



**CONSOLIDATED FINANCIAL STATEMENTS**  
**June 30, 2010**  
**(Unaudited)**

NOTICE OF AUDITOR'S REVIEW OF  
INTERIM CONSOLIDATED 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 an auditor has not reviewed the financial statements.

The accompanying unaudited financial statements of the Company have been prepared by and are the responsibility of the Company's management.

The Company's independent auditor has not performed a review of these financial statements in accordance with standards established by the Canadian Institute of Chartered Accountants for a review of interim financial statements by an entity's auditor.

**TIMMINS GOLD CORP.**  
**CONSOLIDATED BALANCE SHEETS**  
(in Canadian dollars)

|  | June 30, 2010<br>(Unaudited) | March 31, 2010<br>(Audited) |
|--|------------------------------|-----------------------------|
| <b><u>ASSETS</u></b>                                 |                              |                             |
| <b>Current</b>                                       |                              |                             |
| Cash and cash equivalents                            | \$ 5,364,079                 | \$ 2,694,825                |
| Accounts receivable (Note 3)                         | 7,448,183                    | 6,319,583                   |
| Inventory (Note 4)                                   | 8,190,866                    | 6,420,154                   |
| Prepaid expenses                                     | 527,730                      | 655,704                     |
| Due from related party (Note 7)                      | 79,200                       | 92,656                      |
|  | <u>21,610,058</u>            | <u>16,182,922</u>           |
| <b>Equipment</b> (Note 5)                            | 25,155,762                   | 24,397,467                  |
| <b>Resource properties</b> (Note 6)                  | <u>43,153,726</u>            | <u>41,698,893</u>           |
|  | <u>\$ 89,919,546</u>         | <u>\$ 82,279,282</u>        |
| <b>Current</b>                                       |                              |                             |
| Accounts payable and accrued liabilities             | \$ 5,362,420                 | \$ 4,403,822                |
| Vendor loan (Note 5)                                 | 1,808,490                    | 1,758,120                   |
| Current portion of long-term debt (Note 10)          | 15,789,046                   | 8,045,163                   |
|  | <u>22,959,956</u>            | <u>14,207,105</u>           |
| <b>Future income tax</b>                             | 3,947,011                    | 3,967,061                   |
| <b>Long term debt</b> (Note 10)                      | 5,285,469                    | 8,088,563                   |
| <b>Other long term liabilities</b>                   | 1,082,605                    | 1,035,590                   |
| <b>Asset retirement obligation</b> (Note 9)          | 972,210                      | 929,382                     |
|  | <u>34,247,251</u>            | <u>28,227,701</u>           |
| <b>Shareholders' equity</b>                          |                              |                             |
| Share capital (Note 8)                               | 58,705,648                   | 52,271,066                  |
| Convertible preference shares (Note 8)               | 13,586,780                   | 13,586,780                  |
| Warrants (Note 8)                                    | 1,745,449                    | 2,876,305                   |
| Contributed surplus (Note 8)                         | 4,180,910                    | 3,773,765                   |
| Deficit  | (22,546,492)                 | (18,456,335)                |
|  | <u>55,672,295</u>            | <u>54,051,581</u>           |
|  | <u>\$ 89,919,546</u>         | <u>\$ 82,279,282</u>        |
| <b>Nature and continuance of operations</b> (Note 1) |                              |                             |
| <b>Commitments and contingencies</b> (Note 13)       |                              |                             |
| <b>Subsequent events</b> (Note 15)                   |                              |                             |

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

**TIMMINS GOLD CORP.****CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE LOSS**

(Unaudited in Canadian dollars, except for per share amounts)

|  | <b>Three months ended June 30,</b> |              |
|--|------------------------------------|--------------|
|  | <b>2010</b>                        | <b>2009</b>  |
| <b>Metal Revenues</b>  | \$ 14,332,597                      | \$ -         |
| <b>Expenses:</b>   |                                    |              |
| Cost of sales  | 10,845,997                         | -            |
| Amortization and depreciation  | 1,215,903                          | 15,560       |
| Asset write down   | 2,652                              | -            |
| Corporate and administrative   | 773,524                            | 1,187,167    |
| Accretion of reclamation liability                                       | 30,741                             | 3,621        |
| Stock-based compensation (Note 8)  | 553,013                            | 49,023       |
| <b>Income (Loss) From Operations</b>                                     | 910,767                            | (1,255,371)  |
| <b>Other Income / (Expenses):</b>  |                                    |              |
| Other income / (expenses)  | 6,060                              | 820          |
| Interest expense, net  | (2,477,272)                        | (67,190)     |
| Foreign exchange gain / (loss)   | 70,033                             | 517,411      |
| Loss on embedded derivatives   | (2,599,745)                        | -            |
| <b>Income (loss) before taxes</b>  | (4,090,157)                        | (804,330)    |
| Income tax expense   | -                                  | -            |
| <b>Net income (loss) and comprehensive income (loss) for the period</b>  | \$ (4,090,157)                     | \$ (804,330) |
| <b>Loss per share – basic and diluted</b>                                | \$ (0.03)                          | \$ (0.01)    |
| <b>Weighted average number of shares outstanding – basic and diluted</b> | 130,934,846                        | 80,033,913   |

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

**TIMMINS GOLD CORP.**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(Unaudited in Canadian dollars)

|   | <b>Three months ended June 30,</b> |                     |
|---|------------------------------------|---------------------|
|   | <b>2010</b>                        | <b>2009</b>         |
| <b>CASH FLOWS TO OPERATING ACTIVITIES</b>                               |                                    |                     |
| Loss for the year   | \$ (4,090,157)                     | \$ (804,330)        |
| Items not affecting cash:   |                                    |                     |
| Accretion of reclamation liability                                      | 30,741                             | 3,621               |
| Accretion of vendor loan  | -                                  | 67,190              |
| Amortization of equipment   | 1,215,903                          | 15,560              |
| Accrued interest on long-term debt                                      | 2,412,015                          | -                   |
| Loss on embedded derivative   | 2,599,745                          | -                   |
| Stock-based compensation  | 553,013                            | 49,023              |
| Unrealized foreign exchange gain  | 16,091                             | (426,989)           |
| Asset write downs   | 2,652                              | -                   |
|   | <u>2,740,003</u>                   | <u>(1,095,925)</u>  |
| Changes in non-cash working capital items:                              |                                    |                     |
| Accounts receivable   | (1,126,239)                        | (307,665)           |
| Inventory   | (1,770,712)                        | -                   |
| Prepaid expenses  | (185,603)                          | 35,531              |
| Accounts payable and accrued liabilities                                | 934,105                            | 1,078,492           |
| Due from related parties  | 13,456                             | (34,549)            |
|   | <u>605,010</u>                     | <u>(324,116)</u>    |
| Cash flows provided by (used) in operating activities                   |                                    |                     |
|   | <u>605,010</u>                     | <u>(324,116)</u>    |
| <b>CASH FLOWS PROVIDED (USED) BY FINANCING ACTIVITIES</b>               |                                    |                     |
| Shares issued for cash  | 5,157,857                          | 12,745,024          |
| Share issue costs   | -                                  | (625,056)           |
|   | <u>5,157,857</u>                   | <u>12,119,968</u>   |
| Cash flows provided by financing activities                             |                                    |                     |
|   | <u>5,157,857</u>                   | <u>12,119,968</u>   |
| <b>CASH FLOWS USED BY INVESTING ACTIVITIES</b>                          |                                    |                     |
| Purchase of equipment   | (1,335,037)                        | (2,680,436)         |
| Expenditures on resource properties                                     | (1,758,576)                        | (1,745,193)         |
|   | <u>(3,093,613)</u>                 | <u>(4,425,629)</u>  |
| Cash flows used in investing activities                                 |                                    |                     |
|   | <u>(3,093,613)</u>                 | <u>(4,425,629)</u>  |
| <b>Increase (decrease) in cash and cash equivalents during the year</b> | <u>2,669,254</u>                   | <u>7,370,223</u>    |
| <b>Cash and cash equivalents, beginning of year</b>                     | <u>2,694,825</u>                   | <u>700,104</u>      |
| <b>Cash and cash equivalents, end of year</b>                           | <u>\$ 5,364,079</u>                | <u>\$ 8,070,327</u> |

Supplemental disclosure with respect to cash flows (Note 11)

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

**TIMMINS GOLD CORP.**  
**CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY**  
(Unaudited in Canadian dollars)

|  | Number<br>of Common<br>Shares | Amount              | Number of<br>Convertible<br>Preference<br>Shares | Amount              | Warrants           | Contributed<br>Surplus | Deficit               | Total<br>Shareholders'<br>Equity |
|--|-------------------------------|---------------------|--|---------------------|--------------------|------------------------|-----------------------|----------------------------------|
| <b>Balance, March 31, 2009</b>                           | <b>71,730,454</b>             | <b>\$33,915,729</b> | <b>11,000,000</b>                                | <b>\$13,586,780</b> | <b>\$430,400</b>   | <b>\$3,179,625</b>     | <b>\$(9,840,415)</b>  | <b>\$ 41,272,119</b>             |
| Issued:  |                               |                     |  |                     |                    |                        |                       |                                  |
| Pursuant to private placement (Note 8a)                  | 5,989,500                     | 2,021,008           | -  | -                   | 374,792            | -                      | -                     | 2,395,800                        |
| Pursuant to private placement (Note 8b)                  | 25,873,060                    | 8,359,450           | -  | -                   | 1,989,774          | -                      | -                     | 10,349,224                       |
| Pursuant to exercised options (Note 8c)                  | 775,000                       | 833,370             | -  | -                   | -                  | (377,120)              | -                     | 456,250                          |
| Pursuant to exercised warrants (Note 8d)                 | 10,703,500                    | 7,764,026           | -  | -                   | (1,341,926)        | -                      | -                     | 6,422,100                        |
| Share issue costs (Notes 8a and b)                       | -                             | (769,542)           | -  | -                   | (175,146)          | -                      | -                     | (944,688)                        |
| Warrants issued on financing (Note 10)                   | -                             | -                   | -  | -                   | 1,745,436          | -                      | -                     | 1,745,436                        |
| Reclassification of warrants exercised in<br>prior years | -                             | 147,025             | -  | -                   | (147,025)          | -                      | -                     | -                                |
| Stock-based compensation                                 | -                             | -                   | -  | -                   | -                  | 971,260                | -                     | 971,260                          |
| Net loss   | -                             | -                   | -  | -                   | -                  | -                      | (8,615,920)           | (8,615,920)                      |
| <b>Balance, March 31, 2010</b>                           | <b>115,071,514</b>            | <b>52,271,066</b>   | <b>11,000,000</b>                                | <b>13,586,780</b>   | <b>2,876,305</b>   | <b>3,773,765</b>       | <b>(18,456,335)</b>   | <b>54,051,581</b>                |
| Issued:  |                               |                     |  |                     |                    |                        |                       |                                  |
| Pursuant to exercised options (Note 8e)                  | 200,000                       | 292,118             | -  | -                   | -                  | (145,868)              | -                     | 146,250                          |
| Pursuant to exercised warrants (Note 8f)                 | 8,352,680                     | 6,142,464           | -  | -                   | (1,130,856)        | -                      | -                     | 5,011,608                        |
| Stock-based compensation                                 | -                             | -                   | -  | -                   | -                  | 553,013                | -                     | 553,013                          |
| Net loss   | -                             | -                   | -  | -                   | -                  | -                      | (4,090,157)           | (4,090,157)                      |
| <b>Balance, June 30, 2010</b>                            | <b>123,624,194</b>            | <b>\$58,705,648</b> | <b>11,000,000</b>                                | <b>\$13,586,780</b> | <b>\$1,745,449</b> | <b>\$4,180,910</b>     | <b>\$(22,546,492)</b> | <b>\$55,672,295</b>              |

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

## **TIMMINS GOLD CORP.**

(A Production and Exploration Stage Company)

### **NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

June 30, 2010

(Unaudited in Canadian dollars, except for number of options and per share amounts)

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#### **1. NATURE AND CONTINUANCE OF OPERATIONS**

Timmins Gold Corp. (the "Company") was incorporated on March 17, 2005 under the laws of the Province of British Columbia. The Company is in the business of acquiring, exploring and developing and operating mineral resource properties in Mexico, through its wholly-owned subsidiaries, Timmins Goldcorp Mexico, S.A. de C.V and Molimentales del Noroeste, S.A. de C.V. ("MdN") (collectively the "Subsidiary"). MdN owns the San Francisco Mine which was placed into commercial production on April 1, 2010. The Company is listed for trading on the TSX Venture Exchange. The recovery of the Company's investment in its resource properties is dependent upon sale of mineral products produced from these properties, the possible sale of any of its resource properties and the ability to raise sufficient capital to continue to explore, develop and operate these properties at a profit.

These unaudited interim financial statements have been prepared by the Company in accordance with Canadian generally accepted accounting principles ("GAAP"). The preparation of financial data is based on accounting principles and practices consistent with those used in the preparation of the audited annual financial statements. These unaudited interim financial statements do not include in all respects the annual disclosure requirements of GAAP and should be read in conjunction with the most recent audited annual statements.

These consolidated financial statements have been prepared assuming the Company will continue on a going-concern basis. The Company has incurred losses since inception and the ability of the Company to continue as a going-concern depends upon its ability to achieve profitable operations or to continue to raise adequate financing.

#### **2. CHANGES IN ACCOUNTING POLICY AND PRESENTATION**

##### **Reclassification**

The comparative financial statements have been reclassified to conform to the presentation of the current year financial statements.

##### **New accounting pronouncements**

CICA has issued new standards which may affect the financial disclosures and results of operations of the Company. The Company will adopt the requirements on the date specified in each respective section and is considering the impact this will have on the consolidated financial statements.

##### **a) Business combinations, consolidated financial statements and non-controlling interests**

CICA sections 1582, 1601 and 1602 replace the former CICA 1581, Business Combinations and CICA 1600, Consolidated Financial Statements and establish a new section for accounting for a non-controlling interest in a subsidiary. CICA 1582 is effective for business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after January 1, 2011. CICA 1601 and CICA 1602 apply to interim and annual consolidated financial statements relating to years beginning on or after January 1, 2011.

##### **b) Comprehensive revaluation of assets and liabilities**

In August 2009, the CICA amended Section 1625, Comprehensive revaluation of assets and liabilities. This section has been amended as a result of issuing Business combinations, Section 1582, Consolidated financial statements, Section 1601, and Non-controlling interests, Section 1602, in January 2009. The amendments apply prospectively to comprehensive revaluations of assets and liabilities occurring in fiscal years beginning on or after January 1, 2011. Earlier adoption is permitted as of the beginning of a fiscal year. If the Company adopts this section for a fiscal year beginning before January 1, 2011, it also adopts Section 1582. The adoption of this standard is not expected to have a material impact on the Company's results of operations or its financial position.

**TIMMINS GOLD CORP.**

(A Production and Exploration Stage Company)

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

June 30, 2010

(Unaudited in Canadian dollars, except for number of options and per share amounts)

**3. CHANGES IN ACCOUNTING POLICY AND PRESENTATION (continued)****c) International Financial Reporting Standards (“IFRS”)**

In February 2008, the Canadian Accounting Standards Board confirmed that publicly accountable enterprises will be required to adopt IFRS for fiscal years beginning on or after January 1, 2011, with earlier adoption permitted. Accordingly, the conversion to IFRS will be applicable to the Company’s reporting no later than in the first quarter of 2011, with restatement of comparative information presented. The conversion to IFRS will impact the Company’s accounting policies, information technology and data systems, internal control over financial reporting, and disclosure controls and procedures. The transition may also impact business activities, such as foreign currency activities, certain contractual arrangements, capital requirements and compensation arrangements. The Company is currently evaluating the future impact of IFRS on its financial statements and will continue to invest in training and additional resources to ensure a timely conversion.

**4. ACCOUNTS RECEIVABLE**

|                                 | June 30, 2010       | March 31, 2010      |
|---------------------------------|---------------------|---------------------|
| Accounts receivable- Gold sales | \$ 3,995,224        | \$ 2,525,135        |
| Taxes receivable                | 3,352,533           | 3,458,079           |
| Other                           | 100,426             | 336,369             |
|                                 | <u>\$ 7,448,183</u> | <u>\$ 6,319,583</u> |

Taxes receivable are IVA payments made by the Company, which in Mexico, are refundable.

**5. INVENTORY**

The major components of the Company’s inventory accounts at June 30 and March 31, 2010 are as follows:

|                        | June 30, 2010       | March 31, 2010      |
|------------------------|---------------------|---------------------|
| Gold in-process        | \$ 5,621,426        | \$ 4,056,326        |
| Materials and supplies | 2,569,440           | 2,363,828           |
|                        | <u>\$ 8,190,866</u> | <u>\$ 6,420,154</u> |

Cost of goods sold was comprised of the following:

|                                  | <b>Three months ended</b>   |
|----------------------------------|-----------------------------|
|                                  | <b><u>June 30, 2010</u></b> |
| Costs of mining                  | \$ 9,169,463                |
| Crushing and gold recovery costs | 2,307,180                   |
| Administration costs             | 396,227                     |
| Other costs                      | 500,568                     |
| Transport and refining           | 37,659                      |
| Net change in Inventory          | <u>(1,565,100)</u>          |
|                                  | <u>\$ 10,845,997</u>        |

**TIMMINS GOLD CORP.**

(A Production and Exploration Stage Company)

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

June 30, 2010

(Unaudited in Canadian dollars, except for number of options and per share amounts)

**6. EQUIPMENT**

|                                   | June 30, 2010        |                             |                      | March 31, 2010      |                             |                     |
|-----------------------------------|----------------------|-----------------------------|----------------------|---------------------|-----------------------------|---------------------|
|                                   | Cost                 | Accumulated<br>Amortization | Net<br>Book Value    | Cost                | Accumulated<br>Amortization | Net<br>Book Value   |
| Computer equipment                | \$ 309,600           | \$ 122,548                  | \$ 187,053           | \$ 249,097          | \$ 105,932                  | \$ 143,165          |
| Machinery and equipment           | 20,975,374           | 543,149                     | 20,432,225           | 19,784,186          | 29,931                      | 19,754,255          |
| Leasehold improvements            | 8,259                | 6,194                       | 2,065                | 8,259               | 5,781                       | 2,478               |
| Mine equipment and<br>buildings   | 3,832,497            | 3,846                       | 3,828,651            | 3,794,602           | -                           | 3,794,602           |
| Office furniture and<br>equipment | 356,666              | 57,893                      | 298,774              | 325,595             | 49,894                      | 275,701             |
| Vehicles                          | 613,121              | 206,126                     | 406,995              | 598,743             | 171,477                     | 427,266             |
|                                   | <u>\$ 26,095,517</u> | <u>\$ 939,756</u>           | <u>\$ 25,155,762</u> | <u>\$24,760,482</u> | <u>\$ 363,015</u>           | <u>\$24,397,467</u> |

Under the San Francisco Property Acquisition Agreement, the Company was required to purchase certain mine equipment and buildings from the vendor for US \$4,025,000 (or \$4,237,200). Originally, payment for the mine equipment and buildings was to be made at any time prior to March 11, 2010, without interest. Therefore to March 31, 2010, the full acquisition price of the US dollar denominated debt had been discounted at an annualized rate of 6.775% to reflect the implied interest rate. The final payment on this obligation in the amount of US \$1,730,774 (or Canadian \$1,808,490) is expected to be paid by December 2010.

**TIMMINS GOLD CORP.**

(A Production and Exploration Stage Company)

**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**

June 30, 2010

(Unaudited in Canadian dollars, except for number of options and per share amounts)

**6. RESOURCE PROPERTIES**

|  | March 31, 2009    | Additions         | March 31, 2010    | Additions        | June 30, 2010     |
|--|-------------------|-------------------|-------------------|------------------|-------------------|
| <b>San Francisco Property (Note 6a)</b>    |                   |                   |                   |                  |                   |
| Acquisition cost                           | \$ 18,361,027     | \$ 3,030,569      | \$ 21,391,596     | \$ (23,733)      | \$ 21,367,863     |
| Claim staking                              | 40,684            | 431               | 41,115            | -                | 41,115            |
| Mining taxes and assessments               | 354,373           | 70,281            | 424,654           | -                | 424,654           |
| Surface rights                             | 135,534           | -                 | 135,534           | -                | 135,534           |
| <i>Total acquisition and holding costs</i> | <u>18,891,618</u> | <u>3,101,281</u>  | <u>21,992,899</u> | <u>(23,733)</u>  | <u>21,969,166</u> |
| Administration                             | 2,836             | -                 | 2,836             | -                | 2,836             |
| Assays                                     | 330,638           | 9,310             | 339,948           | 134,381          | 474,329           |
| Camp and field costs                       | 89,569            | 32,864            | 122,433           | 10,108           | 132,541           |
| Communication                              | 13,531            | -                 | 13,531            | -                | 13,531            |
| Drilling                                   | 1,602,935         | 1,054,802         | 2,657,737         | 1,020,627        | 3,678,364         |
| Engineering and feasibility                | 113,010           | 33,152            | 146,162           | -                | 146,162           |
| Development expenditures                   | 3,694,816         | 5,821,768         | 9,516,584         | (283,961)        | 9,232,623         |
| Field work and geological consulting       | 887,356           | 87,516            | 974,872           | 61,125           | 1,035,997         |
| Geophysics and metallurgy                  | 79,486            | 19,040            | 98,526            | -                | 98,526            |
| Legal and filing fees                      | 315,137           | -                 | 315,137           | -                | 315,137           |
| Miscellaneous exploration expenses         | 426,484           | 172,314           | 598,798           | 159,630          | 758,428           |
| Pre-feasibility expenses                   | 353,815           | -                 | 353,815           | -                | 353,815           |
| Property investigation                     | 11,216            | 8,576             | 19,792            | -                | 19,792            |
| Reports, drafting and maps                 | 20,823            | 3,260             | 24,083            | 569              | 24,652            |
| Travel and accommodation                   | 213,691           | 17,641            | 231,332           | 3,007            | 234,339           |
| Salaries and consulting fees               | 1,516,427         | 622,769           | 2,139,196         | 239,020          | 2,378,216         |
| <i>Deferred exploration costs</i>          | <u>9,671,770</u>  | <u>7,883,012</u>  | <u>17,554,782</u> | <u>1,344,506</u> | <u>18,899,288</u> |
| Total acquisition and exploration costs    | <u>28,563,388</u> | <u>10,984,293</u> | <u>39,547,681</u> | <u>1,320,773</u> | <u>40,868,454</u> |
| <b>El Capomo Property (Note 6c)</b>        |                   |                   |                   |                  |                   |
| Assaying                                   | 14,292            | -                 | 14,292            | -                | 14,292            |
| Claim staking                              | 18,512            | -                 | 18,512            | -                | 18,512            |
| Camp and accommodation                     | 11,464            | -                 | 11,464            | 32               | 11,496            |
| Geophysics and metallurgy                  | -                 | 2,169             | 2,169             | -                | 2,169             |
| Mining taxes                               | 54,902            | 70,595            | 125,497           | -                | 125,497           |
| Miscellaneous exploration expenses         | 27,263            | -                 | 27,263            | 91               | 27,354            |
| Salaries and consulting fees               | 185,711           | 26,222            | 211,933           | 2,677            | 214,610           |
| Travel                                     | 1,400             | 213               | 1,613             | -                | 1,613             |
| Total acquisition and exploration costs    | <u>313,544</u>    | <u>99,199</u>     | <u>412,743</u>    | <u>2,800</u>     | <u>415,543</u>    |
| <b>Cocula Property (Note 6d)</b>           |                   |                   |                   |                  |                   |
| Acquisition cost                           | 146,315           | 197,384           | 343,699           | -                | 343,699           |
| Assay                                      | 154,189           | -                 | 154,189           | 14,066           | 168,255           |
| Camp and accommodation                     | 16,646            | 4,869             | 21,515            | 5,780            | 27,295            |
| Drafting and reporting                     | 960               | 183               | 1,143             | 86               | 1,232             |
| Drilling                                   | 121,559           | -                 | 121,559           | -                | 121,559           |
| Field work and geological consulting       | 6,121             | -                 | 6,121             | -                | 6,121             |
| Geophysics and metallurgy                  | 8,476             | 1,433             | 9,909             | 5,116            | 15,025            |
| Mining taxes                               | 30,733            | 4,269             | 35,098            | -                | 35,098            |
| Miscellaneous exploration expenses         | 42,160            | 3,730             | 45,794            | 4,225            | 50,019            |
| Salaries and consulting fees               | 304,126           | 65,696            | 369,822           | 9,834            | 379,565           |
| Travel                                     | 4,401             | 379               | 4,780             | 312              | 5,091             |
| Trenching and road work                    | 21,004            | -                 | 21,004            | -                | 21,004            |
| Total acquisition and exploration costs    | <u>856,690</u>    | <u>277,943</u>    | <u>1,134,633</u>  | <u>39,419</u>    | <u>1,174,052</u>  |

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**6. RESOURCE PROPERTIES (continued)**

|   | March 31, 2009       | Additions            | March 31, 2010       | Additions           | June 30, 2010        |
|---|----------------------|----------------------|----------------------|---------------------|----------------------|
| <b>El Picacho Property (Note 6e)</b>    |                      |                      |                      |                     |                      |
| Acquisition cost                        | 46,122               | 30,161               | 76,283               | 13,270              | 89,553               |
| Assay                                   | 11,728               | -                    | 11,728               | -                   | 11,728               |
| Camp and accommodation                  | 139                  | 36                   | 175                  | 145                 | 320                  |
| Geophysics and metallurgy               | -                    | 160                  | 160                  | 3,769               | 3,929                |
| Mining taxes                            | 36,918               | 17,557               | 54,475               | -                   | 54,475               |
| Miscellaneous exploration expenses      | 1,234                | 106                  | 1,340                | 157                 | 1,497                |
| Salaries and consulting fees            | 20,267               | 10,202               | 30,469               | 4,717               | 35,186               |
| Total acquisition and exploration costs | 116,408              | 58,222               | 174,630              | 22,058              | 196,688              |
| <b>Other Properties (Note 6f)</b>       |                      |                      |                      |                     |                      |
| Assay                                   | -                    | -                    | -                    | 17,428              | 17,428               |
| Claim staking                           | 9,733                | -                    | 9,733                | -                   | 9,733                |
| Camp and accommodation                  | 1,872                | 7,908                | 9,780                | 5,396               | 15,176               |
| Drafting and reporting                  | -                    | 496                  | 496                  | 18                  | 514                  |
| Engineering and feasibility             | -                    | 5,624                | 5,624                | -                   | 5,624                |
| Exploration expenses                    | 3,194                | 18,833               | 22,027               | 5,481               | 27,508               |
| Geophysics and metallurgy               | -                    | 28,495               | 28,495               | -                   | 28,495               |
| Mining taxes                            | 49,415               | 85,539               | 134,954              | 76                  | 135,030              |
| Salaries and consulting fees            | 59,180               | 153,083              | 212,263              | 37,816              | 250,079              |
| Travel                                  | 1,656                | 4,178                | 5,834                | 3,568               | 9,402                |
| Total acquisition and exploration costs | 125,050              | 304,156              | 429,206              | 69,783              | 498,989              |
| <b>Total property expenditures</b>      | <b>\$ 31,559,088</b> | <b>\$ 10,139,805</b> | <b>\$ 41,698,893</b> | <b>\$ 1,454,833</b> | <b>\$ 43,153,726</b> |

**a) San Francisco Property**

The Company has title to the Timmins and Timmins II concessions and the Timmins III fraction 1 and 2. These concessions are located in Santa Ana, Sonora, Mexico and are included in the San Francisco Property.

**b) El Capomo Property**

The Company has acquired the mineral rights to four claim blocks by staking the Capomo Property in Nayarit, Mexico.

**c) Cocula Property**

On July 18, 2007, the Company finalized the option agreement to acquire the Cocula Property in Jalisco, Mexico. The terms of the option agreement require the Company to pay a total of US\$1,500,000 over four years, as follows:

US\$50,000 on signing the option agreement (paid);

US\$50,000 on or before January 18, 2008 (paid)

US\$50,000 on or before July 18, 2008 (paid);

US\$75,000 on or before June 15, 2009 (paid);

US\$75,000 on or before September 15, 2009 (paid);

US\$123,437 was paid in July 2010, and US \$26,563 is due in September 2010; and

US\$1,050,000 on or before July 18, 2011.

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#### **6. RESOURCE PROPERTIES (continued)**

##### **d) El Picacho Property**

On December 11, 2007, the Company entered into an exploration agreement with the option to acquire a 100% interest in the 11 mining properties that comprise the Picacho Project in Sonora, Mexico. The agreement requires the Company to pay the vendor a total of US\$1,500,000 over four years, as follows:

US\$15,000 on signing the option agreement (paid);  
US\$15,000 on June 11, 2008 (paid);  
US\$15,000 on December 11, 2008 (paid);  
US\$15,000 on June 11, 2009 (paid);  
US\$15,000 on December 11, 2009 (paid);  
US\$15,000 on June 11, 2010 (paid);  
US\$15,000 on December 11, 2010, and  
US\$1,395,000 on December 11, 2011.

The vendor will retain a 1.5% net smelter return interest, which is limited to US\$1,500,000. The vendor is obligated to sell or transfer to the Company his right to the royalty at any time, upon the Company's request, for which the Company will pay US\$500,000 for every half per cent (0.50%), to a maximum of US\$1,500,000.

The Company has also staked an additional 6,500 hectares encompassing the claims and now controls over 7,200 hectares in the Picacho area.

##### **f) Other Properties**

The Company has received title to the Santa Maria del Oro claim in Jalisco, and the Patricia and Norma concessions in the Municipality of Trincheras, Sonora, Mexico.

#### **7. RELATED PARTY TRANSACTIONS**

During the period ended June 30, 2010, the Company entered into the following transactions with related parties:

- a) The Company incurred \$89,646 (2009 - \$45,129) of consulting fees, including geological to directors and officers of the Company. As of June 30, 2010, \$3,054 (March 31, 2010 - \$3,469) was advanced to these directors and officers.
- b) The Company incurred \$Nil (2009 - \$34,547) for rent and administrative expenses on behalf of a company with directors in common. As of June 30, 2010, \$79,200 (March 31, 2010 - \$92,656) was due from this company.
- c) The Company advanced \$1,198,056 (2009 - \$579,638) to a nominee company incorporated in Mexico. As of June 30, 2010, \$ 120,136 (March 31, 2010 - \$116,866) was advanced to this company. These funds were used to pay the salaries of the Company's Mexican employees as they are employees of this nominee company.

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

#### **8. SHARE CAPITAL AND CONTRIBUTED SURPLUS**

Authorized: unlimited number of common shares without par value

unlimited number of convertible preference shares without par value, with the same rights as the common shares on dissolution and similar events. These shares have no voting rights and are not entitled to dividend payments.

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- a) On April 21, 2009, the Company closed the second tranche of the private placement. This tranche consisted of 5,989,500 units at a price of \$0.40 per unit, for gross proceeds of \$2,395,800. Each unit consisted of one common share and one-half of one share purchase warrant. Each whole warrant entitles the holder to purchase an additional common share at an exercise price of \$0.60 per share until April 21, 2010. A fair value of \$374,792 was assigned to the warrants and was determined using the Black-Scholes. The assumptions used were a risk-free interest rate of 0.98%, an expected life of one year, annualized volatility of 120%, and a dividend rate of 0%. The Company incurred expenses of \$207,514 related to this offering.
- b) On June 17, 2009, the Company closed the third tranche of the non-brokered private placement. This tranche consisted of 25,873,060 units at a price of \$0.40 per unit, for gross proceeds of \$10,349,224. Each unit consisted of one common share and one-half of one share purchase warrant. Each whole warrant entitles the holder to purchase an additional common share at an exercise price of \$0.60 per share until June 17, 2010. A fair value of \$1,989,774 was assigned to the warrants and was determined using the Black-Scholes. The assumptions used were a risk-free interest rate of 1.27%, an expected life of one year, annualized volatility of 125%, and a dividend rate of 0%. The Company incurred expenses of \$737,174 related to this offering..
- c) During the year ended March 31, 2010, 775,000 options were exercised at prices ranging from \$0.55 to \$0.70. A fair value of \$377,120 was transferred from contributed surplus.
- d) During the year ended March 31, 2010, 10,703,500 warrants were exercised at a price of \$0.60. A fair value of \$1,341,926 was transferred to share capital.
- e) During the quarter ended June 30, 2010, 200,000 options were exercised at prices ranging from \$0.55 to \$1.00. A fair value of \$145,868 was transferred from contributed surplus.
- f) During the quarter ended June 30, 2010, 8,352,680 warrants were exercised at a price of \$0.60. A fair value of \$1,130,856 was transferred to share capital.

**Options**

The Company has an incentive stock option plan in place under which it is authorized to grant options to executive officers, directors, employees and consultants. The Company at no time may have more than 10% of the outstanding issued common shares reserved for incentive stock options granted to any one individual. Options granted under the plan will have a term not to exceed five years, have an exercise price not less than the Discounted Market Price as defined by the TSX Corporate Finance Manual and vest over a period of twelve months.

Stock option transactions and the number of stock options outstanding are summarized as follows:

|                             | Shares    | Weighted Average<br>Exercise Price |
|-----------------------------|-----------|------------------------------------|
| Outstanding, March 31, 2009 | 6,262,500 | \$ 0.62                            |
| Granted                     | 2,800,000 | 1.00                               |
| Exercised                   | (775,000) | 0.59                               |
| Expired                     | (337,500) | 0.50                               |
| Outstanding, March 31, 2010 | 7,950,000 | 0.77                               |
| Exercised                   | 200,000   | 0.73                               |
| Expired                     | 430,000   | 0.88                               |
| Outstanding, June 30, 2010  | 7,320,000 | \$ 0.76                            |
| Vested, March 31, 2010      | 5,932,500 | \$ 0.70                            |

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Stock options outstanding at June 30, 2010 are as follows:

| Number of Options Outstanding | Number of Options Exercisable | Exercise Price | Expiry Date       |
|-------------------------------|-------------------------------|----------------|-------------------|
| 300,000                       | 300,000                       | \$ 0.55        | December 31, 2010 |
| 1,170,000                     | 1,170,000                     | \$ 0.35        | July 25, 2011     |
| 1,650,000                     | 1,650,000                     | \$ 0.70        | May 11, 2012*     |
| 100,000                       | 100,000                       | \$ 0.50        | July 18, 2012     |
| 1,325,000                     | 1,325,000                     | \$ 0.75        | November 27, 2012 |
| 2,475,000                     | 1,237,500                     | \$ 1.00        | November 13, 2014 |
| 300,000                       | 150,000                       | \$ 1.00        | November 27, 2014 |
| 7,320,000                     | 5,932,500                     |                |                   |

\* These options were partially exercised after June 30, 2010 (See Note 15).

**Warrants**

Warrant transactions and the number of warrants outstanding are summarized as follows:

|                             | Number of Warrants | Weighted Average Exercise Price |
|-----------------------------|--------------------|---------------------------------|
| Outstanding, March 31, 2009 | 3,125,000          | \$ 0.60                         |
| Issued (Notes 8a,b and 10)  | 18,931,280         | 0.63                            |
| Exercised (Note 8d)         | (10,703,500)       | 0.60                            |
| Outstanding, March 31, 2010 | 11,352,780         | 0.65                            |
| Exercised (Note 8f)         | 8,352,680          | 0.60                            |
| Expired                     | 100                | 0.60                            |
| Outstanding, June 30, 2010  | 3,000,000          | \$ 0.80                         |

Warrants outstanding at June 30, 2010 are as follows:

| Number of Warrants | Exercise Price | Expiry Date      |
|--------------------|----------------|------------------|
| 3,000,000          | \$ 0.80        | January 26, 2012 |
| 3,000,000          |                |                  |

**Stock-based compensation**

The total fair value of stock options recognized as an expense during the period ended June 30, 2010 was \$553,013 (2009 - \$49,023). There were no option grants in the quarter ended June 30, 2010.

The following assumptions were used for the Black-Scholes valuation of stock options and agents' compensation options granted:

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**8. SHARE CAPITAL AND CONTRIBUTED SURPLUS (continued)**

|                          | 2011         | 2010        |
|--------------------------|--------------|-------------|
| Risk-free interest rate  | 1.9 – 2.75 % | 1 – 2.75%   |
| Expected life of options | 4 years      | 1 – 4 years |
| Annualized volatility    | 97 – 102%    | 89 – 119%   |
| Dividend rate            | 0.00%        | 0.00%       |

**Escrow and pooling**

10,000,000 shares are subject to a pooling agreement dated April 21, 2007. At March 31, 2010, 8,500,000 shares were released leaving a balance of 1,500,000 shares held in escrow. The balance of 1,500,000 was released on May 10, 2010.

**9. ASSET RETIREMENT OBLIGATIONS**

|                                   | June 30, 2010     | March 31, 2010    |
|-----------------------------------|-------------------|-------------------|
| Balance, beginning of the period  | \$ 929,382        | \$ 222,236        |
| Accretion                         | 15,987            | 13,465            |
| Effect of foreign exchange        | 26,841            | (43,402)          |
| Change in estimate                | -                 | 737,083           |
| <b>Balance, end of the period</b> | <b>\$ 972,210</b> | <b>\$ 929,382</b> |

The asset retirement obligations consist of mine closure, reclamation and retirement obligations for mine facilities and infrastructure.

During the year ended March 31, 2010, the Company reassessed its asset retirement obligation estimate based on an independent technical report and to reflect the additional liability incurred with the commencement of mining operations. The total undiscounted amount of estimated cash flows required to settle the retirement obligations of the San Francisco Property is US\$1,041,244 (2009: US\$205,494), which has been discounted using a credit-adjusted interest rate of 6.674%. All asset retirement obligations are not expected to be paid for several years in the future and are intended to be funded from cash balances at the time of the mine closure.

**10. LONG TERM DEBT**

On January 22, 2010, the Company issued US\$15 million in notes to Sprott Asset Management LP (the “Gold Loan”). Gold Loan holders were also granted an aggregate of 3 million share purchase warrants exercisable for 24 months at a price of \$0.80. These warrants were valued at \$1,745,436. The warrants were valued using the Black-Scholes model with the following assumptions: (i) volatility-67%, (ii) interest rate-1.21%, (iii) term-730 days and (iv) dividends-nil.

The Gold Loan is to be repaid in 12 equal monthly installments commencing August 2010. At the time of payment, each payment shall be equivalent in value to 1,667 ounces of gold (a total of 20,004 ounces). The Company has guaranteed the gold loan holders a minimum rate of return of 15% per annum and the Gold Loan is secured by among other things a first charge on the assets of MdN.

The total loan payable at the initial transaction date was \$14,137,500. For the three months ended June 30, 2010, the interest expense on this debt was \$2,413,778. During the prior quarter, the Company accrued and capitalized to mineral property \$1.37 million of interest expense which amount was recorded as current portion of long term debt. In addition, in accordance with CICA section 3855 the Company fair valued an embedded derivative associated with this liability and a charge to earnings of \$2,599,745 was recorded as long term debt. The table below summarizes the gold loan accounts:

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|   |    |                    |
|---|----|--------------------|
| Loan proceeds, net of transaction costs | \$ | 15,882,937         |
| Less: value attributable to warrants    |    | <u>(1,745,437)</u> |
| Loan carrying value                     |    | <u>14,137,500</u>  |
| Current portion of carrying value       |    | 11,945,598         |
| Currency translation                    |    | 56,870             |
| Interest expense payable                |    | <u>3,786,578</u>   |
| Current liability                       |    | <u>15,789,046</u>  |
| Long term portion                       |    | 2,062,299          |
| Unrealised loss on derivative           |    | <u>3,223,170</u>   |
| Long term liability                     |    | <u>5,285,469</u>   |

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

Significant non-cash transactions were as follows:

|   | Three months period ended June 30, |           |
|---|------------------------------------|-----------|
|   | 2010                               | 2009      |
| Accrual of obligations for equipment (including IVA and foreign exchange) | \$ -                               | \$ 77,268 |
| Recognition and accretion of long term debt (including IVA)               | 17,015                             | -         |
| Amortization expenses allocated to development expenditures               | 576,742                            | 2,262     |
| Fair value of warrants issued for financings but not exercised            | -                                  | 2,364,566 |

During the periods ended June 30, 2010 and 2009, the Company made no payments relating to income tax or interest expense.

**12. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT****a) Categories of Financial Assets and Liabilities**

In accordance with Canadian generally accepted accounting principles, financial instruments are classified into one of the five following categories: held-for-trading, held-to-maturity investments, loans and receivables, available-for-sale financial assets and other financial liabilities. Cash and cash equivalents are designated as held-for-trading and their carrying value approximates fair value as they are cash or they are readily convertible to cash in the normal course. Accounts receivable and amounts due from related parties are classified as loans and receivables. Their carrying value approximates fair value due to their limited time to maturity and ability to convert them to cash in the normal course. Accounts payable and accrued liabilities, the vendor loan, the gold loan and other long term debt are classified as other financial liabilities. Accretion on the vendor loan has been determined using a market related interest rate and the amortized cost of the gold loan is calculated using the effective interest rate method and as such their carrying values approximate fair value.

Amended CICA section 3862 establishes a fair value hierarchy that reflects the significance of inputs used in making fair value measurements as follows:

Level 1- quoted prices in active markets for identical assets or liabilities;

Level 2- inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. from derived prices); and

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## 12. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (continued)

Level 3- inputs for the asset or liability that are not based upon observable market data.

At June 30, 2010, the following table sets forth the levels in the fair value hierarchy into which the Company's financial assets and liabilities are measured and recognized in the balance sheet. Assets are classified in their entirety based on the lowest level of input that is significant to the fair value measurement.

|                           | Level 1      | Level 2      |
|---------------------------|--------------|--------------|
| Cash and cash equivalents | \$ 5,364,079 | \$ -         |
| Embedded derivative       | \$ -         | \$ 3,223,170 |

The Company has determined the estimated fair values of its financial instruments based upon appropriate valuation methodologies. At June 30, 2010, there were no financial assets or liabilities measured and recognized in the balance sheet at fair value that would be categorized as Level 3 in the fair value hierarchy above.

### b) Derivative Financial instruments

The Company may utilize financial instruments to manage the risks associated with fluctuations in the market prices of gold and silver and foreign exchange rates. As at June 30, 2010, the Company had not entered into any such derivative contracts.

### c) Risk Management

The Company's operations consist of the acquisition, exploration and development mineral resource properties in Mexico. The Company examines the various financial risks to which it is exposed and assesses the impact and likelihood of occurrence. These risks may include credit risk, liquidity risk, currency risk, interest rate risk and commodity price risks. The Company's risk management program strives to evaluate the unpredictability of financial and commodity markets and its objective is to minimize the potential adverse effects of such risks on the Company's financial performance, where financially feasible to do so. When deemed material, these risks may be monitored by the Company's corporate finance group and they are regularly discussed with the Board of Directors or one of its committees.

#### (i) Credit risk

Counterparty credit risk is the risk that the financial benefits of contracts with a specific counterparty will be lost if a counterparty defaults on its obligations under the contract. This includes any cash amounts owed to the Company by those counterparties, less any amounts owed to the counterparty by the Company where a legal right of set-off exists and also includes the fair values of contracts with individual counterparties which are recorded in the financial statements. The Company's credit risk is predominantly limited to cash balances held in financial institutions, the recovery of IVA from the Mexican tax authorities and for any gold and silver sales and related receivables. The maximum exposure to the credit risk is equal to the carrying value of such financial assets. At June 30, 2010, the Company expects to recover the full amount of such assets.

The objective of managing counterparty credit risk is to minimize potential losses in financial assets. The Company assesses the quality of its counterparties, taking into account their credit worthiness and reputation, past performance and other factors. Cash and short term investments are only deposited with or held by major financial institutions where the Company conducts its business. In order to manage credit and liquidity risk the Company invests only in highly rated investment grade instruments that have maturities of three months or less. Limits are also established based on the type of investment, the counterparty and the credit rating.

Gold and silver sales are made to a limited number of large international organizations specializing in the precious metals markets. The Company believe them to be of sound credit worthiness and to date, all receivable have been settled in accordance with agreed upon terms and conditions.

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**12. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (continued)***(ii) Commodity price risks*

Beginning with the commissioning of the San Francisco Mine, the Company is exposed to price risk associated with the volatility of the market price of commodities and in particular gold and silver and also to many consumables that are used in the production of gold and silver dore. The prices of most commodities are determined in international markets and as such the Company has limited or no ability to control or predict the future level of most commodity prices. In some instances, the Company may have the ability to enter into derivative financial instruments to manage the Company's exposure to changes in the price of commodities such as gold, silver, oil and electricity. At this time, the Company has elected not to actively manage its exposure to commodity price risk through the use of derivative financial instruments.

The Company has entered into a gold loan arrangement to partially finance the resumption of mining activities at the San Francisco Mine. As repayment of this obligation is referenced to the spot price of gold, any increase in the price of gold will increase the cost of borrowing related to this financing. For example, at June 30, 2010 for each (US) \$100 per ounce increase in the price of gold, the cost of repaying this obligation will increase by (US) \$2,000,400 over its 18 month term to maturity.

*(iii) Liquidity risk*

The Company has a planning and budgeting process in place to help determine the funds required to support the Company's normal operating requirements and its exploration and production plans. Because the Company remains in its formative stages, no assurance may be given that external financing will be available should the Company's Board of Director determine that such financing will be necessary. The Company's overall liquidity risk has increased since the San Francisco mine was placed into commercial production.

*(iv) Currency risk*

The Company's functional currency is the Canadian dollar and therefore the Company's net loss and other comprehensive loss are impacted by fluctuations in the value of foreign currencies in relation to the Canadian dollar. The Company's foreign currency exposures comprise cash and cash equivalents, metal sales and accounts receivable, accounts payable, accrued liabilities, the gold loan and future income tax liabilities, denominated in Mexican pesos and United States dollars. The San Francisco Mine has operating costs that may be denominated in or referenced to either the Mexican peso or the United States dollar. In addition, several of the Company's agreements to acquire properties in Mexico may result in option payments by the Company denominated in Mexican pesos or in United States dollars. At the present time, the Company does not use any derivative instruments to reduce its exposure to fluctuations in foreign exchange rates. Appreciation in the Mexican peso and the United States dollar against the Canadian dollar will increase the cost of operations in Mexico. A decrease in the United States dollar against the Canadian dollar will result in a loss to the extent that funds are held in United States dollars and its revenue will fall as gold and silver are priced in United States dollars. The Company partially offsets its exposure to foreign exchange risk, principally with respect to the Mexican peso, by maintaining currency balances in Mexican pesos to offset operating costs, amounts payable and tax liabilities that are denominated in pesos. Some balance sheet and income statement exposure remains as it is not possible to fully forecast the peso currency requirements and peso receipts in future periods. The Company is also exposed to inflation risk in Mexico.

The approximate sensitivity of the Company's net loss and other comprehensive loss for the three month period ended June 30, 2010 due to changes in the exchange rate for the Mexican peso in relation to the Canadian dollar is summarized in the following table expressed as an increase in the net loss and comprehensive loss for each 10% appreciation in the peso against the Canadian dollar:

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**12. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (continued)**

|                                       |    |           |
|---------------------------------------|----|-----------|
| Net loss and other comprehensive loss | \$ | 1,211,000 |
|---------------------------------------|----|-----------|

A 10% depreciation of the Canadian dollar against the Mexican peso would have a similar increase in net loss.

A 10% appreciation in the US dollar in relation to the Canadian dollar would have decreased the Company's net loss and comprehensive loss for the year ended June 30, 2010, 2010 by approximately:

|                                       |    |         |
|---------------------------------------|----|---------|
| Net loss and other comprehensive loss | \$ | 925,000 |
|---------------------------------------|----|---------|

A 10% depreciation of the US dollar against the Canadian dollar would have a similar decrease in net loss.

*(v) Interest rate risk*

The Company's interest revenue earned on cash and cash equivalents is exposed to interest rate risk. The Company does not enter into derivative contracts to manage this risk, and the Company's exposure to interest rate risk is very low as the

Company has limited short term investments. In addition, the Company has and may incur additional interest bearing debt obligations. The Company has elected not to enter into interest rate swaps or other instruments to actively manage such risks. In addition, in January, 2010, the Company entered into a gold loan and increases in the price of gold will increase the effective borrowing cost of this obligation (see Commodity price risk). The Company has chosen not to hedge its exposure to changes in the price of gold with respect to the gold loan.

*(vi) Fair value disclosures*

The carrying values of cash and cash equivalents, amounts receivable, prepaid expenses, and accounts payable approximate their fair value based on their short term nature. The carrying value of the vendor loan approximates its fair value as it has been discounted at an interest rate approximating current market rates. The carrying value of the gold loan approximates fair value as it has been amortized using the effective interest method and its embedded derivative is fair valued at each reporting period.

**13. COMMITMENTS AND CONTINGENCIES**

- (a) The Company has lease commitments for office premises and equipment, which require future minimum lease payments for the fiscal years ended as follows:

|      |          |
|------|----------|
| 2011 | \$81,105 |
| 2012 | \$13,520 |

The lease commitments include a guarantee provided by the Company for the office premises at its corporate office.

- (b) Under Mexican regulations, the Company may be obligated to remit taxes to the government on payments made for the acquisition of mineral claims in the event that the recipients of such payments fail to make the required tax remittances relating to those payments. The outcome of this matter is not determinable. The maximum potential remittance is approximately \$477,649; however, the Company believes it has substantive defenses against any claims.
- (c) On March 1, 2010, the Company re-entered into a consulting agreement with Grandich Publications, LLC ("Grandich"). Grandich is paid a monthly fee of US\$2,000. The agreement was for a period of twelve months.
- (d) The Company has entered into a mining contract with Peal de Mexico, S.A. de C.V. ("Peal"). The contract is for 42 months, and is at a contracted price of US\$1.59 per ton (plus IVA). This price may increase subject to the price of diesel, drilling and blasting costs, as well as hauling distance, and is subject to an annual review.

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June 30, 2010

(Unaudited in Canadian dollars, except for number of options and per share amounts)

**13. COMMITMENTS AND CONTINGENCIES (continued)**

Under the Peal contract, the Company is responsible for demobilization costs of US\$900,000 (plus IVA) payable one month prior to the end of the mining contract. These obligations have been recorded at an annualized discount rate of 6.775%, reflecting the implied interest rate, and calculated according to the formula stipulated in the contract. This obligation is recorded at 1,082,605.

**14. SEGMENTED INFORMATION**

The Company primarily operates in one reportable operating segment, being the acquisition, exploration and development of resource properties located in two geographical segments, Canada and Mexico. Geographic information is as follows:

|                | Total<br>Assets      | Equipment            | Resource<br>Properties | Inventory           | Other<br>Assets      |
|----------------|----------------------|----------------------|------------------------|---------------------|----------------------|
| June 30, 2010  |                      |                      |                        |                     |                      |
| Canada         | \$ 1,978,461         | \$ 29,341            | \$ -                   | \$ -                | \$ 1,949,119         |
| Mexico         | 87,941,086           | 25,126,421           | 43,153,726             | 8,190,866           | 11,470,073           |
|                | <u>\$ 89,919,546</u> | <u>\$ 25,155,762</u> | <u>\$ 43,153,726</u>   | <u>\$ 8,190,866</u> | <u>\$ 13,419,192</u> |
| March 31, 2010 |                      |                      |                        |                     |                      |
| Canada         | \$ 1,039,142         | \$ 28,472            | \$ -                   | \$ -                | \$ 1,010,670         |
| Mexico         | 81,240,140           | 24,368,995           | 41,698,893             | 6,420,154           | 8,752,098            |
|                | <u>\$ 82,279,282</u> | <u>\$ 24,397,467</u> | <u>\$ 41,698,893</u>   | <u>\$ 6,420,154</u> | <u>\$ 9,762,768</u>  |

**15. SUBSEQUENT EVENTS**

- (a) In July 2010, payments totalling \$123,437 were made for the Cocula property, with \$26,563 due in September.
- (b) In August 2010 stock options representing 100,000 common shares were exercised at a strike price of \$0.70 per share.