoted prices included within Level 1 that are directly or indirectly observable for the asset or liability and Level 3 inputs are unobservable inputs for the asset or liability that reflect the entity's own assumptions.

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	Fair value			
	June 30, 2010	Level 1	Level 2	Level 3
Cash and cash equivalents	\$ 59,298,629	\$ 59,298,629		
Marketable equity securities	1,376,945	1,376,945		
Restricted cash	8,995,701	8,995,701		

	Fair value			
	December 31, 2009	Level 1	Level 2	Level 3
Cash and cash equivalents	\$ 60,962,813	\$ 60,962,813		
Marketable equity securities	598,825	598,825		
Restricted cash	9,489,777	9,489,777		

The Company is exposed to various risks including credit risk, liquidity risk, currency risk and interest rate risk as described below:

a) Credit risk is the risk that a counter party will fail to meet its obligations to the Company. The Company's primary exposure to credit risk is through its cash and cash equivalents, restricted cash and marketable debt securities balances. The Company diversifies its cash holdings into major Canadian and U.S. financial institutions and corporations.

b) Liquidity risk is the risk that an entity will encounter difficulty in meeting its obligations associated with its financial liabilities. The Company manages this risk by maintaining adequate cash balances through equity and debt offerings to meet its current and foreseeable obligations. The following table presents the Company's payments due on accounts payable and accrued expenses and its undiscounted interest and principal payments due on its convertible notes, based on the estimate that the term of the notes will end on June 15, 2012. If the notes were to reach their contractual maturity date of June 15, 2022, additional interest payments would amount to \$56.3 million over the additional ten year term of the notes.

Payments due by Period	
Less than	More Than

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	Total	1 Year	1-3 Years	4-5 Years	5 Years
A/P and accruals	\$ 1,845,903	\$ 1,845,903			
Interest	11,258,390	5,629,195	\$ 5,629,195		
Principal	102,349,000		102,349,000		
Total	\$ 115,453,293	\$ 7,475,098	\$ 107,978,195		

c) The Company is subject to currency risk mainly due to its operations in Venezuela. Transactions denominated in foreign currency are exposed to exchange rate fluctuations which have an impact on the statement of operations. The Company's cash, value added tax and other monetary assets and liabilities that are held in Venezuelan and Canadian currency are subject to fluctuations against the US dollar. A 10% weakening of those currencies against the US dollar would have increased (decreased) the Company's net gain or loss from the translation of foreign currency denominated financial instruments, for the six months ended June 30, 2010 and 2009, by the amounts shown below.

	2010	2009
Venezuelan Bolívar	\$ (492)	\$ 69,580
Canadian dollar	(412)	625
Total	\$ (904)	\$ 70,205

The Company limits the amount of currency held in non-U.S dollar accounts, but does not actively use derivative instruments to limit its exposure to fluctuations in foreign currency rates.

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d) The Company is subject to the risk that changes in market interest rates will cause fluctuations in the fair values of its financial instruments. Cash and cash equivalents earn floating market rates of interest. Other current financial assets and liabilities are generally not exposed to this risk because of their immediate or short-term maturity. The interest rate on the Company's convertible notes is fixed and therefore the interest payments are not subject to changes in market rates of interest.

## 8. Capital Management

The capital structure of the Company consists of common shares and equity units, convertible notes, stock options, accumulated deficit, accumulated other comprehensive income and KSOP debt. The Company's objectives when managing its capital are to:

- a) maintain sufficient liquidity in order to meet financial obligations including the costs of acquiring and developing mining projects and servicing debt;
- b) safeguard the Company's assets and its ability to continue as a going concern and
- c) maintain a capital structure that provides the flexibility to access additional sources of capital with minimal dilution to existing shareholders.

The Company manages its capital consistent with the objectives stated above and makes adjustments to its capital structure based on economic conditions and the risk characteristics of the underlying assets. The Company is in compliance with the covenants of its convertible notes. There were no changes to the Company's capital management during 2010.

## 9. Property, Plant and Equipment

	Cost	Depreciation	Net	Accumulated
<b>June 30, 2010</b>				
<b>United States</b>				
Machinery and equipment deposits			\$ 29,563,378	\$
29,563,378				
Furniture and office equipment			503,787	
(417,111)	86,676			
Leasehold improvements			41,190	
(37,948)	3,242			
			\$ 30,108,355	\$ (455,059)
\$ 29,653,296				
<b>Venezuela</b>				

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Buildings		\$	403,286	\$	(269,818)	
\$ 133,468						
Furniture and office equipment			482,562			
(451,611)	30,951					
Transportation equipment			329,150			
(292,463)	36,687					
Machinery and equipment			497,808			
(288,427)	209,381					
			1,712,806			
(1,302,319)	410,487					
Total		\$	31,821,161	\$	(1,757,378)	\$
30,063,783						

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	Cost	Depreciation	Net	Accumulated	
<b>December 31, 2009</b>					
<b>United States</b>					
Machinery and equipment deposits			\$ 37,491,372	\$	\$
37,491,372					
Furniture and office equipment			506,007		
(399,737)	106,270				
Leasehold improvements			41,190		
(37,022)	4,168				
			\$ 38,038,569	\$	(436,759)
\$ 37,601,810					
<b>Venezuela</b>					
Buildings			\$ 403,286	\$	(254,200)
\$ 149,086					
Furniture and office equipment			482,562		
(439,028)	43,534				
Transportation equipment			480,198		
(361,907)	118,291				
Machinery and equipment			497,808		
(288,427)	209,381				
			1,863,854		
(1,343,562)	520,292				
Total			\$ 39,902,423	\$	(1,780,321)
38,122,102					\$

Machinery and equipment deposits include amounts paid for infrastructure and milling equipment either in the manufacturing stage or being stored by the manufacturer.

#### 10. KSOP Plan

The KSOP Plan, adopted in 1990 for the benefit of employees, is comprised of two parts, (1) a salary reduction component, or 401(k), and (2) an employee share ownership component, or ESOP. Unallocated shares are recorded as

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

a reduction to shareholders' equity. Allocation of common shares or cash contributions to participants' accounts is at the discretion of the Company's board of directors, subject to certain limitations. The value of the shares allocated is recorded in the statement of operations with a reduction of the KSOP debt account. The Company allocated shares or made cash contributions to eligible participants for the Plan years 2010, 2009 and 2008 valued at \$0, \$57,292 and \$269,679, respectively. As of June 30, 2010, 22,246 common shares remain unallocated to plan participants.

## **11. Stock Based Compensation**

The Company has two equity incentive plans; the 1997 Equity Incentive Plan (last amended in March 2006 and last re-approved by the shareholders in June 2009, the "1997 Plan") and the 2008 Venezuelan Equity Incentive Plan (approved by the shareholders in June 2008, the "Venezuelan Plan"). Both plans permit the grants of stock options, stock appreciation rights and restricted stock, or any combination thereof, and each shall be 10% of the Company's outstanding shares, from time to time. The grants will be for terms up to ten years with vesting periods ranging from immediate to up to 3 years.

Subsequent to shareholder approval in June 2008, 1,056,947 options previously granted to Venezuelan employees and consultants under the 1997 Plan were transferred to the Venezuelan Plan. The 1997 Plan remains available for insiders, employees and consultants of the Company.

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Combined share option transactions for the six months ended June 30, 2010 and 2009 are as follows:

2010	2009			
	Weighted	Weighted	Average	Exercise
Average	Shares	Price	Shares	Price
Options outstanding at beginning of period 3.18	4,573,318	\$ 2.67	5,007,931	\$
Options exercised	(141,666)	0.29		
Options expired 4.15	(339,582)	4.70	(382,922)	
Options forfeited 4.83	(101,917)	2.83	(10,000)	
Options granted 0.73			547,500	
Options outstanding at end of period 2.85	3,990,153	2.58	5,162,509	
Options exercisable at end of period 3.74	3,562,364	\$ 2.85	3,693,199	\$
Options available for grant at end of period under 1997 plan	2,552,189		1,610,988	
Options available for grant at end of period under Venezuelan plan	5,165,338		4,860,661	



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	Price Range	Price Range
Exercise price at end of period	\$0.29 - \$ 5.36	\$ 0.29 - \$ 5.36
Exercise price for exercisable shares	\$0.29 - \$ 5.36	\$ 0.29 - \$ 5.36

The following table relates to stock options at June 30, 2010:

Average Exercise Price Price Exercisable Range Options	Number Outstanding	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Weighted Number of Exercisable
\$0.29 - \$0.29 \$0.29	1,130,577	3.43	\$0.29	702,788
\$0.73 - \$1.89 \$1.22	921,250	2.32	\$1.22	921,250
\$3.95 - \$4.19 \$4.12	686,000	1.27	\$4.12	686,000
\$4.22 - \$4.62 \$4.48	398,500	1.11	\$4.48	398,500
\$4.83 - \$4.83 \$4.83	574,826	0.64	\$4.83	574,826
\$5.07 - \$5.36 \$5.19	279,000	1.42	\$5.19	279,000
\$0.29 - \$5.36 \$2.85	3,990,153	2.03	\$2.58	3,562,364

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The Company recorded compensation expense during the six months ended June 30, 2010 and 2009 of \$81,172 and \$384,742, respectively, for stock options granted. During the six months ended June 30, 2010 and 2009, 0 and 547,500 new options were granted, respectively. The fair value of options granted in 2009 was calculated at \$323,449 using the Black-Scholes model based on the following assumptions:

Weighted average risk free interest rate	1.46%
Expected life years	4.6
Expected volatility	120%
Dividend yield	nil

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In addition to the equity incentive plans, the Company also maintains the Gold Reserve Director and Employee Retention Plan. Units granted under the plan become fully vested and payable upon achievement of certain milestones related to the Brisas project or in the event of a change of control. The Company's Board of Directors is currently evaluating modifying the vesting provisions of the units to more adequately reflect the current business objectives of the Company including successful arbitration, settlement of our dispute with Venezuela, reacquiring the rights to the Brisas Project and successful acquisition of a new business opportunity meeting specific parameters. Each Unit granted to a participant entitles such person to receive a cash payment equal to the fair market value of one Gold Reserve Class A Common Share (1) on the date the Unit was granted or (2) on the date any such participant becomes entitled to payment, whichever is greater. As of June 30, 2010 an aggregate of 1,732,500 unvested Units have been granted to directors and executive officers of the Company and 315,000 Units have been granted to other employees. The value of these units, based on the grant date value of the Class A shares, was approximately \$8.9 million

## 12. Related Party Transactions:

**MGC Ventures.** The Chief Executive Officer, President, Vice President-Finance and Vice President-Administration of the Company are also officers and/or directors and shareholders of MGC Ventures. The Company owned 12,062,953 common shares of MGC Ventures at June 30, 2010 and December 31, 2009, which represented 44% of its outstanding shares. The Company believes it has control over MGC Ventures due to the combined shareholdings of the Company and its officers and directors. MGC Ventures owned 258,083 common shares of the Company at June 30, 2010 and December 31, 2009. In addition, MGC Ventures owned 280,000 common shares of Great Basin at June 30, 2010 and December 31, 2009. During the last three years, the Company sublet a portion of its office space to MGC Ventures for \$6,000 per year.

**Great Basin.** The Chief Executive Officer, President, Vice President-Finance and Vice President-Administration of the Company are also officers and/or directors and shareholders of Great Basin. The Company owned 15,661,595 common shares of Great Basin at June 30, 2010 and December 31, 2009, which represented 45% of its outstanding shares. The Company believes it has control over Great Basin due to the combined shareholdings of the Company and its officers and directors. Great Basin owned 491,192 common shares of the Company at June 30, 2010 and December 31, 2009. Great Basin also owned 170,800 common shares of MGC Ventures at June 30, 2010 and December 31, 2009. During the last three years, the Company sublet a portion of its office space to Great Basin for \$6,000 per year.

## 13. Commitments

In mid 2007, we commenced procurement efforts for the Brisas Project and placed orders totaling approximately \$125 million for a gyratory crusher, pebble crushers, SAG and ball mills, mill motors, and other equipment for the Brisas Project. Since the revocation of the Authorization to Affect, the Company has sold certain equipment (one SAG mill, primary crusher, regrind mill, two ball mills (35,000 tonne per day through-put) and related motors as well as mobile equipment) originally costing approximately \$61.4 million. The Company recovered approximately \$35.1 million of progress payments and the purchaser assumed the Company's remaining payment obligations of approximately \$21.9 million resulting in a combined loss on sale of equipment of approximately \$4.4 million. As of June 30, 2010, the Company has equipment commitments totaling \$61.7 million and has made payments on these orders of \$52.7 million. Payments on the remaining commitments of \$9 million are due within one year. In connection with a portion of these commitments, the Company opened an irrevocable standby letter of credit with a Canadian chartered bank providing security on the performance of obligations. As of June 30, 2010 and December 31, 2009, the Company had restricted cash of \$9 million and \$9.5 million, respectively, as required by this letter of credit.

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#### **14. Shareholder Rights Plan**

The Company instituted a shareholder rights plan (the "Rights Plan") in 1999. Since the original approval by the shareholders, the Rights Plan and the Rights Plan agreement have been amended and continued from time to time. In June 2009, the shareholders approved certain amendments to the Rights Plan including continuing the Shareholder Rights Plan until June 30, 2012. In December 2008, the Company's Board of Directors amended the Rights Plan by extending the definition of "Permitted Bid" to include a bid by an entity which has confidential information about the Company that has executed a confidentiality and standstill agreement within three months prior to the commencement of the bid. The Rights Plan is intended to give adequate time for shareholders of the Company to properly assess the merits of a take-over bid without pressure and to allow competing bids to emerge. The Rights Plan is designed to give the Board of Director's time to consider alternatives to allow shareholders to receive full and fair value for their common shares. One right is issued in respect of each outstanding share. The rights become exercisable only when a person, including any party related to it or acting jointly with it, acquires or announces its intention to acquire 20% or more of the Company's outstanding shares without complying with the "permitted bid" provisions of the Rights Plan. Each right would, on exercise, entitle the holder, other than the acquiring person and related persons, to purchase Class A common shares of the Company at a 50% discount to the market price at the time.

#### **15. Common Shares and Equity Units**

During the six months ended June 30, 2010, the Company issued 141,666 shares at an average price of \$0.29 per share upon exercise of stock options and 201,500 shares at an average price of \$1.18 per share as compensation. As of June 30, 2010, there were a total of 58,038,163 Class A and 500,236 Class B shares issued.

During the six months ended June 30, 2009, the Company issued 551,500 shares at an average price of \$0.71 per share as compensation.

#### **16. Convertible Notes**

In May 2007, the Company issued \$103,500,000 aggregate principal amount of its 5.50% Senior subordinated convertible notes. The notes are unsecured, bear interest at a rate of 5.50% annually, pay interest semi-annually in arrears and are due on June 15, 2022. The notes are convertible into Class A common shares of the Company at the initial conversion rate, subject to adjustment, of 132.626 shares per \$1,000 principal amount (equivalent to a conversion price of \$7.54). Upon conversion, the Company will have the option, unless there has occurred and is then continuing an event of default under the Company's indenture, to deliver common shares, cash or a combination of common shares and cash for the notes surrendered.

The note holders have the option to require the Company to repurchase the notes on June 15, 2012, at a price equal to 100% of the principal amount of the notes plus accrued but unpaid interest. The Company may elect to satisfy its obligation to pay the repurchase price, in whole or in part, by delivering Common Shares. In the event of a change of control of the Company, the Company may be required to offer to repurchase the notes at a purchase price equal to 100% of the principal amount of the notes plus accrued but unpaid interest unless there has occurred and is continuing certain events of default under the Company's indenture.

At any time on or after June 16, 2010, and until June 15, 2012, the Company may redeem the notes, in whole or in part, for cash at a redemption price equal to 100% of the principal amount being redeemed plus accrued and unpaid interest if the closing sale price of the Common Shares is equal to or greater than 150% of the conversion price then in effect and the closing price for the Company's Common Shares has remained above that price for at least twenty trading days in the period of thirty trading days preceding the Company's notice of redemption. Beginning on June 16, 2012, the Company may, at its option, redeem all or part of the notes for cash at a redemption price equal to 100% of the principal amount being redeemed plus accrued and unpaid interest.

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The covenants contained in the 5.50% subordinated note indenture are limited to administrative issues such as payments of interest, maintenance of office or agency location, delivery of reports and other related issues. Likewise, events of default are defined as failure to pay interest and principal amounts when due, default in the performance of covenants, failure to convert notes upon holder's exercise of conversion rights and similar provisions or the Company's failure to give notice of a fundamental change which is generally defined as events related to a change of control in the Company.

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Canadian accounting standards require the Company to allocate the notes between their equity and debt component parts based on their respective fair values at the time of issuance. The liability component was computed by discounting the stream of future payments of interest and principal at the prevailing market rate for a similar liability that does not have an associated equity component. The equity portion of the notes was estimated using the residual value method at approximately \$29 million, net of issuance costs. The fair value of the debt component is accreted to the face value of the notes using the effective interest rate method over the expected life of the notes, with the resulting charge recorded as interest expense. The expected life of the notes is an estimate and is subject to change, if warranted by facts and circumstances related to the potential early redemption of the notes by either the Company or the holders. Interest and accretion expense allocable to the qualifying cost of developing mining properties and to constructing new facilities is capitalized until assets are ready for their intended use. The Company capitalized interest and accretion on the notes until October, 2009, when the Company filed for arbitration and when the Venezuelan government expropriated Brisas. Thereafter all interest and accretion on the notes has been expensed.

As of June 30, 2010, convertible notes with a face value of \$1,151,000 had been settled in cash or repurchased by the Company at a total cost of approximately \$451,000.

## **17. Takeover Defense and Related Litigation**

On December 15, 2008, Rusoro Mining Ltd. (“Rusoro”) commenced an unsolicited offer to acquire all of the outstanding shares and equity units of the Company in consideration for three shares of Rusoro for each Company share or equity unit. On December 16, 2008, the Company filed an action in the Ontario Superior Court of Justice against Rusoro and Rusoro’s financial advisor Endeavour Financial International Corporation (“Endeavour”) seeking an injunction restraining Rusoro and Endeavour from proceeding with Rusoro’s unsolicited offer, significant monetary damages, and various other items. Endeavour was the Company’s financial advisor from 2004 until shortly after the commencement of Rusoro’s offer.

On February 10, 2009, the Ontario Superior Court of Justice granted an interlocutory injunction restraining Rusoro from proceeding with any hostile takeover bid to acquire the shares of the Company until the conclusion and disposition at trial of the action commenced by the Company. The injunction was granted by the Court following a motion by the Company on the basis that Rusoro had access to or benefited from the use of the Company’s confidential information as a result of Rusoro’s relationship with Endeavour. The Court also issued an interlocutory injunction restraining Endeavour from having any involvement with a hostile takeover bid for the Company. The Court further required that Rusoro, Endeavour and their agents return to the Company both all the confidential information of the Company and also anything produced from that confidential information and pay the court costs. Following the issuance of the interlocutory injunctions, Rusoro withdrew its unsolicited offer to acquire the outstanding shares and equity units of the Company.

On February 15, 2009, Rusoro and Endeavour both served a motion with the Ontario Superior Court of Justice seeking permission to appeal to the Divisional Court the February 10, 2009 order that was granted against them. The Company opposed these motions which were heard in Toronto on April 2, 2009. On April 6, 2009 the permission to appeal was denied. Rusoro has filed a counterclaim against the Company for, among other things, damages of Cdn \$102.5 million allegedly arising from the Company’s successful motion for an interlocutory injunction. Endeavour has filed a \$0.5 million counter claim against the Company relating to the lost opportunity to earn a success fee from the successful completion of the Rusoro offer. The Company recently added two additional defendants and amended the claim for monetary damages.

## **18. Differences Between Canadian and U.S. GAAP**

The Company prepares its consolidated financial statements in accordance with generally accepted accounting principles (“GAAP”) in Canada, which differ in certain respects from GAAP in the United States. The effect of the principal measurement differences between U.S. and Canadian GAAP are summarized below.

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



**Consolidated Summarized Balance Sheets**

	Canadian GAAP	Change	U.S. GAAP
<b>June 30, 2010</b>			
<b>Assets</b>			
Current assets		\$ 71,532,010	\$
71,532,010			
Property, plant and equipment, net		30,063,783	
30,063,783			
Other assets		8,995,701	
8,995,701			
		\$ 110,591,494	\$
110,591,494			
<b>Liabilities</b>			
Convertible notes <sup>C</sup>		\$ 95,286,586	\$ 4,925,999
100,212,585			
Other liabilities		4,347,196	
4,347,196			
		99,633,782	4,925,999
104,559,781			
<b>Shareholders equity</b>			
Common shares & equity units <sup>B</sup>		248,212,543	(5,698,031)
242,514,512			
Equity component of convertible notes <sup>C</sup>		28,652,785	
(28,652,785)			
Less, common shares & equity units			
held by affiliates		(636,267)	
(636,267)			
Contributed surplus <sup>E</sup>			5,171,603
5,171,603			
Stock options <sup>B</sup>		10,067,220	
4,434,753	14,501,973		

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



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Accumulated deficit <sup>A,B,D</sup> (255,581,377)		(275,341,372)	19,759,995
Accumulated other comprehensive income <sup>A</sup> 58,466	171,960	113,494	
KSOP debt (110,691)		(110,691)	
(4,925,999)	6,031,713	10,957,712	
110,591,494		\$ 110,591,494	\$

	Canadian GAAP	Change	U.S. GAAP
<b>December 31, 2009</b>			
<b>Assets</b>			
Current assets 72,303,141		\$ 72,303,141	\$
Property, plant and equipment, net 38,122,102		38,122,102	
Other assets 9,489,777	9,489,777	9,489,777	
119,915,020		\$ 119,915,020	\$
<b>Liabilities</b>			
Convertible notes <sup>C</sup> 99,741,722		\$ 93,693,168	\$ 6,048,554
Other liabilities 6,304,252	6,304,252	6,304,252	
106,045,974		99,997,420	6,048,554
<b>Shareholders equity</b>			
Common shares & equity units <sup>B</sup> 242,207,200		247,905,231	(5,698,031)

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

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Equity component of convertible notes <sup>C</sup> (28,652,785)		28,652,785	
Less, common shares & equity units			
held by affiliates		(636,267)	
	(636,267)		
Contributed surplus <sup>E</sup>			
5,171,603	5,171,603		
Stock options <sup>B</sup>		10,014,136	
4,434,753	14,448,889		
Accumulated deficit <sup>B,D</sup>		(265,630,369)	18,695,906
(246,934,463)			
Accumulated other comprehensive income		(277,225)	
	(277,225)		
KSOP debt		(110,691)	
	(110,691)		
		19,917,600	
(6,048,554)	13,869,046		
		\$ 119,915,020	\$
119,915,020			\$

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**Consolidated Summarized Statements of Operations**

<u>2010</u>	<u>2009</u>		
Net Loss under Canadian GAAP (4,498,762)		\$ (9,711,003)	\$
Interest expense <sup>D</sup>		1,122,555	
Gain on settlement of debt <sup>C</sup>		(47,429)	
Income tax <sup>A</sup> 169,815		(58,466)	
Net loss under U.S. GAAP (4,376,376)		(8,646,914)	
Other comprehensive income (loss)			
Unrealized gain on available- for-sale securities: <sup>A</sup>			
Holding gain arising during period 555,736	781,607		
Reclassification adjustment for gain included in net loss (1,853,983)		(106,551)	
<b>Total comprehensive loss under</b>			
<b>U.S. GAAP</b> (5,448,752)		\$ (8,197,729)	\$
<b>Basic and diluted net loss per share</b>			
<b>under U.S. GAAP</b> (0.15)	\$ (0.08)	\$	

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

**Consolidated Summarized Statements of Cash Flows**

2010

2009

Cash flow used in operating activities

under Canadian GAAP  
(9,696,867)

\$ (10,329,604)

\$

**Cash flow used in operating activities**

**under U.S. GAAP**

**&**