

Khan Resources Inc.
Interim Consolidated Financial Statements
December 31, 2011
in thousands of Canadian dollars
(unaudited)

NOTICE OF NO AUDITOR REVIEW OF INTERIM FINANCIAL STATEMENTS

Under National Instrument 51-102, Part 4, subsection 4.3(3) (a), if an auditor has not performed a review of the interim financial statements; they must be accompanied by a notice indicating that the financial statements have not been reviewed by an auditor. The accompanying unaudited interim consolidated financial statements of the Company have been prepared by management and approved by the Audit Committee and Board of Directors of the Company. The Company's independent auditors have not performed a review of these financial statements in accordance with the standards established by the Canadian Institute of Chartered Accountants for a review of interim financial statements by an entity's auditors.

March 8, 2012

Khan Resources Inc.
Unaudited Condensed Consolidated Balance Sheets
(Expressed in thousands of Canadian dollars)

	As at December 31, 2011	As at September 30, 2011	As at October 1, 2010
Assets			
Current			
Cash	\$ 5,005	\$ 5,927	\$ 10,860
Accounts receivable	39	28	61
Prepaid expenses and other assets	77	115	201
Restricted cash (note 3)	52	52	52
Total current assets	5,173	6,122	11,174
Investments (note 4)	2,152	2,264	3,500
Plant and equipment (note 5)	3,242	3,588	3,661
Mineral rights and properties (note 6)	11,861	13,022	12,424
Intangible assets (note 14 (e) (ii))	-	-	1
	\$ 22,428	\$ 24,996	\$ 30,760
Liabilities			
Current			
Accounts payable and accrued liabilities	\$ 512	\$ 628	\$ 422
Commitments and contingencies			
Shareholders' Equity			
Share capital	73,622	73,622	73,407
Contributed surplus	11,682	11,621	11,281
Accumulated other comprehensive income	(2,976)	(1,395)	1,306
Deficit	(60,412)	(59,480)	(55,656)
	21,916	24,368	30,338
	\$ 22,428	\$ 24,996	\$ 30,760

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

On behalf of the Board:

Signed "James B.C. Doak"
Director

Signed "Grant A. Edey"
Director

Khan Resources Inc.
Unaudited Condensed Consolidated Statements of Income
(Expressed in thousands Canadian dollars, except for per share figures)

	Three months ended	
	December 31,	
	2011	2010
Revenue		
Other Income	\$ 11	\$ -
Interest	13	24
	<u>24</u>	<u>24</u>
Expenses		
General corporate	753	558
Mongolian operations	57	169
Amortization	24	36
Share-based compensation (note 7)	61	37
Foreign exchange loss (gain)	23	23
Loss on investments	36	-
Write-off of assets	-	3
	<u>954</u>	<u>826</u>
(Loss) income before income taxes	(930)	(802)
Provision (recovery) of income taxes	<u>2</u>	<u>(502)</u>
Net income (loss) for the period	<u><u>\$ (932)</u></u>	<u><u>\$ (300)</u></u>
Earnings per share:		
Basic earnings per share	\$ (0.02)	\$ (0.01)
Diluted earnings per share	\$ (0.02)	\$ (0.01)
Weighted average number of shares outstanding - Basic	54,525,445	53,982,666
Weighted average number of shares outstanding - Diluted	54,525,445	55,116,000

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

Khan Resources Inc.
Unaudited Condensed Consolidated Statements of Comprehensive Income
(Expressed in thousands Canadian dollars)

	Three months ended	
	December 31,	
	2011	2010
Net income (loss) for the period	\$ <u>(932)</u>	\$ <u>(300)</u>
Other comprehensive income		
Unrealized holding gain (loss) on available-for-sale securities arising during the period,	(78)	4,024
Income tax recover (provision)	<u>-</u>	<u>(503)</u>
	(78)	3,521
Cumulative translation adjustment	<u>(1,503)</u>	<u>393</u>
Other comprehensive income (loss)	<u>(1,581)</u>	<u>3,914</u>
Comprehensive income (loss) for the period	\$ <u><u>(2,513)</u></u>	\$ <u><u>3,614</u></u>

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

Khan Resources Inc.
Unaudited Condensed Consolidated Statements of Cash Flows
(Expressed in thousands Canadian dollars)

	Three months ended	
	December 31,	
	2011	2010
Operating Activities		
Net (loss) income for the period	\$ (932)	\$ (300)
Items not affecting cash:		
Amortization	24	36
Share-based compensation	61	37
Deferred income tax recovery (provision)	-	(503)
Loss on Investments	36	-
Unrealized foreign exchange loss (gain)	(18)	(31)
Write-off of assets	-	3
	<u>(829)</u>	<u>(758)</u>
Changes in non-cash working capital balances related to operations (note 12)	<u>(92)</u>	<u>(19)</u>
Cash used in operating activities	<u>(921)</u>	<u>(777)</u>
Investing Activities		
Mineral rights and properties		
Acquisition and development	(15)	(88)
Plant and equipment		
Acquisition	(1)	-
Other investment		
Acquisition	-	(635)
	<u>(16)</u>	<u>(723)</u>
Cash used in investing activities	<u>(16)</u>	<u>(723)</u>
Financing Activities		
Share capital		
Issuance of common shares	-	19
	<u>-</u>	<u>19</u>
Cash provided by financing activities	<u>-</u>	<u>19</u>
Effect of foreign exchange rate changes and other valuation adjustments on cash and cash equivalents	<u>15</u>	<u>13</u>
Net (decrease) increase in cash during the period	(922)	(1,468)
Cash, beginning of period	<u>5,927</u>	<u>10,860</u>
Cash, end of period	<u>\$ 5,005</u>	<u>\$ 9,392</u>

Supplementary cash flow information (note 12)

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

Khan Resources Inc.
Unaudited Condensed Consolidated Statements of Changes in Equity
(Expressed in thousands Canadian dollars)

	<u>Share capital</u>		Contributed surplus	Accumulated other comprehensive income (loss)	Deficit	Total equity
	Number of shares	Amount				
Balance, October 1, 2010	53,913,779	\$ 73,407	\$ 11,281	\$ 1,306	\$ (55,656)	\$ 30,338
Options exercised	96,666	34	(15)	-	-	19
Share-based compensation	-	-	38	-	-	38
Unrealized net gain (loss) on available-for-sale financial assets	-	-	-	3,521	-	3,521
Net income (loss) for the period	-	-	-	-	(300)	(300)
Currency translation adjustment	-	-	-	393	-	393
Balance, December 31, 2010	54,010,445	73,441	11,304	5,220	(55,956)	34,009
Options exercised	515,000	181	(77)	-	-	104
Share-based compensation	-	-	394	-	-	394
Unrealized net gain (loss) on available-for-sale financial assets	-	-	-	(6,780)	-	(6,780)
Net income (loss) for the period	-	-	-	-	(3,524)	(3,524)
Currency translation adjustment	-	-	-	165	-	165
Balance, September 30, 2011	54,525,445	73,622	11,621	(1,395)	(59,480)	24,368
Options exercised	-	-	-	-	-	-
Share-based compensation	-	-	61	-	-	61
Unrealized net gain (loss) on available-for-sale financial assets	-	-	-	(78)	-	(78)
Net income (loss) for the period	-	-	-	-	(932)	(932)
Currency translation adjustment	-	-	-	(1,503)	-	(1,503)
Balance, December 31, 2011	54,525,445	73,622	11,682	(2,976)	(60,412)	21,916

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

Khan Resources Inc.
Notes to Unaudited Condensed Consolidated Financial Statements
December 31, 2011
(Expressed in thousands of Canadian dollars, unless otherwise stated)

1. Corporate information

Khan Resources Inc., along with its subsidiary companies (collectively the “Company”), is involved in acquiring, exploring and developing mineral properties, primarily in Mongolia. The Company has initiated an International Arbitration action against the Government of Mongolia for its failure to reissue its mining and exploration licenses (see Note 2 (q) (i) and (iii)).

The Company is a publicly listed company incorporated in Canada with limited liability under the legislation of the Province of Ontario. The Company’s shares are listed on the Toronto Stock Exchange.

The head office, registered address and records office of the Company are located at 141 Adelaide Street West, Suite 1007, Toronto, Ontario, Canada, M5H 3L5.

The unaudited condensed consolidated financial statements of the Company as at and for the three months ended December 31, 2011 were authorized for issue in accordance with a resolution of the Board of Directors dated on March 8, 2012.

2. Significant accounting policies

a. Statement of compliance

International Financial Reporting Standards (“IFRS”) require companies that adopt IFRS to make an explicit and unreserved statement in their first annual IFRS financial statements of compliance with IFRS. The Company will make this statement when it issues its financial statements for the year ending September 30, 2012.

Prior to the adoption of IFRS, the Company’s financial statements were prepared in accordance with Canadian generally accepted accounting principles (“Canadian GAAP”). These unaudited condensed consolidated financial statements represent the Company’s initial presentation of its results and financial position under IFRS and as such were prepared in accordance with IAS 34, Interim Financial Reporting and IFRS 1, First-time Adoption of IFRS (“IFRS 1”). The disclosures of the elected transition exemptions, reconciliation and explanation of accounting policy compared to Canadian GAAP have been provided in Note 14 to these financial statements. The policies applied in these condensed consolidated financial statements are based on IFRS issued and effective as at the date the Board of Directors approved these financial statements for issue. Any subsequent changes to IFRS could result in a restatement of these financial statements, including the transition adjustments recognized on conversion to IFRS.

These unaudited condensed consolidated financial statements should be read in conjunction with the Company’s annual financial statements for the year ended September 30, 2011, which were prepared in accordance with Canadian GAAP, and have been restated in the IFRS disclosures included in Note 14.

Khan Resources Inc.
Notes to Unaudited Condensed Consolidated Financial Statements
December 31, 2011
(Expressed in thousands of Canadian dollars, unless otherwise stated)

b. *Basis of measurement*

The consolidated financial statements have been prepared under the historical cost convention, except for the revaluation of certain financial assets and financial liabilities to fair value, including derivative instruments and available-for-sale investments.

c. *Consolidation*

The financial statements of the Company consolidate the accounts of Khan Resources Inc. and its subsidiaries. All intercompany transactions, balances and unrealized gains and losses from intercompany transactions are eliminated on consolidation.

Subsidiaries are those entities which Khan Resources Inc. controls by having the power to govern the financial and operating policies. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether Khan Resources Inc. controls another entity. Subsidiaries are fully consolidated from the date on which control is obtained by Khan Resources Inc. and are de-consolidated from the date that control ceases.

d. *Foreign currency translation*

i. Functional and presentation currency

The functional currency for each subsidiary of the Company is the currency of the primary economic environment in which the entity operates. The functional currency of the Canadian head office and all intermediate holding companies is the Canadian dollar (CAD). The functional currency of all Mongolian subsidiaries is the Mongolian Tugrik (MNT). The consolidated financial statements are presented in Canadian dollars, which is the Khan Resources Inc.'s functional currency.

The financial statements of entities that have a functional currency different from that of Khan Resources Inc. ("foreign operations") are translated into Canadian dollars as follows: assets and liabilities – at the closing rate at the date of the balance sheet, and income and expenses – at the average rate of the period (as this is considered a reasonable approximation to actual rates). All resulting changes are recognized in other comprehensive income as cumulative translation adjustments.

When an entity disposes of its entire interest in a foreign operation, or loses control, joint control, or significant influence over a foreign operation, the foreign currency gains or losses accumulated in other comprehensive income related to the foreign operation are recognized in profit or loss. If an entity disposes of part of an interest in a foreign operation which remains a subsidiary, a proportionate amount of foreign currency gains or losses accumulated in other comprehensive income related to the subsidiary is reallocated between controlling and non-controlling interests.

ii. Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Generally, foreign

Khan Resources Inc.
Notes to Unaudited Condensed Consolidated Financial Statements
December 31, 2011
(Expressed in thousands of Canadian dollars, unless otherwise stated)

exchange gains and losses resulting from the settlement of foreign currency transactions and from the translation at period-end exchange rates of monetary assets and liabilities denominated in currencies other than an operation's functional currency are recognized in the statement of income.

e. ***Cash and cash equivalents***

Cash and cash equivalents include cash on hand, deposits held with banks, and other short-term highly liquid investments with original maturities of three months or less.

f. ***Financial instruments***

Financial assets and liabilities are recognized when the Company becomes a party to the contractual provisions of the instrument. Financial assets are derecognized when the rights to receive cash flows from the assets have expired or have been transferred and the Company has transferred substantially all risks and rewards of ownership.

Financial assets and liabilities are offset and the net amount is reported in the balance sheet when there is a legally enforceable right to offset the recognized amounts and there is an intention to settle on a net basis, or realize the asset and settle the liability simultaneously.

At initial recognition, the Company classifies its financial instruments in the following categories depending on the purpose for which the instruments were acquired:

i. ***Financial assets and liabilities at fair value through profit or loss:***

A financial asset or liability is classified in this category if acquired principally for the purpose of selling or repurchasing in the short-term. Derivatives are also included in this category unless they are designated as hedges (see v below).

The only instruments held by the Company classified in this category are investments in derivatives (warrants).

Financial instruments in this category are recognized initially and subsequently at fair value. Transaction costs are expensed in the statement of income. Gains and losses arising from changes in fair value are presented in the statement of income within other gains and losses in the period in which they arise.

Financial assets and liabilities at fair value through profit or loss are classified as current except for the portion expected to be realized or paid beyond twelve months of the balance sheet date, which is classified as non-current.

ii. ***Available-for-sale investments:***

Available-for-sale investments are non-derivatives that are either designated in this category or not classified in any of the other categories. The Company's available-for-sale assets comprise any marketable securities and investments in debt and equity securities.

Available-for-sale investments are recognized initially at fair value plus transaction costs and are subsequently carried at fair value. Gains or losses arising from changes in fair value are recognized in other comprehensive income. Available-for-sale investments are classified as non-current, unless the investment matures within twelve months, or management expects to dispose

Khan Resources Inc.
Notes to Unaudited Condensed Consolidated Financial Statements
December 31, 2011
(Expressed in thousands of Canadian dollars, unless otherwise stated)

of them within twelve months.

Interest on available-for-sale investments, calculated using the effective interest method, is recognized in the statement of income as part of interest income. Dividends on available-for-sale equity instruments are recognized in the statement of income as part of other gains and losses when the company's right to receive payment is established. When an available-for-sale investment is sold or impaired, the accumulated gains or losses are moved from accumulated other comprehensive income to the statement of income and are included in other gains and losses.

iii. *Loans and receivables:*

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. The Company's loans and receivables comprise accounts receivables and cash and cash equivalents, and are included in current assets due to their short-term nature.

Loans and receivables are initially recognized at the amount expected to be received, less, when material, a discount to reduce the loans and receivables to fair value. Subsequently, loans and receivables are measured at amortized cost using the effective interest method less a provision for impairment.

iv. *Financial liabilities at amortized cost:*

Financial liabilities at amortized cost include accounts payable and any bank debt and long-term debt. Accounts payable are initially recognized at the amount required to be paid, less, when material, a discount to reduce the payables to fair value. Subsequently, accounts payable are measured at amortized cost using the effective interest method. Any bank debt and long-term debt would be recognized initially at fair value, net of any transaction costs incurred, and subsequently at amortized cost using the effective interest method.

Financial liabilities are classified as current liabilities if payment is due within twelve months. Otherwise, they are presented as non-current liabilities.

v. *Derivative financial instruments:*

Derivatives designated as hedges are classified as held-for-trading, are included on the balance sheet within other assets or other liabilities, and are classified as current or non-current based on the contractual terms specific to the instrument. Gains and losses on re-measurement are included in net income. No amount has been recorded in these consolidated financial statements for derivatives designated as hedges as no such financial instruments were held as at the date of these consolidated financial statements.

g. *Impairment of financial assets*

At each reporting date, the Company assesses whether there is objective evidence that a financial asset is impaired. If such evidence exists, the Company recognizes an

Khan Resources Inc.
Notes to Unaudited Condensed Consolidated Financial Statements
December 31, 2011
(Expressed in thousands of Canadian dollars, unless otherwise stated)

impairment loss, as follows:

i. Financial assets carried at amortized cost:

The loss is the difference between the amortized cost of the loan or receivable and the present value of the estimated future cash flows, discounted using the instrument's original effective interest rate. The carrying amount of the asset is reduced by this amount either directly or indirectly through the use of an allowance account.

ii. Available-for-sale financial assets:

The impairment loss is the difference between the original cost of the asset and its fair value at the measurement date, less any impairment losses previously recognized in the statement of income. This amount represents the cumulative loss in accumulated other comprehensive income that is reclassified to net income.

Impairment losses on financial assets carried at amortized cost are reversed in subsequent periods if the amount of the loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized. Impairment losses on available-for-sale equity instruments are not reversed.

h. *Plant and equipment*

Plant and equipment are initially recorded at cost, including all directly attributable costs to bring the assets to the location and condition necessary for it to be capable of operating in the manner intended by management. Plant and equipment are subsequently measured at cost less accumulated depreciation and applicable impairment losses. Depreciation is computed on a straight-line basis based on the nature and useful lives of the assets. The significant classes of plant and equipment and their estimated useful lives are as follows:

Buildings: 5 years

Camp equipment, fixtures, furniture and vehicles: 5 years

Office equipment: 3 years

Subsequent costs that meet the asset recognition criteria are capitalized while costs incurred that do not extend the economic useful life of an asset are considered repairs and maintenance, which are accounted for as an expense recognized during the period.

Assets under construction are capitalized as construction-in-progress. The cost of construction-in-progress comprises its purchase price and any costs directly attributable to bringing it into working condition for its intended use. Construction-in-progress assets are not depreciated until they are completed and available for use.

i. Mineral rights and properties

The cost of acquiring mineral rights and properties either as an individual asset purchase or as part of a business combination is capitalized and represents the property's fair value at the date of acquisition. Fair value is determined by estimating the value of the property's reserves, resources and exploration potential.

Khan Resources Inc.
Notes to Unaudited Condensed Consolidated Financial Statements
December 31, 2011
(Expressed in thousands of Canadian dollars, unless otherwise stated)

Exploration and evaluation costs, incurred associated with specific mineral rights and properties prior to demonstrable technical feasibility and commercial viability of extracting a mineral resource, are capitalized. Upon determination that a mineral property can be economically developed, which occurs at the earlier of: (i) completion of positive economic analysis of the mineral deposit by establishing proven and probable reserves; or (ii) obtaining a mining permit, the subsequent development costs incurred such as to further delineate the ore body and costs incurred during production to increase output by providing access to additional sources of mineral resources, are also capitalized. Administrative expenditures that are not directly related to property maintenance are charged to operations as incurred.

Upon commencement of commercial production, mineral rights and properties and capitalized expenditures will be depleted over the mine's estimated life using the units of production method calculated based on proven and probable reserves. If commercial production commences prior to the determination of proven and probable reserves, depletion will be calculated based on the mineable portion of measured and indicated resources.

j. Impairment of non-financial assets

Non-financial assets, including mineral rights and properties, plant and equipment are reviewed and tested for impairment when indicators of impairment are considered to exist. Impairment assessments are conducted at the level of cash-generating units (CGU), which is the lowest level for which identifiable cash flows are largely independent of the cash flows of other assets. Management has assessed its CGUs as being an individual mine site (the Dornod properties in Mongolia). An impairment loss is recognized for any excess of carrying amount of the CGU over its recoverable amount, which is the greater of its fair value less costs to sell and value in use. For mineral rights and properties and processing facilities, the recoverable amount is estimated as the discounted future net cash flows expected to be derived from expected future production, metal prices, and net proceeds from the disposition of assets on retirement, less operating and capital costs. Impairment losses are recognized in the period they are incurred.

Impairment losses are reversed if the conditions that gave rise to the impairment are no longer present and it has been determined that the asset is no longer impaired as a result. This reversal is recognized in net income in the period the reversal occurs limited by the carrying value that would have been determined, net of any depreciation, had no impairment charge been recognized in prior years.

k. Rehabilitation Provision

The Company will recognize a rehabilitation provision for statutory, contractual, constructive or other legal obligations relating to site reclamation and restoration costs that will incur on the retirement of assets and abandonment of mine and exploration sites. Provisions for the cost of the mine site's rehabilitation program are normally recognized at the time that an environmental disturbance occurs or a constructive obligation is determined. No amount has been recorded in these consolidated financial statements for rehabilitation obligations as no such obligations were incurred as at the

Khan Resources Inc.
Notes to Unaudited Condensed Consolidated Financial Statements
December 31, 2011
(Expressed in thousands of Canadian dollars, unless otherwise stated)

date of these consolidated financial statements.

l. ***Share-based payments***

The Company awards stock options to employees, officers, directors, and consultants. Each tranche in an award is considered a separate award with its own vesting period and grant date fair value. Fair value of each tranche is measured at the date of grant using the Black-Scholes option pricing model. Compensation expense is recognized over the tranche's vesting period by increasing contributed surplus based on the number of awards expected to vest. The number of awards expected to vest is reviewed at least annually, with any impact being recognized immediately.

Upon the exercise of the stock option, consideration received and the related amount transferred from contributed surplus are recorded as share capital.

m. ***Income tax***

Income tax comprises current and deferred tax. Income tax is recognized in the statement of income except to the extent that it relates to items recognized directly in equity, in which case the income tax is also recognized directly in equity.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted, at the end of the reporting period, and any adjustment to tax payable in respect of previous years.

In general, deferred tax is recognized in respect of temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. Deferred income tax is determined on a non-discounted basis using tax rates and laws that have been enacted or substantively enacted at the balance sheet date and are expected to apply when the deferred tax asset or liability is settled. Deferred tax assets are recognized to the extent that it is probable that the assets can be recovered.

Deferred income tax is not provided on temporary differences arising on investments in subsidiaries where the timing of the reversal of the temporary difference is controlled by the Company and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred income tax assets and liabilities are presented as non-current.

Tax on income in interim periods is accrued using the tax rate that would be applicable to expected total annual earnings.

n. ***Share capital***

Common shares are classified as equity. Incremental costs directly attributable to the issuance of shares are recognized as a deduction from equity.

o. ***Earnings per share***

Basic earnings per share (EPS) is calculated by dividing the net income (loss) for the period attributable to equity owners of Khan Resources Inc. by the weighted average

Khan Resources Inc.
Notes to Unaudited Condensed Consolidated Financial Statements
December 31, 2011
(Expressed in thousands of Canadian dollars, unless otherwise stated)

number of common shares outstanding during the period.

Diluted EPS is calculated by adjusting the weighted average number of common shares outstanding for dilutive instruments. The number of shares included with respect to options, warrants and similar instruments is computed using the treasury stock method. Under this method, derivatives, whose exercise price is less than the average market price of our common shares, are assumed to be exercised and the proceeds are used to repurchase common shares at the average market price for the period. The incremental number of common shares issued under stock options, and repurchased from proceeds, is included in the calculation of diluted earnings per share. Khan Resources Inc.'s potentially dilutive common shares comprise stock options granted to directors, officers employees, and consultants.

p. *Segment reporting*

The Company has only a single operating segment, and therefore one reportable segment.

The single operating segment is the company's foreign operation in Mongolia. The Mongolian operation is principally engaged in the acquisition, exploration, evaluation, and development of mining properties. Its Dornod properties have not achieved commercial production and no revenue from the Dornod properties has been recorded in these consolidated financial statements.

The company's non-current assets are located in Mongolia. Non-current assets located at the corporate office in Canada are minor in relation to the total.

q. *Critical accounting estimates and judgments*

The preparation of the Company's consolidated financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the reported amounts of assets, liabilities and contingent liabilities at the date of the consolidated financial statements and reported amounts of revenues and expenses during the reporting period. Estimates and assumptions are continuously evaluated and are based on management's experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. However, actual outcomes can differ from these estimates.

In particular, information about significant areas of estimation uncertainty considered by management in preparing the consolidated financial statements is described below.

i. *Recoverability of mineral rights and properties*

The recoverability of the amounts shown for mineral rights and properties is dependent upon the tenure of mineral licenses, the existence of economically recoverable reserves, and the ability of the Company to obtain necessary financing to complete the development of those reserves and upon future profitable production and/or the proceeds from the disposition thereof. To date, the Company has not earned any revenues from its properties.

On July 16, 2009, the Mongolian Parliament passed a new Nuclear Energy

Khan Resources Inc.
Notes to Unaudited Condensed Consolidated Financial Statements
December 31, 2011
(Expressed in thousands of Canadian dollars, unless otherwise stated)

Law (NEL) that classifies all radioactive mineral deposits, regardless of size, as strategically important mineral deposits and regulates the nuclear energy industry in Mongolia, including the exploration, exploitation, development, mining and sale of uranium. The new law became effective on August 15, 2009. In connection with the passing of the NEL, the Mongolian Parliament also passed certain procedures relating to the re-registration of existing exploration and mining licenses held prior to the NEL becoming effective. Existing license holders were required to submit an application to the newly created Nuclear Energy Agency (NEA) and renew and re-register their existing licenses by November 15, 2009. Khan submitted the applications for the renewal and re-registration of its mining license and exploration license on November 10, 2009.

To date, the mining and exploration licenses have not been reissued to Khan and the Company has initiated an International Arbitration action against the Government of Mongolia for its failure to do so.

There can be no assurance that Khan's licenses will be retained, re-instated or re-registered under the NEL (or any other law pursuant to which such licenses may in the future be required to be registered) or, if retained, re-instated or re-registered, the terms and conditions upon which such licenses may be retained, re-instated or re-registered. In the absence of the mining and exploration licenses being retained, re-instated or re-registered, there is uncertainty surrounding the Company's interest in the title and capitalized values of the Dornod properties.

The Company believes it has complied with all of the Mongolian Government requirements to maintain title and that a settlement arrangement will be reached with the Government of Mongolia whereby the Company will realize value for its interest in the Dornod properties. Management has prepared the Company's consolidated financial statements with no write-down of the capitalized value relating to the Dornod properties (see iii below).

ii. Ore reserve and resource estimates

Ore reserves are estimates of the amount of ore that can be economically and legally extracted from the Company's mineral properties. The Company estimates its ore reserves and mineral resources based on information compiled by qualified persons as defined in accordance with National Instrument 43-101. The estimation of recoverable reserves is based upon factors such as estimates of foreign exchange rates, commodity prices, future capital requirements and production costs along with complex geological assumptions and judgments made in estimating the size and grade of the ore body. Changes in the reserve or resource estimates may impact upon the carrying value of exploration and evaluation assets, mine properties, property, plant and equipment, goodwill, provision for rehabilitation, recognition of deferred tax assets, and depreciation and amortization charges.

Khan Resources Inc.
Notes to Unaudited Condensed Consolidated Financial Statements
December 31, 2011
(Expressed in thousands of Canadian dollars, unless otherwise stated)

iii. *Impairment of assets*

At each reporting date, the Company assesses whether there is objective evidence that an asset is impaired. Where an indicator of impairment exists, a formal estimate of the recoverable amount is made, which is considered to be the higher of the fair value less costs to sell and value in use. These assessments require the use of estimates and assumptions such as long-term commodity prices, discount rates, future capital requirements, exploration potential and operating performance. These estimates and assumptions are set out above in the Company's accounting policies for impairment of financial assets and impairment of non-financial assets.

With respect to mineral rights and properties, If the Government of Mongolia prevails in its assertions that Khan has not met the requirements to retain, re-instate or re-register its licenses with respect to the Dornod properties, and the Company loses its interest in the Dornod properties, then the Company will be required to recognize a material write-down of the Dornod properties and related assets.

iv. *Recovery of deferred tax assets*

Judgment is required in determining whether deferred tax assets are recognized on the balance sheet. Deferred tax assets, including those arising from un-utilized tax losses require management to assess the likelihood that the Company will generate taxable earnings in future periods, in order to utilize recognized deferred tax assets. Estimates of future taxable income are based on forecast cash flows from operations and the application of existing tax laws in each jurisdiction. To the extent that future cash flows and taxable income differ significantly from estimates, the ability of the Company to realize the net deferred tax assets recorded at the reporting date could be impacted. Additionally, future changes in tax laws in the jurisdictions in which the Company operates could limit the ability of the Company to obtain tax deductions in future periods.

v. *Fair value hierarchy*

Where the fair value of financial assets and financial liabilities recorded in the balance sheet cannot be derived from active markets, their fair value is determined using valuation techniques including the discounted cash flow model. The inputs to these models are taken from observable markets where possible, but where this is not feasible, a degree of judgment is required in establishing fair values. The judgments include considerations of inputs such as liquidity risk, credit risk and volatility. Changes in assumptions about these factors could affect the reported fair value of financial instruments.

r. *Accounting standards issued but not yet applied*

i. *IAS 32 Offsetting Financial Assets and Financial Liabilities (Amendments to IAS 32).*

On December 16, 2011 the IASB published amendments to IAS 32 Financial Instruments: Presentation to clarify the application of the offsetting

Khan Resources Inc.
Notes to Unaudited Condensed Consolidated Financial Statements
December 31, 2011
(Expressed in thousands of Canadian dollars, unless otherwise stated)

requirements. The amendments are effective for annual periods beginning on or after January 1, 2014, with earlier application permitted. The Company has not yet assessed the impact of the standard or determined whether it will adopt the standard early.

ii. Disclosures—Offsetting Financial Assets and Financial Liabilities (Amendments to IFRS 7).

On December 16, 2011 the IASB published new disclosures requirements jointly with the FASB that enable users of the financial statements to better compare financial statements prepared in accordance with IFRS and US GAAP. The new requirements are effective for annual periods beginning on or after 1 January 2013. None of these requirements are expected to have a significant effect on the consolidated financial statements of the Company.

iii. Mandatory Effective Date of IFRS 9 and Transition Disclosures (Amendments to IFRS 9 (2009), IFRS 9 (2010) and IFRS 7).

On December 16, 2011 the IASB deferred the mandatory effective date of IFRS 9 to January 1, 2015. The amendments also provide relief from restating comparative information and require disclosures (in IFRS 7) to enable users of financial statements to understand the effect of beginning to apply IFRS 9. The Company has not yet assessed the impact of the standard and transition disclosures.

iv. IFRIC 20 Stripping Costs in the Production Phase of a Surface Mine.

On October 19, 2011 the IASB issued IFRIC 20. The Interpretation clarifies when production stripping should lead to the recognition of an asset and how that asset should be measured, both initially and in subsequent periods. The Interpretation is effective for annual periods beginning on or after January 1, 2013 with earlier application permitted. The Company has not yet assessed the impact of the interpretation.

v. Financial Statement Presentation (Amendments to IAS 1).

On June 16, 2011 the Board issued amendments to IAS 1 Financial Statement Presentation. These amendments improve how components of other comprehensive income are presented. The FASB issued equivalent requirements on the same day. The new requirements are effective for annual periods beginning on or after July 1, 2012. The Company has not yet assessed the impact of these amendments.

vi. Post-employment benefits (Amendments to IAS 19).

On June 16, 2011 the Board issued amendments to IAS 19 Employee Benefits. The amendments will improve the recognition and disclosure requirements for defined benefit plans. The new requirements are effective for annual periods beginning on or after January 1, 2013, with earlier application permitted. This change will have no impact on the consolidated financial statements of the Company. The Company does not have a defined benefit plan.

Khan Resources Inc.
Notes to Unaudited Condensed Consolidated Financial Statements
December 31, 2011
(Expressed in thousands of Canadian dollars, unless otherwise stated)

vii. *Fair value measurement (new IFRS 13).*

On May 13, 2011 the IASB issued IFRS 13 Fair Value Measurement. IFRS 13 defines fair value, sets out in a single IFRS a framework for measuring fair value and requires disclosures about fair value measurements. IFRS 13 applies when other IFRSs require or permit fair value measurements. It does not introduce any new requirements to measure an asset or a liability at fair value, change what is measured at fair value in IFRSs or address how to present changes in fair value. The new requirements are effective for annual periods beginning on or after January 1, 2013, with earlier application permitted. The Company has not yet assessed the impact of the standard or determined whether it will adopt the standard early.

viii. *Consolidations, Joint arrangements and Disclosure of Interests in Other Entities (Amendments to IAS 27 and IAS 28 and new IFRS 10, IFRS 11 and IFRS 12).*

On May 13, 2011 the IASB issued IFRS 10 Consolidated Financial Statements, IFRS 11 Joint Arrangements and IFRS 12 Disclosure of Interests in Other Entities. IFRS 10 provides a single consolidation model that identifies control as the basis for consolidation for all types of entities. IFRS 10 replaces IAS 27 Consolidated and Separate Financial Statements and SIC-12 Consolidation—Special Purpose Entities. IFRS 11 Joint Arrangements establishes principles for the financial reporting by parties to a joint arrangement. IFRS 11 supersedes IAS 31 Interests in Joint Ventures and SIC-13—Jointly Controlled Entities—Non-monetary Contributions by Venturers. IFRS 12 combines, enhances and replaces the disclosure requirements for subsidiaries, joint arrangements, associates and unconsolidated structured entities. As a consequence of these new IFRSs, the IASB also issued amended and retitled IAS 27 Separate Financial Statements and IAS 28 Investments in Associates and Joint Ventures. The new requirements are effective for annual periods beginning on or after January 1, 2013, with earlier application permitted. The Company has not yet assessed the impact of the standard or determined whether it will adopt the standard early.

3. Restricted cash

Restricted cash consists of a guaranteed investment certificate pledged as security for a corporate credit card facility. This guaranteed investment certificate has a maturity date of less than one year.

Khan Resources Inc.
Notes to Unaudited Condensed Consolidated Financial Statements
December 31, 2011
(Expressed in thousands of Canadian dollars, unless otherwise stated)

4. Investments

	As at December 31, 2011	As at September 30, 2011	As at October 1, 2010
Available-for-sale financial assets	\$ 2,096	\$ 2,173	\$ 3,500
Financial assets designated at fair value through profit or loss	56	91	-
	<u>\$ 2,152</u>	<u>\$ 2,264</u>	<u>\$ 3,500</u>

Investments in publicly-traded companies represent equity interests of other publicly-trading mining companies that the Company has acquired through the open market or through private placements. These equity interests are for long-term investment purposes and consist of common shares and warrants.

Common shares are classified as available-for-sale and are measured at fair value on initial recognition and subsequent measurement. Fair value changes are recognized in other comprehensive income of the period. As of December 31, 2011, none of the shares held by the Company was 20% or more of the respective outstanding shares of investees.

Warrants, by their nature, meet the definition of derivatives and are classified as at fair value through profit and loss. The fair value of the warrants was determined using the Black-Scholes pricing model as at the acquisition date as well as at each period end. Fair value changes are recognized in net income of the period. In the three months ended December 31, 2011 a gain of \$16 was recognized (2010 – loss of \$10).

Khan Resources Inc.
Notes to Unaudited Condensed Consolidated Financial Statements
December 31, 2011
(Expressed in thousands of Canadian dollars, unless otherwise stated)

5. Plant and equipment

Plant and equipment consist of:

Cost	Buildings	Camp equipment (a)	Office equipment	Construction in progress (b)	Total
Balance, October 1, 2010	\$ 304	\$ 360	\$ 132	\$ 3,370	\$ 4,166
Additions	-	-	11	-	11
Disposals	(7)	(136)	(25)	(28)	(196)
Currency translation adjustment	10	9	1	120	140
Balance, September 30, 2011	307	233	119	3,462	4,121
Additions	-	1	-	-	1
Disposals	-	(1)	(17)	-	(18)
Currency translation adjustment	(29)	(16)	(3)	(314)	(362)
Balance, December 31, 2011	\$ 278	\$ 217	\$ 99	\$ 3,148	\$ 3,742
Accumulated depreciation and amortization					
Balance, October 1, 2010	\$ (168)	\$ (210)	\$ (127)	\$ -	\$ (505)
Depreciation and amortization	(62)	(59)	(5)	-	(126)
Disposals	7	81	25	-	113
Currency translation adjustment	(7)	(7)	(1)	-	(15)
Balance, September 30, 2011	(230)	(195)	(108)	-	(533)
Depreciation and amortization	(15)	(8)	(1)	-	(24)
Disposals	-	1	17	-	18
Currency translation adjustment	23	13	3	-	39
Balance, December 31, 2011	\$ (222)	\$ (189)	\$ (89)	\$ -	\$ (500)
Carrying amounts					
Balance, October 1, 2010	\$ 136	\$ 150	\$ 5	\$ 3,370	\$ 3,661
Balance, September 30, 2011	\$ 77	\$ 38	\$ 11	\$ 3,462	\$ 3,588
Balance, December 31, 2011	\$ 56	\$ 28	\$ 10	\$ 3,148	\$ 3,242

(a) Camp equipment comprises furniture, fixtures and vehicles.
(b) Construction in progress comprises a power line and a sedimentation pond.

Khan Resources Inc.
Notes to Unaudited Condensed Consolidated Financial Statements
December 31, 2011
(Expressed in thousands of Canadian dollars, unless otherwise stated)

6. Mineral rights and properties

Mineral rights and properties consist of:

	Mineral property acquisition	Mineral property development	Total
Cost			
Balance, October 1, 2010	\$ 487	\$ 11,937	\$ 12,424
Capitalized expenditures	-	153	153
Currency translation adjustment	14	431	445
Balance, September 30, 2011	<u>501</u>	<u>12,521</u>	<u>13,022</u>
Capitalized expenditures		15	15
Currency translation adjustment	(35)	(1,141)	(1,176)
Balance, December 31, 2011	<u>\$ 466</u>	<u>\$ 11,395</u>	<u>\$ 11,861</u>
Accumulated depletion			
Balance, October 1, 2010	\$ -	\$ -	\$ -
Depletion	-	-	-
Currency translation adjustment	-	-	-
Balance, September 30, 2011	<u>-</u>	<u>-</u>	<u>-</u>
Depletion	-	-	-
Currency translation adjustment	-	-	-
Balance, December 31, 2011	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>
Carrying amounts			
Balance, October 1, 2010	\$ 487	\$ 11,937	\$ 12,424
Balance, September 30, 2011	\$ 501	\$ 12,521	\$ 13,022
Balance, December 31, 2011	<u>\$ 466</u>	<u>\$ 11,395</u>	<u>\$ 11,861</u>

Khan Resources Inc.
Notes to Unaudited Condensed Consolidated Financial Statements
December 31, 2011
(Expressed in thousands of Canadian dollars, unless otherwise stated)

7. Share capital

a. Authorized

Unlimited number of common shares without par value. All shares issued as at December 31, 2011 were fully paid.

b. Stock options

The Company has a stock option plan providing for the issuance of stock options to directors, officers, employees and consultants. The number of shares that may be acquired under an option granted to a participant is determined by the Board of Directors. The exercise price of the options granted shall comply with the requirements of the stock exchange or exchanges on which the Company's common shares are listed. The maximum term of any option may not exceed five years. Generally, options vest over 24 months. The following is a summary of option transactions:

	Number of options	Weighted average exercise price per share
Balance, October 1, 2010	3,947,000	\$ 0.56
Options granted	1,225,000	0.55
Options exercised	(611,666)	0.20
Options forfeited	(595,000)	0.72
Options expired	(487,000)	1.49
Balance, September 30, 2011	3,478,334	0.46
Options granted	-	-
Options exercised	-	-
Options forfeited	-	-
Options expired	-	-
Balance, December 31, 2011	3,478,334	\$ 0.46

During the three months ended December 31, 2011, no options were granted to directors, officers, and employees.

For the three months ended December 31, 2011, a total of \$ 61 (three months ended December 31, 2010 - \$37) in share-based compensation expenses was recorded and included in the general and administrative expenses on the consolidated statements of income.

Khan Resources Inc.
Notes to Unaudited Condensed Consolidated Financial Statements
December 31, 2011
(Expressed in thousands of Canadian dollars, unless otherwise stated)

The following table summarizes information about stock options outstanding at December 31, 2011:

Expiry date	Weighted average exercise price	Remaining weighted average contractual life in years	Fair value per option	Number of options outstanding	Number of options vested	Number of options unvested
August 31, 2012	\$ 1.70	\$ 0.67	\$ 1.30	25,000	25,000	-
February 19, 2013	1.40	1.14	1.07	200,000	200,000	-
May 14, 2013	0.89	1.36	0.68	200,000	200,000	-
December 17, 2013	0.20	1.96	0.15	753,334	753,334	-
August 16, 2015	0.29	3.62	0.21	1,200,000	800,000	400,000
February 16, 2016	0.55	4.12	0.39	1,100,000	366,666	733,334
				<u>3,478,334</u>	<u>2,345,000</u>	<u>1,133,334</u>

Subsequent to December 31, 2011, a total of 1,400,000 options with a life of three years were granted to directors, officers, and employees at an exercise price of \$ 0.20 per share subject to a vesting schedule over a one-year term with one-third vesting immediately, one-third vesting in six months and one-third vesting in one year.

8. Compensation of key management

Key management includes the company's directors and officers. Compensation awarded to key management included:

	Three months ended December 31,	
	2011	2010
Directors' fees	\$ 39	\$ 46
Salaries and short-term benefits	92	151
Share-based compensation	56	42
	<u>\$ 187</u>	<u>\$ 239</u>

9. Related party transactions

An officer of the Company is a partner in a firm that provides legal services to the company. The company paid an aggregate of \$7 for the three months ended December 31, 2011. There were no related party transactions for the three months ended December 31, 2010.

10. Capital management

The Company's objectives of capital management are intended to safeguard the entity's ability to continue as a going concern and to continue the development of its Dornod mineral properties in Mongolia into production (the "Project") or to receive full value for the Project from the Government of Mongolia.

The capital of the Company consists of the items included in shareholders' equity. Risk and capital management are monitored by the Board of Directors. The Company manages the capital structure and makes adjustments depending on economic conditions. Funds have been

Khan Resources Inc.
Notes to Unaudited Condensed Consolidated Financial Statements
December 31, 2011
(Expressed in thousands of Canadian dollars, unless otherwise stated)

primarily secured through issuances of equity capital. The Company invests all capital that is surplus to its immediate needs in short-term, liquid and highly rated financial instruments, such as cash and other short-term deposits, all held with major financial institutions. Significant risks are monitored and actions are taken, when necessary, according to the Company's approved policies.

11. Financial instruments

The Company manages its exposure to financial risks, including liquidity risk, foreign exchange rate risk, interest rate risk, credit risk and equity price risk in accordance with its risk management framework. The Company's Board of Directors has overall responsibility for the establishment and oversight of the Company's risk management framework and reviews the Company's policies on an ongoing basis.

a. Fair value

The Company classifies its fair value measurements within a fair value hierarchy, which reflects the significance of the inputs used in making the measurements as defined in IFRS 7, Financial Instruments: Disclosures (IFRS 7).

Level 1 – Unadjusted quoted prices at the measurement date for identical assets or liabilities in active markets.

Level 2 – Observable inputs other than quoted prices included in Level 1, such as quoted prices for similar assets and liabilities in active markets; quoted prices for identical or similar assets and liabilities in markets that are not active; or other inputs that are observable or can be corroborated by observable market data.

Level 3 – Unobservable inputs which are supported by little or no market activity.

The following table sets forth the Company's financial assets that are measured at fair value on a recurring basis by level within the fair value hierarchy. As required by IFRS 7, assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement. As of October 1, 2010, September 30, 2011 and December 31, 2011, the Company did not have financial liabilities measured at fair value on a recurring basis.

Khan Resources Inc.
Notes to Unaudited Condensed Consolidated Financial Statements
December 31, 2011
(Expressed in thousands of Canadian dollars, unless otherwise stated)

Financial assets at October 1, 2010	Level 1	Level 2	Level 3	Total
Cash and cash equivalents	\$ 10,860	\$ -	\$ -	\$ 10,860
Available-for-sale financial assets				
Equity securities	3,500	-	-	3,500
Financial assets at fair value through profit and loss				
Trading derivatives (warrants)	-	-	-	-
Total financial assets	\$ 14,360	\$ -	\$ -	\$ 14,360
Financial assets at September 30, 2011	Level 1	Level 2	Level 3	Total
Cash and cash equivalents	\$ 5,627	\$ -	\$ -	\$ 5,627
Available-for-sale financial assets				
Equity securities	2,173	-	-	2,173
Financial assets at fair value through profit and loss				
Trading derivatives (warrants)	-	91	-	91
Total financial assets	\$ 7,800	\$ 91	\$ -	\$ 7,891
Financial assets at December 31, 2011	Level 1	Level 2	Level 3	Total
Cash and cash equivalents	\$ 5,005	\$ -	\$ -	\$ 5,005
Available-for-sale financial assets				
Equity securities	2,096	-	-	2,096
Financial assets at fair value through profit and loss				
Trading derivatives (warrants)	-	56	-	56
Total financial assets	\$ 7,101	\$ 56	\$ -	\$ 7,157

b. Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its short term business requirements. The Company has in place a planning and budgeting process to help determine the funds required to support the Company's normal operating requirements on an ongoing basis and its international arbitration program.

In the normal course of business, the Company enters into contracts that give rise to commitments for future minimum payments (see Note 13).

c. Foreign exchange risk

The Company undertakes transactions denominated in foreign currencies and is exposed to foreign exchange risk arising from such transactions.

The Company conducts its operations in Mongolia and thereby the majority of the Company's assets, liabilities and some expenses are denominated in MNT.

The Company currently does not engage in foreign currency hedging. As at December 31, 2011, with other variables unchanged, a 1% strengthening (weakening) of the MNT against the CAD would have increased (decreased) other comprehensive income by approximately \$150.

d. Interest rate risk

Interest risk is the risk that the fair value or future cash flows of a financial instrument

Khan Resources Inc.
Notes to Unaudited Condensed Consolidated Financial Statements
December 31, 2011
(Expressed in thousands of Canadian dollars, unless otherwise stated)

will fluctuate due to changes in market interest rates. The Company's cash equivalents and short term investments primarily includes highly liquid investments that earn interests at market rates that are fixed to maturity or at variable interest rates. Due to the short-term nature of these financial instruments, fluctuations in market rates do not have significant impact on the fair values of the financial instruments as of December 31, 2011.

e. ***Credit risk***

Credit risk is the risk that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss. The Company is exposed to credit risk primarily associated to accounts receivable, interest receivable, cash and cash equivalents and short term investments. The carrying amount of assets included on the balance sheet represents the maximum credit exposure.

Credit risk is the risk that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss. The Company's primary exposure to credit risk is on its bank accounts and guaranteed investment certificate. Bank accounts are held with major banks in Canada and Mongolia. As the majority of the Company's cash is held by a Canadian bank and the guaranteed investment certificate is also held by the same Canadian bank, there is a concentration of credit risk with one bank in Canada. This risk is managed by using a major bank that is a high credit quality financial institution as determined by rating agencies. The Company's secondary exposure to credit risk is on its accounts receivable. This risk is minimal as accounts receivable consist primarily of refundable government sales taxes.

f. ***Equity price risk***

The Company holds certain equity securities that will fluctuate in value as a result of trading on Canadian financial markets. As the Company's equity securities holding are in mining companies, the value will also fluctuate based on commodity prices. Based upon the Company's portfolio at December 31, 2011, a 10% increase (decrease) in the market price of the securities held, ignoring any foreign currency effects, would have resulted in an increase (decrease) to comprehensive income of approximately \$210.

12. Supplemental cash flow information

	<u>Three months ended December 31,</u>	
	<u>2011</u>	<u>2010</u>
Changes in non-cash working capital related to operations:		
Accounts Receivable	\$ (12)	\$ (11)
Prepaid expenses and other assets	37	84
Accounts Payable and accrued liabilities	<u>(117)</u>	<u>(92)</u>
	<u>\$ (92)</u>	<u>\$ (19)</u>

The Company did not make any cash payments of interest in either of the three months ended

Khan Resources Inc.
Notes to Unaudited Condensed Consolidated Financial Statements
December 31, 2011
(Expressed in thousands of Canadian dollars, unless otherwise stated)

December 31, 2011 and 2010. The Company did make cash payments in the amount of \$2 for taxes withheld by the Government of the Netherlands in both of the three months ended December 31, 2011 and 2010.

13. Commitments and contingencies

The Company has entered into a five-year lease for its head office premises that commenced on March 1, 2006. The lease has been extended until September 2012 essentially under the same terms and conditions. The expected rent for the year is \$95.

14. Transition to IFRS

The Company adopted IFRS effective October 1, 2011 with a transition date of October 1, 2010. This note explains the principal adjustments made by the Company in restating its previous Canadian GAAP consolidated balance sheet as at October 1, 2010 and its previously published Canadian GAAP consolidated financial statements for the three months ended December 31, 2010 and for the year ended September 30, 2011.

a. *First-time adoption exemptions applied*

In preparing these consolidated financial statements in accordance with IFRS 1, the Company has applied certain of the optional exemptions from full retrospective application of IFRS. The optional exemptions applied are described below.

- i. *Business combinations*** – the Company has elected the business combinations exemption in IFRS 1 to not apply IFRS 3, Business Combinations retrospectively to past business combinations. Accordingly, the Company has not restated business combinations that took place prior to the transition date.
- ii. *Cumulative translation differences*** – the Company has elected to set the previously cumulative translation account, which was included in accumulated other comprehensive income, to zero as at the transition date, and absorbed the balance to retained earnings.
- iii. *Share-based payment*** – the Company has elected to not apply IFRS 2, Share-based Payment to equity instruments granted on or before November 7, 2002, or equity instruments that were granted subsequent to November 7, 2002 and vested before the date of transition to IFRS.

Khan Resources Inc.
Notes to Unaudited Condensed Consolidated Financial Statements
December 31, 2011
(Expressed in thousands of Canadian dollars, unless otherwise stated)

b. Reconciliation of equity

The following is a reconciliation of the Company's equity reported in accordance to Canadian GAAP to its equity under IFRS as at the transition date October 1, 2010:

	Canadian GAAP (in USD)	Change in functional currency (Note e. i)	Note	Other IFRS adjustments	IFRS
Assets					
Current					
Cash	\$ 10,554	\$ 10,860		-	\$ 10,860
Accounts receivable	59	61		-	61
Prepaid expenses and other assets	191	201		-	201
Restricted cash	51	52		-	52
	<u>10,855</u>	<u>11,174</u>		<u>-</u>	<u>11,174</u>
Total current assets	10,855	11,174		-	11,174
Investments	3,401	3,500		-	3,500
Plant and equipment	3,828	3,662	e. ii	(1)	3,661
Mineral rights and properties	12,012	12,424		-	12,424
Intangible assets	-	-	e. ii	1	1
	<u>\$ 30,096</u>	<u>\$ 30,760</u>		<u>-</u>	<u>\$ 30,760</u>
Liabilities					
Current					
Accounts payable and accrued liabilities	\$ 409	\$ 422		-	\$ 422
Commitments and contingencies					
Shareholders' Equity					
Share capital	61,184	73,407		-	73,407
Contributed surplus	10,063	11,302	e. iii	(21)	11,281
Accumulated other comprehensive income	1,321	1,306		-	1,306
Cumulative translation adjustment		(3,216)	e. i	3,216	-
Deficit	(42,881)	(52,461)	e. iv	(3,195)	(55,656)
	<u>29,687</u>	<u>30,338</u>		<u>-</u>	<u>30,338</u>
	<u>\$ 30,096</u>	<u>\$ 30,760</u>		<u>-</u>	<u>\$ 30,760</u>

Khan Resources Inc.
Notes to Unaudited Condensed Consolidated Financial Statements
December 31, 2011
(Expressed in thousands of Canadian dollars, unless otherwise stated)

The following is a reconciliation of the Company's equity reported in accordance to Canadian GAAP to its equity under IFRS as at December 31, 2010:

	Canadian GAAP (in USD)	Change in functional currency (Note e. i)	Note	Other IFRS adjustments	IFRS
Assets					
Current					
Cash	\$ 9,441	\$ 9,392		-	\$ 9,392
Accounts receivable	56	55		-	55
Prepaid expenses and other assets	111	117		-	117
Restricted cash	52	52		-	52
	<u>9,660</u>	<u>9,616</u>		<u>-</u>	<u>9,616</u>
Total current assets	9,660	9,616		-	9,616
Investments	8,203	8,159		-	8,159
Plant and equipment	3,764	3,695		-	3,695
Mineral rights and properties	12,099	12,827		-	12,827
Intangible Assets	-	-		-	-
	<u>\$ 33,726</u>	<u>\$ 34,297</u>		<u>-</u>	<u>\$ 34,297</u>
Liabilities					
Current					
Accounts payable and accrued liabilities	\$ 288	\$ 288		-	\$ 288
Commitments and contingencies					
Shareholders' Equity					
Share capital	61,215	73,441		-	73,441
Contributed surplus	10,086	11,325	e. iii	(21)	11,304
Accumulated other comprehensive income	4,984	4,827		-	4,827
Cumulative translation adjustment		393	e. i	-	393
Deficit	<u>(42,847)</u>	<u>(55,977)</u>	e. iii	<u>21</u>	<u>(55,956)</u>
	<u>33,438</u>	<u>34,009</u>		<u>-</u>	<u>34,009</u>
	<u>\$ 33,726</u>	<u>\$ 34,297</u>		<u>-</u>	<u>\$ 34,297</u>

Khan Resources Inc.
Notes to Unaudited Condensed Consolidated Financial Statements
December 31, 2011
(Expressed in thousands of Canadian dollars, unless otherwise stated)

The following is a reconciliation of the Company's equity reported in accordance to Canadian GAAP to its equity under IFRS as at September 30, 2011:

	Canadian GAAP (in USD)	Change in functional currency (Note e. i)	Note	Other IFRS adjustments	IFRS
Assets					
Current					
Cash	\$ 5,656	\$ 5,927		-	\$ 5,927
Accounts receivable	26	28		-	28
Prepaid expenses and other assets	114	115		-	115
Restricted cash	50	52		-	52
	<u>5,846</u>	<u>6,122</u>		<u>-</u>	<u>6,122</u>
Total current assets	5,846	6,122		-	6,122
Investments	2,160	2,264		-	2,264
Plant and equipment	3,630	3,588		-	3,588
Mineral rights and properties	12,165	13,022		-	13,022
Intangible Assets	-	-		-	-
	<u>\$ 23,801</u>	<u>\$ 24,996</u>		<u>-</u>	<u>\$ 24,996</u>
Liabilities					
Current					
Accounts payable and accrued liabilities	\$ 599	\$ 628		-	\$ 628
Commitments and contingencies					
Shareholders' Equity					
Share capital	61,383	73,622		-	73,622
Contributed surplus	10,418	11,642	e. iii	(21)	11,621
Accumulated other comprehensive income	(1,961)	(1,953)		-	(1,953)
Cumulative translation adjustment		558	e. i	-	558
Deficit	<u>(46,638)</u>	<u>(59,501)</u>		<u>21</u>	<u>(59,480)</u>
	<u>23,202</u>	<u>24,368</u>	e. iii	<u>-</u>	<u>24,368</u>
	<u>\$ 23,801</u>	<u>\$ 24,996</u>		<u>-</u>	<u>\$ 24,996</u>

Khan Resources Inc.
Notes to Unaudited Condensed Consolidated Financial Statements
December 31, 2011
(Expressed in thousands of Canadian dollars, unless otherwise stated)

c. **Reconciliation of comprehensive income**

The following is reconciliation of the Company's comprehensive income reported in accordance with Canadian GAAP to its comprehensive income under IFRS for the year ended September 30, 2011:

	Canadian GAAP (in USD)	Change in functional currency (Note e. i)	Note	Other IFRS adjustments	IFRS
Revenue					
Other Income	\$ 282	\$ 277		-	\$ 277
Interest	74	73		-	73
	<u>356</u>	<u>350</u>		<u>-</u>	<u>350</u>
Expenses					
General Corporate	2,784	2,778		-	2,778
Mongolian Operations	412	413		-	413
Amortization	130	126		-	126
Share-based compensation	432	432		-	432
Foreign exchange loss (gain)	(58)	12	e. i	-	12
Loss on investments	213	207		-	207
Loss on sale of assets	2	2		-	2
Write-off assets	3	3		-	3
	<u>3,918</u>	<u>3,973</u>		<u>-</u>	<u>3,973</u>
Income (loss) before income taxes	(3,562)	(3,623)		-	(3,623)
Recovery of Income Taxes	(195)	(201)		-	(201)
Net Income (Loss) for the period	(3,757)	(3,824)		-	(3,824)
Other Comprehensive Income					
Unrealize holding gain (loss) on available for sale securities	(3,471)	(3,453)		-	(3,453)
Future tax recovery (provision)	189	194		-	194
	<u>(3,282)</u>	<u>(3,259)</u>		<u>-</u>	<u>(3,259)</u>
Cumulative Translation Adjustment	-	558	e. i	-	558
Comprehensive income (loss) for the period	\$ (7,039)	\$ (6,525)		-	\$ (6,525)

Khan Resources Inc.
Notes to Unaudited Condensed Consolidated Financial Statements
December 31, 2011
(Expressed in thousands of Canadian dollars, unless otherwise stated)

The following is reconciliation of the Company's comprehensive income reported in accordance with Canadian GAAP to its comprehensive income under IFRS for the quarter ended December 31, 2010:

	Canadian GAAP (in USD)	Change in functional currency (Note e. i)	Note	Other IFRS adjustments	IFRS
Revenue					
Interest	\$ 24	\$ 24		-	\$ 24
	<u>24</u>	<u>24</u>		<u>-</u>	<u>24</u>
Expenses					
General Corporate	555	558		-	558
Mongolian Operations	164	169		-	169
Amortization	37	36		-	36
Share-based compensation	36	37		-	37
Foreign exchange loss (gain)	(283)	23	e. i	-	23
Write-off assets	3	3		-	3
	<u>512</u>	<u>826</u>		<u>-</u>	<u>826</u>
Income (loss) before income taxes	(488)	(802)		-	(802)
Recovery of Income Taxes	522	502		-	502
	<u>34</u>	<u>(300)</u>		<u>-</u>	<u>(300)</u>
Net Income (Loss) for the period					
Other Comprehensive Income					
Unrealized holding gain (loss) on available for sale securities	4,186	4,024		-	4,024
Future tax recovery (provision)	(523)	(503)		-	(503)
	<u>3,663</u>	<u>3,521</u>		<u>-</u>	<u>3,521</u>
Cumulative translation adjustment	-	393	e. i	-	393
	<u>-</u>	<u>393</u>		<u>-</u>	<u>393</u>
Comprehensive income (loss) for the period	<u>\$ 3,697</u>	<u>\$ 3,614</u>		<u>-</u>	<u>\$ 3,914</u>

d. **Statements of cash flows**

The conversion to IFRS did not result in material changes to the statement of cash flows.

e. **Notes to the reconciliations**

Transitional adjustments are made according to the following notes:

i. **Foreign exchange impact on translation**

With the adoption of IFRS, the functional currency of the Canadian head office and all intermediate holding companies changed from USD to CAD. The Company's Mongolian subsidiaries changed their functional currency from the

Khan Resources Inc.
Notes to Unaudited Condensed Consolidated Financial Statements
December 31, 2011
(Expressed in thousands of Canadian dollars, unless otherwise stated)

USD to the MNT. Such change resulted in a foreign exchange difference between the two accounting standards on certain non-monetary assets. These assets were previously translated from MNT to USD by using historical rates (temporal method). However under IFRS, they are translated from MNT to CAD directly by using period end rates (current method). Under Canadian GAAP, exchange differences were recognized in net income whereas under IFRS exchange differences are recognized in other comprehensive income. The Company's share capital has been restated at historic CAD carrying amounts.

ii. *Intangible assets*

Certain specialized mining computer software recognized as a tangible asset under Canadian GAAP has been identified as an intangible asset under IFRS. At transition the acquisition cost of \$12 had been depreciated to a carrying amount of \$1 and was fully depreciated by December 31, 2011.

iii. *Share-based compensation*

In accordance with IFRS transitional provisions, the company elected to apply IFRS relating to share-based payments retrospectively to outstanding stock options that had not vested prior to the transition date. This resulted in an adjustment of \$21 relating to a small number of stock options that had not vested by October 1, 2010.

iv. *Cumulative translation difference*

The Company has elected to eliminate its cumulative translation difference that existed at the date of transition to IFRS. Cumulative translation difference of \$3,216 was reclassified from accumulated other comprehensive income to retained earnings.