SouthGobi Resources Ltd.
Consolidated Financial Statements

December 31, 2013
(Expressed in U.S. Dollars)

Independent Auditor's Report

To the Shareholders of SouthGobi Resources Ltd.

We have audited the accompanying consolidated financial statements of SouthGobi Resources Ltd. ("SouthGobi" or the "Company"), which comprise the consolidated statements of financial position as at December 31, 2013 and December 31, 2012 and the consolidated statements of comprehensive income, cash flows and changes in equity for the years then ended, and the related notes, which comprise a summary of significant accounting policies and other explanatory information.

Management's responsibility for the consolidated financial statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained in our audits is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2013 and December 31, 2012 and its financial performance and its cash flows for the years then ended in accordance with International Financial Reporting Standards.

Emphasis of matter
Without qualifying our opinion, we draw attention to Note 1 in the financial statements which describes matters and conditions that indicate the existence of a material uncertainty that may cast significant doubt about the Company's ability to continue as a going concern.

signed "PricewaterhouseCoopers LLP"

Chartered Accountants
Vancouver, Canada
March 24, 2014

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SOUTHGOBI RESOURCES LTD.

Consolidated Statements of Comprehensive Income

(Expressed in thousands of U.S. Dollars, except for share and per share amounts)

	Notes	Year ended December 31, 2013	2012
Revenue		**$ 58,636**	$ 78,061
Cost of sales	5	**(112,627)**	(127,407)
Gross loss		**(53,991)**	(49,346)
Other operating expenses	6	**(126,040)**	(41,645)
Administration expenses	7	**(15,629)**	(24,637)
Evaluation and exploration expenses	8	**(1,169)**	(8,598)
Loss from operations		**(196,829)**	(124,226)
Finance costs	9	**(21,162)**	(15,385)
Finance income	9	**5,566**	39,942
Share of earnings/(losses) of joint venture	13	**(53)**	635
Loss before tax		**(212,478)**	(99,034)
Current income tax expense	10	**(3)**	(354)
Deferred income tax recovery/(expense)	10	**(24,983)**	1,886
Net loss attributable to equity holders of the Company		**(237,464)**	(97,502)
Other comprehensive income/(loss) to be reclassified to profit or loss in subsequent periods			
Change in value of available-for-sale financial asset, net of tax		**514**	(16,559)
Net comprehensive loss attributable to equity holders of the Company		**$ (236,950)**	$ (114,061)
Basic loss per share	11	**$ (1.30)**	$ (0.54)
Diluted loss per share	11	**$ (1.30)**	$ (0.60)

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

SOUTHGOBI RESOURCES LTD.

Consolidated Statements of Financial Position

(Expressed in thousands of U.S. Dollars)

	Notes	As at December 31, 2013	2012
Assets			
Current assets			
Cash		**$ 21,837**	$ 19,674
Trade and other receivables	12	**2,578**	3,292
Short term investments	13	**-**	15,000
Inventories	14	**40,288**	59,735
Prepaid expenses and deposits	15	**11,506**	47,432
Total current assets		**76,209**	145,133
Non-current assets			
Prepaid expenses and deposits	15	**-**	16,778
Property, plant and equipment	16	**399,395**	521,473
Long term investments	13	**30,602**	24,084
Deferred income tax assets	10	**-**	24,984
Total non-current assets		**429,997**	587,319
Total assets		**$ 506,206**	$ 732,452
Equity and liabilities			
Current liabilities			
Trade and other payables	17	**$ 31,241**	$ 10,216
Deferred revenue		**997**	8,181
Current portion of convertible debenture	19	**2,301**	6,301
Total current liabilities		**34,539**	24,698
Non-current liabilities			
Convertible debenture	19	**94,302**	99,667
Decommissioning liability	20	**2,308**	4,104
Total non-current liabilities		**96,610**	103,771
Total liabilities		**131,149**	128,469
Equity			
Common shares		**1,067,839**	1,059,710
Share option reserve	23	**51,198**	51,303
Investment revaluation reserve	23	**514**	-
Accumulated deficit	21	**(744,494)**	(507,030)
Total equity		**375,057**	603,983
Total equity and liabilities		**$ 506,206**	$ 732,452
Net current assets		**$ 41,670**	$ 120,435
Total assets less current liabilities		**$ 471,667**	$ 707,754

Corporate information and going concern (Note 1), commitments for expenditure (Note 28) and contingencies (Note 29)

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

APPROVED BY THE BOARD:

"Andre Deepwell"
Director

"Pierre Lebel"
Director

SOUTHGOBI RESOURCES LTD.

Consolidated Statements of Changes in Equity

(Expressed in thousands of U.S. Dollars and shares in thousands)

	Number of shares	Common shares	Share option reserve	Investment revaluation reserve	Accumulated deficit	Total
Balances, January 1, 2012	181,320	$ 1,054,298	$ 44,143	$ 16,559	$ (409,433)	$ 705,567
Shares issued for:						
Interest settlement on convertible debenture	522	4,000	-	-	-	4,000
Exercise of stock options, net of redemptions	163	1,882	(1,368)	-	-	514
Employee share purchase plan	71	395	-	-	-	395
Share-based compensation charged to operations	-	-	8,528	-	-	8,528
Common shares repurchased and cancelled	(148)	(860)	-	-	(95)	(955)
Common share repurchase costs	-	(5)	-	-	-	(5)
Net loss for the year	-	-	-	-	(97,502)	(97,502)
Reclassification of gain on available-for-sale financial asset, net of tax	-	-	-	(16,559)	-	(16,559)
Balances, December 31, 2012	181,928	$ 1,059,710	$ 51,303	$ -	$ (507,030)	$ 603,983
Balances, January 1, 2013	**181,928**	**1,059,710**	**51,303**	**-**	**(507,030)**	**$ 603,983**
Shares issued for:						
Interest settlement on convertible debenture	**5,310**	**8,000**	**-**	**-**	**-**	**8,000**
Employee share purchase plan	**71**	**129**	**-**	**-**	**-**	**129**
Share-based compensation recovery	**-**	**-**	**(105)**	**-**	**-**	**(105)**
Net loss for the year	**-**	**-**	**-**	**-**	**(237,464)**	**(237,464)**
Change in value of available-for-sale financial asset, net of tax	**-**	**-**	**-**	**514**	**-**	**514**
Balances, December 31, 2013	**187,309**	**$ 1,067,839**	**$ 51,198**	**$ 514**	**$ (744,494)**	**$ 375,057**

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

SOUTHGOBI RESOURCES LTD.

Consolidated Statements of Cash Flows

(Expressed in thousands of U.S. Dollars)

	Notes	Year ended December 31, 2013	2012
Operating activities			
Loss before tax		**$ (212,478)**	$ (99,034)
Adjustments for:			
Depreciation and depletion		**45,253**	46,495
Share-based compensation	22	**(105)**	8,528
Finance costs	9	**21,162**	15,385
Finance income	9	**(5,566)**	(39,942)
Share of losses/(earnings) of joint venture	13	**53**	(635)
Interest paid		**(16,184)**	(16,322)
Income taxes paid		**-**	(2,349)
Unrealized foreign exchange loss/(gain)		**(236)**	467
Loss on disposal of property, plant and equipment		**895**	720
Provision for doubtful trade and other receivables	12	**200**	1,032
Impairment loss on available-for-sale financial asset	13	**3,067**	19,184
Impairment of inventories	14	**35,697**	20,531
Impairment of prepaid expenses and deposits	15	**30,152**	-
Impairment of property, plant and equipment	16	**72,669**	15,245
Operating cash flows before changes in non-cash working capital items		**(25,421)**	(30,695)
Net change in non-cash working capital items	27	**32,980**	4,412
Cash generated from/(used in) operating activities		**7,559**	(26,283)
Investing activities			
Expenditures on property, plant and equipment		**(11,819)**	(97,388)
Proceeds from disposal of property, plant and equipment		**1,703**	1,030
Interest received		**94**	400
Proceeds from maturity or disposal of short and long term investments		**15,486**	31,485
Investment in joint venture		**(10,356)**	(13,264)
Cash used in investing activities		**(4,892)**	(77,737)
Financing activities			
Proceeds from issuance of common shares and exercise of stock options, net of issue costs		**129**	909
Repurchase of common shares, including transaction costs		**-**	(960)
Drawings under line of credit facility		**-**	26,753
Repayments of line of credit facility		**-**	(26,753)
Cash generated from/(used in) financing activities		**129**	(51)
Effect of foreign exchange rate changes on cash		**(633)**	178
Increase/(decrease) in cash		**2,163**	(103,893)
Cash, beginning of year		**19,674**	123,567
Cash, end of year		**$ 21,837**	$ 19,674

Supplemental cash flow information (Note 27)

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

1. CORPORATE INFORMATION AND GOING CONCERN

SouthGobi Resources Ltd. is a publicly listed company incorporated in Canada with limited liability under the legislation of the Province of British Columbia and its shares are listed on the Toronto Stock Exchange (Symbol: SGQ) and Hong Kong Stock Exchange (Symbol: 1878). The company, together with its subsidiaries (collectively referred to as the "Company"), is an integrated coal mining, development and exploration company. The Company's immediate parent company is Turquoise Hill Resources Ltd. ("Turquoise Hill") and at December 31, 2013, Turquoise Hill owned approximately 56% of the outstanding common shares of the Company (Note 26). Turquoise Hill is controlled by Rio Tinto plc ("Rio Tinto").

The Company owns the following significant coal projects in Mongolia: the Ovoot Tolgoi open pit producing coal mine ("Ovoot Tolgoi Mine") and the following significant development projects, the Soumber Deposit, the Zag Suuj Deposit and the Ovoot Tolgoi Underground Deposit. These projects are located in the Umnugobi Aimag (South Gobi Province) of Mongolia, within 150 kilometers of each other and in close proximity to the Mongolia-China border. The Company owns a 100% interest in these coal projects.

The head office, principal address and registered and records office of the Company is located at 354 – 200 Granville Street, Vancouver, British Columbia, Canada, V6C 1S4.

The Company curtailed its mining activities at the Ovoot Tolgoi Mine during the three months ended June 30, 2012 to varying degrees to manage coal inventories and to maintain efficient working capital levels. As at June 30, 2012, mining activities had been fully curtailed. The Company's mining activities remained fully curtailed until March 22, 2013, when the Company recommenced mining activities at the Ovoot Tolgoi Mine.

Going concern assumption

Several adverse conditions and material uncertainties cast significant doubt upon the going concern assumption. The Company had cash of $21,837 and working capital of $41,670 at December 31, 2013. However, the Company anticipates that coal prices in China will remain under pressure in 2014, which will continue to impact the Company's margins and liquidity. Based on its forecasts for the year ended December 31, 2014, the Company is unlikely to have sufficient capital resources and does not expect to generate sufficient cash flows from mining operations in order to satisfy its ongoing obligations and future contractual commitments, including cash interest payments due on the China Investment Corporation ("CIC") convertible debenture. Therefore, the Company is actively seeking additional sources of financing to continue operating and meet its objectives.

The Company's consolidated financial statements have been prepared on a going concern basis which assumes that the Company will continue operating until at least December 31, 2014 and will be able to realize its assets and discharge its liabilities in the normal course of operations as they come due. While the Company is actively seeking additional sources of financing to continue operating and meet its objectives, there can be no assurance that such financing will be available on terms acceptable to the Company. If for any reason, the Company is unable to secure the additional sources of financing and continue as a going concern, then this could result in adjustments to the amounts and classifications of assets and liabilities in the Company's consolidated financial statements and such adjustments could be material.

1. CORPORATE INFORMATION AND GOING CONCERN (CONTINUED)

While the Company intends to secure additional sources of financing as soon as possible, a continued delay in securing additional financing could ultimately result in an event of default of the $250,000 CIC convertible debenture, which if not cured within applicable cure periods in accordance with the terms of such debenture, may result in the principal amount owing and all accrued and unpaid interest becoming immediately due and payable upon notice to the Company by CIC.

2. BASIS OF PREPARATION

2.1 Statement of compliance

The consolidated financial statements, including comparatives, have been prepared in accordance with and using accounting policies in compliance with the International Financial Reporting Standards ("IFRS") issued by the International Accounting Standards Board ("IASB") and Interpretations of the IFRS Interpretations Committee ("IFRIC").

The consolidated financial statements of the Company for the year ended December 31, 2013 were approved and authorized for issue by the Board of Directors of the Company on March 24, 2014.

2.2 Basis of presentation

The consolidated financial statements have been prepared on a historical cost basis except for certain financial assets and financial liabilities which are measured at fair value. The Company's financial instruments are further disclosed in Note 25.

The Company's reporting currency and the functional currency of all of its operations is the U.S. Dollar as this is the principal currency of the economic environment in which the Company operates.

2.3 Adoption of new and revised standards and interpretations

The Company has adopted the new and revised standards and interpretations issued by the IASB listed below effective January 1, 2013. These changes were made in accordance with the transitional provisions outlined in the respective standards and interpretations.

IFRS 10 Consolidated Financial Statements

IFRS 10 replaces IAS 27 "Consolidated and Separate Financial Statements" and SIC 12 "Consolidation – Special Purpose Entities". IFRS 10 establishes principles for the presentation and preparation of consolidated financial statements when an entity controls multiple entities. The new consolidation standard changes the definition of control so that the same criteria apply to all entities, both operating and special purpose entities, to determine control. The revised definition focuses on the need to have both power over the investee and exposure to variable returns before control is present. The adoption of IFRS 10 did not result in any change in the consolidation status of any of the Company's subsidiaries and investees.

2. BASIS OF PREPARATION (CONTINUED)

IFRS 11 Joint Arrangements

IFRS 11 replaces IAS 31 "Interests in Joint Ventures". IFRS 11 classifies joint arrangements as either joint operations or joint ventures, depending on the rights and obligations of the parties involved in the joint arrangement. Joint arrangements that are classified as joint operations require the venturers to recognize the individual assets, liabilities, revenues and expenses to which they have legal rights or are responsible. Joint arrangements that are classified as a joint venture are accounted for using the equity method of accounting.

As a result of the adoption of IFRS 11, the Company's 40% interest in RDCC LLC is now classified as a joint venture (previously classified as a jointly-controlled entity under IAS 31). Prior to the adoption of IFRS 11, the Company accounted for its investment in RDCC LLC under the equity method of accounting. Therefore, the adoption of IFRS 11 did not have an impact on the consolidated financial statements for the current or prior periods presented.

IFRS 12 Disclosure of Interests in Other Entities

IFRS 12 outlines the disclosure requirements for interests in subsidiaries and other entities. The adoption of IFRS 12 has resulted in additional disclosures in the Company's consolidated financial statements. The additional disclosures are included in Note 13.

IFRS 13 Fair Value Measurement

IFRS 13 provides a definition of fair value, sets out a single IFRS framework for measuring fair value and outlines disclosure requirements for fair value measurements. The adoption of IFRS 13 has resulted in additional fair value measurement disclosures in the Company's consolidated financial statements. The additional disclosures are included in Note 25.

IAS 1 Presentation of Financial Statements (Amendment)

The amendments to IAS 1 requires companies preparing financial statements under IFRS to group items within other comprehensive income that may be reclassified to profit or loss and those that will not be reclassified. The consolidated statement of comprehensive income in these consolidated financial statements has been amended to reflect the presentation requirements under the amended IAS 1.

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

IFRIC 20 provides guidance on the accounting for the costs of stripping activities during the production phase of a surface mine. Under IFRIC 20, stripping activity assets are recognized when the following three criteria are met:

- it is probable that the future economic benefit (improved access to the ore body) associated with the stripping activity will flow to the entity;
- the entity can identify the component of the ore body for which access has been improved; and
- the costs relating to the stripping activity associated with that component can be measured reliably

If not all of the criteria are met, the stripping activity costs are included in the costs of inventory produced during the period incurred.

(Expressed in thousands of U.S. Dollars and shares in thousands, unless otherwise indicated)

2. BASIS OF PREPARATION (CONTINUED)

The Company assessed its open-pit mining operations at the Ovoot Tolgoi Mine and concluded that as at January 1, 2012 there are identifiable coal seams with which the predecessor stripping activity related to. Therefore, no adjustment to the consolidated financial statements was required upon initial transition to IFRIC 20.

The adoption of IFRIC 20 has not resulted in a change in the Company's capitalization of stripping activity costs, and therefore no adjustment was required to the Company's consolidated financial statements in the current or prior periods presented. The Company classifies stripping activity assets capitalized under IFRIC 20 as mineral property costs within property, plant and equipment and these costs are amortized on a units-of-production basis based on proven and probable reserves.

Other

The IASB also amended IAS 19 "Employee benefits", IAS 28 "Investments in Associates" (2003), IAS 36 "Impairment of Assets", IFRS 7 "Financial Instruments" and set out amendments to a number of standards under the "Annual Improvements 2009-2011 Cycle" effective January 1, 2013. The amendments to these standards did not impact the Company's consolidated financial statements.

2.4 Standards issued but not yet effective

The standards and interpretations that are issued up to the date of issuance of the Company's financial statements, but were not effective during the year ended December 31, 2013, are disclosed below. The Company intends to adopt these standards, if applicable, when they become effective.

IFRS 9	Financial Instruments(iii)
IFRS 9, IFRS 7 and IAS 39 Amendments	Hedge Accounting and amendments to IFRS 9, IFRS 7 and IAS 39(iii)
IFRS 10, IFRS 12 and IAS 27 (2011) Amendments	Amendments to IFRS 10, IFRS 12 and IAS 27 (2011) – Investment Entities(i)
IAS 19 Amendments	Amendments to IAS 19 Employee Benefits – Defined Benefit Plans: Employee Contributions(ii)
IAS 32 Amendments	Amendments to IAS 32 Financial Instruments: Presentation – Offsetting Financial Assets and Financial Liabilities(i)
IAS 39 Amendments	Amendments to IAS 39 Financial Instruments: Recognition and Measurement – Novation of Derivatives and Continuation of Hedge Accounting(i)
IFRIC 21	Levies(i)

(i) Effective for annual periods beginning on or after January 1, 2014.
(ii) Effective for annual periods beginning on or after July 1, 2014.
(iii) Mandatory effective date not yet determined.

The Company anticipates that the adoption of these standards and interpretations in future periods will have no material impact on the financial statements of the Company.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

3.1 Basis of consolidation

The consolidated financial statements include the financial statements of SouthGobi Resources Ltd. and its controlled subsidiaries and investees (Note 26).

The results of subsidiaries acquired or disposed of during the year are included in the consolidated statement of comprehensive income from the effective date of acquisition or up to the effective date of disposal, as appropriate. All intercompany transactions, balances, income and expenses are eliminated in full on consolidation.

The Company controls an entity when the Company is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity.

Non-controlling interests in the net assets of consolidated subsidiaries are identified separately from the Company's equity therein. Total comprehensive income of the Company's subsidiaries is attributed to the equity holders of the Company and to the non-controlling interests even if this results in the non-controlling interest having a deficit balance. The Company did not have any non-controlling interests in the net assets of consolidated subsidiaries during the years presented.

3.2 Foreign currencies

The functional currency of all of the Company's operations is the U.S. Dollar as this is the principal currency of the economic environment in which the Company operates. Transactions in foreign currencies are initially recorded at the U.S. Dollar rate of exchange at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the U.S. Dollar rate of exchange ruling at the end of each reporting period. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rate prevailing at the date of the transaction. Non-monetary items measured at fair value in a foreign currency are translated using the exchange rate at the date when the fair value is determined.

3.3 Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, which are assets that necessarily take a substantial period of time to get ready for their intended use or sale, are capitalized as part of the cost of those assets. All other borrowing costs are expensed and included in profit or loss.

3.4 Inventories

Coal stockpile inventories are measured at the lower of production cost and net realizable value. Production cost is determined by the weighted average cost method and includes direct and indirect labor, operating materials and supplies, processing costs, transportation costs and an appropriate portion of fixed and variable overhead expenses. Fixed and variable overhead expenses include depreciation and depletion. Net realizable value represents the future estimated selling price of the product, less estimated costs to complete production and costs necessary to bring the product to sale.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Materials and supplies inventory consists of consumable parts and supplies which are valued at the lower of weighted average cost and net realizable value, less allowances for obsolescence. Replacement cost is used as the best available measure of net realizable value. Supplies used in the production of inventories are not written down below cost if the finished products in which they will be incorporated are expected to be sold at or above cost.

3.5 Property, plant and equipment

Property, plant and equipment includes the Company's operating equipment and infrastructure, construction in progress and mineral properties. Property, plant and equipment is stated at cost less accumulated depreciation and depletion and accumulated impairment losses.

Initial recognition

The cost of an item of operating equipment and infrastructure consists of the purchase price or construction cost, including vendor prepayments, any costs directly attributable to bringing the asset to the location and condition necessary for its intended use, an initial estimate of the decommissioning liability and capitalized borrowing costs.

Construction in progress is classified to the appropriate category of property, plant and equipment when it is completed and is ready for its intended use.

All direct costs related to the acquisition of mineral property interests are capitalized on a property by property basis. The cost of mineral properties also includes mineral property development costs, certain production stripping costs and decommissioning liabilities related to the reclamation of the Company's mineral properties.

Depreciation and depletion

Depreciation and depletion are recorded based on the cost of an item of property, plant and equipment, less its estimated residual value, using the straight-line method or unit-of-production method over the following estimated useful lives:

Mobile equipment	5 to 7 years
Other operating equipment	1 to 10 years
Buildings and roads	5 to 20 years
Construction in progress	not depreciated
Mineral properties	unit-of-production basis based on proven and probable reserves

An item of property, plant and equipment is derecognized upon disposal, when held for sale or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss arising on disposal of the asset, determined as the difference between the net disposal proceeds and the carrying amount of the asset, is recognized in profit or loss.

The Company conducts an annual assessment of the residual balances, estimated useful lives and depreciation methods being used for property, plant and equipment and any changes arising from the assessment are applied by the Company prospectively.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

3.6 Mineral properties

Evaluation and exploration expenses

Evaluation and exploration expenses are charged to profit or loss in the period incurred until such time as it has been determined that a mineral property has proven and probable reserves, is technically feasible and commercially viable and management has determined that the mineral property will be developed.

Commencement of commercial production

On the commencement of commercial production, depletion of each mineral property is recorded on a unit-of-production basis using proven and probable reserves as the depletion base. Management's determination of when commercial production commences is based on several qualitative and quantitative factors including, but not limited to, the following:

- the elevation or bench where the coal to be mined has been reached
- the commissioning of major operating equipment and infrastructure is completed

3.7 Development and production stripping costs

Once a property is determined to have economically recoverable reserves, the Company's subsequent exploration and evaluation and development expenses are capitalized as mineral property costs within property, plant and equipment.

Production stripping activity assets are recognized when the following three criteria are met:

- it is probable that the future economic benefit (improved access to the ore body) associated with the stripping activity will flow to the entity;
- the entity can identify the component of the ore body for which access has been improved; and
- the costs relating to the stripping activity associated with that component can be measured reliably

If not all of the criteria are met, the stripping activity costs are included in the costs of inventory produced during the period incurred.

3.8 Decommissioning, restoration and similar liabilities

The Company recognizes provisions for statutory, contractual, constructive or legal obligations, including those associated with the reclamation of mineral properties, when those obligations result from the acquisition, construction, development or normal operation of the assets. Initially, a provision for a decommissioning liability is recognized as its present value in the period in which it is incurred. Upon initial recognition of the liability, a corresponding amount is added to the carrying amount of the related asset and the cost is amortized as an expense over the estimated useful life of the asset using either the unit-of-production method or the straight-line method, as appropriate. Following the initial recognition of the decommissioning liability, the carrying amount of the liability is increased for the passage of time and adjusted for changes to the discount rate and the amount or timing of the underlying cash flows required to settle the obligation. The discount rate used is a credit adjusted risk free rate.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

3.9 Joint arrangements

The Company classifies joint arrangements as either joint operations or joint ventures, depending on the rights and obligations of the parties involved in the joint arrangement. Joint arrangements that are classified as joint operations require the venturers to recognize the individual assets, liabilities, revenues and expenses to which they have legal rights or are responsible. Joint arrangements that are classified as a joint venture are accounted for using the equity method of accounting.

3.10 Share-based payments

Share-based payment transactions

Employees (including directors and senior executives) of the Company receive a portion of their remuneration in the form of share-based payments, whereby employees render services as consideration for equity instruments ("equity-settled transactions").

In situations where equity instruments are issued to non-employees and the value of some or all of the goods or services received by the entity as consideration cannot be measured reliably, they are measured at the fair value of the share-based payment. Otherwise, share-based payments are measured at the fair value of goods or services received.

Equity-settled transactions

The costs of equity-settled transactions with employees are measured by reference to the fair value at the date on which the awards are granted.

The costs of equity-settled transactions are recognized, together with a corresponding increase in the share option reserve, over the period in which the performance and/or service conditions are fulfilled and end on the date on which the relevant employees become fully entitled to the award. The cumulative expense recognized for equity-settled transactions at each reporting date reflects the Company's best estimate of the number of equity instruments that will ultimately vest. No expense is recognized for awards that do not ultimately vest.

When the terms of an equity-settled award are modified, the minimum expense recognized is the expense as if the terms had not been modified. An additional expense is recognized for any modification which increases the total fair value of the share-based payment arrangement, or is otherwise beneficial to the employee as measured at the date of the modification.

3.11 Earnings per share

Basic earnings per share is calculated by dividing the profit or loss attributable to equity holders of the Company by the weighted average number of shares outstanding during the reporting period.

Diluted earnings per share is calculated by adjusting the profit or loss attributable to equity holders of the Company and the weighted average number of shares outstanding for the effects of all dilutive share equivalents. The Company's dilutive share equivalents include stock options and convertible debt.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

3.12 Taxation

Income tax expense represents the sum of tax currently payable and deferred tax.

Current income tax

Current income tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are substantively enacted at the end of each reporting period.

Deferred income tax

Deferred income tax is provided using the liability method on temporary differences, at the end of each reporting period, between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes.

Deferred income tax liabilities are recognized for all taxable temporary differences, except:

- where the deferred income tax liability arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of taxable temporary differences associated with investments in subsidiaries, associates and joint ventures, where the timing of the reversal of the temporary differences can be controlled by the parent, investor or venturer and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred income tax assets are recognized for all deductible temporary differences, carry forward of unused tax credits and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences and the carry forward of unused tax credits and unused tax losses can be utilized except:

- where the deferred income tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of deductible temporary differences associated with investments in subsidiaries, associates and joint ventures, deferred income tax assets are recognized only to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilized.

The carrying amount of deferred income tax assets is reviewed at the end of each reporting period and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred income tax asset to be utilized. Unrecognized deferred income tax assets are reassessed at the end of each reporting period and are recognized to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be recovered.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realized or the liability is settled, based on tax rates (and tax laws) that have been substantively enacted at the end of each reporting period.

Deferred income tax relating to items recognized directly in equity is recognized in equity and not in profit or loss.

Deferred income tax assets and deferred income tax liabilities are offset if, and only if, a legally enforceable right exists to set off current tax assets against current tax liabilities and the deferred tax assets and liabilities relate to income taxes levied by the same taxation authority on either the same taxable entity or different taxable entities which intend to either settle current tax liabilities and assets on a net basis, or to realize the assets and settle the liabilities simultaneously, in each future period in which significant amounts of deferred tax assets or liabilities are expected to be settled or recovered.

3.13 Financial assets

All financial assets are initially recorded at fair value and designated upon inception into one of the following four categories: held-to-maturity, available-for-sale, loans-and-receivables or at fair value through profit or loss (“FVTPL”).

Financial assets classified as FVTPL are measured at fair value with unrealized gains and losses recognized through profit or loss.

Financial assets classified as loans-and-receivables and held-to-maturity are measured at amortized cost using the effective interest method less any allowance for impairment. The effective interest method is a method of calculating the amortized cost of a financial asset and of allocating interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts (including all fees paid or received that form an integral part of the effective interest rate, transaction costs and other premiums or discounts) through the expected life of the financial asset, or, where appropriate, a shorter period.

Financial assets classified as available-for-sale are measured at fair value with unrealized gains and losses recognized in other comprehensive income except when there is objective evidence that the financial asset is impaired. Impairment losses on available-for-sale financial assets are recognized in profit or loss.

Transaction costs associated with FVTPL financial assets are expensed as incurred, while transaction costs associated with all other financial assets are included in the initial carrying amount of the asset.

3.14 Financial liabilities

All financial liabilities are initially recorded at fair value and designated upon inception as FVTPL or other-financial-liabilities.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Financial liabilities classified as other-financial-liabilities are initially recognized at fair value less directly attributable transaction costs. After initial recognition, other-financial-liabilities are subsequently measured at amortized cost using the effective interest method. The effective interest method is a method of calculating the amortized cost of a financial liability and of allocating interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments through the expected life of the financial liability, or, where appropriate, a shorter period.

Financial liabilities classified as FVTPL include financial liabilities designated upon initial recognition as FVTPL. Derivatives, including separated embedded derivatives, are also classified as FVTPL unless they are designated as effective hedging instruments. Transaction costs on financial liabilities classified as FVTPL are expensed as incurred. At the end of each reporting period subsequent to initial recognition, financial liabilities classified as FVTPL are measured at fair value, with changes in fair value recognized directly in profit or loss in the period in which they arise. The net gain or loss recognized in profit or loss excludes any interest paid on the financial liabilities.

3.15 Impairment of financial assets

The Company assesses at the end of each reporting period whether a financial asset is impaired.

Assets carried at amortized cost

If there is objective evidence that an impairment loss on assets carried at amortized cost has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the financial asset's original effective interest rate. The carrying amount of the asset is then reduced by the amount of the impairment. The amount of the loss is recognized in profit or loss.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized, the previously recognized impairment loss is reversed to the extent that the carrying value of the asset does not exceed what the amortized cost would have been had the impairment not been recognized. Any subsequent reversal of an impairment loss is recognized in profit or loss.

Available-for-sale

A significant or prolonged decline in the fair value of an available-for-sale financial asset below its cost provides objective evidence that the asset is impaired. If an available-for-sale financial asset is impaired, an amount comprising the difference between its cost and its current fair value, less any impairment loss previously recognized in profit or loss, is transferred from equity to profit or loss. Reversals of impairment losses in respect of equity instruments classified as available-for-sale are not recognized in profit or loss.

3.16 Derecognition of financial assets and financial liabilities

Financial assets are derecognized when the rights to receive cash flows from the assets expire or, the financial assets are transferred and the Company has transferred substantially all the risks and rewards of ownership of the financial assets. On derecognition of a financial asset, the difference between the asset's carrying amount and the sum of the consideration received and receivable and the cumulative gain or loss that had been recognized directly in equity is recognized in profit or loss.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Financial liabilities are derecognized when the obligation specified in the relevant contract is discharged, cancelled or expires. The difference between the carrying amount of the financial liability derecognized and the consideration paid and payable is recognized in profit or loss.

3.17 Impairment of non-financial assets

At the end of each reporting period, the Company reviews the carrying amounts of its tangible and intangible assets to determine whether there is an indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). Where it is not possible to estimate the recoverable amount of an individual asset, the Company estimates the recoverable amount of the cash-generating unit to which the assets belong.

Recoverable amount is the higher of fair value less costs to sell and value in use. In assessing fair value less costs to sell, recent market transactions are taken into account. The Company also considers the results of an appropriate valuation model which would generally be determined based on the present value of estimated future cash flows arising from the continued use and eventual disposal of the asset. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

If the recoverable amount of an asset (or cash-generating unit) is estimated to be less than its carrying amount, the carrying amount of the asset (or cash-generating unit) is reduced to its recoverable amount. An impairment loss is recognized immediately in the statement of comprehensive income.

Where an impairment loss subsequently reverses, the carrying amount of the asset (or cash-generating unit) is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognized for the asset (or cash-generating unit) in prior periods.

3.18 Cash and cash equivalents

Cash and cash equivalents include cash at banks and short term money market instruments with original maturities of three months or less.

3.19 Revenue recognition

Revenue is recognized to the extent it is probable that the economic benefits will flow to the Company and the revenue can be reliably measured. Revenue is measured at the fair value of the consideration received or receivable, excluding discounts, rebates or duties. Revenue from the sale of goods is recognized when the significant risks and rewards of ownership pass to the buyer, collection is reasonably assured and the selling price is reasonably determinable.

Revenue from the sale of coal is recognized when the significant risks and rewards of ownership and effective control of the coal are transferred to the buyer and the selling prices are known or can be reasonably estimated. Revenue recognition occurs when the coal is loaded into customer trucks at mine-gate.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

3.20 Provisions

Provisions are recognized when the Company has a present obligation (legal or constructive) that has arisen as a result of a past event and it is probable that a future outflow of resources will be required to settle the obligation, provided that a reliable estimate can be made of the amount of the obligation.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risk specific to the obligation. The increase in the provision due to the passage of time is recognized as a finance cost.

3.21 Related party transactions

Parties are considered to be related if one party has the ability, directly or indirectly, to control the other party or exercise significant influence over the other party in making financial and operating decisions. Parties are also considered to be related if they are subject to common control; related parties may be individuals or corporate entities. A transaction is considered to be a related party transaction when there is a transfer of resources or obligations between related parties.

3.22 Significant accounting judgments and estimates

Information about judgments and estimates in applying accounting policies that have the most significant effect on the amounts recognized in the consolidated financial statements are as follows:

Liquidity and going concern assumption

In the determination of the Company's ability to meet its ongoing obligations and future contractual commitments, management relies on the Company's planning, budgeting and forecasting process to help determine the funds required to support the Company's normal operations on an ongoing basis and its expansionary plans. The key inputs used by the Company in this process include forecasted capital deployment, results from operations, results from the exploration and development of its properties and general industry conditions.

Several adverse conditions and material uncertainties cast significant doubt upon the going concern assumption. Based on its forecasts for the year ended December 31, 2014, the Company is unlikely to have sufficient capital resources and does not expect to generate sufficient cash flows from mining operations in order to satisfy its ongoing obligations and future contractual commitments, including cash interest payments due on the CIC convertible debenture (refer to Note 1).

If for any reason, the Company is unable to continue as a going concern, then this could result in adjustments to the amounts and classifications of assets and liabilities in the Company's consolidated financial statements and such adjustments could be material.

Valuation of embedded derivatives

The embedded derivatives in the Company's convertible debenture are valued using a Monte Carlo simulation valuation model. A Monte Carlo simulation model is a valuation model that relies on random sampling and is often used when modeling systems with a large number of inputs and where there is significant uncertainty in the future value of inputs and where the movement of the inputs can be independent of each other.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

The key inputs used by the Company in its Monte Carlo simulation are further disclosed in Note 19.2 and Note 19.3. Changes in the inputs to the valuation model could impact the carrying value of the embedded derivatives in the convertible debenture and the amount of unrealized gains or losses recognized in profit or loss. The carrying value of the embedded derivatives in the Company's convertible debenture as at December 31, 2013 was a liability of $3,395 (December 31, 2012: $8,876).

Review of carrying value of assets and impairment charges

In the determination of carrying values and impairment charges, management of the Company reviews the recoverable amount (the higher of the fair value less costs to sell or the value in use) in the case of non-financial assets and objective evidence indicating impairment in the case of financial assets. These determinations and their individual assumptions require that management make a decision based on the best available information at each reporting period. Changes in these assumptions may alter the results of non-financial asset and financial asset impairment testing, impairment charges recognized in profit or loss and the resulting carrying amounts of assets.

Dry coal handling facility

Refer to Note 16.3 for further analysis of the $66,325 impairment charge recorded on the dry coal handling facility ("DCHF") at the Ovoot Tolgoi Mine.

Prepaid toll washing fees

Refer to Note 15 for further analysis of the $30,152 impairment loss recorded on the prepaid toll washing fees which are part of the contract with Ejinaqi Jinda Coal Industry Co. Ltd ("Ejin Jinda").

Ovoot Tolgoi Mine cash generating unit

The Company determined that an indicator of impairment existed for its Ovoot Tolgoi Mine cash generating unit as at December 31, 2013. The impairment indicator was the continued weakness in the Company's share price during 2013 and the fact that the market capitalization of the Company, as at December 31, 2013, was less than the carrying value of its net assets.

Therefore, the Company conducted an impairment test whereby the carrying value of the Company's Ovoot Tolgoi Mine cash generating unit was compared to its "value in use" using a discounted future cash flow valuation model. The Company's Ovoot Tolgoi Mine cash generating unit carrying value was $416,559 as at December 31, 2013.

Key estimates and assumptions incorporated in the valuation model included the following:

- Long term real selling price of $110 per tonne for semi-soft coking coal FOB Australia;
- Life-of-mine coal production and operating costs; and
- A discount rate of 12.5% based on an analysis of market, country and company specific factors

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Key sensitivities in the valuation model are as follows:

- For each 1% increase/(decrease) in the long term real selling price of semi-soft coal FOB Australia, the calculated fair value of the cash generating unit increases/(decreases) by approximately $34,000/($34,000); and
- For each 1% increase/(decrease) in the discount rate, the calculated fair value of the cash generating unit (decreases)/increases by approximately ($44,000)/$50,000.

The impairment analysis did not result in the identification of an impairment loss and no charge was required as at December 31, 2013. The Company believes that the estimates and assumptions incorporated in the impairment analysis are reasonable; however, the estimates and assumptions are subject to significant uncertainties and judgments.

Estimated recoverable reserves

Reserve estimates involve expressions of judgment based on various factors such as knowledge, experience and industry practice, and the accuracy of these estimates may be affected by many factors, including estimates and assumptions with respect to coal prices, operating costs, mine plan and life, coal quality and recovery, foreign currency exchange rates and inflation rates. Reserve estimates are made by qualified persons, but will be impacted by changes in the above estimates and assumptions.

Estimated recoverable reserves are used to determine the depletion of mineral properties, in accounting for deferred production stripping costs, in performing impairment testing and for forecasting the timing of the payment of decommissioning, restoration and similar costs. Therefore, changes in the estimates and assumptions used to determine recoverable reserves could impact the carrying value of assets, depletion expense and impairment charges recognized in profit or loss and the carrying value of the decommissioning, restoration and similar liabilities.

Useful lives and depreciation rates for property, plant and equipment

Depreciation expense is allocated based on estimated property, plant and equipment useful lives and depreciation rates. Therefore, changes in the useful life or depreciation rates from the initial estimate could impact the carrying value of property, plant and equipment and an adjustment would be recognized in profit or loss.

Income taxes and recoverability of deferred tax assets

Actual amounts of income tax expense are not final until tax returns are filed and accepted by the taxation authorities. Therefore, profit or loss in future reporting periods will be affected by the amount that income tax expense estimates differ from the final tax returns. Judgment is required in determining whether deferred tax assets are recognized on the statement of financial position. Deferred tax assets, including those arising from unutilized tax losses, require management of the Company to assess the likelihood that the Company will generate sufficient taxable profit in future periods in order to utilize recognized deferred tax assets. Estimates of future taxable profit 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 profit differ from estimates, the ability of the Company to realize the deferred tax assets recorded on the statement of financial position could be impacted. The carrying value of the Company's deferred income tax assets as at December 31, 2013 was $nil (December 31, 2012: $24,984).

(Expressed in thousands of U.S. Dollars and shares in thousands, unless otherwise indicated)

4. SEGMENTED INFORMATION

The Company's one reportable operating segment is its Mongolian Coal Division. The Company's Chief Executive Officer (chief operating decision maker) reviews the Mongolian Coal Division's discrete financial information in order to make decisions about resources to be allocated to the segment and to assess its performance. The division is principally engaged in coal mining, development and exploration in Mongolia. The Company's Corporate Division does not earn revenues and therefore does not meet the definition of an operating segment.

During the year ended December 31, 2013, the Mongolian Coal Division had 6 active customers with the largest customer accounting for 52% of revenues, the second largest customer accounting for 17% of revenue, the third largest customer accounting for 16% of revenue and the other customers accounting for the remaining 15% of revenue.

The carrying amounts of the Company's assets, liabilities, reported income or loss and revenues analyzed by operating segment are as follows:

	Mongolian Coal Division	Unallocated (i)	Consolidated Total
Segment assets			
As at December 31, 2013	$ 490,949	$ 15,257	$ 506,206
As at December 31, 2012	676,981	55,471	732,452
Segment liabilities			
As at December 31, 2013	$ 25,393	$ 105,756	$ 131,149
As at December 31, 2012	19,496	108,973	128,469
Segment loss			
For the year ended December 31, 2013	$ (199,248)	$ (38,216)	$ (237,464)
For the year ended December 31, 2012	(84,992)	(12,510)	(97,502)
Segment revenues			
For the year ended December 31, 2013	$ 58,636	$ -	$ 58,636
For the year ended December 31, 2012	78,061	-	78,061
Impairment charge on assets (ii) (iii)			
For the year ended December 31, 2013	$ 138,718	$ 3,067	$ 141,785
For the year ended December 31, 2012	36,808	19,184	55,992

(i) The unallocated amount contains all amounts associated with the Corporate Division.
(ii) The impairment charge on assets for the year ended December 31, 2012 relates to trade and other receivables (Note 12), investments (Note 13), inventories (Note 14) and property, plant and equipment (Note 16).
(iii) The impairment charge on assets for the year ended December 31, 2013 relates to trade and other receivables (Note 12), investments (Note 13), inventories (Note 14), prepaid expenses and deposits (Note 15) and property, plant and equipment (Note 16).

The operations of the Company are primarily located in Mongolia, Hong Kong and Canada.

	Mongolia	Hong Kong	Canada	Consolidated Total
Revenues				
For the year ended December 31, 2013	$ 58,636	$ -	$ -	$ 58,636
For the year ended December 31, 2012	78,061	-	-	78,061
Non-current assets				
As at December 31, 2013	$ 422,679	$ 81	$ 7,237	$ 429,997
As at December 31, 2012	566,629	100	20,590	587,319

(Expressed in thousands of U.S. Dollars and shares in thousands, unless otherwise indicated)

5. COST OF SALES

The Company's cost of sales consists of the following amounts:

	Year ended December 31, 2013	2012
Operating expenses	**$ 41,746**	$ 39,671
Share-based compensation expense/(recovery) (Note 22)	**(293)**	1,205
Depreciation and depletion	**20,000**	13,042
Impairment of coal stockpile inventories (Note 14)	**20,735**	20,531
Cost of sales from mine operations	**82,188**	74,449
Cost of sales related to idled mine assets (i)	**30,439**	52,958
Cost of sales	**$ 112,627**	$ 127,407

(i) Cost of sales related to idled mine assets for the year ended December 31, 2013 includes $25,053 of depreciation expense (2012: includes $33,198 of depreciation expenses and $942 of share-based compensation expense). The depreciation expense relates to the Company's idled plant and equipment.

The Company curtailed its mining activities at the Ovoot Tolgoi Mine during the three months ended June 30, 2012 to varying degrees to manage coal inventories and to maintain efficient working capital levels. As at June 30, 2012, mining activities had been fully curtailed and remained curtailed for the remainder of 2012. The 2012 idled mine asset depreciation expense relates to the Company's idled plant and equipment during the curtailment of its mining activities. The Company's mining activities remained fully curtailed until March 22, 2013, when the Company recommenced mining activities at the Ovoot Tolgoi Mine. The 2013 idled mine asset depreciation expense relates to the Company's idled plant and equipment as the 2013 production plan did not fully utilize the Company's existing mining fleet.

6. OTHER OPERATING EXPENSES

The Company's other operating expenses consist of the following amounts:

	Year ended December 31, 2013	2012
Public infrastructure	**$ 7**	$ 1,273
Sustainability and community relations	**235**	894
Foreign exchange loss	**1,659**	3,226
Provision for doubtful trade and other receivables (Note 12)	**200**	1,032
Mark-to-market loss on available-for-sale financial asset (Note 13)	**3,067**	19,184
Loss on disposal of property, plant and equipment (Note 16)	**895**	720
Impairment of property, plant and equipment (Note 16)	**72,669**	15,245
Impairment of prepaid expenses and deposits (Note 15)	**30,152**	-
Impairment of materials and supplies inventories (Note 14)	**14,962**	-
Other	**2,194**	71
Other operating expenses	**$ 126,040**	$ 41,645

(Expressed in thousands of U.S. Dollars and shares in thousands, unless otherwise indicated)

7. ADMINISTRATION EXPENSES

The Company's administration expenses consist of the following amounts:

	Year ended December 31,	
	2013	2012
Corporate administration	**$ 3,269**	$ 5,525
Professional fees	**8,252**	7,293
Salaries and benefits	**3,748**	5,556
Share-based compensation expense (Note 22)	**167**	6,048
Depreciation	**193**	215
Administration expenses	**$ 15,629**	$ 24,637

8. EVALUATION AND EXPLORATION EXPENSES

The Company's evaluation and exploration expenses consist of the following amounts:

	Year ended December 31,	
	2013	2012
Drilling and trenching	**$ 243**	$ 3,708
Other direct expenses	**84**	655
License fees	**657**	773
Share-based compensation expense (Note 22)	**21**	333
Overhead and other	**164**	3,129
Evaluation and exploration expenses	**$ 1,169**	$ 8,598

9. FINANCE COSTS AND INCOME

The Company's finance costs consist of the following amounts:

	Year ended December 31,	
	2013	2012
Interest expense on convertible debenture (Note 19)	**$ 20,290**	$ 10,466
Unrealized loss on FVTPL investments	**656**	4,482
Interest expense on line of credit facility	**11**	322
Realized loss on disposal of FVTPL investments (Note 13)	**91**	-
Accretion of decommissioning liability (Note 20)	**114**	115
Finance costs	**$ 21,162**	$ 15,385

The Company's finance income consists of the following amounts:

	Year ended December 31,	
	2013	2012
Unrealized gain on embedded derivatives in convertible debenture (Note 19)	**$ 5,481**	$ 39,512
Interest income	**85**	406
Realized gain on disposal of FVTPL investments	**-**	24
Finance income	**$ 5,566**	$ 39,942

(Expressed in thousands of U.S. Dollars and shares in thousands, unless otherwise indicated)

10. TAXES

10.1 Income tax recognized in profit or loss

A reconciliation between the Company's tax expense/(recovery) and the product of the Company's loss before tax multiplied by the Company's domestic tax rate is as follows:

	Year ended December 31,	
	2013	**2012**
Loss before tax	**$ 212,478**	$ 99,034
Statutory tax rate	**25.75%**	25.00%
Income tax recovery based on combined Canadian federal and provincial statutory rates	**(54,713)**	(24,759)
Deduct:		
Lower effective tax rate in foreign jurisdictions	**1,467**	323
Tax effect of tax losses and temporary differences not recognized	**59,878**	15,563
Non-deductible expenses	**18,354**	7,341
Income tax expenses/(recovery)	**$ 24,986**	$ (1,532)

10.2 Income tax recognized in other comprehensive income

	Year ended December 31,	
	2013	**2012**
Fair value remeasurement of available-for-sale financial asset	**$ -**	$ (2,366)
Deferred tax recovery	**$ -**	$ (2,366)

10.3 Deferred tax balances

The Company's deferred tax assets consist of the following amounts:

	As at December 31,	
	2013	**2012**
Tax loss carryforwards	**$ 332**	$ 8,473
Property, plant and equipment	**-**	5,048
Other assets	**(332)**	11,463
Total deferred tax balances	**$ -**	$ 24,984

(i) Deferred income tax expense for the year ended December 31 2013 includes a $17,487 expense related to the derecognition of deferred tax assets (2012: $nil).

(Expressed in thousands of U.S. Dollars and shares in thousands, unless otherwise indicated)

10. TAXES (CONTINUED)

10.4 Unrecognized deductible temporary differences and unused tax losses

The Company's deductible temporary differences and unused tax losses for which no deferred tax asset is recognized consist of the following amounts:

	As at December 31, 2013	As at December 31, 2012
Non-capital losses	$ 136,185	$ 46,130
Capital losses	2,676	-
Deductible temporary differences	257,016	103,589
Total unrecognized amounts	$ 395,877	$ 149,719

10.5 Expiry dates

The expiry dates of the Company's unused tax losses are as follows:

	As at December 31, 2013 U.S. Dollar Equivalent	As at December 31, 2013 Expiry dates
Non-capital losses		
Canada	$ 65,494	2032 - 2033
Mongolia	57,890	2016 - 2017
Hong Kong	13,990	indefinite
Singapore	137	indefinite
	$ 137,511	
Capital losses		
Canada	2,676	indefinite

(Expressed in thousands of U.S. Dollars and shares in thousands, unless otherwise indicated)

11. LOSS PER SHARE

The calculation of basic loss and diluted loss per share is based on the following data:

	Year ended December 31, 2013	2012
Net loss	$ (237,464)	$ (97,502)
Weighted average number of shares	182,883	181,859
Basic loss per share	**$ (1.30)**	$ (0.54)
Loss		
Net loss	$ (237,464)	$ (97,502)
Interest expense on convertible debenture	-	10,466
Unrealized gain on embedded derivatives in convertible debenture	-	(39,512)
Diluted net loss	$ (237,464)	$ (126,548)
Number of shares		
Weighted average number of shares	182,883	181,859
Convertible debenture (i)	-	28,406
Diluted weighted average number of shares	182,883	210,265
Diluted loss per share	**$ (1.30)**	$ (0.60)

(i) The convertible debenture was anti-dilutive for the year ended December 31, 2013

Potentially dilutive items not included in the calculation of diluted loss per share for the year ended December 31, 2013 were 2,583 stock options that were anti-dilutive.

12. TRADE AND OTHER RECEIVABLES

The Company's trade and other receivables consist of the following amounts:

	As at December 31, 2013	2012
Trade receivables	$ 1,818	$ 1,439
Other receivables	760	1,853
Total trade and other receivables	**$ 2,578**	$ 3,292

The aging of the Company's trade and other receivables is as follows:

	As at December 31, 2013	2012
Less than 1 month	$ 396	$ 2,376
1 to 3 months	1,321	95
3 to 6 months	141	159
Over 6 months	720	662
Total trade and other receivables	**$ 2,578**	$ 3,292

Included in trade and other receivables are amounts due from related parties which are further disclosed in Note 26. The amounts due from related parties are unsecured, interest free and repayable upon written notice from the Company.

(Expressed in thousands of U.S. Dollars and shares in thousands, unless otherwise indicated)

12. TRADE AND OTHER RECEIVABLES (CONTINUED)

Trade receivables are normally due within 30 days from the date of billing. Customers with balances that are more than 30 days past due are normally requested to settle all outstanding balances before any further credit is granted.

For the year ended December 31, 2013, the Company recorded a $200 loss provision on its trade and other receivables in other operating expenses (2012: $1,032). The loss provisions relate to a reduction in expected insurance proceeds. The Company anticipates full recovery of its remaining outstanding trade and other receivables; therefore, no further loss provisions have been recorded in respect of the Company's trade and other receivables.

13. INVESTMENTS

The Company's investments consist of the following amounts:

	As at December 31,	
	2013	2012
Current investments at fair value		
Money market investments	$ -	$ 15,000
Non-current investments at fair value		
Investment in Kangaroo Resources Limited (i)	222	1,455
Investment in Aspire Mining Limited (ii)	6,175	8,727
Non-current investment in joint venture		
Investment in RDCC LLC	24,205	13,902
	30,602	24,084
Total investments	$ 30,602	$ 39,084

(i) At December 31, 2013, the Company owned 0.5% of Kangaroo's issued and outstanding shares.
(ii) At December 31, 2013, the Company owned 18.8% of Aspire's issued and outstanding shares.

13.1 Investment in Kangaroo Resources Limited

Kangaroo Resources Limited ("Kangaroo") is a company listed on the Australian Securities Exchange. Kangaroo's primary focus is its coal projects in Indonesia. The Company classifies its investment in Kangaroo as a FVTPL financial asset with any change in value being recognized in profit or loss. During the year ended December 31, 2013, the Company disposed of 22,236 shares of Kangaroo for gross proceeds of $486 and realized a loss of $91. For the year ended December 31, 2013, the Company recognized an unrealized mark to market loss of $656 related to its investment in Kangaroo (2012: loss of $4,515).

13.2 Investment in Aspire Mining Limited

Aspire Mining Limited ("Aspire") is a company listed on the Australian Securities Exchange. Aspire's primary focus is its mineral exploration and mining licenses in Mongolia, particularly those pertaining to the Ovoot Coking Coal Project. The Company classifies its investment in Aspire as an available-for-sale financial asset.

(Expressed in thousands of U.S. Dollars and shares in thousands, unless otherwise indicated)

13. INVESTMENTS (CONTINUED)

During the year ended December 31, 2012, it was determined that objective evidence of impairment in the Company's investment in Aspire existed and such evidence continued to exist during the year ended December 31, 2013. Therefore, an impairment loss of $3,067 was recognized for the year ended December 31, 2013 in other operating expenses (2012: loss of $19,184) . The impairment loss represents the difference between the acquisition cost of the Company's investment in Aspire and its fair market value at December 31, 2013.

13.3 Investment in RDCC LLC

The Company has a 40% interest in RDCC LLC, a joint venture. RDCC LLC has signed a concession agreement with the State Property Committee of Mongolia to construct a paved highway from the Company's Ovoot Tolgoi Mine to the Mongolia-China border. The concession agreement is structured as a 17-year build, operate and transfer agreement.

RDCC LLC accounts for the concession agreement in accordance with IFRIC 12 "Service Concession Arrangements" under the intangible asset model. In accordance with IFRIC 12, infrastructure associated with the concession agreement is recorded by RDCC LLC as an intangible asset. Construction revenue is recognized during the construction phase of the concession agreement as an exchange of construction services for the intangible asset and toll revenue is recognized during the operational phase of the concession agreement.

The movement of the Company's investment in RDCC LLC is as follows:

	Year ended December 31,	
	2013	**2012**
Balance, beginning of year	**$ 13,902**	$ 3
Funds advanced	**10,356**	13,264
Share of earnings/(losses) of joint venture	**(53)**	635
Balance, end of year	**$ 24,205**	$ 13,902

Summarized financial statement information of RDCC LLC is as follows:

	As at December 31,	
	2013	**2012**
Current assets	**$ 3,254**	$ 1,850
Non-current assets	**37,292**	20,075
Total assets	**$ 40,546**	$ 21,925
Current liabilities	**$ 1**	$ 97
Total liabilities	**$ 1**	$ 97

	Year ended December 31,	
	2013	**2012**
Construction revenue	**$ 21,219**	$ 20,203
Gross profit margin	**12**	1,837
Other operating and finance costs	**(144)**	(248)
Income/(loss) before tax	**(133)**	1,588
Net income/(loss)	**$ (133)**	$ 1,588

(Expressed in thousands of U.S. Dollars and shares in thousands, unless otherwise indicated)

14. INVENTORIES

The Company's inventories consist of the following amounts:

	As at December 31, 2013	2012
Coal stockpiles	$ 8,305	$ 16,048
Materials and supplies	31,983	43,687
Total inventories	$ 40,288	$ 59,735

Cost of sales for the year ended December 31, 2013 includes an impairment loss of $20,735 related to the Company's coal stockpile inventories (2012: $20,531). As at December 31, 2013, $4,853 of the Company's coal stockpile inventories are carried at their net realizable value (2012: $7,858).

Other operating expenses for the year ended December 31, 2013 includes an impairment loss of $14,962 related to surplus materials and supplies inventories. These items are not expected to be utilized with the Company's existing mining fleet and, therefore, were adjusted to their net realizable value during the year ended December 31, 2013.

15. PREPAID EXPENSES AND DEPOSITS

The Company's prepaid expenses and deposits consist of the following amounts:

	As at December 31, 2013	2012
Vendor prepayments	$ 6,044	$ 11,628
Ejin Jinda toll coal washing prepayment	3,405	16,778
Other prepaid expenses and deposits	2,057	19,026
Total short term prepaid expenses and deposits	11,506	47,432
Ejin Jinda toll coal washing prepayment	-	16,778
Total short and long term prepaid expenses and deposits	$ 11,506	$ 64,210

15.1 Ejin Jinda toll coal washing prepayment

During the year ended December 31, 2011, the Company entered into an agreement with Ejin Jinda, a subsidiary of China Mongolia Coal Co. Ltd., to toll wash coal from the Ovoot Tolgoi Mine. The agreement has a duration of 5-years from commencement and provides for an annual wet washing capacity of approximately 3.5 million tonnes of input raw coal.

Commercial operations at the wet washing facility have not commenced. The Company identified the results of a trial sample from the wet washing facility and the delay in starting the commercial operations at the wet washing facility as indicators of impairment for the prepaid toll washing fees which are part of the contract with Ejin Jinda. Based on updated estimates and assumptions related to wash yields from the facility, a $30,152 impairment loss on the $33,556 of prepaid toll washing fees was recorded in other operating expenses during the year ended December 31, 2013.

(Expressed in thousands of U.S. Dollars and shares in thousands, unless otherwise indicated)

16. PROPERTY, PLANT AND EQUIPMENT

The Company's property, plant and equipment consist of the following amounts:

	Mobile equipment	Other operating equipment	Buildings and roads	Mineral properties	Construction in progress	Total
Cost						
As at December 31, 2012	$ 366,159	$ 28,043	$ 69,922	$ 116,084	$ 55,912	$ 636,120
Additions	**1,162**	**266**	**2,129**	**10,984**	**122**	**14,663**
Disposals	**(3,632)**	**(507)**	**-**	**-**	**-**	**(4,139)**
Reclassifications	**-**	**548**	**163**	**-**	**(711)**	**-**
As at December 31, 2013	**$ 363,689**	**$ 28,350**	**$ 72,214**	**$ 127,068**	**$ 55,323**	**$ 646,644**
Accumulated depreciation and impairment charges						
As at December 31, 2012	$ (93,519)	$ (7,359)	$ (9,299)	$ (4,470)	$ -	$ (114,647)
Charge for the year	**(39,908)**	**(4,581)**	**(6,565)**	**(10,420)**	**-**	**(61,474)**
Impairment charges	**(6,267)**	**(5,765)**	**(11,590)**	**-**	**(49,047)**	**(72,669)**
Eliminated on disposals	**1,067**	**474**	**-**	**-**	**-**	**1,541**
As at December 31, 2013	**$ (138,627)**	**$ (17,231)**	**$ (27,454)**	**$ (14,890)**	**$ (49,047)**	**$ (247,249)**
Carrying amount						
As at December 31, 2012	$ 272,640	$ 20,684	$ 60,623	$ 111,614	$ 55,912	$ 521,473
As at December 31, 2013	**$ 225,062**	**$ 11,119**	**$ 44,760**	**$ 112,178**	**$ 6,276**	**$ 399,395**

	Mobile equipment	Other operating equipment	Buildings and roads	Mineral properties	Construction in progress	Total
Cost						
As at December 31, 2011	$ 333,245	$ 10,253	$ 31,155	$ 94,641	$ 82,569	$ 551,863
Additions	46,375	1,677	2,844	20,215	29,022	100,133
Disposals	(13,461)	(1,279)	(10)	-	-	(14,750)
Reclassifications	-	17,392	35,933	1,228	(54,553)	-
As at December 31, 2012	$ 366,159	$ 28,043	$ 69,922	$ 116,084	$ 57,038	$ 637,246
Accumulated depreciation and impairment charges						
As at December 31, 2011	$ (41,498)	$ (3,465)	$ (4,631)	$ (3,736)	$ -	$ (53,330)
Charge for the year	(39,509)	(4,873)	(4,677)	(734)	-	(49,793)
Impairment charges	(14,119)	-	-	-	(1,126)	(15,245)
Eliminated on disposals	1,607	979	9	-	-	2,595
As at December 31, 2012	$ (93,519)	$ (7,359)	$ (9,299)	$ (4,470)	$ (1,126)	$ (115,773)
Carrying amount						
As at December 31, 2011	$ 291,747	$ 6,788	$ 26,524	$ 90,905	$ 82,569	$ 498,533
As at December 31, 2012	$ 272,640	$ 20,684	$ 60,623	$ 111,614	$ 55,912	$ 521,473

16. PROPERTY, PLANT AND EQUIPMENT (CONTINUED)

16.1 Borrowing costs

For the year ended December 31, 2013, the Company did not capitalize borrowing costs into construction in progress as the Company suspended active development of its qualifying assets (2012: $9,628).

16.2 Prepayments on property, plant and equipment

As at December 31, 2013, the cost of the Company's property, plant and equipment includes $41,240 of prepayments to vendors (December 31, 2012: $81,370). The prepayments primarily relate to ordered but not yet delivered mobile equipment or mobile equipment delivered to the location of its intended use but not yet commissioned.

16.3 Impairment charges

For the year ended December 31, 2013, the Company recorded $72,669 of impairment charges to reduce various items of property, plant and equipment to their recoverable amounts. The impairments relate to the following items of property, plant and equipment:

- DCHF – following an extensive review that commenced in the fourth quarter of 2013, the Company concluded that it does not plan to either complete or use the DCHF at the Ovoot Tolgoi Mine in the foreseeable future. This conclusion constituted an indicator of impairment and the Company performed an impairment assessment over the DCHF. As a result of the impairment assessment, the Company recorded a $66,325 impairment charge to reduce the carrying value of the DCHF to its recoverable amount. The Company used a value in use cash flow model, with a discount rate of 10.4%, to estimate the recoverable amount. The Company has assessed, using updated assumptions and estimates, that it currently has the adequate equipment and capacity to efficiently meet its commercial objectives and execute its product strategy without the use of the DCHF. The use of mobile screens at stockpile areas closer to the pits has enabled the Company to realize a cost benefit compared to hauling the coal to the central DCHF and operating the rotary breaker. This provides a lower cost solution without adversely impacting the coal quality of the coal planned to be mined in the foreseeable future. Subsequent to the impairment charge, the DCHF has a carrying value of $11,200 at December 31, 2013 (December 31, 2012: $80,458).
- Surplus capital spares – the Company recorded an impairment provision of $6,344 related to surplus capital spares not expected to be utilized with the Company's existing mining fleet.

For the year ended December 31, 2012, the Company recorded $15,245 of impairment charges to reduce various items of mobile equipment and construction in progress to their recoverable amounts.

17. TRADE AND OTHER PAYABLES

Trade and other payables of the Company primarily consists of amounts outstanding for trade purchases relating to coal mining, development and exploration activities and mining royalties payable. The usual credit period taken for trade purchases is between 30 to 90 days.

(Expressed in thousands of U.S. Dollars and shares in thousands, unless otherwise indicated)

17. TRADE AND OTHER PAYABLES (CONTINUED)

The aging of the Company's trade and other payables is as follows:

	As at December 31,	
	2013	2012
Less than 1 month	$ 28,786	$ 8,999
1 to 3 months	554	176
3 to 6 months	367	-
Over 6 months	1,534	1,041
Total trade and other payables	$ 31,241	$ 10,216

Included in trade and other payables are amounts due to related parties which are further disclosed in Note 26.

18. LINE OF CREDIT FACILITY

As at December 31, 2012, the Company had a twelve month revolving line of credit facility with Golomt Bank in Mongolia. The maximum draw-down available was $3,500 and 8.1 billion Mongolian Tugriks (approximately $5,800) and the line of credit incurred interest at 11% for any U.S. Dollar amounts outstanding and 12% for any Mongolian Tugrik amounts outstanding. The line of credit was secured by operating equipment in Mongolia to a value of not less than 150% of the total facility amount.

The line of credit facility was used by the Company's Mongolian Coal Division as part of its working capital management. The line of credit facility expired on January 19, 2013 and was not renewed.

19. CONVERTIBLE DEBENTURE

19.1 Key commercial terms

On November 19, 2009, the Company issued a convertible debenture to a wholly owned subsidiary of CIC for $500,000.

The Company had the right to call for the conversion of up to $250,000 of the debenture on the earlier of twenty four months after the issue date, if the conversion price was greater than Cdn$10.66, or upon the Company achieving a public float of 25% of its common shares under certain agreed circumstances, if the conversion price was greater than Cdn$10.66. On March 29, 2010, pursuant to the debenture conversion terms, the Company exercised this conversion right and completed the conversion of $250,000 of the convertible debenture into 21,471 shares at a conversion price of $11.64 (Cdn$11.88).

19. CONVERTIBLE DEBENTURE (CONTINUED)

The key commercial terms of the financing include:

- Interest - 8% per annum (6.4% payable semi-annually in cash and 1.6% payable annually in the Company's common shares, where the number of shares to be issued is calculated based on the 50-day volume-weighted average price ("VWAP")).
- Term - Maximum of 30 years.
- Security - First charge over the Company's assets, including shares of its material subsidiaries. An event of default on the convertible debenture can be triggered as a result of certain encumbrances on the Company's assets (Note 29.3).
- Conversion price - The conversion price is set as the lower of Cdn$11.88 or the 50-day VWAP at the date of conversion, with a floor price of Cdn$8.88 per share.
- CIC's conversion right - CIC has the right to convert the convertible debenture, in whole or in part, into common shares twelve months after the date of issue.
- Company's normal conversion right – After sixty months from the issuance date, and when the conversion price is greater than Cdn$10.66, the Company is entitled to force conversion of the outstanding convertible debenture, in whole or in part, into common shares at the conversion price.
- Representation on the Company's Board - While the convertible debenture is outstanding, or while CIC has a minimum 15% direct or indirect stake in the Company, CIC has the right to nominate one director to the Company's Board of Directors. The Company currently has nine Board of Directors members of which none were elected by CIC.
- Voting restriction - CIC has agreed that it will not have any voting rights in the Company beyond 29.9% if CIC ever acquires ownership of such a shareholder stake.
- Pre-emption rights - While the convertible debenture is outstanding, or while CIC has a 15% direct or indirect stake in the Company, CIC has certain pre-emption rights on a pro-rata basis to subscribe for any new shares to be allotted and issued by the Company for the period which the convertible debenture is outstanding. The pre-emption rights will not apply to new shares issued pursuant to pro-rata public equity offerings made to all shareholders, exercise of stock options and shares issued to achieve a 25% public float.
- Right of first offer - While a portion of the convertible debenture is outstanding, or while CIC has a 15% direct or indirect stake in the Company, CIC has the right of first offer for any direct and indirect sale of Turquoise Hill's ownership stake in the Company. At December 31, 2013, Turquoise Hill owned directly and indirectly approximately 56% of the Company's issued and outstanding shares.
- Registration rights - CIC has registration rights under applicable Canadian provincial securities laws in connection with the common shares issuable upon conversion of the convertible debenture.

19.2 Debt host and embedded derivatives

The convertible debenture is presented as a liability since it contains no equity components. The convertible debenture is a hybrid instrument, containing a debt host component and three embedded derivatives - the investor's conversion option, the issuer's conversion option and the equity based interest payment provision (the 1.6% share interest payment) (the "embedded derivatives"). The debt host component is classified as other-financial-liabilities and is measured at amortized cost using the effective interest rate method and the embedded derivatives are classified as FVTPL and all changes in fair value are recorded in profit or loss. The difference between the debt host component and the principal amount of the loan outstanding is accreted to profit or loss over the expected life of the convertible debenture.

(Expressed in thousands of U.S. Dollars and shares in thousands, unless otherwise indicated)

19. CONVERTIBLE DEBENTURE (CONTINUED)

The embedded derivatives were valued upon initial measurement and subsequent periods using a Monte Carlo simulation valuation model. A Monte Carlo simulation model is a valuation model that relies on random sampling and is often used when modeling systems with a large number of inputs and where there is significant uncertainty in the future value of inputs and where the movement of the inputs can be independent of each other. Some of the key inputs used by the Company in its Monte Carlo simulation include: the floor and ceiling conversion prices, the Company's common share price, the risk-free rate of return, expected volatility of the Company's common share price, forward foreign exchange rate curves (between the Cdn$ and U.S. Dollar) and spot foreign exchange rates.

19.3 Valuation assumptions

The assumptions used in the Company's valuation models are as follows:

	As at December 31,	
	2013	**2012**
Floor conversion price	**Cdn$8.88**	Cdn$8.88
Ceiling conversion price	**Cdn$11.88**	Cdn$11.88
Common share price	**Cdn$0.84**	Cdn$2.05
Historical volatility	**71%**	70%
Risk free rate of return	**3.11%**	2.26%
Foreign exchange spot rate (Cdn$ to U.S. Dollar)	**0.94**	1.01
Forward foreign exchange rate curve (Cdn$ to U.S. Dollar)	**0.92 - 0.94**	0.96 - 1.01

19.4 Presentation

Based on the Company's valuation as at December 31, 2013, the fair value of the embedded derivatives decreased by $5,481 compared to December 31, 2012. The decrease was recorded as finance income for the year ended December 31, 2013.

For the year ended December 31, 2013, the Company recorded interest expense of $20,290 related to the convertible debenture as a finance cost (2012: the Company recorded interest expenses of $20,094 related to the convertible debenture of which $9,628 was capitalized as borrowing costs and the remaining $10,466 was recorded as a finance cost). The interest expense consists of the interest at the contract rate and the accretion of the debt host component of the convertible debenture. To calculate the accretion expense, the Company uses the contract life of 30 years and an effective interest rate of 22.2%.

The movements of the amounts due under the convertible debenture are as follows:

	Year ended December 31,	
	2013	**2012**
Balance, beginning of year	**$ 105,968**	$ 145,386
Interest expense on convertible debenture	**20,290**	20,094
Decrease in fair value of embedded derivatives	**(5,481)**	(39,512)
Interest paid	**(24,174)**	(20,000)
Balance, end of year	**$ 96,603**	$ 105,968

(Expressed in thousands of U.S. Dollars and shares in thousands, unless otherwise indicated)

19. CONVERTIBLE DEBENTURE (CONTINUED)

The convertible debenture balance consists of the following amounts:

	As at December 31,	
	2013	2012
Current convertible debenture		
Interest payable	$ **2,301**	6,301
Non-current convertible debenture		
Debt host	**90,907**	$ 90,791
Fair value of embedded derivatives	**3,395**	8,876
	94,302	99,667
Total convertible debenture	$ **96,603**	$ 105,968

19.5 Convertible debenture share interest payment and application of Mongolian Foreign Investment Law

On May 17, 2012, the Parliament of Mongolia approved a Law on Regulation of Foreign Investment in Business Entities Operating in Sectors of Strategic Importance (“Foreign Strategic Sectors Law”) that regulated foreign direct investment into a number of key sectors of strategic importance, which included mineral resources.

As a result of the Foreign Strategic Sectors Law, the Company expected that it would require parliamentary approval for the shares to be issued for the November 19, 2012 share interest payment to the CIC. As a result, during the three months ended March 31, 2013, the Company settled the 1.6% share interest payment of $4,000 in cash.

Following amendments to the Foreign Strategic Sectors Law, passed in the three months ended June 30, 2013, the requirement for parliamentary approval was limited to circumstances where a state owned entity is to exceed 49% share ownership of a strategic asset, irrespective of the amount of investment. As a result, the Company is only required to give notice, rather than obtaining parliamentary or other approval, under the Foreign Strategic Sectors Law for the 1.6% share interest payment to the CIC.

On October 3, 2013 Mongolia’s foreign investment environment changed again when the Parliament of Mongolia passed the Investment Law to repeal and replace the Foreign Strategic Sectors Law. The Investment Law regulates, amongst other things, investment by Foreign State Owned Entities (“FSOEs”) in sectors of strategic importance, which includes mineral resources, by requiring that FSOEs obtain a permit from Mongolia’s Ministry of Economic Development if they are to acquire 33% or more of the shareholding of a Mongolian entity operating in a sector of strategic importance. The Company understands that it will not be required to obtain a permit from the Ministry of Economic Development in connection with the 1.6% share interest payment to CIC, unless such share interest payment will result in CIC acquiring 33% or more of the shareholding in the Company. The Company will fully comply with the requirements of the Investment Law in connection with share interest payments.

On September 19, 2013, the Company issued 1,846 common shares to the CIC (Note 19.6). On November 21, 2013, the Company issued 3,463 common shares to settle the $4,000 November 19, 2013 share interest payment. The number of common shares was based on the 50-day volume-weighted average share price on November 19, 2013 of Cdn$1.21.

(Expressed in thousands of U.S. Dollars and shares in thousands, unless otherwise indicated)

19. CONVERTIBLE DEBENTURE (CONTINUED)

19.6 Interest deferral and settlement

During the three months ended June 30, 2013, the Company and the CIC mutually agreed upon a three month deferral of the convertible debenture semi-annual $7,934 cash interest payment due on May 19, 2013. The Company and the CIC subsequently agreed to an additional deferral of one month, and the cash interest payment became due on September 19, 2013.

On September 19, 2013, the Company settled the $7,934 amount, plus additional accrued interest of $173, as follows:

- the Company issued 1,846 common shares to the CIC for the November 19, 2012 1.6% share interest payment, where the number of common shares was based on the 50-day volume-weighted average share price on November 19, 2012 of Cdn$2.16;
- in consideration of the common share issue, the CIC applied the $4,000 in cash already paid by the Company in the three months ended March 31, 2013 for the November 19, 2012 share interest payment against the amount due on September 19, 2013; and
- the Company paid the remaining $4,107 balance in cash.

The mutually agreed upon deferral of the cash interest payment, and subsequent settlement in cash and common shares of the Company, did not trigger an event of default and all other terms of the convertible debenture remain unchanged.

20. DECOMMISSIONING LIABILITY

At December 31, 2013, the decommissioning liability primarily relates to reclamation and closure costs of the Company's Ovoot Tolgoi Mine.

The Ovoot Tolgoi Mine decommissioning liability is calculated as the net present value of the estimated future reclamation and closure costs, which at December 31, 2013 totaled $6,286 (2012: $23,577). The estimated future reclamation and closure costs are discounted at 9.6% per annum (2012: 9.6% per annum) to determine the year end decommissioning liability. The settlement of the decommissioning liability will occur through to 2031.

The movement in the decommissioning liability during the years ended December 31, 2013 and 2012 were as follows:

	Year ended December 31, 2013	2012
Balance, beginning of year	**$ 4,104**	$ 4,156
Adjustments	**(1,910)**	(167)
Accretion	**114**	115
Balance, end of year	**$ 2,308**	$ 4,104

21. EQUITY

21.1 Share capital

The Company has authorized an unlimited number of common and preferred shares with no par value. At December 31, 2013, the Company had 187,309 common shares outstanding (December 31, 2012: 181,928) and no preferred shares outstanding (December 31, 2012: nil).

During the year ended December 31, 2012, the Company repurchased 148 common shares at an average price of Cdn$6.44 per share. The share repurchase program concluded on June 14, 2012. The Company cancelled all of the repurchased shares. No additional common shares were repurchased by the Company during the year ended December 31, 2013.

The Company's volume weighted average share price for the year ended December 31, 2013 was Cdn$1.26 (2012: Cdn$5.45).

21.2 Accumulated deficit and dividends

At December 31, 2013, the Company has accumulated a deficit of $744,494 (December 31, 2012: $507,030). No dividends have been paid or declared by the Company since inception.

22. SHARE-BASED PAYMENTS

22.1 Stock option plan

The Company has a stock option plan which permits the Board of Directors of the Company to grant options to acquire common shares of the Company at the volume weighted average closing price for the five days preceding the date of grant. The Company is authorized to issue stock options for a maximum of 10% of the issued and outstanding common shares pursuant to the stock option plan. The stock option plan permits the Board of Directors of the Company to set the terms for each stock option grant; however, the general terms of stock options granted under the plan include a maximum exercise period of 5 years and a vesting period of 3 years with 33% of the grant vesting on the first anniversary of the grant, 33% vesting on the second anniversary of the grant and 34% vesting on the third anniversary of the grant.

For the year ended December 31, 2013, the Company granted 282 stock options (2012: 2,066) to officers, employees, directors and other eligible persons at exercise prices ranging from Cdn$1.16 to Cdn$2.10 (2012: exercise prices ranging from Cdn$1.92 to Cdn$6.16) and expiry dates ranging from March 27, 2018 to August 14, 2018 (2012: expiry dates ranging from March 21, 2017 to December 6, 2017). The weighted average fair value of the options granted in the year ended December 31, 2013 was estimated at $0.60 (Cdn$0.62) (2012: $2.28, Cdn$2.26) per option at the grant date using the Black-Scholes option pricing model.

(Expressed in thousands of U.S. Dollars and shares in thousands, unless otherwise indicated)

22. SHARE-BASED PAYMENTS (CONTINUED)

The weighted average assumptions used for the Black-Scholes option pricing model were as follows:

	Year ended December 31,	
	2013	**2012**
Risk free interest rate	**1.56%**	1.51%
Expected life	**3.4 years**	3.4 years
Expected volatility (i)	**56%**	59%
Expected dividend per share	**$nil**	$nil

(i) Expected volatility has been calculated based on historical volatility of the Company's publicly traded shares over a period equal to the expected life of the options.

A share-based compensation expense of $151 for the options granted in the year ended December 31, 2013 (2012: $4,383) will be amortized over the vesting period, of which $58 was recognized in the year ended December 31, 2013 (2012: $1,905).

The total share-based compensation recovery for the year ended December 31, 2013 was $105 (2012: share-based compensation expense of $8,528). Share-based compensation expense of $167 (2012: $6,048) has been allocated to administration expenses and $21 (2012: $333) has been allocated to evaluation and exploration expenses. A share-based compensation recovery of $293 (2012: share-based compensation expense of $2,147) has been allocated to cost of sales.

22.2 Outstanding stock options

The option transactions under the stock option plan are as follows:

	Year ended December 31, 2013		Year ended December, 2012	
	Number of options	Weighted average exercise price (Cdn$)	Number of options	Weighted average exercise price (Cdn$)
Balance, beginning of year	**7,507**	**$ 9.72**	10,768	$ 10.73
Options granted	**282**	**1.37**	2,066	4.95
Options excercised	**-**	**-**	(433)	5.81
Options forfeited	**(807)**	**6.91**	(2,099)	9.92
Options expired	**(4,399)**	**10.42**	(2,795)	10.53
Balance, end of year	**2,583**	**$ 8.48**	7,507	$ 9.72

(Expressed in thousands of U.S. Dollars and shares in thousands, unless otherwise indicated)

22. SHARE-BASED PAYMENTS (CONTINUED)

The stock options outstanding and exercisable as at December 31, 2013 are as follows:

	Options Outstanding				Options Exercisable			
Exercise price (Cdn$)	Options outstanding		Weighted average exercise price (Cdn$)	Weighted average remaining contractual life (years)	Options outstanding and exercisable		Weighted average exercise price (Cdn$)	Weighted average remaining contractual life (years)
$1.16 - $2.10	**658**	**$**	**1.68**	**4.19**	**230**	**$**	**1.92**	**3.93**
$5.10 - $10.21	**840**		**8.43**	**2.63**	**651**		**8.72**	**2.52**
$11.51 - $14.25	**1,085**		**12.65**	**1.41**	**1,069**		**12.67**	**1.39**
	2,583	**$**	**8.48**	**2.52**	**1,950**	**$**	**10.08**	**2.07**

23. RESERVES

23.1 Share option reserve

The Company's share option reserve relates to stock options granted by the Company to officers, employees, directors and other eligible persons under its stock option plan. Details about the Company's share-based payments are further disclosed in Note 22.

The share option reserve transactions for the years ended December 31, 2013 and 2012 are as follows:

	Year ended December 31,			
		2013		**2012**
Balance, beginning of year	**$**	**51,303**	$	44,143
Share-based compensation charged/(credited) to operations		**(105)**		8,528
Exercise of share options		**-**		(1,368)
Balance, end of year	**$**	**51,198**	$	51,303

23.2 Investment revaluation reserve

The Company's investment revaluation reserve represents the cumulative gains and losses arising on the revaluation of available-for-sale financial assets that have been recognized in other comprehensive income.

The investment revaluation reserve transactions for the years ended December 31, 2013 and 2012 are as follows:

	Year ended December 31,			
		2013		**2012**
Balance, beginning of year	**$**	**-**	$	16,559
Loss arising on revaluation of available-for-sale financial assets		**(2,553)**		(35,034)
Deferred income tax relating to revaluation of available-for-sale financial assets		**-**		2,366
Reclassification of impairment loss on available-for-sale financial asset		**3,067**		16,109
Balance, end of year	**$**	**514**	$	-

24. CAPITAL RISK MANAGEMENT

The Company's capital risk management objectives are to safeguard the Company's ability to continue as a going concern in order to support the Company's normal operating requirements, continue the development and exploration of its mineral properties and to maintain a flexible capital structure which optimizes the costs of capital at an acceptable risk.

The Company manages its capital structure and makes adjustments to it in light of changes in economic conditions and the risk characteristics of the underlying assets. In order to maintain or adjust the capital structure, the Company may issue new shares, acquire previously issued shares, issue new debt, acquire or dispose of assets or adjust the amount of cash and cash equivalents. In order to facilitate the management of its capital requirements, the Company prepares annual expenditure budgets that are updated as necessary depending on various factors, including capital deployment, results from operations, results from the exploration and development of its properties and general industry conditions. The annual and updated budgets are approved by the Board of Directors.

At December 31, 2013, the Company's capital structure consists of convertible debt (Note 19) and the equity of the Company (Note 21). The Company is not subject to any externally imposed capital requirements. In order to maximize ongoing development efforts, the Company does not pay dividends.

For the year ended December 31, 2013, there were no significant changes in the processes used by the Company or in the Company's objectives and policies for managing its capital. As at December 31, 2013, the Company had cash of $21,837 and working capital of $41,670.

Based on the Company's forecasts for the year ended December 31, 2014, the Company is unlikely to have sufficient capital resources and does not expect to generate sufficient cash flows from mining operations in order to satisfy its ongoing obligations and future contractual commitments, including cash interest payments due on the CIC convertible debenture. Therefore, the Company is actively seeking additional sources of financing to continue operating and meet its objectives (Note 1).

(Expressed in thousands of U.S. Dollars and shares in thousands, unless otherwise indicated)

25. FINANCIAL INSTRUMENTS AND FAIR VALUE MEASUREMENTS

25.1 Categories of financial instruments

The Company's financial assets and financial liabilities are categorized as follows:

	As at December 31, 2013	As at December 31, 2012
Financial assets		
Loans-and-receivables		
Cash	**$ 21,837**	$ 19,674
Trade and other receivables (Note 12)	**2,578**	3,292
Available-for-sale		
Investment in Aspire (Note 13)	**6,175**	8,727
Fair value through profit or loss		
Investment in Kangaroo (Note 13)	**222**	1,455
Money market investments (Note 13)	**-**	15,000
Total financial assets	**$ 30,812**	$ 48,148
Financial liabilities		
Fair value through profit or loss		
Convertible debenture - embedded derivatives (Note 19)	**$ 3,395**	$ 8,876
Other-financial-liabilities		
Trade and other payables (Note 17)	**31,241**	10,216
Convertible debenture - debt host (Note 19)	**93,208**	97,092
Total financial liabilities	**$ 127,844**	$ 116,184

25.2 Fair value

The fair value of financial assets and financial liabilities measured at amortized cost is determined in accordance with generally accepted pricing models based on discounted cash flow analysis or using prices from observable current market transactions. The Company considers that the carrying amount of all its financial assets and financial liabilities measured at amortized cost approximates their fair value.

The fair values of the Company's financial instruments classified as FVTPL or available-for-sale are determined as follows:

- The fair value of financial instruments that are traded on an active liquid market are determined with reference to the quoted market prices. The fair value of the Company's investment in the shares of Kangaroo, shares of Aspire and its money market investments are determined using this methodology.
- The fair value of financial instruments that are not traded in an active market are determined using generally accepted valuation models using inputs that are directly (i.e. prices) or indirectly (i.e. derived from prices) observable. The fair value of the embedded derivatives within the convertible debenture (Note 19) is determined using a Monte Carlo simulation. None of the fair value change in the embedded derivatives for the year ended December 31, 2013 is related to a change in the credit risk of the convertible debenture. All of the change in fair value is associated with changes in market conditions.

(Expressed in thousands of U.S. Dollars and shares in thousands, unless otherwise indicated)

25. FINANCIAL INSTRUMENTS AND FAIR VALUE MEASUREMENTS (CONTINUED)

The fair value of all the other financial instruments of the Company approximates their carrying value because of the demand nature or short-term maturity of these instruments.

The following table provides an analysis of the Company's financial instruments that are measured subsequent to initial recognition at fair value, grouped into Level 1 to 3 based on the degree to which the inputs used to determine the fair value are observable.

- Level 1 fair value measurements are those derived from quoted prices in active markets for identical assets or liabilities.
- Level 2 fair value measurements are those derived from inputs other than quoted prices included within Level 1, that are observable either directly or indirectly.
- Level 3 fair value measurements are those derived from valuation techniques that include inputs that are not based on observable market data. As at December 31, 2013 and 2012, the Company did not have any Level 3 financial instruments.

	As at December 31, 2013			
Recurring measurements	**Level 1**	**Level 2**	**Level 3**	**Total**
Financial assets at fair value				
Investment in Aspire	$ 6,175	$ -	$ -	$ 6,175
Investment in Kangaroo	222	-	-	222
Total financial assets at fair value	$ 6,397	$ -	$ -	$ 6,397
Financial iabilities at fair value				
Convertible debenture - embedded derivatives	$ -	$ 3,395	$ -	$ 3,395
Total financial liabilities at fair value	$ -	$ 3,395	$ -	$ 3,395
Non-recurring measurements				
Assets at fair value				
Inventories	$ -	$ -	$ 4,853	$ -
Total assets at fair value	$ -	$ -	$ 4,853	$ -

(Expressed in thousands of U.S. Dollars and shares in thousands, unless otherwise indicated)

25. FINANCIAL INSTRUMENTS AND FAIR VALUE MEASUREMENTS (CONTINUED)

	As at December 31, 2012			
Recurring measurements	**Level 1**	**Level 2**	**Level 3**	**Total**
Financial assets at fair value				
Investment in Aspire	$ 8,727	$ -	$ -	$ 8,727
Investment in Kangaroo	1,455	-	-	1,455
Money market investments	15,000	-	-	15,000
Total financial assets at fair value	$ 25,182	$ -	$ -	$ 25,182
Financial liabilities at fair value				
Convertible debenture - embedded derivatives	$ -	$ 8,876	$ -	$ 8,876
Total financial liabilities at fair value	$ -	$ 8,876	$ -	$ 8,876
Non-recurring measurements				
Assets at fair value				
Inventories	$ -	$ -	$ 7,858	$ -
Total assets at fair value	$ -	$ -	$ 7,858	$ -

At December 31, 2013, certain coal stockpile inventories were written down to their net realizable value of $4,853 (December 31, 2012: $7,858). The net realizable value has become the carrying value and will not be revalued. Certain assumptions used in the calculation of the net realizable value are categorized as Level 3 in the fair value hierarchy.

There were no transfers between Level 1, 2 and 3 for the year ended December 31, 2013.

25.3 Financial risk management objectives and policies

The financial risk arising from the Company's operations are currency risk, interest rate risk, credit risk, liquidity risk and commodity price risk. These risks arise from the normal course of operations and all transactions undertaken are to support the Company's ability to continue as a going concern. The risks associated with these financial instruments and the policies on how to mitigate these risks are set out below. Management of the Company manages and monitors these exposures to ensure appropriate measures are implemented on a timely and effective manner.

Currency risk

The Company is exposed to foreign currency risk on its sales or purchases in currencies other than the U.S. Dollar. The Company manages this risk by matching receipts and payments in the same currency and through monitoring.

(Expressed in thousands of U.S. Dollars and shares in thousands, unless otherwise indicated)

25. FINANCIAL INSTRUMENTS AND FAIR VALUE MEASUREMENTS (CONTINUED)

The sensitivity of the Company's comprehensive income due to changes in the carrying values of monetary assets and liabilities denominated in foreign currencies is as follows. A positive number indicates an increase in comprehensive income, whereas a negative number indicates a decrease in comprehensive income.

	As at December 31,	
	2013	**2012**
Increase / decrease in foreign exchange rate		
+5%	**$ 59**	$ 177
–5%	**$ (59)**	$ (177)

Interest rate risk

The Company is exposed to interest rate risk on the variable rate of interest earned on its cash. However, the rate of interest earned on these instruments is below 3%; therefore, the interest rate risk is not significant.

The Company's convertible debenture (Note 19) accrues interest at fixed rates; therefore the Company is not exposed to interest rate risk on this instrument.

Credit risk

The Company is exposed to credit risk associated with its cash and trade and other receivables. The Company's maximum exposure to credit risk is equal to the carrying amount of these instruments.

The Company's credit risk on cash arises from default of the counterparty. The Company limits its exposure to counterparty credit risk on cash by only dealing with financial institutions with high credit ratings.

The Company seeks to manage its credit risk on trade and other receivables by trading with third party customers it considers to be creditworthy. It is the Company's policy that all customers who wish to trade on credit terms are subject to credit verification procedures. In addition, the trade and other receivables balances are monitored on an ongoing basis and, if appropriate, the Company records provisions for uncollectible trade and other receivables.

Liquidity risk

Liquidity risk is the risk that the Company will not be able to settle or manage its obligations associated with financial liabilities. Based on the Company's forecasts for the year ended December 31, 2014, the Company is unlikely to have sufficient capital resources and does not expect to generate sufficient cash flows from mining operations in order to satisfy its ongoing obligations and future contractual commitments, including cash interest payments due on the CIC convertible debenture. Therefore, the Company is actively seeking additional sources of financing to continue operating and meet its objectives (Note 1).

(Expressed in thousands of U.S. Dollars and shares in thousands, unless otherwise indicated)

25. FINANCIAL INSTRUMENTS AND FAIR VALUE MEASUREMENTS (CONTINUED)

The Company's current and expected remaining contractual maturities for its financial liabilities with agreed repayment periods are as follows. The table includes the undiscounted cash flows of financial liabilities based on the earliest date on which the Company can be required to satisfy the liabilities.

	0 to 6 months	6 to 12 months	Total
As at December 31, 2013			
Trade and other payables	**$ 31,241**	**$ -**	**$ 31,241**
Convertible debenture - cash interest (Note 19) (i)	**8,000**	**8,000**	**16,000**
	$ 39,241	**$ 8,000**	**$ 47,241**
As at December 31, 2012			
Trade and other payables	$ 10,216	$ -	$ 10,216
Convertible debenture - cash interest (Note 19)	8,000	8,000	16,000
	$ 18,216	$ 8,000	$ 26,216

(i) The expected undiscounted cash flows of the above noted financial liabilities include the cash interest payment on the convertible debenture for the year ended December 31, 2014. Refer to Note 19 for the terms of the convertible debenture.

Commodity price risk

The Company is exposed to the risk of fluctuations in prevailing market prices for its coal products. Coal prices are affected by numerous factors such as interest rates, exchange rates, inflation or deflation and global and regional supply and demand.

The Company enters into sales contracts with its customers to manage the risk of off-take of coal at prevailing market prices by, in most cases, entering into short term coal contracts which fix the quantity and price of the Company's coal. The Company has not entered into any coal hedging instruments to manage its exposure to fluctuations in coal prices. As coal sales are the only source of revenue for the Company, a 5% increase or decrease in coal prices will result in a corresponding increase or decrease in revenue.

(Expressed in thousands of U.S. Dollars and shares in thousands, unless otherwise indicated)

26. RELATED PARTY TRANSACTIONS

The consolidated financial statements include the financial statements of SouthGobi Resources Ltd. and its significant subsidiaries listed in the following table:

Name	Country of incorporation	% equity interest As at December 31, 2013	2012
SouthGobi Resources (Hong Kong) Limited	Hong Kong	100%	100%
SouthGobi Sands LLC	Mongolia	100%	100%
SGQ Coal Investment Pte. Ltd.	Singapore	100%	100%

During the year ended December 31, 2013 and 2012, the Company had related party transactions with the following companies related by way of directors or shareholders in common:

- Turquoise Hill – Turquoise Hill is the Company's immediate parent company and at December 31, 2013 owned approximately 56% of the outstanding common shares of the Company. Turquoise Hill provides various administrative services to the Company on a cost-recovery basis. The Company also provided some office and investor relations services to Turquoise Hill in the Company's Hong Kong office and recovered the costs for those services on a cost-recovery basis. The Company's provision of office and investor relations services to Turquoise Hill ceased on June 30, 2012.
- Rio Tinto – Rio Tinto is the Company's ultimate parent company and at December 31, 2013 Rio Tinto controlled Turquoise Hill. The Company recovers administration and other costs incurred on behalf of Rio Tinto on a cost-recovery basis. Rio Tinto recovers from the Company the costs of salaries and benefits of employees assigned to work for the Company.
- Global Mining Management ("GMM") – GMM is a private company owned equally by seven companies, two of which include the Company and Turquoise Hill. GMM provides administration, accounting and other office services to the Company on a cost-recovery basis. The provision of these services ceased on October 31, 2013.
- Turquoise Hill Resources Singapore Pte. Ltd. ("Turquoise Hill Singapore") – Turquoise Hill Singapore (formerly I2MS.NET Pte. Ltd.) is a private company 100% owned by Turquoise Hill. Turquoise Hill Singapore provides information technology and other related services to the Company on a cost-recovery basis.
- Ivanhoe Energy Inc. ("Ivanhoe Energy") – Ivanhoe Energy is a publicly listed company and in 2012 had two directors in common with the Company. The Company provided some office and investor relations services to Ivanhoe Energy in the Company's Hong Kong office and recovered the costs for those services on a cost-recovery basis. The Company's provision of office and investor relations services to Ivanhoe Energy ceased on June 30, 2012.

26.1 Related party expenses

The Company's related party expenses consist of the following amounts:

	Year ended December 31, 2013	2012
Corporate administration	**$ 781**	$ 1,309
Salaries and benefits	**1,505**	919
Related party expenses	**$ 2,286**	$ 2,228

(Expressed in thousands of U.S. Dollars and shares in thousands, unless otherwise indicated)

26. RELATED PARTY TRANSACTIONS (CONTINUED)

The Company's related party expenses relate to the following related parties:

	Year ended December 31, 2013	2012
GMM	**$ 40**	$ 1,012
Turquoise Hill	**205**	7
Rio Tinto	**1,353**	68
Turquoise Hill Singapore	**688**	1,141
Related party expenses	**$ 2,286**	$ 2,228

26.2 Related party expense recoveries

The Company's expenses recovered from related parties consist of the following amounts:

	Year ended December 31, 2013	2012
Corporate administration	**$ 17**	$ 589

The Company's related party expense recoveries relate to the following related parties:

	Year ended December 31, 2013	2012
Turquoise Hill	**$ -**	$ 479
Ivanhoe Energy	**-**	77
Rio Tinto	**17**	33
Related party expense recoveries	**$ 17**	$ 589

26.3 Related party assets

The assets of the Company include the following amounts due from related parties:

	As at December 31, 2013	2012
Amounts due from GMM	**$ 74**	$ 420
Amounts due from Turquoise Hill	**-**	317
Amounts due from Turquoise Hill Singapore	**-**	2
Total assets due from related parties	**$ 74**	$ 739

26.4 Related party liabilities

The liabilities of the Company include the following amounts due to related parties:

	As at December 31, 2013	2012
Amounts payable to Rio Tinto	**$ 1,375**	$ 35
Accounts payable to Turquoise Hill	**34**	-
Total liabilities due to related parties	**$ 1,409**	$ 35

(Expressed in thousands of U.S. Dollars and shares in thousands, unless otherwise indicated)

26. RELATED PARTY TRANSACTIONS (CONTINUED)

26.5 Key management personnel compensation

The remuneration of the Company's directors and other members of key management, who have the authority and responsibility for planning, directing and controlling the activities of the Company, consists of the following amounts:

	Year ended December 31, 2013	Year ended December 31, 2012
Salaries, fees and other benefits	**$ 2,635**	$ 3,788
Share-based compensation	**170**	2,132
Total remuneration	**$ 2,805**	$ 5,920

27. SUPPLEMENTAL CASH FLOW INFORMATION

27.1 Non-cash financing and investing activities

The Company's non-cash investing and financing transactions are as follows:

	Year ended December 31, 2013	Year ended December 31, 2012
Convertible debenture interest settlement in shares	**$ 8,000**	$ 4,000
Transfer of share option reserve upon exercise of stock options	**-**	1,368

27.2 Net change in non-cash working capital items

The net change in the Company's non-cash working capital items is as follows:

	Year ended December, 31 2013	Year ended December, 31 2012
Decrease/(increase) in inventories	**$ (4,759)**	$ 45,339
Decrease in trade and other receivables	**2,513**	12,942
Decrease/(increase) in prepaid expenses and deposits	**22,552**	(11,061)
Increase/(decrease) in trade and other payables	**19,858**	(33,336)
Decrease in deferred revenue	**(7,184)**	(9,472)
Net change in non-cash working capital items	**$ 32,980**	$ 4,412

(Expressed in thousands of U.S. Dollars and shares in thousands, unless otherwise indicated)

28. COMMITMENTS FOR EXPENDITURE

As at December 31, 2013, the Company's commitments for expenditure that have not been disclosed elsewhere in the consolidated financial statements are as follows:

	As at December 31, 2013			
	Within 1 year	2-3 years	Over 3 years	Total
Capital expenditure commitments	$ 16,158	$ 11,273	$ -	$ 27,431
Operating expenditure commitments (i)	24,170	1,010	154	25,334
Commitments	**$ 40,328**	**$ 12,283**	**$ 154**	**$ 52,765**

(i) Operating expenditure commitments include $18,481 of fees related to the Company's toll wash plant agreement with Ejin Jinda. This amount reflects the minimum expenditure due under this agreement.

29. CONTINGENCIES

29.1 Governmental and regulatory investigations

The Company is subject to investigations by Mongolia's Independent Authority against Corruption (the "IAAC") and the Mongolian State Investigation Office (the "SIA") regarding allegations against the Company and some of its former employees. The IAAC investigation concerns possible breaches of Mongolia's anti-corruption laws, while the SIA investigation concerns possible breaches of Mongolia's money laundering and taxation laws.

While the IAAC investigation into allegations of possible breaches of Mongolian anti-corruption laws has been suspended, the Company has not received formal notice that the IAAC investigation is completed. The IAAC has not formally accused any current or former Company employees of breach of Mongolia's anti-corruption laws.

A report issued by the experts appointed by the SIA on June 30, 2013 and again in January 2014 has recommended that the accusations of money laundering as alleged against the Company's three former employees be withdrawn. However, to date, the Company has not received notice or legal document confirming such withdrawal as recommended by the experts appointed by the SIA.

A third investigation ordered by the SIA and conducted by the National Forensic Center ("NFC") into alleged violations of Mongolian taxation law was concluded at the end of January 2014. The Company has received notice that the report with conclusions of the investigations by the NFC have been provided to the Prosecutor General of Mongolia. The Prosecutor General may undertake criminal actions against the three former employees for alleged violations of taxation laws and the Company may be held liable as "civil defendant" as a result of these alleged criminal actions. These actions could result in the investigation case being imminently transferred to a Court of Justice under the relevant Mongolian law. The likelihood or consequences of such an outcome or any civil action taken against the Company are uncertain and unclear at this time but could include financial or other penalties, which could be material, and which could have a material adverse effect on the Company.

The Company disputes and will vigorously defend itself against any civil or criminal actions. At this point, the three former employees remain designated as "accused" in connection with the allegations of tax evasion, and continue to be subject to a travel ban. The Company remains designated as a "civil defendant" in connection with the tax evasion allegations, and may potentially be held financially liable for the alleged criminal misconduct of its former employees under Mongolian Law.

29. CONTINGENCIES (CONTINUED)

The SIA also continues to enforce administrative restrictions, which were initially imposed by the IAAC investigation, on certain of the Company's Mongolian assets, including local bank accounts, in connection with its continuing investigation of these allegations. While the orders restrict the use of in-country funds pending the outcome of the investigation, they are not expected to have a material impact on the Company's activities in the short term, although they could create potential difficulties for the Company in the medium to long term. The Company will continue to take all appropriate steps to protect its ability to conduct its business activities in the ordinary course.

In the opinion of management of the Company, at December 31, 2013 a provision for this matter is not required.

29.2 Internal investigations

Through its Audit Committee (comprised solely of independent directors), the Company has conducted an internal investigation into possible breaches of law, internal corporate policies and codes of conduct arising from the allegations which have been raised. The Audit Committee has had the assistance of independent legal counsel in connection with its investigation.

The Chair of the Audit Committee has also participated in a tripartite committee, comprised of the Audit Committee Chairs of the Company and Turquoise Hill and a representative of Rio Tinto, which focused on the investigation of a number of those allegations, including possible violations of anti-corruption laws. Independent legal counsel and forensic accountants assisted this committee with its investigation. The tripartite committee substantially completed the investigative phase of its activities during the third quarter of 2013. The Company continues to cooperate with the IAAC, SIA and with Canadian and United States government and regulatory authorities that are monitoring the Mongolian investigations. It is possible that these authorities may subsequently conduct their own review or investigation or seek further information from the Company. Pending further reviews or questions from any of such government or regulatory authorities, the tripartite committee has been stood down and investigations have been paused.

The investigations referred to above could result in one or more Mongolian, Canadian, United States or other governmental or regulatory agencies taking civil or criminal action against the Company, its affiliates or its current or former employees. The likelihood or consequences of such an outcome are unclear at this time but could include financial or other penalties, which could be material, and which could have a material adverse effect on the Company.

The Company, through its Board of Directors and new management, has taken a number of steps to address issues noted during the investigations and to focus ongoing compliance by employees with all applicable laws, internal corporate policies and codes of conduct, and with the Company's disclosure controls and procedures and internal controls over financial reporting.

In the opinion of management of the Company, at December 31, 2013 a provision for this matter is not required.

29. CONTINGENCIES (CONTINUED)

29.3 Mongolian IAAC investigation

In the first quarter of 2013, the IAAC informed the Company that orders placing restrictions on certain of its Mongolian assets had been imposed in connection with its continuing investigation. The orders were imposed on the Company in connection with the IAAC's investigation of the Company. The SIA also continues to enforce the orders on the Company.

The orders placing restrictions on certain of the Company's Mongolian assets could ultimately result in an event of default of the Company's CIC convertible debenture. Following a review by the Company and its advisers, it is the Company's view that this does not result in an event of default as defined under the CIC convertible debenture terms. However, if an event of default of the Company's CIC convertible debenture occurs that remains uncured for ten business days, the principal amount owing and all accrued and unpaid interest will become immediately due and payable upon notice to the Company by CIC.

The orders relate to certain items of operating equipment and infrastructure and the Company's Mongolian bank accounts. The orders related to the operating equipment and infrastructure restricts the sale of these items; however, the orders do not restrict the use of these items in the Company's mining activities. The orders related to the Company's Mongolian bank accounts restrict the use of in-country funds. While the orders restrict the use of in-country funds pending outcome of the investigation, they are not expected to have any material impact on the Company's activities.

29.4 Class action lawsuit

On or about January 6, 2014, Siskinds LLP, a Canadian law firm, filed a proposed securities class action (the "Ontario Action") against the Company, certain of its former senior officers and current directors, and its former auditors, Deloitte LLP, in the Ontario Superior Court of Justice in relation to the Company's restatement of financial statements as previously disclosed in the Company's public filings.

The plaintiff seeks leave to bring a claim under applicable Canadian securities legislation and seeks certification of a class action with respect to a class of persons who purchased shares of the Company between March 30, 2011 and November 7, 2013, alleging that the financial reporting of the Company during that period contained misrepresentations giving rise to liability at common law and under applicable Canadian securities legislation. The Ontario Action also seeks general damages against all defendants in the sum of Cdn$30 million, without particulars as to how such amount was determined, or such other amount that the Court deems appropriate. Assuming that leave is granted, the action is certified as a class proceeding, and there is a finding of liability, the actual quantum of damages will depend upon the evidence which is adduced in the court proceedings.

Named in the Ontario Action as individual defendants are the Company's former Chief Executive Officer, former Chief Financial Officers and the members of its Audit Committee.

The Company disputes and will vigorously defend itself against these claims through independent Canadian litigation counsel retained by the Company and the other defendants for this purpose. Due to the inherent uncertainties of litigation, it is not possible to predict the final outcome of the Ontario Action or determine the amount of any potential losses, if any. However, in the opinion of management of the Company, at December 31, 2013 a provision for this matter is not required.

(Expressed in thousands of U.S. Dollars and shares in thousands, unless otherwise indicated)

ADDITIONAL STOCK EXCHANGE INFORMATION

Additional information required by the Hong Kong Stock Exchange and not shown elsewhere in this report is as follows:

A1. LOSS FOR THE YEAR

Loss for the year has been arrived at after charging the following items:

	Year ended December 31,			
	2013		2012	
Auditor's remuneration	**$**	**406**	$	430
Loss on disposal of property, plant and equipment	**$**	**895**	$	720
Depreciation and depletion				
Depreciation included in administration expenses	**$**	**193**	$	212
Depreciation included in evaluation and exploration expenses		**5**		40
Depreciation and depletion included in cost of sales		**45,055**		46,243
Total depreciation and depletion	**$**	**45,253**	$	46,495
Staff costs				
Directors' emoluments - executive directors (Note A2)	**$**	**1,103**	$	1,183
Directors' emoluments - non-executive directors (Note A2)		**827**		1,366
Other staff costs		**1,985**		9,055
Staff costs included in administration expenses		**3,915**		11,604
Staff costs included in evaluation and exploration expenses		**46**		437
Total staff costs	**$**	**3,961**	$	12,041

A2. DIRECTOR AND EMPLOYEE EMOLUMENTS

Directors' emoluments

The Company's directors' emoluments consist of the following amounts:

	Year ended December 31,			
	2013		2012	
Directors' fees	**$**	**721**	$	719
Other emoluments for executive and non-executive directors				
Salaries and other benefits		**1,162**		799
Share-based compensation		**47**		1,031
Directors' emoluments	**$**	**1,930**	$	2,549

(Expressed in thousands of U.S. Dollars and shares in thousands, unless otherwise indicated)

A2. DIRECTOR AND EMPLOYEE EMOLUMENTS (CONTINUED)

Year ended December 31, 2013

Name of director	Directors' fees	Salaries and other benefits	Share-based compensation	Total
Executive directors				
K. Ross Tromans	$ -	$ 1,103	$ -	$ 1,103
Non-executive directors				
Kay Priestly	$ 126	$ -	$ -	$ 126
Sean Hinton	83	59	47	189
Kelly Sanders	64	-	-	64
Brett Salt (i)	26	-	-	26
Lindsay Dove	81	-	-	81
Pierre Lebel	126	-	-	126
André Deepwell	114	-	-	114
W. Gordon Lancaster	89	-	-	89
Bold Baatar	12	-	-	12
	$ 721	$ 59	$ 47	$ 827
Directors' emoluments	$ 721	$ 1,162	$ 47	$ 1,930

(i) Resigned from the Board of Directors during the year ended December 31, 2013.

(Expressed in thousands of U.S. Dollars and shares in thousands, unless otherwise indicated)

A2. DIRECTOR AND EMPLOYEE EMOLUMENTS (CONTINUED)

Year ended December 31, 2012

Name of director	Directors' fees	Salaries and other benefits	Share-based compensation	Total
Executive directors				
K. Ross Tromans	$ -	$ 124	$ -	$ 124
Alexander Molyneux (i)	-	473	586	1,059
	$ -	$ 597	$ 586	$ 1,183
Non-executive directors				
Kay Priestly	$ 39	$ -	$ -	$ 39
Sean Hinton	29	202	37	268
Kelly Sanders	17	-	-	17
Brett Salt	13	-	-	13
Lindsay Dove	23	-	37	60
Peter Meredith (i)	18	-	70	88
John Macken (i)	-	-	41	41
Pierre Lebel	153	-	62	215
André Deepwell	128	-	62	190
R. Edward Flood (i)	69	-	41	110
R. Stuart (Tookie) Angus (i)	22	-	-	22
Robert Hanson (i)	100	-	41	141
W. Gordon Lancaster	108	-	54	162
	$ 719	$ 202	$ 445	$ 1,366
Directors' emoluments	$ 719	$ 799	$ 1,031	$ 2,549

(i) Resigned from the Board of Directors during the year ended December 31, 2012.

Salaries and other benefits paid to Ross Tromans during the year ended December 31, 2013 includes a bonus of $193 paid in accordance with the Company's annual incentive plans.

Five highest paid individuals

The five highest paid individuals included one director of the Company for the years ended December 31, 2013 and 2012. The emoluments of the five highest paid individuals are as follows:

	Year ended December 31, 2013	2012
Salaries and other benefits	**$ 2,138**	$ 2,571
Share-based compensation	**-**	1,743
Compensation for loss of office	**344**	424
Total emoluments	**$ 2,482**	$ 4,738

(Expressed in thousands of U.S. Dollars and shares in thousands, unless otherwise indicated)

A2. DIRECTOR AND EMPLOYEE EMOLUMENTS (CONTINUED)

The emoluments for the five highest paid individuals were within the following bands:

	Year ended December 31, 2013	2012
HK$ 1,500,001 to HK$ 2,000,000	**1**	-
HK$ 2,000,001 to HK$ 2,500,000	**1**	-
HK$ 2,500,001 to HK$ 3,000,000	**1**	-
HK$ 4,000,001 to HK$ 4,500,000	**1**	
HK$ 4,500,001 to HK$ 5,000,000	**-**	1
HK$ 6,500,001 to HK$ 7,000,000	**-**	1
HK$ 7,000,001 to HK$ 7,500,000	**-**	1
HK$ 8,000,001 to HK$ 8,500,000	**-**	1
HK$ 8,500,001 to HK$ 9,000,000	**1**	-
HK$ 9,500,001 to HK$ 10,000,000	**-**	1
	5	5

A3. FIVE YEAR SUMMARY

The following table contains a five year summary of the Company’s results, assets and liabilities:

	Year ended December 31, 2013	2012	2011	2010	2009
Revenue	**$ 58,636**	$ 78,061	$ 130,756	$ 60,412	$ 36,038
Gross profit/(loss)	**(53,991)**	(49,346)	38,578	7,761	6,613
Net comprehensive income/(loss) attributable to equity holders of the Company	**$ (236,950)**	$ (114,061)	$ 37,350	$ (89,855)	$ (110,805)
Basic income/(loss) per share from continuing and discontinued operations	**$ (1.30)**	$ (0.54)	$ 0.27	$ (0.67)	$ (0.83)
Diluted loss per share from continuing and discontinued operations	**$ (1.30)**	$ (0.60)	$ (0.24)	$ (0.67)	$ (0.83)

	As at December 31, 2013	2012	2011	2010	2009
Total assets	**$ 506,206**	$ 732,452	$ 918,680	$ 968,682	$ 560,684
Less: total liabilities	**(131,149)**	(128,469)	(213,113)	(291,212)	(563,476)
Total net assets/(liabilities)	**$ 375,057**	$ 603,983	$ 705,567	$ 677,470	$ (2,792)

(Expressed in thousands of U.S. Dollars and shares in thousands, unless otherwise indicated)

A4. CASH

The Company's cash is denominated in the following currencies:

	As at December 31, 2013	As at December 31, 2012
Denominated in U.S. Dollars	**$ 15,912**	$ 18,107
Denominated in Chinese Renminbi	**4,888**	-
Denominated in Mongolian Tugriks	**632**	911
Denominated in Canadian Dollars	**200**	260
Denominated in Hong Kong Dollars	**182**	396
Others	**23**	-
Total cash	**$ 21,837**	$ 19,674