

Financial Statements of

**ALHAMBRA RESOURCES LTD.**

Years ended December 31, 2009 and 2008

## **MANAGEMENT'S REPORT**

The accompanying consolidated financial statements and all information in the annual report are the responsibility of management.

The financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles. Other financial information appearing throughout the report is presented on a basis consistent with the financial statements.

Alhambra Resources Ltd. has established procedures and systems of internal control designed to provide reasonable assurance that assets are safeguarded and that reliable financial information is produced in a timely manner.

The Audit Committee of the Board of Directors has reviewed these financial statements with management and the independent auditors and reports its findings to the Board of Directors before such statements are approved by the Board of Directors.

The financial statements have been audited by KPMG LLP, the independent auditors, in accordance with Canadian generally accepted auditing standards on behalf of the shareholders. KPMG LLP have full and free access to the Audit Committee. The Audit Committee is responsible for determining their reappointment and the setting of their fees.

April 28, 2010

*(Signed) "John J. Komarnicki"*  
Chairman of the Board and Chief Executive Officer

*(Signed) "Donald D. McKechnie"*  
Vice-President Finance and Chief Financial Officer

## AUDITORS' REPORT

To the Shareholders of  
Alhambra Resources Ltd.

We have audited the consolidated balance sheets of Alhambra Resources Ltd. as at December 31, 2009 and 2008 and the consolidated statements of operations and retained earnings (deficit), comprehensive income (loss), and cash flows for the years then ended. These financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these financial statements based on our audits.

Except as explained in the following paragraph, 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 financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the 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.

As a result of the unfavorable decision reached by a Kazakhstan court, the Corporation's ownership of its Kazakhstan subsidiaries was invalidated effective December 26, 2008. As a result, the Corporation was not granted sufficient access to the accounting records of these subsidiaries. Consequently, we were unable to obtain sufficient appropriate audit evidence for expenses related to the Kazakhstan operations, and income taxes. The Corporation was uncertain if they would be granted access to the accounting records or if the mineral licenses would be returned to the Corporation. Accordingly, we were not able to determine whether any adjustments might be necessary to expenses, income taxes, and net loss from the Kazakhstan operations for the year ended December 31, 2008 as further described in Note 3.

In our opinion, except for the effect of adjustments, if any, which we might have determined to be necessary had we been able to satisfy ourselves with respect to the accounts described in the preceding paragraph, these consolidated financial statements present fairly, in all material respects, the financial position of the Corporation as at December 31, 2009 and 2008 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

The image shows a handwritten signature in dark ink that reads "KPMG LLP". The letters are slightly slanted and have a casual, professional appearance.

Chartered Accountants

Calgary, Canada  
April 28, 2010

# ALHAMBRA RESOURCES LTD.

## Consolidated Balance Sheets

As at December 31, 2009 and 2008  
(Expressed in U.S. Dollars)

	2009	2008
<b>Assets</b>		
Current assets:		
Cash	\$ 343,619	\$ 25,818
Accounts receivable	1,904,000	11,275
Deposits and prepaid expenses	263,821	27,267
Supplies inventory	1,362,058	-
Work in progress (note 4)	9,494,769	-
	<u>13,368,267</u>	<u>64,360</u>
Mineral assets (note 5)	90,457,436	-
Equipment (note 6)	36,767	39,102
Investment (note 7)	561,902	586,068
	<u>\$104,424,372</u>	<u>\$ 689,530</u>
<b>Liabilities and Shareholders' Equity</b>		
Current liabilities:		
Accounts payable and accrued liabilities	\$ 4,474,668	\$ 806,114
Secured debentures (note 8)	968,069	816,593
	<u>5,442,737</u>	<u>1,622,707</u>
Asset retirement obligations (note 10)	175,411	-
Future income taxes (note 11)	30,831,929	-
Shareholders' equity (deficiency):		
Share capital (note 12(b))	35,494,990	34,585,094
Warrants (note 12(c))	50,795	-
Equity portion of convertible debentures (note 12(d))	116,101	-
Contributed surplus (note 12(e))	4,995,418	4,417,966
Accumulated other comprehensive income (loss) (note 13)	178,715	(322,360)
Retained earnings (deficit)	27,138,276	(39,613,877)
	<u>67,974,295</u>	<u>(933,177)</u>
	<u>\$104,424,372</u>	<u>\$ 689,530</u>

Going concern and nature of operation (note 1)  
Commitments and contingencies (note 19)

See accompanying notes to consolidated financial statements.

On behalf of the Board:

(Signed) John J. Komarnicki, Director

(Signed) Clarence K. Wagenaar, Director

# ALHAMBRA RESOURCES LTD.

Consolidated Statements of Operations and Retained Earnings (Deficit)

Years ended December 31, 2009 and 2008  
(Expressed in U.S. Dollars)

	2009	2008
<b>Revenue:</b>		
Sales	\$ 6,160,094	\$ 14,852,032
Less royalty and production taxes		
Net smelter royalty	(184,803)	(445,561)
Mineral extraction tax	(283,934)	-
	5,691,357	14,406,471
Interest and other	-	13,795
	5,691,357	14,420,266
<b>Expenses:</b>		
Operations	3,650,538	9,799,464
General and administrative	1,748,695	4,043,513
Interest and accretion on debt (notes 8 and 9)	501,262	142,336
Stock-based compensation (note 12(e))	573,860	1,181,990
Depreciation, depletion and accretion	264,040	1,636,650
Foreign exchange gain	(356,474)	(286,575)
Equity loss	115,032	104,055
Loss (gain) on write-off (re-acquisition) of investment		
In subsidiary (note 3)	(68,866,350)	30,965,442
	(62,369,397)	47,586,875
Income (loss) before income taxes	68,060,754	(33,166,609)
Income tax expense (reduction) (note 11):		
Current	485,936	-
Future	822,665	507,514
	1,308,601	507,514
Net income (loss)	66,752,153	(33,674,123)
Deficit, beginning of year	(39,613,877)	(5,939,754)
Retained earnings (deficit), end of year	\$27,138,276	\$(39,613,877)
<b>Net income (loss) per share (note 16):</b>		
Basic	\$ 0.87	\$ (0.44)
Diluted	0.81	(0.44)

## Consolidated Statements of Comprehensive Income (Loss)

Years ended December 31, 2009 and 2008  
(Expressed in U.S. Dollars)

	2009	2008
Net income (loss)	\$ 66,752,153	\$(33,674,123)
Translation gain (loss) on self-sustaining operations (note 13)	501,075	(1,282,874)
Total comprehensive income (loss)	\$ 67,253,228	\$(34,956,997)

See accompanying notes to consolidated financial statements.

# ALHAMBRA RESOURCES LTD.

## Consolidated Statements of Cash Flows

Years ended December 31, 2009 and 2008  
(Expressed in U.S. Dollars)

	2009	2008
Cash provided by (used in):		
Operating:		
Net income (loss)	\$ 66,752,153	\$(33,674,123)
Items not involving cash:		
Stock-based compensation	573,860	1,181,990
Accretion on debt	282,063	-
Depreciation, depletion and accretion	264,040	1,636,650
Future income taxes	822,665	507,514
Unrealized foreign exchange gain	(345,340)	(120,087)
Equity loss on investment	115,032	104,055
Gain on re-acquisition (write-off) of investment in subsidiary	(68,866,350)	30,965,442
	(401,877)	601,441
Change in non-cash working capital (note 15)	(751,818)	253,369
	(1,153,695)	854,810
Financing:		
Secured debentures retired	(816,593)	-
Secured debentures issued	1,024,046	936,680
Secured notes issued	545,886	-
Secured notes retired	(630,546)	-
Issuance of common shares and warrants	719,016	108,009
	841,809	1,044,689
Investing:		
Expenditures on mineral assets	(347,682)	(4,616,858)
Acquisition of equipment	(360)	(4,245)
Change in non-cash working capital (note 15)	58,568	(92,875)
	(289,474)	(4,713,978)
Cash acquired in re-acquisition	1,234,898	-
Effect of exchange rate changes on cash and cash equivalents	(315,737)	(216,515)
Change in cash and cash equivalents	317,801	(3,030,994)
Cash and cash equivalents, beginning of year	25,818	3,056,812
Cash, end of year	\$ 343,619	\$ 25,818
Supplemental disclosure of cash flow information:		
Interest paid	\$ 143,976	\$ 101,558
Taxes paid	48,833	256,293

See accompanying notes to consolidated financial statements.

# ALHAMBRA RESOURCES LTD.

Notes to Consolidated Financial Statements

Years ended December 31, 2009 and 2008

(Expressed in U.S. Dollars, unless otherwise stated)

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## 1. Going concern and nature of operations:

### (a) Going concern:

On December 26, 2008, Alhambra Resources Ltd. (“Alhambra” or the “Corporation”) lost ownership of assets that generated cash flow as a result of the unfavorable decision reached in the Kazakhstan Lawsuit (note 3). With the ruling by the Supreme Court of the Republic of Kazakhstan (“Kazakhstan”), Alhambra re-acquired ownership of its Kazakhstan operating subsidiary, Saga Creek Gold Company (“Saga Creek”) effective September 15, 2009. The re-acquisition of Saga Creek once again gave Alhambra ownership of revenue producing assets, which has once again given Alhambra access to cash flow to meet its obligations. This cash flow however is not sufficient to enable Alhambra to meet all its obligations and carry out significant exploration and development programs. Additional financing will be required to enable the Corporation to carry out sufficient exploration and development programs to continue as a going concern. There is no assurance at this time that the Corporation will be able to obtain the necessary financing.

These consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles applicable to a going concern, which assume that the Corporation will continue in operation for the foreseeable future and will be able to realize its assets and discharge its liabilities in the normal course of operations.

If the going concern assumption was not appropriate for these consolidated financial statements, then material adjustments would be necessary to the carrying amounts of the assets and liabilities, the reported revenues and expenses and the balance sheet classifications used.

### (b) Nature of operations:

The business of Alhambra consists of the exploration for and development of mineral properties in the Kazakhstan. In addition to its exploration and development activity, Alhambra also produces gold from a pilot project on a portion of its Kazakhstan license that commenced production on May 1, 2006. The Corporation’s operations are subject to economic, political and social risks inherent in doing business in Kazakhstan. These risks include matters arising out of the policies of the government, economic conditions, imposition of or changes to taxes and regulations, foreign currency exchange fluctuation and the enforceability of contract rights.

As a result of the unfavorable decision reached in the Kazakhstan Lawsuit (note 3), Alhambra’s interest in mineral licenses held by its former Kazakhstan subsidiaries had been invalidated and the ownership was re-registered in the name of the former owners. With the loss of the Kazakhstan subsidiaries effective December 26, 2008, Alhambra no longer had any operations in Kazakhstan and as such took a \$30,965,442 write-off of its investment in its Kazakhstan subsidiaries.

# ALHAMBRA RESOURCES LTD.

Notes to Consolidated Financial Statements, page 2

Years ended December 31, 2009 and 2008

(Expressed in U.S. Dollars, unless otherwise stated)

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The decision by the Supreme Court to reverse the decisions of the lower courts in Kazakhstan enabled the ownership of the shares of the Kazakhstan subsidiaries to be re-registered in the name of the Corporation (note 3). Alhambra has accounted for the re-registration of the ownership of the shares of the Kazakhstan subsidiaries as a purchase according to Handbook Section 1582, Business Combinations (note 3). Operations commenced on September 15, 2009 upon re-acquisition.

(c) Basis of presentation:

The consolidated financial statements of the Corporation have been prepared by management in accordance with accounting principles generally accepted in Canada. In these consolidated financial statements, unless otherwise indicated, all dollar amounts are expressed in United States dollars.

## 2. Significant accounting policies:

(a) Principles of consolidation and accounting for investments:

The consolidated financial statements include the accounts of the Corporation and its wholly-owned subsidiaries, Alhambra Overseas Limited, Alhambra Cooperatief U.A., Saga Creek and Goodwin Golems LLP ("Goodwin"). For 2009, the accounts for Saga Creek and Goodwin have been included from September 15, 2009 being the effective date of the re-acquisition (note 3). The Corporation accounts for its investment in DOT Resources Ltd. ("DOT") using the equity method of accounting (note 7).

(b) Use of estimates:

The preparation of the consolidated financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities as at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results may differ from those reported. Significant areas requiring the use of management estimates include the determination of fair values on business combinations, impairment of mining assets, equipment and exploration and development costs, asset retirement obligations, and assumptions used in calculating stock-based compensation expense. These estimates are reviewed periodically and, as adjustments become necessary, they are reported in earnings in the periods in which they become known.

(c) Translation of foreign currencies:

The accounts of the self-sustaining Canadian and Kazakhstan operations are translated using the current rate method, whereby assets and liabilities are translated at year end exchange rates, while revenues and expenses are translated using average annual rates. Translation gains and losses relating to the self-sustaining Canadian and Kazakhstan operations are included as a separate component of shareholders' equity in accumulated other comprehensive income.



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Notes to Consolidated Financial Statements, page 3

Years ended December 31, 2009 and 2008

(Expressed in U.S. Dollars, unless otherwise stated)

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(d) Cash and cash equivalents:

Cash and cash equivalents consist of bank balances and term deposits with original maturities of three months or less.

(e) Supplies inventory:

Inventory of materials and supplies is valued at the lower of cost and net realizable value.

(f) Work in progress:

All costs associated with the production of gold, including direct costs incurred in the mining, leaching and resin stripping processes as well as depreciation of equipment used in each process and depletion of mineral assets, are charged to work in progress and expensed based on the quantity of gold sold as a percentage of total gold mined. Work in progress is valued at the lower of cost and net realizable value and on a weighted average basis. The portion of work in progress that is not expected to be recovered within the next year is classified as mineral assets.

(g) Mineral assets:

Mineral assets include exploration costs, equipment, construction in progress, the fair value of the Uzboy Project (note 3), and the portion of work in progress not expected to be recovered within the next year. The amount shown for exploration costs includes the direct costs of acquiring, maintaining, exploring properties, an allocation of management fees and salaries based on time spent and other costs directly related to specific properties. Depreciation on equipment utilized in the development of mineral properties is capitalized to exploration and development costs until such time these properties commence commercial production. All other costs, including administrative overhead, are expensed as incurred. Revenues from the sale of minerals are credited to exploration and development costs until such time as these properties are considered to have commenced commercial production.

The Corporation reviews and evaluates its mining properties for impairment at least annually or when events or changes in circumstances indicate that the related carrying amounts may not be recoverable. A decision to abandon, reduce or expand activity on a specific project is based upon many factors including general and specific assessments of exploration results, anticipated future mineral prices, anticipated costs of developing and operating a producing mine and the general likelihood that the Corporation will continue exploration on the project. The Corporation does not set a pre-determined holding period for properties. However, properties which have not demonstrated positive exploration results at the conclusion of each phase of an exploration program are re-evaluated to determine if future exploration is warranted and that carrying amounts are appropriate.

Impairment is considered to exist if the total estimated future undiscounted cash flows are less than the carrying amount of the assets. An impairment loss is measured and recorded based on discounted estimated future cash flows. Future cash flows are estimated based on expected future production, commodity prices, operating costs, capital costs and reclamation and remediation obligations. Expected future production is determined from proved and

# ALHAMBRA RESOURCES LTD.

Notes to Consolidated Financial Statements, page 4

Years ended December 31, 2009 and 2008

(Expressed in U.S. Dollars, unless otherwise stated)

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probable reserves and measured mineral resources after taking into account losses during processing and treatment.

If a mineral property is abandoned or it is determined that its carrying amount cannot be supported by future production or sales, the related costs are charged against operations in the year of abandonment or determination of impairment of value. The amounts recorded as exploration and development costs do not necessarily reflect present or future values.

Once a mineral property reaches commercial production, the accumulated costs of exploration and development costs related to that mineral property are amortized to operations on a unit-of-production basis over economically recoverable gross proved plus probable reserves as determined by the Corporation's independent geological and engineering consultant.

(h) Equipment:

Equipment consists of office equipment in the Corporation's head office. Office equipment is depreciated using the declining balance method at annual rates from 20% to 30%.

(i) Asset retirement obligations ("ARO"):

The Corporation recognizes the fair value of ARO in the period in which it is incurred when a reasonable estimate of the fair value can be made. The fair value of the estimated ARO is recorded as a liability, with a corresponding increase in the carrying amount of the related asset. The capitalized amount is depleted on the unit-of-production method over proved and probable reserves. The liability amount is increased each reporting period due to the passage of time and the amount of accretion is expensed to income in the period. Actual costs incurred upon the settlement of the ARO are charged against the ARO to the extent recorded. Any difference between the actual costs incurred and the ARO recorded is recognized as a gain or loss in earnings in the period the costs are incurred.

(i) Revenue recognition:

Revenue is recognized from the sale of gold when the price is determinable, the product has been delivered and title has been transferred to the customer and collection of the sales price is reasonably assured.

(k) Stock-based compensation:

The Corporation has a stock-based compensation plan for employees and non-employees as described in note 12(e). The Corporation uses the fair value method of accounting for stock options granted. The fair value of employee stock options is estimated on the date of grant and the resulting fair value is recorded as an expense over the vesting period of the stock option. The fair value of non-employee stock options is revalued each reporting date with the change in fair value of the unvested options expensed over the remaining vesting period. In determining the fair value of the stock options granted, the Black-Scholes model is used and assumptions regarding interest rates, underlying volatility of the Corporation's stock and expected life of the options are made.

# ALHAMBRA RESOURCES LTD.

Notes to Consolidated Financial Statements, page 5

Years ended December 31, 2009 and 2008

(Expressed in U.S. Dollars, unless otherwise stated)

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(l) Income taxes:

The Corporation uses the asset and liability method of accounting for income taxes. 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 basis. Future tax assets and liabilities are measured using enacted or substantively enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on future tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the date of enactment or substantive enactment. A valuation allowance is recorded against any future income tax assets if it is more likely than not that the asset will not be realized.

(m) Loss per share:

Basic per share amounts are calculated using the weighted average common shares outstanding during the year. Diluted per share amounts are calculated using the treasury stock method, whereby it is assumed that proceeds from the exercise of stock options and warrants are used by the Corporation to repurchase Corporation shares at the weighted average market price during the year. Anti-dilutive options and warrants are not included in the calculation. The dilutive effect of the Corporation's convertible debt is calculated by applying the "if-converted" method, which assumes that the securities are converted at the beginning of the period or the time of issuance, if later, and that income items are adjusted to net earnings.

(n) Financial instruments:

The Corporation's financial instruments consist of cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities and secured debentures.

Financial instruments are measured at fair value on initial recording except in specific circumstances. Changes in fair value in subsequent periods depend on whether the financial instrument has been classified as: "held for trading", "held to maturity", "loans and receivables", "available for sale" or "other financial liabilities". "Held for trading" financial assets and financial liabilities are measured at fair value with changes in fair value recognized in earnings. "Available for sale" financial assets are measured at fair value, with changes in fair value recognized in other comprehensive income until derecognized or impaired. "Held to maturity" financial assets, "loans and receivables" and "other financial liabilities" are measured at amortized cost. The Corporation has classified its cash and cash equivalents as "held for trading", its accounts receivable as "loans and receivables" and its accounts payable and accrued liabilities and its secured debentures as "other financial liabilities".

(o) Adoption of new accounting standards:

(i) Goodwill and intangible assets

Effective January 1, 2009, the Corporation adopted the Canadian Institute of Chartered Accountants (CICA) Handbook Section 3064, Goodwill and Intangible

# ALHAMBRA RESOURCES LTD.

Notes to Consolidated Financial Statements, page 6

Years ended December 31, 2009 and 2008

(Expressed in U.S. Dollars, unless otherwise stated)

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Assets. This section provides guidance on the recognition, measurement, presentation and disclosure for goodwill and intangible assets, other than the initial recognition of goodwill or intangible assets acquired in a business combination. There was no impact to the financial statements as a result of this adoption.

(ii) Business combinations

In January 2009, the CICA Accounting Standards Board (AcSB) issued Section 1582, Business Combinations. Section 1582 replaces Section 1581, Business Combinations and harmonizes the Canadian standards with International Financial Reporting Standards (IFRS). Section 1582 establishes principles and requirements of the acquisition method for business combinations and related disclosures. This section is effective January 1, 2011, and applies prospectively to business combinations for which the acquisition date is on or after the first reporting period of the Corporation beginning on or after January 1, 2011. Early adoption is permitted. The Corporation elected to adopt Section 1582 prospectively, effective January 1, 2009. Adoption of this section was applied in the accounting for the re-acquisition of Saga Creek (note 3).

(iii) Consolidated statements and non-controlling interests

In January 2009, the AcSB issued Section 1601, Consolidated Financial Statements and Section 1602, Non-controlling Interests, which together replace Section 1600, Consolidated Financial Statements and harmonize the Canadian standards with IFRS. Section 1601 establishes standards for the preparation of consolidated financial statements. Section 1602 provides guidance on accounting for a non-controlling interest in a subsidiary in consolidated financial statements subsequent to a business combination. These sections are effective on or after the beginning of the first reporting period beginning on or after January 1, 2011. Early adoption is permitted. The Corporation adopted Section 1601 and Section 1602 prospectively, effective January 1, 2009. Adoption of these standards did not impact the Corporation's results of operations or financial position.

(iv) Financial instruments

In May 2009, the CICA amended Section 3862, Financial Instruments – Disclosures, to improve disclosure requirements about fair value measurement for financial instruments and liquidity risk disclosures. These amendments require a three-level hierarchy that reflects the significance of the inputs used in making the fair value measurements. Fair values of assets and liabilities included in level 1 are determined by reference to quoted prices in active markets for identical assets and liabilities. Assets and liabilities in level 2 include valuations using inputs other than quoted prices for which all significant outputs are observable, either directly or indirectly. Level 3 valuations are based on inputs that are unobservable and significant to the overall fair value measurement. See note 18, financial instruments for further disclosure.

# ALHAMBRA RESOURCES LTD.

Notes to Consolidated Financial Statements, page 7

Years ended December 31, 2009 and 2008  
(Expressed in U.S. Dollars, unless otherwise stated)

### 3. Re-acquisition of Saga Creek Gold Company:

On September 26, 2008 a statement of claim (“Kazakhstan Lawsuit”) was filed in the Specialized Interdistrict Economical Court of the East-Kazakhstan Oblast (“Lower Court”) seeking to invalidate Alhambra’s ownership of its former Kazakhstan Subsidiaries. Alhambra had acquired 100% interest in the Kazakhstan Subsidiaries from Marsa Aktiengesellschaft (“Marsa”), a Liechtenstein company and Teragol Investments Limited (“Teragol”), a Cyprus company (jointly the “Plaintiffs”) by virtue of a Partnership Unit Purchase and Exchange Agreement dated March 21, 2002 (the “Agreement”), as amended. The basis for the claim was that the Corporation’s 100% owned subsidiary, Alhambra Overseas Limited, incorporated to hold Alhambra’s interest in the Kazakhstan Subsidiaries, was not incorporated at the time the Agreement was initially entered into and despite the fact that such incorporation was subsequently completed soon thereafter. Alhambra applied to the Lower Court to have the litigation dismissed for the lack of jurisdiction, however, such application was denied as was the appeal to the Civil Cases Review Board of the East-Kazakhstan Oblast Court (the “Review Board”). As a result, hearings in the Lower Court on the merits of the case began on November 17, 2008 and were completed on November 24, 2008. On November 25, 2008 the Lower Court rendered its decision in favor of the Plaintiffs. The Corporation appealed the Lower Court’s decision to the Review Board but on December 26, 2008 the Review Board issued their ruling upholding the Lower Court’s decision. The Corporation appealed to the Supervisory Chamber of the East-Kazakhstan Oblast Court whose decision, rendered on February 27, 2009, again upheld the decisions of the previous courts.

As a result of the decision the courts in favor of the Plaintiffs, the Corporation wrote off its investment in the Kazakhstan Subsidiaries effective December 26, 2008 which resulted in a loss of \$31.0 million. Details of the write-off are as follows:

	2008
Accounts receivable	\$ 1,507,887
Inventory	734,753
Work in progress	7,820,283
Mineral assets	27,746,232
Accounts payable and accrued liabilities	(4,480,251)
Asset retirement obligations	(427,991)
Future income taxes	(1,935,471)
	\$ 30,965,442

On April 16, 2009 the Corporation filed an appeal with the Supreme Court of Kazakhstan asking the Supreme Court to overturn the decisions of the lower courts. The Supreme Court hearing was held on August 12, 2009 at which time the Supreme Court reversed the decisions of the Lower Courts and dismissed the Plaintiffs’ claim.

On September 15, 2009 the ownership of Saga Creek was officially re-registered back into the name of Alhambra as a result of the Supreme Court’s decision on August 12, 2009 to overturn the decisions of the lower courts of Kazakhstan which had invalidated the original agreement under

# ALHAMBRA RESOURCES LTD.

Notes to Consolidated Financial Statements, page 8

Years ended December 31, 2009 and 2008  
(Expressed in U.S. Dollars, unless otherwise stated)

which Alhambra had purchased Saga Creek. This decision effectively dismissed the plaintiff's claim that had originally been filed on September 26, 2008.

As a result of this re-registration, Alhambra re-acquired 100% of the ownership of Saga Creek and Goodwin for no consideration which resulted in a recognized gain of \$68.9 million. Alhambra had previously written off its investment in Saga Creek as of December 26, 2008 in the amount of \$31.0 million. The following table reflects the combined net identifiable assets and liabilities of Saga Creek including fair value adjustments at the time of re-registration. The Corporation undertook a review of the net identifiable assets and liabilities at the date of re-registration and, where available, third party information (including the NI 43-101 compliant report entitled "Resource and Reserve Estimation Study on the Uzboy Gold Deposit, Akmola Oblast Kazakhstan" with an effective date of December 31, 2007 prepared by Alhambra's Independent Geological Consultants) was utilized in determining these fair values. In determining the fair value of Saga Creek's assets, the Corporation made assumptions about reserves and resources, recovery rates, prices, operating, general and administration costs and capital costs and future income tax rates as well as made assumptions in determining the Corporation's weighted average cost of capital used to discount the estimated annualized cash flows that were derived from the modeling work done. These values are management's best estimates based on current information and are preliminary in nature. The Corporation recognizes that there may be changes as the calculations are finalized. Those changes may be material. Accounting standards permit up to twelve months for provisional acquisition accounting to be finalized following the re-acquisition date if any subsequent information, in particular related to the finalization of income tax accounts, provides better evidence of the item's fair value at the date of re-acquisition.

	Fair values recognized on re-acquisition at September 15, 2009
<b>Cost of re-acquisition</b>	<b>\$ -</b>
<b>Fair value of assets and liabilities:</b>	
Cash	1,234,898
Accounts receivable	1,400,111
Deposits and prepaid expenses	391,956
Supplies inventory	1,088,399
Work in progress	14,000,000
Mineral assets	84,505,496
Accounts payable and accrued charges	(4,083,317)
Asset retirement obligations	(165,618)
Future income taxes	(29,505,575)
<b>Gain recognized on re-acquisition of former subsidiary</b>	<b>\$ 68,866,350</b>

# ALHAMBRA RESOURCES LTD.

Notes to Consolidated Financial Statements, page 9

Years ended December 31, 2009 and 2008  
(Expressed in U.S. Dollars, unless otherwise stated)

Sales revenue and net income from Saga Creek from the date of re-acquisition to December 31, 2009 are disclosed in note 20 to these financial statements.

#### 4. Work in progress:

Work in progress consists of the cost of gold in various stages of production as follows:

	2009	2008
Pad	\$10,379,967	\$ —
Resin	5,442,560	—
Stripping plant	463,721	—
	16,286,248	—
Less long-term portion classified as mineral assets (note 5)	(6,791,479)	—
	\$ 9,494,769	\$ —

The balance of work in progress as at December 31, 2008 was written off as a result of the unfavorable decision reached in the Kazakhstan Lawsuit (note 3).

#### 5. Mineral assets:

Mineral assets consist of the following:

	2009	2008
Exploration costs	\$ 4,822,403	\$ —
Equipment, net of accumulated depreciation of \$332,239 as at December 31, 2009	6,679,040	—
Mineral assets, net of accumulated depletion of \$59,844 as at December 31, 2009	72,164,514	—
Long-term portion of work in progress	6,791,479	—
	\$ 90,457,436	\$ —

Costs excluded from costs subject to depletion at December 31, 2009 totaled \$4,822,403 which represents costs related to the exploration of those portions of the Corporation's mineral licenses not currently in production.

The net book value of mineral assets as at December 31, 2008 was written off as a result of the unfavorable decision reached in the Kazakhstan Lawsuit. As a result of the favorable decision by the Supreme Court of Kazakhstan and the re-registration of shares of Saga Creek back into the name of Alhambra on September 15, 2009, the assets of Saga Creek were recorded at their fair values on that date (note 3).

# ALHAMBRA RESOURCES LTD.

Notes to Consolidated Financial Statements, page 10

Years ended December 31, 2009 and 2008  
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## 6. Equipment:

2009	Cost	Accumulated depreciation	Net book value
Office equipment	\$ 100,300	\$ 63,533	\$ 36,767

  

2008	Cost	Accumulated depreciation	Net book value
Leasehold improvements	\$ 22,192	\$ 22,192	\$ –
Office equipment	85,355	46,253	39,102
	\$ 107,547	\$ 68,445	\$ 39,102

## 7. Investment:

Pursuant to a Plan of Arrangement effective August 29, 2007, the Corporation transferred its 100% interest in its claim units located in the Province of British Columbia (“DOT Properties”), together with related assets and obligations pertaining thereto, in exchange for 30,000,000 common shares. Every shareholder of the Corporation received one (1) new common share and 0.21153 of a DOT common share for every one (1) common share of the Corporation held on the effective date of the Arrangement resulting in 15,000,000 DOT common shares held by Alhambra being distributed to Alhambra shareholders on a pro rata basis.

As a result of the Arrangement, Alhambra holds 15,000,001 common shares of DOT which represents approximately 27% of the outstanding common shares of DOT. At December 31, 2009, the market trading value of the 15,000,001 DOT shares owned by Alhambra was CDN\$1,725,000.

The Corporation’s carrying value of its investment in DOT is \$561,902 (2008 - \$586,068) which is made up its cost of \$891,864 (2008 - \$762,228) less Alhambra’s share of DOT losses recorded to date of \$329,962 (2008 - \$176,160).

## 8. Secured debentures:

The Corporation had outstanding a series of twelve percent (12%) secured debentures due August 11, 2009 in the principle amount of CDN\$1,000,000 (the “Debentures”). As the Corporation was unable to pay the outstanding principal and accrued interest at the maturity date, the holders of the Debentures agreed to add the accrued interest to the principal outstanding and extend the maturity date of the Debentures to August 11, 2010. The accrued interest at August 11, 2009 totaled CDN\$125,222 resulting in the principal amount of the Debentures at August 11, 2009 totaling CDN\$1,125,222. In consideration for agreeing not to call the Debentures, the Corporation issued convertible debentures including warrants (“the Convertible Debentures”) as follows:



# ALHAMBRA RESOURCES LTD.

Notes to Consolidated Financial Statements, page 11

Years ended December 31, 2009 and 2008

(Expressed in U.S. Dollars, unless otherwise stated)

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- (a) The Convertible Debenture holders have the option to convert the principal amount and unpaid interest at any time prior to maturity into common shares of the Corporation at a price of CDN\$0.30 per common share;
- (b) Warrants to purchase up to 2,500,450 common shares ("Debenture Warrants") were granted with an expiry date of August 11, 2011. Each Debenture Warrant may be converted into one common share of the Corporation at any time prior to expiry at a purchase price of CDN\$0.45 per common share;
- (c) Interest accrues on the new principal amount at a rate of 12% per annum, compounded quarterly and payable at the earlier of the date of conversion or the new maturity date; and
- (d) The Corporation has the right at any time prior to maturity, to prepay all or a portion thereof, of the Convertible Debentures and accrued interest, without notice, bonus or penalty. If the Corporation exercises this right, then the Convertible Debenture holders will have the option of converting the principal amount of the Convertible Debentures plus accrued interest, or any portion thereof prior to the prepayment date, into common shares of the Corporation at a price of CDN\$0.30 per common share.

The Convertible Debentures continue to be secured by way of a first floating charge against all of the assets, property and undertakings of Alhambra, and are held by certain officers and/or directors of the Corporation. The issue of the Convertible Debentures and Debenture Warrants were approved by the independent members of the board of directors with the applicable directors abstaining.

The Convertible Debentures are classified as current liabilities on the balance sheet with \$50,795 ascribed to the fair value of the Debenture Warrants (note 12(c)) and \$116,101 ascribed to the fair value of the conversion feature of the Convertible Debentures (note 12(d)). The fair value of the Debenture Warrants and the conversion feature have been recorded in shareholders' equity. The carrying value of the Convertible Debentures is accreted to the original face value of the obligations over the one year term of the Convertible Debentures. Accretion expense of \$66,645 has been expensed as "interest and accretion on debt" during year ended December 31, 2009.

## **9. Secured subordinated promissory notes:**

On April 29, 2009, the Corporation issued CDN\$675,000 of subordinated secured promissory notes (the "Notes"). The Notes bore simple interest at an annual rate of 20%, were to mature April 29, 2010, were secured against assets of the Corporation and were subordinated to the Debentures.

In connection with the Notes, the Corporation issued 5,400,000 non-transferable warrants (the "Note Warrants") to purchase 5,400,000 common shares of the Corporation. Of the 5,400,000 Note Warrants issued, 2,700,000 had an exercise price of CDN\$0.10 per common share and the other 2,700,000 had an exercise price of CDN\$0.20 per common share. All Note Warrants were exercisable until October 29, 2009. The Note Warrants and any common shares acquired upon exercise of the Note Warrants were subject to a hold period expiring on August 29, 2009. A total of CDN\$215,000 of Notes were subscribed for by officers and directors of the Corporation.

# ALHAMBRA RESOURCES LTD.

Notes to Consolidated Financial Statements, page 12

Years ended December 31, 2009 and 2008  
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The Notes were classified as current liabilities on the balance sheet with \$194,472 of the proceeds allocated to the fair value of the Note Warrants (note 12(c)). The fair value of the Note Warrants was recorded in shareholders' equity. The carrying value of the Notes was accreted to the original face value of the obligations over the one year term of the Notes. Accretion expense of \$215,418 was expensed as "interest and accretion on debt" during year ended December 31, 2009.

On October 29, 2009, 5,300,274 common shares of the Corporation were issued on the conversion of 5,300,274 Note Warrants for a gross proceeds of CDN\$790,055 of which 1,620,274 common shares were issued to insiders of the Corporation. The remaining 99,726 of Note Warrants expired unexercised and were recorded to contributed surplus. The proceeds from the exercise of the Note Warrants were used to retire CDN\$758,507 of principal and accrued interest on the Notes for which the Note Warrants were originally issued.

## 10. Asset retirement obligations:

The following table presents the reconciliation of the asset retirement obligations associated with the retirement of the Uzboy Project in Kazakhstan. At December 31, 2009, the Corporation's total estimated inflated and undiscounted costs to settle its asset retirement obligation were approximately \$685,000. The estimated costs were inflated at an annual rate of 9%. Payments to settle these asset retirement obligations are estimated to be incurred in 2020 and have been discounted using a credit-adjusted risk-free interest rate of 14%.

	2009	2008
Balance, beginning of year	\$ -	\$ 374,427
Acquired on re-acquisition	165,618	-
Revisions	2,839	(1,673)
Accretion expense	6,954	55,237
Elimination of accounts of former subsidiary (note 3)	-	(427,991)
Balance, end of year	\$ 175,411	\$ -

# ALHAMBRA RESOURCES LTD.

Notes to Consolidated Financial Statements, page 13

Years ended December 31, 2009 and 2008  
(Expressed in U.S. Dollars, unless otherwise stated)

## 11. Income taxes:

- (a) Significant components of future income tax assets and liabilities at December 31, 2009 and 2008 are as follows:

	2009	2008
Future income tax assets:		
Equipment	\$ 21,140	\$ 16,165
Eligible capital expenditures	8,626	7,927
Non-capital losses	1,459,978	909,242
Share issue costs	14,097	40,372
Investments	1,482,586	3,398,832
Valuation allowance	(2,986,427)	(4,372,538)
Future income tax liabilities:		
Mineral assets	(30,831,929)	—
Future income tax liability	<u>\$(30,831,929)</u>	<u>\$ —</u>

Due to the history of operating losses, the Corporation did not consider it more likely than not that it would be able to realize a future tax benefit on continuing corporate operations and as a result, a valuation allowance is provided against the future tax assets.

- (b) Future income tax reduction differs from that which would be expected from applying the combined effective Canadian federal and provincial income tax rates of 29.00% (2008 – 29.50%) to net income (loss) before income taxes as follows:

	2009	2008
Expected income tax expense (reduction)	\$19,737,619	\$(9,784,150)
Difference resulting from:		
Stock-based compensation	166,419	348,687
Non-deductible expenses	729,623	1,460,284
Change in tax rates	2,032,293	348,456
Other	—	62,531
Impact of gain/write-off of subsidiary	(19,971,242)	4,400,362
Change in valuation allowance	(1,386,111)	3,671,344
	<u>\$ 1,308,601</u>	<u>\$ 507,514</u>

The Corporation has Canadian non-capital losses, for which no benefit has been recognized in the financial statements, of approximately CDN\$6,112,000 which commence expiring in 2014.

# ALHAMBRA RESOURCES LTD.

Notes to Consolidated Financial Statements, page 14

Years ended December 31, 2009 and 2008  
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## 12. Share capital:

(a) Authorized:

Unlimited voting common shares

Unlimited non-voting preferred shares, of which none have been issued

(b) Issued and outstanding:

	2009		2008	
	Number	Amount	Number	Amount
Common shares				
Balance, beginning of year	75,774,147	\$34,585,094	75,578,147	\$34,432,307
Exercise of warrants	5,300,274	719,016	-	-
Transfer from warrants	-	190,880	-	-
Exercise of stock options	-	-	196,000	108,009
Transfer from contributed surplus	-	-	-	44,778
Balance, end of year	81,074,421	\$35,494,990	75,774,147	\$34,585,094

(i) During the year ended December 31, 2009, a total of 5,300,274 common shares were issued upon the exercise of 5,300,274 Note Warrants for a gross proceeds of CDN\$790,055 (US\$719,016). A total of \$190,880 was transferred from warrants in connection with the exercise of the Note Warrants (note 9).

(ii) During the year ended December 31, 2009, a total of nil (2008 – 196,000) stock options were exercised for cash proceeds of \$nil (2008 - \$108,009). In addition, a total of \$nil (2008 - \$44,778) was transferred from contributed surplus to reflect the value of the options calculated on the grant date and charged as stock-based compensation expense.

(c) Warrants:

	2009		2008	
	Number	Amount	Number	Amount
Balance, beginning of year	-	\$ -	2,333,333	\$ 675,595
Pursuant to Notes (note 9)	5,400,000	194,472	-	-
Pursuant to Debentures (note 8)	2,500,450	50,795	-	-
Exercised (note 9)	(5,300,274)	(190,880)	-	-
Expired unexercised (note 9)	(99,726)	(3,592)	(2,333,333)	(675,595)
Balance, end of year	2,500,450	\$ 50,795	-	\$ -

The fair value of the Debenture Warrants granted in 2009 in conjunction with the Convertible Debentures (note 8) was estimated on the date of the issue of the Debenture Warrants using the Black-Scholes option pricing model. The fair value of the Note Warrants was calculated to be \$50,795 using the following weighted-average assumptions:

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Notes to Consolidated Financial Statements, page 15

Years ended December 31, 2009 and 2008  
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	2009
Fair value of warrants granted (CDN\$/share)	0.02
Expected life (years)	1.00
Risk free interest rate (%)	1.22
Expected volatility (%)	150
Expected dividend yield (%)	–

The fair value of the Note Warrants granted in 2009 in conjunction with the Notes (note 9) was estimated on the date of the issue of the Note Warrants using the Black-Scholes option pricing model. The fair value of the Note Warrants was calculated to be \$194,472 using the following weighted-average assumptions:

	2009
Fair value of warrants granted (CDN\$/share)	0.04
Expected life (years)	0.50
Risk-free interest rate (%)	0.80
Expected volatility (%)	150
Expected dividend yield (%)	–

	2009		2008	
	Number of warrants	Weighted average exercise price CDN\$	Number of warrants	Weighted average exercise price CDN\$
Outstanding, beginning of year	–	\$ –	2,333,333	\$ 2.00
Pursuant to Notes (note 9)	5,400,000	0.15	–	–
Pursuant to Debentures (note 8)	2,500,450	0.45	–	–
Exercised (note 9)	(5,300,274)	0.15	–	–
Expired unexercised (note 9)	(99,726)	0.20	(2,333,333)	2.00
Outstanding, end of year	2,500,450	\$ 0.45	–	\$ –
Exercisable, end of year	2,500,450	\$ 0.45	–	\$ –

(d) Equity portion of convertible debentures:

The fair value of the conversion feature granted in 2009 in conjunction with the issuance of the Convertible Debentures (note 8) was estimated on the date of the reissuance using the Black-Scholes option pricing model. The fair value of the conversion feature was calculated to be \$116,101 using the following weighted-average assumptions:

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Notes to Consolidated Financial Statements, page 16

Years ended December 31, 2009 and 2008  
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	2009
Fair value of conversion feature (CDN\$/share)	0.03
Expected life (years)	1.00
Risk-free interest rate (%)	1.22
Expected volatility (%)	150
Expected dividend yield (%)	–

(e) Options:

The Corporation has a stock option plan under which directors, officers, employees and consultants of the Corporation are eligible to receive stock options. The aggregate number of common shares to be issued upon the exercise of all options granted under the plan shall not exceed 10% of the issued common shares of the Corporation at the time of granting of the options. Options granted under the plan generally have a term of five years which is also the maximum term available and vest at terms to be determined by the directors at the time of grant. The exercise price of each option shall be determined by the directors at the time of grant but shall not be less than the price permitted by the policies of the stock exchanges on which the Corporation's common shares are then listed.

A summary of the status of the Corporation's stock option plan as at December 31, 2009 and 2008 and changes during the years then ended are as follows:

	2009		2008	
	Number of options	Weighted average exercise price CDN\$	Number of options	Weighted average exercise price CDN\$
Outstanding, beginning of year	5,670,000	\$ 1.18	3,905,000	\$ 1.18
Granted	3,600,000	0.25	2,750,000	1.15
Exercised	–	–	(196,000)	0.55
Forfeited	(2,745,000)	1.36	(789,000)	1.26
Outstanding, end of year	6,525,000	\$ 0.58	5,670,000	\$ 1.18
Exercisable, end of year	3,825,000	\$ 0.81	4,445,000	\$ 1.17

# ALHAMBRA RESOURCES LTD.

Notes to Consolidated Financial Statements, page 17

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The following table summarizes information about stock options outstanding and exercisable at December 31, 2009.

Exercise price	Outstanding		Exercisable	
	Number	Weighted average remaining contractual life (years)	Number	Weighted average remaining contractual life (years)
CDN\$0.22	3,050,000	4.67	762,500	4.67
CDN\$0.315	350,000	4.88	87,500	4.88
CDN\$0.53	200,000	4.97	50,000	4.97
CDN\$0.55	800,000	0.38	800,000	0.38
CDN\$1.15	2,125,000	1.06	2,125,000	1.06
	6,525,000	2.99	3,825,000	1.77

The fair value of the options granted is estimated on the date of grant using the Black-Scholes option-pricing model. The fair value of the options was calculated to be \$741,671 (2008 - \$1,595,975) using the following weighted-average assumptions:

	2009	2008
Expected dividend yield (%)	–	–
Expected life (years)	5.00	3.00
Risk-free interest rate (%)	2.60	3.17
Expected volatility (%)	150	79
Fair value of options granted (\$/share)	0.22	0.58

A reconciliation of contributed surplus is provided below:

	2009	2008
Balance, beginning of year	\$ 4,417,966	\$ 2,576,263
Stock-based compensation expense	573,860	1,181,990
Stock-based compensation capitalized	–	28,896
Warrants expired	3,592	675,595
Transfer to share capital on the exercise of stock options	–	(44,778)
Balance, end of year	\$ 4,995,418	\$ 4,417,966

# ALHAMBRA RESOURCES LTD.

Notes to Consolidated Financial Statements, page 18

Years ended December 31, 2009 and 2008  
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## 13. Accumulated other comprehensive income (loss):

	2009	2008
Balance, beginning of year	\$ (322,360)	\$ 960,514
Translation gains (losses) on self-sustaining operations net of tax of \$503,689 (2008 - \$nil)	501,075	(1,282,874)
Balance, end of year	\$ 178,715	\$ (322,360)

## 14. Related party transactions:

- (a) During the year ended December 31, 2009, the Corporation paid \$2,349 (2008 - \$93,294) in consulting fees to a company controlled by a former director and officer of the Corporation. The amount owing to the company controlled by the former director and officer as of December 31, 2009 was \$nil (2008 - \$11,983). The former director and officer resigned his position on September 23, 2009.
- (b) During the year ended December 31, 2009, the Corporation incurred \$48,161 (2008 - \$158,018) in costs from a law firm in which an officer of the Corporation is a partner. The officer resigned his position effective April 29, 2009. The amount owing to the law firm as of December 31, 2009 was \$126,411 (2008 - \$122,657).
- (c) On August 29, 2007, the Corporation and DOT entered into an Administrative and Corporate Services Contract (the "Contract") whereby DOT agreed to engage the Corporation to provide management, administration and corporate services to DOT. The Contract provides for a monthly remuneration of CDN\$20,000 plus all reasonable out of pocket expenses and is for an indefinite term but may be terminated by either party upon providing thirty (30) days prior written notice. The Corporation billed DOT CDN\$240,000 (2008 - CDN\$240,000) under the Contract. The amount uncollected as of December 31, 2009 was CDN\$105,368 (2008 - CDN\$nil).

These transactions are measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties.



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Notes to Consolidated Financial Statements, page 19

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## 15. Supplementary cash flow information:

Changes in non-cash working capital are as follows:

	2009	2008
Accounts receivable	\$ (581,210)	\$ (620,559)
Deposits and prepaid expenses	194,369	37,991
Supplies inventory	(252,696)	73,021
Work in progress	295,315	(2,193,714)
Accounts payable and accrued liabilities	(349,028)	3,608,720
Advances	-	(744,965)
	<u>\$ (693,250)</u>	<u>\$ 160,494</u>
Relating to:		
Operating activities	\$ (751,818)	\$ 253,369
Investing activities	58,568	(92,875)
	<u>\$ (693,250)</u>	<u>\$ 160,494</u>

## 16. Income (loss) per share:

Basic loss per share is calculated using the weighted average number of shares outstanding during the year.

	2009	2008
Weighted average shares outstanding:		
Basic	76,688,989	75,701,163
Diluted	81,957,985	75,701,163

In 2009, 3,125,000 options and 5,200,450 warrants were excluded from the diluted earnings per share. In 2008, no options or warrants have been included in the calculation of per share amounts as their effect would have been anti-dilutive.

## 17. Management of capital:

The Corporation defines capital that it manages as its shareholders' equity and working capital. The Corporation's objective when managing capital is to safeguard its ability to continue as a going concern so that it can continue to maintain investor confidence and to not expose the Corporation to excess risk. The Corporation manages its capital structure and makes adjustments to it based on the level of funds available to support the exploration and development of its mineral properties. While the re-acquisition of Saga Creek effective September 15, 2009 has resulted in the Corporation once again owning assets that generate cash flow, it is still necessary for the Corporation to raise funds to carry out its capital expenditure programs.

To date, the Corporation has raised some funds through the issue of secured indebtedness (notes 8 and 9) however these funds were raised to fund a portion of its obligations incurred during the period in which the Corporation had lost its ownership of Saga Creek. Additional financing must be obtained in order to continue as a going concern. The Corporation is currently attempting to

# ALHAMBRA RESOURCES LTD.

Notes to Consolidated Financial Statements, page 20

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raise additional funds, however, there is no assurance it will be able to do so. The Corporation is not subject to externally imposed capital requirements.

## 18. Financial Instruments:

### (a) Overview:

The Corporation has exposure to the following risks from its use of financial instruments:

- (i) Credit risk
- (ii) Liquidity risk
- (iii) Market risk

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

The board of directors has overall responsibility for the establishment and oversight of the Corporation's risk management framework. These risks are discussed with management and to the extent the board of directors determines that the risks are of such a nature that they need to be mitigated, procedures are put in place. To date, no specific risk management tools have been put in place to mitigate these risks.

### (b) Credit risk:

Credit risk is the risk of financial loss to the Corporation if a customer or counterparty to a financial instrument fails to meet its obligation and arises principally from Saga Creek's receivable from the Government of Kazakhstan owing as a result of refundable Value Added Tax ("VAT") paid on goods and services purchased by Saga Creek. To date Saga Creek has been able to collect all VAT due and owing but with the economic crisis that has affected Kazakhstan like most countries, there is no assurance that the refunds will be made on a timely basis in the future. At December 31, 2009 approximately 45% of the recorded value of accounts receivable relates to VAT.

Cash and cash equivalents consist of bank balances and short-term deposits that are redeemable at any time at the option of the Corporation. The Corporation manages the credit exposure related to short-term investments by depositing the cash equivalents only with large banks within a particular region which management believes the risk of loss to be remote.

The carrying amount of accounts receivable and cash and cash equivalents represents the maximum credit exposure. The Corporation does not have an allowance for doubtful accounts as at December 31, 2009.

### (c) Liquidity risk:

Liquidity risk is the risk that the Corporation will not be able to meet its obligations as they come due. With the re-registration of the shares of the Kazakhstan Subsidiaries, Alhambra now has ownership of revenue producing assets. However, in defending the lawsuit, the Corporation incurred substantial liabilities and the cash generated from its properties will not be enough to meet all its obligations in addition to resuming an aggressive exploration and

# ALHAMBRA RESOURCES LTD.

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development program. Therefore, additional financing must still be obtained in order to continue as a going concern. The Corporation is currently attempting to raise additional funds however there is no assurance that it will be able to do so.

(d) Market risk:

Market risk is the risk that changes in market prices, such as foreign currency exchange rates, commodity prices and interest rates will affect the Corporation's net earnings. The objective of market risk management is to manage and control market risk exposures within acceptable limits, while maximizing returns.

(i) Foreign currency risk

Foreign currency risk is the risk that the fair value or future cash flows will fluctuate as a result of changes in foreign exchange rates. The Corporation's revenue is denominated in United States dollars or Euros, its operating costs are primarily denominated in Kazakhstan Tenge while its general and administration costs are denominated in either Canadian dollars or Kazakhstan Tenge. To date the Corporation has not attempted to mitigate these foreign currency risks.

(ii) Commodity price risk

Commodity price risk is the risk that the fair value of future cash flows will fluctuate as a result of changes in commodity prices. The price of gold is impacted by economic events that dictate the levels of supply and demand for the commodity. To date the Corporation has not attempted to mitigate this commodity price risk.

(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. Currently, the Corporation's debt is all at fixed interest rates therefore there is no exposure to variations in interest rates except on cash balances.

(e) Fair value of financial assets and liabilities:

Section 3862, Financial instruments – Disclosures requires an explanation about how fair value is determined for assets and liabilities measured in the financial statements at fair value and establishes a hierarchy for which these assets and liabilities must be grouped, based on significant levels of input as follows:

Level 1: observable inputs such as quoted prices in active markets;

Level 2: inputs, other than the quoted market prices in active markets, which are observable, either directly and/or indirectly; and

Level 3: unobservable inputs for the asset or liability in which little or no market data exists therefore requiring an entity to develop its own assumptions.

# ALHAMBRA RESOURCES LTD.

Notes to Consolidated Financial Statements, page 22

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As at December 31, 2009 and 2008 the financial assets measured at fair value on the Corporation's balance sheet using level 1 is cash. Except for the Debentures, fair values of these financial instruments approximate their carrying amounts due to their short terms to maturity. The Debentures are carried at their amortized cost which is equal to their face value less the unaccreted portion of the fair value assigned to the Debenture Warrants and conversion feature.

## 19. Commitments and contingencies:

### (a) Lease agreement on premises:

Effective September 1, 2008 the Corporation entered into a lease on the premises it used for its corporate head office. The terms of the lease committed the Corporation to make monthly rental payments of CDN\$11,542 (exclusive of occupancy costs) up until expiry of the lease on August 31, 2013. The total amount remaining to be paid under the lease as of December 31, 2009 was approximately CDN\$612,000 (exclusive of occupancy costs). Effective June 1, 2009 the landlord terminated the lease as the Corporation had not paid its current obligation under the lease. Despite the landlord terminating the lease, it has informed the Corporation that it believes the Corporation wrongly repudiated the lease and remains liable for the loss of rental revenue over the unexpired term of the lease. On June 16, 2009 the landlord notified the Corporation that it is seeking to recover CDN\$97,793 in outstanding rent plus damages of CDN\$810,877 for the loss of the benefit of the lease over the balance of the term. To the extent that the landlord recovers rent from a subsequent tenant, the amount claimed by the landlord would be reduced. The landlord gave the Corporation until June 30, 2009 to settle the claim. The Corporation has held discussions with the landlord relative to their claim and to the best of the Corporation's knowledge, the landlord has not yet taken any further legal action regarding enforcement of their claim. As at December 31, 2009, the Corporation has recorded all amounts due under the lease agreement. No provision for damages has been recorded in these financial statements. The Corporation is currently assessing its options in this matter.

### (b) Mineral Extraction Tax:

Effective January 1, 2009, the Government of Kazakhstan enacted new tax legislation that included a tax on the value of useful mineral reserves extracted under the terms of a subsoil use contract. Under the provision of the legislation, the tax is based on production volumes priced at the average daily benchmark price. The rate for gold and silver, being the two products which the Corporation currently mines and sells is 5% from January 1, 2009 to December 31, 2010 and 5.5% thereafter. As the tax is new, the determination of what constitutes useful mineral reserves extracted is not well understood. While the Corporation believes that it is correct in its interpretation of the rules relative to the determination of useful mineral reserves extracted, there still exists some uncertainty at this time as to whether the tax authorities will be in agreement. No provision has been made in these financial statements for the costs and penalties that may be applicable should it be determined that the Corporation's interpretation is incorrect.

# ALHAMBRA RESOURCES LTD.

Notes to Consolidated Financial Statements, page 23

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## 20. Segment information:

During 2009, the Corporation and its subsidiaries operated in one reportable segment, the exploration for and the development of mineral properties. Information for the years ended December 31, 2009 and 2008 in each of the Corporation's geographic areas are as follows:

2009	Kazakhstan	Corporate	Total
Sales of gold	\$ 6,160,094	\$ -	\$ 6,160,094
Net income (loss)	69,171,446	(2,419,293)	66,752,153
Depreciation, depletion and accretion	255,371	8,669	264,040
Assets	103,436,477	987,895	104,424,372
Capital expenditures	347,682	360	348,042

  

2008	Kazakhstan	Corporate	Total
Sales of gold	\$ 14,852,032	\$ -	\$ 14,852,032
Net loss	(30,206,284)	(3,467,839)	(33,674,123)
Depreciation, depletion and accretion	1,623,541	13,109	1,636,650
Assets	-	689,530	689,530
Capital expenditures	4,616,858	4,245	4,621,103