

# TITANIUM

INVESTING IN THE FUTURE

## SECOND QUARTER REPORT

*For the six months ended June 30, 2004*

### Highlights

- Tiomin signs 21-year Mining License for its Kwale titanium project
- Completion of engineering review of 2000 Feasibility Study by Ausenco Limited of Australia – confirms fiscal strengths of Kwale
- Resolution of Ramisi land resettlement issue by Government of Kenya
- Signed letters of intent and sales agreements in place for approximately 60% of projected revenues for the first three to five years of production
- Closing of \$4.2 million private placement financing

On July 6, 2004, Tiomin Resources signed the 21-year Mining License for its Kwale titanium project at a Government ceremony held in Nairobi, Kenya attended by the Minister of Environment and Natural Resources, Kalonzo Musyoka and Tiomin's President and CEO, Jean-Charles Potvin. The 21-year mining lease, which is renewable for a further 21 years, has been issued for the mining of ilmenite, rutile, and zircon at Kwale which is projected to produce an average of 330,000 tonnes of ilmenite, 77,000 tonnes of rutile and 37,000 tonnes of zircon per year for the first six years of operation.



The Mining Lease approval coincides with the announcement of the Government's intention to use some 11,000 acres of land previously leased to the now defunct Ramisi sugarcane plantation for the re-settlement of affected individuals to make way for the Kwale project. These developments present a definite turning point for the advancement of Kwale and set the stage for the finalization of the fiscal agreement which is expected to be announced in the coming weeks. Tiomin's Kwale project has the potential to become a significant producer rutile and zircon, creating over 350 permanent jobs directly and twice as many during the

construction phase, and places Kenya in good company with other African mineral sands producers.

Tiomin has also completed a comprehensive environmental impact study according to World Bank standards and recently announced the completion of an engineering review of the 2000 Feasibility Study by Ausenco Limited of Australia, confirming the \$120 million capital costs of the project, excluding working capital and contingencies, in addition to the product quality which should ensure the project is developed. The finalization of the report with respect to the financial parameters is dependent on the terms of the fiscal agreement which is currently under negotiation with the Government of Kenya. In addition,

Tiomin has formally filed an Export Processing Zone (EPZ) application with the Government of Kenya which, if approved, would allow for significant fiscal incentives towards the processing plants.

During the quarter, Tiomin also closed a private placement financing of 12 million units at \$0.35 per unit for total proceeds of \$4.2 million. Each unit consists of one common share and one-half common share purchase warrant exercisable at \$0.50 for eighteen months. The proceeds from the issue will be used for general working capital purposes and to advance the Kwale project as it prepares to enter the construction phase with production commencing in 2006.

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## Management's Discussion and Analysis of Financial Condition and Results of Operations

This management's discussion and analysis of the financial results of the Company's operations for the second quarter and six-months ended June 30, 2004 should be read in conjunction with the consolidated financial statements and related notes that follow. This discussion covers the most recently completed quarter and the subsequent period to July 28, 2004.

### Overview

Tiomin Resources Inc. is involved in the exploration and development of industrial mineral projects. Since mid-1998, the Company has focused on the development of its Kwale titanium bearing mineral sands project in Kenya. The Company is currently not in production on any of its properties and has only minimal revenue derived from interest earned on its cash balances.

In December 2002, the Government of Kenya ("GOK") approved Tiomin's application for a Special Mining Lease on its Kwale project, subject to the statutory 90-day public notice period. On September 29, 2003, the Commissioner of Mines and Geology for Kenya issued the formal approval of Tiomin's application for a mining lease and established the basic terms of the Special Mining Lease. On July 6, 2004, at a signing ceremony hosted in Nairobi, the Company received the 21 year renewable Special Mining Lease for the Kwale project.

In December 2003, Tiomin submitted the draft comprehensive fiscal/investment agreement setting out the commercial and fiscal parameters for the proposed mining operations. At the time of writing, the Company is in the late stages of negotiations with the GOK concerning the fiscal agreement and Tiomin expects to have this agreement executed during the third quarter of 2004. In mid-2003, the Company engaged Ausenco Limited to perform an engineering review of the positive feasibility study previously completed in 2000 to reflect the changes that have taken place since that time. The engineering review was completed in May 2004 and confirmed the robust economics of the Kwale project. Capital costs are expected to be in the range of US\$120 million. The finalization of the fiscal agreement and the terms of using the Kenyan electrical grid will have a significant impact on the economics of the project.

Substantial progress has been made in marketing the expected production from Kwale, with letters of intent being executed for a significant portion of the future production of zircon and rutile.

The Company will continue to focus its efforts on developing the Kwale project. Important issues that need to be resolved include; receipt of all the necessary government permits, finalize negotiations with the Government on the use of Kenyan electrical power and obtaining the necessary financing to enable construction to commence.

## Selected Financial Information

The following table provides selected consolidated financial information that should be read in conjunction with the consolidated financial statements of the Company. All dollar amounts are stated in Canadian dollars.

	3 months ended June 30, 2004 (unaudited)	3 months ended June 30, 2003 (unaudited)	6 months ended June 30, 2004 (unaudited)	6 months ended June 30, 2003 (unaudited)	Year ended Dec. 31, 2003 (audited)
Operating expenses	\$ 383,296	\$ 309,814	\$ 728,721	\$ 512,228	\$ 2,362,923
Net loss	383,209	305,613	728,104	504,708	2,309,887
Net loss per share	0.00	0.00	0.01	0.01	0.03
Cumulative deferred exploration and development costs	16,540,862	14,197,240	16,540,862	14,197,240	15,574,836
Working capital	2,839,629	(315,603)	2,839,629	(315,603)	178,653
Long term debt	404,935	439,661	404,935	439,661	420,931

## Results of Operations

During the quarter ended June 30, 2004, the Company's operations consisted of the continued development of its Kenyan mineral sands properties, with most of it being invested in the Kwale project. During the quarter, \$432,000 was invested in deferred exploration (capitalized asset) as work on the engineering review of the project continued. This was similar to the previous quarter's investment of \$530,000 and a significant increase over the \$125,000 invested during the corresponding period in 2003, as the resumption of test work and the engineering review of the Kwale project commenced in mid-2003.

Operating expenses of \$383,000 and loss per share of \$0.00 for the second quarter was in line with the first quarter of 2004 (\$345,000) and were comparable with the same period in 2003 (\$306,000), with the exception that in 2003 the Company had a non-cash foreign exchange gain of \$94,000 during the second quarter on the translation of a US\$

denominated loan. The loan was paid off in October 2003 and the Company has minimal long-term debt now. Salaries and compensation expenses increased modestly in 2004 in comparison to 2003 as additional staff resources were employed beginning in mid-2003 and are fully reflected in 2004 results. Travel costs have increased in 2004 as more personnel are traveling to Kenya and Australia with the engineering update underway. Administrative expenses for 2004 are expected to remain at 2003 levels (with the exception of foreign exchange gains) until late 2004 when the Company may incur additional expenses should it decide to proceed with the construction of the Kwale project and additional key personnel are hired.

The Company as at June 30, 2004 has approximately \$3 million in working capital which it believes is sufficient to fund the Company's operations and complete all required engineering, permitting and other related development work prior to project financing drawdown and construction commencing in early 2005.

## Summary of Quarterly Results

	3 months ended June 30, 2004 (unaudited)	3 months ended June 30, 2003 (unaudited)	6 months ended June 30, 2004 (unaudited)	6 months ended June 30, 2003 (unaudited)
Total operating expenses	\$ 383,296	\$ 309,814	\$ 728,721	\$ 512,228
Salaries & compensation	186,599	174,620	376,617	333,097
Net loss	383,209	305,613	728,104	504,708
Net loss per share	0.00	0.00	0.01	0.01
Investment in deferred exploration & development	432,021	124,919	958,920	280,309

## Liquidity and Capital Resources

As the Company has not begun production on any of its properties, the Company does not have any cash flow from operations. The Company receives cash for use in operations from issuing common shares, sales of selected assets and investment income. The Company has been successful in accessing the equity markets in the past and while there is no guarantee that this will continue to be available, management has no reason to expect that this will diminish in the immediate term.

The Company raised an additional \$4.2 million during the second quarter of 2004 via a private placement of common shares with attached half-warrants to fund its ongoing working capital requirements and finalize the engineering and design of the Kwale project, currently underway.

Should the Company decide to put the Kwale project into production, the Company will have to raise the necessary funds to enable construction to commence. The engineering review recently completed has outlined an expected capital requirement of approximately US\$120-US\$130 million. The Company at this time believes the capital cost will be financed through a combination of debt and equity likely to occur in late 2004. There is no guarantee at this time that the Company will be able to raise the funds necessary to start construction.

There are no significant long-term debt obligations as at June 30, 2004. The long-term debt of \$405,000 is comprised mostly of a CIDA grant (as described in note 6 to the financial statements) that is not repayable until the Company earns in excess of \$5 million from the Kwale project, which is not expected before 2007.

The ability of the Company to continue operations beyond 2005 is dependent upon obtaining the necessary financing to develop the Kwale project or the realization of proceeds from the sale of one or more of its properties and/or assets.

## Transactions with Related Parties

From time to time during the Company's history, directors of the Company have advanced funds to the Company on a short term basis to assist the Company during brief periods of illiquidity. During the first and second quarter of 2004, two directors, Jean-Charles Potvin and Roland Bertin, advanced a total of \$750,000 to the Company on a demand loan basis at an interest rate of 10%. The Company repaid these loans, with associated interest of \$19,450, upon the closing of the equity new issue on June 16, 2004.

## Critical Accounting Estimates

Critical accounting estimates used in the preparation of the consolidated financial statements include the Company's estimate of recoverable value of its mineral properties and related deferred expenditures as well as the value of stock-based compensation. Both of these estimates involve considerable judgment and are, or could be, affected by significant factors that are out of the Company's control.

The factors affecting stock-based compensation include estimates of when stock options and compensation warrants might be exercised and the stock price volatility. The timing for exercise of options is out of the Company's control and

will depend upon a variety of factors including the market value of the Company's share and financial objectives of the stock-based instrument holders. The Company used historical data to determine volatility in accordance with the Black-Scholes model, however the future volatility is uncertain and the model has its limitations.

The Company's recoverability of the recorded value of its mineral properties and associated deferred expenses is based on market conditions for minerals, underlying mineral resources associated with the properties and future costs that may be required for ultimate realization through mining operations or by sale. The Company is in an industry that is dependent on a number of factors including environmental, legal and political risks, the existence of economically recoverable reserves, the ability of the Company and its subsidiaries to obtain necessary financing to complete the development and future profitable production or the proceeds of disposition thereof.

## Change in Accounting Policies

### *Stock Based Compensation*

In 2003 the Company adopted the recommendations for fair value accounting of employee stock option grants under section 3870 of Canadian Institute of Chartered Accountants Handbook. These recommendations require compensation costs, for stock options granted to employees, be recorded in earnings based on the fair value of the options on the grant date. Previously these costs were disclosed in the notes to the consolidated financial statements. This policy change was adopted on a prospective basis and an expense was recorded in 2003. The comparative results for 2003 in this report reflect the adoption of this policy (please also see note 9 of the consolidated financial statements).

## Other Information

### *General*

The Company also discloses information related to its activities in the Annual Information Form ("AIF"). The AIF and other pertinent information on the Company is available on SEDAR at [www.sedar.com](http://www.sedar.com).

### *Outstanding share data*

As at June 30, 2004, The Company had issued and outstanding 115,547,625 common shares, and 127,007,954 common shares issued on a fully diluted basis (December 2003 – 102,834,574 and 108,961,574, respectively). Included in the fully diluted number are 7,345,329 warrants and 4,115,000 stock options which are described in detail in notes 8 and 9 to the financial statements.

The increase in common shares and warrants issued and outstanding during the second quarter of 2004 is the result of the Company issuing 11,991,051 common shares through a private placement that closed on June 16, 2004. The private placement was done at a price of \$0.35 per share for gross proceeds of approximately \$4.2 million and each common share had an attached one-half warrant that was exercisable at \$0.50 until December 16, 2005. Also during the quarter, 722,000 stock options were exercised prior to their expiry in July for proceeds of \$222,000 to the Company.

## CONSOLIDATED BALANCE SHEETS

as at June 30 (amounts in \$)

	<b>June 30, 2004</b>	December 31, 2003
	<i>(Unaudited)</i>	<i>(Audited)</i>
<b>ASSETS</b>		
Current		
Cash and cash equivalents	<b>2,897,281</b>	469,184
Receivables	<b>19,535</b>	54,871
Prepaid expenses	<b>137,018</b>	80,440
	<b>3,053,834</b>	604,495
Fixed assets, net of accumulated depreciation <i>(note 3)</i>		
Mineral properties <i>(note 4)</i>	<b>1,151,365</b>	1,072,034
Deferred exploration and development <i>(note 4)</i>	<b>16,540,862</b>	15,574,836
	<b>18,414,286</b>	17,366,939
	<b>21,468,120</b>	17,971,434
<b>LIABILITIES</b>		
Current		
Accounts payable and accrued liabilities	<b>214,205</b>	425,842
Long-term		
Long-term liabilities <i>(note 6)</i>	<b>404,935</b>	420,931
<b>SHAREHOLDERS' EQUITY</b>		
Capital stock <i>(note 8)</i>	<b>91,896,300</b>	87,476,782
Contributed Surplus <i>(note 8 (b) and 9)</i>	<b>553,621</b>	465,516
Deficit	<b>(71,600,941)</b>	(70,817,637)
	<b>20,848,980</b>	17,124,661
	<b>21,468,120</b>	17,971,434

See accompanying notes

## CONSOLIDATED STATEMENTS OF OPERATIONS AND DEFICIT

<i>for the quarters and six months ended June 30 (amounts in \$)</i>	<b>2004</b>	2003	<b>2004</b>	2003
	<i>(Unaudited)</i>	<i>(Unaudited)</i>	<i>(Unaudited)</i>	<i>(Unaudited)</i>
<b>EXPENSES</b>				
Salaries & other compensation <i>(note 9)</i>	<b>186,599</b>	174,620	<b>376,617</b>	333,097
Office costs	<b>54,826</b>	52,911	<b>88,618</b>	104,725
Foreign exchange loss (gain)	<b>738</b>	(93,750)	<b>3,510</b>	(219,077)
Depreciation	<b>3,013</b>	1,882	<b>6,707</b>	3,930
Interest	–	11,999	–	29,709
Travel	<b>31,516</b>	6,482	<b>68,878</b>	14,672
Stock exchange fees	–	–	<b>11,040</b>	9,520
Shareholders' information	<b>48,596</b>	36,529	<b>54,203</b>	56,750
Promotion	<b>21,780</b>	66,875	<b>63,986</b>	108,915
Professional fees	<b>23,591</b>	47,012	<b>40,320</b>	64,733
Capital tax and other taxes	–	4,685	<b>445</b>	4,685
General exploration	<b>12,637</b>	569	<b>14,397</b>	569
<b>Total expenses</b>	<b>383,296</b>	309,814	<b>728,721</b>	512,228
Less: interest income and other income	<b>(87)</b>	(4,201)	<b>(617)</b>	(7,520)
<b>Net loss for the period</b>	<b>383,209</b>	305,613	<b>728,104</b>	504,708
Share issue costs	<b>55,200</b>	61,343	<b>55,200</b>	527,476
Deficit, beginning of the period	<b>71,162,532</b>	68,524,020	<b>70,817,637</b>	67,858,792
<b>Deficit, end of the period</b>	<b>71,600,941</b>	68,890,976	<b>71,600,941</b>	68,890,976
Basic and diluted loss per share	<b>0.00</b>	0.00	<b>0.01</b>	0.01
Basic and diluted weighted average shares outstanding			<b>104,025,606</b>	86,586,808

*See accompanying notes*

## CONSOLIDATED STATEMENTS OF CASH FLOWS

<i>for the quarters and six months ended June 30 (amounts in \$)</i>	<b>2004</b>	2003	<b>2004</b>	2003
	<i>(Unaudited)</i>	<i>(Unaudited)</i>	<i>(Unaudited)</i>	<i>(Unaudited)</i>
<b>OPERATING ACTIVITIES</b>				
Net loss for the period	<b>(383,209)</b>	(305,613)	<b>(728,104)</b>	(504,708)
<i>Add (deduct) non-cash items</i>				
Depreciation charges	<b>1,761</b>	1,882	<b>6,707</b>	3,930
Compensation expense	<b>44,053</b>	53,410	<b>88,105</b>	97,570
Foreign exchange gain on long-term liabilities	–	(76,992)	–	(192,552)
Sub-lease expense	<b>(7,998)</b>	–	<b>(15,996)</b>	–
<i>Change in non-cash working capital</i>				
Decrease (increase) in accounts receivable	<b>(791)</b>	(17,105)	<b>35,336</b>	(15,521)
Decrease (increase) in prepaid expenses	<b>(12,599)</b>	9,180	<b>(56,578)</b>	5,040
Decrease in accounts payables and accrued liabilities	<b>(635,284)</b>	(186,224)	<b>(211,637)</b>	(384,498)
Decrease in accrued interest	–	(5,188)	–	(61,304)
	<b>(994,067)</b>	(526,650)	<b>(882,167)</b>	(1,052,043)
<b>INVESTING ACTIVITIES</b>				
Mineral properties acquired	<b>(77,918)</b>	(27,724)	<b>(79,331)</b>	(62,979)
Deferred exploration and development expenditures	<b>(432,021)</b>	(124,919)	<b>(958,920)</b>	(280,309)
Patent – TSR technology expenditures	–	(2,280)	–	(2,999)
Net fixed assets acquisitions	<b>(1,418)</b>	(2,695)	<b>(15,803)</b>	(3,357)
	<b>(511,357)</b>	(157,618)	<b>(1,054,054)</b>	(349,644)
<b>FINANCING ACTIVITIES</b>				
Common shares issued for cash	<b>4,384,418</b>	249,750	<b>4,419,518</b>	4,449,750
Loan facility repayment ( <i>note 7</i> )	–	–	–	(2,100,248)
Share issue costs	<b>(55,200)</b>	(1,277)	<b>(55,200)</b>	(407,344)
	<b>4,329,218</b>	248,473	<b>4,364,318</b>	1,942,158
Increase (decrease) in cash and short-term investments	<b>2,823,794</b>	(435,795)	<b>2,428,097</b>	540,471
Cash and short-term investments, beginning of the period	<b>73,487</b>	1,242,707	<b>469,184</b>	266,441
Cash and short-term investments, end of the period	<b>2,897,281</b>	806,912	<b>2,897,281</b>	806,912

*See accompanying notes*

# NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

June 30, 2004

## 1. NATURE OF OPERATIONS

Tiomín Resources Inc. (the "Corporation" or "Tiomín") and its subsidiaries have mineral exploration properties located in Canada and Kenya. The exploration and development of mineral properties involves significant financial risk. The recoverability of the amounts shown for the mineral properties and the related deferred expenditures is dependent on a number of factors including environmental, legal and political risks, the existence of economically recoverable reserves, confirmation of the Corporation's and its subsidiaries' interest in the underlying mineral claims, the ability of the Corporation and its subsidiaries to obtain necessary financing to complete the development and future profitable production or the proceeds of disposition thereof.

The consolidated financial statements for the period ended June 30, 2004 have been prepared on the basis that the Corporation is a going concern, which contemplates the realization of its assets and the settlement of its liabilities in the normal course of operations. These consolidated financial statements do not include any adjustments related to the carrying values and classification of assets and liabilities should the Corporation be unable to continue as a going concern.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting policies of the Corporation are in accordance with Canadian generally accepted accounting principles and their basis of application is consistent with prior periods. Outlined below are those policies considered particularly significant.

### Mineral Properties and Deferred Exploration and Development:

Acquisition and exploration expenses relating to mineral properties with proven resource potential are deferred until the properties are brought into production at which time they are depleted on a unit-of-production basis. If it is determined that capitalized acquisition, exploration and development costs are not recoverable over the economic life of the property, or the project is abandoned, the project is written-down to its net realizable value. All other exploration expenses are expensed in the year that they occur. The Corporation does not accrue the future cost of maintaining the properties in good standing.

### Fixed Assets and Depreciation:

Fixed assets are stated at acquisition cost. Depreciation is provided on the straight-line basis over the following periods:

Computers	3 years
Vehicles	3 years
Furniture	5 years
Mining equipment	3 years

### Foreign Currency Translation:

Monetary assets and liabilities denominated in foreign currencies have been translated into Canadian dollars at the period end exchange rates. Non-monetary assets have been translated at the rates prevailing at the dates of acquisition. Revenue and expense items other than depreciation are translated at the average rates of exchange for the period. Any exchange gain or loss that arises on translation is included in the determination of net loss for the period.

### Cash and Cash Equivalents:

Cash and cash equivalents comprised cash on hand and short-term investments that mature within 90 days from date of acquisition.

### Income Taxes:

Current income taxes are recognized for the estimated income and mining taxes payable for the current year. Future income tax assets and liabilities are recognized for temporary differences between the tax and accounting bases of assets and liabilities as well as for the benefit of losses available to be carried forward to future years for tax purposes that are more likely than not to be realized. Future income taxes are measured using the tax rates and laws that will be in effect when the differences are expected to reverse or the losses to be realized.

### Stock-based Compensation:

The Corporation has a stock-based compensation plan that is described in note 9. Effective January 1, 2003, the Corporation adopted the recommendations issued by The Canadian Institute of Chartered Accountants dealing with stock-based compensation on a prospective basis, as permitted by the standard. This standard requires a fair value based method of accounting to be applied to all stock-based awards. Effective January 1, 2003, the Corporation accounts for employee stock-based compensation by measuring all awards granted on or after January 1, 2003 under the fair value based method of accounting, using the Black – Scholes pricing model. Consideration paid on the exercise of stock options and warrants is credited to share capital.

### 3. FIXED ASSETS

The following table provides a breakdown of the Corporation's fixed assets:

	June 2004 \$	December 2003 \$
Computers	86,071	83,879
Furniture & fixtures	24,206	24,206
Equipment	55,897	55,897
Vehicles	12,902	12,902
Land	686,573	672,962
Cost	865,649	849,846
Accumulated Depreciation	(143,590)	(129,777)
Net Fixed Assets	722,059	720,069

### 4. MINERAL PROPERTIES AND DEFERRED EXPLORATION AND DEVELOPMENT

The interests in mineral properties and respective deferred exploration and development costs are as follows:

	Mineral Properties		Deferred Exploration and Development	
	June 30, 2004 (cost)	December 31, 2003 (cost)	June 30, 2004 (cost)	December 31, 2003 (cost)
Kenya	1,151,365	1,072,034	16,540,862	15,574,836
Total	\$1,151,365	\$1,072,034	\$16,540,862	\$15,574,836

In June 1996, the Corporation acquired from Pangea Goldfields Inc. (Pangea) a 100% interest, subject to a 20% net profit interest royalty (NPI), in the exploration rights of three Special Licences along the Kenyan coast. Under the terms of the agreement, the Corporation must spend a minimum of US\$200,000 on exploration on the properties during the first year and complete a feasibility study within five years. If the properties are placed into production, Pangea will receive 20% of the net profits from any mining operation following payback of Tiomin's capital investment in the mine and processing operation. In 2000, the Corporation completed a positive feasibility study and made a decision to proceed to production, thus satisfying the terms of the agreement with Pangea. The three Special Licences require the Corporation to spend a minimum of 14,000,000 Kenyan shillings (approximately US\$235,000) per annum on exploration. The licences were renewed in April 2004 and currently expire in 2006.

In April 1997, the Corporation acquired a fourth licence in Kenya known as Kwale. The licence was for an initial term of two years and required the Corporation to spend a minimum of 500,000 Kenyan shillings (approximately US\$8,500) per annum on exploration. This licence was added to the initial agreement with Pangea whereby Pangea retains a 20% NPI in the Kenyan properties. This licence currently expires in 2005.

### 5. TIOMIN SYNTHETIC RUTILE ("TSR") PROCESS

The proprietary TSR Process developed by Tiomin is used to upgrade the mineral ilmenite into a high-grade titanium dioxide feedstock known as synthetic rutile. The TSR Process employs the latest chemical processing technology to produce a synthetic rutile product containing up to 97% titanium dioxide, the highest titanium dioxide content in the market place. In 1997, the Corporation submitted several patent applications to various international Intellectual Property Offices around the world for its TSR Process and has been granted patents in several countries. In December 2003, Tiomin has written-off the \$1,236,796 previously capitalized value of the TSR Process as it could not determine its realizable value in the foreseeable future. Tiomin will maintain its patents in good standing because the Corporation believes that the TSR Process is still a valuable asset.

## 6. LONG-TERM LIABILITIES

### a) Development Loan

On April 22, 1999, the Canadian International Development Agency and the Corporation entered into a loan agreement under the Industrial Overseas Development Programme. The proceeds of the loan were to be used to offset the cost of certain environmental work incorporated in the Kwale feasibility study. Under the terms of the agreement, Tiomin had to spend a minimum of \$1,480,000 on the feasibility study prior to June 30, 2000 in order to be entitled to the maximum loan amount of \$391,000. The loan is non-interest bearing and is repayable once the Corporation's cumulative product sales from the project exceed \$5,000,000. In the event that the Kwale project is not put into production or fails to achieve the sales threshold, the loan will be treated as a grant and the Corporation will not be required to repay the loan. The Corporation met the minimum level of expenses of \$1,480,000 and received \$386,000 of the maximum loan amount.

### b) Operating lease

On July 2, 2002, the Corporation agreed to sublease its current office space to a third party at a lower price than the original lease agreement. The totality of the space has been subleased to the third party and started on September 1, 2003. This resulted in the aggregate rent differential of \$77,325 being recognized as a charge to earnings in 2002. As at June 30, 2004, long-term liabilities include \$18,673 which represents net rent payments which will be made in 2005 to 2006.

## 7. LOAN FACILITY

On January 27<sup>th</sup>, 2000, the Corporation completed a US\$2,000,000 financing with Resource Capital Fund L.P. The financing was structured as a US\$2,000,000 loan facility (the "Loan Facility"). Under the terms of the Loan Facility, the Corporation issued 5,158,000 warrants with an exercise price of \$0.57, expiring December 31, 2002. The warrants were not exercised prior to December 31 2002 and therefore expired. The Loan Facility carried an interest rate of LIBOR plus 2%. The Loan Facility is secured by a charge on all the assets and undertaking of the Corporation, until a mining licence is obtained for Kwale and pledges of all issued and outstanding shares of the Corporation's subsidiaries.

Under the terms of the Loan Facility, the Corporation can elect to pay interest by the delivery of common shares of the Corporation. The number of common shares issued in lieu of interest is equal to the amount of interest payable divided by the number that is 90% of the weighted average trading price of the Corporation's shares for a period of 20 days immediately preceding the scheduled interest payment date.

The Loan Facility was scheduled to mature on December 31, 2002. On January 17, 2003, the Corporation amended the terms of the Loan Facility and repaid US\$1,360,000 of the loan. The remaining outstanding principal of US\$640,000 was extended to September 1, 2003 bearing an interest rate of LIBOR plus 4%. Under the terms of the Loan Facility amendment, the Corporation issued 3,698,044 common share warrants with an exercise price of \$0.27, expiring December 31, 2003 (also see note 8). The warrants were all exercised prior to expiry.

On August 20, 2003, the maturity date of the Loan Facility was extended to October 31 2003. On October 28 2003, the balance of US\$640,000 was repaid to Resource Capital Fund L.P.

## 8. CAPITAL STOCK

a) The Corporation is authorized to issue an unlimited number of common shares.

	Shares #	Amount \$
Common shares, January 1, 2003	68,809,030	79,935,891
Issued upon exercise of options (note 9)	250,000	75,000
Private placement	20,000,000	4,200,000
Issued upon exercise of warrants	13,775,544	3,265,891
Total common shares, December 31, 2003	102,834,574	87,476,782
Issued upon exercise of options (note 9)	722,000	222,650
Private Placement	11,991,051	4,196,868
Total common shares, June 30, 2004	115,547,625	91,896,300

On June 16<sup>th</sup>, 2004 the Corporation, pursuant to a private placement, issued 11,991,051 units at \$0.35 for gross proceeds of \$4,196,868. Each unit consists of one common share and one half a share purchase warrant. Each whole share purchase warrant entitles the holder to purchase one common share at \$0.50 for a period of 18 months from the issue date.

On January 10, 2003, the Corporation completed a private placement of 20,000,000 common shares for gross proceeds of \$4,200,000. As part of the use of proceeds, \$2,200,000 (US\$1,360,000) was used to repay a significant portion of the outstanding loan facility with Resource Capital Fund L.P. on January 17, 2003 (see note 7).

On April 28, 1997, the Corporation adopted a Shareholder Rights Plan. Each shareholder of record from the close of business on April 28, 1997 will be issued one right for each common share held. In the event that a bidder acquires 20% or more of the outstanding voting shares of the Corporation other than by a permitted bid or with the approval of the Board of Directors of the Corporation, the rights would become exercisable to purchase common shares of the Corporation at a 50% discount to the then current market price. The Shareholder Rights Plan was re-approved by the shareholders on June 20, 2002 and extended for a further five year period.

#### b) WARRANTS

The following is a list of the warrants outstanding as at June 30<sup>th</sup>, 2004. All warrants are convertible into one common share of the Corporation.

Type	Total Outstanding	Exercise Price	Expiry Date
Series G	1,349,800	\$0.27	Jan 10, 2005
Series I	5,995,529	\$0.50	Dec 15, 2005

Following the adoption of the recommendations issued by The Canadian Institute of Chartered Accountants dealing with stock-based compensation, the compensation warrants (Series G) were valued at \$240,264 and have been included as part of issue cost in 2003. The valuation was done using the Black-Scholes pricing model with the following assumptions: risk free interest rate of 4.0%, expected dividend yield of nil, expected volatility of 107% and expected warrant life term of two years.

#### 9. STOCK OPTIONS

Under the Corporation's Stock Option Plan (the "Plan") established in 1996 and approved by shareholders in 1996, 2000 and 2004, the Corporation may grant to directors, officers, employees and consultants options to purchase common shares of the Corporation. The aggregate number of shares reserved for issuance under the Plan shall not exceed 13,000,000 common shares. The total number of shares which may be reserved for issuance to any one individual under the Plan shall not exceed 5% of the total number of issued and outstanding shares (on a non-diluted basis) and shares reserved for issuance under the Plan. Options granted since 1995 have a five-year term and are priced at the TSE closing price of the Corporation's common shares on the day immediately prior to the date of granting. Vesting provisions vary according to the terms of the individual granting.

A summary of the outstanding stock options is presented below.

	June 2004		December 2003	
	Options	Weighted Average Exercise Price \$	Options	Weighted Average Exercise Price \$
Outstanding, Beginning of year	4,902,000	0.39	4,420,000	0.48
Granted	–	–	1,950,000	0.28
Exercised	(722,000)	0.31	(250,000)	0.30
Cancelled / Expired	(65,000)	0.30	(1,218,000)	0.59
Outstanding, end of period	4,115,000	0.40	4,902,000	0.39
Options exercisable at the end of period	2,985,000		2,802,000	

The following table summarizes information about the stock options outstanding as at June 30, 2004.

Range of Exercise Prices	OPTIONS OUTSTANDING			OPTIONS EXERCISABLE	
	Number Outstanding As at June 30, 2004	Weighted Average Remaining Life (years)	Weighted Average Exercise Price	Number Exercisable As at June 30, 2004	Weighted Average Exercise Price
\$0.23-0.28	1,685,000	3.16	\$0.25	1,555,000	\$0.25
\$0.30-0.38	1,670,000	3.19	0.32	670,000	0.34
\$0.65	50,000	1.85	0.65	50,000	0.65
\$0.94	710,000	1.20	0.94	710,000	0.94
	4,115,000	2.71	0.40	2,985,000	0.44

In 2003, the fair value of the options granted during the year was estimated at the date of grant using the Black-Scholes pricing model with the following assumptions: risk free interest rate of 4.0%, expected dividend yield of nil, expected volatility of 107% and expected option life term of four years. Under this method of calculation the fair value of all options granted during the year ended December 31, 2003, was \$225,252, which reflects the options' vesting periods in accordance with the Plan. As a result, \$225,252 has been recognized as compensation expense in December 2003. An additional \$88,105 was also included as compensation expense during the first two quarters of 2004 for the portion of the 2003 options granted that will vest in 2004. No options were granted during the six month period ended June 30, 2004.

## 10. INCOME TAXES

The components of the Corporation's future income tax assets (liabilities) are as follows:

	2003	2002
	\$	\$
Non-capital losses carried forward	4,033,000	3,287,000
Resource related deductions	3,752,000	2,757,000
Share issuance costs	257,000	214,000
Capital assets	287,000	231,000
Future income tax asset	8,329,000	6,489,000
Valuation allowance	(8,329,000)	(6,489,000)
Net future income tax asset	–	–

As at December 31, 2003, the Corporation had non-capital losses to be carried forward and applied against taxable income of future years. The non-capital losses have expiry dates as follows:

2004	1,760,000
2006	2,013,000
2007	2,233,000
2008	2,332,000
2009	1,282,000
2010	1,460,000

## 11. LEASE COMMITMENT

The Corporation is committed to minimum annual rents under a lease, which expires on January 31, 2006. As at December 31, 2003, future minimum annual rental payments, net of proceeds from subleases, are as follows:

2004	31,990
2005	31,990
2006	2,666

## 12. RELATED PARTY TRANSACTIONS

During the first and second quarter of 2004, the Corporation borrowed a total of \$750,000 from two of its directors. The loans were repaid on June 16<sup>th</sup> and included \$19,450 of interest.

## 13. COMPARATIVE STATEMENTS

Some comparative figures (June 30, 2003) have been reclassified or updated to conform with the December 31, 2003 and the 2004 presentation of the financial statements.

