U.S. SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 40-F

o **REGISTRATION STATEMENT PURSUANT TO SECTION 12 OF THE SECURITIES EXCHANGE ACT OF 1934.**

þ **ANNUAL REPORT PURSUANT TO SECTION 13(a) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the fiscal year ended: December 31, 2011 **Commission File Number: 001-35297**

FORTUNA SILVER MINES INC.

(Exact name of Registrant as specified in its charter)
British Columbia, Canada
(Province or other jurisdiction of incorporation or organization)

1040	**None**
(Primary Standard Industrial Classification Code Number)	(I.R.S. Employer Identification Number)

200 Burrard Street, Suite 650
Vancouver, British Columbia, Canada V6C 3L6
(604) 484-4085

(Address and telephone number of Registrant's principal executive offices)

National Corporate Research, Ltd.
10 East 40th Street, 10th Floor
New York, New York 10016
(212) 947-7200

(Name, address (including zip code) and telephone number (including area code)
of agent for service in the United States)

Securities registered or to be registered pursuant to Section 12(b) of the Act.

Title of each class	**Name of each exchange on which registered**
Common Shares	New York Stock Exchange

Securities registered or to be registered pursuant to Section 12(g) of the Act.

None
(Title of Class)

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act.

None
(Title of Class)

For Annual Reports indicate by check mark the information filed with this Form:

þ Annual information form þ Audited annual financial statements

Indicate the number of outstanding shares of each of the issuer 's classes of capital or common stock as of the close of the period covered by the annual report:

There were 124,945,921 Common Shares, of no par value, outstanding as of December 31, 2011.

Indicate by check mark whether the Registrant (1) has filed all reports to be filed by Section 13 or 15(d) of the Exchange Act during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports) and (2) has been subject to filing requirements for the past 90 days.

Yes þ No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the Registrant was required to submit and post such files).

Yes o No o

PRINCIPAL DOCUMENTS

The following documents have been filed as part of this Annual Report on Form 40-F as Exhibits hereto:

A. Annual Information Form

The Annual Information Form of Fortuna Silver Mines Inc. (the "Company" or "Registrant") for the year ended December 31, 2011, is included as Exhibit 99.1 of this Annual Report on Form 40-F.

B. Audited Annual Financial Statements

The Company's audited consolidated financial statements for the years ended December 31, 2011 and December 31, 2010, including the auditor's report with respect thereto, are included as Exhibit 99.2 of this Annual Report on Form 40-F.

C. Management's Discussion and Analysis

The Company's Management's Discussion and Analysis for the year ended December 31, 2011 is included as Exhibit 99.3 of this Annual Report on Form 40-F.

CERTIFICATIONS AND DISCLOSURE REGARDING CONTROLS AND PROCEDURES

Certifications. See Exhibits 99.14, 99.15, 99.16 and 99.17 to this Annual Report on Form 40-F.

Disclosure Controls and Procedures. The required disclosure is included in the section entitled "Disclosure Controls and Procedures" contained in the Registrant's Management's Discussion and Analysis for the fiscal year ended December 31, 2011, filed as part of this Annual Report on Form 40-F.

Management's Annual Report on Internal Control Over Financial Reporting. This Annual Report on Form 40-F does not include a report of management's assessment regarding internal control over financial reporting or an attestation report of the Company's registered public accounting firm due to a transition period established by rules of the Securities and Exchange Commission (the "SEC") for newly public companies.

Attestation Report of the Registered Public Accounting Firm. This Annual Report on Form 40-F does not include an attestation report of the Company's registered public accounting firm due to a transition period established by rules of the SEC for newly public companies.

Changes in Internal Control Over Financial Reporting. During the fiscal year ended December 31, 2011, there were no changes in the Registrant's internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, the Registrant's internal control over financial reporting.

NOTICES PURSUANT TO REGULATION BTR

None.

IDENTIFICATION OF THE AUDIT COMMITTEE

The Registrant has a separately-designated standing audit committee established in accordance with Section 3(a)(58)(A) of the Exchange Act. The members of the audit committee are: Messrs. Robert Gilmore, Tomas Guerrero and Thomas Kelly.

AUDIT COMMITTEE FINANCIAL EXPERT

The board of directors of the Registrant has determined that Robert Gilmore, a member of the Registrant's audit committee, qualifies as an audit committee financial expert for purposes of paragraph (8) of General Instruction B to Form 40-F. The board of directors has further determined that each of Messrs. Robert Gilmore, Tomas Guerrero and Thomas Kelly is independent, as that term is defined in the Corporate Governance Listing Standards of the New York Stock Exchange. The Commission has indicated that the designation of Robert Gilmore as an audit committee financial expert does not make him an "expert" for any purpose, impose any duties, obligations or liabilities on him that are greater than those imposed on members of the audit committee and the board of directors who do not carry this designation or affect the duties, obligations or liabilities of any other member of the audit committee or the board of directors.

ADDITIONAL DISCLOSURE

Code of Ethics.

The Registrant has adopted a "code of ethics" (as that term is defined in Form 40-F), entitled the "Code of Business Conduct and Ethics and Whistle Blower Policy", that applies to all of its directors, officers, employees, and consultants including its principal executive officer, principal financial officer, principal accounting officer or controller, and persons performing similar functions.

The Code of Business Conduct and Ethics and Whistle Blower Policy is available for viewing on the Registrant's website at www.fortunasilver.com.

Principal Accountant Fees and Services.

The required disclosure is included under the heading "Audit Committee" of the Registrant's Annual Information Form for the fiscal year ended December 31, 2011, filed as part of this Annual Report on Form 40-F in Exhibit 99.1.

Pre-Approval Policies and Procedures.

The required disclosure is included under the heading "Audit Committee" of the Registrant's Annual Information Form for the fiscal year ended December 31, 2011, filed as part of this Annual Report on Form 40-F in Exhibit 99.1.

Off-Balance Sheet Arrangements.

The required disclosure is included in Notes 17(d) and 19(a), (b), (c) and (d) of the Registrant's audited consolidated financial statements for the fiscal years ended December 31, 2011 and 2010, filed as part of this Annual Report on Form 40-F in Exhibit 99.2.

Tabular Disclosure of Contractual Obligations.

The required disclosure is included under the heading "Contractual Obligations" of the Registrant's Management's Discussion and Analysis for the fiscal year ended December 31, 2011, filed as part of this Annual Report on Form 40-F in Exhibit 99.3.

UNDERTAKING

Registrant undertakes to make available, in person or by telephone, representatives to respond to inquiries made by the Commission staff, and to furnish promptly, when requested to do so by the Commission staff, information relating to: the securities registered pursuant to Form 40-F; the securities in relation to which the obligation to file an annual report on Form 40-F arises; or transactions in said securities.

CONSENT TO SERVICE OF PROCESS

Form F-X signed by the Registrant and its agent for service of process has been filed with the Commission together with Registrant's Registration Statement on Form 40-F (001-35297) in connection with its securities registered on such form.

Any changes to the name or address of the agent for service of process of the Registrant shall be communicated promptly to the Commission by an amendment to the Form F-X referencing the file number of the Registrant.

SIGNATURES

Pursuant to the requirements of the Exchange Act, the Registrant certifies that it meets all of the requirements for filing on Form 40-F and has duly caused this Annual Report to be signed on its behalf by the undersigned, thereunto duly authorized.

Date: March 30, 2012

FORTUNA SILVER MINES INC.

By: *"Jorge Ganoza Durant"*

Name: Jorge Ganoza Durant
Title: President, Chief Executive Officer & Director

EXHIBIT INDEX

Exhibit	Description
99.1	The Annual Information Form of Fortuna Silver Mines Inc. for the year ended December 31, 2011
99.2	Fortuna Silver Mines Inc. audited consolidated financial statements for the years ended December 31, 2011 and December 31, 2010, including the auditor's report with respect thereto
99.3	Fortuna Silver Mines Inc. Management's Discussion and Analysis for the year ended December 31, 2011
99.4	Consent of Deloitte & Touche LLP
99.5	Consent of Richard L. Nielsen of Chlumsky, Armbrust & Meyer LLC
99.6	Consent of Robert L. Sandefur of Chlumsky, Armbrust & Meyer LLC
99.7	Consent of Craig S. Bow of Chlumsky, Armbrust & Meyer LLC
99.8	Consent of Gregory Chlumsky of Chlumsky, Armbrust & Meyer LLC
99.9	Consent of Steve L. Milne of Chlumsky, Armbrust & Meyer LLC
99.10	Consent of Chlumsky, Armbrust & Meyer LLC
99.11	Consent of Eric Chapman
99.12	Consent of Edgard Vilela
99.13	Consent of Thomas Vehrs
99.14	Certification of Chief Executive Officer pursuant to Section 302 of the *Sarbanes-Oxley Act of 2002*
99.15	Certification of Chief Financial Officer pursuant to Section 302 of the *Sarbanes-Oxley Act of 2002*
99.16	Certification of Chief Executive Officer pursuant to Section 906 of the *Sarbanes-Oxley Act of 2002*
99.17	Certification of Chief Financial Officer pursuant to Section 906 of the *Sarbanes-Oxley Act of 2002*



FORTUNA
SILVER MINES INC.

ANNUAL INFORMATION FORM

For the Fiscal Year Ended December 31, 2011

DATED: March 27, 2012

CORPORATE OFFICE:
Suite 650, 200 Burrard Street
Vancouver, BC V6C 3L6, Canada
Tel: 604.484.4085
Fax: 604.484.4029

MANAGEMENT HEAD OFFICE:
Piso 5, Av. Jorge Chávez #154
Miraflores, Lima, Peru
Tel: 511.616.6060, ext. 2

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PRELIMINARY NOTES

Cautionary Statement – Forward Looking Statements

Certain statements and information in this Annual Information Form are not based on historical facts and constitute forward-looking statements or forward looking information within the meaning of Canadian securities laws ("forward looking statements"), including but not limited to, the Company's plans at its San Jose Project, Mexico and Caylloma Mine, Peru, estimated production, capital and operating cash flow estimates and other matters.

Forward-looking statements:

- are statements that address or discuss activities, events or developments that we expect or anticipate may occur in the future;
- can be identified by the use of words such as "believe", "expect", "anticipate", "intend", "plan", "likely", "predicts", "estimates", "forecasts", and similar words or phrases or the negative of such words or phrases;
- reflect our current beliefs, intentions or expectations based on certain assumptions and estimates, including those identified below, which could prove to be significantly incorrect:
    - that all required third party contractual, regulatory and governmental approvals will be obtained for the development, construction and production of the Company's properties;
    - there being no significant disruptions affecting operations, whether due to labour disruptions, supply disruptions, power disruptions, civil unrest and protest, damage to equipment or otherwise;
    - permitting, development, expansion and power supply proceeding on a basis consistent with the Company's current expectations;
    - currency exchange rates being approximately consistent with current levels;
    - certain price assumptions for silver, lead, zinc, gold and copper;
    - prices for and availability of natural gas, fuel oil, electricity, parts and equipment and other key supplies remaining consistent with current levels;
    - production forecasts meeting expectations;
    - the accuracy of the Company's current mineral resource and reserve estimates;
    - labour and materials costs increasing on a basis consistent with the Company's current expectations;
    - that any additional required financing will be available on reasonable terms;
    - assumptions made and judgments used in engineering and geological interpretation;
- while considered reasonable by management, are inherently subject to known and unknown risks and uncertainties and other factors that could cause actual results or events to differ from historical or anticipated results or events. These risk factors and others are discussed in this Annual Information Form and in Management's Discussion and Analysis for the financial year ended December 31, 2011, which may be found on SEDAR at www.sedar.com. Certain of these material risks are listed below:
    - uncertainties and risks relating to the start-up of the San Jose Project, including timely receipt of all required permits;
    - fluctuations in precious and base metal prices;
    - inherent hazards and risks associated with mining operations;
    - inherent uncertainties associated with mineral exploration and development activities;
    - uncertainties inherent in the estimation of mineral reserves and/or resources and precious metal recoveries;
    - uncertainties related to actual capital costs, operating costs and expenditures, production schedules and economic returns from the Company's mining projects;
    - uncertainties related to the current global financial conditions;
    - uncertainties related to the availability of future financing necessary to undertake mining, processing, development and exploration activities on the Company's properties;
    - the Company's substantial reliance on its Caylloma and San Jose Mines for revenues;
    - risks related to the integration of businesses and assets acquired by Fortuna;
    - uncertainties related to the competitiveness of the mining industry;
    - risks associated with Fortuna being subject to government regulation, including changes in law, regulation and taxation, and risks associated with Fortuna's need for governmental licenses and permits;
    - risks associated with Fortuna being subject to extensive environmental laws and regulations, including a change in regulation;
    - risks that the Company's title to its properties could be challenged;
    - political and country risk;
    - risk of water shortages and risks associated with competition for water;
    - the Company's need to attract and retain qualified personnel;
    - increases in off-site transportation and concentrate processing costs;
    - risks related to the storage of tailings and the need for reclamation activities on the Company's properties, including the nature of reclamation required and uncertainty of costs estimates related thereto;
    - risks associated with potential conflicts of interest;
    - risks associated with potential labour disputes;
    - risks associated with potential blockades of mining operations.

As a result, no assurance can be given that any of the events or results anticipated by such forward looking statements will occur or, if they do occur, what benefit they will have on our operations or financial condition. Readers are cautioned not to place undue reliance on these forward-looking statements. We disclaim any intention or obligation to update or revise any forward looking

statements, whether as a result of new information, future events or otherwise, except as required by law.

Cautionary Note to U.S. Investors Concerning Estimates of Measured, Indicated and Inferred Resources

This document and the documents incorporated by reference herein have been prepared in accordance with the requirements of securities laws in effect in Canada, which differ from the requirements of United States securities laws. Without limiting the foregoing, this document, and the documents incorporated by reference herein, use the terms "measured," "indicated" and "inferred" resources. United States investors are advised that, while such terms are recognized and required by Canadian securities laws, the SEC does not recognize them. Under current United States standards, mineralization may not be classified as a "reserve" unless the determination has been made that the mineralization could be economically and legally produced or extracted at the time the reserve determination is made. United States investors are cautioned not to assume that all or any part of measured or indicated resources will ever be converted into reserves. Further, "inferred resources" have a great amount of uncertainty as to their existence and as to whether they can be mined legally or economically. It cannot be assumed that all or any part of the "inferred resources" will ever be upgraded to a higher category. Therefore, United States investors are also cautioned not to assume that all or any part of the inferred resources exist, or that they can be mined legally or economically. Disclosure of "contained ounces" is permitted disclosure under Canadian regulations; however, the SEC only permits issuers to report "resources" as in place tonnage and grade without reference to unit measures. Accordingly, information concerning descriptions of mineralization and resources contained in this document, or in the documents incorporated by reference, may not be comparable to information made public by United States companies subject to the reporting and disclosure requirements of the SEC. National Instrument 43-101 Standards of Disclosure for Mineral Projects ("NI 43-101") is a rule developed by the Canadian Securities Administrators that establishes standards for all public disclosure an issuer makes of scientific and technical information concerning mineral projects. Unless otherwise indicated, all reserve and resource estimates contained in or incorporated by reference in this document have been prepared in accordance with NI 43-101. These standards differ significantly from the requirements of the SEC, and reserve and resource information contained herein and incorporated by reference herein may not be comparable to similar information disclosed by U.S. companies. NI 43-101 permits historical estimates made prior to the adoption of NI 43-101 that do not comply with NI 43-101 to be disclosed using the historical terminology if the disclosure: (a) identifies the source and date of the historical estimate; (b) comments on the relevance and reliability of the historical estimate; (c) states whether the historical estimate uses categories other than those prescribed by NI 43-101; and (d) includes any more recent estimates or data available.

Documents Incorporated by Reference

The information provided in this Annual Information Form ("AIF") is supplemented by disclosure contained in the documents listed below which are incorporated by reference into this AIF. These documents must be read together with the AIF in order to provide full, true and plain disclosure of all material facts relating to Fortuna Silver Mines Inc. (referred to herein as the "Company" or "Fortuna"). The documents listed below are not contained within or attached to this document. The documents may be accessed on SEDAR at www.sedar.com under the Company's profile, Fortuna Silver Mines Inc.:

Document	Effective Date / Period Ended	Date Filed on SEDAR website	Document Category on the SEDAR website
Management Information Circular	April 11, 2011	May 2, 2011	Management Proxy / Information Circular - English
Technical Report, Caylloma Project, Peru	August 11, 2009	August 27, 2009	Technical Report(s)
Technical Report, San Jose Project, Mexico	June 9, 2010	June 10, 2010	Technical Report(s)

Date of Information

This AIF is dated March 27, 2012. Except as otherwise indicated, the information contained herein is as at December 31, 2011, being the date of the Company's most recently completed financial year end.

CORPORATE STRUCTURE

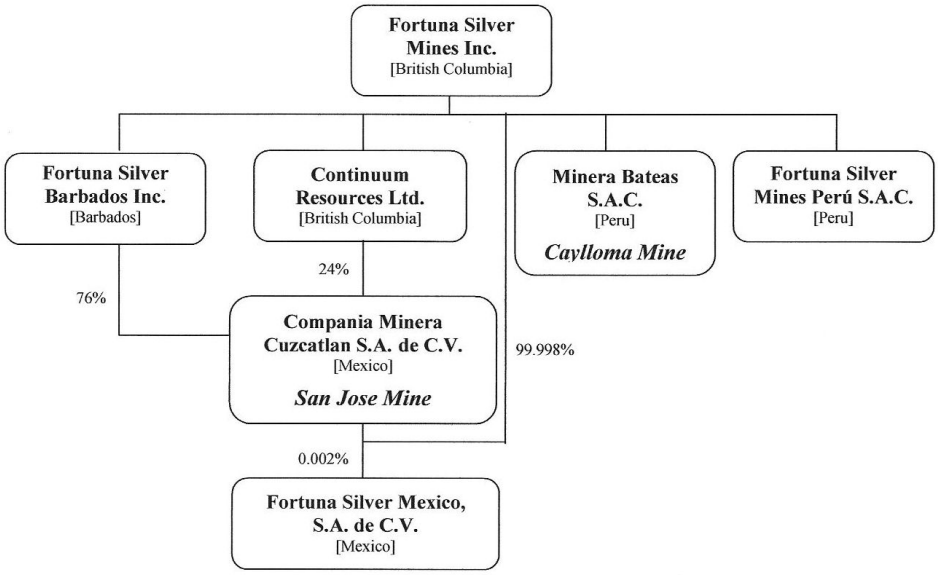
Name, Address and Incorporation

The Company was incorporated on September 4, 1990 under the laws of the Province of British Columbia under the name Jopec Resources Ltd. On February 3, 1999, the Company changed its name to Fortuna Ventures Inc. and on June 28, 2005 to Fortuna Silver Mines Inc.

The management head office of the Company is located at Piso 5, Av. Jorge Chávez #154, Miraflores, Lima, Peru. The corporate and registered office of the Company is located at 200 Burrard Street, Suite 650, Vancouver, BC V6C 3L6.

Intercorporate Relationships

The Company carries on a significant portion of its business through a number of 100%-owned subsidiaries, held either directly or indirectly, as follows:



GENERAL DEVELOPMENT OF THE BUSINESS

Three-Year History and Recent Developments

Caylloma Mine, Peru

The Company purchased a 100% interest in the Caylloma Mine and related mining concessions in 2005 and returned the Mine to production in October of 2006 following a significant upgrading and modernization of the ore processing plant. In 2009, the Company successfully commissioned an expansion project that allowed an increase in plant capacity to 1,200 tonnes per day ("tpd") and the addition of a copper circuit which started commercial production in December 2009. For the year 2010, the mine and processing plant operated at an average rate of 1,231 tpd with production sourced primarily from the Animas Vein. Silver production totaled 1,906,423 oz and cash cost per Ag oz, net of by-product credits was negative $5.99. For the year 2011, the processing plant operated at an average rate of 1,264 tpd and silver production increased 5% year on year to 2,008,488. In January 2011, production of copper-silver concentrate was discontinued at Caylloma due to a material deterioration in treatment and refining smelter charges with respect to 2010. Cash cost per Ag oz net of by-product credits in 2011 increased to negative $0.59. This increment was driven by a cash cost increase and lower base metal credits in the second half of 2011, with special emphasis in the fourth quarter. Cash cost per oz throughout 2011 went from negative $5.82 in Q1 2011 to $6.67 in Q4 of the same year. The sharp increment throughout the 2011 is explained by a decrease in by-product credits of $9.40/oz and a 29% unit cash cost per tonne increase. The decrease in by-product credits was primarily due to lower base metal prices (Pb 24%, Zn 21%) and lower lead production (13%). The unit cost increments reflect cost increases in qualified labor and industry related services that have been mounting in the Peruvian underground mining industry since late 2010. For 2012, the Company anticipates cost pressures to continue; several productivity and cost control initiatives are included in the 2012 operational and capital budgets.

The Company released an updated National Instrument 43-101 – *Standards of Disclosure for Mineral Projects* ("NI 43-101") resource estimation for its Caylloma Mine, Peru on July 16, 2009. On February 2, 2010, the Company announced the discovery of high-grade silver mineralization in the upper portion of the Animas Vein at the Caylloma Mine in southern Peru. The Animas vein, traditionally a polymetallic vein, is the source of 85% per cent of ore tones mined at the Company's Caylloma Mine. The main focus of development in Animas in 2010 was extending the mineralization along strike towards the north east on levels 10 and 12, and habilitating the resource blocks between level 10 and level 12 with infrastructure as the mine plan extends below level 10 in 2011. In the upper part of Animas development and preparation was focused on incorporating level 6 into the production plan.

On December 15, 2010 the Company announced the discovery and confirmation of two new high-grade silver ore shoots in the Bateas Vein, located in the central portion of the Caylloma Mine District. Historically the Bateas Vein has been a significant producer of high-grade silver ore with the past production coming from those portions of the vein located to the southwest of the newly discovered ore shoots. From the newly discovered ore shoots along strike to the northeast, the Bateas Vein is open and essentially unexplored over a horizontal distance of approximately 1,150 meters, where the vein is projected to intersect with the San Cristobal Vein.

These new high-grade silver ore shoots entered into production in late June 2011. Exploration drifting towards the northeast area of the Bateas Vein was stopped by the end of September in order to improve ventilation and infrastructure for auxiliary services in levels 10 and 12. By mid December a ventilation shaft from surface to level 12 was completed, and two more shafts between levels 10 and 12 should be completed by the end of March 2012 to resume exploration drifting.

San Jose Silver-Gold Mine, Mexico

The San Jose property is a high-grade silver-gold bearing epithermal vein system located in the state of Oaxaca in southern Mexico. In late 2006, the Company acquired a 76% interest in the San Jose property, with Continuum Resources Ltd. owning a 24% interest. In March 2009, the Company completed an acquisition of all of the issued and outstanding securities of Continuum in

consideration of the issuance by the Company of 6,786,706 common shares. As a result, the Company owns a 100% interest in the San Jose Property.

The Company released an updated NI 43-101 resource estimation for its San Jose Project in October 2009, and in December 2009, the Mexican Environmental Agency approved the Company's application for a change of land use from agricultural to industrial for the property. This was the final permit required to commence construction of a mine at San Jose and complemented the environmental impact study which was approved by the Mexican Environmental Agency in late October 2009. In April 2010, the Company announced the results of a pre-feasibility study completed for the project. Highlights of the pre-feasibility study included:

- 3.5 million tonnes of probable mineral reserves with 23.2 million ounces of contained silver and 181,000 ounces of contained gold (average head grades of 205 g/t of silver and 1.6 g/t of gold).
- 2.7 million tonnes of inferred mineral resources (above the break even cut-off grade).
- Base case after-tax net present value of US$36.4 million at an 8% discount rate.
- Base case metal prices of OUS$15/oz silver and US$897/oz gold.
- Base case after-tax internal rate of return of 18%.
- Estimated pre-production capital expenditures of US$55.7 million.
- Average cash cost per silver equivalent (Ag Eq) ounce over life of reserves of US$6.90.
- 9 year production plan based on existing reserves.
- Incremental throughput rate starting at 750 tpd, scaling to 1,000 tpd in 2014 and to 1,500 tpd in 2016.

Construction activities began at the San Jose Project in early 2010 and commercial production of the San Jose Mine commenced on September 1, 2011. The initial production rate is 1,000 tpd, greater than the rate contemplated in the pre-feasibility study. During 2012, the Company intends to initiate expansion of capacity to 1,500 tpd, bringing the estimated production for the year to 1.7 million ounces silver and 15,000 ounces gold.

Updated Mineral Reserves and Mineral Resources – Caylloma and San Jose Mines

On March 27, 2012, the Company released updated Mineral Reserve and Mineral Resource estimates for the Caylloma Mine and the San Jose Mine.

Highlights of Reserve and Resource Update

- Proven and Probable Reserves of the silver-rich veins at Caylloma increased by 51.7% to 781,000 tonnes. Contained silver increased by 40.3% to 9.4 million ounces.
- Combined Proven and Probable Reserves for the silver-rich and polymetallic veins at Caylloma increased by 12.2% to 4.6 million tonnes after replacement of 674,010 tonnes consumed through production. Contained silver decreased by 1.9% to 20.2 million ounces.
- Measured and Indicated Resources at Caylloma increased by 19.7% to 2.3 million tonnes and contained silver increased by 20.3% to 8.9 million ounces.
- Inferred Resources at Caylloma decreased by 2.3% to 3.3 million tonnes while contained silver decreased by 7.8% to 11.8 million ounces.
- Proven and Probable Reserves at San Jose decreased marginally by 4.5% to 3.6 million tonnes, all related to extraction of 171,000 tonnes following mine start-up in August 2011. Contained silver decreased by 3.7% to 23.6 million ounces. There were no material changes in the Indicated or Inferred Resources at San Jose.
- Combined Proven and Probable Reserves for the Caylloma and San Jose mines increased by 4.2% to 8.2 million tonnes containing 43.8 million ounces of silver and 233,200 ounces of gold.
- Combined Measured and Indicated Resources for the Caylloma and San Jose mines increased by 16.4% to 2.6 million tonnes containing 11.9 million ounces of silver and 47,400 ounces of gold.
- Combined Inferred Resources for the Caylloma and San Jose mines decreased marginally by 1.2% to 6.3 million tonnes containing 33.8 million ounces of silver and 216,000 ounces of gold.

Mineral Reserves - Proven and Probable

							Contained Metal	
Property	Classification	Tonnes (000)	Ag (g/t)	Au (g/t)	Pb (%)	Zn (%)	Ag (Moz)	Au (koz)
Caylloma, Peru								
Silver Veins	Proven	26	687	0.28	0.32	0.32	0.6	0.2
	Probable	755	365	0.42	0.06	0.06	8.9	10.3
	Proven + Probable	781	376	0.42	0.07	0.07	9.4	10.5
Polymetallic Veins	Proven	1,318	87	0.32	1.59	2.39	3.7	13.5
	Probable	2,543	86	0.31	1.58	2.27	7.1	25.5
	Proven + Probable	3,861	86	0.31	1.59	2.31	10.7	39.0
Combined-All Veins	Proven	1,344	98	0.32	1.57	2.35	4.2	13.7
	Probable	3,297	150	0.34	1.23	1.76	15.9	35.8

	Proven + Probable	4,642	135	0.33	1.33	1.93	20.2	49.5
San Jose, Mexico	Probable	3,600	204	1.59	N/A	N/A	23.6	183.7
Total	Proven + Probable	8,241	165	0.88	N/A	N/A	43.8	233.2

Mineral Resources - Measured and Indicated

							Contained Metal	
Property	Classification	Tonnes (000)	Ag (g/t)	Au (g/t)	Pb (%)	Zn (%)	Ag (Moz)	Au (koz)
Caylloma, Peru	Measured	574	100	0.31	1.17	1.75	1.8	5.8
	Indicated	1,684	131	0.30	0.74	1.11	7.1	16.0
	Measured + Indicated	2,258	123	0.30	0.85	1.28	8.9	21.8
San Jose, Mexico	Indicated	376	243	2.12	N/A	N/A	2.9	25.6
Total	Measured + Indicated	2,634	140	0.56	N/A	N/A	11.9	47.4

Mineral Resources - Inferred

							Contained Metal	
Property	Classification	Tonnes (000)	Ag (g/t)	Au (g/t)	Pb (%)	Zn (%)	Ag (Moz)	Au (koz)
Caylloma, Peru	Inferred	3,258	112	0.36	0.99	1.50	11.8	37.9
San Jose, Mexico	Inferred	3,072	223	1.80	N/A	N/A	22.0	178.1
Total	Inferred	6,330	166	1.06	N/A	N/A	33.8	216.0

1. Mineral Reserves and Mineral Resources are as defined by CIM Definition Standards on Mineral Resources and Mineral Reserves
2. Mineral Resources are exclusive of Mineral Reserves
3. Mineral Resources that are not Mineral Reserves do not have demonstrated economic viability
4. Caylloma Mineral Resources and Mineral Reserves are estimated as of June 30, 2011 and reported as of December 31, 2011 taking into account production-related depletion for the period of July 1, 2011 through December 31, 2011
5. Caylloma Mineral Reserves are estimated using break-even cut-off grades based on estimated NSR values using assumed metal prices of US$26.59/ oz Ag, US$1,279.31/oz Au, US$2,116/t Pb and US$2,028/t Zn; historical metallurgical recovery rates of 82% for Ag, 45% for Au, 93% for Pb and 88% for Zn; and historic operating costs adjusted for inflation. Caylloma Mineral Resources are reported based on estimated NSR values using the aforementioned assumed metal prices and metallurgical recovery rates and a cut-off value of US$30/t
6. Caylloma Mineral Resources include oxide material that is not amenable to processing in the existing flotation plant. Measured and Indicated Oxide Resources are estimated at 1,077,000 tonnes averaging 197 g/t Ag, 0.39 g/t Au, 1.00% Pb and 1.28% Zn. Inferred Oxide Resources are estimated at 544,000 tonnes averaging 143 g/t Ag, 0.27 g/t Au, 0.55% Pb and 0.94% Zn
7. San Jose Mineral Resources are estimated as of December 10, 2009 with Mineral Reserves estimated as of December 31, 2010 and actualized as of December 31, 2011 taking into account production-related depletion from start-up in August 2011 through December 31, 2011
8. San Jose Mineral Reserves are estimated using break-even cut-off grades based on assumed metal prices of US$15.12/oz Ag and US$ 897.51/oz Au, estimated metallurgical recovery rates of 88% for Ag and 90% for Au and projected operating costs. San Jose Mineral Resources are estimated and reported at a Ag Equivalent cut-off grade of 100 g/t, with Ag Eq in g/t = Ag (g/t) + Au (g/t)*((US$856.16/US$13.75)*(91.5/92.5))
9. Totals may not add due to rounding procedures
10. N/A = Not Applicable

Caylloma Mine

Through exploration and development activities, the Mineral Reserves consumed through production at Caylloma were replaced and Proven and Probable Reserves increased by 12.2% to 4.6 million tonnes relative to the Mineral Reserves previously reported as of June 30, 2010. Contained silver decreased marginally by 1.9%. As of December 31, 2011, the Caylloma Mine had Proven and Probable Mineral Reserves containing 20.2 million ounces silver, Measured and Indicated Mineral Resources containing 8.9 million ounces silver and Inferred Mineral Resources containing 11.8 million ounces silver. Variations from the previously reported reserves and resources (see Fortuna news release dated April 12, 2011) are the result of exploration drilling, exploration advances, mine development and increases in metal prices, partially offset by the production of 674,010 tonnes for the period of July 1, 2010 through December 31, 2011. Of particular significance is the 51.7% increase in the Proven and Probable Mineral Reserves for the silver-rich veins accompanied by a 40.3% increase in the contained silver content. This increase in high-grade silver reserves will allow the Company to continue to expand silver production.

The 2012 exploration program at Caylloma includes 24,000 meters of exploration drilling and 3,500 meters of underground exploration advances with the program being primarily focused on the exploration of silver-rich veins in the northern portion of the Caylloma District.

A NI 43-101 technical report supporting the December 31, 2011 Mineral Reserve and Mineral Resource update at Caylloma will be released to the public upon finalization.

San Jose Mine

The San Jose Mine commenced commercial production on schedule in September of 2011. Mine production for the period from start-up in August 2011 through December 31, 2011 totaled 171,000 tonnes with approximately 46,000 tonnes remaining in the

crushed ore stockpile at year-end. Mine development is continuing and is projected to reach the 1300 meter level prior to the end of 2012 at which time underground development drilling will be initiated for conversion of the Inferred Resources in the lower portion of the deposit to Measured and Indicated Resources and subsequently with the application of qualifying factors, to Mineral Reserves.

As of December 31, 2011, the San Jose Mine had Proven and Probable Mineral Reserves of 3.6 million tonnes containing 23.6 million ounces of silver and 183,700 ounces of gold. Measured and Indicated Resources total 376,000 tonnes, containing 2.9 million ounces of silver and 25,600 ounces of gold. Inferred Resources total 3.1 million tonnes and contain an estimated 22 million ounces of silver and 178,100 ounces of gold. End-of-year mine-model reconciliation results indicate that the Mineral Resource and Mineral Reserve models are reliable indicators of the global metal content of the deposit. Variations from the previously reported reserves and resources (see Fortuna news release dated April 12, 2011) are the result of depletion through the development of the mine and extraction of ore between the start-up of the mine in August, 2011 and the end of 2011.

The San Jose deposit remains open to the southeast and to-depth. The 2012 exploration program includes 15,000 meters of surface diamond drilling which will follow up on leads developed in the 2011 exploration program as well as the testing of new targets in the 58,000 hectare concession package controlled by the Company in the San Jose area.

Qualified Persons

The updated Mineral Resource estimate for the Caylloma Mine has been prepared under the supervision of Eric Chapman of the Company. The Mineral Reserve estimate and the Mineral Resource estimate exclusive of the Mineral Reserves for Caylloma were prepared under the supervision of Edgard Vilela of the Company. The updated Mineral Reserve estimate and the Mineral Resource estimate exclusive of the Mineral Reserves for the San Jose Mine were prepared under the supervision of Edgard Vilela of Fortuna Silver Mines Inc.

Eric Chapman and Edgard Vilela are Qualified Persons as defined by the National Instrument 43-101. Thomas Vehrs, Vice President of Exploration, is the Qualified Person for the Company as defined by the National Instrument 43-101. Dr. Vehrs is a Founding Registered Member of the Society for Mining, Metallurgy, and Exploration, Inc. (SME Registered Member Number 3323430RM) and is responsible for ensuring that the information contained in this document relating to the updated Mineral Resources and Mineral Reserves is an accurate summary of the original reports and data provided to or developed by the Company.

Financing

In 2010, the Company entered into a credit agreement with the Bank of Nova Scotia for a US$20 million senior secured revolving credit facility to be refinanced or repaid before December 2012. The proceeds of the facility may be used for general corporate purposes, including the development of the San Jose Project. The facility was intended to complement the Company's cash position and provide additional financing flexibility during the construction stage at San Jose. No funds have been drawn under this facility.

On March 3, 2010, the Company completed a bought-deal public financing with a syndicate of underwriters co-led by CIBC and Canaccord Financial Ltd. pursuant to which the Company issued 15,007,500 common shares at a price of CAD$2.30 per share, for gross proceeds of CAD$34.5 million. Net proceeds were CAD$32.8 million after underwriting fees of CAD$1.7 million. The net proceeds from the financing were used to partially fund the mine construction at the San Jose Project.

On December 23, 2010, the Company completed a second bought-deal financing with a syndicate of underwriters led by Canaccord Genuity Corp. pursuant to which the Company issued 11,500,000 common shares at a price of CAD$4.00 per share, for gross proceeds of CAD$46.0 million. Net proceeds were CAD$43.7 million after underwriting fees of CAD$2.3 million. A portion of the net proceeds from the financing were used to fund exploration programs in Mexico and Peru and for general working capital, and the balance of the proceeds are intended to be used to fund the planned expansion to 1,500 tpd at the San Jose Mine.

TSX Listing

The Company graduated from the TSX Venture Exchange to the TSX and its Common Shares began trading on the TSX on January 18, 2010.

NYSE Listing

The Company completed a listing application on the New York Stock Exchange and its Common Shares began trading on the NYSE on September 19, 2011.

DESCRIPTION OF THE BUSINESS

General

Summary. The Company is engaged in silver and gold mining and related activities, including exploration, extraction, and processing. The Company operates the Caylloma silver/lead/zinc Mine in southern Peru and the San Jose silver/gold Mine in Mexico.

The lead-silver, ,zinc, and gold-silver concentrates produced by the Company at its Caylloma Mine in Peru and its San Jose Mine in Mexico are sold to international metals traders who in turn deliver the products to different clients around the world. The revenue

breakdown by product for 2011 and 2010 is as follows:

By type of concentrate	2011	2012
· Lead-silver concentrate:	73%	43%
· Zinc concentrate:	14%	21%
· Gold-silver concentrate:	11%	0%
· Copper-silver concentrate	1%	36%
By metal contained in concentrate		
· Silver:	65%	48%
· Lead:	15%	23%
· Zinc:	14%	22%
· Gold:	6%	3%
· Copper	0%	4%

The method of production both at Caylloma and San Jose consist of underground mining through cut and fill mechanized operations. Extracted ore is trucked to a conventional flotation processing plant which consists of inc, and lead-silver flotation circuits for Caylloma, and a gold-silver circuit for San Jose.

Specialized Skill and Knowledge. All aspects of the Company's business require specialized skills and knowledge. Such skills and knowledge include the areas of geology, mining, metallurgy, engineering, environment issues, permitting, social issues, and accounting. While recent increased activity in the resource mining industry has made it more difficult to locate and retain competent employees in such fields, the Company has been successful in finding and retaining personnel for the majority of its key processes.

Competitive Conditions. The Company competes with other mining companies, some of which have greater financial resources and technical facilities, for the acquisition of mineral property interests, as well as for the recruitment and retention of qualified employees.

Environmental Protection. The Company is currently in compliance with all material environmental regulations applicable to its exploration, development, construction and operating activities. The financial and operational effects of environmental protection requirements on capital expenditures, earnings and expenditures during the fiscal year ended December 31, 2011 were not material. The Company has recorded in its financial statements for the year 2011 an asset retirement obligation which reflects its environmental obligations associated with the Caylloma Mine closure plan as approved by the Peruvian government and the San Jose Mine closure plan as estimated in the pre-feasibility study.

Employees. The Company and its subsidiaries have 751 direct employees and 786 indirect employees through contractors.

Foreign Operations. The Company's material mineral resource properties are located in Peru and Mexico, each of which has a stable government and non-volatile currency.

Social or Environmental Policies. The Company has built strong relationships with the communities in which it operates, and has adopted a formal social policy that is fundamental to its operations. The Company is committed to complying in all material respects with all environmental laws and regulations applicable to its activities.

Risk Factors

The Company's ability to generate revenues and profits from its natural resource properties is dependent upon a number of factors, including, without limitation, the following:

Risks Related to the Caylloma and San Jose Mines

Operating hazards and risks. Mining operations generally involve a high degree of risk, which even a combination of experience, knowledge and careful evaluation may not be able to overcome. Hazards such as unusual or unexpected formations and other conditions can occur. Operations in which the Company has a direct or indirect interest will be subject to all the hazards and risks normally incidental to exploration, development and production of precious and base metals, any of which could result in work stoppages, damage to or destruction of mines and other producing facilities, damage to life and property, environmental damage and possible legal liability for any or all damages. The Company may become subject to liability for pollution, cave-ins or hazards against which it cannot insure or against which it may elect no to insure. Any compensation for such liabilities may have a material, adverse effect on the Company's financial position.

Concentrate treatment charges and transportation costs. The Company has entered into agreements to sell its forecast concentrate production from the Caylloma and San Jose Mines for 2012. Smelting and refining rates correspond to contract rates established mainly at 2011 year end. There is no assurance that the Company will be able to enter into smelting and refining contracts at similar competitive terms for 2013. The cost of transporting concentrate from the Mines to the smelters is dependent on, among other things, the concentrate destination. Transportation related costs have been volatile over the last several years and could continue to be volatile due to a number of factors, including changes in the price of oil, or a shortage in the number of vessels available to ship concentrate to smelters. Increases in these rates will have an adverse impact on the Company's results of operations and financial condition.

Risks Relating to the Company

Capital and operating costs, production schedules, and economic returns. The Company's expected operating costs and expenditures, production schedules, economic returns and other projections from a mining project which are contained in this document and in any technical reports, scoping studies, pre-feasibility studies and feasibility studies prepared for or by the Company are based on assumed or estimated future metals prices, cut-off grades, operating costs, capital costs, and expenditures and other factors any of which may prove to be inaccurate. Therefore, feasibility studies and other studies and reports may prove to be unreliable.

The Company's operating costs are affected by the cost of commodities and goods such as steel, fuel, electrical power and supplies, including tires and reagents. Management prepares its cost and production guidance and other forecasts based on its review of current and estimated future costs, and assumes that the materials and supplies required for operations will be available for purchase. An increase in any of these costs, or a lack of availability of commodities and goods, may have an adverse impact on the Company's financial condition.

General economic conditions. Events in global financial markets in the latter part of 2008 have had a profound impact on the global economy. Many industries, including the precious and base metals mining industry, have been impacted by these market conditions. Some of the key impacts of the financial market turmoil at that time included contraction in credit markets resulting in a widening of credit risk, devaluations and high volatility in global equity, commodity, foreign exchange and precious metal markets, and a lack of market liquidity. The world economy today continues dealing with the aftermath of the 2008 crisis, with the sovereign debt crisis in Europe being the most visible risk to world financial stability. A continued or worsened slowdown in economic conditions, including but not limited to, consumer spending, employment rates, business conditions, inflation, fuel and energy costs, consumer debt levels, lack of available credit, the state of the financial markets, interest rates, and tax rates may adversely affect the Company's growth and profitability. Specifically:

- Under a worst case scenario a new global credit/liquidity crisis could impact the cost and availability of financing and the Company's overall market liquidity;
- the volatility of metal prices could impact the Company's revenues, profits, losses and cash flow;
- volatile energy prices, commodity and consumables prices and currency exchange rates could impact the Company's production costs; and
- the devaluation and volatility of global stock markets could impact the valuation of the Company's equity and other securities.

These factors could have a material adverse effect on the Company's financial condition and results of operations.

Substantial reliance on the Caylloma and San Jose Mines. All of the Company's revenues in the current and prior years have been generated by the Caylloma Mine, until September 2011 when commercial production commenced at the San Jose Mine. For 2012, the Company anticipates a significant percentage of its future revenue will come from the Caylloma and San Jose Mines. Unless the Company develops or acquires additional properties or projects, the Company will remain largely dependent upon the operation of the Caylloma and San Jose Mines for its revenue and profits, if any. If for any reason production at either Mine was reduced or stopped, the Company's revenues and profits would decrease significantly.

Additional businesses and assets may not be successfully integrated. The Company undertakes evaluations of opportunities to acquire additional mining assets and businesses. Any acquisitions may be significant in size, may change the scale of the Company's business, and may expose the Company to new geographic, political, operating, financial and geological risks. The Company's success in its acquisition activities depends on its ability to identify suitable acquisition candidates, acquire them on acceptable terms, and integrate their operations successfully. Any acquisitions would be accompanied by risks such as a significant decline in the relevant metal price after the Company commits to complete an acquisition on certain terms; the quality of the mineral deposit acquired proving to be lower than expected; the difficulty of assimilating the operations and personnel of any acquired companies; the potential disruption of the Company's ongoing business; the inability of management to realize anticipated synergies and maximize the financial and strategic position of the Company; the failure to maintain uniform standards, controls, procedures and policies; the impairment of relationships with employees, customers and contractors as a result of any integration of new management personnel, and the potential unknown liabilities associated with acquired assets and businesses. There can be no assurance that any assets or business acquired will prove to be profitable or that the Company will be able to integrate the required businesses successfully, which could slow the Company's rate of expansion and the Company's business, results of operations and financial condition could suffer.

Fortuna may need additional capital to finance other acquisitions. If the Company obtains further debt financing, it will be exposed to the risk of leverage and its operations could become subject to restrictive loan and lease covenants and undertakings. If the Company obtains equity financing, existing shareholders may suffer dilution. There can be no assurance that the Company would be successful in overcoming these risks or any other problems encountered in connection with such financings.

Political and country risk. The Company conducts, or will conduct, exploration, development and production activity in a number of countries, namely Peru and Mexico and potentially others. The State of Oaxaca in Mexico has a history of social conflicts and political agitation which can lead to public demonstrations and blockades that can from time to time affect the Company's operations. The Company is not able to determine the impact of potential political, social, economic or other risks on its future financial position, including:

- Cancellation or renegotiation of contracts;
- Changes in foreign laws or regulations;
- Changes in tax laws;

- Royalty and tax increases or claims by governmental entities;
- Retroactive tax or royalty claims;
- Expropriation or nationalization of property;
- Inflation of costs that is not compensated by a currency devaluation;
- Restrictions on the remittance of dividend and interest payments offshore;
- Environmental controls and permitting;
- Risks of loss due to civil strife, acts of war, guerrilla activities, insurrection and terrorism, and
- Other risks arising out of foreign sovereignty over the areas in which the Company's operations are conducted.

Such risks could potentially arise in any country in which the Company operates. Furthermore, in the event of a dispute arising from such activities, the Company may be subject to the exclusive jurisdiction of courts outside North America or may not be successful in subjecting persons to the jurisdiction of the courts in North America, which could adversely affect the outcome of a dispute.

Commodity forward and option contracts for base metals production. From time to time the Company may enter into agreements to receive fixed prices on any mineral production to offset the risk of revenue losses if commodity prices decline; however, if commodity prices increase beyond the levels set in such agreements, the Company will not benefit from such increases.

Government regulation. Operations, development and exploration on the Company's properties are affected to varying degrees by political stability and government regulations relating to such matters as environmental protection, health, safety and labour, mining law reform, restrictions on production, price controls, tax increases, maintenance of claims, tenure, and expropriation of property. There is no assurance that future changes in such regulations, if any, will not adversely affect the Company's operations.

The activities of the Company require licenses and permits from various governmental authorities. While the Company currently has been granted the requisite licenses and permits to enable it to carry on its existing business and operations, there can be no assurance that the Company will be able to obtain all the necessary licenses and permits which may be required to carry out exploration, development and mining operations for its projects.

Environmental matters. All phases of the Company's operations are subject to environmental regulation in the various jurisdictions in which it operates. Environmental legislation is evolving in a manner which will require stricter standards and enforcement, increased fines and penalties for non-compliance, more stringent environmental assessments of proposed projects and a heightened degree of responsibility for companies and their officers, directors and employees. There is no assurance that future changes in environmental regulation, if any, will not adversely affect the Company's operations. Environmental hazards may exist on the Company's properties which are unknown to the Company at present which have been caused by previous or existing owners or operators of the properties.

Competition for water and water shortages. The Company's operations require water, and its Mines are located in regions where water is scarce. While the Company believes it holds sufficient water rights to support its current operations, future developments could limit the amount of water available to the Company. New water development projects, or climatic conditions such as extended drought, could adversely affect the Company. There can be no guarantee that the Company will be successful in maintaining adequate supplies of water for its operations.

Dependence on key management personnel. The Company is dependent on a number of key management personnel, including the services of certain key employees. The Company's ability to manage its exploration, development, construction and operating activities, and hence its success, will depend in large part on the ability to retain current personnel and attract and retain new personnel, including management, technical and unskilled employees. The loss of the services of one or more key management personnel could have a material adverse effect on the Company's ability to successfully manage and expand its affairs.

The Company is expecting significant growth in its number of employees as a result of its growth strategy. This growth will place substantial demands on the Company and its management. The Company's ability to recruit and assimilate new personnel will be critical to its performance. The Company will be required to recruit additional personnel and to train, motivate and manage its employees. The international mining industry is very active and the Company is facing increased competition for personnel in all disciplines and areas of operation, and there can be no assurance that it will be able to retain current personnel and attract and retain new personnel.

Director and officer conflicts of interest. Certain of the directors and officers of the Company also serve as directors and/or officers of other companies involved in natural resource exploration and development and consequently there exists the possibility for such directors and officers to be in a position of conflict. In such case, the Company's directors and officers comply with conflict of interest provisions in Canadian corporate law, including relevant securities regulatory instruments, in order to ensure that they exercise independent judgment in considering transactions and agreements in respect of which a director or officer has a material interest.

Title to properties. Although the Company has or will receive title opinions for any properties in which it has a material interest, there is no guarantee that title to such properties will not be challenged or impugned. The Company has not conducted surveys of the claims in which it holds direct or indirect interests and, therefore the precise area and location of the properties may be in doubt. The Company's properties may be subject to prior unregistered agreements or transfers or native land claims and title may be affected by unidentified or unknown defects. The Company has conducted as thorough investigation as possible on the title of properties that it has acquired or will be acquiring to be certain that there are no other claims or agreements that could affect its title to the properties.

Dilution from further equity financing. If the Company raises additional funding by issuing additional equity securities, such financing may substantially dilute the interests of existing shareholders of the Company and reduce the value of their investment.

Foreign currency. The Company's activities and operations in Mexico and Peru make it subject to foreign currency fluctuations. The Company's operating expenses are primarily incurred in Mexican pesos and Peruvian Sol, and the fluctuation of the US dollar in relation to these currencies will consequently have an impact upon the profitability of the Company and may also affect the value of the Company's assets and the amount of shareholders' equity. The Company has not entered into any agreements or purchased any instruments to hedge possible currency risks.

Exploration and development. Development of the Company's non-producing properties will only follow upon obtaining satisfactory exploration results that confirm economically recoverable and saleable volumes of minerals and metal. The business of mineral exploration and development is speculative in nature and involve a high degree of risk, as few properties which are explored are ultimately developed into producing mines. There is no assurance that the Company's mineral exploration and development activities will result in any discoveries of reserves of commercial ore. The long-term profitability of the Company's operations will be in part directly related to the cost and success of its exploration programs, which may be affected by a number of factors.

Substantial expenditures are required to establish resources and reserves through drilling and development and for mining and processing facilities and infrastructure. Although substantial benefits may be derived from the discovery of a major mineralized deposit, no assurance can be given that minerals will be discovered in sufficient quantities to justify commercial operations or that the funds required for development can be obtained on a timely basis.

The marketability of any minerals acquired or discovered may be affected by numerous factors which are beyond the Company's control and which cannot be accurately foreseen or predicted, such as market fluctuations, the global marketing conditions for precious and base metals, the proximity and capacity of milling facilities, mineral markets and processing equipment, and such other factors as government regulations, including regulations relating to royalties, allowable production, importing and exporting minerals and environmental protection.

Estimation of mineral resources and reserves and precious metal recoveries. There is a degree of uncertainty attributable to the estimation of resources and reserves and to expected mineral grades. Mineral resources and mineral reserves may require revision based on actual production experience. Market fluctuations in the price of metals, as well as increased production costs and reduced recovery rates, may render certain mineral reserves uneconomic and may ultimately result in a restatement of mineral resources and/or reserves. Short term operating factors relating to the mineral resources and reserves, such as the need for sequential development of ore bodies may adversely affect the Company's profitability in any accounting period.

Reclamation. There is a risk that monies allotted for land reclamation may not be sufficient to cover all risks, due to changes in the nature of the waste rock or tailings and/or revisions to government regulations. Therefore, additional funds, or reclamation bonds or other forms of financial assurance may be required over the tenure of the project to cover potential risks. These additional costs may have material adverse impact on the financial condition and results of the Company.

Uncertainty of funding. The Company's operating cash flow from the Caylloma and San Jose Mines may not be sufficient to cover the current costs of exploration and development of the Company's other, non-producing properties. Exploration and development activities may be dependent upon the Company's ability to obtain financing through joint venturing, equity or debt financing or other means, and although the Company has been successful in the past in obtaining financing through the sale of equity securities, there can be no assurance that the Company will be able to obtain additional financing or that the terms of such financing will be favorable. Failure to obtain such additional financing could result in delay or indefinite postponement of further exploration and development of some of its projects.

Competition. The mining industry is intensely competitive in all of its phases, and such competition could adversely affect the Company's ability to acquire suitable resource properties in the future.

Material Mineral Properties

The Company has two material mineral projects, described below.

Caylloma Mine, Peru

The Company owns a 100% interest in the Caylloma Mine, Peru.

The following is the Summary from the report (the "Caylloma Report") entitled "Technical Review (NI 43-101), Caylloma Project, Peru" dated August 11, 2009 prepared by Richard L. Nielsen, PhD., Steve Milne, P.E. and Robert L. Sandefur, P.E. of Chlumsky, Armbrust and Meyer, LLC. The full text of the Caylloma Report is available for viewing on SEDAR at www.sedar.com and is incorporated by reference in this AIF. Defined terms and abbreviations used herein and not otherwise defined shall have the meanings ascribed to such terms in the Caylloma Report.

At the request of Fortuna Silver Mines Inc. (FSM), Chlumsky, Armbrust and Meyer, LLC (CAM) conducted a technical due diligence review of the updated mineral resources and reserves at the Caylloma Silver Mine, located north-northwest of Arequipa, Peru. CAM's scope of work for this technical review focused on a new model for the Animas Vein and checks of the updated reserve

estimation, based on all available data through 31 December 2008, except for the Bateas vein, which includes all data through 31 March, 2009.

The Caylloma property was previously evaluated by CAM in 2005-2006 through a Technical Report dated 2006, when FSM was in the process of acquiring the property. This report constitutes a substantial update of the previous investigation, and includes a revised resource model for the Animas Vein and changes to the previous resources and reserves in the other veins due to changes in metal prices, operating costs, mining of some previous resources and reserves, and new sampling data.

The property was owned by Compañía Minera Arcata, S.A. prior to 2005. The mine was in production by Arcata until early 2003, when it was shut down due to depletion of accessible mineral reserves. Fortuna Silver Mines Inc. (FSM), formerly Fortuna Ventures Inc., acquired the property in 2005, and placed it into production in September 2006 with a refurbished mill which included separate circuits for silver-lead, for zinc, and later (in 2009) for copper.

Operations at Caylloma are carried out under the name of Minera Bateas S.A.C., a wholly-owned subsidiary of FSM. The current operation exploits the Animas Vein and other polymetallic (Ag-Pb-Zn) veins, rather than the silver-only veins previously exploited by Arcata.

The Caylloma mine is located in the Caylloma Mining District, 225 road-kilometers north-northwest of Arequipa, Peru, and 14 kilometers northwest of the town of Caylloma. It lies at 4,400 to 4,800 meters above sea level in the Peruvian Andes.

The mineral property consists of mineral rights in 3 "*acumulaciones*" and 26 mining concessions for a total surface area of 8,171.3 hectares. All of the acumulaciones and mining concessions constitute the Unidad Económica Administrativa (UEA) San Cristobal. In addition, FSM owns extensive surface rights.

The host rocks for mineralized veins in the district are volcanic rocks of the upper Miocene Tacaza Group, which lie in angular unconformity over a sedimentary sequence of quartzites and shales of the upper Mesozoic Yura Group. Portions of the property area are covered by a variable thickness of postmineral Plio-Pleistocene volcanic deposits and recent alluvial sediments.

Six major vein systems are recognized in the Caylloma District, all having a general northeast-southwest strike, and mainly dipping to the southeast. The host rocks of the Caylloma vein systems are breccias, lavas and andesitic volcaniclastic units of the Tacaza volcanic group. The Caylloma District is located near the northwestern margin of the Caylloma caldera complex.

The economic mineralization mined in the past come from five of the vein systems, which were all silverrich with low base metal contents. In contrast, the Animas vein system contains polymetallic silver basemetal mineralization, with minor gold credits. The mineralization in all six vein systems occurs in ore shoots which are up to several hundred meters long, with vertical extents ranging up to 300 meters. Width of the veins varies from a few centimeters to 20 meters, averaging about 1.2 meters for the silver veins, and 2.5 meters for the polymetallic veins.

The geology and mineralization controls are well-understood by FSM geologists, who have several years of operations experience.

The mineral resources as of 31 December 2008 (31 March 2009 for the Bateas Vein) have been estimated in eight different veins on the Caylloma property. CAM believes that there is good potential for the discovery of additional resources and reserves on the property. This added potential is present in:

- Developed veins are open at depth and some potential exists along strike.
- Undeveloped veins identified on surface or in underground workings where only low-grade mineralization has been encountered at a limited number of exposures.
- Undiscovered veins on the remainder of the property.

Historically, core drilling has been used at Caylloma to determine the locations of extensions for known mineralized structures, which are followed up by underground drifting and development. Both core samples and underground channel samples are used for resource estimation.

As with most high-grade, multi-metal, vein deposits, local variations in metal content are commonly high and large differences can exist between successive sampling campaigns of the same areas. As a check on analytical accuracy and precision, the mine laboratory, which assays channel samples, uses an elaborate and thorough quality assurance/quality control (QA/QC) series of checks, including standards, blanks, preparation duplicates, pulp duplicates, and re-sampling. Core samples are assayed at ALS Chemex, an independent laboratory, and are subject to equally rigid QA/QC procedures. Separate limits of acceptable deviation in values for silver, gold, zinc, lead and copper are applied, and re-assaying is done whenever the limits are exceeded.

It is CAM's opinion that the QA/QC procedures followed by FSM are thorough and appropriate. CAM believes that the assay database is adequate and appropriate for resource estimation.

On the basis of this review, CAM believes that the databases for the polymetallic veins have been assembled according to accepted practices, and are suitable for use in ongoing mine planning for the life of the operation.

For the polymetallic Animas Central, Animas NE7, Animas NE8, Santa Catalina, Soledad, Silvia and Bateas veins, three dimensional wireframe models were constructed for each vein system and drill hole and channel sample grades were composited to 2.5meters or to the vein width for veins of less than 2.5 meters. Block models were constructed within each wireframe using the DataMine software package with block sizes varying according to vein dimensions and ranging to a maximum size of 5 by 5 by 2.5 meters. Sub-blocking was used as necessary to more precisely reflect actual vein geometry. Metal grades were estimated using

ordinary kriging in sectors with channel sample data from stopes and crosscuts, and using inverse distance squared in sectors with only drillhole data. A density factor of 3.00 grams per cubic centimeter has been used for conversion of block volumes to tonnes. Resource classification was based on the number of composite samples used in estimation of the grade for each block with Measured Resources being estimated by 12 to 20 composite samples, Indicated Resources being estimated by 8 to 11 composite samples and Inferred Resources being estimated by 1 to 7 composite samples. An NSR value of US$37.15 was used as the lower cut-off value for the reporting of mineral resources.

For the silver-bearing San Cristobal, San Pedro, San Carlos, La Plata, Cimoide La Plata, Paralela and Ramal Paralela veins, mineral resources were estimated by inverse distance squared methods using density factors ranging from 2.82 to 2.95 grams per cubic centimeter. Classification of resources was based on distance from development workings with Measured Resources being blocks extending up to 25 meters from horizontal or vertical workings, Indicated Resources are those blocks located beyond 25 meters but within 40 meters of development workings, and Inferred Resources being those blocks located at distances of greater than 40 meters from workings.

Mineral resources are given in Table 1-1 (Measured and Indicated) and Table 1-2 (Inferred), both of which exclude mineral reserves. Mineral resources which have been converted to mineral reserves are given in Table 1-3.

Table 1-1
Measured and Indicated Resources, All Veins, Exclusive of Reserves

Category	**Tonnes**	**Ag (g/t)**	**Au (g/t)**	**Pb (%)**	**Zn (%)**	**Cu (%)**	**Width (m)**
Measured Resources	247,070	63	0.31	1.19	2.23	0.11	**1.69**
Indicated Resources	20,400	71	0.29	1.00	1.40	0.15	**2.74**
Measured + Indicated Resources	**267,470**	**64**	**0.31**	**1.18**	**2.17**	**0.11**	**1.77**

Table 1-2
Inferred Resources, all Veins, Exclusive of Reserves

Category	**Tonnes**	**Ag (g/t)**	**Au (g/t)**	**Pb (%)**	**Zn (%)**	**Cu (%)**	**Width (m)**
Inferred Resources	**1,279,000**	**187**	**0.29**	**1.92**	**3.25**	**-**	**2.58**

Caylloma has been operating normally since October 2006, with mill throughput increasing gradually toward the optimized capacity of 423,600 tonnes per year.

Economic cutoff and dilution factors have been applied to the mineral resource estimates to determine mineable reserves as shown in Table 1-3.

Table 1-3
Diluted Mineable Ore Reserves at Caylloma as of December 31, 2008

Description	**Tonnes**	**Ag (g/t)**	**Au (g/t)**	**Pb (%)**	**Zn (%)**
Silver Veins					
Proven	421,320	387	0.83	0.01	**0.02**
Probable	228,500	369	0.55	0.05	**0.09**
Total, Silver Veins	649,820	380	0.73	0.02	**0.04**
Polymetallic Veins					
Proven	3,280,100	103	0.52	2.03	**3.09**
Probable	103,000	426	0.44	1.74	**2.41**
Total, Polymetallic	3,383,100	113	0.51	2.02	**3.07**
All Veins					
Proven	3,701,420	136	0.55	1.80	**2.74**
Probable	331,500	387	0.51	0.58	**0.81**
Total All Veins	**4,032,920**	**156**	**0.55**	**1.70**	**2.58**

Underground mining is currently focused on the Animas, Santa Catalina, and Soledad veins. These veins are polymetallic veins, containing silver, gold, lead, zinc and copper mineralization. Production from these veins during the year 2008 was 331, 380 tonnes, or about 950 tonnes per day, of which about 95 percent originated in the Animas vein. The veins are accessed from adits driven from the surface.

In the Animas vein, where vein widths reach up to eight meters, the mining method is mechanized ascending cut-and-fill, using hydraulic deslimed mill tailings as backfill. The Soledad vein is much narrower, and is also mined by cut-and-fill methods, but requires the use of micro-scoops for loading of broken ore. Production from the Soledad vein averaged about 5% of total production. Santa Catalina is also a narrow vein, mined by a shrinkage method.

The milling process consists of conventional crushing and grinding, followed by selective flotation, producing concentrates for lead and zinc. The mill is being modified to raise the capacity from 1,000 tonnes per day to 1,200 tonnes per day of silver and polymetallic vein ores, by the year 2010. The mineralogy at Caylloma is relatively straightforward, and mill recoveries have increased steadily since the 2006 start-up. During the fourth quarter of 2008, recoveries were:

- Silver..... 82.4 percent
- Gold ..... 37.5 percent
- Lead ..... 93.4 percent
- Zinc ..... 87.2 percent

In April 2009, subsequent to the effective date of this Technical Report, a copper-recovery circuit was added to the mill.

FSM has signed contracts for all of its lead and zinc concentrates with AYSSA (GLENCORE's representative in Peru). During 2008, 20,960 wet-tonnes of zinc concentrate and 12,620 wet tonnes of lead concentrate were sold. Transportation of all concentrates from the mine site to the port of Callao is by truck.

CAM's conclusions regarding the mineral resources and reserves at Caylloma are as follow:

1. It is CAM's opinion that FSM personnel have a clear understanding of the geology and features controlling the distribution of economic-grade mineralization.
2. Considerable potential exists for discovery of additional resources through exploration on extensions of known mineralized structures on the property.
3. CAM has reviewed the methods used by FSM to collect information for the resource database and believes that proper practices have been used in sample collection, sample preparation, and assaying. QA/QC procedures followed by FSM were thorough and appropriate. The bulk-density database is satisfactory, but could be improved.
4. The resource models are constructed according to accepted engineering practice and the acceptability of these models for use in mine planning and financial decisions is confirmed by the reconciliation on the veins with a reasonable amount of production.
5. Mining and milling operations are relatively straightforward, and do not present unusual challenges for profitable operations at current or foreseeable metals prices.

CAM's recommendations regarding the mineral resources and reserves at Caylloma are as follow:

1. Continuing exploration is recommended to augment the known resources and reserves.
2. There are some minor inconsistencies relating to mined out samples which should be reviewed.
3. Some minor theoretical improvements in statistical and geostatistical analysis are possible. These should be implemented if future reconciliations of reserves versus mill feed are not satisfactory.
4. The practice of reporting precious-metals assays as Troy ounces per metric tonnes should be discontinued, and these results should be reported as grams per metric tonne.
5. Continuation of mining and milling operations is recommended, with recovery of copper and continuing optimization of metals recoveries.

San Jose Mine, Mexico

The Company owns a 100% interest in the San Jose Mine, Mexico.

The following is the Summary from the report (the "San Jose Pre-Feasibility Report") entitled "NI 43-101 Technical Report, San Jose Project, Oaxaca, México" dated June 9, 2010 prepared by Craig S. Bow, PhD and Gregory Chlumsky, QP-MSSA and Steve L. Milne, PE, of Chlumsky, Armbrust & Meyer, LLC. The full text of the San Jose Pre-Feasibility Report is available for viewing on SEDAR at www.sedar.com and is incorporated by reference in this AIF. Defined terms and abbreviations used herein and not otherwise defined shall have the meanings ascribed to such terms in the San Jose Pre-Feasibility Report.

The following information regarding the San Jose Project has been extracted from the San Jose Pre-Feasibility Report.

Introduction

This Pre-Feasibility Study ("Pre-Feasibility Study" or "Report") of the San José Project (the "Project" or "San José") has been prepared by Chlumsky, Armbrust & Meyer LLC ("CAM") at the request of Compañia Minera Cuzcatlán S.A. de C.V. ("CMC"). This Report was compiled and prepared as a collaborative effort between CAM and CMC, and based on input from a number of technical consultants acting on behalf of CMC.

Table 1-1 displays the list of Technical Consultants that performed geological evaluation, resource estimation, engineering, and design activities, together with evaluations of capital and operating costs in support of the Pre-Feasibility Study.

Table 1-1
Technical Consultants

Area	Company
2009 43-101 Geology	Resource Evaluations, Inc. (REI)
2009 43-101 Resources	Resource Modeling, Inc. (RMI)
Mine	Proyectos y Estudios Mineros-S.A.C. (PEM)
Geotechnical	SVS Ingenieros S.A.C. (SVS)
Metallurgy/Process	Transmin Metallurgical Consultants (Transmin) METCON Research (METCON)
Process Plant	Procesos Mineros Metalúrgicos S.A. de C.V. (PROMIMET)
Tailings	SVS Ingenieros S.A.C. (SVS)
Water Supply	Ingeniería de Control Ambiental y Saneamiento S.A de C.V. (ICAYS)
Power/Substation	Soto Ortega Ingenieros S.A. de C.V. (SOI)
Environmental/Social	Clifton Associates Ltd. (Clifton)

Location and Access

The San José Project is located in the central portion of the state of Oaxaca, Mexico (Latitude 16° 41'39.10"N, Longitude 96°42 ´06.32"W; UTM coordinates (NAD27, UTM Zone14N).745100E, 1846925N).

The Project location is approximately 47 kilometers by road south of the city of Oaxaca, a city of 460,000 inhabitants, which lies 470 kilometers southeast of Mexico City. The mine is located approximately 0.8 kilometers east of Federal Highway 175, the major highway between Oaxaca and Puerto Angel on the Pacific coast. The nearest large population center to the property is the town of Ocotlán de Morelos, which has approximately 25,000 inhabitants and lies 12 kilometers north of the Project site.

The Project site and surrounding area is characterized by rolling hills and plains. The concessions are located at elevations between 1,540 and 1,675 meters above sea level (San Jose) and 1640 to 1840 meters (Taviche) The vegetation is grassland and thorn-bush typical of dry tropical savannah.

The climate is of "tropical wet-and-dry savannah" type, and is compatible with year-round mining operations. The average annual precipitation is 500 to 750 millimetres.

Geology and Resources

Geology and Mineralization

The San Jose Project occurs within the "Oaxaca Terrane," one of a series of structurally-bounded, lithostratigraphic blocks in southern Mexico distinguishable on the basis of its diagnostic stratigraphy, structural patterns, and tectonic history. Basement rocks in the vicinity of San Jose comprise Proterozoic-age amphibolite to granulite facies migmatite and gneiss, overlain by a sequence of Mesozoic and Tertiary sedimentary and volcanic rocks. Bedrock in the project area is dominated by sub-horizontal andesitic to dacitic volcanic and volcaniclastic rocks of Tertiary age. These units have been cut be north- and north-northwest-trending extensional faults.

Silver and gold mineralization in the Trinidad deposit is hosted by steeply dipping hydrothermal breccias, crackle breccias and sheeted or stockworked quartz/carbonate veins emplaced along north and north-northwest trending, east-northeast dipping faults. The "east side down" faults exhibit dip-slip motion with cumulative displacements of up to 300 meters recorded between the footwall and the hanging wall of the mineralized structural corridor. The mineralized structural corridor extends for greater than three kilometers in a north-south direction and has been subdivided into the Trinidad deposit area, and the San Ignacio area. The Mineral Resource and Reserve estimates described in this report are located in the Trinidad deposit area. The major vein systems recognized in the Trinidad deposit area are identified as the Trinidad, Fortuna and the Bonanza structures. In addition, a prominent zone of mineralized sheeted and stockwork quartz/carbonate veins has been identified in the zone between the Trinidad and Bonanza vein systems. Drilling has defined the Trinidad and Bonanza vein systems over a strike length of approximately 700 meters.

Minerals of economic interest are mainly acanthite and silver-rich electrum. These occur with pyrite in distinctively banded crustiform-colloform veins with quartz, chalcedony, calcite and local adularia. Sulfide contents typically are low, from less than 1 to 5 percent of the rock in the upper portion of the deposit, to somewhat higher at depth, where sphalerite, galena and chalcopyrite appear. Hydrothermal alteration includes regional propylitic alteration of the volcanic host rocks, grading to proximal alteration zones consisting of quartz, illite, illite/smectite, Fe-carbonates, and pyrite around the mineralized zones. The Trinidad Ag/Au deposit has been assigned to the low-sulfidation epithermal deposit classification.

Resources

The mineral resources cited in this report were originally estimated by Mr. Michael J. Lechner, President of Resource Modeling Inc. ("RMI") in a 2009 43-101-compliant Technical Report. Inverse distance powers of two or three were selected to estimate block silver and gold grades within wireframe solids. CAM has reviewed input and methodology, and concurs fully with the cited indicated and inferred resources.

The estimated blocks were classified into Indicated and Inferred mineral resource categories based on several criteria. Indicated resources were restricted to the four primary veins (Bonanza, Trinidad, Fortuna, and Paloma) provided that the blocks were within a specified distance from a required number of drill holes. Those criteria include: 1) at least three drill holes within 33 meters, or 2) two drill holes within 23 meters, or 3) one hole within 13 meters of the four primary veins. All remaining estimated blocks inside of the

various wireframes were classified as Inferred resources based on the currently understood geologic continuity of the mineralized structures. Additional drilling would be required to determine if those Inferred resources could be upgraded to an Indicated status.

Mineral resources were tabulated using a silver equivalent cutoff grade that incorporates metal prices and recoveries. The parameters used to calculate the silver equivalent grade are summarized in Tables 1-2.

Table 1-2
Silver Equivalent Parameters

Parameter	Value
Silver Price, USD per troy ounce	$13.75
Gold Price, USD per troy ounce	$856.16
Silver Recovery	92.5%
Gold Recovery	91.5%

The expressions for calculating the silver equivalent grade is:

*AgEq = Ag + Au * (($856.16/13.75)*(91.5/92.5)) or AgEq = Ag + Au * 61.6*

Mineral Resources at a 150 g/t AgEq cutoff grade are shown in Table 1-3 with Indicated and Inferred Resources at various cutoffs shown in Tables 1-4 and 1-5.

Table 1-3
Mineral Resources at a 150 g/t AgEq Cutoff Grade

Resource Category	Tonnes (x 1000)	AgEq (g/t)	Ag (g/t)	Au (g/t)	Contained Metal		
					AgEq oz (x 1000)	Ag oz (x 1000)	Au oz (x 1000)
Indicated	2,690	435	295	2.27	37,596	25,504	196
Inferred	2,411	392	262	2.11	30,357	20,293	164

Table 1-4
Indicated Mineral Resources at Various Cutoffs

AgEq Cutoff (g/t)	Tonnes (x 1000)	AgEq (g/t)	Ag (g/t)	Au (g/t)	Contained Metal		
					AgEq oz (x 1000)	Ag oz (x 1000)	Au oz (x 1000)
50	4,636	292	196	1.56	43,465	29,163	232
75	4,018	327	220	1.74	42,231	28,422	224
100	3,478	364	246	1.92	40,725	27,486	215
125	3,043	400	271	2.10	39,153	26,497	205
150	2,690	435	295	2.27	37,596	25,504	196
175	2,370	471	321	2.45	35,930	24,429	187
200	2,102	508	346	2.63	34,314	23,382	177
225	1,883	542	370	2.79	32,823	22,416	169
250	1,685	578	396	2.96	31,315	21,433	160

Table 1-5
Inferred Mineral Resources at Various Cutoffs

AgEq Cutoff (g/t)	Tonnes (x 1000)	AgEq (g/t)	Ag (g/t)	Au (g/t)	Contained Metal		
					AgEq oz (x 1000)	Ag oz (x 1000)	Au oz (x 1000)
50	4,020	272	181	1.48	35,199	23,389	192
75	3,497	304	202	1.65	34,151	22,735	185
100	3,074	334	222	1.80	32,963	21,988	178
125	2,681	366	244	1.97	31,545	21,061	170
150	2,411	392	262	2.11	30,357	20,293	164
175	2,137	421	282	2.26	28,922	19,351	155
200	1,883	452	304	2.41	27,393	18,379	146
225	1,696	479	321	2.56	26,113	17,522	140
250	1,545	503	337	2.69	24,958	16,747	133

Mining and Mineable Reserves

Mine planning studies were based on an escalating production schedule from 750 to 1500 tonnes per day (t/d). The PEM minable reserve study, dated March 2010, is based on the first two and a half (2.5) years at 750 t/d, then increasing to 1,000 t/d for two more years, and finally increasing to 1,500 t/d for the balance of the reserve.

Cutoff Grade

The economic portion of the resource is typically determined by the application of a breakeven cutoff grade, or value, that considers the total operating costs (variable and fixed mine, process plant and administration costs).

The total operating costs are then formulated into an algorithm that also considers: metal price(s), process recovery(s), applicable royalties, and forward costs for concentrate freight, insurance, smelting and/or refining. These parameters are then equated to determine the minimum grade, grade equivalent, or value of metal(s) that will need to be mined in order to cover these total operating costs. The cutoff grade may also be expressed as a revenue value (US$ per tonne), that equals the total operating costs.

At the San José Project there will be two payable metals – silver and gold, with silver being the predominant metal. Therefore, it would be easier to express the breakeven cutoff as a silver equivalent grade, or as a minimum net smelter return (NSR) value of the smelted concentrate, expressed in US$ per tonne of ore, which covers the total operating cost. The following basic algorithm illustrates the typical relationship, between the various parameters, to calculate at the breakeven cutoff silver equivalent grade:

$$\text{AgEq} = \frac{Total\ Operating\ Cost + Transport\ Costs + Ag\ Refining\ Costs}{(Ag\ Price + Credits)(Ag\ Recovery)} = grams\ of\ AgEq\ per\ tonne$$

If the breakeven cutoff is expressed as a value (typically an NSR in US$ per tonne ore), this value can then be compared to the sum of the mine, mill, G&A, and forward unit operating costs. The NSR value must equal, or exceed, the on-site total operating costs for the block, or stope, tonnes to be economically viable and included in the minable reserve.

The parameters in Tables 1-6 and 1-7 were utilized to estimate the silver equivalent breakeven cutoff grade for production rates of 750, 1000, and 1500 t/d.

Table 1-6
Estimated Total Operating Costs (US$ per tonne)

Production Rate	750 t/d	1,000 t/d	1,500 t/d
Mining, US$ per tonne	25.42	22.89	19.82
Processing, US$ per tonne	14.26	12.00	9.41
G&A US$ per tonne	10.06	7.55	5.03
Total Operating Cost	49.74	42.44	34.26

Table 1-7
Other Operating Parameters

Item	Value
Process Recoveries	
Gold (%)	90
Silver (%)	88
Metals Prices	
Gold (US$ per ounce)	897.51
Gold (US$ per gram)	28.85
Silver (US$ per ounce)	15.12
Silver (US$ per gram)	0.4861
Credits	
Au Credit Factor	1.55
Forward Costs	
Freight, Marketing, etc	1.96, US$ per tonne of ore
Smelting/Refining	23.68, US$ per tonne of ore

Applying the above parameters provides the following breakeven silver equivalent grade for the initial 750 t/d production rate:

$$AgEq = \frac{(\$49.74 + \$1.96 + \$23.68)}{(\$0.4861/gm\ x\ 1.55)(0.88)} = 114\ grams\ of\ AgEq\ per\ tonne$$

The corresponding breakeven cutoff grades for production rates of 1,000 t/d and 1,500 t/d are 103 grams AgEq and 90 grams AgEq per tonne.

Typically, this breakeven cutoff grade is used to identify the economic portion of the measured and indicated resource. Minable shapes (stopes) are then applied to the economical portion of the resource model. This shape may include some sub-economic material that must be taken in the mine planning and stoping process, which is included as internal dilution. In addition, some of the economic blocks may have to be dropped due to their location outside of the mining shapes, or because they would require excessive development to access and prepare the block for mining. This may decrease the minable portion of the resource recovery. Since no “Measured” resources have yet been delineated, all minable reserves tabulated in this report have been based on “Indicated” resources, and as such, are classified as “Probable” reserves.

Mining Recovery

The anticipated method for mining the veins at the San José Project is mechanized cut and fill, utilizing backfill from process tailings combined with waste generated from within the mine and from the surface. This mining method is very selective and generally allows for a high percentage recovery of the ore. Based on a review of the vein cross sections, the ore loss due to irregularities in the vein walls would typically be estimated at two percent. An additional two percent would be estimated for pillars left around stope openings, and six percent for planned sill pillars at the bottom of each stope, for a total ore loss of around ten percent, indicating an average mining recovery of 90 percent (10 percent loss).

Mining Dilution

Internal waste dilution from expanding the vein widths to minimum mining widths in the stope design process, and waste included in the drillhole compositing process has already been accounted for in the resource block model preparation.

External waste in the mining process originates from three principal sources; 1) irregularities in the vein walls, both horizontally and vertically, 2) miners over-drilling in the stope, both in the ribs and the back, and 3) mucking up backfill from the floor. Typically, irregularities in the vein walls generally account for about two percent of the dilution. Over-drilling by the miners typically adds another three percent. Another five percent typically results from loader operators mucking up waste backfill from the floor during the ore loading phase. An average total external dilution of approximately 15 percent would normally be estimated for the average mining widths of the veins at the San José Project. Typically, all dilution would be considered to be at zero grade.

Minable Reserves

After the application of a breakeven cutoff grade and factors for mining recovery and mining dilution, the minable reserves calculated by PEM for mining all of the deposit at production rates of 750, 1000 and 1500 t/d, are presented in the following Table 1-8.

Table 1-8
Minable Reserves (Probable)

Mining Rate	Tonnes	Ag (g/t)	Au (g/t)	AgEq (g/t)
750 t/d	914,405	188	1.7	288
1,000 t/d	735,279	187	1.5	277
1,500 t/d	1,866,144	221	1.6	320
Total	3,515,828	205	1.6	303

Metallurgy

Six-stage locked-cycle flotation tests were conducted on composite samples to determine final concentrate grades and recoveries to be expected in a continuous commercial operation where interim flotation products as well as reclaimed water are recycled. The locked-cycle flotation tests were conducted utilizing to the following process approaches:

a) The scheme of reagents and dosages of flotation reagents specified by Transmin achieved an overall grind size of 80 percent passing 105 microns.

b) The scheme of reagents, dosages of flotation reagents and two stages of grind process specified by METCON achieved an overall grind size of 80 percent passing 74 microns.

c) The scheme of reagents, dosages of flotation reagents, two stages of grind process and Flash Flotation procedures specified by METCON achieved an overall grind size of 80 percent passing 74 microns.

The metallurgical data and results achieved are summarized in Table 1-9.

Table 1-9
Locked Cycle Flotation on VC02 Composite Sample
Summary of Results

Locked Cycle Process	Concentrate Grade (g/t)		Recovery (%)	
	Au	Ag	Au	Ag
Transmin Process Flow Sheet	65	5,621	87.67	86.12
METCON Research Flow Sheet using Two Stages of Grind	74	6,676	89.84	87.56
METCON Research Flow Sheet using Two Stages of Grind & Flash Flotation	71	6,256	90.63	89.50
Remarks: (1) Average Metallurgical Results of the Last Three Cycles				

The METCON flowsheet test data has been selected as the basis for the process plant design and metal recoveries. CMC has decided to use a simple circuit with a single stage of grinding without flash flotation. This circuit with pyrite depression and reagent optimization has been demonstrated to produce gold recoveries of 88 percent and silver recoveries of 90 percent with concentrate grades of 65g/t gold and 7,000 g/t silver, which are considered more than reasonable taking into account the lower capital cost. The reason for the slightly lower gold grades and recoveries and higher silver grades in the concentrate is due to pyrite depression. The values noted above are those used in the Financial Model of this report.

The option for the addition of a regrind circuit with flash flotation remains available to the Project if desirable and cost effective.

Process Description

The San José concentrator facilities have been designed to process a gold and silver ore from the ore zones and produce a bulk concentrate. The concentrate will carry enriched values of silver and gold. Acanthite and electrum carry the values in the ore, and recovered with the bulk minerals. Table 1-10 displays the general characterization and the average bulk grade of the ore that the concentrator will process throughout the life of the Project.

Table 1-10
Ore Characterization and Bulk Grade

Characteristics	Units	Value
Maximum Feed Size	mm	300
Average F80	mm	159
Percent Moisture	%	3
Percent Moisture Maximum	%	5
Apparent Density	g/cm3	2.55
Au Grade	g/t	1.6
Ag grade	g/t	205
Concentrate Grade Au	g/t	65
Concentrate Grade Ag	g/t	7000
Au Recovery	%	90
Ag Recovery	%	88

The gold and silver minerals are finely disseminated throughout the ore. Size reduction of the run-of-mine (ROM) ore is completed in a series of steps that includes crushing, followed by grinding in a water slurry to a P80 of 74 microns (200 mesh). At this particle size, the majority of the gold and silver minerals are sufficiently liberated to allow recovery into flotation products.

The recovery of the valuable minerals is completed using differential froth flotation. Associated silver and gold minerals are recovered from the ore, while the final waste product reports to the mine hydraulic backfill and the tailing pond.

Infrastructure

A full range of services and supplies required to support the Project is available within a radius of 100 kilometers from the Project Site. Major seaports capable of providing services to the Project as needed are Salina Cruz on the Pacific Ocean and Veracruz on the Atlantic Ocean.

Electrical Power Supply

The electrical power for the San Jose Project will be supplied from the existing electrical grid system, which is administered by the Comision Federal de Electricidad (CFE). A 115-thousand volt (kV) transmission line passes within less than 50 meters of the proposed Project Main Substation. The 115-kV transmission line will pass through a new switching substation, installed adjacent to the Main Substation.

Water Supply

CMC has calculated a sufficient supply for fresh (makeup) water from the following sources:

- § Effluent from the Water Wastewater Treatment Facility (WWTF) at the municipality of Ocotlán de Morelos, Oaxaca;
- § Incident precipitation collected on the surface area of the Tailings Management Facility (TMF), and
- § Contingency source: Extraction and treatment of water from the Rio Atoyac, through the water treatment plant at the municipality of Ocotlán de Morelos, Oaxaca.

Support Facilities

Non process facilities for the Project will include newly constructed buildings for mine operations, Project staff and management offices, and metallurgical testing activities. Other service buildings will include warehousing, a clinic/security/fire station, and a cafeteria. A fueling station and a weighing station will also be included in the support facilities.

Tailings Management Facilities

A conventional slurry tailings facility will be developed at the San Jose Project to accommodate 5 million tonnes of tailings during the mine life. Sixty five percent of the tailings from the milling process will be deposited at a rate of 750 t/d in the first two and a half (2.5) years of operation, 1000 t/d for the next two years, and 1500 t/d until the end of the operations.

Probabilistic seismic hazard analyses (PSHA) were performed for the Project site. The results of the stability analyses indicated that all of the embankments would have factors of safety greater than the minimums prescribed by international standards.

Environmental Aspects

Environmental activities conducted for the San Jose Project were performed by several consulting groups. Clifton Associates LTD was responsible for developing the Environmental Impact Assessment (EIA), using the information collected during baseline study development for the environmental and social areas. Consulting firms involved in baseline development included: (1) Clifton Associates LTD (Environmental Baseline Studies including Soils, Vegetation, Wildlife, Noise, Air Quality, etc.); Water Management Consultants (Groundwater evaluation); (3) Independent University San Luis Potosí (Water Resources); and (4) Ingenieria de Control y Saneamiento (ICAYS SA de CV), (Water Project).

The San Jose Project has a total surface area of 92 hectares (ha).

Background information has been collected and initial studies have been performed in the areas of air quality; noise and vibration control; surface and groundwater resources; and water quality.

An initial evaluation has been conducted and a preliminary mitigation plan has been developed with regard to potential impacts to

the groundwater system in that area of the Project. In addition, a detailed water management system will be developed to assure responsible use of water to support the operations without impacting communities and households in the vicinity of the mine.

A wildlife survey was conducted to evaluate the different species present in the environmental surroundings of the proposed Project. A total of 94 species of fauna were described according to their taxonomic group. None of the wildlife species observed or otherwise noted to be present in the area during the survey is designated as threatened, vulnerable or at risk.

The vegetation of the area is classified as an evergreen Tropical Forest (Annex IV.29 Classification of the Rzedowski vegetation) with predominating species having humidity limitations (Rzedowski, 1978). The baseline sampling program identified a total of 68 species of vegetation pertaining to 31 Families. One species, Echinocactus platycanthus, was found in the primary tailings disposal area and is considered to be a threatened species.

The primary impact of the mining operation on the vegetation community of the area will be associated with disturbances in the tailings storage areas and the facilities area. Disturbed areas not occupied with permanent facilities (processing mill, shops, etc.) will be stabilized using native plant materials produced on site in a greenhouse facility. In addition, mine closure will consist of removing facilities not deemed necessary to support communities and the capping of the tailings storage facilities. A reforestation program will be initiated to re-establish the natural ecosystem in these reclaimed areas using native species promulgated in an on-sight greenhouse facility. Appropriate management consisting of weed control and fire protection will be established.

Soil materials will be removed from all areas to be disturbed during the construction period and stored in appropriate locations. Salvaged topsoil material will be used to achieve contemporaneous reclamation of disturbed sites not scheduled for future impact. In addition, the tailings storage facilities will be capped with a layer of soil and planted with vegetation, which will reduce movement of water into the tailings.

Waste rock generated during expansion of the underground mine and/or currently stored on site will be used to fill old mine workings constructed during previous operations or new workings as mining progresses. The chemical composition of the waste rock is not expected to cause significant water quality issues in the mine or in adjacent groundwater.

The cumulative impact evaluation for the Project indicated that no other projects exist in the area that will contribute to impacts of air quality and water resources. As the Project progresses, the situation will be monitored to assess whether additional projects are discovered or initiated in the area. If other impacts are found, an appropriate cumulative impact evaluation will be developed.

An environmental management plan will be developed that includes the major components including: water management, tailings management, waste rock management, soil management, revegetation and reforestation, waste and sewage management, and air quality. In addition, a detailed monitoring program has been outlined for all components of the ecosystem.

A reclamation and closure plan has been outlined that provides a reasonable approach for the final reclamation and closure of the site.

Social Aspects

The development of the San Jose Project is achieving a positive impact on the local community. Community relations are being developed to promote communication and participation with community leaders, authorities and inhabitants. The Project supports social development for local inhabitants, avoiding migration of the local population to large metropolitan areas. The major social objectives of the San Jose Project are to use the available manpower of the region, to create a relatively large number of stable jobs and to improve the quality of life of the population. Also, the Project is expected to promote environmental stewardship, while establishing agreements at the community level to develop activities to improve soil protection, and the construction of a dam to retain runoff water for use in agriculture.

The planning, implementation, coordination and pursuit of the community policies are the responsibility of the Company's Community Relations Department. The objectives of the Company Community Relations Policy are: (1) To develop and to implement mechanisms, procedures, plans and strategies that respect the dynamics of local communities with consideration for the norms and laws; (2) To generate dialog and interaction with the communities, that allow their participation in the decisions that impacted the community; (3) To work with the local communities to maximize the development of cultural and education programs that maximize the opportunities for their development; and (4) To communicate with the local communities with regard to potential impacts of the operation on the environment. Discussions will identify the potential environmental effects, positive and negative, of the San Jose Project and the activities of the company in the different stages of development. The procedures for mitigating potential impacts will be provided along with procedures for monitoring the status of mitigation.

Estimated Capital Cost

The capital cost estimate for the San José Project at a production rate of 750 tonnes per day (t/d) is US$ 55.71 million based on costs compiled in the fourth quarter of 2009. The exchange rate used for conversion from Mexican Pesos to United States dollars was 13 $MXN = US$1.00.

The capital cost summary is presented in Table 1-11 and reflects a level of accuracy of plus or minus 25 percent.

Table 1-11
Capital Cost Summary

Area	Estimate (US$ x 1,000)	Contingency (%)	Contingency (US$ x 1,000)	Total with Contingency (US$ x 1,000)
Mine Preparation and Development	9,914	20%	1,983	11,896

Concentrator	16,664	15%	2,500	19,164
Auxiliaries	4,002	15%	600	4,602
Tailings Pond	3,224	15%	484	3,707
Wastewater Treatment Plant (Ocotlán de Morelos)	698	5%	35	733
Pipeline from Ocotlán de Morelos to San José	1,307	5%	65	1,373
Water Treatment Plant at San Jose	664	5%	33	697
Substation115 KV – CFE	1,458	5%	73	1,530
Substation 5.0 MVA	1,011	5%	51	1,062
Freight	239	20%	48	287
Engineering, Design and Project Management	2,732	3%	82	2,814
Construction Management	2,326	3%	70	2,396
Travel for Equipment Inspections and Miscellaneous Activities	56	3%	2	58
CMC Supervision	2,466	3%	74	2,540
Community Activities & Other	1,350			1,350
Misc. Owner Costs	1,500			1,500
Total Capital Cost	49,611		6,098	55,710

1,000 tpd CASE

CMC has provided the following estimate of additional capital required to increase the ore and process plant production rates from 750 to 1,000 tonnes per day in year 3 of operation:

- Mine US$27.018 million
- Process Plant US$2.508 million
- Other US$2.350 million

Total US$31.876 million

This increase would result in a Total Capital Cost of US$87.59 million.

1,500 tpd CASE

CMC has provided the following estimate of additional capital required to increase the ore and process plant production rates from 1,000 to 1,500 tonnes per day in year 6 of operation:

- Mine US$ 7.122 million
- Process Plant US$ 7.020 million
- Auxiliaries US$1.000 million
- Tailings Facility US$7.044 million
- EPCM US$1.193 million
- CMC Supervision US$0.442 million
- Other US$4.350 million

Total US$28.170 million

This increase would result in a Total Capital Cost of US$115.76 million.

Estimated Operating Cost

The overall operating costs are summarized in Table 1-12 and are based on a total of 3.516 million tonnes of ore milled over the mine life with an average of 22,500 tonnes per month or 750 tonnes per day. Table 1-12 also shows the proposed operating costs for the expansions to 1,000 tpd with an average of 30,000 tonnes-per-month then to 1,500 tpd with an average of 45,000 tonnes per month.

Table 1-12
Overall Estimated Operating Cost

Area	No. of Personnel (750 tpd)	US$ per Month (750 tpd)	US$ per Tonne Milled (750 tpd)	US$ per Tonne Milled (1,000 tpd)	US$ per Tonne Milled (1,500 tpd)
Geology and Exploration	12	31,102	1.382	1.04	0.69
Mine	199	571,950	25.42	22.89	19.82
Plant	74	320,850	14.26	12.00	9.41
Security and Environment	12	24,376	1.083	0.813	0.542
Community Relations	7	20,671	0.919	0.689	0.459
Administration and Finance	23	116,356	5.171	3.879	2.586
General Management	4	33,667	1.496	1.122	0.748
Property and Concessions	-	376	0.017	0.013	0.009
Totals	**331**	**1,119,330**	**49.743**	**42.44**	**34.26**

Financial Analysis

Based on the total of 3.516 million tonnes contained in the mineable Probable Reserves, a project life of approximately nine years is proposed. The estimates of metal production, capital costs and operating costs are combined in the discounted cash flow

evaluation. The economic evaluation is treated on a project basis using a silver price of US$15.12 per troy ounce and a gold price of US$897.51 per troy ounce. All applicable mineral extraction taxes have been allowed for in the cash flow analysis.

The results of the cash flow evaluation are summarized in Table 1-13 showing life-of-mine totals.

Table 1-13
Economic Evaluation Summary

Item	Units	Value
Payable Silver	Ounces (Millions)	19.40
Payable Gold	Ounces (Thousands)	155.13
Free Cash Flow (After-tax)	US$ (Millions)	95.1
Pre-tax NPV @8%	US$ (Millions)	46.0
After-tax NPV@8%	US$ (Millions)	36.3
Pre-tax IRR	%	19.5%
After-tax IRR	%	17.8%

It should be noted that the Financial Analysis is performed utilizing only Indicated Mineral Resources, which have been converted to Probable Reserves; however, Inferred Resources such as those indicated in Table 1-14, which are not in the model, can potentially have an impact on the Project economics and the life of the mine.

Table 1-14
Inferred Mineral Resources at Various Cutoffs

AgEq Cutoff (g/t)	Tonnes (x 1000)	AgEq (g/t)	Ag (g/t)	Au (g/t)	Contained Metal		
					AgEq oz (x 1000)	Ag oz (x 1000)	Au oz (x 1000)
50	4,020	272	181	1.48	35,199	23,389	192
75	3,497	304	202	1.65	34,151	22,735	185
100	3,074	334	222	1.80	32,963	21,988	178
125	2,681	366	244	1.97	31,545	21,061	170
150	2,411	392	262	2.11	30,357	20,293	164
175	2,137	421	282	2.26	28,922	19,351	155
200	1,883	452	304	2.41	27,393	18,379	146
225	1,696	479	321	2.56	26,113	17,522	140
250	1,545	503	337	2.69	24,958	16,747	133

A series of sensitivity analyses were undertaken to determine which parameters most effected the NPV and IRR of the Project on an after tax basis.

Figure 1-1 reflects the effects on After-tax NPV@8 percent while varying combined gold and silver prices and Figure 1-2 reflects the effects while varying the gold and silver prices independently.

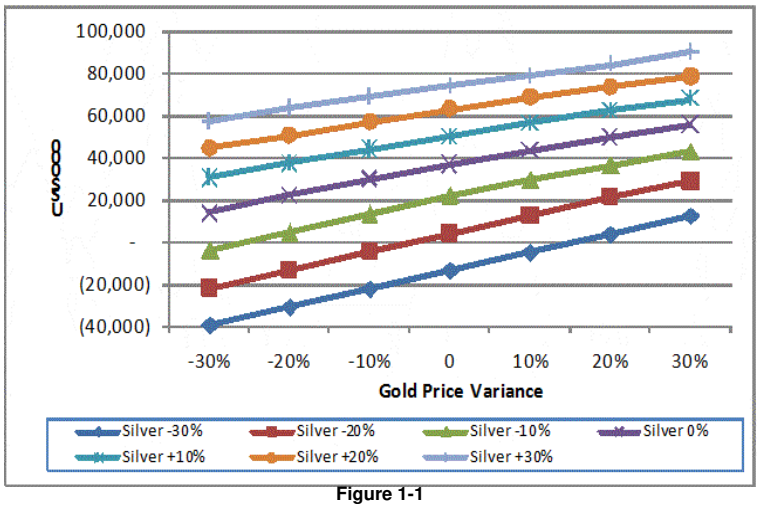


Figure 1-1
Sensitivity of After-tax NPV@8% to Gold and Silver Price (Combined)

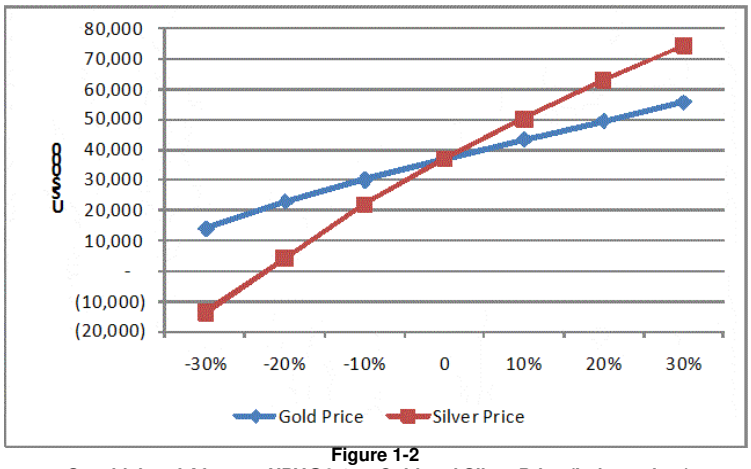


Figure 1-2
Sensitivity of After-tax NPV@8% to Gold and Silver Price (Independent)

On a total Project basis the internal rate of return (IRR) is 19.5 percent before tax and 17.8 percent after taxes.

Figure 1-3 reflects the effects on IRR while varying combined gold and silver prices and Figure 1-4 reflects the effects while varying the gold and silver prices independently.

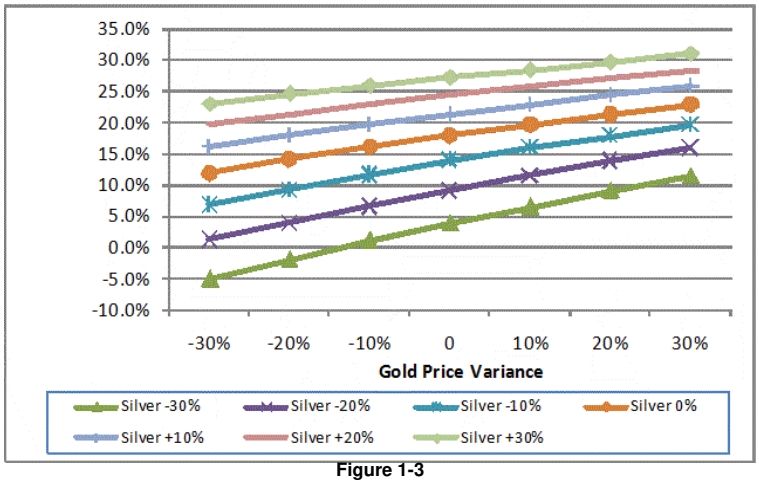


Figure 1-3
Sensitivity of IRR to Gold and Silver Price (Combined)

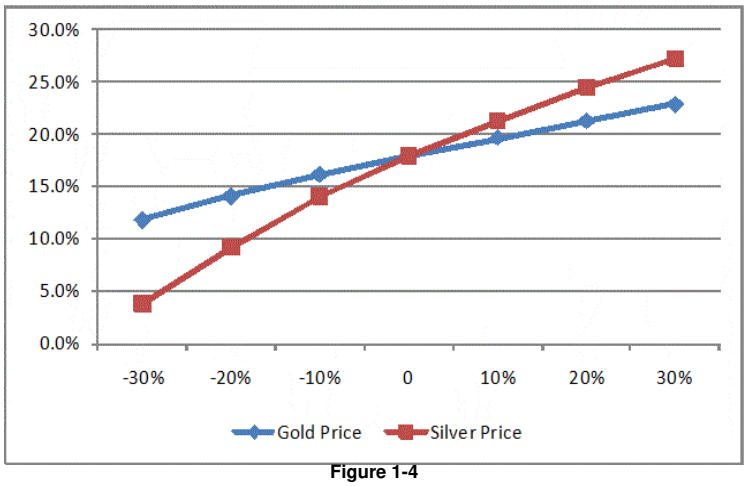


Figure 1-4
Sensitivity of IRR to Gold and Silver Price (Independent)

DIVIDENDS

The Company has not paid any dividends on its common shares nor does it intend to pay any dividends on its shares in the immediate future as management anticipates that all available funds will be invested to finance further acquisition, exploration and

development of its mineral properties.

DESCRIPTION OF CAPITAL STRUCTURE

The Company's authorized share capital is an unlimited number of common shares without par value. All common shares of the Company rank equally as to dividends, voting powers and participation in assets and in all other respects.

Voting. The holders of common shares are entitled to receive notice of, attend and vote at any meeting of the shareholders of the Company. Each common share carries one vote per share.

Dividends. The holders of common shares are entitled to receive on a pro-rate basis such dividends as the Board of Directors from time to time may declare, out of funds legally available therefor.

Rights on Dissolution. In the event of a liquidation, winding-up or dissolution of the Company, whether voluntary or involuntary or for the purpose of a reorganization or otherwise or upon any distribution of capital, the holders of the common shares have the right to receive on a pro-rata basis all of the assets of the Company remaining after payment of all of the Company's liabilities.

Pre-emptive, Conversion and Other Rights. No pre-emptive, redemption, sinking fund or conversion rights are attached to the common shares, and the common shares, when fully paid, will not be liable to further call or assessment. No other class of shares may be created without the approval of the holders of the common shares.

MARKET FOR SECURITIES

The Company's common shares were listed and posted for trading on the TSX Venture Exchange ("TSXV") until January 18, 2010 when the Company graduated to the Toronto Stock Exchange ("TSX"). On September 19, 2011, the Company's common shares were listed and posted for trading on the New York Stock Exchange ("NYSE"). The Company's shares currently trade on the NYSE under the symbol "FSM", on the TSX under the symbol "FVI", on the Lima Stock Exchange in Peru under the symbol "FVI", and on the Frankfurt Open Market, the unofficial market organized by Deutsche Börse in Germany, under the symbol "F4S".

Trading Prices and Volume

The following table provides the high and low prices and volume for the Company's shares as traded on the TSX during the fiscal year ended December 31, 2011:

Period	High ($)	Low ($)	Volume
December 2011	7.00	5.11	17,950,675
November 2011	7.03	5.90	9,810,385
October 2011	6.58	4.42	8,688,754
September 2011	7.22	5.14	15,148,409
August 2011	6.18	4.85	11,279,279
July 2011	6.19	5.01	7,565,828
June 2011	5.23	4.41	17,474,524
May 2011	5.35	4.48	18,290,480
April 2011	6.81	5.02	22,434,841
March 2011	5.98	4.35	21,124,155
February 2011	5.11	4.00	10,194,461
January 2011	4.76	3.54	12,911,653

DIRECTORS AND EXECUTIVE OFFICERS

Name, Occupation and Shareholding

The Board of Directors presently consists of seven directors. Each director will hold office until the next annual general meeting of the Company or until his successor is elected or appointed, unless his office is earlier vacated in accordance with the Articles of the Company, or with the provisions of the British Columbia *Business Corporations Act*.

The following are the full name, place of residence, position with the Company, and principal occupation within the preceding five years of each of the directors and executive officers of the Company:

Name, Position and Residency [(1)]	Principal Occupation or Employment [(1)]	Period as a Director of the Company

JORGE GANOZA DURANT President, Chief Executive Officer & Director Lima, Peru	President & CEO of the Company.	December 2, 2004 to present
SIMON RIDGWAY Chairman and Director British Columbia, Canada	Chairman of the Company, March 2006 to present; President & CEO of Radius Gold Inc. (mineral exploration), over five years.	January 25, 2005 to present
MICHAEL IVERSON [(3) (4)] Director British Columbia, Canada	Chairman & CEO of Niogold Mining Corporation (mineral exploration); President of Triple K Ventures Inc. (private management).	March 30, 1998 to present
TOMAS GUERRERO [(2) (3)] Director Lima, Peru	President of BO Consulting SA (geological engineering).	July 15, 2005 to present
MARIO SZOTLENDER [(3) (4)] Director Caracas, Venezuela	Independent Consultant and Director of several public mineral exploration companies; President of Rusoro Mining Ltd. (mineral exploration), November 2006 to August 2007.	June 16, 2008 to present
ROBERT GILMORE [(2) (4)] Director Colorado, USA	Independent Certified Public Accountant; Independent Financial Consultant, over five years; Director of Eldorado Gold Corporation (mining), over five years; Chief Financial Officer of NextAction Corporation (technology-based market), May 2006 to February 2008; Director of Layne Christensen Company (drilling, water treatment & construction services and products, and natural gas producer), January 2009 to present; Director of Great Western Minerals Group, Ltd., March 2012 to present.	June 23, 2010 to present
THOMAS KELLY [(2)] Director Lima, Peru	Mining Engineer; CEO of Apurimac Ferrum (mineral exploration), 2011 to present; COO of Inca Pacific Resources, Inc. (mineral exploration), 2008 to 2010; Managing Director of AITCO BOL SRL (mineral exploration), 2005 to 2007.	April 11, 2011 to present
LUIS GANOZA DURANT Chief Financial Officer Lima, Peru	Chief Financial Officer of the Company.	N/A
MANUEL RUIZ-CONEJO Vice-President, Operations Lima, Peru	Vice-President, Operations of the Company, August 2011 to present; formerly Vice-President, Project Development, July 2009 to August 2011, and Vice-President, Business Development of the Company, February 2008 to July 2009; Chief Operating Officer of Minera Atacocha SA (mining), March 2005 to December 2007.	N/A
THOMAS VEHRS Vice-President, Exploration Colorado, USA	Vice-President, Exploration of the Company.	N/A
CESAR PERA Vice-President, Human Resources Lima, Peru	Vice-President, Human Resources of the Company, August 2010 to present; Partner, Hrlatam (human resources), January 2009 to July 2010; Vice-President, Administration and Human Resources, Pacifico Grupo Asegurador (insurance), September 2006 to December 2008.	N/A

Notes:

(1) The information as to country of residence, principal occupation, and shares held is not within the knowledge of the management of the Company and has been furnished by the respective nominees.
(2) Member of the Audit Committee of the Company.
(3) Member of the Compensation Committee of the Company.
(4) Member of the Corporate Governance and Nominating Committee of the Company.

As at the date hereof, the directors and executive officers of the Company beneficially own, directly or indirectly, or have control or

direction over, an aggregate of 797,260 common shares of the Company, representing approximately 0.6% of the issued shares of the Company.

Cease Trade Orders or Bankruptcies

As at the date of the AIF and during the 10 years prior to the date of the AIF, none of the directors or officers of the Company or a shareholder holding a sufficient number of securities of the Company to affect materially the control of the Company:

(a) is or has been a director or executive officer of any company (including the Company), that while that person was acting in that capacity:

(i) was the subject of a cease trade order or similar order or an order that denied the relevant company access to any exemption under securities legislation, for a period of more than 30 consecutive days, other than Simon Ridgway and Mario Szotlender who are directors of a company that was the subject of a cease trade order for a period of more than 30 consecutive days from each of the BC Securities Commission and the Alberta Securities Commission. The cease trade orders were issued as a result of that company's failure to file its annual financial statements within the prescribed deadline, and upon the company's filing of the outstanding documents, such orders were revoked. In addition, the United States Securities and Exchange Commission ("SEC") revoked this company's registration under Section 12(g) of the Securities Exchange Act of 1934 for failure to keep its filings with the SEC up-to-date. Upon receipt of the SEC's notice of proposed revocation, the company filed a settlement agreement with the SEC consenting to the revocation as the company was dormant;

(ii) was subject to an event that resulted, after the director or executive officer ceased to be a director or executive officer, in the company being the subject of a cease trade or similar order or an order that denied the relevant company access to any exemption under securities legislation, for a period of more than 30 consecutive days; or

(iii) within a year of that person ceasing to act in that capacity, became bankrupt, made a proposal under any legislation relating to bankruptcy or insolvency or was subject to or instituted any proceedings, arrangement or compromise with creditors or had a receiver, receiver manager or trustee appointed to hold its assets; or

(b) has become bankrupt, made a proposal under any legislation relating to bankruptcy or insolvency, or become subject to or instituted any proceedings, arrangement or compromise with creditors, or had a receiver, receiver manager or trustee appointed to hold the assets of the director, officer and shareholder.

Penalties or Sanctions

As at the date of the AIF and during the 10 years prior to the date of the AIF, none of the directors or officers of the Company or a shareholder holding a sufficient number of securities of the Company to affect materially the control of the Company has been subject to:

(a) any penalties or sanctions imposed by a court relating to securities legislation or by a securities regulatory authority or has entered into a settlement agreement with a securities regulatory authority other than the settlement agreement described in paragraph (a)(i) under "Cease Trade Orders or Bankruptcies" above; or

(b) any other penalties or sanctions imposed by a court or regulatory body that would likely be considered important to a reasonable investor making an investment decision.

Conflicts of Interest

There are no existing or potential material conflicts of interest between the Company or any of its subsidiaries and a director or officer of the Company or any subsidiary.

AUDIT COMMITTEE

Pursuant to the provisions of Multilateral Instrument 52-110 (the "Instrument"), the Company's Audit Committee has adopted a written charter (the "Charter") that sets out its mandate and responsibilities. The Charter is attached hereto as Schedule "A".

The Audit Committee is presently comprised of Robert Gilmore, Tomas Guerrero and Thomas Kelly. All members of the Committee are "independent" and "financially literate", within the meanings given to those terms in the Instrument.

The education and experience of each audit committee member that is relevant to the performance of his responsibilities as an audit committee member is as follows:

Audit Committee Member	**Education and Experience**

Robert Gilmore	Mr. Gilmore is a Certified Public Accountant and independent financial consultant with more than 30 years' experience working with resource companies. He is a graduate of the University of Denver with a Bachelor of Science degree in Business Administration, Accounting. He is Chairman of the Board and of the Audit Committee of Eldorado Gold Corporation, and is a director and Audit Committee Chairman of Layne Christensen Company. Mr. Gilmore has also served as Chairman of the Audit Committees of Global Med Technologies, MK Resources, Inc., Frontera Copper Corporation and Ram Power Corporation.
Tomas Guerrero	Mr. Guerrero is a geological engineer with over 30 years of mine geology and mineral exploration experience in Peru, Mexico, Bolivia, Venezuela, Chile, Argentina and Ecuador. Until 2001, Mr. Guerrero held a ten-year tenure as Director of Explorations for the Hochschild Group, a leading private Peruvian mining company with multiple mine operations. Under his leadership Hochschild discovered and put in production three mid size gold-silver mines. He is currently the principle of BO Consulting, an engineering consulting firm specializing in servicing the mining sector.
Thomas Kelly	Mr. Kelly has Bachelor and Masters Degrees in Mining Engineering from the Colorado School of Mines and is a Fellow of Aus.IMM and a Registered Member of SME. He has over 35 years of world-wide mineral industry experience including underground and open pit mining, project development, project management, corporate management and consulting services. Mr. Kelly has held senior positions with Freeport-McMoRan Copper & Gold Inc., AMEC Americas, Inca Pacific Resources Inc. and other recognized industry-leading companies. He is a recognized expert in project management/development and is fluent in Spanish.

At the time of each annual audit, the auditors of the Company obtain, as necessary, the pre-approval of the Audit Committee for any anticipated additional services required of the auditors for the coming fiscal year. If other service requirements arise during the year, the Audit Committee will pre-approve such services at that time, prior to the commencement of such services.

During the Company's most recently completed fiscal year, the Company's auditors performed certain non-audit services. Fees charged by the auditors during the last two fiscal years are as follows:

	2011	**2010**
Audit Fees	$310,450	$138,900
Audit-Related Fees	$ 64,200	$ 76,700
Tax Fees (tax return preparation)	$ 98,665	$ 69,400
All Other Fees (services other than reported above)	$ 15,000	$ 52,100
	$488,315	$337,100

LEGAL PROCEEDINGS

There are no known legal proceedings involving an amount exceeding 10% of the current assets of the Company to which the Company is a party or which any of its properties is the subject during the most recently completed financial year, or any such proceedings known to the Company to be contemplated.

TRANSFER AGENT AND REGISTRAR

The Company's transfer agent and registrar is Olympia Trust Company, at its offices in Vancouver, BC and Toronto, ON.

MATERIAL CONTRACTS

There are no contracts, other than those herein disclosed in this AIF and other than those entered into in the ordinary course of the Company's business, that are material to the Company and that were entered into during the most recently completed fiscal year ended December 31, 2011 or before the most recently completed financial year, but are still in effect as of the date of this AIF.

INTERESTS OF EXPERTS

Names of Experts

Richard L. Nielsen, PhD., Steve Milne, P.E. and Robert L. Sandefur, P.E. of Chlumsky, Armbrust and Meyer, LLC, each an independent Qualified Person as defined by NI 43-101, prepared the Caylloma Report referred to in this document.

Craig S. Bow, PhD, Gregory Chlumsky, QP-MSSA and Steve L. Milne, PE of Chlumsky, Armbrust and Meyer, LLC, each an independent Qualified Person as defined by NI 43-101, prepared the San Jose Pre-Feasibility Report referred to in this document.

Eric Chapman and Edgard Vilela prepared and/or supervised the updated Mineral Resource and/or Mineral Reserve estimates for

the Caylloma Mine and the San Jose Mine described in this document. Thomas Vehrs is responsible for ensuring that the information contained in this document regarding the updated Mineral Resource and Mineral Reserve estimates is an accurate summary of the original reports and data provided to or developed by the Company. Messrs. Chapman, Vilela and Vehrs are employees of the Company and are Qualified Persons as defined by the National Instrument 43-101.

Interests of Experts

To the knowledge of the Company, the experts named above did not have any registered or beneficial interest, direct or indirect, in any securities or other property of the Company when the experts prepared their respective reports, other than Thomas Vehrs who currently holds 425,000 shares and 252,189 options in the Company, and Eric Chapman who currently holds 16,542 options in the Company.

ADDITIONAL INFORMATION

Additional information relating to the Company is available for viewing atwww.sedar.com. Information regarding directors' and officers' remuneration and indebtedness, principal holders of the Company's securities and securities authorized for issuance under equity compensation plans, if applicable, is contained in the Company's Information Circular pertaining to its Annual General Meeting held on May 26, 2011. Additional financial information is provided in the Company's audited financial statements for the fiscal year ended December 31, 2011 and the management's discussion and analysis thereon.

SCHEDULE "A"

FORTUNA SILVER MINES INC.
(the "Company")

AUDIT COMMITTEE CHARTER

PURPOSE

The primary function of the Audit Committee is to assist the Board of Directors of the Company (the 'Board") in fulfilling its oversight responsibilities by reviewing the financial information to be provided to the shareholders and others, the systems of internal controls and management information systems established by the senior officers of the Company ("Management") and the Company's internal and external audit process and monitoring compliance with the Company's legal and regulatory requirements with respect to its financial statements.

The Audit Committee is accountable to the Board. In the course of fulfilling its specific responsibilities hereunder, the Audit Committee is expected to maintain an open communication between the Company's external auditors and the Board.

The Audit Committee does not plan or perform audits or warrant the accuracy or completeness of the Company's financial statements or financial disclosure or compliance with generally accepted accounting procedures as these are the responsibility of Management.

RESPONSIBILITIES

Subject to the powers and duties of the Board, the Board hereby delegates to the Audit Committee the following powers and duties to be performed by the Audit Committee on behalf of and for the Board. Nothing in this Charter is intended to or does confer on any member a higher standard of care or diligence than that which applies to the directors as a whole.

External Auditors

The Audit Committee has primary responsibility for the selection, appointment, dismissal, compensation and oversight of the external auditors, subject to the overall approval of the Board. For this purpose, the Audit Committee may consult with Management.

The external auditors shall report directly to the Audit Committee.

Also, the Audit Committee:

a. recommends to the Board:

   i. whether the current external auditors should be nominated for reappointment for the ensuing year and if applicable, select and recommend a suitable alternative for nomination; and

   ii. the amount of compensation payable to the external auditors;

b. resolves disagreements, if any, between Management and the external auditors regarding financial reporting;

c. provides the Board with such recommendations and reports with respect to the financial statements of the Company as it deems advisable;

d. takes reasonable steps to confirm the independence of the external auditors, including but not limited to pre-approving any non-audit related services provided by the external auditors to the Company or the Company's subsidiaries, if any;

e. confirms that the external auditors are a 'participating audit' firm for the purpose of National Instrument 52-108 *Auditor Oversight* and are in compliance with governing regulations;

f. reviews the plan and scope of the audit to be conducted by the external auditors of the Company;

g. reviews and evaluates the performance of the external auditors; and

h. reviews and approves the Company's hiring policy regarding partners, employees and former partners and employees of the Company's present and former external auditors.

Audit and Review Process and Results

The Audit Committee has a duty to receive, review and make any inquiry regarding the completeness, accuracy and presentation of the Company's financial statements to ensure that the financial statements fairly present the financial position and risks of the organization and that they are prepared in accordance with generally accepted accounting principles. To accomplish this, the Audit Committee:

a. considers the scope and general extent of the external auditors' review, including their engagement letter and major changes

to the Company's auditing and accounting principles and practices;

b. consults with management regarding the sufficiency of the Company's internal system of audit and financial controls, internal audit procedures and results of such audits;

c. ensures the external auditors have full, unrestricted access to required information and have the cooperation of management;

d. reviews with the external auditors the audit process and standards, as well as regulatory or Company-initiated changes in accounting practices and policies and the financial impact thereof, and selection or application of appropriate accounting principles;

e. reviews with the external auditors and, if necessary, legal counsel, any litigation, claim or contingency, including tax assessments, that could have a material effect upon the financial position of the Company and the manner in which these matters are being disclosed in the financial statements;

f. reviews the appropriateness and disclosure of any off-balance sheet matters;

g. reviews disclosure of related-party transactions;

h. receives and reviews with the external auditors, the external auditors' audit report and the audited financial statements;

i. makes recommendations to the Board respecting approval of the audited financial statements;

j. meets with the external auditors separately from management to review the integrity of the Company's financial reporting, including the clarity of financial disclosure and the degree of conservatism or aggressiveness of the accounting policies and estimates, any significant disagreements or difficulties in obtaining information, adequacy of internal controls over financial reporting, adequacy of disclosure controls and procedures, and the degree of compliance by the Company with prior recommendations of the external auditors;

k. directs management to implement such changes as the Audit Committee considers appropriate, subject to any required approvals of the Board arising out of the review; and

l. meets at least annually with the external auditors, independent of management, and reports to the Board on such meetings.

Interim Financial Statements

The Audit Committee:

a. reviews and determines the Company's practice with respect to review of interim financial statements by the external auditors;

b. conducts all such reviews and discussions with the external auditors and Management as it deems appropriate; and

c. makes recommendations to the Board respecting approval of the interim financial statements.

Involvement with Management

The Audit Committee has primary responsibility for overseeing the actions of management in all aspects of financial management and reporting. The Audit Committee:

a. reviews the Company's annual and interim financial statements, Management's Discussion and Analysis and earnings press releases, if any, before the Company publicly discloses this information;

b. reviews all of the Company's public disclosure of financial information extracted from the Company's financial statements, if such financial statements have not previously been reviewed by the Committee, prior to such information being made public by the Company and for such purpose, the CFO assumes responsibility for providing the information to the Audit Committee for its review;

c. reviews material financial risks with Management, the plan that Management has implemented to monitor and deal with such risks and the success of Management in following the plan;

d. consults annually and otherwise as required with the Company's CEO and CFO respecting the adequacy of the internal controls over financial reporting and disclosure controls and procedures and reviews any breaches or deficiencies;

e. obtains such certifications of annual and interim filings by the CEO and CFO attesting to internal controls over financial reporting and disclosure controls and procedures as deemed advisable;

f. reviews Management's response to significant written reports and recommendations issued by the external auditors and the extent to which such recommendations have been implemented by Management;

g. reviews with Management the Company's compliance with applicable laws and regulations respecting financial reporting

matters, and any proposed regulatory changes and their impact on the Company; and

h. reviews as required with Management and approves disclosure of the Audit Committee Charter, and Audit Committee disclosure required in the Company's Annual Information Form, Information Circular and on the Company's website.

PROCEDURAL MATTERS

The Audit Committee:

a. invites the Company's external auditors, the CFO, and such other persons as deemed appropriate by the Audit Committee to attend meetings of the Audit Committee;

b. reports material decisions and actions of the Audit Committee to the Board, together with such recommendations as the Committee may deem appropriate;

c. has the power to conduct or authorize investigations into any matter within the scope of its responsibilities;

d. has the right to engage independent counsel and other advisors as it determines necessary to carry out its duties and the right to set the compensation for any advisors employed by the Audit Committee;

e. has the right to communicate directly with the CFO and other members of Management who have responsibility for the internal and external audit process, as well as to communicate directly with the internal and external auditors; and

f. pre-approves non-audit services to be performed by the external auditors.

COMPOSITION

The Audit Committee is composed of a minimum of three directors, all of whom meet the independence and experience requirements and have relevant skills and/or experience in the Audit Committee's areas of responsibility as required by the securities laws applicable to the Company, including those of any stock exchange on which the Company's securities are traded.

Appointment of Committee Members and Vacancies

Members of the Audit Committee are appointed or confirmed by the Board annually and hold office at the pleasure of the Board. The Board fills any vacancy on, or any additional members to, the Audit Committee.

Committee Chair

The Board appoints a Chair for the Audit Committee.

STRUCTURE AND OPERATIONS

Meetings

The Chair of the Audit Committee or the Chair of the Board or any two of its members may call a meeting of the Audit Committee. The Audit Committee meets at least four times each fiscal year, and at such other times during each year as it deems appropriate.

Quorum

A majority of the members appointed to the Audit Committee constitutes a quorum.

Notice of Meetings

The Chair of the Audit Committee arranges to provide notice of the time and place of every meeting in writing (including by facsimile) to each member of the Audit Committee at least two (2) business days prior to the time fixed for such meeting, provided, however, that a member may in any manner waive a notice of a meeting. Attendance of a member at a meeting constitutes a waiver of notice of the meeting, except where a member attends a meeting for the express purpose of objecting to the transaction of any business on the grounds that the meeting is not lawfully called. The Chair also ensures that an agenda for the meeting and all required materials for review by the members of the Audit Committee are delivered to the members with sufficient time for their review, or that such requirement is waived.

Absence of Committee Chair

If the Chair of the Audit Committee is not present at any meeting of the Audit Committee, the other members of the Audit Committee will be chose a Chair to preside at the meeting.

Secretary of Committee

At each meeting the Audit Committee appoints a secretary who need not be a director of the Company.

Attendance of the Company's Officers at Meetings

The Chair of the Audit Committee or any two members of the Audit Committee may invite one or more officers of the Company to attend any meeting of the Audit Committee.

Delegation

The Audit Committee may, in its discretion and where permitted by National Instrument 52-110 – Audit Committees, delegate all or a portion of its duties and responsibilities to a subcommittee, management or, to the extent otherwise permitted by applicable plans, laws or regulations, to any other body or individual.

Procedure and Records

Subject to any statute or constating documents of the Company, the Audit Committee determines its own procedures at meetings and may conduct meetings by telephone and keeps records of its proceedings.

COMPLAINTS

The Audit Committee has established a Whistle Blower Policy which sets out the procedures for:

a. the receipt, retention and treatment of complaints received by the Company regarding accounting, internal accounting controls, or auditing matters; and

b. the confidential, anonymous submission to the Company of concerns regarding questionable accounting or auditing matters.

The Audit Committee reviews the Whistle Blower Policy annually.

REPORTING AND ASSESSMENT

The Audit Committee reports to the Board of Directors, and on an annual basis, presents to the Board a Committee Annual Report consisting of the Audit Committee's review of its charter, the Committee's and its Chair's performance over the past year, and any recommendations the Audit Committee makes in respect thereto.

EFFECTIVE DATE

This Charter was implemented by the Board on August 10, 2011.



Fortuna Silver Mines Inc.

Years ended December 31, 2011 and 2010

Consolidated Financial Statements

March 23, 2012

(All amounts in US$'000's unless otherwise stated)

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2800 - 1055 Dunsmuir Street
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Vancouver BC V7X 1P4
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Report of Independent Registered Chartered Accountants

To the Board of Directors and Shareholders of Fortuna Silver Mines Inc.

We have audited the accompanying consolidated financial statements of Fortuna Silver Mines Inc. and subsidiaries, which comprise the consolidated statements of financial position as at December 31, 2011, December 31, 2010 and January 1, 2010, and the consolidated statements of income, statements of comprehensive income, statements of changes in equity, and statements of cash flows for the years ended December 31, 2011 and December 31, 2010, and 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 as issued by the International Accounting Standards Board, 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 and the standards of the Public Company Accounting Oversight Board (United States). 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 Fortuna Silver Mines Inc. and subsidiaries as at December 31, 2011, December 31, 2010 and January 1, 2010 and their financial performance and cash flows for the years ended December 31, 2011 and December 31, 2010 in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board.

(Signed) Deloitte & Touche LLP

Independent Registered Chartered Accountants
March 23, 2012
Vancouver, Canada

FORTUNA SILVER MINES INC.
CONSOLIDATED STATEMENTS OF INCOME
FOR THE YEARS ENDED DECEMBER 31,
(Expressed in thousands of US Dollars, except for share and per share amounts)

	Notes	2011	2010 23 h)
Sales	18	$ 110,104	$ 74,056
Cost of sales	21	49,030	34,844
Mine operating income		60,974	39,212
Other expenses			
Selling, general and administrative expenses	10a)b),21	19,840	10,984
Exploration and evaluation costs	21	1,715	547
Net gain on commodity contracts		(481)	(736)
(Gain) loss on disposal of mineral properties, property, plant and equipment		(59)	127
Loss on disposal of investment		-	119
Write-off of deferred exploration costs		-	443
Impairment of mineral properties, property, plant and equipment	8	1,894	-
Operating income		38,065	27,728
Finance Items			
Interest income		830	493
Interest expense		(560)	(708)
Net finance income (expense)	20	270	(215)
Income before tax		38,335	27,513
Income taxes	13	18,802	11,510
Income for the period		$ 19,533	$ 16,003
Earnings per Share -Basic	14 e)i	$ 0.16	$ 0.15
Earnings per Share - Diluted	14 e)ii	$ 0.16	$ 0.14
Weighted average number of shares outstanding - Basic	14 e)i	123,295,063	108,120,452
Weighted average number of shares outstanding - Diluted	14 e)ii	124,711,984	110,564,767
Expenses by Nature	21		

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

FORTUNA SILVER MINES INC.
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
FOR THE YEARS ENDED DECEMBER 31,
(Expressed in thousands of US Dollars)

	Notes	2011	2010 23 i)
Income for the year		**$ 19,533**	$ 16,003
Other comprehensive income			
Unrealized gain on translation of net investment		**751**	-
Unrealized (loss) gain on translation to presentation currency on foreign operations		**(79)**	2,723
Other comprehensive income		**672**	2,723
Total comprehensive income for the year		**$ 20,205**	$ 18,726

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

FORTUNA SILVER MINES INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31,
(Expressed in thousands of US Dollars)

	Notes	Years ended December 31, 2011	2010 23 i)
OPERATING ACTIVITIES			
Net income		**$ 19,533**	$ 16,003
Items not involving cash			
Depletion and depreciation		**9,421**	6,462
Accretion of provisions		**173**	163
Income tax expense		**18,802**	11,510
Share-based payments (recovery)		**3,682**	(501)
Unrealized (gain) on commodity contracts		**(116)**	(2,922)
Write-off of deferred exploration costs		**-**	443
Impairment of mineral properties, property, plant and equipment		**1,894**	-
(Gain) loss on disposal of mineral properties, property, plant and equipment		**(59)**	127
Accrued interest on long term loans receivable and payable		**24**	50
		53,354	31,335
Changes in non-cash working capital items			
Accounts receivable and other assets		**(3,085)**	(4,788)
Inventories		**(7,273)**	(1,536)
Trade and other payables		**6,829**	3,677
Due to/from related parties		**134**	(9)
Provisions		**(201)**	-
Cash provided by operating activities before interest and income taxes		**49,758**	28,679
income taxes paid		**(15,007)**	(7,301)
Interest income paid		**(80)**	(127)
Interest income received		**837**	462
Net cash provided by operating activities		**35,508**	21,713
INVESTING ACTIVITIES			
Purchase of short term investments		**(49,671)**	(47,675)
Redemptions in short term investments		**53,406**	33,817
Expenditures on mineral properties, property, plant and equipment		**(76,676)**	(36,711)
Payments of value added taxes on purchase of property, plant and equipment		**(522)**	(2,915)
Advances of deposits on long term assets		**(31,859)**	(4,661)
Receipts of deposits on long term assets		**35,424**	-
Proceeds on disposal of mineral properties, property, plant and equipment		**41**	81
Net cash used in investing activities		**(69,857)**	(58,064)
FINANCING ACTIVITIES			

Proceeds from long term debt			**18**		-
Repayment of long term debt			**(18)**		-
Net proceeds on issuance of common shares			**3,656**		74,922
Repayment of finance lease obligations			**(1,178)**		(1,187)
Net cash provided by financing activities			**2,478**		73,735
Effect of exchange rate changes on cash and cash equivalents			**303**		2,151
(DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS			**(31,871)**		37,384
Cash and cash equivalents - beginning of year	**3**		**70,298**		30,763
CASH AND CASH EQUIVALENTS - END OF YEAR	**3**	**$**	**38,730**	$	70,298
Supplemental cash flow information	**15**				

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

FORTUNA SILVER MINES INC.
CONSOLIDATED STATEMENTS OF FINANCIAL POSITION
(Expressed in thousands of US Dollars)

	Notes		December 31, 2011		December 31, 2010 23 g)		January 1, 2010 23 g)
ASSETS							
CURRENT ASSETS							
Cash and cash equivalents	**3**	**$**	**38,730**	$	70,298	$	30,763
Short term investments	**4**		**17,000**		20,509		6,034
Derivative assets	**5**		**70**		-		37
Accounts receivable and other assets	**6**		**15,609**		13,454		8,635
GST/HST and value added tax receivable	**6**		**4,777**		3,542		601
Inventories	**7**		**11,291**		4,018		2,328
			87,477		111,821		48,398
NON-CURRENT ASSETS							
Deposits on long-term assets	**6**		**2,260**		4,686		16
Deferred income tax assets	**13 b)**		**36**		-		-
Mineral properties, property, plant and equipment	**8**		**181,833**		117,363		85,175
Total assets		**$**	**271,606**	$	233,870	$	133,589
LIABILITIES AND EQUITY							
CURRENT LIABILITIES							
Trade and other payables	**9**	**$**	**17,156**	$	9,303	$	5,136
Due to related parties	**10 c)**		**169**		40		49
Derivative liabilities	**5**		**87**		133		3,092
Provisions	**12**		**727**		-		-
Income tax payable	**13 a)**		**3,923**		4,192		2,949
Current portion of long term liability	**11**		**1,512**		1,083		1,038
			23,574		14,751		12,264
NON-CURRENT LIABILITIES							
Leases and long term liabilities	**11**		**2,764**		3,166		1,454
Provisions	**12**		**4,247**		4,881		2,917
Deferred income tax liabilities	**13 b)**		**12,710**		8,482		5,593
			43,295		31,280		22,228
EQUITY							
Share capital			**186,540**		180,403		104,701
Share option and warrant reserve			**10,495**		11,116		14,315
Retained earnings (deficit)			**27,881**		8,348		(7,655)
Accumulated other comprehensive income			**3,395**		2,723		-
			31,276		11,071		(7,655)
			228,311		202,590		111,361
		$	**271,606**	$	233,870	$	133,589
Contingencies and capital commitments	**19**						
Subsequent events	**22**						

APPROVED BY THE DIRECTORS:

"*Jorge Ganoza Durant*", Director — Jorge Ganoza Durant

"*Robert R. Gilmore*" , Director — Robert R. Gilmore

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

FORTUNA SILVER MINES INC.
CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY
FOR THE YEARS ENDED DECEMBER 31,
(Expressed in thousands of US Dollars, except for share amounts)

		Attributable to equity holders of the Company						
		Share Capital						
	Notes	Shares	Amount	Share Option and Warrant Reserve	Retained Earnings (Deficit)	Accumulated Other Comprehensive Income ("AOCI")	Total Retained Earnings (Deficit) and AOCI	Total Equity
Balance - December 31, 2010		122,497,465	$ 180,403	$ 11,116	$ 8,348	$ 2,723	$ 11,071	$ 202,590
Issuance of shares under bought deal financing, net of issuance costs		-	(95)	-	-	-	-	(95)
Exercise of options		2,441,700	3,751	-	-	-	-	3,751
Issuance of shares for property	**14 a)**	6,756	30	-	-	-	-	30
Transfer of contributed surplus on exercise of options		-	2,451	(2,451)	-	-	-	-
Share-based payments on option grants		-	-	1,830	-	-	-	1,830
Income for the year		-	-	-	19,533	-	19,533	19,533
Unrealized gain on translation of net investment		-	-	-	-	751	751	751
Unrealized (loss) on translation to presentation currency on foreign operations		-	-	-	-	(79)	(79)	(79)
Total comprehensive income for the year					19,533	672	20,205	20,205
Balance – December 31, 2011		**123,945,921**	**$ 186,540**	**$ 10,495**	**$ 27,881**	**$ 3,395**	**$ 31,276**	**$ 228,331**
Balance - December 31, 2009		94,982,652	$ 104,701	$ 14,315	$ (7,655)	$ -	$ (7,655)	$ 111,361
Issuance of shares under bought deal financing, net of issuance costs		26,507,500	73,919	-	-	-	-	73,919
Exercise of options		999,500	1,004	-	-	-	-	1,004
Issuance of shares for property	**14 a)**	7,813	20	-	-	-	-	20
Transfer of contributed surplus on exercise of options		-	759	(759)	-	-	-	-
Share-based payments (recoveries) on option grants		-	-	(2,440)	-	-	-	(2,440)
Income for the year		-	-	-	16,003	-	16,003	16,003
Unrealized gain on translation to presentation currency on foreign operations		-	-	-	-	2,723	2,723	2,723
Total comprehensive income for the year					16,003	2,723	18,726	18,726
Balance – December 31, 2010	**23 f)**	122,497,465	$ 180,403	$ 11,116	$ 8,348	$ 2,723	$ 11,071	$ 202,590

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

1. Corporate Information

Fortuna Silver Mines Inc. ("Fortuna" or the "Company") is engaged in silver mining and related activities, in Latin America, including exploration, extraction, and processing. The Company operates the Caylloma zinc/lead/silver mine in southern Peru and the San Jose silver/gold mine in Mexico.

Fortuna is a publicly traded company incorporated and domiciled in Canada and is listed on the New York Stock Exchange under the trading ticker symbol "FSM", and on the Toronto Stock Exchange and Lima Stock Exchange under the trading ticker symbol "FVI".

The Company's registered office is at Suite 650, 200 Burrard Street, Vancouver, British Columbia, Canada, V6C 3L6.

2. Basis of Consolidation and Summary of Significant Accounting Policies

a) Statement of Compliance

These consolidated financial statements have been prepared in accordance with the International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB"). The policies applied in these consolidated financial statements are based on IFRS issued and effective as at December 31, 2011. The Board of Directors approved these financial statements for issue on March 23, 2012.

b) Basis of Consolidation

These consolidated financial statements include the accounts of the Company and wholly owned subsidiaries: Minera Bateas S.A.C. ("Bateas"); Fortuna Silver (Barbados) Inc.; Compania Minera Cuzcatlan SA ("Cuzcatlan"); Continuum Resources Ltd. ("Continuum"); Fortuna Silver Mines Peru S.A.C. ("FSM Peru"); and Fortuna Silver Mexico, S.A. de CV. ("FS Mexico").

All significant inter-company transactions, balances, revenues, and expenses have been eliminated upon consolidation.

c) Revenue Recognition

Revenue arising from the sale of metal concentrates is recognized when title and the significant risks and rewards of ownership of the concentrates have been transferred to the buyer. The passing of title to the customer is based on the terms of the sales contract. Final commodity prices are set in a period subsequent to the date of sale based on a specified quotational period, either one or three months after delivery at the option of the customer or one month after delivery. The Company's metal concentrates are provisionally priced at the time of sale based on the prevailing market price.

Variations between the price recorded at the shipment date and the actual final price set under the sales contracts are caused by changes in market prices, and result in an embedded derivative in accounts receivable. The embedded derivative is recorded at fair value each period until final settlement occurs, with changes in fair value classified as provisional price adjustments and included in sales in the consolidated statement of income. Sales of metal concentrates are net of refining and treatment charges.

FORTUNA SILVER MINES INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010
(All amounts in US$'000's unless otherwise stated)

2. Basis of Consolidation and Summary of Significant Accounting Policies (continued)

d) Cash and Cash Equivalents

Cash and cash equivalents are designated as fair value through profit or loss ("FVTPL"). Cash and cash equivalents include cash on hand, demand deposits, and money market instruments, with maturities from the date of acquisition of 90 days or less, which are readily convertible to known amounts of cash and are subject to insignificant changes in value. Transaction costs are expensed when incurred through profit or loss.

e) Mineral Properties, Property, Plant and Equipment

Costs directly related to construction projects are capitalized to work-in-progress until the asset is available for use in the manner

intended by management. Completed property, plant and equipment are recorded at cost, net of accumulated depreciation and accumulated impairments. Assets, other than capital work in progress, will be depreciated to their residual values over their estimated useful lives as follows:

Land and buildings		
Land	Not depreciated	
Mineral properties	Units of production	
Buildings	6 - 20 years	Straight line
Leasehold improvements	7 - 8 years	Straight line
Plant and equipment		
Machinery and equipment	3 - 8 years	Straight line
Furniture and other equipment	3 - 13 years	Straight line
Transport units	4 - 5 years	Straight line
Capital work in progress	Not depreciated	

Equipment under finance lease is initially recorded at the present value of minimum lease payments at the inception of the lease and depreciated as above. Spare parts and components included in machinery and equipment, depending on the replacement period of the initial component, are depreciated over 8 to 18 months.

Borrowing costs allocable to the costs of construction projects are capitalized to mineral properties, property, plant and equipment and included in the carrying amounts of related assets until the asset is available for use in the manner intended by management.

Costs associated with commissioning activities on constructed plants are deferred from the date of mechanical completion of the facilities until the date the assets are ready for use in the manner intended by management.

On an annual basis, the depreciation method, useful economic life and the residual value of each component asset is reviewed, with any changes recognized prospectively over its remaining useful economic life.

2. Basis of Consolidation and Summary of Significant Accounting Policies (continued)

e) Mineral Properties, Property, Plant and Equipment (continued)

i. Evaluation and Exploration Assets

Significant payments related to the acquisition of land and mineral rights are capitalized as incurred. Prior to acquiring such land or mineral rights, the Company makes a preliminary evaluation to determine that the property has significant potential to develop an economic ore body. The time between initial acquisition and full evaluation of a property's potential is dependent on many factors including: location relative to existing infrastructure, the property's stage of development, geological controls and metal prices.

The Company defers the cost of acquiring, maintaining its interest, exploring and developing mineral properties as exploration and evaluation assets when future inflow of economic benefits from the properties is probable and until such time as the properties are placed into development, abandoned, sold or considered to be impaired in value.

If a mineable ore body is discovered, exploration and evaluation costs are reclassified to mining properties. If no mineable ore body is discovered, such costs are expensed in the period in which it is determined the property has no future economic value.

Proceeds received from the sale of interests in exploration and evaluation assets are credited to the carrying value of the mineral properties, with any excess included in income.

Write-downs due to impairment in value are charged to income. The cash-generating unit for assessing impairment is a geographic region and shall be no larger than the operating segment.

Exploration costs that do not relate to any specific property are expensed as incurred.

ii. Operational Mining Properties and Mine Development

For operating mines, all exploration within the mineral deposit is capitalized and amortized on a unit-of-production basis over proven and probable reserves as part of the production cost.

Costs of producing properties are amortized on a unit-of-production basis over proven and probable reserves, and costs of abandoned properties are written-off.

iii. Commercial Production

Capital work in progress consists of expenditures for the construction of future mines and include pre-production revenues and expenses prior to achieving commercial production. Commercial production is a convention for determining the point in time in which a mine and plant has completed the operational commissioning and has operational results that are expected to remain at a sustainable commercial level over a period of time, after which production costs are no longer capitalized and are reported as operating costs. The determination of when commercial production commences is based on several qualitative and quantitative factors including but not limited to the following:

2. Basis of Consolidation and Summary of Significant Accounting Policies (continued)

e) Mineral Properties, Property, Plant and Equipment (continued)

iii. Commercial Production (continued)

- all major capital expenditures to bring the mine to the condition necessary for it to be capable of operating in the manner intended by management have been completed;
- the mine or mill is operating within eighty percent of design capacity;
- metallurgical recoveries are achieved within eighty percent of projections; and,
- the ability to sustain ongoing production of ore at a steady or increasing level.

On the commencement of commercial production, depletion of each mining property will be provided on a unit-of-production basis. Any costs incurred after the commencement of production are capitalized to the extent they give rise to a future economic benefit.

f) Asset Impairment

Assets are assessed for impairment at each reporting date when changes in events or circumstances occur that indicate the assets may not be recoverable. An impairment loss is recognized for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less cost to sell and value in use. For the purposes of assessing impairment, assets are grouped at the lowest level for which there are separately identifiable cash inflows or cash generating units. These are typically individual mines or development projects. Brownfields exploration projects, located close to existing mine infrastructure, are assessed for impairment as part of the associated mine cash generating unit.

When the recoverable amount is assessed using pre-tax discounted cash flow techniques, the resulting estimates are based on detailed mine and/or production plans. For value in use, recent cost levels are considered, together with expected changes in costs that are compatible with the current condition of the business.

The cash flow forecasts are based on best estimates of expected future revenues and costs, including the future cash costs of production, capital expenditure and reclamation and closures costs.

Where a fair value less cost to sell model is used the cash flow forecast includes net cash flows expected to be realized from extraction, processing and sale of mineral resources that do not currently qualify for inclusion in proven or probable reserves.

Where an impairment loss subsequently reverses, the carrying amount of the asset or cash-generating unit is increased to the revised estimate of recoverable amount, but not beyond the carrying amount that would have been determined had no impairment loss been recognized for the asset or cash-generating unit in prior years. A reversal of an impairment loss is recognized into earnings immediately.

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2. Basis of Consolidation and Summary of Significant Accounting Policies (continued)

g) Provisions

i. Decommissioning and restoration provisions

Future obligations to retire an asset, including dismantling, remediation and ongoing treatment and monitoring of the site related to normal operations are initially recognized and recorded as a liability based on estimated future cash flows discounted at a credit adjusted risk-free rate. The decommissioning and restoration provision ("DRP") is adjusted at each reporting period for changes to factors including the expected amount of cash flows required to discharge the liability, the timing of such cash flows and the credit adjusted risk-free discount rate.

The liability is accreted to full value over time through periodic charges to income. This accretion of provisions is charged to finance costs in the consolidated statements of income.

The amount of the DRP initially recognized is capitalized as part of the related asset's carrying value and amortized to income. The method of amortization follows that of the underlying asset. The costs related to a DRP are only capitalized to the extent that the amount meets the definition of an asset and can bring about future economic benefit. For a closed site or where the asset which generated a DRP no longer exists, there is no longer future benefit related to the costs and as such, the amounts are expensed. For operating sites, a revision in estimates or a new disturbance will result in an adjustment to the liability with an offsetting adjustment to the capitalized retirement cost. For closed sites, adjustments to the DRP that are required as a result of changes in estimates are charged to income in the period in which the adjustment is identified.

ii. Environmental disturbance restoration provisions

During the operating life of an asset, events such as infractions of environmental laws or regulations may occur. These events are not related to the normal operation of the asset and are referred to as environmental disturbance restoration provisions ("EDRP"). The costs associated with an EDRP are accrued and charged to earnings in the period in which the event giving rise to the liability occurs. Any subsequent adjustments to an EDRP due to changes in estimates are also charged to earnings in the period of adjustment. These costs are not capitalized as part of the long-lived asset's carrying value.

iii. Other provisions

Provisions are recognized when a present legal or constructive obligation exists, as a result of past events, and it is probable that an outflow of resources that can be reliably estimated will be required to settle the obligation. Where the effect is material, the provision is discounted using an appropriate current market-based pre-tax discount rate.

2. Basis of Consolidation and Summary of Significant Accounting Policies (continued)

h) Inventories

Inventories include metals contained in concentrates, stockpiled ore, materials, and supplies. The classification of metals inventory is determined by the stage in the production process. Product inventories are sampled for metal content and are valued based on the lower of actual production costs incurred or estimated net realizable value based upon the period ending prices of contained metal.

Ore stockpile and finished goods inventories are valued at the lower of production cost and net realizable value. Materials and supplies are valued at the lower of average cost and net realizable value. Production costs include all mine site costs.

i) Income taxes

Income tax expense consists of current and deferred tax expense. Income tax is recognized in the income or loss.

Current tax expense is the expected tax payable on the taxable income for the year, using tax rates enacted or substantially enacted at period end, adjusted for amendments to tax payable with regards to previous years.

Deferred tax assets and liabilities are recognized for deferred tax consequences attributable to unused tax loss carry forwards, unused tax credits and differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax basis. Deferred tax assets and liabilities are measured using the enacted or substantially enacted tax rates expected to apply when the asset is realized or the liability settled.

The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income or loss in the period that substantive enactment occurs.

A deferred tax asset is recognized to the extent that it is probable that future taxable income will be available against which the asset can be utilized. To the extent that the Company does not consider it probable that deferred tax asset will be recovered, the deferred tax asset is reduced.

The following temporary differences do not result in deferred tax assets or liabilities:

- the initial recognition of assets or liabilities, not arising in a business combination, that does not affect accounting or taxable income;
- goodwill; and,
- investments in subsidiaries, associates and jointly controlled entities where the timing of reversal of the temporary differences can be controlled and reversal in the foreseeable future is not probable.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to the set off current tax assets against current tax liabilities and when they relate to income taxes levied by the same taxation authority and the Company intends to settle its current tax assets and liabilities on a net basis.

2. Basis of Consolidation and Summary of Significant Accounting Policies (continued)

j) Share-Based Payments

The fair value method of accounting is used for share-based payment transactions. Under this method, the cost of share options and other equity-settled share-based payment arrangements are recorded based on the estimated fair value at the grant date and charged to earnings over the vesting period. Where awards are forfeited because non-market based vesting conditions are not satisfied, the expense previously recognized is proportionately reversed in the period the forfeiture occurs.

Share-based payment expense relating to cash-settled awards, including deferred and restricted share units is accrued over the vesting period of the units based on the quoted market value of Company's common shares. As these awards will be settled in cash, the expense and liability are adjusted each reporting period for changes in the underlying share price.

i. Stock Option Plan

The Company applies the fair value method of accounting for all stock option awards. Under this method, the Company recognizes a compensation expense for all stock options awarded to employees, based on the fair value of the options on the date of grant which is determined by using the Black-Scholes option pricing model. The fair value of the options is expensed over the graded vesting period of the options.

ii. Deferred Share Unit ("DSU") Plan

The Company's DSU compensation liability is accounted for based on the number of units outstanding and the quoted market value of the Company's common shares at the financial position date. The year-over-year change in the deferred share unit compensation liability is recognized in income.

iii. Restricted Share Unit ("RSU") Plan

The Company's RSU compensation liability is accounted for based on the number of units outstanding and the quoted market value of the Company's common shares at the financial position date. The Company recognizes a compensation cost in operating income on a graded vesting basis for each RSU granted equal to the quoted market value of the Company's common shares at the date of which RSUs are awarded to each participant prorated over the performance period and adjusts for changes in the fair value until the end of the performance date. The cumulative effect of the change in fair value is recognized in income in the period of change.

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2. Basis of Consolidation and Summary of Significant Accounting Policies (continued)

k) Earnings (Loss) per Share

Basic earnings (loss) per share is computed by dividing income for the year by the weighted average number of common shares outstanding during the period.

The diluted earnings (loss) per share calculation is based on the weighted average number of common shares outstanding during the period, plus the effects of dilutive common share equivalents. This method requires that the dilutive effect of outstanding options issued should be calculated using the treasury stock method. This method assumes that all common share equivalents have been exercised at the beginning of the period (or at the time of issuance, if later), and that the funds obtained thereby were used to purchase common shares of the Company at the average trading price of the common shares during the period, but only if dilutive.

l) Foreign Currency Translation

The presentation currency of the Company is the United States Dollar ("US$").

The functional currency of each of the entities in the group is the US$, with the exception of the parent entity and certain holding companies which have a Canadian dollar functional currency.

Transactions in foreign currencies are initially recorded in the functional currency at the exchange rate at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are retranslated at the rate of exchange at each financial position date. Foreign exchange gains or losses on translation to the functional currency of an entity are recorded in income. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rate as at the date of the initial transaction.

For entities with a functional currency different from the presentation currency, translation to the presentation currency is required. Assets and liabilities are translated at the rate of exchange at the financial position date. Revenue and expenses are translated at the average rate for the period. All resulting exchange differences are recognized in other comprehensive income.

m) Financial Instruments

i. Financial Assets

The Company classifies all financial assets as either fair value through profit or loss ("FVTPL"), held-to-maturity ("HTM"), loans and receivables, or available-for-sale "(AFS"). The classification is determined at initial recognition and depends on the nature and purpose of the financial asset.

a) Financial Assets at Fair Value Through Profit or Loss

Financial assets are classified as FVTPL when the financial asset is held-for-trading or it is a designated FVTPL on initial recognition. A financial asset is classified in this category if acquired principally for the purpose of selling in the short-term.

2. Basis of Consolidation and Summary of Significant Accounting Policies (continued)

m) Financial Instruments (continued)

i. Financial Assets (continued)

a) Financial Assets at Fair Value through Profit or Loss (continued)

Financial assets classified as FVTPL are stated at fair value with any resulting gain or loss recognized in income or loss in the period in which they arise. Transaction costs related to financial assets classified as FVTPL are recognized immediately in net income (loss).

Derivatives are categorized as held-for-trading. Derivatives are initially recognized at fair value on the date a derivative contract is entered into and are subsequently remeasured at their fair value. Fair value of the Company's recognized commodity-based derivatives are based on the forward prices of the associated market index. Gains or losses are recorded in the statement of income.

b) Held-to-Maturity Investments ("HTM")

HTM investments are recognized on a trade-date basis and are initially measured at fair value, including transaction costs. The Company does not have any assets classified as HTM investments.

c) Loans and Receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They are stated at fair value, net of transaction costs and are classified as current or non-current assets based on their maturity date. They are carried at amortized cost less any impairment. The impairment loss of receivables is based on a review of all outstanding amounts at period end. Interest income is recognized by applying the effective interest rate, except for short term receivables when the recognition of interest would not be material.

d) Available-For-Sale ("AFS") Assets

AFS financial assets are non-derivatives that are either designated in this category or not classified in any of the other categories.

AFS financial assets are subsequently measured at fair value, determined by published market prices in an active market, except for investments in equity instruments that do not have quoted market prices in an active market which are measured at cost. Changes in fair value are recorded in other comprehensive income (loss) until the assets are removed from the statement of financial position. Investments classified as available-for-sale are written down to fair value through income whenever it is necessary to reflect prolonged or significant decline in the value of the assets. Realized gains and losses on the disposal of available-for-sale securities are recognized in investment and other income.

The Company does not have any assets classified as AFS.

2. Basis of Consolidation and Summary of Significant Accounting Policies (continued)

m) Financial Instruments (continued)

i. Financial Assets (continued)

e) Impairment of Financial Assets

Financial assets, other than those at FVTPL, are assessed for indicators of impairment at each period end. Financial assets are impaired when there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows of the investment have been impacted.

Objective evidence of impairment could include the following:

- significant financial difficulty of the issuer or counterparty;
- default or delinquency in interest or principal payments; or
- it has become probable that the borrower will enter bankruptcy or financial reorganization.

For financial assets carried at amortized cost, the amount of the impairment is the difference between the asset's carrying amount and the present value of the estimated future cash flows, discounted at the financial asset's original effective interest rate.

The carrying amount of all financial assets at amortized cost, excluding trade receivables, is directly reduced by the impairment loss. The carrying amount of trade receivables is reduced through the use of an allowance account. When a trade receivable is considered uncollectable, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited against the allowance account. Changes in the carrying amount of the allowance account are recognized in income or loss.

With the exception of AFS equity instruments, if a subsequent period, the amount of the impairment loss decreases and the decrease relates to an event occurring after the impairment was recognized, the previously recognized impairment loss is reversed through income or loss. On the date of impairment reversal, the carrying amount of the financial asset cannot exceed its amortized cost had impairment not been recognized.

f) Derecognition of Financial Assets

A financial asset is derecognized when:

- the contractual right of the asset's cash flows expire; or

- if the Company transfers the financial asset and substantially all risks and reward of ownership to another entity.

2. Basis of Consolidation and Summary of Significant Accounting Policies (continued)

m) Financial Instruments (continued)

ii. Financial Liabilities

Derivatives are categorized as held-for-trading. Derivatives are initially recognized at fair value on the date a derivative contract is entered into and are subsequently remeasured at their fair value. Fair value of the Company's recognized commodity-based derivatives are based on the forward prices of the associated market index. Gains or losses are recorded in the statement of income.

Long term debt and other financial liabilities are recognized initially at the fair value, net of transaction costs incurred, and are subsequently stated at amortized cost. Any difference between the amounts originally received (net of transaction costs) and the redemption value is recognized in the income statement of income over the period to maturity using the effective interest method.

iii. Classification and Subsequent Measurements

The Company has designated each of its significant categories of financial instruments as follows:

Financial Instrument	Classification	Measurement
Cash and Cash Equivalents	FVTPL	Fair value
Short Term Investments	FVTPL	Fair value
Derivative Assets	FVTPL	Fair value
Trade Receivable from Concentrate Sales	FVTPL	Fair value
Other Accounts Receivables	Loans and receivables	Amortized cost
Due from Related Parties	Loans and receivables	Amortized cost
Long Term Receivables	Loans and receivables	Amortized cost
Trade and Other Payables	Other liabilities	Amortized cost
Due to Related Parties	Other liabilities	Amortized cost
Derivative Liabilities	FVTPL	Fair value
Income Tax Payable	Other liabilities	Amortized cost
Long Term Liabilities	Other liabilities	Amortized cost

iv. Effective Interest Method

The effective interest method calculates the amortized cost of a financial instrument and allocates interest income or expense over the corresponding period. The effective interest rate is the rate that discounts estimated future cash receipts or payments over the expected life of the financial instrument, or where appropriate, a shorter period, to the net carrying amount on initial recognition. Income or expense is recognized on an effective interest basis for instruments other than those financial instruments classified as FVTPL.

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2. Basis of Consolidation and Summary of Significant Accounting Policies (continued)

n) Segment Reporting

A geographical segment is a distinguishable component of the entity that is engaged in providing products or services within a particular economic environment and is subject to risks and returns that are different than those of segments operating in other

economic environments.

The business operations comprise the mining and processing of silver-lead, zinc, and silver-gold and the sale of these products.

o) Leases

A lease is a finance lease when substantially all of the risks and rewards incidental to ownership of the leased asset are transferred from the lessor to the lessee by the agreement. The leased assets are initially recorded at the lower of the fair value and the present value of the minimum lease payments and are depreciated over the shorter of the asset's useful lives and the term of the lease. Interest on the lease instalments is recognized as interest expense over the lease term using the effective interest method. Leases for land and buildings are recorded separately if the lease payments can be allocated accordingly.

Leases that do not transfer all the risks and rewards of ownership are classified as operating leases. Payments are recorded in the income statement using the straight line method over their estimated useful lives.

p) Share Capital

Common shares are classified as equity. Incremental costs directly attributable to the issue of shares are shown in equity as a deduction from the proceeds. Share-based payments including stock option plan, deferred share unit plan, and restricted share unit plan are discussed in Note 2. j).

q) 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.

r) Significant Accounting Judgments and Estimates

The preparation of consolidated financial statements requires management to make judgments and estimates that affect the reported amounts of assets and liabilities at the date of the financial statements and reported amounts of expenses during the reporting period. Actual outcomes could differ from these judgments and estimates. The consolidated financial statements include judgments and estimates which, by their nature, are uncertain. The impacts of such judgments and estimates are pervasive throughout the consolidated financial statements, and may require accounting adjustments based on future occurrences. Revisions to accounting estimates are recognized in the period in which the estimate is revised and the revision affects both current and future periods.

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2. Basis of Consolidation and Summary of Significant Accounting Policies (continued)

r) Significant Accounting Judgments and Estimates (continued)

Significant assumptions about the future and other sources of judgments and estimates that management has made at the statement of financial position date, that could result in a material adjustment to the carrying amounts of assets and liabilities, in the event that actual results differ from assumptions made, relate to, but are not limited to, the following:

i. Critical Judgments

- The analysis of the functional currency for each entity of the Company. In concluding that the United States dollar ("US$") functional currency for its Peruvian and Mexican entities and the Canadian and Barbados entities have a Canadian dollar ("CAD$") functional currency, management considered the currency that mainly influences the cost of providing goods and services in each jurisdiction in which the Company operates. As no single currency was clearly dominant the Company also considered secondary indicators including the currency in which funds from financing activities are denominated and the currency in which funds are retained.
- In concluding when commercial production has been achieved, the Company considered the following factors:
- all major capital expenditures to bring the mine to the condition necessary for it to be capable of operating in the manner intended by management have been completed;
- the mine or mill is operating as per design capacity and metallurgical recoveries were achieved; and,
- the ability to sustain ongoing production of ore at a steady or increasing level.

- The identification of reportable segments, basis for measurement and disclosure of the segmented information.
- The determination of estimated useful lives and residual values of tangible and long-lived assets and the measurement of depreciation expense.
- The identification of impairment indicators, cash generating units and determination of value in use and the write down of tangible and long lived assets.
- Measurement of financial instruments involve significant judgments related to interpretation of the terms of the instrument, identification, classification, impairment and the overall measurement to approximate fair values.

ii. ***Estimates***

- the recoverability of amounts receivable which are included in the consolidated statements of financial position;
- the estimation of assay grades of metal concentrates sold in the determination of the carrying value of accounts receivable which are included in the consolidated statements of financial position and included as sales in the consolidated statements of income;
- the carrying value of the short term investments and the recoverability of the carrying value which are included in the consolidated statements of financial position;
- the determination of net realizable value of inventories on the consolidated statements of financial position;

2. Basis of Consolidation and Summary of Significant Accounting Policies (continued)

r) Significant Accounting Judgments and Estimates (continued)

ii. Estimates (continued)

- the estimated useful lives of property, plant and equipment which are included in the consolidated statements of financial position and the related depreciation included in the consolidated statements of income;
- the determination of mineral reserves, carrying amount of mineral properties, and depletion of mineral properties included in the consolidated statements of financial position and the related depletion included in the consolidated statements of income;
- review of tangible and intangible assets carrying value, the determination of whether these assets are impaired and the measurement of impairment charges or reversals which are included in the consolidated statements of income;
- the determination of the fair value of financial instruments and derivatives included in the consolidated statements of financial position;
- the fair value estimation of share-based awards included in the consolidated statements of financial position and the inputs used in accounting for share-based compensation expense in the consolidated statements of income;
- the provision for income taxes which is included in the consolidated statements of income and composition of deferred income tax asset and liabilities included in the consolidated statement of financial position;
- the recognition of deferred income tax assets, amounts recorded for uncertain tax positions, the measurement of income tax expense and indirect taxes included in the consolidated statement of financial position;
- the inputs used in determining the net present value of the liability for provisions related to decommissioning and restoration included in the consolidated statements of financial position;
- the inputs used in determining the various commitments and contingencies accrued in the consolidated statements of financial position; and,
- the assessment of indications of impairment of each mineral properties and related determination of the net realizable value and write-down of those properties where applicable.

s) New Accounting Standards

The Company is currently assessing the impact of adopting the new accounting standards, noted below, on our consolidated financial statements.

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2. Basis of Consolidation and Summary of Significant Accounting Policies (continued)

s) New Accounting Standards (continued)

i) New Accounting Standards Impacting on or after January 1, 2012

IFRS 7 *Financial Instruments: Disclosures* (Amendment)
The amendment, effective for annual periods beginning on or after July 1, 2011, with early application permitted, requires additional quantitative and qualitative disclosures relating to transfers of financial assets, where: financial assets are derecognized in their entirety, but where the entity has a continuing involvement in them; financial assets that are not derecognized in their entirety.

IAS 12 *Income Taxes* (Amendment)
IAS 12 *Income Taxes*, amendments regarding Deferred Tax: Recovery of Underlying Assets introduces an exception to the existing principle for the measurement of deferred tax assets and liabilities arising on investment property measured at fair value, and the requirement that deferred tax on non-depreciable assets measured using the revaluation model in IAS 16 should always be measured on a sale basis. The amendment is effective for annual periods beginning on or after January 1, 2012.

ii) New Accounting Standards Impacting on or after July 1, 2012

IAS 1 Presentation of Financial Statements (Amendment)
The amendments to IAS 1 *Presentation of Financial Statements* require companies preparing financial statements in accordance with IFRSs to group together items within OCI that may be reclassified to the profit or loss section of the income statement. The amendments retain the 'one or two statement' approach at the option of the entity and only revise the way other comprehensive income is presented: requiring separate subtotals for those elements which may be 'recycled' (e.g. cash-flow hedging, foreign currency translation), and those elements that will not (e.g. fair value through OCI items under IFRS 9). In addition, the tax associated with items presented before tax to be shown separately for each of the two groups of OCI items (without changing the option to present items of OCI either before tax or net of tax).

The amendment is effective for annual periods beginning on or after July 1, 2012.

iii) New Accounting Standards Impacting on or after January 1, 2013

IFRS 7 *Financial Instruments: Disclosures in Respect of Offsetting* (Amendment)
At its meeting on December 13-15, 2011, the IASB approved amendments to IFRS 7, *Financial Instruments*: Disclosures, with respect to offsetting financial assets and financial liabilities. The common disclosure requirements issued by the IASB and the FASB in December 2011 are intended to help investors and other users to better assess the effect or potential effect of offsetting arrangements on a company's financial position. Companies and other entities are required to apply the amendments for annual reporting periods beginning on or after January 1, 2013, and interim periods within those annual periods. The required disclosures should be provided retrospectively.

2. Basis of Consolidation and Summary of Significant Accounting Policies (continued)

s) New Accounting Standards (continued)

iii) New Accounting Standards Impacting on or after January 1, 2013 (continued)

IFRS 10 *Consolidated Financial Statements*
IFRS 10 *Consolidated Financial Statements* replaces the portion of IAS 27 *Consolidated and Separate Financial Statements* that addresses the accounting for consolidated financial statements, and SIC12 *Consolidation - Special Purpose Entities*. IFRS 10 establishes principles for the presentation and preparation of consolidated financial statements when an entity controls one or more entities. This standard (i) requires a parent entity (an entity that controls one or more other entities) to present consolidated financial statements; (ii) defines the principle of control, and establishes control as a basis for consolidation; (iii) sets out how to apply the principle of control whether an investor controls an investee and therefore must consolidate the investee; and (iv) sets out the accounting requirements for the preparation of consolidated financial statements.

IFRS 10 is effective for annual periods beginning on or after January 1, 2013, with early adoption permitted. IFRS 10 may be adopted to an earlier accounting period, but in doing so, an entity must disclose the fact that it has early adopted the standard and apply IFRS 11 *Joint Arrangements*, IFRS 12 *Disclosure of Interests in Other Entities*, IAS 27 *Separate Financial Statements* (as

amended in 2011), IAS 28 *Investments in Associates and Joint Ventures* (as amended in 2011).

IFRS 11 *Joint Arrangements*

IFRS 11 replaces IAS 31 *Interest in Joint Ventures* and SIC-13 *Jointly-Controlled Entities-Non-Monetary Contributions by Venturers.* This standard establishes the core principle that a party to a joint arrangement determines the type of joint arrangement in which it is involved by assessing its rights and obligations and accounts for those rights and obligations in accordance with that type of joint arrangement (joint operations or joint ventures). This standard is effective for annual periods on or after January 1, 2013, with early adoption permitted.

IFRS 12 *Disclosure of Interests in Other Entities*

IFRS 12 combines the disclosure requirements for an entity's interest in subsidiaries, joint arrangements, associates and structured entities into one comprehensive disclosure standard. This standard requires the disclosure of information that enable users of financial statements to evaluate the nature of, and risks associated with, its interest in other entities and the effects of those interests on its financial position, financial performance and cash flows. This standard is effective for annual periods beginning on or after January 1, 2013, with early adoption permitted, and entities are permitted to incorporate any of the new disclosures into their financial statements before that date.

2. Basis of Consolidation and Summary of Significant Accounting Policies (continued)

s) New Accounting Standards (continued)

iii) New Accounting Standards Impacting on or after January 1, 2013 (continued)

IFRS 13 *Fair Value Measurement*

IFRS 13 *Fair Value Measurement* provides guidance on how to measure fair value, but does not change when fair value is required or permitted under IFRS. IFRS 13 defines fair value, sets out a single IFRS framework for measuring fair value and requires disclosures about fair value measurements. IFRS 13 applies when another IFRS requires or permits fair value measurements or disclosures about fair value measurements (and measurements, such as fair value less costs to sell, based on fair value or disclosures about those measurements), except for: share-based payment transactions within the scope of IFRS 2 *Share-based Payment*; leasing transactions with the scope of IAS 17 *Leases*; measurements that have some similarities to fair value that are not fair value, such as net realizable value in IAS 2 *Inventories*; or value in use IAS 36 *Impairment of Assets*. This standard is effective for annual periods beginning on or after January 1, 2013, with early adoption permitted.

IAS 19 *Post-employment Benefits*

On June 16, 2011 the IASB issued amendments to IAS 19, *Employee Benefit,* in order to improve the accounting for pensions and other post-employment benefits.

The amendments make important improvements by:

- eliminating the option to defer the recognition of gains and losses, known as the 'corridor method' or the "deferral and amortization approach";
- streamlining the presentation of changes in assets and liabilities arising from defined benefit plans, including requiring re-measurements to be presented in OCI, thereby separating those changes from changes that many perceive to be the result of an entity's day-to-day operations;
- enhancing the disclosure requirements for defined benefit plans, providing better information about the characteristics of defined benefit plans and the risks that entities are exposed to through participation in those plans.

The amendments are effective for financial years beginning on or after January 1, 2013. Earlier application is permitted.

IAS 27 *Separate Financial Statements*

IAS 27 has the objective of setting standards to be applied in accounting for investments in subsidiaries, jointly controlled entities, and associates when an entity elects, or is required by local regulations, to present separate (non-consolidated) financial statements. This standard is effective for annual periods beginning on or after January 1, 2013, with early adoption permitted. This standard will not have an impact on the consolidated financial statements.

IAS 28 *Investments in Associates and Joint Ventures*

IAS 28 prescribes the accounting for investments in associates and to set the requirements for the application of the equity method when accounting for investments in associates and joint ventures. This standard is effective for annual periods beginning on or after January 1, 2013, with early adoption permitted.

2. Basis of Consolidation and Summary of Significant Accounting Policies (continued)

s) New Accounting Standards (continued)

iv) New Accounting Standards Impacting on or after January 1, 2014

IAS 32 *Financial Instruments - Presentation in Respect of Offsetting* (Amendment)

At its meeting on December 13-15, 2011, the IASB approved amendments to IFRS 7, *Financial Instruments*: Disclosures, with respect to offsetting financial assets and financial liabilities. As part of this project the IASB also clarified aspects of IAS 32, *Financial Instruments*: Presentation. The amendments to IAS 32 address inconsistencies in current practice when applying the requirements. The amendments are effective for annual periods beginning on or after January 1, 2014 and are required to be applied retrospectively.

v) New Accounting Standards Impacting on or after January 1, 2015

IFRS 9 *Financial Instruments - Classification and Measurement*

IFRS 9*, Financial Instruments:* IFRS 9 introduces the new requirements for the classification, measurement and de-recognition of financial assets and financial liabilities. Specifically, IFRS 9 requires all recognized financial assets that are within the scope of IAS 39 *Financial Instruments: Recognition and Measurement* to be subsequently measured at amortized cost or fair value, and all financial liabilities classified as subsequently measured at amortized cost except for financial liabilities as at FVTPL. The amendments are effective for annual periods beginning on or after January 1, 2015, with earlier application permitted.

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3. Cash and Cash Equivalents

	December 31, 2011	December 31, 2010	January 1, 2010
Cash	**$ 25,652**	$ 61,118	$ 21,863
Cash equivalents	**13,078**	9,180	8,900
	$ 38,730	$ 70,298	$ 30,763

Cash and cash equivalents include cash on hand, demand deposits, and money market instruments, with maturities from the date of acquisition of 90 days or less.

4. Short Term Investments

	December 31, 2011	December 31, 2010	January 1, 2010
Held for trading short term investments	**$ 17,000**	$ 20,509	$ 6,034

Short term investments include deposits with maturities from the date of acquisition of more than 90 days.

5. Derivative Assets and Derivative Liabilities

	December 31, 2011		December 31, 2010		January 1, 2010	
	Assets	**Liabilities**	Assets	Liabilities	Assets	Liabilities
Lead Asian options	**$ -**	**$ -**	$ -	$ -	$ 2	$ -
Zinc Asian options	**-**	**-**	-	-	-	263
Lead forward contracts	**-**	**53**	-	14	-	1,356
Zinc forward contacts	**70**	**-**	-	6	-	1,473
Silver forward contracts	**-**	**34**	-	113	35	-
Total	**$ 70**	**$ 87**	$ -	$ 133	$ 37	$ 3,092

The Company occasionally enters into forward commodity contracts as well as put and call option commodity arrangements to secure a minimum price level on part of its zinc and lead metal production. As at the end of the year no such contracts are outstanding.

Additionally, the Company enters regularly into short term forward and option contracts to fix the final settlement price of metal delivered in concentrates, where the final settlement price is yet to be set at a future quotational period according to contract terms. The forward sale and option contracts are settled against the arithmetic average of metal spot prices over the month in which the contract matures. No initial premium associated with these trades has been paid.

6. Accounts Receivable and Other Assets and Deposits on Long Term Assets

The current accounts receivables and other assets are comprised of the following:

	December 31, 2011	December 31, 2010	January 1, 2010
Current			
Trade receivables from concentrate sales	**$ 11,287**	$ 11,224	$ 7,154
Current portion of long term receivables - net	**891**	39	121
Prepaid expenses	**1,171**	903	313
Deposits	**47**	-	24
Advances and other receivables	**2,213**	1,288	1,023
Accounts receivable and other assets	**$ 15,609**	$ 13,454	$ 8,635
GST/HST and value added tax receivable	**$ 4,777**	$ 3,542	$ 601

Deposits on long term assets includes the non-current accounts receivable and other assets comprised of the following:

	December 31, 2011	December 31, 2010	January 1, 2010
Non-Current			
Long term receivables	**$ 1,415**	$ 47	$ 137
Less: current portion of long term receivables	**(891)**	(39)	(121)
Non-current portion of long term receivables - net	**524**	8	16
Deposits on equipment	**1,167**	3,097	-
Deposits paid to contractors	**448**	1,581	-
Other	**121**	-	-
	$ 2,260	$ 4,686	$ 16

As at December 31, 2011, the Company had $100 trade receivables (2010: $nil) (January 1, 2010: $nil) which were past due with no impairment. The Company's allowance for doubtful accounts is $nil for all reporting periods.

The aging analysis of these trade receivables is as follows:

	December 31, 2011	December 31, 2010	January 1, 2010
0-30 days	**$ 9,518**	$ 9,754	$ 7,154
31-60 days	**911**	1,057	-
61-90 days	**758**	413	-
over 90 days	**100**	-	-
	$ 11,287	$ 11,224	$ 7,154

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7. Inventories

	December 31, 2011	December 31, 2010	January 1, 2010
Concentrate stock piles	**$ 2,488**	$ 346	$ 651
Ore stock piles	**4,008**	1,274	203
Materials and supplies	**4,795**	2,398	1,474
Total inventories	**$ 11,291**	$ 4,018	$ 2,328

For the years ended December 31, 2011, $31,655 (2010: $22,270) of inventory was expensed in cost of sales and there has been

no impairment during 2011 (2010: $nil).

8. Mineral Properties, Property, Plant and Equipment

	Mineral Properties Non-Depletable	Mineral Properties Depletable (Caylloma, San Jose*)	Machinery and Equipment	Land, Buildings, and Leasehold Improvements	Furniture and Other Equipment	Transport Units	Equipment under Finance Lease	Capital Work in Progress	Total
Year ended December 31, 2011									
Opening carrying amount	$ 49,129	$ 33,608	$ 6.897	$ 7,013	$ 3,177	$ 112	$ 2,893	$ 14,534	$ 117,363
Additions	6,258	30,091	5,429	729	2,032	131	500	33,837	79,007
Disposals	-		(1,532)	-	(33)	-	-	-	(1,565)
Depreciation charge	-	(6,107)	(1,847)	(1,820)	(334)	(97)	(873)	-	(11,078)
Impairment charge	-		(1,688)	(195)	-	(11)	-	-	(1,894)
Reclassification	(48,076)	48,076	10,057	31,725	(1,657)	-	-	(40,125)	-
Closing carrying amount	**$ 7,311**	**$ 105,668**	**$ 17,316**	**$ 37,452**	**$ 3,185**	**$ 135**	**$ 2,520**	**$ 8,246**	**$ 181,833**
As at December 31, 2011									
Cost	7,311	125,667	$ 22,870	$ 41,212	$ 4,296	$ 520	$ 4,674	$ 8,246	$ 214,796
Accumulated depreciation and impairment	-	(19,999)	(5,554)	(3,760)	(1,111)	(385)	(2,154)	-	(32,963)
Closing carrying amount	**$ 7,311**	**$ 105,668**	**$ 17,316**	**$ 37,452**	**$ 3,185**	**$ 135**	**$ 2,520**	**$ 8,246**	**$ 181,833**

*Commercial production began on September 1, 2011 for San Jose and included in mineral properties non-depletable as at December 31, 2010 and January 1, 2010.

In 2011, non-depletable mineral properties include the following properties: Mario, Don Mario, Tlacolula, and Taviche.

8. Mineral Properties, Property, Plant and Equipment (continued)

	Mineral Properties Non-Depletable	Mineral Properties Depletable (Caylloma)	Machinery and Equipment	Land, Buildings, and Leasehold Improvements	Furniture and Other Equipment	Transport Units	Equipment under Finance Lease	Capital Work in Progress	Total
Year ended December 31, 2010									
Opening carrying amount	$ 39,907	$ 28,370	$ 6,916	$ 4,033	$ 1,117	$ 197	$ 2,682	$ 1,953	$ 85,175
Additions	9,334	8,499	1,729	155	2,542	88	928	16,490	39,765
Disposals	(112)	(443)	(20)	(1)	(10)	(67)	-	-	(653)
Depreciation charge	-	(3,604)	(1,509)	(768)	(273)	(106)	(664)	-	(6,924)
Reclassification	-	786	(219)	3,594	(199)	-	(53)	(3,909)	-
Closing carrying amount	$ 49,129	$ 33,608	$ 6,897	$ 7,013	$ 3,177	$ 112	$ 2,893	$ 14,534	$ 117,363
As at December 31, 2010									
Cost	49,129	47,500	$ 11,060	$ 9,076	$ 3,985	$ 436	$ 4,174	$ 14,534	$ 139,894
Accumulated depreciation and impairment	-	(13,892)	(4,163)	(2,063)	(808)	(324)	(1,281)	-	(22,531)
Closing carrying amount	$ 49,129	$ 33,608	$ 6,897	$ 7,013	$ 3,177	$ 112	$ 2,893	$ 14,534	$ 117,363

	Mineral Properties Non-Depletable	Mineral Properties Depletable (Caylloma)	Machinery and Equipment	Land and Buildings	Furniture and Other Equipment	Transport Units	Equipment under Finance Lease	Capital Work in Progress	Total
As at January 1, 2010									
Opening carrying amount	$ 35,755	$ 25,947	$ 6,661	$ 3,365	$ 1,025	$ 392	$ 1,629	$ 1,493	$ 76,267
Additions	5,402	5,019	418	138	229	-	1,425	2,652	15,283
Disposals	(1,250)		(77)	(1)	(26)	(80)	(23)	-	(1,457)
Depreciation charge	-	(2,596)	(1,250)	(392)	(216)	(115)	(349)	-	(4,918)
Reclassification	-		1,164	923	105	-	-	(2,192)	-
Closing carrying amount	$ 39,907	$ 28,370	$ 6,916	$ 4,033	$ 1,117	$ 197	$ 2,682	$ 1,953	$ 85,175
As at January 1, 2010									
Cost	39,907	38,658	$ 9,933	$ 5,071	$ 1,548	$ 437	$ 3,249	$ 1,953	$ 100,756
Accumulated depreciation and impairment	-	(10,288)	(3,017)	(1,038)	(431)	(240)	(567)	-	(15,581)
Closing carrying amount	$ 39,907	$ 28,370	$ 6,916	$ 4,033	$ 1,117	$ 197	$ 2,682	$ 1,953	$ 85,175

Mineral properties includes bonuses paid of $1,350 (2010: $nil) (January 1, 2010: $nil) which were paid upon commissioning of the San Jose mine to a director, a director and officer, and an officer. The bonus comprises of $1,113 paid to key management and $237 paid to a company controlled by a director. Refer to Note 10 Related Party Transactions.

8. Mineral Properties, Property, Plant and Equipment (continued)

a) Mario Property

In May 2011, the Company entered into an agreement to acquire a 100% interest in the Mario Property, located in the Department of Junin in central Peru. Under the terms of the agreement, the Company is granted the exclusive right and option to purchase an undivided 100% interest in the Mario Property subject to the following payments:

1. $500 on signing of agreement;
2. $500 on or before six months from the signing of the agreement;
3. $500 on or before 12 months from the signing of the agreement; and,
4. $2,500 on or before 24 months from the signing of the agreement.

The transfer of the property to the Company is subject to a 1% net smelter return ("NSR") royalty on production from the property payable to Crocodile Gold ("Crocodile"). The Company shall have the right to purchase the NSR royalty from Crocodile at any time during the five-year period following the final option payment for the sum of $3,000. The property is also subject to a 2% NSR royalty on production payable to Teck Cominco and a 0.5% NSR royalty on production payable to Socrate Capital Inc., with each royalty in turn subject to certain buy-back provisions. As at December 31, 2011, $1,000 has been paid under the agreement.

b) Don Mario Property

The Company entered into an option agreement, effective July 20, 2011, to acquire 100% interest in the Don Mario property, with Consorcio Empresarial Agmin S.A.C.("AGMIN"). Under the terms of the mining assignment and option to purchase mineral rights agreement ("agreement"), the Company is required to make the following payments:

1. $200 on signing the agreement;
2. $300 after 12 months from signing the agreement;
3. $500 after 24 months from signing the agreement; and,
4. $2,000 after 36 months from signing the agreement.

Under the terms of the agreement, once the option is exercised and technical report is prepared under National Instrument 43-101 and published, if the pre-feasibility study indicates that the property contains more than five million silver equivalent ounces, the Company would further pay AGMIN, one dollar for each additional resource and reserves indicated in the pre-feasibility report. The Company has the option to buy-out the additional pay-out for a further $3,000, subject to certain conditions.

As at December 31, 2011, $200 has been paid under the agreement.

8. Mineral Properties, Property, Plant and Equipment (continued)

c) Tlacolula Property

In September 2009, the Company, through its wholly owned subsidiary, Cuzcatlan, was granted an option (the "Option") to acquire a 60% interest (the "Interest") in the Tlacolula silver project ("property") located in the State of Oaxaca, Mexico from Radius Gold Inc.'s wholly owned subsidiary, Radius (Cayman) Inc. ("Radius") (a related party by way of directors in common with the Company described further in Note 10).

The Company can earn the Interest by spending $2,000, which includes a commitment to drill 1,500 meters within three years, and making staged annual payments of $250 cash and $250 in common stock of the Company to Radius according to the following schedule:

- Ø $20 cash and $20 cash equivalent in shares upon stock exchange approval;
- Ø $30 cash and $30 cash equivalent in shares by the first year anniversary;
- Ø $50 cash and $50 cash equivalent in shares by the second year anniversary;
- Ø $50 cash and $50 cash equivalent in shares by the third year anniversary; and,
- Ø $100 cash and $100 cash equivalent in shares by the fourth year anniversary.

Upon completion of the cash payments and share issuances, and incurring the exploration expenditures as set forth above, the Company will be deemed to have exercised the Option and acquired a 60% interest in the property, whereupon a joint venture will be formed to further develop the property on the basis of the Company owning 60% and Radius 40%.

On January 15, 2010, the transaction was approved by the TSX Venture Exchange, The Company has issued 7,813 common shares at a fair market value of $2.56 per share and paid $20 cash according to the terms of the option agreement.

On January 14, 2011, the Company issued 6,756 common shares of the Company, at a fair market value of $4.44 per share and paid $30 cash according to the terms of the option agreement.

Subsequent to December 31, 2011, on January 13, 2012, the Company issued 8,605 common shares of the Company, at a fair market value of $5.81 per share and paid $50 cash according to the terms of the option agreement.

8. Mineral Properties, Property, Plant and Equipment (continued)

d) Taviche Property

In 2010, the Company included the idle plant in Taviche as part of the San Jose mine plant as it was more likely than not that the idle plant could be used to treat excess ore from San Jose or from surrounding areas where the company was conducting exploration. On September 1, 2011, the San Jose mine plant commenced commercial production and in the fourth quarter of 2011, achieved an average of 955 tonnes milled per day with the San Jose plant having sufficient capacity for the production. In the fourth quarter, management reassessed the usability of the idle plant and in conjunction, obtained an independent third party appraisal of various assets acquired under an asset purchase agreement dated 2007 related to the Taviche property.

Management used the fair value less cost to sell method to determine the recoverable amount of the idle plant. Based upon an independent appraisal of the assets, which is in accordance with fair value less cost to sell, the Company has taken an impairment charge of $1.89 million that comprised of the following impairments: $1.08 million on the tailing dam, $0.14 million on the mine infrastructure, and $0.67 million on equipment, machinery, and buildings. As at December 31, 2011, the net book value of assets related to the Taviche property for machinery, and equipment amount to $0.36 million.

9. Trade and other payables

	December 31, 2011	December 31, 2010	January 1, 2010
Trade accounts payable	**$ 8,800**	$ 3,967	$ 2,580
Payroll and other payables	**7,152**	5,249	2,556
Restricted share unit payable	**1,204**	87	-
	$ 17,156	$ 9,303	$ 5,136

10. Related Party Transactions

The consolidated financial statements include the financial statements of Fortuna Silver Mines Inc. and it subsidiaries listed in the following table:

		Equity Interest as at December 31,	
Name	**Country of Incorporation**	**2011**	2010
Minera Bateas S.A.C.	Peru	100%	100%
Fortuna Silver Mines Peru S.A.C.	Peru	100%	100%
Compania Minera Cuzcatlan SA	Mexico	100%	100%
Fortuna Silver Mexico, S.A. de CV	Mexico	100%	n/a
Fortuna Silver (Barbados) Inc.	Barbados	100%	100%
Continuum Resources Ltd.	Canada	100%	100%

Fortuna Silver Mexico, S.A. de CV was incorporated in 2011.

10. Related Party Transactions (continued)

a) Purchase of Goods and Services

The Company entered into the following related party transactions:

	Years ended December 31,	
Transactions with related parties	**2011**	2010
Salaries and wages [1,2]	**$ 173**	$ 174
Other general and administrative expenses [2]	**292**	185
Leasehold improvements [2]	**93**	-
	$ 558	$ 359

[1] Salaries and wages includes employees' salaries and benefits charged to the Company based on a percentage of the estimated hours worked for the Company

[2] Radius Gold Inc. ("Radius") has directors in common with the Company and shares office space, and is reimbursed for salaries and wages, general and administrative costs, and leasehold improvements incurred on behalf of the Company.

During the year ended December 31, 2011, the Company transferred two mining concessions to Focus Ventures Ltd., a Company with directors in common, in exchange for a 1% net smelter return royalty.

During the year ended December 31, 2011, the Company issued 6,756 (2010: 7,813) common shares, at a fair market value of $4.44 (2010: $2.56) per share and paid $30 cash (2010: $20) to Radius, under the option to acquire a 60% interest in Tlacolula silver project located in the State of Oaxaca, Mexico.

Subsequent to the year ended December 31, 2011 to March 23, 2012, the Company issued 8,605 common shares, at a fair market value of $5.81 per share and paid $50 cash to Radius, under the option to acquire a 60% interest in Tlacolula silver project located in the State of Oaxaca, Mexico.

10. Related Party Transactions (continued)

b) Key Management Compensation

Key management includes all persons named or performing the duties of Vice-President, Chief Financial Officer, President, Chief Executive Officer, and non-executive Directors of the Company. The compensation paid and payable to key management for services is shown below:

	Years ended December 31,	
	2011	2010
Salaries and other short term employee benefits	**$ 3,492**	$ 2,633
Directors fees	**333**	300
Consulting fees	**416**	174
Share-based payments	**4,398**	188
	$ 8,639	$ 3,295

The share-based payments includes the change in the DSU and RSU fair value over each reporting period and payments made under the DSU and RSU plans and the non-cancellation of share options.

Consulting fees includes fees paid to two non-executive directors in both 2011 and 2010.

c) Year-end Balances arising from Purchases of Goods/Services

Amounts due to/(from) related parties	**December 31, 2011**	December 31, 2010	January 1, 2010
Owing from a director and officer [3]	**$ (36)**	$ (1)	$ (1)
Owing to a company with common directors [2]	**205**	41	50

	$ 169	$ 40	$ 49

[3] Owing from a director includes non-interest bearing advances to a director and officers and December 31, 2011 and one officer and director at December 31, 2010 and January 1, 2010.

11. Leases and Long Term Liabilities

Leases and long term liabilities are comprised of the following:

	December 31, 2011	December 31, 2010	January 1, 2010
Obligations under finance lease (a)	**$ 866**	$ 1,545	$ 1,848
Long term liability (b)	**771**	705	644
Deferred share units (Note 14 c))	**2,639**	1,955	-
Restricted share units (Note 14 d))	**1,204**	131	-
	5,480	4,336	2,492
Less: current portion			
Obligations under finance lease	**741**	1,083	1,038
Long term liability	**771**	-	-
Current portion of long term liability	**1,512**	1,083	1,038
Restricted share unit payable, current (Note 9)	**1,204**	87	-
Leases and long term liability, non-current	**$ 2,764**	$ 3,166	$ 1,454

a) Obligations under Finance Lease

The following is a schedule of the Company's future minimum lease payments. These are related to the acquisition of mining equipment, vehicles, and buildings.

Obligations under Finance Lease	**December 31, 2011**	December 31, 2010	January 1, 2010
Not later than 1 year	**$ 763**	$ 1,150	$ 1,151
Less: future finance charges on finance lease	**(22)**	(67)	(113)
	741	1,083	1,038
Later than 1 year but less than 5 years	**126**	472	862
Less: future finance charges on finance lease	**(1)**	(10)	(52)
	125	462	810
Present value of finance lease payments	**$ 866**	$ 1,545	$ 1,848

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11. Leases and Long Term Liabilities (continued)

b) Long Term Liabilities

In May 2008, the Company acquired the Monte Alban II concession for which a payment of $800 is due May 2012. This payment is non-interest bearing.

12. Provisions

A summary of the Company's provisions for other liabilities and charges is presented below:

	Decommissioning and Restoration Liability

Balance - January 1, 2010	$	2,917
New provisions		1,583
Increase to existing provisions		125
Accretion of provisions (Note 20)		163
Foreign exchange differences		93
Balance - December 31, 2010	**$**	**4,881**
Increase to existing provisions		**126**
Accretion of provisions (Note 20)		**173**
Foreign exchange differences		**(5)**
Cash payments		**(201)**
Total provisions – December 31, 2011	**$**	**4,974**
Less: current portion		**(727)**
Non current – December 31, 2011	**$**	**4,247**

In view of the uncertainties concerning environmental reclamation, the ultimate cost of reclamation activities could differ materially from the estimated amount recorded. The estimate of the Company's decommissioning and restoration liability relating to the Caylloma and San Jose mine is subject to change based on amendments to laws and regulations and as new information regarding the Company's operations becomes available.

Future changes, if any, to the estimated liability as a result of amended requirements, laws, regulations, operating assumptions, estimated timing and amount of obligations may be significant and would be recognized prospectively as a change in accounting estimate. Any such change would result in an increase or decrease to the liability and a corresponding increase or decrease to the mineral properties, property, plant and equipment balance.

13. Income Tax

a) Income tax expense differs from the amount that would be computed by applying the Canadian statutory income tax rate of 26.50% (2010: 28.50%) to income before income taxes. The reasons for the differences are as follows:

		December 31, 2011		December 31, 2010
Income before tax	**$**	**38,335**	$	27,513
Statutory income tax rate		**26.50%**		28.50%
Expected income tax	**$**	**10,159**	$	7,841
Items non-deductible for income tax purposes		**1,401**		292
Difference between Canadian and foreign tax rates		**1,376**		874
Effect of change in tax rates		**620**		431
Impact of foreign exchange on tax assets and liabilities		**3,271**		(133)
Impact of Mexican inflation on tax values		**(16)**		(130)
Under(over) provided in prior periods		**704**		(1,495)
Unused tax losses and tax offsets not recognized in tax asset		**1,287**		3,830
Total income taxes	**$**	**18,802**	$	11,510
Represented by:				
Current income tax	**$**	**14,607**	$	8,620
Deferred income tax		**4,195**		2,890
	$	**18,802**	$	11,510

The effective tax rate for the years ended December 31, 2011 and 2010 was 49.05% and 41.8%, respectively. The change in the effective tax rate was primarily attributable to the geographical mix of income, fluctuations in exchange rates for foreign currency, the impact of foreign exchange on the tax basis on non-monetary assets, and the non-recognition of tax benefits.

Effective January 1, 2011, the Canadian Federal corporate tax rate decreased from 18% to 16.5% and the British Columbia provincial tax decreased from 10.5% to 10%. The overall reduction in tax rates has resulted in a decrease in the Company's statutory tax rate from 28.50% to 26.50%.

In 2009, the Mexican government approved tax reform that includes a 2% increase in the income tax rate in Mexico from 28% to 30% for a three-year period starting in 2010.

Income taxes payable of $3,923 (December 31, 2010: $4,192, January 1, 2010 $2,949) relates to current taxes.

13. Income Tax (continued)

b) The tax effected items that give rise to significant portions of the deferred income tax assets and deferred income tax liabilities at December 31, 2011 and 2010 are presented below:

	December 31, 2011	December 31, 2010
Deferred income tax assets:		
Non-capital losses	**$ 12,544**	$ 2,939
Provisions and other	**2,059**	1,095
Financial derivatives	**5**	42
Mineral properties, property, plant and equipment	**296**	186
Net deferred income tax assets	**14,904**	4,262
Deferred income tax liabilities:		
Mineral properties – Peru	**$ (11,790)**	$ (9,912)
Mineral properties – Mexico	**(5,640)**	(2,832)
Equipment	**(10,148)**	-
Total deferred income tax liabilities	**$ (27,578)**	$ (12,744)
Net deferred income tax liabilities	**$ (12,674)**	$ (8,482)

c) The Company recognizes tax benefits on losses or other deductible amounts generated in countries where the probable criteria for the recognition of deferred tax assets has been met.
The Company's unrecognized deductible temporary differences and unused tax losses for which no deferred tax asset is recognized consist of the following amounts:

	December 31, 2011	December 31, 2010
Non-capital losses	**$ 38,503**	$ 29,689
Provisions and other	**3,841**	3,563
Share issue cost	**2,913**	4,146
Mineral properties, property, plant and equipment	**1,532**	3,966
Unrecognized deductible temporary differences	**46,789**	41,364

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13. Income Tax (continued)

The Company's unrecognized deferred tax assets related to unused tax losses have the following expiry dates:

		Expiry date
Non-capital losses, expiring as follows:		
Canada	$ 35,346	2013 - 2031
Mexico	2,850	2016 - 2031
Barbados	172	2017 – 2020
	$ 38,368	

14. Share Capital

a) Unlimited Common Shares Without Par Value

During the year ended December 31, 2010, the Company issued an aggregate of 26,507,500 common shares, under two bought deal financings, for gross proceeds of $78,528. Net proceeds of $73,919 after share issuance costs of $4,609 were raised from

the bought deal financings comprised of: 15,007,500 common shares at CAD$2.30 per share, for net proceeds of $31,135; and 11,500,000 common shares at CAD$4.00 per share, for net proceeds of $42,784.

During the year ended December 31, 2011, the Company issued 6,756 (2010: 7,813) common shares, at a fair market value of $4.44 (2010: $2.56) per share to Radius Gold, under the option to acquire a 60% interest in Tlacolula silver project located in the State of Oaxaca, Mexico.

Subsequent to the year ended December 31, 2011 to March 23, 2012, the Company issued 8,605 common shares, at a fair market value of $5.81 per share to Radius Gold, under the option to acquire a 60% interest in Tlacolula silver project located in the State of Oaxaca, Mexico.

b) Share Options

The Company's stock option plan, approved by the shareholders on August 30, 2006 and accepted by the TSX Venture Exchange on October 16, 2006 provides a rolling maximum of the issuance of common treasury shares equal to up to ten percent of the issued and outstanding common shares with no vesting provisions. The exercise price of the optioned shares are no less than the market price, with a maximum term of ten years from grant. Shareholder approval of the Company's stock option plan was not obtained at the Company's annual general meeting held on June 23, 2010.

Shareholder approval of the Company's new Stock Option Plan (the "New Plan"), dated April 11, 2011, was obtained at the Company's annual general meeting held on May 26, 2011. The New Plan provides that the number of common shares of the Company issuable under the Plan, together with all of the Company's other previously established or proposed share compensation arrangements, may not exceed 12,200,000 shares, which equals 9.92% of the current total number of issued and outstanding common shares of the Company, as at April 11, 2011.

14. Share Capital (continued)

b) Share Options (continued)

Option pricing models require the input of highly subjective assumptions including the estimate of the share price volatility, risk-free interest rate and expected life of the options. Changes in the subjective input assumptions can materially affect the fair value estimate.

The following is a summary of option transactions:

	December 31, 2011		December 31, 2010	
	Shares (in 000's)	**Weighted average exercise price (CAD$)**	Shares (in 000's)	Weighted average exercise price (CAD$)
Outstanding at beginning of the year	**4,551**	**$ 1.51**	8,215	$ 1.50
Granted	**1,792**	**4.46**	-	$ -
Exercised	**(2,242)**	**1.55**	(999)	$ 1.03
Cancelled	**-**	**-**	(2,665)	$ 1.62
Forfeited	**(25)**	**4.46**	-	$ -
Outstanding at end of the year	**3,876**	**$ 2.83**	4,551	$ 1.51
Vested and exercisable at end of the year	**2,557**	**$ 1.99**	4,551	$ 1.51

The non-cash compensation recovery of $2,440 recognized for the year ended December 31, 2010 is associated with the 2,665,000 share purchase options granted in the fourth quarter of 2009 and cancelled as shareholder approval was not obtained at the Company's annual general meeting held on June 23, 2010.

During the year ended December 31, 2011, 1,792,289 share purchase options were granted with an exercise price of CAD$4.46 per share with a term of three years and vesting 25% within six months of grant date, 50% within 12 months of grant date, 75% within 18 months of grant date, and fully vested after 24 months of grant date. As at December 31, 2011, 24,814 share purchase options were forfeited and 8,271 share purchase options were accelerated to expire March 8, 2012. The share based compensation charge of $1,830 covering option grants, forfeitures, and accelerated vesting, was recognized for the year ended December 31, 2011 has been determined under the fair value method using the Black-Scholes option pricing model with the following assumptions:

Years ended December 31,	
2011	2010

Risk-free interest rate	**1.91%**	n/a
Expected stock price volatility	**56.48%**	n/a
Expected term in years	**3**	n/a
Expected dividend yield	**0%**	n/a
Expected forfeiture rate	**1.38%**	n/a

14. Share Capital (continued)

b) Share Options (continued)

The expected volatility assumption is based on the historical volatility of the Company's Canadian dollar common share price on the Toronto Stock Exchange

The following table summarizes information related to stock options outstanding and exercisable at December 31, 2011:

Exercise price in CAD$	Number of outstanding share purchase options (in 000's)	Weighted average remaining contractual life of outstanding share purchase options (years)	Weighted average exercise price on outstanding share purchase options CAD$	Exercisable share purchase options (in 000's)	Weighted average exercise price on exercisable share purchase options CAD$
$0.80 to $0.99	816	6.8	$ 0.85	816	$ 0.85
$1.00 to $1.99	693	4.4	1.53	693	1.53
$2.00 to $4.46	2,367	3.0	3.90	1,048	3.19
$0.80 to $4.46	3,876	4.1	$ 2.83	2,557	$ 1.99

Subsequent to December 31, 2011 to March 23, 2012, 184,138 share purchase options were granted with an exercise price of CAD$6.67 per share with a term of five years and vesting 33.33% within twelve months of grant date, 33.33% within 24 months of grant date, and 33.34% within thirty six months of grant date.

Subsequent to December 31, 2011, 49,628 share purchase options were forfeited and 41,542 share purchase options were accelerated to expire March 30, 2012.

Subsequent to December 31, 2011 to March 23, 2012, 314,225 share purchase options were exercised at prices ranging from CAD$0.85 to CAD$4.46 per share, resulting in issued and outstanding shares of 125,268,751.

c) Deferred Share Units ("DSU") Cost

During 2010, the Company implemented a DSU plan which allows for up to 1% of the number of shares outstanding from time to time to be granted to eligible directors. All grants under the plan are fully vested upon credit to an eligible directors' account.

During the year ended December 31, 2011, 70,000 DSU were settled in cash for $5.36 per unit for a total payment of $375.

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14. Share Capital (continued)

c) Deferred Share Units ("DSU") Cost (continued)

During the year ended December 31, 2011, the Company granted 48,824 DSU with a market value of CAD$232, at the date of grant, to a director, and 93,544 DSU with a market value of CAD$473, at the date of grant, to a director, with vesting subject to the commissioning of the San Jose mine, which occurred on September 1, 2011.

During the year ended December 31, 2010, the Company granted 409,097 DSU with a market value of CAD$1,358, at the date of grant, to directors.

As at December 31, 2011, there are 481,465 (2010: 409,097) DSU outstanding with a fair value of $2,639 (2010: $1,955).

d) Restricted Share Units ("RSU") Cost

During 2010, the Company implemented a RSU plan for certain employees or officers. The RSU entitle employees or officers to a cash payment after the end of a performance period of up to two years following the date of the award. The RSU payment will be an amount equal to the fair market value of the Company's common share on the five trading days immediately prior to the end of the performance period multiplied by the number of RSU held by the employee.

During the year ended December 31, 2011, the Company granted 155,674 RSU with a market value of CAD$788, at the date of grant, to a director, with vesting subject to the commissioning of the San Jose mine, which occurred on September 1, 2011.

During the year ended December 31, 2011, the Company paid $736 (2010: $nil) on 109,557 (2010: nil) RSU to directors, a former director, and officers of the Company.

As at December 31, 2011, there are 265,231 (2010: 219,114) RSU outstanding with a fair value of $1,204 (2010: $131).

e) Earnings per Share

i. Basic

Basic earnings per share is calculated by dividing the income for the year by the weighted average number of shares outstanding during the year.

The following table sets forth the computation of basic earnings per share:

	Years ended December 31,	
	2011	2010
income available to equity owners	**$ 19,533**	$ 16,003
Weighted average number of shares (in '000's)	**123,295**	108,120
Earnings per share - basic	**$ 0.16**	$ 0.15

14. Share Capital (continued)

e) Earnings per Share (continued)

i. Diluted

Diluted earnings per share is calculated by adjusting the weighted average number of shares outstanding to assume conversion of all potentially dilutive shares. The following table sets forth the computation of diluted earnings per share:

	Years ended December 31,	
	2011	2010
Income available to equity owners	**$ 19,533**	$ 16,003
Weighted average number of shares ('000's)	**123,295**	108,120
Incremental shares from share options	**1,417**	2,445
Weighted average diluted shares outstanding	**124,712**	110,565
Earnings per share - diluted	**$ 0.16**	$ 0.14

15. Supplemental Cash Flow Information

	Note	Years ended December 31, 2011	2010
Non-cash Investing and Financing Activities:			
Issuance of shares on purchase of mineral properties, property, plant and equipment	**8**	**$ 30**	$ 20

16. Capital Disclosure

The Company's objectives when managing capital are to provide shareholder returns through maximization of the profitable growth of the business and to maintain a degree of financial flexibility relevant to the underlying operating and metal price risks

while safeguarding the Company's ability to continue as a going concern.

The capital of the Company consists of equity and available credit facility, net of cash. The Board of Directors does not establish a quantitative return on capital criteria for management. The Company manages the capital structure and makes adjustments to it in light of changes in economic conditions and the risk characteristics of the underlying assets.

The management of the Company believes that the capital resources of the Company as at December 31, 2011, are sufficient for its present needs for at least the next 12 months. The Company is not subject to externally imposed capital requirements.

The Company's overall strategy with respect to capital risk management remained unchanged during the year.

17. Management of Financial Risk

The Company's financial instruments are exposed to certain financial risks, including currency risk, credit risk, liquidity risk, interest risk, and price risk. The Company's Board of Directors has overall responsibility for the establishment and oversight of the Company's risk management framework and reviews the Company's policies on an ongoing basis.

a) Fair Value of Financial Instruments

The carrying value of cash and cash equivalents, short term investments, derivative assets, trade receivable from concentrate sales, other accounts receivables, trade and other payables, due to related parties, and derivative liabilities approximate their fair value due to the relatively short periods to maturity and the terms of these financial instruments. Fair value estimates are made at a specific point in time, based on relevant market information and information about the financial instrument.

The amortized value of long term receivables approximates their fair value as these are measured at the amortized cost using the effective interest method. The fair value of the lease and long term liabilities is $5,531 as at December 31, 2011.

The analysis of financial instruments that are measured subsequent to initial recognition at fair value can be categorized into Levels 1 to 3 based upon the degree to which the fair value is observable.

- Level 1 - inputs to the valuation methodology are quoted (unadjusted) for identical assets or liabilities in active markets.
- Level 2 - inputs to valuation methodology include quoted market prices for similar assets and liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument.
- Level 3 - inputs to the valuation methodology are unobservable and significant to the fair value of measurement.

The Company has classified the determination of fair value of trade receivable from concentrate sales, and derivatives as level 2, as the valuation method used by the Company includes an assessment of assets in quoted markets with significant observable inputs.

	Financial assets (liabilities) at fair value as at December 31, 2011			
	Level 1	**Level 2**	**Level 3**	**Total**
Cash and cash equivalents	**$ 38,730**	**$ -**	**$ -**	**$ 38,730**
Short term investments	**17,000**	**-**	**-**	**17,000**
Trade receivable from concentrate sales	**-**	**11,287**	**-**	**11,287**
Derivatives	**-**	**(17)**	**-**	**(17)**
	$ 55,730	**$ 11,270**	**$ -**	**$ 67,000**

There were no changes in the levels during the year ended December 31, 2011.

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17. Management of Financial Risk (continued)

a) Fair Value of Financial Instruments (continued)

	Financial assets (liabilities) at fair value as at December 31, 2010			
	Level 1	Level 2	Level 3	Total
Cash and cash equivalents	$ 70,298	$ -	$ -	$ 70,298
Short term investments	20,509	-	-	20,509
Trade receivable from concentrate sales	-	12,551	-	12,551
Derivatives	-	(133)	-	(133)
	$ 90,807	$ 12,418	$ -	$ 103,225

There were no changes in the levels during the year ended December 31, 2010.

Accounts receivable includes trade receivable from concentrate sales, provisional price adjustments, and final price adjustments. The fair value of accounts receivable resulting from provisional pricing reflect observable market commodity prices. Resulting fair value changes to accounts receivable are through sales. Transactions involving accounts receivable are with counterparties the Company believes are creditworthy. As such, these accounts receivable are classified within level 2 of the fair value hierarchy.

Derivatives are carried at their fair value, which is determined based on internal valuation models that reflect observable forward market commodity prices. Resulting fair value changes to derivatives are through net gain (loss) on commodity contracts. Transactions involving derivatives are with counterparties the Company believes to be creditworthy.

During the year ended December 31, 2011, there have been no changes in the classification of financial assets and liabilities in levels 1, 2, and 3 of the hierarchy.

b) Currency Risk

The Company is exposed to the financial risk related to the fluctuation of foreign exchange rates. The Company operates in Canada, Peru and Mexico and a portion of its expenses are incurred in Canadian dollars, Nuevo Soles, and Mexican Pesos. A significant change in the currency exchange rates between the United States dollar relative to the other currencies could have a material effect on the Company's income, financial position, or cash flows. The Company has not hedged its exposure to currency fluctuations.

As at December 31, 2011, the Company is exposed to currency risk through the following assets and liabilities denominated in Canadian dollars, Nuevo Soles and Mexican Pesos (all amounts are expressed in thousands of Canadian dollars, thousands of Nuevo Soles or thousands of Mexican Pesos):

17. Management of Financial Risk (continued)

b) Currency Risk (continued)

	December 31, 2011			December 31, 2010		
	Canadian Dollars	**Nuevo Soles**	**Mexican Pesos**	Canadian Dollars	Nuevo Soles	Mexican Pesos
Cash and cash equivalents	**$ 18,457**	S/. **1,396**	**$ 1,758**	$ 54,782	S/. 741	$ 2,201
Accounts receivable and other assets	**42**	**5,657**	**58,939**	71	1,304	42,452
Deposits on long term assets	**-**	**-**	**-**	-	-	24,209
Trade and other payables	**(1,580)**	**(17,993)**	**(24,310)**	(625)	(15,493)	(6,390)
Provisions, current	**-**	**(1,351)**	**(3,163)**	-	-	-
Income tax payable	**-**	**(10,581)**	**-**	-	(11,775)	-
Leases and long term liabilities	**(2,691)**	**-**	**-**	(1,999)	-	-
Provisions	**-**	**(8,079)**	**(17,494)**	-	(9,169)	(19,959)
Total	**14,228**	**(30,951)**	**15,730**	52,229	(34,392)	42,513
Total US$ equivalent	**13,950**	**(11,476)**	**1,125**	52,219	(12,244)	3,440

Based on the above net exposure as at December 31, 2011, and assuming that all other variables remain constant, a 10% depreciation or appreciation of the US dollar against the above currencies would result in an increase or decrease, as follows: impact to other comprehensive income of $1,550 (2010: $5,802) and a net loss of $1,150 (2010: $978).

c) Credit Risk

Credit risk is the risk of an unexpected loss if a customer or third party to a financial instrument fails to meet its contractual obligations. The Company's cash and cash equivalents and short term investments are held through large Canadian, international and foreign national financial institutions. These investments mature at various dates within one year. All of the Company's trade

accounts receivables are held with large international metals trading companies.

The Company holds derivative contracts with financial institutions and in this regard is exposed to counterparty risk. The Company mitigates this risk by transacting only with reputable financial institutions to minimize credit risk.

The Company's maximum exposure to credit risk at December 31, 2011 is as follows:

17. Management of Financial Risk (continued)

c) Credit Risk (continued)

	December 31, 2011	December 31, 2010
Cash and cash equivalents	**$ 38,730**	$ 70,298
Short term investments	**17,000**	20,509
Accounts receivable	**14,391**	12,551
Derivative assets	**70**	-
Due from related parties	**36**	-
GST/HST and value added tax receivable	**4,777**	3,542
	$ 75,004	$ 106,900

The carrying amount of financial assets recorded in the financial statements represents the Company's maximum exposure to credit risk. The Company believes it is not exposed to significant credit risk and overall, the Company's credit risk has not declined significantly from the prior year.

d) Liquidity Risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due. The Company manages liquidity risk by continuing to monitor forecasted and actual cash flows. The Company has in place a planning and budgeting process to help determine the funds required to support the Company's normal operating requirements on an ongoing basis and its development plans. The Company strives to maintain sufficient liquidity to meet its short term business requirements, taking into account its anticipated cash flows from operations, its holdings of cash, short term investments, and its committed liabilities.

The Company expects the following maturities of its financial liabilities (including interest), finance leases, and other contractual commitments:

	Expected payments due by period as at December 31, 2011				
	Less than 1 year	1 - 3 years	4 - 5 years	After 5 years	Total
Trade and other payables	$ 17,156	$ -	$ -	$ -	$ 17,156
Due to related parties	205	-	-	-	205
Derivative liabilities	87	-	-	-	87
Income tax payable	3,923	-	-	-	3,923
Long term liabilities	1,534	2,765	-	-	4,299
Operating leases	696	1,410	1,177	531	3,814
Provisions	734	849	774	3,725	6,082
	$ 24,335	**$ 5,024**	**$ 1,951**	**$ 4,256**	**$ 35,566**

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17. Management of Financial Risk (continued)

d) Liquidity Risk (continued)

Operating leases includes leases for office premises, computer and other equipment used in the normal course of business. Refer to Note 19 c) for details of operating leases.

In 2010, the Company entered into a credit agreement with the Bank of Nova Scotia for a $20 million senior secured revolving credit facility ("credit facility") to be refinanced or repaid on or within two and one-half years or before December 2012. The credit facility is secured by a first ranking lien on Bateas and its assets and bears interest and fees at prevailing market rates. In the event that utilization under the credit facility is less than $10 million, a commitment fee of 1.50% per annum is payable quarterly on the unutilized portion of the available credit facility. No funds were drawn from this credit facility during the year.

e) Interest Rate Risk

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The risk that the Company will realize a loss as a result of a decline in the fair value is limited because the balances are generally held with major financial institutions in demand deposit accounts.

A 10% change in interest rates would cause a $12 change in income on an annualized basis.

f) Metal Price Risk

The Company is exposed to metals price risk with respect to silver, gold, zinc, lead, and copper sold through its mineral concentrate products. The Company mitigates this risk by implementing price protection programs for some of its zinc and lead production through the use of derivative instruments. As a matter of policy, the Company does not hedge its silver production.

18. Segmented Information

All of the Company's operations are within the mining sector, conducted through operations in three countries. Due to geographic and political diversity, the Company's mining operations are decentralized whereby management are responsible for achieving specified business results within a framework of global policies and standards. Country corporate offices provide support infrastructure to the mine in addressing local and country issues including financial, human resources, and exploration support.

Products are silver, gold, lead, zinc and copper produced from mines in Peru and Mexico. Segments have been aggregated where operations in specific regions have similar products, production processes, types of customers and economic environment.

The Company's operating segments are based on the reports reviewed by the senior management group that are used to make strategic decisions. The Chief Executive Officer considers the business from a geographic perspective considering the performance of the Company's business units.

18. Segmented Information (continued)

The segment information provided to the Board of Directors for the reportable segments for the year ended December 31, 2011 and 2010 are as follows:

Reportable Segments	Corporate	Bateas	Cuzcatlan	Total
Year ended December 31, 2011				
Sales to external customers	**$ -**	**$ 97,740**	**$ 12,264**	**$ 110,004**
Silver concentrates	**$ -**	**$ -**	**$ 7,586**	**$ 7,586**
Gold concentrates	**$ -**	**$ -**	**$ 4,678**	**$ 4,678**
Lead concentrates	**$ -**	**$ 80,689**	**$ -**	**$ 80,689**
Zinc concentrates	**$ -**	**$ 15,290**	**$ -**	**$ 15,290**
Copper concentrates	**$ -**	**$ 1,761**	**$ -**	**$ 1,761**
Sales to internal customers	**$ 5,961**	**$ -**	**$ -**	**$ 5,961**
Cost of sales	**$ -**	**$ 42,236**	**$ 6,794**	**$ 49,030**
Depreciation, depletion and amortization	**$ 100**	**$ 7,053**	**$ 2,268**	**$ 9,421**
Selling, general and administrative expenses	**$ 14,352**	**$ 3,920**	**$ 1,568**	**$ 19,840**
Exploration and evaluation costs	**$ 1,715**	**$ -**	**$ -**	**$ 1,715**
Impairment of mineral properties, property, plant and equipment	**$ -**	**$ -**	**$ 1,894**	**$ 1,894**
Interest income	**$ 494**	**$ 297**	**$ 39**	**$ 830**
Interest expense	**$ 306**	**$ 219**	**$ 35**	**$ 560**
Income (loss) before tax	**$ (15,881)**	**$ 52,133**	**$ 2,083**	**$ 38,335**
Income taxes	**$ 183**	**$ 15,804**	**$ 2,815**	**$ 18,802**

Income (loss) for the year	**$ (16,064)**	**$ 36,329**	**$ (732)**	**$ 19,533**
Capital expenditures	**$ 814**	**$ 25,066**	**$ 53,127**	**$ 79,007**

18. Segmented Information (continued)

Reportable Segments	Corporate	Bateas	Cuzcatlan	Total
Year ended December 31, 2010				
Sales to external customers	$ -	$ 74,056	$ -	$ 74,056
Lead concentrates	$	$ 31,180	$ -	$ 31,180
Zinc concentrates	$ -	$ 15,883	$ -	$ 15,883
Copper concentrates	$ -	$ 26,993	$ -	$ 26,993
Sales to internal customers	$ 2,464	$ -	$ -	$ 2,464
Cost of sales	$ -	$ 34,844	$ -	$ 34,844
Depreciation, depletion and amortization	$ 202	$ 6,347	$ -	$ 6,549
Selling, general and administrative expenses	$ 6,941	$ 4,043	$ -	$ 10,984
Exploration and evaluation costs	$ 547	$ -	$ -	$ 547
Interest income	$ 44	$ 449	$ -	$ 493
Interest expense	$ 417	$ 291	$ -	$ 708
Income (loss) before tax	$ (6,491)	$ 34,004	$ -	$ 27,513
Income taxes	$ (47)	$ 11,557	$ -	$ 11,510
Income (loss) for the year	$ (6,444)	$ 22,447	$ -	$ 16,003
Capital expenditures	$ 1,190	$ 14,614	$ 23,961	$ 39,765

Reportable Segments	**Corporate**	**Bateas**	**Cuzcatlan**	**Total**
As at December 31, 2011				
Total assets	**$ 27,843**	**$ 112,746**	**$ 131,017**	**$ 271,606**
Total liabilities	**$ 5,694**	**$ 29,793**	**$ 7,808**	**$ 43,295**
As at December 31, 2010				
Total assets	$ 81,900	$ 74,950	$ 77,020	$ 233,870
Total liabilities	$ 3,404	$ 24,794	$ 3,082	$ 31,280
As at January 1, 2010				
Total assets	$ 25,330	$ 65,439	$ 42,820	$ 133,589
Total liabilities	$ 321	$ 21,037	$ 870	$ 22,228

For the years ended December 31, 2011 three (2010: two) customers, respectively, represented 100% of total sales to external customers.

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18. Segmented Information (continued)

External Sales by Customer and Region	**Years ended December 31, 2011**		2010	
Customer 1	**$ 95,978**	**98%**	$ 47,062	64%
Customer 2	**1,762**	**2%**	26,994	36%
Bateas/Peru	**$ 97,740**	**100%**	$ 74,056	100%
% of total sales	**89%**		100%	
Customer 1	**$ 12,264**	**100%**	$ -	0%
Cuzcatlan/Mexico	**$ 12,264**	**100%**	$ -	0%
% of total sales	**11%**		0%	
Consolidated	**$ 110,004**	**100%**	$ 74,056	100%
% of total sales	**100%**		100%	

19. Contingencies and Capital Commitments

a) Bank Letter of Guarantee

The Caylloma mine closure plan was approved in November 2009 with total closure costs of $3,587 of which $1,756 is subject to annual collateral in the form of a letter of guarantee, to be awarded each year in increments of $146 over 12 years based on the estimated life of the mine.

Banco Bilbao Vizcaya Argentaria, S.A., a third party, has established a bank letter of guarantee on behalf of Bateas in favor of the Peruvian mining regulatory agency in compliance with local regulation associated with the approved Bateas' mine closure plan, for the sum of $439. This bank letter of guarantee expires 360 days from December 2011.

Banco Bilbao Vizcaya Argentaria, S.A. has also established bank letters of guarantee totalling $54 to provide an annual guarantee associated with an office lease contract and truck rentals. These bank letters of guarantee were renewed in June 2011 with expiry 360 days to June 2012.

b) Capital Commitments

As at December 31, 2011, $8,122 of capital commitments not disclosed elsewhere in the consolidated financial statements, and forecasted to be expended within one year, includes the following: $5,800 for the ramp development at the San Jose property located in Mexico; $2,247 for the tailing dam, concentrator plant and electrical infrastructure renewal, and mine camp development at the Caylloma Property; and $75 for software development.

19. Contingencies and Capital Commitments (continued)

c) Other Commitments

The Company has a contract to guarantee power supply at its Caylloma mine. Under the contract, the seller is obligated to deliver a "maximum committed demand" (for the present term this stands at 3,500 Kw) and the Company is obligated to purchase subject to exemptions under provisions of "Force Majeure". The contract is automatically renewed every two years for a period of 10 years and expiring in 2017. Renewal can be avoided without penalties by notifying 10 months in advance of renewal date.

Tariffs are established annually by the energy market regulator in accordance with applicable regulations in Peru.

The Company acts as guarantor to finance lease obligations held by two of its mining contractors. These finance lease contracts are related to the acquisition of mining equipment deployed at the Caylloma mine. As at December 31, 2011, these obligations amounted to $231 with $74 maturing in 2012 and $157 maturing in 2013.

The Company, jointly with Radius Gold Inc., has entered into an office premise lease located in Canada, effective on November 28, 2011, the date the Company commenced carrying on business in the premises. The shared office with Radius has been finalized with the Company obligated to pay 50% of the total rent payable. The lease term is eight years with the Company's annual net rent payable, on 3,195 rentable square feet, as follows:

- years one to two $111;
- years three to five $115; and,
- years six to eight $118.

In addition, estimated operating costs, utilities, and realty taxes is $71 in the first year of occupancy. During 2011, the Company has advanced 50% of the three month security deposit in the amount of $47.

On May 24, 2010, the Company entered into a seven year office premise lease located Peru. The annual rent payable on 1,717 rentable square meters for office space, is as follows:

- year one $289;
- year two $297;
- year three $306; and,
- years four through seven the lease is subject a minimum annual increase of 3% or the Consumer Price Index published by Bureau of Labor Statistics of the United States Department of Labor, whichever is higher.

The lease also includes the use of additional space for mini-warehouse and parking spots, the obligation for which is $58 per annum for the first year and is subject to an annual increase of 3% as stated above until the end of the lease.

As at December 31, 2011, the Company has advanced rent $159 (2010:$426) and provided a security deposit of $44.

19. Contingencies and Capital Commitments (continued)

c) Other Commitments (continued)

On March 15, 2011, the Company entered into a one year office premise lease located in Mexico with an annual lease obligation of $37. The office premise leases are included as operating leases in Note 17 d).

	Expected payments due by period as at December 31, 2011				
	Less than 1 year	1 – 3 years	4 – 5 years	After 5 years	Total
Office premises – Canada	181	549	372	359	1,461
Office premises – Peru	363	758	805	172	2,098
Office premises – Mexico	8	-	-	-	8
Total office premises	**$ 552**	**$ 1,307**	**$ 1,177**	**$ 531**	**$ 3,567**
Computer equipment – Peru	128	75	-	-	203
Computer equipment – Mexico	16	28	-	-	44
Total computer equipment	**$ 144**	**$ 103**	**$ -**	**$ -**	**$ 247**
Total operating leases	**$ 696**	**$ 1,410**	**$ 1,177**	**$ 531**	**$ 3,814**

d) Other Contingencies

In February 2009, the Environmental Assessment and Oversight Agency ("OEFA") in Peru, alleged the Company had five violations: two were for breaches of recommendations; two for excess of total suspended solids in water over the maximum allowable; and an alleged unauthorized discharge of effluent. The Ministry of Energy and Mines in Peru ("OSINERGMIN") decided to close the two alleged violations for failure to adopt recommendations and punish the Company for the three alleged violations and imposed a fine of $200 in 2010. The Company appealed on June 23, 2010. Subsequent to December 31, 2011 and on February 22, 2012, the alleged unauthorized discharge of effluent was dismissed and confirmed a fine of $133 for the two alleged violations of excess of total suspended solids in water over the maximum allowable. The Company is proceeding with an administrative appeal to the Ministry of Energy and Mines in Peru ("OSINERGMIN") for the remaining two alleged offenses. The Company believes it is more likely than not that it will defend itself successfully in the claims and therefore has not recorded a provision for the potential exposure relating to these alleged violations.

20. Net Finance Income (Expense)

	Years ended December 31,	
	2011	2010
Finance income		
Interest income on FVTPL financial assets	**$ 830**	$ 493
Total finance income	**830**	493
Finance expenses		
Interest expense	**81**	128
Standby and commitment fees	**306**	417
Accretion of provisions (Note 12)	**173**	163
Total finance expense	**560**	708
Net finance income (expense)	**$ 270**	$ (215)

21. Expenses by Nature

	Years ended December 31,

		2011		2010
Costs of sales				
Direct mining costs [1]	**$**	**38,649**	$	27,729
Depreciation and depletion		**9,059**		6,327
Royalty expenses		**1,322**		788
Total cost of sales	**$**	**49,030**	$	34,844

[1] Direct mining costs includes salaries and other short term benefits, contractor charges, energy, consumables and production related costs.

	Years ended December 31,			
		2011		2010
Selling, general and administrative expenses				
Salaries and benefits		**12,168**		5,312
Corporate administration		**3,409**		2,253
Audit, legal and professional fees		**2,915**		2,414
Filing and listing fees		**467**		311
Director's fees		**519**		472
Depreciation		**362**		222
Total selling, general and administrative expenses	**$**	**19,840**	$	10,984

	Years ended December 31,			
		2011		2010
Exploration and evaluation costs				
Brownfields exploration	**$**	**206**	$	160
Greenfields exploration		**344**		253
		550		413
Evaluation costs		**1,165**		134
Total exploration and evaluation costs	**$**	**1,715**	$	547

22. Subsequent Events up to March 23, 2012

Subsequent to December 31, 2011 and at March 23, 2012 the value of the DSU and RSU liabilities have increased by $832 and $622, respectively.

On February 17, 2012, the Company entered into a one year office premise lease, effective March 1, 2012, located in Mexico with an annual lease obligation of $18.

23. First-time Adoption of IFRS

IFRS 1 *First-time Adoption of International Financial Reporting Standards*, which governs the first-time adoption of IFRS, in general requires accounting policies to be applied retrospectively to determine the opening financial position at the Company's transition date of January 1, 2010, and allows certain exemptions on the transition to IFRS. The elections the Company has decided to apply and that are considered significant to the Company include:

- Business Combinations Exemption
  - IFRS 1 allows a first-time adopter to not apply of IFRS 3 retrospectively to business combinations that occur before either the date of transition to IFRS or an alternative pre-transition date.
  - The Company elected the business combinations exemption in IFRS 1 to not apply IFRS 3 retrospectively to past business combinations. Accordingly, the Company has not restated business combinations that took place prior to the transition date.
- Share-Based Payment Exemption
  - IFRS 1 gives a first-time adopter the option to not apply IFRS 2 Share-Based Payment to (i) equity instruments that were granted for the periods on or before November 7, 2002 or after November 7, 2002 but that vested before the date of transition to IFRS and (ii) liabilities arising from cash-settled share-based payment transactions if those liabilities were settled before January 1, 2005 or before the date of transition to IFRS.
  - The Company elected to apply this exemption at the transition date.
- Cumulative Translation differences
  - IFRS 1 gives a first-time adopter through IAS 21 The Effects of Changes in Foreign Exchange Rates which allows for the cumulative translation differences that existed at the date of transition to IFRS to be reset to zero.

- The Company elected to set the previously accumulated cumulative translation amount, which was included in accumulated other comprehensive income ("AOCI"), to zero as at the date of transition with the balance being reclassified to retained earnings.

· Borrowing Costs Exemption
  - This exemption in IFRS 1 allows a first-time adopter to apply the transitional provisions set out in IAS 23 Borrowing Costs at January 1, 2009 or the date of transition to IFRS, whichever is later. IAS 23 requires the capitalization of borrowing costs related to all qualifying assets.
  - The Company elected to apply IAS 23 to borrowing costs relating to all qualifying assets for which the commencement date for capitalization is on or after the transition date.

· Decommissioning Liability Exemption
  - IFRS 1 indicates that a first-time adopter may elect not to apply IFRIC 1 Changes in Existing Decommissioning, Restoration and Similar Liabilities retrospectively.

23. First-time Adoption of IFRS (continued)

- The Company elected to take a simplified approach to calculate and record the asset related to the decommissioning and restoration liability on our opening IFRS consolidated statement of financial position. The decommissioning and restoration liability calculated on the transition date in accordance with IFRS 37 Provisions, Contingent Liabilities and Contingent Assets was discounted back to the date when the provision first arose on the mineral property, at which date the corresponding asset and liability was set up and then depreciated to its carrying amount at the transition date.

The IFRS 1 mandatory exceptions applied by the Company in the conversion from Canadian Generally Accepted Accounting Principles ("CAD GAAP") to IFRS included estimates. In accordance with IFRS 1, an entity's estimates under IFRS at the date of transition to IFRS must be consistent with estimates made for the same date under previous GAAP unless those estimates were in error. The Company's IFRS estimates as at the Transition Date are consistent with its CAD GAAP estimates as at that date.

Adjustments on transition to IFRS

Adoption of IFRS resulted in changes to the Company's Statements of Financial Position, Statements of Income, Statements of Comprehensive Income (Loss), Statements of Cash Flows, and Statements of Changes in Equity as set out below:

a) Foreign Exchange

Under IAS 21, each entity in a group must be analyzed, through application of primary and secondary factors, to determine its functional currency. Based on this assessment, the functional currency of each of the entities in the group is the US$, with the exception of the parent entity and certain holding companies which have a Canadian dollar functional currency. Under CAD GAAP, the parent entity had a Canadian dollar presentation currency and all subsidiaries were integrated with the exception of Bateas which was self-sustaining. The presentation currency will continue to be US$.

The parent entity and the holding companies which have a CAD$ functional currency will be translated to US$ using the closing rate method with the differences to the cumulative translation adjustment account, on consolidation. Those entities with a US$ functional currency do not require translation on consolidation. Under CAD GAAP, the Company used the indirect consolidation method whereby all entities were first translated to CAD$ and then the entire consolidation translated to US$ for presentation purposes.

b) Deferred Income Tax

Under IFRS, income taxes include all domestic and foreign taxes based on taxable profits. The Company accounted for Peruvian statutory workers participation under CAD GAAP as an income tax. Under IFRS the statutory workers participation is accounted for as an employee benefit under IAS 19. Accordingly, future Peruvian Workers Participation balances have been derecognized and current Peruvian Workers Participation expense has been reclassified from income tax expense to operating expenses.

FORTUNA SILVER MINES INC.
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(All amounts in US$'000's unless otherwise stated)

23. First-time Adoption of IFRS (continued)

Adjustments on transition to IFRS (continued)

b) Deferred Income Tax (continued)

Under IFRS, deferred tax is recognized on the difference between the accounting basis and tax basis of all items. Under CAD GAAP income tax assets or liabilities were not recognized for differences arising between the historical exchange rate and the current exchange rate translation of the cost of non-monetary assets or liabilities of integrated foreign operations.

For foreign currency non-monetary assets or liabilities where the tax basis currency differs from the functional currency of the entity, foreign exchange differences will result in tax assets or liabilities which were not previously recognized under CAD GAAP. This difference will result in added volatility in the tax expense as foreign exchange rate changes will have an impact on the tax expense.

IAS 12 does not permit recognition of temporary differences on the initial acquisition of assets that do not constitute a business combination. There is no similar prohibition under CAD GAAP. Deferred tax arising from temporary differences on initial recognition have been reversed against mineral properties, property, plant and equipment and retained earnings.

c) Reset Accumulated Other Comprehensive Income to Zero

The Company has taken the exemption under IFRS 1 which allows for the cumulative translation differences that existed at the date of transition to IFRS to be reset to zero.

d) Provisions

Where a provision is recognized, IFRS requires the estimate to be discounted at a risk-free pre-tax rate, typically that of a government bond that is matched to the expected risk adjusted cash flows. On transition, the Company used a risk free rate to discount their decommissioning liabilities and this results in an increased decommissioning liability being recognized under IFRS as compared to CAD GAAP.

23. First-time Adoption of IFRS (continued)

Adjustments on transition to IFRS (continued)

e) Reclassification of items in the Consolidated Statements of Income

The Company has reclassified the following income and expense items in the consolidated statements of income:

- government royalties to cost of sales from selling, general and administrative expenses;
- distribution costs to cost of sales from selling, general and administrative expenses;
- community relation costs to cost of sales from selling, general and administrative expenses;
- other income and expenses from interest and other income and expenses to selling, general and administrative expenses;
- interest expense includes interest on debt financing and accretion of provisions;
- current workers participation from income tax to cost of sales and selling, general and administrative expenses; and,
- depletion and depreciation combined with cost of sales.

In addition, exploration and evaluation costs moved from selling, general and administrative expenses.

The above changes are reclassifications within our statement of income so there is no net impact to our income as a result of these changes.

f) Reconciliation of Consolidated Statements of Changes in Equity

The reconciliations between the CAD GAAP and IFRS consolidated Equity, for January 1, 2010 and December 31, 2010 are provided below:

Expressed in $ '000's	January 1, 2010	December 31, 2010
Equity, CAD GAAP	$ 112,557	$ 206,008

Adjustments:			
Effect of foreign exchange on inventory, deposits on long term assets, and mineral properties, property, plant and equipment	**23 a)**	(2,538)	(5,339)
Deferred income tax adjustments	**23 b)**	1,475	1,944
Transfer of accumulated other comprehensive income to retained earnings	**23 c)**	2,898	2,898
Reset accumulated other comprehensive income to zero	**23 c)**	(2,898)	(2,898)
Adjustment to revise provisions	**23 d)**	(311)	(254)
Adjustment for depletion on mineral properties related to provisions	**23 d)**	178	231
Total IFRS adjustments to Equity		**(1,196)**	**(3,418)**
Equity, IFRS		**$ 111,361**	**$ 202,590**

23. First-time Adoption of IFRS (continued)

g) Reconciliation of Consolidated Statement of Financial Position

The reconciliations between the CAD GAAP and IFRS consolidated statement of financial position at December 31, 2010 (date of transition to IFRS) are provided below.

		December 31, 2010		
	Notes	**Canadian GAAP**	**Effect of Transition to IFRS**	**IFRS**
ASSETS				
CURRENT ASSETS				
Cash and cash equivalents		$ 70,298	$ -	$ 70,298
Short term investments		20,509	-	20,509
Accounts receivable and other assets		13,454	-	13,454
GST/HST and value added tax receivable		3,542	-	3,542
Inventories	**23 a)**	4,034	(16)	4,018
		111,837	(16)	111,821
NON-CURRENT ASSETS				
Deposits on long term assets	**23 a)**	4,533	153	4,686
Mineral properties, property, plant and equipment	**23 a) b) d)**	126,813	(9,450)	117,363
Total assets		$243,183	$ (9,313)	$ 233,870
LIABILITIES AND EQUITY				
CURRENT LIABILITIES				
Trade and other payables		$ 9,303	$ -	$ 9,303
Due to related parties		40	-	40
Derivative liabilities		133	-	133
Income tax payable		4,192	-	4,192
Current portion of long term liability		1,083	-	1,083
		14,751	-	14,751
NON-CURRENT LIABILITIES				
Leases and long term liabilities		3,166	-	3,166
Provisions	**23 d)**	4,924	(43)	4,881
Deferred income tax liabilities	**23 b) d)**	14,334	(5,852)	8,482
		37,175	(5,895)	31,280
EQUITY				
Share capital		180,403	-	180,403
Share option and warrant reserve		11,116	-	11,116
Retained earnings (deficit)	**23 a) b) c) d)**	3,597	4,751	8,348
Accumulated other comprehensive income	**23 c)**	10,892	(8,169)	2,723
		14,489	(3,418)	11,071
		206,008	(3,418)	202,590
		$243,183	$ (9,313)	$ 233,870

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(All amounts in US$'000's unless otherwise stated)

23. First-time Adoption of IFRS (continued)

h) Reconciliations of Consolidated Statement of Income

The reconciliation between the CAD GAAP and IFRS consolidated statement of income for the year ended December 31, 2010 are provided below:

		Year ended December 31, 2010		
	Notes	CAD GAAP	Effect of Transition to IFRS	IFRS
Sales	23 e)	$ 74,056	-	$ 74,056
Cost of sales	23 d) e)	29,129	5,715	34,844
Mine operating income (loss)		44,927	(5,715)	39,212
Other expenses				
Selling, general and administrative expenses	23 a) e)	16,529	(5,545)	10,984
Exploration and evaluation costs	23 e)	547	-	547
Net (gain) on commodity contracts		(736)	-	(736)
Loss on disposal of mineral properties, property, plant and equipment		127	-	127
Loss on disposal of investment		119	-	119
Write-off of deferred exploration costs		443	-	443
Operating income (loss)		27,898	(170)	27,728
Finance items				
Interest income	23 d) e)	(379)	872	493
Interest expense	23 e)	(544)	(164)	(708)
Net finance income (expense)		(923)	708	(215)
Income before tax		26,975	538	27,513
Income taxes	23 b) d) e)	14,020	(2,510)	11,510
Income for the year		$ 12,955	$ 3,048	$ 16,003

23. First-time Adoption of IFRS (continued)

i) Reconciliation of Consolidated Statement of Comprehensive Income

The reconciliation between the CAD GAAP and IFRS consolidated statement of comprehensive income for the year ended December 31, 2010 are provided below:

		Year ended December 31, 2010		
	Notes	CAD GAAP	Effect of Transition to IFRS	IFRS
Income for the year		$ 12,955	$ 3,048	$ 16,003
Other comprehensive income (loss)				
Transfer of unrealized loss to realized loss upon reduction of net investment, net of taxes	23 c)	2,100	(2,100)	-
Unrealized (loss) gain on translation to presentation currency on foreign operations	23 a)	5,895	(3,172)	2,723
Other comprehensive (loss) income		7,994	(5,271)	2,723
Total comprehensive (loss) income for the year		$ 20,949	$ (2,223)	$ 18,726

j) Reconciliation of Consolidated Statement of Cash Flows

The adoption of IFRS has had no material impact on the net cash flows of the Company. The changes made to the Consolidated Statement of Financial Position and Consolidated Statement of Comprehensive Income has resulted in reclassifications of various amounts on the Consolidated Statement of Cash Flows, however as there have been no material changes to the net cash flows, summarized reconciliation has been presented below.

		Year ended December 31, 2010		
	Notes	CAD GAAP	Effect of Transition to IFRS	IFRS
Effect of exchange rate changes on cash and cash equivalents	**23 a)**	2,128	23	2,151
(**DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS**	**23 a)**	37,407	(23)	37,384
Cash and cash equivalents - beginning of year		30,763	-	30,763
CASH AND CASH EQUIVALENTS - END OF YEAR		$ 70,298	$ -	$ 70,298

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MANAGEMENT'S DISCUSSION AND ANALYSIS

FOR THE

YEAR ENDED DECEMBER 31, 2011

As at March 23, 2012

(Dollar amounts expressed in US dollars, unless otherwise indicated)

FORTUNA SILVER MINES INC.
Management's Discussion and Analysis
For the year ended December 31, 2011
(Dollar amounts expressed in US dollars, unless otherwise indicated)

Management's Discussion and Analysis ("MD&A") is intended to help the reader understand the significant factors that have affected Fortuna Silver Mines Inc. and its subsidiaries' ("Fortuna" or the "Company") performance and such factors that may affect its future performance. For a comprehensive understanding of Fortuna's financial condition and financial performance, this MD&A should be read in conjunction with the Company's audited consolidated financial statements for year ended December 31, 2011 and the related notes contained therein. The Company reports its financial position, financial performance and cash flows in accordance with the International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB"). This MD&A refers to various non-GAAP financial measures, such as cash cost per tonne of processed ore, cash cost per ounce of payable silver, adjusted net income (loss), cash generated by operating activities before changes in working capital, income taxes, and interest income, used by the Company to manage and evaluate operating performance and ability to generate cash and are widely reported in the silver mining industry as benchmarks for performance, but do not have a standardized meaning and may differ from methods used by other companies with similar descriptions. The Company believes that certain investors use these non-GAAP financial measures to evaluate the Company's performance. Accordingly, non-GAAP financial measures should not be considered in isolation or as a substitute for measures of performance prepared in accordance with IFRS. To facilitate a better understanding of these measures as calculated by the Company, we have provided detailed descriptions and reconciliations as required.

This document contains forward-looking statements. Please refer to the cautionary language under the heading "Cautionary Statement on Forward-Looking Statements".

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Business of the Company

Fortuna is engaged in silver mining and related activities, in Latin America, including exploration, extraction, and processing. The Company operates the Caylloma zinc/lead/silver mine in southern Peru and the San Jose silver/gold mine in Mexico.

Fortuna is a publicly traded company incorporated and domiciled in Canada and is listed on the New York Stock Exchange under the trading ticker symbol "FSM", and on the Toronto Stock Exchange and Lima Stock Exchange under the trading ticker symbol "FVI".

The Company's registered office is at Suite 650, 200 Burrard Street, Vancouver, British Columbia, Canada, V6C 3L6.

The financial results include the accounts of the Company and wholly owned subsidiaries: Minera Bateas S.A.C. ("Bateas"); Fortuna Silver (Barbados) Inc.; Compania Minera Cuzcatlan SA ("Cuzcatlan"); Continuum Resources Ltd. ("Continuum"); Fortuna Silver Mines Peru S.A.C. ("FSM Peru"); and Fortuna Silver Mexico, S.A. de CV. ("FS Mexico").

Recent Developments and 2011 Highlights

Fatal Accident Report

It is with great sorrow the Company informs that on February 26, 2012 a fatal accident claimed the life of a driller and injured a supervisor, both working for the Company's mine contractor operating the Animas vein on Level 12 of the Caylloma mine. All mine operations were stopped immediately. The supervisor is in stable condition and recovering in a hospital in Arequipa. Mine operations resumed on February 28, 2012. Fortuna´s senior operations management team traveled to the mine site the same day of the accident

and a corporate investigation of this tragic accident was launched. Findings indicate the crew of contractors suffered a premature detonation on a round of rib and ditch blast. Levels of responsibility and breaches of safety regulations and procedures that led to the accident were identified as a result of the investigation. Under the recommendations of the investigation report, Fortuna is implementing companywide measures to ensure additional safeguards are in place against violations of safety regulations and procedures.

This is the first tragic accident in the history of Fortuna´s operations. The Company has a culture of zero tolerance for insecure acts and conditions and is acting accordingly.

Financial and Operating Results

During the quarter ended December 31, 2011, the Company generated a net loss of $1.76 million (Q4 2010: income $4.33 million) on operating income of $4.44 million (Q4 2010: $8.03 million) and sales of $31.05 million (Q4 2010: $23.91 million).

During the year ended December 31, 2011, the Company generated a net income of $19.53 million (2010: income $16.00 million) on operating income of $38.07 million (2010: $27.73 million) and sales of $110.00 million (2010: $74.06 million).

Silver ounces produced during the quarter ended December 31, 2011 were 913,803 (Q4 2010: 481,802) ounces, 90% above the prior year. Gold ounces produced during the quarter ended December 31, 2011 were 4,153 (Q4 2010: 1,822) ounces, 128% above the prior year.

Silver ounces produced during the year ended December 31, 2011 were 2,486,655 (2010: 1,906,423) ounces, 30% above the prior year. Gold ounces produced during the year ended December 31, 2011 were 6,843 (2010: 2,556) ounces, 168% above the prior year.

During the quarter ended December 31, 2011 silver comprised 68% (Q4 2010: 55%) of revenue and the realized silver price was $27.64 (Q4 2010: $23.73) per ounce. San Jose contributed to our consolidated revenue stream for the full quarter after commencing operations in September 2011. As at the end of 2011, San Jose had accumulated approximately $4.4 million worth of silver-gold concentrate inventory based on average prices for the quarter. Consolidated cash cost per ounce, for the quarter, net of by-product credits, was $5.11 (Q4 2010: negative $6.31). Refer to cash cost per silver ounce and cash cost per tonne (non-GAAP financial measures) for reconciliation of cash cost to the cost of sales.

During the year ended December 31, 2011 silver comprised 65% (2010: 49%) of revenue and the realized silver price was $31.11 (2010: $18.18) per ounce. Consolidated cash cost per ounce, for the year, net of by-product credits, was $0.37 (2010: negative $5.99). Refer to cash cost per silver ounce and cash cost per tonne (non-GAAP financial measures) for reconciliation of cash cost to the cost of sales.

Cash generated by operating activities before changes in working capital, income taxes, and interest income for the year ended December 31, 2011 totalled $53.35 million, up from $31.34 million in 2010.

Commercial production at the San Jose silver and gold mine was delivered on September 1, 2011 on-time and on-budget after fifteen months of construction and commissioning. The mine and mill are operating within design parameters at a rate of 1,000 tpd with a planned investment in infrastructure, in 2012 and 2013, to expand to 1,500 tpd by Q3 2013. Cash cost per Ag oz, net of by-product credits, for 2011 was $4.51.

Corporate Highlights

On April 19, 2011 the Company announced changes to the Board of Directors with the appointment of Mr. Thomas Kelly and the resignation of Mr. Jeffrey Franzen.

On May 26, 2011 Mr. Jorge Ganoza Aicardi resigned as Vice-President, Operations. Effective August 1, 2011 Mr. Manuel Ruiz-Conejo, previously Vice-President, Project Development was appointed to the position.

The Company's common shares began trading on the New York Stock Exchange ("NYSE") at the opening of trading on Monday, September 19, 2011 (refer to Sedar.com for releases dated August 29, 2011 and September 15, 2011).

Effective at the market open on December 19, 2011, the Company was added to the S&P/TSX Composite.

Results of Operations

Consolidated Metal Production

	QUARTERLY RESULTS		YEAR TO DATE RESULTS	
	Three months ended December 31,		Years ended December 31,	
	2011	2010	**2011**	2010
Consolidated Metal Production	**Consolidated**	Consolidated	**Consolidated**	Consolidated
Silver (Oz)*	**913,803**	481,802	**2,486,655**	1,906,423
Gold (Oz)*	**4,153**	1,822	**6,843**	2,556
Lead (000's lb)	**4,396**	5,338	**19,678**	21,373
Zinc (000's lb)	**5,688**	6,158	**23,425**	26,137
Copper (000's lb)	**0**	987	**36**	4,596

* Caylloma: Silver in lead and copper concentrates; San Jose: Silver in silver and gold concentrates

The Company's silver production in Q4 of 2011 was 90% higher than Q4 2010 as a result of higher silver production from Caylloma of 11% and the contribution from San Jose for its first full quarter under commercial operations.

The Company´s silver production in 2011 was 30% higher than in 2010 as a result of higher silver production from Caylloma of 5% and

the contribution from San Jose for the second half of the year.

Consolidated Production Highlights for Q4 2011:

- Silver production of 913,803 ounces; 90% increase over Q4 2010;
- Gold production of 4,153 ounces; 128% increase over Q4 2010;
- Lead production of 4,396 (000's) pounds; 18% decrease over Q4 2010, and,
- Zinc production of 5,688 (000's) pounds; 8% decrease over Q4 2010.

Consolidated Production Highlights for 2011:

- Silver production of 2.49 million ounces; 30% increase over 2010;
- Gold production of 6,843 ounces; 168% increase over 2010;
- Lead production of 19,678 (000's) pounds; 8% decrease over 2010, and,
- Zinc production of 23,425 (000's) pounds; 10% decrease over 2010.

Caylloma Mine Production

	QUARTERLY RESULTS		YEAR TO DATE RESULTS	
	Three months ended December 31,		Years ended December 31,	
	2011	2010	**2011**	2010
	Caylloma	Caylloma	**Caylloma**	Caylloma
Mine Production				
Silver*				
Grade (g/t)	**177.42**	159.51	**170.91**	159.24
Recovery %*	**80.82**	83.69	**81.43**	85.67
Production (Oz)*	**536,426**	481,802	**2,008,488**	1,906,423
Gold				
Grade (g/t)	**0.35**	0.40	**0.36**	0.40
Recovery %*	**44.97**	51.00	**45.71**	46.28
Production (Oz)*	**591**	734	**2,393**	2,556
Lead				
Grade (%)	**1.85**	2.37	**2.15**	2.44
Recovery %	**92.39**	90.93	**92.68**	91.28
Production (000's lb)	**4,396**	5,338	**19,678**	21,373
Zinc				
Grade (%)	**2.47**	2.87	**2.68**	3.10
Recovery %	**89.73**	86.77	**88.46**	87.99
Production (000's lb)	**5,688**	6,158	**23,425**	26,137
Copper				
Production (000's lb)	**0**	987	**36**	4,596
Unit Costs				
Production cash cost (US$/oz ag)**	**6.67**	(6.31)	**(0.59)**	(5.99)
Production cash cost (US$/tonne)	**79.68**	64.55	**68.98**	58.43
Unit Net Smelter Return (US$/tonne)	**188.42**	185.96	**217.70**	163.59

*** Caylloma: Silver in lead and copper concentrates**
**** Net of by-product credits**

Summary of Q4 2011 Caylloma Mine Production Results:

- Silver production of 536,426 ounces; 11% increase over Q4 2010;
- Gold production of 591 ounces; 68% decrease over Q4 2010;
- Lead production of 4,396 ('000's) pounds; 18% decrease over Q4 2010;
- Zinc production of 5,688 ('000's) pounds, 8% decrease over Q4 2010; and,
- Cash cost per silver ounce, net of by-product credits, $6.67 (refer to cash cost per silver ounce and cash cost per tonne (non-GAAP financial measures) for reconciliation of cash cost to the cost of sales).

Summary of 2011 Caylloma Mine Production Results:

- Silver production of 2,008,488 ounces; 5% increase over 2010;
- Gold production of 2,319 ounces; 9% decrease over 2010;
- Lead production of 19,678 ('000's) pounds; 8% decrease over 2010;
- Zinc production of 23,425 ('000's) pounds; 10% decrease over 2010; and,
- Cash cost per silver ounce, net of by-product credits, negative $0.59 (refer to cash cost per silver ounce and cash cost per tonne (non-GAAP financial measures) for reconciliation of cash cost to the cost of sales).

Discussion on Caylloma Mine Operations

Silver production at Caylloma for the year was 2,008,488 ounces with mill feed being sourced mainly from the Animas (88%), Bateas (6%), and Soledad (5%) veins. The increase in silver production for the year compared to the same period last year was achieved through higher throughput and head grades in spite of a decrease in metallurgical recovery rates of 5%. Higher grades are a result of an increase in mill feed contribution from the high silver grade ore shoot on level 6 in Animas vein and bonanza ore from Bateas vein. The reduction in metallurgical recoveries is a result of mixed sulfide-oxide material on level 6 of the animas vein.

In January 2011, production of copper-silver concentrate was discontinued at Caylloma due to a material deterioration in treatment and refining smelter charges with respect to 2010. The Company is monitoring market conditions to evaluate restarting the circuit. Copper accounted for 0.18% of sales in 2011 (2010: 3.68%).

The new high-grade silver ore shoots that were discovered through the extension of exploration and development drifts from current production areas on the 10th and 12th levels of the Bateas Vein (refer to press release dated April 14, 2011) entered into production in late June. Exploration drifting towards the northeast area of the Bateas Vein was stopped by the end of September 2011 in order to improve ventilation and infrastructure for auxiliary services in levels 10 and 12. By mid December 2011, a ventilation shaft from surface to level 12 was completed, and two more shafts between levels 10 and 12 should be completed by the end of March 2012 to resume exploration drifting.

In June 2011, the Company received the approval of the environmental impact study for the construction of a plant expansion to 1,500 tpd encompassing a new tailings facility. The construction of the tailings dam for the first two years of operation concluded in late 2011. The tailings pipeline and pumping system is scheduled for completion in June 2012. Total design capacity of the tailings facility including future expansions is for 9 years of operation at the current mill throughput rate.

In May 2011, the Company submitted to the Ministry of Energy and Mines ("MEM"), in Peru, the application for construction permit of the tailings facility. Approval of this permit has not been received as of March 23, 2012. All technical and surface rights observations made by MEM in November 2011 have been addressed and the Company is awaiting final resolution. Although the Company is working closely with MEM and expects to receive the permits on time, the delay in obtaining this permit represents a risk for the commissioning of the new tailings facility in June 2012 which could lead to a subsequent temporary stoppage of operations.

Cash cost per payable ounce of silver, for the year ended December 31, 2011, was negative $0.59 net of by-product credits compared to negative $5.99 in 2010. This increment was driven by a cash cost increase and lower base metal credits in the second half of 2011, with special emphasis in the fourth quarter. Cash cost per oz throughout 2011 went from negative $5.82 in Q1 2011 to $6.67 in Q4 2011. The sharp increment throughout the year is explained by a decrease in by-product credits of $9.40/oz and a 29% unit cash cost per tonne increase. The decrease in by-product credits was primarily due to lower base metal prices (lead 24%, zinc 21%) and lower lead production (13%). The unit cost increments reflect cost increases in qualified labor and industry related services that have been mounting in the Peruvian underground mining industry since late 2010. For 2012, the Company anticipates cost pressures to continue; several productivity and cost control initiatives are included in the 2012 operational and capital budgets.

Capital expenditures for the year ended December 31, 2011 amounted to $17.1 million. The main components were the first phase of the new tailings facility ($7.8 million), mine development ($3.7 million), and camp infrastructure and ancillary facilities ($1.7 million).

Capital expenditures budgeted for the year 2012 amount to $25.1 million which includes the second phase of the new tailings facility ($4.8 million), upgrading of the processing plant ($8.2 million), mine camp improvements ($4.8 million), and mine development ($4.5 million).

A total of 10,551 meters were drilled in Caylloma in 2011 with close to 50% of the program allocated to Animas vein and the other 50% distributed among high grade silver targets at La Plata, San Cristobal, and Bateas veins. A total of 3,642 meters of exploration drifting were done with 50% allocated to Bateas and San Cristobal veins, and 40% allocated to Animas vein.

The brownfields exploration budget for 2012, amounts to $7.2 million including 3,552 meters of drifting and 16,000 meters of drilling.

Cash cost is a non-GAAP financial measure, refer to cash cost per silver ounce and cash cost per tonne (non-GAAP financial measures) for reconciliation of cash cost to the cost of sales.

*San Jose Mine Production****

	QUARTERLY RESULTS		YEAR TO DATE RESULTS	
	Three months ended December 31,		Years ended December 31,	
	2011	2010	**2011**	2010
	San Jose	San Jose	**San Jose**	San Jose
Mine Production				
Tonnes milled	**87,884**	0	**116,410**	0
Average tons milled per day	**955**	0	**954**	0
Silver*				
Grade (g/t)	**159.00**	0.00	**150.40**	0.00
Recovery %*	**84.00**	0.00	**84.95**	0.00
Production (Oz)*	**377,377**	0	**478,167**	0
Gold				
Grade (g/t)	**1.48**	0.00	**1.43**	0.00
Recovery %*	**84.90**	0.00	**84.62**	0.00
Production (Oz)*	**3,562**	0	**4,524**	0
Unit Costs				
Production cash cost (US$/oz ag)**	**2.85**	na	**4.51**	na
Production cash cost (US$/tonne)	**47.16**	na	**50.73**	na
Unit Net Smelter Return (US$/tonne)	**147.31**	0.00	**147.33**	0.00

*** San Jose: Silver in gold concentrates**
**** Net of by-product credits**
*****From commercial production, which commenced on September 1, 2011**

Summary of Q4 2011 San Jose Mine Production Results:

- Silver production of 377,377 ounces;
- Gold production of 3,562 ounces; and,
- Cash cost per silver ounce, net of by-product credits, $2.85 (refer to cash cost per silver ounce and cash cost per tonne (non-GAAP financial measures) for reconciliation of cash cost to the cost of sales).

Summary of 2011 San Jose Mine Production Results:

- Silver production of 478,167 ounces;
- Gold production of 4,524 ounces; and,
- Cash cost per silver ounce, net of by-product credits, $4.51 (refer to cash cost per silver ounce and cash cost per tonne (non-GAAP financial measures) for reconciliation of cash cost to the cost of sales).

Discussion on San Jose Mine Operations

Production at the San Jose silver and gold mine commenced on September 1, 2011 on-time and on-budget after fifteen months of construction and commissioning. The mine and mill are operating within design parameters at a rate of 1,000 tpd with a planned investment in infrastructure, in 2012 and 2013, to expand to 1,500 tpd by Q3 2013. Cash cost per tonne of processed ore was $50.73.

Mine production is currently taking place above level 1,400 on blocks K, L, and M with production targets being met according to plan. Production in level 1,300 is scheduled to commence during the second quarter of 2012, 3 months ahead of the original mine plan. As of the end of the second week of March 2012, the main ramp reached the 1,300 meter elevation where production blocks C and D will be developed by year end as the mine moves towards the planned expansion of 1,500 tpd.

The plant is processing ore at an average throughput rate of 1,000 tpd. Metallurgical recovery is still undergoing an adjustment process and remains within 95% of design parameters. Concentrate grade is already at planned levels for the current head grades.

Capital expenditures budgeted for the year 2012, amounts to $30.7 million which includes a new concentrate leaching facility to produce dore bars ($12 million), ramp and mine development ($9.2 million), tailings dam expansion to support 1,500 tpd ($4.5 million), processing plant expansion ($1.6 million), a hydraulic fill plant and the underground power grid ($2.6 million).

A total of 13,527 meters were drilled in San Jose and our surrounding properties in 2011 with 60% of the program directed to test the southern extension of the San Jose deposit ("San Ignacio") and the balance allocated to new target zones Taviche and El Rancho. A follow up program for San Ignacio in 2012 will continue testing for extensions of mineralization open to the south of existing reserves.

The 2012 brownfields program amounts to $5.8 million including over 15,000 meters of drilling.

Violent acts have claimed the life of two members of the San Jose del Progreso community on January 18 and March 15, 2012. These murders are being investigated by local authorities and mourned by the entire community. Continuous violence in Mexico and in the state of Oaxaca is a concern for the Company. Security measures are being taken to ensure the safeguard of our personnel.

Cash cost, cash cost per silver ounce, and cash cost per tonne are non-GAAP financial measures, refer to cash cost per silver ounce and cash cost per tonne (non-GAAP financial measures) for reconciliation of cash cost to the cost of sales.

Caylloma Mine and San Jose Mine Concentrates*

	QUARTERLY RESULTS				YEAR TO DATE RESULTS			
	Three months ended December 31,				Years ended December 31,			
	2011		2010		2011		2010	
	Caylloma	San Jose	Caylloma	San Jose	Caylloma	San Jose	Caylloma	San Jose
Mine Concentrates		**730**						
Silver Gold								
Opening Inventory (t)	**0**	**538**	0	0	**0**	**0**	0	0
Production (t)	**0**	**2,276**	0	0	**0**	**2,958**	0	0
Sales (t)	**0**	**2,084**	0	0	**0**	**2,227**	0	0
Adjustment (t)	**0**	**0**	0	0	**0**	**0**	0	0
Closing Inventory (t)	**0**	**730**	0	0	**0**	**730**	0	0
Ag in concentrate (g/t)**	**0**	**5,155**	0	0	**0**	**5,028**	0	0
Au in concentrate (g/t)**	**0**	**49**	0	0	**0**	**48**	0	0
Zinc								
Opening Inventory (t)	**273**	**0**	540	0	**263**	**0**	369	0
Production (t)	**4,964**	**0**	5,467	0	**20,569**	**0**	22,291	0
Sales (t)	**4,920**	**0**	5,749	0	**20,490**	**0**	22,419	0
Adjustment (t)	**-12**	**0**	5	0	**-37**	**0**	22	0
Closing Inventory (t)	**305**	**0**	263	0	**305**	**0**	263	0
Zn in concentrate (%)**	**51.98**	**0.00**	51.09	0.00	**51.66**	**0.00**	53.86	0.00
Lead								
Opening Inventory (t)	**232**	**0**	404	0	**188**	**0**	408	0
Production (t)	**3,599**	**0**	3,829	0	**15,767**	**0**	15,015	0
Sales (t)	**3,590**	**0**	4,053	0	**15,760**	**0**	15,250	0
Adjustment (t)	**14**	**0**	8	0	**60**	**0**	14	0
Closing Inventory (t)	**255**	**0**	188	0	**255**	**0**	188	0
Ag in concentrate (g/t)**	**4,636**	**0**	1,685	0	**3,881**	**0**	1,499	0
Pb in concentrate (%)**	**55.41**	**0.00**	63.23	0.00	**56.61**	**0.00**	64.56	0.00
Copper								
Opening inventory (t)	**4**	**0**	44	0	**29**	**0**	46	0
Production (t)	**0**	**0**	448	0	**80**	**0**	2,085	0
Sales (t)	**0**	**0**	464	0	**104**	**0**	2,117	0
Adjustment (t)	**0**	**0**	1	0	**-1**	**0**	15	0
Closing Inventory (t)	**4**	**0**	29	0	**4**	**0**	29	0
Ag in concentrate (g/t)**	**0**	**0**	19,056	0	**15,876**	**0**	17,644	0
Cu in concentrate (%)**	**0.00**	**0.00**	21.62	0.00	**20.23**	**0.00**	22.31	0.00

***Commercial production commenced on September 1, 2011.**
**** Grades from commercial production.**

Property Option Agreements

Mario Property

In May 2011, the Company entered into an agreement to acquire a 100% interest in the Mario Property, located in the Department of Junin in central Peru. Under the terms of the agreement, the Company is granted the exclusive right and option to purchase an undivided 100% interest in the Mario Property subject to the following payments:

1. $0.50 million on signing of agreement;
2. $0.50 million on or before six months from the signing of the agreement;
3. $0.50 million on or before 12 months from the signing of the agreement; and,
4. $2.50 million on or before 24 months from the signing of the agreement.

The transfer of the property to the Company is subject to a 1% net smelter return ("NSR") royalty on production from the property payable to Crocodile Gold ("Crocodile"). The Company shall have the right to purchase the NSR royalty from Crocodile at any time during the five-year period following the final option payment for the sum of $3.0 million. The property is also subject to a 2% NSR royalty on production payable to Teck Cominco and a 0.5% NSR royalty on production payable to Socrate Capital Inc., with each royalty in turn subject to certain buy-back provisions.

As at December 31, 2011, $1.0 million has been paid under the agreement.

Don Mario Property

The Company entered into an option agreement, effective July 20, 2011, to acquire 100% interest in the Don Mario property, with Consorcio Empresarial Agmin S.A.C.("AGMIN"). Under the terms of the mining assignment and option to purchase mineral rights agreement ("agreement"), the Company is required to make the following payments:

1. $0.20 million on signing the agreement;
2. $0.30 million after 12 months from signing the agreement;
3. $0.50 million after 24 months from signing the agreement; and,
4. $2.00 million after 36 months from signing the agreement.

Under the terms of the agreement, once the option is exercised and technical report is prepared under National Instrument 43-101 and published, if the pre-feasibility study indicates that the property contains more than five million silver equivalent ounces, the Company would further pay AGMIN, one dollar for each additional resource and reserves indicated in the pre-feasibility report. The Company has the option to buy-out the additional pay-out for a further $3.0 million, subject to certain conditions.

As at December 31, 2011, $0.20 million has been paid under the agreement.

Annual Financial Results

	Years Ended December 31,		
Expressed in $000's, except per share data */**	**2011***	2010*	2009**
Sales	**110,004**	74,056	51,428
Operating income	**38,065**	27,728	14,383
Income	**19,533**	16,003	623
Earnings per share, basic	**0.16**	0.15	0.01
Earnings per share, diluted	**0.16**	0.14	0.01
Total assets	**271,606**	233,870	139,738
Leases and long term liabilities	**2,764**	3,166	1,454

* Figures for 2011 and 2010 expressed under IFS

** Figures for 2009 expressed under Canadian Generally Accepted Accounting Principles ("CAD GAAP")

The comparative financial information for 2009 is presented in accordance with Canadian Generally Accepted Accounting Principles ("CAD GAAP") and was not required to be restated to IFRS in this MD&A.

During the year ended December 31, 2011 the Company generated net income of $19.53 million (2010: $16.00 million) on operating income of $38.07 million (2010: $27.73 million). The increase in net income is mainly attributable to higher mine operating income of $60.97 million (2010: $39.21 million) driven by higher sales at Caylloma and the contribution of the San Jose mine, offset by higher selling, general and administrative expenses of $19.84 million (2010: $10.98 million), income taxes of $18.80 million (2010: $11.51 million), impairment of mineral properties, property, plant and equipment of $1.89 million (2010: $nil), exploration and evaluation costs of $1.72 million (2010: $0.55 million), and lower gain on commodity contracts of $0.48 million (2010: $0.74 million).

Sales, for the year end December 31, 2011, increased by 49% to $110.00 million (2010: $74.06 million), compared to the prior year. The sales increase is mainly a result of higher realized prices for silver, gold, lead and zinc of 71%, 29%, 9% and 9%, respectively, and higher metals sold for silver and gold of 23% and 124%, respectively, offset by lower metal sold for lead and zinc of 8% and 11%, respectively.

	YEAR TO DATE RESULTS					
	Years ended December 31,					
	2011			2010		
	Caylloma	**San Jose**	**Consolidated**	Caylloma	San Jose	Consolidated
Mine Metal Sold and Prices						
Silver						
Sales (Oz)*	**2,004,457**	**320,599**	**2,325,056**	1,894,703	-	1,894,703
Net Realized Price (US$/Oz)**	**31.91**	**26.42**	**31.11**	18.18	-	18.18

Gold						
Sales (Oz)*	**2,438**	**2,952**	**5,391**	2,411	-	2,411
Net Realized Price (US$/Oz)**	**1,116.09**	**1,230.34**	**1,183.39**	920.85	-	920.85
Lead						
Sales (000's lb)*	**19,685**	**-**	**19,685**	21,461	-	21,461
Net Realized Price (US$/lb)**	**0.86**	**-**	**0.86**	0.79	-	0.79
Zinc						
Sales (000's lb)*	**23,323**	**-**	**23,323**	26,306	-	26,306
Net Realized Price (US$/lb)**	**0.66**	**-**	**0.66**	0.60	-	0.60
Copper						
Sales (000's lb)*	**52**	**-**	**52**	1,021	-	1,021
Net Realized Price (US$/lb)**	**2.65**	**-**	**2.65**	2.60	-	2.60

* Contained metal in concentrate. The current and subsequent period may include final settlement quantity adjustments from prior periods.
** Calculated based on contained metals and after deductions, treatment, and refining charges.
Treatment charges are allocated to the base metals in Caylloma and to gold in San Jose.
Net realized prices are based on provisional sales and are calculated before government royalties.

Cost of sales, for the year ended December 31, 2011, increased by 41% to $49.03 million (2010: $34.84 million) compared to the prior year. The increase is primarily attributable to 18% higher unit production cash costs per tonne of processed ore in Caylloma and an overall throughput increase of 30%. The higher unit production cash cost per tonne of processed ore reflect cost increases in qualified labor and industry related services that have been mounting in the Peruvian underground mining industry since late 2010. (Refer to cash cost per silver ounce and cash cost per tonne (non-GAAP financial measures), discussion on Caylloma mine operations, and discussion on San Jose mine operations).

Selling, general and administrative expenses, for the year ended December 31, 2011, increased by 81% to $19.84 million (2010: $10.98 million). The increase is primarily attributable to share-based payments of $4.79 million in 2011 compared to a net recovery of $0.42 million in 2010, a $2.61 million increase in corporate general and administrative expenses mainly as a result of higher salaries and professional fees related to the growth of the company, the New York Stock Exchange ("NYSE") listing, and $0.87 million from Cuzcatlan as a result of the commencement of commercial production in the second half of 2011.

	Expressed in $ millions	
	Year ended December 31,	
	2011	2010
Corporate general and administrative expenses	**$ 9.97**	$ 7.36
Bateas general and administrative expenses	**3.36**	3.83
Cuzcatlan general and administrative expenses	**0.87**	-
Foreign exchange	**0.22**	0.21
Share-based payments	**4.79**	(0.42)
Peruvian workers' participation	**0.63**	-
	$ 19.84	$ 10.98

Exploration and evaluation costs, for the year ended December 31, 2011, increased to $1.72 million (2010: $0.55 million) as the Company pursues its exploration program.

Impairment of mineral properties, property, plant and equipment, for year ended December 31, 2011, amounted to $1.89 million (2010: $nil) as the Company has taken an impairment charge related to the Taviche property comprised of: $1.08 million on the tailing dam, $0.14 million on the mine infrastructure, and $0.67 million on equipment, machinery, and buildings.

In 2010, the Company included the idle plant in Taviche as part of the San Jose mine plant as it was more likely than not that the idle plant could be used to treat excess ore from San Jose or from surrounding areas where the company was conducting exploration. On September 1, 2011, the San Jose mine plant commenced commercial production and in the fourth quarter of 2011, achieved an average of 955 tonnes milled per day with the San Jose plant having sufficient capacity for the production. In the fourth quarter, management reassessed the usability of the idle plant and in conjunction, obtained an independent third party appraisal of various assets acquired under an asset purchase agreement dated 2007 related to the Taviche property.

Management used the fair value less cost to sell method to determine the recoverable amount of the idle plant. Based upon an independent appraisal of the assets, which is in accordance with fair value less cost to sell, the Company has taken an impairment charge of $1.89 million that comprised of the following impairments: $1.08 million on the tailing dam, $0.14 million on the mine infrastructure, and $0.67 million on equipment, machinery, and buildings. As at December 31, 2011, the net book value of assets related to the Taviche property for machinery, and equipment amount to $0.36 million.

Net gain on commodity contract, for the year ended December 31, 2011, was $0.48 million (2010: $0.74 million). The gain is related to short term contracts used to fix the final settlement price on metal contained in concentrate delivered throughout the period.

Interest income, for the year ended December 31, 2011, increased by 68% to $0.83 million (2010: $0.49 million). The increase in interest income is primarily attributable to interest earned on long term receivables through the sale of assets and higher invested cash balances at the first half of the year.

Interest expense, for the year ended December 31, 2011, decreased by 21% to $0.56 million (2010: $0.71 million) as a result of a reduction in standby and commitment fees, compared to the prior year.
Income taxes, for the year ended December 31, 2011, increased by 63% to $18.80 million (2010: $11.51 million) due to higher income recorded at Bateas and deferred tax arising from Cuzcatlan.

Income tax provision is comprised of $14.61 million of current income tax expense and $4.19 million of deferred income tax expense mainly related to our Peruvian and Mexican operations.

Quarterly Information

The following table provides information for the eight fiscal quarters ended December 31, 2011:

	Quarters ended							
Expressed in $000's, except per share data*	**31-Dec-11**	30-Sep-11	30-Jun-11	31-Mar-11	31-Dec-10	30-Sep-10	30-Jun-10	31-Mar-10
Sales	**31,047**	32,543	24,528	21,886	23,909	18,039	14,565	17,543
Operating income	**4,437**	14,886	10,665	8,077	8,031	1,030	9,629	9,038
Income before taxes	**4,443**	14,948	10,754	8,190	8,033	780	9,666	9,034
Income (loss)	**(1,755)**	10,309	6,197	4,782	4,333	(773)	6,719	5,724
Earnings per share, basic	**(0.01)**	0.08	0.05	0.04	0.04	(0.01)	0.06	0.06
Earnings per share, diluted	**(0.01)**	0.08	0.05	0.04	0.04	(0.01)	0.06	0.05
Total assets	**271,606**	270,259	253,287	242,564	233,870	180,473	175,445	170,198
Leases and long term liabilities	**2,764**	2,873	2,988	3,384	3,166	2,653	1,384	1,306

* Figures for 2011 and 2010 expressed under IFRS

The past eight quarters show a consistent trend of sales growth with a marginal decline in Q4 2011 from Q3 2011. This trend reflects the surge in silver price since the beginning of 2010 and the commencement of commercial production at the San Jose mine starting in September 2011.

Fourth Quarter Financial Results

	Three months ended December 31,	
Expressed in $'000's	**2011**	**2010**
Sales	**$ 31,047**	$ 23,909
Cost of sales	**17,782**	9,804
Mine operating income	**13,265**	14,105
Other expenses		
Selling, general and administrative expenses	**5,871**	4,583
Exploration and evaluation costs	**605**	202
Net gain on commodity contracts	**442**	725
Loss on disposal of mineral properties, property, plant and equipment	**16**	2
Loss on disposal of investment	**-**	119
Write-off of deferred exploration costs	**-**	443
Impairment of mineral properties, property, plant and equipment	**1,894**	-
Operating income	**4,437**	8,031
Finance items		
Interest income	**155**	159
Interest expense	**(149)**	(157)
Net finance income	**6**	2
Income before tax	**4,443**	8,033
Income taxes	**6,198**	3,700
(Loss) Income for the period	**$ (1,755)**	$ 4,333

During the fourth quarter ended December 31, 2011 the Company generated net loss of $1.76 million (Q4 2010: $4.33 million) on operating income of $4.44 million (Q4 2010: $8.03 million). The decrease in net income compared to the same period in 2010 is mainly attributable to lower mine operating income of $13.27 million (Q4 2010: $14.11 million), higher selling, general and administrative expenses of $5.87 million (Q4 2010: $4.58 million), impairment of mineral properties, property, plant and equipment of $1.89 million (Q4 2010: $nil), exploration and evaluation costs of $0.61 million (Q4 2010: $0.20 million) , and income taxes of $6.20 million (Q4 2010: $3.70 million). The decrease in mine operating income in spite of the contribution from the San Jose mine in 2011 and a higher silver price is explained by lower revenue from base metals of $4 million, negative price adjustments in Caylloma associated with the sharp fall in silver price in the fourth quarter, and higher unit costs of 23% at Caylloma.

Sales, for the fourth quarter ended December 31, 2011 increased by 30% to $31.05 million (Q4 2010: $23.91 million) compared to the same quarter a year ago with San Jose contributing $11.39 million (Q4 2010: $nil). Sales at Caylloma decreased by 18% to $19.66 (Q4 2010: $23.91), in spite of higher silver prices (20%) and higher silver sold (11%), mainly due to lower lead and zinc sold (22% and 13% respectively) with lower lead and zinc prices (23% and 15%, respectively) representing $4.25 million of decreased revenue, and a negative final sales adjustments of $2.33 million (Q4 2010: positive $1.85 million) associated with the sharp fall in silver price in the quarter.

	QUARTERLY RESULTS					
	Three months ended December 31,					
	2011			2010		
Mine Metal Sold and Prices	**Caylloma**	**San Jose**	**Consolidated**	Caylloma	San Jose	Consolidated
Silver						
Sales (Oz)*	**547,542**	**300,411**	**847,952**	494,451	-	494,451
Net Realized Price (US$/Oz)**	**28.58**	**26.08**	**27.64**	23.73	-	23.73
Gold						
Sales (Oz)*	**597**	**2,770**	**3,367**	696	-	696
Net Realized Price (US$/Oz)**	**1,245.14**	**1,227.19**	**1,229.99**	1,031.09	-	1,031.09
Lead						

Sales (000's lb)*	**4,385**	**-**	**4,385**	5,605	-	5,605
Net Realized Price (US$/lb)**	**0.67**	**-**	**0.67**	0.87	-	0.87
Zinc						
Sales (000's lb)*	**5,613**	**-**	**5,613**	6,487	-	6,487
Net Realized Price (US$/lb)**	**0.54**	**-**	**0.54**	0.64	-	0.64
Copper						
Sales (000's lb)*	**-**	**-**	**-**	221	-	221
Net Realized Price (US$/lb)**	**-**	**-**	**-**	3.07	-	3.07

* Contained metal in concentrate. The current and subsequent period may include final settlement quantity adjustments from prior periods.
**Calculated based on contained metals and after deductions, treatment and refining charges
Treatment charges are allocated to the base metals in Caylloma and to gold in San Jose
Net realized prices are based on provisional sales and are calculated before government royalties

Cost of sales, for the fourth quarter ended December 31, 2011 increased by 81% to $17.78 million (Q4 2010: $9.80 million) compared to the prior year. The increase is primarily attributable to the contribution of the San Jose mine which was in production for the full quarter resulting in an overall throughput increase of 82%, and to 23% higher unit production cash costs per tonne of processed ore at Caylloma (Refer to cash cost per silver ounce and cash cost per tonne (non-GAAP financial measures)).

Selling, general and administrative expenses, for the fourth quarter ended December 31, 2011 increased by 28% to $5.87 million (Q4 2010: $4.58 million). The increase is primarily attributable to share-based payments of $1.20 million (Q4 2010: $0.76 million), a $0.75 million increase in corporate general and administrative expenses, mainly as a result of higher salaries and professional fees related to the growth of the Company, and $0.67 million from Cuzcatlan (Q4 2010: $nil).

	Expressed in $ millions Three months ended December 31,		
	2011		2010
Corporate general and administrative expenses	**$ 2.90**	$	2.15
Bateas general and administrative expenses	**0.82**		1.50
Cuzcatlan general and administrative expenses	**0.67**		-
Foreign exchange	**0.19**		0.17
Share-based payments	**1.20**		0.76
Peruvian workers' participation	**0.09**		-
	$ 5.87	$	4.58

Exploration and evaluation costs, for the fourth quarter ended December 31, 2011 increased to $0.61 million (Q4 2010: $0.20 million) as the Company pursues its exploration program.

Impairment of mineral properties, property, plant and equipment, for the fourth quarter ended December 31, 2011, amounted to $1.89 million (Q4 2010: $nil) as the Company has taken an impairment charge related to the Taviche property comprised of: $1.08 million on the tailing dam, $0.14 million on the mine infrastructure, and $0.67 million on equipment, machinery, and buildings.

Net loss on commodity contract, for the fourth quarter ended December 31, 2011, was $0.44 million (Q4 2010: $0.73 million). The loss is related to short term contracts used to fix the final settlement price on metal contained in concentrate delivered throughout the period.

Interest income, for the fourth quarter ended December 31, 2011 decreased by 3% to $0.16 million (Q4 2010: $0.16 million) as a result of a reduction in cash balances.

Interest expense, for the fourth quarter ended December 31, 2011 decreased by 5% to $0.15 million (Q4 2010: $0.16 million) as a result of a reduction in the balance of finance leases.

Income taxes, for the fourth quarter ended December 31, 2011 increased by 68% to $6.20 million (Q4 2010: $3.70 million) due to higher recorded income at Bateas and deferred tax arising from Cuzcatlan.

Cash cost per silver ounce and cash cost per tonne (non-GAAP financial measures)

Cash cost per ounce and cash cost per tonne are key performance measures that management uses to monitor performance. In addition, cash costs are presented as they represent an industry standard method of comparing certain costs on a per unit basis but do not have a standardized meaning and may differ from methods used by other companies with similar descriptions. Management believes that certain investors use these non-GAAP financial measures to evaluate the Company's performance. These performance measures have no meaning under International Financial Reporting Standards ("IFRS") and, therefore, amounts presented may not be comparable to similar data presented by other mining companies.

The following table presents a reconciliation of cash costs per tonne of processed ore and cash cost per ounce of payable silver to the cost of sales in the consolidated financial statements for the three months and years ended December 31, 2011 and 2010.

Consolidated Mine Cash Cost	**Expressed in $'000's**		**Expressed in $'000's**	
	Q4 2011	**YTD Q4 2011**	Q4 2010	YTD Q4 2010
Cost of sales [2, 3]	**17,782**	**49,030**	9,804	34,844
Add / (Subtract)				
Change in concentrate inventory	**415**	**2,142**	(295)	(305)
Depletion and depreciation in concentrate inventory	**(207)**	**(781)**	124	5
Inventory adjustment	**-**	**-**	525	290
Government royalties and mining taxes	**(385)**	**(1,322)**	(320)	(788)
Workers participation	**(436)**	**(3,141)**	(881)	(2,320)
Depletion and depreciation [2]	**(3,752)**	**(9,060)**	(1,711)	(6,327)
Cash cost	**13,417**	**36,868**	7,246	25,399

Total processed ore (tonnes)	**204,248**	**565,276**	112,257	434,656
Cash cost per tonne of processed ore ($/t)	**65.69**	**65.22**	64.55	58.43
Cash cost	**13,417**	**36,868**	7,246	25,399
Add / (Subtract)				
By-product credits [1]	**(11,252)**	**(40,267)**	(10,544)	(37,825)
Refining charges	**2,234**	**4,280**	410	1,576
Cash cost applicable per payable ounce	**4,399**	**881**	(2,888)	(10,850)
Payable silver ounces	**860,565**	**2,352,759**	457,712	1,811,102
Cash cost per ounce of payable silver ($/oz)	**5.11**	**0.37**	(6.31)	(5.99)

1 By-product credits as included in the provisional sales
2 2010 and 2011 figures in accordance with IFRS
3 includes depletion, depreciation, distribution, community relations, government royalties and mining taxes, and workers participation

Caylloma Mine Cash Cost	**Expressed in $'000's**		**Expressed in $'000's**	
	Q4 2011	**YTD Q4 2011**	Q4 2010	YTD Q4 2010
Cost of sales [2, 3]	**11,777**	**42,236**	9,804	34,844
Add / (Subtract)				
Change in concentrate inventory	**92**	**206**	(295)	(305)
Depletion and depreciation in concentrate inventory	**(12)**	**(97)**	124	5
Government royalties and mining taxes	**(385)**	**(1,322)**	(320)	(788)
Workers participation	**(436)**	**(3,141)**	(881)	(2,320)
Depletion and depreciation [2]	**(1,764)**	**(6,919)**	(1,711)	(6,327)
Cash cost	**9,272**	**30,963**	7,246	25,399
Total processed ore (tonnes)	**116,363**	**448,866**	112,257	434,656
Cash cost per tonne of processed ore ($/t)	**79.68**	**68.98**	64.55	58.43
Cash cost	**9,272**	**30,963**	7,246	25,399
Add / (Subtract)				
By-product credits [1]	**(6,773)**	**(34,676)**	(10,544)	(37,825)
Refining charges	**900**	**2,590**	410	1,576
Cash cost applicable per payable ounce	**3,399**	**(1,123)**	(2,888)	(10,850)
Payable silver ounces	**509,605**	**1,908,064**	457,712	1,811,102
Cash cost per ounce of payable silver ($/oz)	**6.67**	**(0.59)**	(6.31)	(5.99)

1 By-product credits as included in the provisional sales
2 2010 and 2011 figures in accordance with IFRS
3 includes depletion, depreciation, distribution, community relations, government royalties and mining taxes, and workers participation

San Jose Mine Cash Cost	**Expressed in $'000's**	
	Q4 2011	**YTD Q4 2011**
Cost of sales [2, 3]	**6,005**	**6,794**
Add / (Subtract)		
Change in concentrate inventory	**323**	**1,936**
Depletion and depreciation in concentrate inventory	**(195)**	**(684)**
Depletion and depreciation [2]	**(1,988)**	**(2,141)**
Cash cost	**4,145**	**5,905**
Total processed ore (tonnes)	**87,884**	**116,410**
Cash cost per tonne of processed ore ($/t)	**47.16**	**50.73**
Cash cost	**4,145**	**5,905**
Add / (Subtract)		
By-product credits [1]	**(4,479)**	**(5,591)**
Refining charges	**1,334**	**1,690**
Cash cost applicable per payable ounce	**1,000**	**2,004**
Payable silver ounces	**350,961**	**444,695**
Cash cost per ounce of payable silver ($/oz)	**2.85**	**4.51**

Commercial production commenced on September 1, 2011.

1 By-product credits as included in the provisional sales
2 2010 and 2011 figures in accordance with IFRS
3 includes depletion, depreciation, distribution, community relations, government royalties and mining taxes, and workers participation

Liquidity and Capital Resources

The capital of the Company consists of equity and available credit facility, net of cash. The Board of Directors does not establish a quantitative return on capital criteria for management. The Company manages the capital structure and makes adjustments to it in light

of changes in economic conditions and the risk characteristics of the underlying assets.

The Company's cash and cash equivalents as at December 31, 2011 totalled $38.73 million, and short term investments totalled $17.00 million. The $31.87 million decrease (2010: $37.38 million increase) in cash and cash equivalents at December 31, 2011 compared to the end of the prior year is largely due to the use of $45.48 million on the construction of the San Jose mine. In 2010, the $37.38 million increase in cash is primarily a result of the $74.92 million net proceeds on the issuance of shares. As at December 31, 2011, working capital amounted to $63.90 million (2010: $97.07 million). The 2011 decrease in working capital reflects: decreases in cash and cash equivalents and short term investments; increases in trade and other payables due to related parties, derivative liabilities, provisions, and current portion of long term liabilities; offset by increases in derivative assets, accounts receivable and other assets, GST/HST and value added tax receivable, inventories.

During the fourth quarter ended December 31, 2011, cash generated by operating activities before changes in non-cash working capital items, income taxes paid, and interest income paid and received was $10.45 million (Q4 2010: $7.60 million).

During the year ended December 31, 2011, cash generated by operating activities before changes in non-cash working capital items, income taxes paid, and interest income paid and received was $49.76 million (2010: $28.68 million). Changes in non-cash working capital items amounted to $33.82 million (2010: $15.33 million), and income taxes paid and interest income paid and received amounted to $14.25 million (2010: $6.97 million), resulting in net cash provided by operating activities of $35.51 million (2010: $21.71 million).

Cash generated by operating activities before changes in working capital, income taxes, and interest income is calculated as follows (expressed in '000's):

	Three months ended December 31,		**Years ended December 31,**	
	2011	2010	**2011**	2010
OPERATING ACTIVITIES				
Net income	**$ (1,755)**	$ 4,333	**$ 19,533**	$ 16,003
Items not involving cash				
Depletion and depreciation	**3,943**	1,782	**9,421**	6,462
Accretion of provisions	**57**	42	**173**	163
Income tax expense	**6,199**	3,700	**18,802**	11,510
Share-based payments (recovery)	**475**	676	**3,682**	(501)
Unrealized (gain) on commodity contracts	**1,089**	(325)	**(116)**	(2,922)
Write-off of deferred exploration costs	**-**	443	**-**	443
Impairment of mineral properties, property, plant and equipment	**1,894**	-	**1,894**	-
(Gain) loss on disposal of mineral properties, property, plant and equipment	**16**	6	**(59)**	127
Accrued interest on long term loans receivable and payable	**7**	14	**24**	50
	11,925	10,671	**53,354**	31,335
Changes in non-cash working capital items				
Accounts receivable and other assets	**1,693**	(3,091)	**(3,085)**	(4,788)
Inventories	**(2,189)**	(144)	**(7,273)**	(1,536)
Trade and other payables	**(963)**	165	**6,829**	3,677
Due to/from related parties	**183**	(2)	**134**	(9)
Provisions	**(201)**	-	**(201)**	-
Cash provided by operating activities before interest and income taxes	**10,448**	7,599	**49,758**	28,679

Cash consumed by the Company for the fourth quarter ended December 31, 2011, in investing activities totalled $31.64 million (Q4 2010: $24.77 million) with $16.24 million (Q4 2010: $14.37 million) for mineral properties, property, plant and equipment, $0.63 million (Q4 2010: receipts $0.14 million) net advances on deposits on long term assets, $15.05 million (Q4 2010: $9.48 million) net purchases of short term investments, offset by receipts of VAT $0.28 million (Q4 2010: payments $1.13 million), and proceeds on disposal of mineral properties, property, plant and equipment $nil (Q4 2010: $0.07 million).

Cash consumed by the Company, for the year ended December 31, 2011, in investing activities totalled $69.86 million (2010: $58.06 million) with $76.68 million (2010: $36.71 million) for mineral properties, property, plant and equipment, $3.57 million (2010: advances $4.66 million) for net receipts on deposits on long term assets, $3.73 million net redemptions (2010: purchases $13.85 million) of short term investments, payments of VAT of $0.52 million (2010: $2.92 million), and offset by proceeds on disposal of mineral properties, property, plant, and equipment of $0.04 million (2010: $0.08 million). The total investment in San Jose amounted to $45.48 million.

During the fourth quarter ended December 31, 2011, cash provided by financing activities totalled $1.95 million (Q4 2010: $42.73 million) with repayment of finance lease obligations of $0.30 million (Q4 2010: $0.26 million), offset by cash provided by net proceeds on the issuance of common shares of $2.25 million (Q4 2010: $42.99 million).

During the year ended December 31, 2011, cash provided by financing activities totalled $2.48 million (2010: $73.74 million) with repayment of finance lease obligations of $1.18 million (2010: $1.18 million), offset by cash provided by net proceeds on the issuance of common shares of $3.66 million (2010: $74.92 million).

In 2010, the Company entered into a credit agreement with the Bank of Nova Scotia for a $20 million senior secured revolving credit facility ("credit facility") to be refinanced or repaid on or within two and one-half years or before December 2012. The credit facility is secured by a first ranking lien on Bateas and its assets and bears interest and fees at prevailing market rates. In the event that utilization under the credit facility is less than $10 million, a commitment fee of 1.50% per annum is payable quarterly on the unutilized portion of the available credit facility. No funds were drawn from this credit facility during the year.

The Company has raised funds from two prospectus financings in 2010. The details of the expected use of proceeds and actual use of proceeds are discussed below.

Prospectus February 18, 2010 Closed March 2, 2010	**Prospectus December 17, 2010 Closed December 23, 2010**
San Jose Project Financing	**San Jose Project Financing****
Expressed in CAD $ millions	**Expressed in CAD $ millions**

	Expected Use of Proceeds*	Actual Use of Proceeds**	Variance
Mine development	$ 6.7	$ 11.2	$ (4.5)
Processing plant	16.6	30.4	(13.8)
Tailings dam	1.9	4.4	(2.5)
Water and Infrastructure	3.0	3.5	(0.5)
Energy supply	-	2.5	(2.5)
Construction management	-	2.5	(2.5)
Total	**$ 28.2**	**$ 54.5**	**$ (26.3)**

*excludes over-allotment
**US CAD FX rate at 1.0

	Expected Use of Proceeds*	Actual Use of Proceeds**	Variance
Planned expansion	$ 14.5	$ -	$ 14.5
Exploration programs	5.5	10.7	(5.2)
Working Capital	17.7	26.3	(8.6)
Total	**$ 37.7**	**$ 37.0**	**$ 0.7**

*excludes over-allotment
** funds to be utilized post development

Management believes the Company's cash position, along with its ongoing operations, in Caylloma and San Jose, and the available credit facility, is sufficient to support the Company's operating and capital requirements on an ongoing basis. Actual funding requirements may vary from those planned due to further acquisition opportunities. Management believes it will be able to raise equity capital or access debt facilities as required in both the short and long term, but it recognizes the uncertainty attached thereto.

Contractual Obligations

The Company expects the following maturities of its financial liabilities (including interest), finance leases, and other contractual commitments:

Expressed in $ millions

	Expected payments due by period as at December 31, 2011				
	Less than 1 year	1 - 3 years	4 -5 years	After 5 years	Total
Trade and other payables	$ 17.16	$ -	$ -	$ -	$ 17.16
Due to related parties	0.21	-	-	-	0.21
Derivative liabilities	0.09	-	-	-	0.09
Income tax payable	3.92	-	-	-	3.92
Long term liabilities	1.53	2.77	-	-	4.30
Operating leases	0.70	1.41	1.18	0.53	3.82
Provisions	0.73	0.85	0.77	3.73	6.08
	24.34	**5.03**	**1.95**	**4.26**	**35.58**

Capital Commitments (expressed in $'000's)

As at December 31, 2011, $8.12 million of capital commitments not disclosed elsewhere in the consolidated financial statements, and forecasted to be expended within one year, includes the following: $5.80 million for the ramp development at the San Jose property located in Mexico; $2.25 million for the tailing dam, concentrator plant and electrical infrastructure renewal, and mine camp development at the Caylloma Property; and $0.08 million for software development.

Other Commitments (expressed in $'000's)

The Company has a contract to guarantee power supply at its Caylloma mine. Under the contract, the seller is obligated to deliver a "maximum committed demand" (for the present term this stands at 3,500 Kw) and the Company is obligated to purchase subject to exemptions under provisions of "Force Majeure". The contract is automatically renewed every two years for a period of 10 years and expiring in 2017. Renewal can be avoided without penalties by notifying 10 months in advance of renewal date.

Tariffs are established annually by the energy market regulator in accordance with applicable regulations in Peru.

The Company, jointly with Radius Gold Inc., a related party by way of common directors, has entered into an office premise lease located in Canada, effective on November 28, 2011, the date the Company commenced carrying on business in the premises. The shared office with Radius has been finalized with the Company obligated to pay 50% of the total rent payable. The lease term is eight years with the Company's annual net rent payable, on 3,195 rentable square feet, as follows:

- years one to two $111;
- years three to five $115; and,
- years six to eight $118.

In addition, estimated operating costs, utilities, and realty taxes is $71 in the first year of occupancy. During 2011, the Company has advanced 50% of the three month security deposit in the amount of $47.

On May 24, 2010, the Company entered into a seven year office premise lease located Peru. The annual rent payable on 1,717 rentable square meters for office space, is as follows:

- year one $289;
- year two $297;
- year three $306; and,
- years four through seven the lease is subject a minimum annual increase of 3% or the Consumer Price Index published by Bureau of Labor Statistics of the United States Department of Labor, whichever is higher.

The lease also includes the use of additional space for mini-warehouse and parking spots, the obligation for which is $58 per annum for

the first year and is subject to an annual increase of 3% as stated above until the end of the lease.

As at December 31, 2011, the Company has advanced rent $159 (2010: $426) and provided a security deposit of $44.

On March 15, 2011, the Company entered into a one year office premise lease located in Mexico with an annual lease obligation of $37.

	Expected payments due by period as at December 31, 2011				
	Less than 1 year	1 - 3 years	4 -5 years	After 5 years	Total
Office premises – Canada	181	549	372	359	1,461
Office premises – Peru	363	758	805	172	2,098
Office premises – Mexico	8	-	-	-	8
Total office premises	**$ 552**	**$ 1,307**	**$ 1,177**	**$ 531**	**$ 3,567**
Computer equipment – Peru	128	75	-	-	203
Computer equipment – Mexico	16	28	-	-	44
Total computer equipment	**$ 144**	**$ 103**	**$ -**	**$ -**	**$ 247**
Total operating leases	**$ 696**	**$ 1,410**	**$ 1,177**	**$ 531**	**$ 3,814**

On February 17, 2012, the Company entered into a one year office premise lease, effective March 1, 2012, located in Mexico with an annual lease obligation of $18.

Other Contingencies (expressed in $'000's)

In February 2009, the Environmental Assessment and Oversight Agency ("OEFA") in Peru, alleged the Company had five violations: two were for breaches of recommendations; two for excess of total suspended solids in water over the maximum allowable; and an alleged unauthorized discharge of effluent. The Ministry of Energy and Mines in Peru ("OSINERGMIN") decided to close the two alleged violations for failure to adopt recommendations and punish the Company for the three alleged violations and imposed a fine of $200 in 2010. The Company appealed on June 23, 2010. Subsequent to December 31, 2011 and on February 22, 2012, the alleged unauthorized discharge of effluent was dismissed and confirmed a fine of $133 for the two alleged violations of excess of total suspended solids in water over the maximum allowable. The Company is proceeding with an administrative appeal to the Ministry of Energy and Mines in Peru ("OSINERGMIN") for the remaining two alleged offenses. The Company believes it is more likely than not that it will defend itself successfully in the claims and therefore has not recorded a provision for the potential exposure relating to these alleged violations.

Guarantees and Indemnifications (expressed in $'000's)

The Company may provide guarantees and indemnifications in conjunction with transactions in the normal course of operations. These are recorded as liabilities when reasonable estimates of the obligations can be made. Indemnifications that the Company has provided include obligation to indemnify:

- directors and officers of the Company and its subsidiaries for potential liability while acting as a director or officer of the Company, together with various expenses associated with defending and settling such suits or actions due to association with the Company;
- certain vendors of acquired company for obligations that may or may not have been known at the date of the transaction; and,
- the dollar value cannot be reasonably estimated.

The Caylloma mine closure plan was approved in November 2009 with total closure costs of $3,587 of which $1,756 is subject to annual collateral in the form of a letter of guarantee, to be awarded each year in increments of $146 over 12 years based on the estimated life of the mine.

Banco Bilbao Vizcaya Argentaria, S.A., a third party, has established a bank letter of guarantee on behalf of Bateas in favor of the Peruvian mining regulatory agency in compliance with local regulation associated with the approved Bateas' mine closure plan, for the sum of $439. This bank letter of guarantee expires 360 days from December 2011.

Banco Bilbao Vizcaya Argentaria, S.A. has also established bank letters of guarantee totalling $54 to provide an annual guarantee associated with an office lease contract and truck rentals. These bank letters of guarantee were renewed in June 2011 with expiry 360 days to June 2012.

The Company acts as guarantor to finance lease obligations held by two of its mining contractors. These finance lease contracts are related to the acquisition of mining equipment deployed at the Caylloma mine. As at December 31, 2011, these obligations amounted to $231 with $74 maturing in 2012 and $157 maturing in 2013.

Off-Balance Sheet Arrangements

The Company does not have any off-balance sheet arrangements or commitments that are expected to have a current or future effect on our financial condition, results of operations, liquidity, capital expenditures, or capital resources that are material to investors, other than those disclosed in this MD&A and the consolidated financial statements and the related notes.

Derivatives

	Expressed in $ millions			
	December 31, 2011		December 31, 2010	
	Assets	**Liabilities**	Assets	Liabilities
Lead forward contracts	**-**	**0.05**	-	0.01
Zinc forward contracts	**0.07**	**-**	-	0.01

Silver forward contracts	**-**	**0.04**	-	0.11
Total	**$ 0.07**	**$ 0.09**	$ -	$ 0.13

The Company occasionally enters into forward commodity contracts as well as put and call option commodity arrangements to secure a minimum price level on part of its zinc and lead metal production. As at the end of the period no such contracts are outstanding.

Additionally, the Company enters regularly into short term forward and option contracts to fix the final settlement price of metal delivered in concentrates, where the final settlement price is yet to be set at a future quotational period according to contract terms. The forward sale and option contracts are settled against the arithmetic average of metal spot prices over the month in which the contract matures. No initial premium associated with these trades has been paid.

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. The consolidated financial statements include the financial statements of Fortuna Silver Mines Inc. and its subsidiaries listed in the following table:

		Equity Interest as at December 31,	
Name	**Country of Incorporation**	**2011**	2010
Minera Bateas S.A.C.	Peru	100%	100%
Fortuna Silver Mines Peru S.A.C.	Peru	100%	100%
Compania Minera Cuzcatlan SA	Mexico	100%	100%
Fortuna Silver Mexico, S.A. de CV	Mexico	100%	n/a
Fortuna Silver (Barbados) Inc.	Barbados	100%	100%
Continuum Resources Ltd.	Canada	100%	100%

Fortuna Silver Mexico, S.A. de CV was incorporated in 2011.

a) Purchase of Goods and Services

The Company entered into the following related party transactions:

	Expressed in $'000's Years ended December 31,	
Transactions with related parties	**2011**	2010
Salaries and wages [1,2]	**$ 173**	$ 174
Other general and administrative expenses [2]	**292**	185
Leasehold improvements [2]	**93**	-
	$ 558	$ 359

[1] Salaries and wages includes employees' salaries and benefits charged to the Company based on a percentage of the estimated hours worked for the Company.

[2] Radius Gold Inc. ("Radius") has directors in common with the Company and shares office space, and is reimbursed for salaries and wages, general and administrative costs, and leasehold improvements incurred on behalf of the Company.

During the year ended December 31, 2011, the Company transferred two mining concessions to Focus Ventures Ltd., a Company with directors in common, in exchange for a 1% net smelter return royalty.

During the year ended December 31, 2011, the Company issued 6,756 (2010: 7,813) common shares, at a fair market value of $4.44 (2010: $2.56) per share and paid $0.03 million cash (2010: $0.02 million) to Radius, under the option to acquire a 60% interest in Tlacolula silver project located in the State of Oaxaca, Mexico.

Subsequent to the year ended December 31, 2011 to March 23, 2012, the Company issued 8,605 common shares, at a fair market value of $5.81 per share and paid $0.05 million cash to Radius, under the option to acquire a 60% interest in Tlacolula silver project located in the State of Oaxaca, Mexico.

b) Key Management Compensation

Key management includes all persons named or performing the duties of Vice-President, Chief Financial Officer, President, Chief Executive Officer, and non-executive Directors of the Company. The compensation paid or payable to key management for services is shown below:

	Expressed in $'000's Years ended December 31,	
	2011	2010
Salaries and other short term employee benefits	**$ 3,492**	$ 2,633
Directors fees	**333**	300
Consulting fees	**416**	174
Share-based payments	**4,398**	188
	$ 8,639	$ 3,295

The share-based payments includes the change in the deferred share unit ("DSU") and restricted share unit ("RSU") fair value over each reporting period and payments made under the DSU and RSU plans and the non-cancellation of share options.
Consulting fees includes fees paid to two non-executive directors in both 2011 and 2010.

c) Year end Balances arising from Purchases of Goods/Services

	Expressed in $'000's	
Amounts due to/(from) related parties	**December 31, 2011**	December 31, 2010
Owing from a director and officer [3]	**$ (36)**	$ (1)
Owing to a company with common directors [2]	**205**	41
	$ 169	$ 40

[3] Owing from a director includes non-interest bearing advances to a director and officers at December 31, 2011 and one officer and director at December 31, 2010.

Significant Accounting Judgments and Estimates

The preparation of these consolidated financial statements requires management to make judgments and estimates that affect the reported amounts of assets and liabilities at the date of the financial statements and reported amounts of expenses during the reporting period. Actual outcomes could differ from these judgments and estimates. The consolidated financial statements include judgments and estimates which, by their nature, are uncertain. The impacts of such judgments and estimates are pervasive throughout the consolidated financial statements, and may require accounting adjustments based on future occurrences. Revisions to accounting estimates are recognized in the period in which the estimate is revised and the revision affects both current and future periods. Significant assumptions about the future and other sources of judgments and estimates that management has made at the statement of financial position date, that could result in a material adjustment to the carrying amounts of assets and liabilities, in the event that actual results differ from assumptions made, relate to, but are not limited to, the following:

i. Critical Judgments

- The analysis of the functional currency for each entity of the Company. In concluding that the United States dollar ("US$") functional currency for its Peruvian and Mexican entities and the Canadian and Barbados entities have a Canadian dollar ("CAD$") functional currency, management considered the currency that mainly influences the cost of providing goods and services in each jurisdiction in which the Company operates. As no single currency was clearly dominant the Company also considered secondary indicators including the currency in which funds from financing activities are denominated and the currency in which funds are retained.
- In concluding when commercial production has been achieved, the Company considered the following factors:
- all major capital expenditures to bring the mine to the condition necessary for it to be capable of operating in the manner intended by management have been completed;
- the mine or mill is operating within eighty percent of design capacity;
- metallurgical recoveries are achieved within eighty percent of projections; and,
- the ability to sustain ongoing production of ore at a steady or increasing level.
- The identification of reportable segments, basis for measurement and disclosure of the segmented information.
- The determination of estimated useful lives and residual values of tangible and long-lived assets and the measurement of depreciation expense.
- The identification of impairment indicators, cash generating units and determination of value in use and the write down of tangible and long lived assets.
- Measurement of financial instruments involve significant judgments related to interpretation of the terms of the instrument, identification, classification, impairment and the overall measurement to approximate fair values.

ii. Estimates

- the recoverability of amounts receivable which are included in the consolidated statements of financial position;
- the estimation of assay grades of metal concentrates sold in the determination of the carrying value of accounts receivable which are included in the consolidated statements of financial position and included as sales in the consolidated statements of income;
- the carrying value of the short term investments and the recoverability of the carrying value which are included in the consolidated statements of financial position;
- the determination of net realizable value of inventories on the consolidated statements of financial position;
- the estimated useful lives of property, plant and equipment which are included in the consolidated statements of financial position and the related depreciation included in the consolidated statements of income;
- the determination of mineral reserves, carrying amount of mineral properties, and depletion of mineral properties included in the consolidated statements of financial position and the related depletion included in the consolidated statements of income;
- review of tangible and intangible assets carrying value, the determination of whether these assets are impaired and the measurement of impairment charges or reversals which are included in the consolidated statements of income;
- the determination of the fair value of financial instruments and derivatives included in the consolidated statements of financial position;
- the fair value estimation of share-based awards included in the consolidated statements of financial position and the inputs used in accounting for share-based compensation expense in the consolidated statements of income;
- the provision for income taxes which is included in the consolidated statements of income and composition of deferred income tax asset and liabilities included in the consolidated statement of financial position;
- the recognition of deferred income tax assets, amounts recorded for uncertain tax positions, the measurement of income tax expense and indirect taxes included in the consolidated statement of financial position;
- the inputs used in determining the net present value of the liability for provisions related to decommissioning and restoration included in the consolidated statements of financial position;
- the inputs used in determining the various commitments and contingencies accrued in the consolidated statements of financial

position; and,

- the assessment of indications of impairment of each mineral properties and related determination of the net realizable value and write-down of those properties where applicable.

Financial Instruments and Related Risks *(expressed in 000's)*

The Company's financial instruments are exposed to certain financial risks, including currency risk, credit risk, liquidity risk, interest risk, and price risk. The Company's Board of Directors has overall responsibility for the establishment and oversight of the Company's risk management framework and reviews the Company's policies on an ongoing basis.

a) Fair Value of Financial Instruments

The carrying value of cash and cash equivalents, short term investments, derivative assets, trade receivable from concentrate sales, other accounts receivables, trade and other payables, due to related parties, and derivative liabilities approximate their fair value due to the relatively short periods to maturity and the terms of these financial instruments. Fair value estimates are made at a specific point in time, based on relevant market information and information about the financial instrument.

The amortized value of long term receivables approximates their fair value as these are measured at the amortized cost using the effective interest method. The fair value of the lease and long term liabilities is $5,531 as at December 31, 2011.

The analysis of financial instruments that are measured subsequent to initial recognition at fair value can be categorized into Levels 1 to 3 based upon the degree to which the fair value is observable.

- Level 1 - inputs to the valuation methodology are quoted (unadjusted) for identical assets or liabilities in active markets.
- Level 2 - inputs to valuation methodology include quoted market prices for similar assets and liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument.
- Level 3 - inputs to the valuation methodology are unobservable and significant to the fair value of measurement.

The Company has classified the determination of fair value of trade receivable concentrate sales, and derivatives as level 2, as the valuation method used by the Company includes an assessment of assets in quoted markets with significant observable inputs.

Expressed in $'000's

	Level 1	**Level 2**	**Level 3**	**Total**
Cash and cash equivalents	**$ 38,730**	**$ -**	**$ -**	**$ 38,730**
Short term investments	**17,000**	**-**	**-**	**17,000**
Trade receivable from concentrate sales	**-**	**11,287**	**-**	**11,287**
Derivatives	**-**	**(17)**	**-**	**(17)**
	$ 55,730	**$ 11,270**	**$ -**	**$ 67,000**

There were no changes in the levels during the year ended December 31, 2011.

Expressed in $'000's

	Financial assets (liabilities) at fair value as at December 31, 2010			
	Level 1	Level 2	Level 3	Total
Cash and cash equivalents	$ 70,298	$ -	$ -	$ 70,298
Short term investments	20,509	-	-	20,509
Trade receivable from concentrate sales	-	12,551	-	12,551
Derivatives	-	(133)	-	(133)
	$ 90,807	$ 12,418	$ -	$ 103,225

There were no changes in the levels during the year ended December 31, 2010.

Accounts receivable includes trade receivable from concentrate sales, provisional price adjustments, and final price adjustments. The fair value of accounts receivable resulting from provisional pricing reflect observable market commodity prices. Resulting fair value changes to accounts receivable are through sales. Transactions involving accounts receivable are with counterparties the Company believes are creditworthy. As such, these accounts receivable are classified within level 2 of the fair value hierarchy.

Derivatives are carried at their fair value, which is determined based on internal valuation models that reflect observable forward market commodity prices. Resulting fair value changes to derivatives are through net gain (loss) on commodity contracts. Transactions involving derivatives are with counterparties the Company believes to be creditworthy.

During the year ended December 31, 2011, there have been no changes in the classification of financial assets and liabilities in levels 1, 2, and 3 of the hierarchy.

b) Currency Risk

The Company is exposed to the financial risk related to the fluctuation of foreign exchange rates. The Company operates in Canada, Peru and Mexico and a portion of its expenses are incurred in Canadian dollars, Nuevo Soles, and Mexican Pesos. A significant change in the currency exchange rates between the United States dollar relative to the other currencies could have a material effect on the Company's income, financial position, or cash flows. The Company has not hedged its exposure to currency fluctuations.

As at December 31, 2011, the Company is exposed to currency risk through the following assets and liabilities denominated in

Canadian dollars, Nuevo Soles and Mexican Pesos (all amounts are expressed in thousands of Canadian dollars, thousands of Nuevo Soles or thousands of Mexican Pesos):

	Expressed in '000's					
	December 31, 2011			December 31, 2010		
	Canadian Dollars	**Nuevo Soles**	**Mexican Pesos**	Canadian Dollars	Nuevo Soles	Mexican Pesos
Cash and cash equivalents	**$ 18,457**	S/. **1,396**	**$ 1,758**	$ 54,782	S/. 741	$ 2,201
Accounts receivable and other assets	**42**	**5,657**	**58,939**	71	1,304	42,452
Deposits on long term assets	**-**	**-**	**-**	-	-	24,209
Trade and other payables	**(1,580)**	**(17,993)**	**(24,310)**	(625)	(15,493)	(6,390)
Provisions, current	**-**	**(1,351)**	**(3,163)**	-	-	-
Income tax payable	**-**	**(10,581)**	**-**	-	(11,775)	-
Leases and long term liabilities	**(2,691)**	**-**	**-**	(1,999)	-	-
Provisions	**-**	**(8,079)**	**(17,494)**	-	(9,169)	(19,959)
Total	**14,228**	**(30,951)**	**15,730**	52,229	(34,392)	42,513
Total US$ equivalent	**13,950**	**(11,476)**	**1,125**	52,219	(12,244)	3,440

Based on the above net exposure as at December 31, 2011, and assuming that all other variables remain constant, a 10% depreciation or appreciation of the US dollar against the above currencies would result in an increase or decrease, as follows: impact to other comprehensive income of $1,550 (2010: $5,802) and a net loss of $1,150 (2010: $978).

c) Credit Risk

Credit risk is the risk of an unexpected loss if a customer or third party to a financial instrument fails to meet its contractual obligations. The Company's cash and cash equivalents and short term investments are held through large Canadian, international and foreign national financial institutions. These investments mature at various dates within one year. All of the Company's trade accounts receivables are held with large international metals trading companies.

The Company holds derivative contracts with financial institutions and in this regard is exposed to counterparty risk. The Company mitigates this risk by transacting only with reputable financial institutions to minimize credit risk.

The Company's maximum exposure to credit risk at December 31, 2011 is as follows:

	Expressed in '000's	
	December 31, 2011	December 31, 2010
Cash and cash equivalents	**$ 38,730**	$ 70,298
Short term investments	**17,000**	20,509
Accounts receivable	**14,391**	12,551
Derivative assets	**70**	-
Due from related parties	**36**	-
GST/HST and value added tax receivable	**4,777**	3,542
	$ 75,004	$ 106,900

The carrying amount of financial assets recorded in the financial statements represents the Company's maximum exposure to credit risk. The Company believes it is not exposed to significant credit risk and overall, the Company's credit risk has not declined significantly from the prior year.

d) Liquidity Risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due. The Company manages liquidity risk by continuing to monitor forecasted and actual cash flows. The Company has in place a planning and budgeting process to help determine the funds required to support the Company's normal operating requirements on an ongoing basis and its development plans. The Company strives to maintain sufficient liquidity to meet its short term business requirements, taking into account its anticipated cash flows from operations, its holdings of cash, short term investments, and its committed liabilities.

Refer to Contractual Obligations for the expected payments due as at December 31, 2011.

Changes in Accounting Policies including Initial Adoption

The Company is currently assessing the impact of adopting the new accounting standards, noted below, on our consolidated financial statements.

The following standards and amendments to existing standards have been published and are mandatory for the Company's annual accounting periods beginning January 1, 2012, or later:

i) New Accounting Standards Impacting on or after January 1, 2012

IFRS 7 ***Financial Instruments: Disclosures*** (Amendment)
The amendment, effective for annual periods beginning on or after July 1, 2011, with early application permitted, requires additional quantitative and qualitative disclosures relating to transfers of financial assets, where: financial assets are derecognized in their entirety, but where the entity has a continuing involvement in them; financial assets that are not derecognized in their entirety.

IAS 12 ***Income Taxes*** (Amendment)

IAS 12 *Income Taxes*, amendments regarding Deferred Tax: Recovery of Underlying Assets introduces an exception to the existing principle for the measurement of deferred tax assets and liabilities arising on investment property measured at fair value, and the requirement that deferred tax on non-depreciable assets measured using the revaluation model in IAS 16 should always be measured on a sale basis. The amendment is effective for annual periods beginning on or after January 1, 2012.

ii) New Accounting Standards Impacting on or after July 1, 2012

IAS 1 Presentation of Financial Statements (Amendment)

The amendments to IAS 1 *Presentation of Financial Statements* require companies preparing financial statements in accordance with IFRSs to group together items within OCI that may be reclassified to the profit or loss section of the income statement. The amendments retain the 'one or two statement' approach at the option of the entity and only revise the way other comprehensive income is presented: requiring separate subtotals for those elements which may be 'recycled' (e.g. cash-flow hedging, foreign currency translation), and those elements that will not (e.g. fair value through OCI items under IFRS 9). In addition, the tax associated with items presented before tax to be shown separately for each of the two groups of OCI items (without changing the option to present items of OCI either before tax or net of tax).

The amendment is effective for annual periods beginning on or after July 1, 2012.

iii) New Accounting Standards Impacting on or after January 1, 2013

IFRS 7 *Financial Instruments: Disclosures in Respect of Offsetting* (Amendment)

At its meeting on December 13-15, 2011, the IASB approved amendments to IFRS 7, *Financial Instruments*: Disclosures, with respect to offsetting financial assets and financial liabilities. The common disclosure requirements issued by the IASB and the FASB in December 2011 are intended to help investors and other users to better assess the effect or potential effect of offsetting arrangements on a company's financial position. Companies and other entities are required to apply the amendments for annual reporting periods beginning on or after January 1, 2013, and interim periods within those annual periods. The required disclosures should be provided retrospectively.

IFRS 10 *Consolidated Financial Statements*

IFRS 10 *Consolidated Financial Statements* replaces the portion of IAS 27 *Consolidated and Separate Financial Statements* that addresses the accounting for consolidated financial statements, and SIC12 *Consolidation - Special Purpose Entities*. IFRS 10 establishes principles for the presentation and preparation of consolidated financial statements when an entity controls one or more entities. This standard (i) requires a parent entity (an entity that controls one or more other entities) to present consolidated financial statements; (ii) defines the principle of control, and establishes control as a basis for consolidation; (iii) sets out how to apply the principle of control whether an investor controls an investee and therefore must consolidate the investee; and (iv) sets out the accounting requirements for the preparation of consolidated financial statements.

IFRS 10 is effective for annual periods beginning on or after January 1, 2013, with early adoption permitted. IFRS 10 may be adopted to an earlier accounting period, but in doing so, an entity must disclose the fact that it has early adopted the standard and apply IFRS 11 *Joint Arrangements*, IFRS 12 *Disclosure of Interests in Other Entities*, IAS 27 *Separate Financial Statements* (as amended in 2011), IAS 28 *Investments in Associates and Joint Ventures* (as amended in 2011).

IFRS 11 *Joint Arrangements*

IFRS 11 replaces IAS 31 *Interest in Joint Ventures* and SIC-13 *Jointly-Controlled Entities-Non-Monetary Contributions by Venturers.* This standard establishes the core principle that a party to a joint arrangement determines the type of joint arrangement in which it is involved by assessing its rights and obligations and accounts for those rights and obligations in accordance with that type of joint arrangement (joint operations or joint ventures). This standard is effective for annual periods on or after January 1, 2013, with early adoption permitted.

IFRS 12 *Disclosure of Interests in Other Entities*

IFRS 12 combines the disclosure requirements for an entity's interest in subsidiaries, joint arrangements, associates and structured entities into one comprehensive disclosure standard. This standard requires the disclosure of information that enable users of financial statements to evaluate the nature of, and risks associated with, its interest in other entities and the effects of those interests on its financial position, financial performance and cash flows. This standard is effective for annual periods beginning on or after January 1, 2013, with early adoption permitted, and entities are permitted to incorporate any of the new disclosures into their financial statements before that date.

IFRS 13 *Fair Value Measurement*

IFRS 13 *Fair Value Measurement* provides guidance on how to measure fair value, but does not change when fair value is required or permitted under IFRS. IFRS 13 defines fair value, sets out a single IFRS framework for measuring fair value and requires disclosures about fair value measurements. IFRS 13 applies when another IFRS requires or permits fair value measurements or disclosures about fair value measurements (and measurements, such as fair value less costs to sell, based on fair value or disclosures about those measurements), except for: share-based payment transactions within the scope of IFRS 2 *Share-based Payment*; leasing transactions with the scope of IAS 17 *Leases*; measurements that have some similarities to fair value that are not fair value, such as net realizable value in IAS 2 *Inventories*; or value in use IAS 36 *Impairment of Assets*. This standard is effective for annual periods beginning on or after January 1, 2013, with early adoption permitted.

IAS 19 *Post-employment Benefits*

On June 16, 2011 the IASB issued amendments to IAS 19, *Employee Benefit,* in order to improve the accounting for pensions and other post-employment benefits.

The amendments make important improvements by:

- eliminating the option to defer the recognition of gains and losses, known as the 'corridor method' or the "deferral and amortization approach";
- streamlining the presentation of changes in assets and liabilities arising from defined benefit plans, including requiring re-measurements to be presented in OCI, thereby separating those changes from changes that many perceive to be the result of an entity's day-to-day operations;
- enhancing the disclosure requirements for defined benefit plans, providing better information about the characteristics of defined benefit plans and the risks that entities are exposed to through participation in those plans.

The amendments are effective for financial years beginning on or after January 1, 2013. Earlier application is permitted.

IAS 27 *Separate Financial Statements*

IAS 27 has the objective of setting standards to be applied in accounting for investments in subsidiaries, jointly controlled entities, and associates when an entity elects, or is required by local regulations, to present separate (non-consolidated) financial statements. This standard is effective for annual periods beginning on or after January 1, 2013, with early adoption permitted. This standard will not have an impact on the consolidated financial statements.

IAS 28 *Investments in Associates and Joint Ventures*

IAS 28 prescribes the accounting for investments in associates and to set the requirements for the application of the equity method when accounting for investments in associates and joint ventures. This standard is effective for annual periods beginning on or after January 1, 2013, with early adoption permitted.

iv) New Accounting Standards Impacting on or after January 1, 2014

IAS 32 *Financial Instruments - Presentation in Respect of Offsetting* (Amendment)

At its meeting on December 13-15, 2011, the IASB approved amendments to IFRS 7, *Financial Instruments*: Disclosures, with respect to offsetting financial assets and financial liabilities. As part of this project the IASB also clarified aspects of IAS 32, *Financial Instruments*: Presentation. The amendments to IAS 32 address inconsistencies in current practice when applying the requirements. The amendments are effective for annual periods beginning on or after January 1, 2014 and are required to be applied retrospectively.

v) New Accounting Standards Impacting on or after January 1, 2015

IFRS 9 *Financial Instruments - Classification and Measurement*

IFRS 9*, Financial Instruments:* IFRS 9 introduces the new requirements for the classification, measurement and de-recognition of financial assets and financial liabilities. Specifically, IFRS 9 requires all recognized financial assets that are within the scope of IAS 39 *Financial Instruments: Recognition and Measurement* to be subsequently measured at amortized cost or fair value, and all financial liabilities classified as subsequently measured at amortized cost except for financial liabilities as at FVTPL. The amendments are effective for annual periods beginning on or after January 1, 2015, with earlier application permitted.

Other Data

Additional information related to the Company is available for viewing at www.sedar.com and the Company's website at www.fortunasilver.com.

As at March 23, 2012, there are 481,465 DSU outstanding with a fair value of $2.98 million and 265,231 RSU outstanding with a fair value of $1.45 million.

Share Position and Outstanding Warrants and Options

The Company's outstanding share position as at March 23, 2012 is 125,268,751 common shares. In addition, a total of 3,696,560 incentive stock options are currently outstanding as follows:

Type of Security	No. of Shares	Exercise Price (CAD$)	Expiry Date
Incentive Stock Options:	8,271	$4.46	March 30, 2012
	1,663,651	$4.46	June 8, 2014
	200,000	$1.35	February 5, 2016
	50,000	$2.29	March 30, 2016
	10,000	$1.75	May 8, 2016
	2,500	$0.85	July 5, 2016
	225,000	$1.55	July 5, 2016
	225,000	$1.66	July 10, 2016
	35,000	$0.85	January 11, 2017
	350,000	$2.22	January 11, 2017
	184,138	$6.67	February 20, 2017
	38,000	$0.85	June 27, 2017
	25,000	$0.85	October 24, 2017
	250,000	$0.85	October 5, 2018
	230,000	$0.85	November 5, 2018
	200,000	$0.83	July 6, 2019
TOTAL OUTSTANDING OPTIONS	**3,696,560**		

International Financial Reporting Standards ("IFRS")

Effective January 1, 2011, Canadian publicly listed entities were required to prepare their financial statements in accordance with IFRS. Due to the requirement to present comparative financial information, the effective transition date is January 1, 2010. Refer to Note 23 of the consolidated financial statements for the year ended December 31, 2011.

Our IFRS conversion team identified three phases to our conversion: Scoping and Diagnostics, Analysis and Development, and Implementation and Review.

We have now completed our IFRS conversion project through implementation. Review and post-implementation will continue in future periods, as outlined below.

The following outlines our transition project, IFRS transitional impacts and the on-going impact of IFRS on our financial results.

Transitional Financial Impact

Equity Impact

As a result of the policy choices we have selected and the changes we were required to make under IFRS, we have recorded a reduction in our equity of approximately $1.20 million and $3.42 million as at January 1, 2010 and December 31, 2010, respectively. The table below outlines adjustments to our equity on adoption of IFRS on January 1, 2010 and December 31, 2010.

Expressed in $ millions	**January 1, 2010**	**December 31, 2010**
Equity, CAD GAAP	$ 112.56	$ 206.01
Adjustments:		
Effect of foreign exchange on inventory, deposits on long term assets, and mineral properties, property, plant and equipment	(2.54)	(5.34)
Deferred income tax adjustments	1.48	1.94
Transfer of accumulated other comprehensive income to retained earnings	2.90	2.90
Reset accumulated other comprehensive income to zero	(2.90)	(2.90)
Adjustment to revise provisions	(0.32)	(0.25)
Adjustment for depletion on mineral properties related to provisons	0.18	0.23
Total IFRS adjustments to Equity	**(1.20)**	**(3.42)**
Equity, IFRS	**$ 111.36**	**$ 202.59**

Note: There may be differences due to rounding of decimal places

A reconciliation of our comprehensive income under CAD GAAP and IFRS for the year ended December 31, 2010 and a discussion of the impact of IFRS on our cash flows are provided below.

Comprehensive Income Impact

As a result of the policy choices we have selected and the changes we were required to make under IFRS, we have also recorded an increase in our net income of approximately $3.0 million for the year ended December 31, 2010. We have recorded a decrease in our total comprehensive income of approximately $2.2 million for the year ended December 31, 2010.

The following is a summary of the adjustments to comprehensive income for year ended December 31, 2010 under IFRS (all of which are outlined in the notes to our consolidated financial statements):

	Year ended December 31, 2010		
expressed in $ millions	**CAD GAAP**	**Effect of Transition to IFRS**	**IFRS**
Income (loss) for the year	$ 13.0	$ 3.0	$ 16.0
Other comprehensive income (loss)			
Transfer of unrealized loss to a realized loss upon reduction of net investment, net of taxes	2.1	(2.1)	-
Unrealized (loss) gain on translation to presentation currency on foreign operations	5.9	(3.2)	2.7
Other comprehensive income	8.0	(5.3)	2.7
Total comprehensive income for the year	$ 20.9	$ (2.2)	$ 18.7

Note: There may be differences due to rounding of decimal places

Cash Flow Impact

The adoption of IFRS has had no material impact on the net cash flows of the Company. The changes made to the Consolidated Statements of Financial Position and Consolidated Statements of Comprehensive Income have resulted in reclassifications of various amounts on the Consolidated Statements of Cash Flows, however there is no net impact on cash and cash equivalents.

Financial Statement Presentation Changes

The transition to IFRS has resulted in financial statement presentation changes in our financial statements, most significantly on the consolidated statement of income. The changes to the balance sheet relate mainly to the combining of mineral properties, property, plant and equipment and renaming of asset retirement obligations to provisions; future income tax liability to deferred income tax liabilities; and contributed surplus to share option and warrant reserve.

The following is a summary of the significant changes to our consolidated statement of income:

- expenses by function and nature – our statement of income presents expenses by function. Accordingly, depreciation, depletion, and accretion are no longer presented as a separate line item on the statement of income but depreciation and depletion are included in cost of sales. Accretion of provisions is included in interest expense;
- government royalties to cost of sales from selling, general and administrative expenses;
- distribution costs to cost of sales from selling, general and administrative expenses;
- community relation costs to cost of sales from selling, general and administrative expenses;
- other income and expenses from interest and other income and expenses to selling, general and administrative expenses;
- interest expense includes interest on debt financing and accretion of provisions; and,
- current workers participation from income tax to cost of sales and selling, general and administrative expenses.

In addition, exploration and evaluation costs moved from selling, general and administrative expenses.

The above changes are reclassifications within our statement of income so there is no net impact to our income as a result of these changes.

Control Activities

For all changes to policies and procedures that have been identified, the effectiveness of internal controls over financial reporting and disclosure controls and procedures has been assessed and any changes have been implemented. In addition, controls over the IFRS changeover process have been implemented, as necessary. We have identified and implemented the required accounting process changes that resulted from the application of IFRS accounting policies and these changes were not material. We have completed the design, implementation and documentation of the internal controls over accounting process changes resulting from the application of IFRS accounting policies and these changes were not material. We applied our existing control framework to the IFRS changeover process. All accounting policy changes and transitional financial position impacts were subject to review by senior management and the Audit Committee of the Board of Directors.

Business Activities and Key Performance Measures

We have assessed the impact of the IFRS transition project on our financial covenants and key ratios. The transition did not significantly impact our covenants and key ratios that have an equity component.

We have also reviewed the impact of the IFRS transition project on our compensation arrangements. We have identified compensation arrangements that are calculated based on indicators in our financial statements. We are continuing to work with our Human Resources department to ensure that all compensation arrangements incorporate indicators from our financial statements prepared under IFRS in accordance with our compensation policies.

Information Technology and Systems

The IFRS transition project did not have a significant impact on our information systems for the convergence periods. We also do not expect significant changes in the post-convergence periods.

Review

The post-implementation phase will involve continuous monitoring of changes in IFRS in future periods. We note that the standard-setting bodies that determine IFRS have significant ongoing projects that could impact the IFRS accounting policies that we have selected. In particular, there may be additional new or revised IFRSs or IFRICs in relation to financial instruments, hedge accounting, discontinued operations, leases and revenue recognition. We also note that the International Accounting Standards Board is currently working on an extractive industries project, which could significantly impact our financial statements primarily in the areas of capitalization of exploration costs and disclosures. We have processes in place to ensure that potential changes are monitored and evaluated. The impact of any new IFRSs and IFRIC Interpretations will be evaluated as they are drafted and published.

Other Risks and Uncertainties

There have been no major changes from the reported risks factors outlined in the Annual Information Form for the financial year ended December 31, 2011.

Controls and Procedures

Disclosure Controls and Procedures

The Company's management, with the participation of the Chief Executive Officer and the Chief Financial Officer, have evaluated the effectiveness of the Company's disclosure controls and procedures (as defined in the rules of the SEC and the Canadian Securities Administrators ("CSA") as of December 31, 2011, and have concluded that such disclosure controls and procedures are effective to ensure that information required to be disclosed by the Company in reports that it files or submits under the Securities Exchange Act of 1934 and Canadian securities laws is (i) recorded, processed, summarized and reported within the time periods specified in SEC rules and forms and Canadian securities laws and (ii) accumulated and communicated to them Company's management, including its principal executive officer and principal financial officer, to allow timely decisions regarding required disclosure.

Internal Control over Financial Reporting

The Company's management, with the participation of its CEO and CFO, are responsible for establishing a system of internal control

over financial reporting to provide reasonable assurance regarding the reliability and integrity of the Company's financial information and the preparation of its financial statements in accordance with IFRS as issued by the IASB.

The Company's management, including its CEO and CFO, believe that due to its inherent limitations, internal control over financial reporting may not prevent or detect misstatements on a timely basis. Also, projection of any evaluation of the effectiveness of internal control over financial reporting to future periods are subject to the risk that the controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies and procedures may deteriorate.

There has been no change in the Company's internal control over financial reporting that occurred during the year that has materially affected, or is reasonably likely to materially affect, its internal control over financial reporting.
Management concludes that, as of December 31, 2011, the Company's internal control over financial reporting was effective and no material weaknesses were identified.

Outlook

San Jose Mine, Mexico

Exploration at San Jose in 2012 will continue to focus on the evaluation and advancement of multiple mineral occurrences outlined through mapping and stream and soil sampling on the 58,000 hectare land package the Company controls in the area surrounding the San Jose Mine. A 15,000 meter drill program has been budgeted for the year to drill test new targets and follow-up on the results of the 2011 program.

Caylloma Mine, Peru

For 2012, the mine is scheduled to produce 2 million ounces of silver with additional by-product gold, lead and zinc. Capital projects budgeted for the year total $25 million and include a new tailings facility with total holding capacity for seventeen years, camp improvements, upgrading of the power grid and plant equipment and infrastructure optimizations.

2012 Production Guidance

For 2012, the Company is scheduled to produce 3.7 million ounces of silver and 17,400 ounces of gold production or 4.6 million Ag Eq ounces plus base metal credits.

Mine	Silver (M oz)	Gold (k oz)	Zinc (M lbs)	Lead (M lbs)
Caylloma, Peru	2.0	2.4	21.0	18.0
San Jose, Mexico	1.7	15.0	--	--
Total:	**3.7**	**17.4**	**21.0**	**18.0**

- 2012 forecast silver production of 3.7 million ounces and gold production of 17,400 ounces or 4.6 million Ag Eq ounces plus base metal credits (Ag = US$30/oz, Au = US$1,660/oz; metallurgical recoveries of 88% and 90% for Ag and Au respectively)
- Ag Eq = Silver Equivalent

Mining tax in Peru

Effective October 1, 2011, the Peruvian Government approved a change in the tax law for the mining sector which consists of a progressive royalty scheme based on operating margins. Management expects that the impact on taxes paid by its Peruvian subsidiary under the current metal price environment will be between 2 and 3 added percentage points on the total royalty and mining tax.

Cautionary Statement on Forward-Looking Statements

Certain statements contained in this MD&A and any documents incorporated by reference into this MD&A constitute forward-looking statements within the meaning of the U.S. Private Securities Litigation Reform Act of 1995 and Section 21E of the United States Securities Exchange Act of 1934, as amended, and forward-looking information within the meaning of applicable Canadian securities legislation (collectively, "forward-looking statements"). Forward-looking statements express or involve discussions with respect to predictions, expectations, beliefs, plans, projections, objectives, assumptions or future events or performance (often, but not always, identified using words or phrases such as "expects", "is expected", "anticipates", "believes", "plans", "projects", "estimates", "assumes", "intends", "strategies", "targets", "goals", "forecasts", "objectives", "budgets", "schedules", "potential" or variations thereof or stating that certain actions, events or results "may", "could", "would", "might" or "will" be taken, occur or be achieved, or the negative of any of these terms and similar expressions) and are not statements of historical fact. Forward-looking statements relate to, among other things:

- mineral "reserves" and "resources" as they involve the implied assessment, based on estimates and assumptions that the reserves and resources described exist in the quantities predicted or estimated and can be profitably produced in the future;
- timing of the completion of construction activities at the Company's properties and their completion on budget;
- production rates at the Company's properties;
- cash cost estimates;
- timing to achieve full production capacity at the Company's properties;
- timing for completion of infrastructure upgrades related to the Company's properties;
- timing for delivery of materials and equipment for the Company's properties; and
- the sufficiency of the Company's cash position and its ability to raise equity capital or access debt facilities.

Forward-looking statements are necessarily based upon a number of estimates and assumptions that, while considered reasonable by the Company as at the date of such statements, are inherently subject to significant business, economic, social, political and competitive uncertainties and contingencies and other factors that could cause actual results or events to differ materially from those

projected in the forward-looking statements. The estimates and assumptions of the Company contained or incorporated by reference in this MD&A which may prove to be incorrect, include, but are not limited to, (1) that all required third party contractual, regulatory and governmental approvals will be obtained for the development, construction and production of its properties, (2) there being no significant disruptions affecting operations, whether due to labor disruptions, supply disruptions, power disruptions, damage to equipment or otherwise; (3) permitting, development, expansion and power supply proceeding on a basis consistent with the Company's current expectations; (4) currency exchange rates being approximately consistent with current levels; (5) certain price assumptions for silver, lead, zinc and copper; (6) prices for and availability of natural gas, fuel oil, electricity, parts and equipment and other key supplies remaining consistent with current levels; (7) production forecasts meeting expectations; (8) the accuracy of the Company's current mineral resource and reserve estimates; (9) labor and materials costs increasing on a basis consistent with the Company's current expectations; and (10) assumptions made and judgments used in engineering and geological interpretation.

In addition, there are known and unknown risk factors which could cause the Company's actual results, performance or achievements to differ materially from any future results, performance or achievements expressed or implied by the forward-looking statements. Known risk factors include, risks associated with project development; the need for additional financing; operational risks associated with mining and mineral processing; changes in national and local government legislation, taxation, controls, regulations and political or economic developments in Canada, Mexico, the United States, Peru or other countries in which the Company does or may carry on business; the possibility of cost overruns or unanticipated expenses; fluctuations in silver, lead, zinc and copper prices; title matters; uncertainties and risks related to carrying on business in foreign countries; environmental liability claims and insurance; reliance on key personnel; currency exchange rate fluctuations; competition; and other risks and uncertainties, including those described in the "Risks and Uncertainties" section in the MD&A and in the "Risk Factors" section in the Company's Annual Information Form for the financial year ended December 31, 2011 filed with the Canadian Securities Administrators and the U.S. Securities and Exchange Commission and available at www.sedar.com and www.edgar.gov.

Although the Company has attempted to identify important factors that could cause actual actions, events or results to differ materially from those described in forward-looking statements, there may be other factors that cause actions, events or results not to be as anticipated, estimated or intended. These forward-looking statements are made as of the date of this MD&A. There can be no assurance that forward looking statements will prove to be accurate, as actual results and future events could differ materially from those anticipated in such statements. Accordingly, readers are cautioned not to place undue reliance on forward-looking statements. Except as required by law, the Company does not assume the obligation to revise or update these forward looking statements after the date of this document or to revise them to reflect the occurrence of future unanticipated events.

Exhibit 99.4

Consent of Independent Registered Chartered Accountants

We consent to the use of our report dated March 23, 2012 relating to the consolidated financial statements of Fortuna Silver Mines Inc. appearing in this Annual Report on Form 40-F of Fortuna Silver Mines Inc. for the year ended December 31, 2011.

/s/ Deloitte & Touche LLP

Independent Registered Chartered Accountants
Vancouver, Canada
March 30, 2012

EXHIBIT 99.5

CONSENT OF RICHARD L. NIELSEN

CONSENT OF AUTHOR

I hereby consent to the use of my name, Richard L. Nielsen, and reference to my name and the "Technical Review (NI 43-101), Caylloma Project, Peru" dated as of August 11, 2009 (the "Report") evaluating Fortuna Silver Mines Inc.'s Caylloma Project, and the information contained in the Report, as described or incorporated by reference in Fortuna Silver Mines Inc.'s Annual Report on Form 40-F for the year ended December 31, 2011 filed with the United States Securities and Exchange Commission.

RICHARD L. NIELSEN

"Richard L. Nielsen"

March 30, 2012

12600 W. Colfax Ave., Suite A-140
Lakewood, Colorado 80215
Telephone: (303) 716-1617
Fax: (303) 716-3386

EXHIBIT 99.6

CONSENT OF ROBERT L. SANDEFUR

CONSENT OF AUTHOR

I hereby consent to the use of my name, Robert L. Sandefur, and reference to my name and the "Technical Review (NI 43-101), Caylloma Project, Peru" dated as of August 11, 2009 (the "Report") evaluating Fortuna Silver Mines Inc.'s Caylloma Project, and the information contained in the Report, as described or incorporated by reference in Fortuna Silver Mines Inc.'s Annual Report on Form 40-F for the year ended December 31, 2011 filed with the United States Securities and Exchange Commission.

ROBERT L. SANDEFUR

"Robert L. Sandefur"

March 30, 2012

12600 W. Colfax Ave., Suite A-140
Lakewood, Colorado 80215
Telephone: (303) 716-1617
Fax: (303) 716-3386

EXHIBIT 99.7

CONSENT OF CRAIG S. BOW

CONSENT OF AUTHOR

I hereby consent to the use of my name, Craig S. Bow, and reference to my name and the "NI 43-101 Technical Report, San Jose Project, Oaxaca, México" dated as of June 9, 2010 (the "Report") evaluating Fortuna Silver Mines Inc.'s San Jose Project, and the information contained in the Report, as described or incorporated by reference in Fortuna Silver Mines Inc.'s Annual Report on Form 40-F for the year ended December 31, 2011 filed with the United States Securities and Exchange Commission.

CRAIG S. BOW

"Craig S. Bow"

March 30, 2012

12600 W. Colfax Ave., Suite A-140
Lakewood, Colorado 80215
Telephone: (303) 716-1617
Fax: (303) 716-3386

EXHIBIT 99.8

CONSENT OF GREGORY CHLUMSKY

CAM Chlumsky Armbrust & Meyer

Professionals in resources, mining, processing, construction and the environment *www.cam-llc.com*

CONSENT OF AUTHOR

I hereby consent to the use of my name, Gregory Chlumksy, and reference to my name and the "NI 43-101 Technical Report, San Jose Project, Oaxaca, México" dated as of June 9, 2010 (the "Report") evaluating Fortuna Silver Mines Inc.'s San Jose Project, and the information contained in the Report, as described or incorporated by reference in Fortuna Silver Mines Inc.'s Annual Report on Form 40-F for the year ended December 31, 2011 filed with the United States Securities and Exchange Commission.

GREGORY CHLUMSKY

"Gregory Chlumsky"

March 30, 2012

12600 W. Colfax Ave., Suite A-140
Lakewood, Colorado 80215
Telephone: (303) 716-1617
Fax: (303) 716-3386

EXHIBIT 99.9

CONSENT OF STEVE L. MILNE

CAM Chlumsky Armbrust & Meyer

Professionals in resources, mining, processing, construction and the environment *www.cam-llc.com*

CONSENT OF AUTHOR

I hereby consent to the use of my name, Steve Milne, and reference to my name and the "Technical Review (NI 43-101), Caylloma Project, Peru" dated as of August 11, 2009 and the "NI 43-101 Technical Report, San Jose Project, Oaxaca, México" dated as of June 9, 2010 (the "Reports") evaluating Fortuna Silver Mines Inc.'s Caylloma and San Jose Projects respectively, and the information contained in the Reports, as described or incorporated by reference in Fortuna Silver Mines Inc.'s Annual Report on Form 40-F for the year ended December 31, 2011 filed with the United States Securities and Exchange Commission.

STEVE MILNE

"Steve Milne"

March 30, 2012

12600 W. Colfax Ave., Suite A-140
Lakewood, Colorado 80215
Telephone: (303) 716-1617
Fax: (303) 716-3386

EXHIBIT 99.10

CONSENT OF CHLUMSKY, ARMBRUST & MEYER LLC

CAM Chlumsky Armbrust & Meyer

Professionals in resources, mining, processing, construction and the environment www.cam-llc.com

CONSENT OF AUTHOR

We hereby consent to the use of our name, Chlumsky, Armbrust & Meyer, LLC, and reference to our name and the "Technical Review (NI 43-101), Caylloma Project, Peru" dated as of August 11, 2009 and the "NI 43-101 Technical Report, San Jose Project, Oaxaca, México" dated as of June 9, 2010 (the "Reports") evaluating Fortuna Silver Mines Inc.'s Caylloma and San Jose Projects respectively, and the information contained in the Reports, as described or incorporated by reference in Fortuna Silver Mines Inc.'s Annual Report on Form 40-F for the year ended December 31, 2011 filed with the United States Securities and Exchange Commission.

CHLUMSKY, ARMBRUST & MEYER, LLC

Per: *"Michael Read"*

Michael Read, Principal

March 30, 2012

12600 W. Colfax Ave., Suite A-140
Lakewood, Colorado 80215
Telephone: (303) 716-1617
Fax: (303) 716-3386

EXHIBIT 99.11

CONSENT OF ERIC CHAPMAN

I hereby consent to the use of my name, Eric Chapman, and reference to my name and the information describing reserves and/or resources at Fortuna Silver Mines Inc.'s Caylloma Mine and San Jose Mine contained in Fortuna Silver Mines Inc.'s Annual Information Form ("AIF") for the year ended December 31, 2011 and Annual Report on Form 40-F for the year ended December 31, 2011 as filed with the United States Securities and Exchange Commission.

ERIC CHAPMAN

"Eric Chapman"

March 30, 2012

EXHIBIT 99.12

CONSENT OF EDGARD VILELA

I hereby consent to the use of my name, Edgard Vilela, and reference to my name and the information describing reserves and/or resources at Fortuna Silver Mines Inc.'s Caylloma Mine and San Jose Mine contained in Fortuna Silver Mines Inc.'s Annual Information Form ("AIF") for the year ended December 31, 2011 and Annual Report on Form 40-F for the year ended December 31, 2011 as filed with the United States Securities and Exchange Commission.

EDGARD VILELA

"Edgard Vilela"

March 30, 2012

EXHIBIT 99.13

CONSENT OF THOMAS VEHRS

I hereby consent to the use of my name, Thomas Vehrs, and reference to my name and the information describing reserves and/or resources at Fortuna Silver Mines Inc.'s Caylloma Mine and San Jose Mine contained in Fortuna Silver Mines Inc.'s Annual Information Form ("AIF") for the year ended December 31, 2011 and Annual Report on Form 40-F for the year ended December 31, 2011 as filed with the United States Securities and Exchange Commission.

THOMAS VEHRS

"Thomas Vehrs"

March 30, 2012

EXHIBIT 99.14

CERTIFICATION PURSUANT TO RULE 13a-14 OR 15d-14 OF THE SECURITIES EXCHANGE ACT OF 1934, AS ADOPTED PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Jorge Ganoza Durant, certify that:

1. I have reviewed this annual report on Form 40-F of Fortuna Silver Mines Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the issuer as of, and for, the periods presented in this report;

4. The issuer's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the issuer and have:

   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the issuer, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   (c) Evaluated the effectiveness of the issuer's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   (d) Disclosed in this report any change in the issuer's internal control over financial reporting that occurred during the period covered by the annual report that has materially affected, or is reasonably likely to materially affect, the issuer's internal control over financial reporting; and

5. The issuer's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the issuer's auditors and the audit committee of the issuer's board of directors (or persons performing the equivalent functions):

   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the issuer's ability to record, process, summarize and report financial information; and

   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the issuer's internal control over financial reporting.

Dated: March 30, 2012

"Jorge Ganoza Durant"

Name: Jorge Ganoza Durant
Title: President, Chief Executive Officer & Director

EXHIBIT 99.15

CERTIFICATION PURSUANT TO RULE 13a-14 OR 15d-14 OF THE SECURITIES EXCHANGE ACT OF 1934, AS ADOPTED PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Luiz Ganoza Durant, certify that:

1. I have reviewed this annual report on Form 40-F of Fortuna Silver Mines Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the issuer as of, and for, the periods presented in this report;

4. The issuer's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the issuer and have:

   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the issuer, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   (c) Evaluated the effectiveness of the issuer's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   (d) Disclosed in this report any change in the issuer's internal control over financial reporting that occurred during the period covered by the annual report that has materially affected, or is reasonably likely to materially affect, the issuer's internal control over financial reporting; and

5. The issuer's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the issuer's auditors and the audit committee of the issuer's board of directors (or persons performing the equivalent functions):

   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the issuer's ability to record, process, summarize and report financial information; and

   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the issuer's internal control over financial reporting.

Dated: March 30, 2012

"Luis Ganoza Durant"

Name: Luiz Ganoza Durant
Title: Chief Financial Officer

EXHIBIT 99.16

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Annual Report of Fortuna Silver Mines Inc. (the "Company") on Form 40-F for the fiscal year ended December 31, 2011, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Jorge Ganoza Durant, President, Chief Executive Officer & Director of the Company, certify, pursuant to 18 U.S.C. section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that to the best of my knowledge:

1. The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: March 30, 2012

"Jorge Ganoza Durant"

Name: Jorge Ganoza Durant
Title: President, Chief Executive Officer & Director

EXHIBIT 99.17

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Annual Report of Fortuna Silver Mines Inc.(the "Company") on Form 40-F for the fiscal year ended December 31, 2011, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Luis Ganoza Durant, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that to the best of my knowledge:

1. The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: March 30, 2012

"Luis Ganoza Durant"

Name: Luiz Ganoza Durant
Title: Chief Financial Officer