



CONSOLIDATED FINANCIAL STATEMENTS

For the year ended

December 31, 2014

and

December 31, 2013

(Expressed in Canadian dollars)

Management's Responsibility

To the Shareholders of Kootenay Silver Inc.:

Management is responsible for the preparation and presentation of the accompanying consolidated financial statements, including responsibility for significant accounting judgments and estimates in accordance with International Financial Reporting Standards and ensuring that all information in the annual report is consistent with the statements. This responsibility includes selecting appropriate accounting principles and methods, and making decisions affecting the measurement of transactions in which objective judgment is required.

In discharging its responsibilities for the integrity and fairness of the consolidated financial statements, management designs and maintains the necessary accounting systems and related internal controls to provide reasonable assurance that transactions are authorized, assets are safeguarded and financial records are properly maintained to provide reliable information for the preparation of the consolidated financial statements.

The Board of Directors and the Audit Committee are composed primarily of Directors who are neither management nor employees of Kootenay Silver Inc. The Board is responsible for overseeing management in the performance of its financial reporting responsibilities, and for approving the financial information included in the annual report. The Board fulfills these responsibilities by reviewing the financial information prepared by management and discussing relevant matters with management and external auditors. The Audit Committee has the responsibility of meeting with management and external auditors to discuss the internal controls over the financial reporting process, auditing matters and financial reporting issues. The Committee is also responsible for recommending the appointment of Kootenay Silver Inc.'s external auditors.

We draw attention to Note 1 in the consolidated financial statements which indicates the existence of a material uncertainty that may cast significant doubt on the Company's ability to continue as a going concern

MNP LLP, an independent firm of Chartered Accountants, is appointed by the shareholders to audit the financial consolidated statements and report directly to them; their report follows. The external auditors have full and free access to, and meet periodically and separately with, both the Audit Committee and management to discuss their audit findings.

April 29, 2015

"James McDonald"
James McDonald
Chief Executive Officer

"Rajwant Kang"
Rajwant Kang
Chief Financial Officer

INDEPENDENT AUDITORS' REPORT

To the Shareholders of Kootenay Silver Inc.:

We have audited the accompanying consolidated financial statements of Kootenay Silver Inc. and its subsidiaries, which comprise the consolidated statements of financial position as at December 31, 2014 and 2013 and the consolidated statements of loss, comprehensive loss, changes in equity, and cash flows for the years then ended and the related notes, which comprise a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

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

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audits 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 auditors' 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 Kootenay Silver Inc. and its subsidiaries as at December 31, 2014 and December 31, 2013, and the results of their financial performance and their cash flows for the years then ended in accordance with International Financial Reporting Standards.

Emphasis of Matter

Without qualifying our opinion, we draw attention to Note 1 of these consolidated financial statements, which states that Kootenay Silver Inc. incurred significant losses from operations, negative cash flows from operating activities and has an accumulated deficit. This, along with other matters described in Note 1, indicates the existence of a material uncertainty which may cast significant doubt about the ability of Kootenay Silver Inc. to continue as a going concern.



April 29, 2015
Vancouver, British Columbia

Chartered Accountants

Index

CONSOLIDATED FINANCIAL STATEMENTS

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION	2
CONSOLIDATED STATEMENTS OF LOSS.....	3
CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS.....	4
CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY	5
CONSOLIDATED STATEMENTS OF CASH FLOWS	6
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS	7

KOOTENAY SILVER INC.

(Expressed in Canadian dollars)

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

Exhibit 1

	December 31, 2014	December 31, 2013
ASSETS		
Current:		
Cash and cash equivalents	\$ 2,360,822	\$ 2,804,423
Receivables and advances (Note 8, 11)	724,641	846,081
Prepaid expenses	68,392	332,344
Marketable securities (Note 4)	173,815	382,140
Total current assets	3,327,670	4,364,988
Non-current assets:		
Equipment (Note 5)	217,872	253,749
Advances and deposits	106,000	88,500
Mineral properties (Note 6)	31,697,553	33,717,768
	\$ 35,349,095	\$ 38,425,005
LIABILITIES AND EQUITY		
Current Liabilities:		
Accounts payable and accrued liabilities (Note 11)	\$ 416,852	\$ 536,435
Equity:		
Share capital (Note 7)	48,935,618	47,043,736
Contributed surplus (Note 7)	18,703,382	17,243,528
Accumulated other comprehensive loss (Exhibit 4)	(716,130)	(297,672)
Deficit	(31,990,627)	(26,101,022)
Total Equity	34,932,243	37,888,570
Total liabilities and equity	\$ 35,349,095	\$ 38,425,005

Approved on Behalf of the Board:

"James McDonald"

Director

"Kenneth Berry"

Director

- see accompanying notes -

KOOTENAY SILVER INC.

(Expressed in Canadian dollars)

CONSOLIDATED STATEMENTS OF LOSS

		Exhibit 2
	Year ended December 31, 2014	Year ended December 31, 2013
General and Administrative Expenses		
Depreciation (Note 5)	\$ 64,980	\$ 56,929
Office and general (Note 11)	1,051,208	1,140,333
Management fees (Note 11)	359,000	359,000
Bad debt expense	-	4,775
Share based payments (Note 7)	557,762	1,436,764
Professional fees	417,717	469,640
Regulatory and filing fees	46,139	79,136
Rent	93,684	111,380
Loss before Exploration and Other Items	2,590,490	3,657,957
Exploration Expenditures		
Mineral property investigation (Note 6)	94,618	253,803
Impairment of mineral property (Note 6)	3,215,783	944,199
	3,310,401	1,198,002
Other Items		
Impairment of equipment	13,202	-
Administration income	-	(4,711)
(Gain)/loss on sale of marketable securities	(74,825)	413,615
Foreign exchange loss/(gain)	78,674	(334,856)
Finance income	(28,337)	(91,360)
	(11,286)	(17,312)
Loss for the year	5,889,605	4,838,647
Basic and Diluted Loss per Share (Note 7)		
	\$ (0.089)	\$ (0.080)
Weighted Average Number of Shares Outstanding	66,064,625	60,805,535

- see accompanying notes -

KOOTENAY SILVER INC.

(Expressed in Canadian dollars)

CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS

Exhibit 3

	Year ended December 31, 2014	Year ended December 31, 2013
Loss for the year	\$ 5,889,605	\$ 4,838,647
Other comprehensive loss		
Unrealized loss on available-for-sale financial assets arising during the year	184,325	149,123
Foreign currency translation differences of foreign operations	234,133	(1,044,268)
Total other comprehensive (income)/loss	418,458	(895,145)
Comprehensive loss	\$ 6,308,063	\$ 3,943,502

- see accompanying notes -

KOOTENAY SILVER INC.

(Expressed in Canadian dollars)

CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

Exhibit 4

	Number of Shares	Capital Stock	Contributed Surplus	Accumulated Other Comprehensive Income (Loss)	Deficit	Total Equity
Balance, December 31, 2012	56,488,850	\$ 42,991,181	\$ 15,108,951	\$ (1,192,817)	\$ (21,262,375)	\$ 35,644,940
Shares issued, net of issuance costs	6,250,000	4,000,055	697,813	-	-	4,697,868
Acquisition of mineral properties	70,000	52,500	-	-	-	52,500
Share based payment	-	-	1,436,764	-	-	1,436,764
Unrealized loss on available-for-sale financial assets arising during the period	-	-	-	(149,123)	-	(149,123)
Foreign currency translation differences of foreign operations	-	-	-	1,044,268	-	1,044,268
Loss for the year	-	-	-	-	(4,838,647)	(4,838,647)
Balance, December 31, 2013	62,808,850	\$ 47,043,736	\$ 17,243,528	\$ (297,672)	\$ (26,101,022)	\$ 37,888,570
Subscription received in advance	-	-	-	-	-	-
Shares issued, net of issuance costs	9,366,833	1,883,137	888,287	-	-	2,771,424
Acquisition of mineral properties	55,000	22,550	-	-	-	22,550
Share based payment	-	-	557,762	-	-	557,762
Warrant expiration date amendment	-	(13,805)	13,805	-	-	-
Unrealized loss on available-for-sale financial assets arising during the period	-	-	-	(184,325)	-	(184,325)
Foreign currency translation differences of foreign operations	-	-	-	(234,133)	-	(234,133)
Loss for the year	-	-	-	-	(5,889,605)	(5,889,605)
Balance, December 31, 2014	72,230,683	\$ 48,935,618	\$ 18,703,382	\$ (716,130)	\$ (31,990,627)	\$ 34,932,243

- see accompanying notes -

KOOTENAY SILVER INC.

(Expressed in Canadian dollars)

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Exhibit 5	
	Year ended December 31, 2014	Year ended December 31, 2013
Cash Flows from Operating Activities		
Loss for the year	\$ (5,889,605)	\$ (4,838,647)
Add items not involving any outlay of cash:		
Share based payment	557,762	1,436,764
Impairment of mineral property	3,215,783	944,199
(Gain)/loss from the sale of marketable securities	(74,825)	413,615
Depreciation	64,980	56,929
Impairment of equipment	13,202	-
Bad debt expense	-	4,775
	(2,112,703)	(1,982,365)
Changes in non-cash working capital balances:		
Receivable and advances	170,105	(202,407)
Prepaid expenses	273,208	(215,207)
Accounts payable and accrued liabilities	(130,182)	(751)
	(1,799,572)	(2,400,730)
Cash Flows from Financing Activities		
Shares issued, net of share issuance costs	2,771,424	4,697,868
	2,771,424	4,697,868
Cash Flows from Investing Activities		
Investment in mineral properties	(1,953,975)	(6,026,499)
Investment in equipment	(30,140)	(106,216)
Receipt of mining exploration refund	212,707	-
Reclamation deposits paid	(17,500)	-
Proceeds from the sale of marketable securities	334,825	31,660
	(1,454,083)	(6,101,055)
Effect of foreign exchange rate changes on cash	38,630	(316,713)
Decrease in Cash and Cash Equivalents during the year	(443,601)	(4,120,630)
Cash and Cash Equivalents, Beginning of the year	2,804,423	6,925,053
Cash and Cash Equivalents, End of the year	\$ 2,360,822	\$ 2,804,423

Supplemental Disclosure of Cash and Non-Cash Activities (Note 10)

- see accompanying notes -

KOOTENAY SILVER INC.

((Expressed in Canadian dollars))

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS December 31, 2014 and 2013

1 Reporting Entity:

Kootenay Silver Inc. (the "Company") is a Canadian exploration stage company incorporated under the *Business Corporations Act* (British Columbia). The address of the Company's registered office is 1820 – 1055 West Hastings St. Vancouver, British Columbia, Canada.

The Company is focused on acquiring and exploring mineral properties principally located in North America, with the objective of identifying mineralized deposits economically worthy of subsequent development, mining or sale.

Going Concern

These consolidated financial statements have been prepared on a going concern basis which assumes that the Company will be able to realize its assets and discharge its liabilities in the normal course of business for the foreseeable future. There are conditions and events, which constitute material uncertainties that may cast significant doubt on the validity of this assumption.

The continuing operations of the Company are dependent upon its ability to continue to raise adequate financing and to commence profitable operations in the future. During the year ended December 31, 2014, the Company raised aggregate gross proceeds of \$2,916,050 from the closing of two non-brokered private placements. Subsequent to December 31, 2014, a final tranche raising gross proceeds of \$835,875 was closed. During the year ended December 31, 2013, the Company raised \$4,750,000 from the closing of a private placement that was fully subscribed by Agnico-Eagle Mines Limited. While the Company has been successful in the past at raising funds, there can be no assurance that it will be able to do so in the future.

During the years ended December 31, 2014 and 2013, the Company experienced operating losses and negative operating cash flows; operations of the Company having been primarily funded by the issuance of share capital. The Company expects to incur further losses in the development of its business. Management has estimated that the Company has sufficient financing to complete current work plans; however, future development will require additional financing in order to complete all planned exploration and other programs during the year ending December 31, 2015 and thereafter. If funds are unavailable on terms satisfactory to the Company, some or all planned activities may be cancelled or postponed.

The business of mining and exploration involves a high degree of risk and there can be no assurance that current exploration programs will result in profitable mining operations. The recoverability of resource property expenditures is dependent upon several factors. These include the discovery of economically recoverable reserves, the ability of the Company to obtain the necessary financing to complete the development of these properties, and future profitable production or proceeds from disposition of mineral properties. The Company will need access to capital to continue advancing its primary project located in Sonora Mexico called the Promotorio Silver Project (the "Promontorio"), which includes the discovery of a recent zone of mineralization within the Promotorio concession block called La Negra (the "La Negra Discovery"), as well as other property interests.

These consolidated financial statements do not reflect adjustments that would be necessary if the going concern assumption were not appropriate. If the going concern basis was not appropriate for these consolidated financial statements, then adjustments to the carrying values of assets and liabilities would be necessary.

	December 31, 2014	December 31, 2013
Deficit	\$ 31,990,627	\$ 26,101,022
Working capital	\$ 2,910,818	\$ 3,828,553

KOOTENAY SILVER INC.
(Expressed in Canadian dollars)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2014 and 2013

2 Basis of Presentation:

Statement of Compliance

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards and Interpretations (collectively, "IFRS") applicable to the preparation of financial statements.

The policies applied in these consolidated financial statements are presented in Note 3 and were consistently applied to all the years presented unless otherwise noted. These policies are based on IFRS issued and outstanding as of April 29, 2015, the date the Board of Directors approved the consolidated financial statements.

Functional and presentation currency

These consolidated financial statements are presented in Canadian dollars. Under IFRS, the Canadian dollar is the functional currency of the parent and Kootenay Resources Inc. The functional currency of Minera JM S.A. de C.V. and Kootenay Gold (US) Corp. is the US dollar and Servicios de Exploraciones Sonora, S.A. de C.V. is the Mexican Peso.

Assets and liabilities of the subsidiaries with a functional currency in US dollars and Mexican pesos are translated at the year-end exchange rates, and the results of its operations are translated at average exchange rates for the year. The resulting translation adjustments are recorded in accumulated other comprehensive loss in shareholders' equity. Additionally, foreign exchange gains and losses related to certain intercompany loans that are permanent in nature are included in accumulated other comprehensive loss.

3 Significant Accounting Policies:

The accounting policies set out below have been applied consistently to all years presented in these consolidated financial statements.

The significant accounting policies adopted by the Company are as follows:

Basis of measurement

These consolidated financial statements have been prepared on a historical cost basis, except for available-for-sale financial instruments which are measured at fair value through other comprehensive loss and share based payments which are measured at fair value through profit or loss.

Consolidation

These consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries, Kootenay Resources Inc. (formerly Kootenay Gold Corp) (a company incorporated in Canada), Minera JM S.A. de C.V. (a company incorporated in Mexico), Servicios de Exploraciones Sonora, S.A. de C.V. (a company incorporated in Mexico) and Kootenay Gold (US) Corp. (a company incorporated in US).

Control exists when the Company has the power, directly or indirectly, to govern the financial and operating policies of an entity so as to obtain benefits from its activities. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases. All intercompany transactions and balances have been eliminated in full upon consolidation.

KOOTENAY SILVER INC.
(Expressed in Canadian dollars)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2014 and 2013

3 Significant Accounting Policies *(continued)*:

Critical accounting estimates and judgements

The preparation of the consolidated financial statements requires management to make estimates and judgments that affect the reported amounts of assets and liabilities at the date of the consolidated financial statements, and revenues and expenses for the year. By their nature, these estimates and judgments are subject to uncertainty and the effect on the consolidated financial statements of changes in such estimates in future periods could be significant. Actual results may differ from those estimates and judgements.

Significant estimates used in the preparation of the consolidated financial statements include, but are not limited to:

- (i) asset carrying values and impairment charges;
- (ii) the economic recoverability of exploration expenditures incurred and the probability of future economic benefits from development expenditures incurred;
- (iii) the expected costs of decommissioning liabilities; and,
- (iv) the calculation of share-based compensation and warrants which include the assumptions used in the Black-Scholes option pricing model including volatility, estimated forfeiture rates and expected time until exercise.

The key sources of estimation uncertainty that have a significant risk of causing material adjustment to the amounts recognized in the consolidated financial statements are as follows:

(i) Equipment

The Company estimates the useful lives of equipment based on the period over which the assets are expected to be available for use. The depreciation method and useful lives reflect the pattern in which management expects the asset's future economic benefits to be consumed by the Company. The amounts and timing of recorded expenses for any year would be affected by changes in assumptions and estimates used.

(ii) Exploration and evaluation assets

The Company makes certain estimates and assumptions regarding the recoverability of the carrying values of exploration and evaluation assets. These assumptions are changed when conditions exist that indicate the carrying value may be impaired, at which time an impairment loss is recorded.

(iii) Decommissioning liabilities

The Company recognizes the liability for statutory, contractual, constructive or legal obligations, including those associated with the reclamation of mineral properties, when those obligations result from the exploration or development of its properties. The Company assesses its provision for site reclamation at each reporting date. Significant estimates and assumptions are made in determining the provision for site reclamation, as there are numerous factors that will affect the ultimate liability payable. These factors include estimates of the extent and costs of rehabilitation activities, technological changes, regulatory changes, cost increases as compared to inflation rates, and discount rates. Those uncertainties may result in future actual expenditures differing from the amounts currently provided. The provision at the reporting date represents management's best estimate of the present value of the future reclamation costs required.

KOOTENAY SILVER INC.
(Expressed in Canadian dollars)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2014 and 2013

3 Significant Accounting Policies *(continued)*:

(iv) Share based payments

The Company has an equity-settled share-based scheme for directors, officers, employees and consultants. Services received, and the corresponding increase in equity, are measured by reference to the fair value of the equity instruments at the date of the grant, excluding the impact of any non-market vesting conditions. The fair value of share options is estimated by using the Black-Scholes model on the date of the grant based on certain assumptions. Those assumptions are described in Note 7 and include, among others, expected volatility, expected life of the options and number of options expected to vest. Where vesting conditions exist for share options, the Board reviews progress against those vesting conditions annually and reviews the estimated date of the financial close of project, which will impact the consolidated financial statements. In the event that milestone conditions are not met, it is anticipated that certain options will lapse.

(v) Taxes

Significant management judgement is required to determine the amount of deferred tax assets that can be recognized, based upon the likely timing and the level of future taxable income realized, including the usage of tax planning strategies.

Significant judgments used in the preparation of these consolidated financial statements include, but are not limited to:

- (i) those relating to the assessment of the Company's ability to continue as a going concern; and
- (ii) the determination of functional currency.

Foreign currency transactions

Items included in the financial statements of each consolidated entity are measured using the currency of the primary economic environment in which the entity operates (the "functional currency"). Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transaction. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation of monetary assets and liabilities not denominated in the functional currency of an entity are recognized in the consolidated statements of loss.

Cash and cash equivalents

Cash is comprised of cash on hand. Cash equivalents are short-term, highly liquid investments with original maturities of three months or less that are readily convertible to known amounts of cash and which are subject to an insignificant risk of change in value.

Mineral property interests

Mineral properties corresponded to acquired interests in mining exploration claim tenures and concessions, which include the right to explore, mine, extract and sell all minerals from such claims.

All pre-exploration costs, i.e. costs incurred prior to obtaining the legal right to undertake exploration and evaluation activities on an area of interest, are expensed as incurred. Once the legal right to explore has been acquired, exploration and evaluation expenditures are capitalized in respect of each identifiable area of interest until the technical feasibility and commercial viability of extracting a mineral resource are demonstrable. Exploration and evaluation assets are carried at historical cost, less any impairment losses recognized.

KOOTENAY SILVER INC.
(Expressed in Canadian dollars)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2014 and 2013

3 Significant Accounting Policies *(continued)*:

When technical feasibility and commercial viability of extracting a mineral resource are demonstrable for an area of interest, the Company stops capitalizing exploration and evaluation costs for that area, tests recognized exploration and evaluation assets for impairment and reclassifies any unimpaired exploration and evaluation assets either as tangible or intangible mine development costs according to the nature of the assets.

The amounts shown for mineral properties do not necessarily represent present or future values. The recoverability of mineral properties is dependent upon the discovery of economically recoverable reserves, the ability of the Company to obtain the necessary financing and permits necessary to complete the development and future profitable production, or proceeds from the disposition thereof.

Although the Company has taken steps to verify title to mineral properties in which it has an interest, according to usual industry standards for the stage of exploration of such properties, these procedures do not guarantee the Company's title. Such properties may be subject to prior agreements or transfers and title that are not in the public domain or the title registry office and/or may be affected by undetected defects.

Equipment

Equipment is recorded at cost less accumulated depreciation and accumulated impairment losses. Depreciation methods, useful lives and residual values are reviewed at each financial year-end and adjusted, if appropriate. Depreciation is recognized using the declining balance method at the following annual rates:

Office furniture	20%
Computer equipment	30%
Exploration equipment	30%
Vehicles	30%

For leasehold improvements, the Company recognized depreciation using the straight-line method over the term of the lease. For the year of acquisition, the rate is one-half of the above. The Company reviews the carrying values of its property and equipment for impairment at each reporting period. If the carrying value exceeds the amount recoverable, a write-down to their fair value is charged to the consolidated statements of loss.

Decommissioning liabilities

The Company recognizes the present value of estimated costs of legal and constructive obligations for decommissioning liabilities in the year in which it is incurred or when there is a legal or constructive obligation. The fair value of asset retirement obligation is recorded as a liability and a corresponding increase in mineral properties. Changes in the liability for decommissioning liabilities due to the passage of time will be measured by applying an interest method of allocation. The amount will be recognized as an increase in the liability and an accretion expense in the statement of loss. Changes resulting from revisions to the timing or the amount of the original estimate of undiscounted cash flows are recognized as an increase or a decrease to the carrying amount of the liability and the related long-lived asset. Actual costs incurred upon settlement are charged against the decommissioning liabilities. Any difference between the actual costs and the recorded liability is recognized as a gain or loss in earnings in the year in which the settlement occurs. At present, estimated future site restoration costs for the Company's mineral property interests are considered minimal.

Marketable securities

Marketable securities are recorded at market value by reference to published price quotations in an active market, and are written down when the value is impaired on other-than-temporary basis, or when no other means exist to independently confirm the recorded value is reasonable. Realized gains or losses on the sale of securities are determined based on specific cost basis. Unrealized gains or losses for available-for-sale securities are recorded at market value and included in other comprehensive loss (income) on a quarterly basis.

KOOTENAY SILVER INC.
(Expressed in Canadian dollars)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2014 and 2013

3 Significant Accounting Policies *(continued)*:

Impairment

i) Financial assets

A financial asset is impaired if objective evidence indicates that a loss event has occurred after the initial recognition of the asset, and that the loss event had a negative effect on the estimated future cash flows of that asset that can be estimated reliably.

ii) Non-financial assets

The carrying amounts of mineral properties are assessed for impairment only when indicators of impairment exist, typically when one of the following circumstances applies:

- Exploration rights have / will expire in the near future;
- No future substantive exploration expenditures are budgeted;
- No commercially viable quantities discovered and exploration and evaluation activities will be discontinued;
or
- Exploration and evaluation assets are unlikely to be fully recovered from successful development or sale.

If any such indication exists, then the assets' recoverable amount is estimated.

The recoverable amount of an asset or cash-generating unit is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For the purpose of impairment testing, assets that cannot be tested individually are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups of assets (the "cash-generating unit", or "CGU"). The level identified by the group for the purposes of testing exploration and evaluation assets for impairment corresponds to each mining property.

An impairment loss is recognized if the carrying amount of an asset or its CGU exceeds its estimated recoverable amount. Impairment losses are recognized in profit or loss. Impairment losses recognized in respect of CGUs are allocated to the assets in the unit (group of units) on a pro rata basis.

Impairment losses recognized in prior years are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation, if no impairment loss had been recognized.

Share capital

Common shares are classified as equity. The Company records proceeds from share issuances net of share issuance costs. Share capital issued for non-monetary consideration is recorded at the fair market value of the shares on the date the shares are issued.

KOOTENAY SILVER INC.
(Expressed in Canadian dollars)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2014 and 2013

3 Significant Accounting Policies *(continued)*:

Earnings per share

Basic earnings per share is calculated by dividing the profit or loss attributable to the common shareholders of the Company divided by the weighted average number of common shares outstanding during the year. The diluted earnings per share is calculated based on the weighted average number of common shares outstanding during the year, plus the effects of the dilutive common share equivalents. This method requires that the dilutive effect of outstanding options and warrants issued be calculated using the treasury stock method. This method assumes that all common share equivalents have been exercised at the beginning of the year (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 common shares during the year.

The calculation of diluted loss per share excludes the effects of various conversions and exercise of options and warrants that would be anti-dilutive.

Warrants

Warrants are classified as equity as they are derivatives over the Company's own equity that will be settled only by the Company exchanging a fixed amount of cash for a fixed number of the Company's own equity instruments.

When shares and warrants are issued at the same time, the proceeds are allocated first to warrants issued, according to their fair value using the Black-Scholes pricing model, the residual value being allocated to shares.

Share-based payments

The grant date fair value of share-based payment awards granted to employees, officers, consultants and directors is recognized as a share-based payment expense, with a corresponding increase in contributed surplus, over the period during which the employees, officers, consultants and directors unconditionally become entitled to the awards. The amount recognized as an expense is adjusted to reflect the number of awards for which the related service and non-market vesting conditions are expected to be met, such that the amount ultimately recognized as an expense is based on the number of awards that do meet the related service and non-market performance conditions at the vesting date.

KOOTENAY SILVER INC.
(Expressed in Canadian dollars)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2014 and 2013

3 Significant Accounting Policies *(continued)*:

Financial instruments

All financial instruments are recognised, initially, at fair value. The Company classifies financial instruments as available-for-sale, fair value through profit or loss, loans and receivables, and other liabilities. Financial assets, loans and receivables and financial liabilities other than those designated as fair value through profit or loss, are measured at amortized cost using the effective interest method. Available-for-sale instruments are measured at fair value with unrealized gains and losses recognized in other comprehensive income, unless an unrealized loss is considered to be other than temporary in which case the loss is recorded on the consolidated statements of loss for the year. Instruments classified as fair value through profit or loss are measured at fair value with unrealized gains and losses recognized on the consolidated statements of loss.

Transaction costs on financial assets and liabilities classified other than fair value through profit or loss are treated as part of the investment cost.

All financial assets except those measured at fair value through profit or loss are subject to review for impairment at least at each reporting date. Financial assets are impaired when there is objective evidence of impairment as a result of one or more events that have occurred after initial recognition of the asset and that event has an impact on the estimated future cash flows of the financial asset or the group of financial assets. The Company has classified its financial assets and liabilities as follows:

<u>Fair value through profit or loss</u>	<u>Loans and receivables</u>	<u>Available-for-sale</u>	<u>Other liabilities</u>
Cash and cash equivalents	Receivable and advances Advances (Exploration) and deposits (Reclamation)	Marketable securities	Accounts payable and accrued liabilities

Comprehensive income/loss

Other comprehensive income represents the change in net equity for the year that arises from unrealized gains and losses on available-for-sale financial instruments, and foreign currency translation adjustments on foreign subsidiaries. Amounts included in other comprehensive income are shown net of tax. Cumulative changes in other comprehensive income are included in accumulated other comprehensive loss which is presented as a separate category in shareholders' equity.

Finance income and finance costs

Interests received and interests paid are classified under operating activities in the consolidated statements of cash flows.

KOOTENAY SILVER INC.
(Expressed in Canadian dollars)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2014 and 2013

3 Significant Accounting Policies *(continued)*:

Income taxes

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

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

Deferred tax is recognized using the liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognized on the initial recognition of assets or liabilities in a transaction that is not a business combination. In addition, deferred tax is not recognized for taxable temporary differences arising on the initial recognition of goodwill. Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date. Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset, and they relate to income taxes levied by the same tax authority on the same taxable entity, or on different tax entities, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realized simultaneously.

A deferred tax asset is recognized to the extent that it is probable that future taxable profits will be available against which the temporary difference can be utilized. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realized.

Segment reporting

An operating segment is a component of the Company that engages in business activities from which it may earn revenues and incur expenses, including revenues and expenses that relate to transactions with any of the Company's other components. Results of all operating segments' are reviewed regularly by the Company's management to make decisions about resources to be allocated to the segment and assess its performance, and for which discrete financial information is available. The Company manages its business on the basis of one reportable segment under two geographic regions, being Canada and Mexico.

Risk management

The Company's activities expose it to a variety of financial risks: market risk (foreign exchange risk), credit risk and liquidity risk. The Company's risk management program focuses on ensuring liquidity is available to the Company in order to fund its exploration efforts. Risk management is the responsibility of the Company's management who identifies and evaluates financial risks.

KOOTENAY SILVER INC.
(Expressed in Canadian dollars)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2014 and 2013

3 Significant Accounting Policies *(continued)*:

The following new standards, interpretations and amendments were issued by the International Accounting Standards Board ("IASB") or the International Financial Reporting Interpretations Committee ("IFRIC"), and are effective for annual periods beginning on or after January 1, 2014.

New accounting standards adopted during 2014

The following standards were applied for periods beginning on or after January 1, 2014 and had no material impact on the Company's consolidated financial statements:

IFRS 2, *Share-based Payment* ("IFRS 2"): Amended to clarify the definition of a vesting condition and separately define performance and service conditions.

IFRS 3, *Business Combinations* ("IFRS 3"): Amended to clarify that an obligation to pay contingent consideration that meets the definition of a financial instrument is classified as a financial liability or as equity on the basis of the definitions in IAS 32. Non-equity consideration is measured at fair value at each reporting date, with changes recognized in the results of operations. As well, the amendment clarifies that IFRS 3 does not apply to the formation of any joint arrangement and that the scope exemption only applies in the financial statements of the joint arrangement itself.

IFRS 13, *Fair Value Measurement* ("IFRS 13"): Amended to clarify that the portfolio exception in IFRS 13, which allows fair value measurement of a group of financial assets and liabilities on a net basis, applies to all contracts within the scope of IAS 39 or IFRS 9, regardless of whether they meet the definitions of financial assets or liabilities as defined in IAS 32.

IFRIC 21, *Levies* ("IFRIC 21"): Amended to provide guidance for the accounting for an obligation to pay a levy that is not income tax. The interpretation addresses what the obligating event is that gives rise to pay a levy and when should a liability be recognized.

IAS 24, *Related Party Disclosures* ("IAS 24"): Amended to include as a related party, an entity that provides key management personnel services to the reporting entity or to the parent of the reporting entity.

IAS 32, *Financial Instruments: Presentation* ("IAS 32"): Amended to provide further clarity around details relating to the right to offset and the application of offsetting under certain circumstances.

Future accounting standards issued but not yet adopted

The following amendments to existing standards were issued by the IASB and are effective for annual periods beginning on or after January 1, 2015. Pronouncements that are not applicable or do not have a significant impact to the Company have been excluded from below:

The IASB intends to replace IAS 39, *Financial Instruments: Recognition and Measurement* in its entirety with IFRS 9, *Financial Instruments* ("IFRS 9") and to reduce the complexity in the classification and measurement of financial instruments. The completed version of IFRS 9 includes classification and measurement, impairment and hedge accounting requirements and is effective for annual periods beginning on or after January 1, 2018. The Company is currently evaluating the impact of IFRS 9 on its consolidated financial statements.

KOOTENAY SILVER INC.
(Expressed in Canadian dollars)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2014 and 2013

4 Marketable Securities:

Marketable securities are classified as available for sale financial instruments, which are adjusted to market value at the end of the reporting period. As at December 31, 2014, the market value of securities held is \$173,815 (2013 – \$382,140). The Company recorded an unrealized comprehensive loss of \$184,325 (2013 – \$149,123) for fair value adjustments to marketable securities.

5 Equipment:

	Vehicle	Office Equipment	Computer Equipment	Leasehold	Total
Cost					
Balance December 31, 2012	223,000	58,374	139,288	2,828	423,490
Additions	-	8,111	49,010	57,493	114,614
Balance December 31, 2013	223,000	66,485	188,298	60,321	538,104
Additions	-	-	30,352	-	30,352
Impaired	-	-	(15,960)	-	(15,960)
Effect of foreign exchange	9,691	-	13,452	-	23,143
Balance December 31, 2014	232,691	66,485	216,142	60,321	575,639
Accumulated Depreciation					
Balance December 31, 2012	127,029	30,083	70,031	283	227,426
Depreciation for year	27,434	5,578	18,546	5,371	56,929
Balance December 31, 2013	154,463	35,661	88,577	5,654	284,355
Depreciation for year	28,247	5,023	19,364	12,347	64,981
Effect of foreign exchange	4,528	800	3,103	-	8,431
Balance December 31, 2014	187,238	41,484	111,044	18,001	357,767
Carrying Value					
December 31, 2013	68,537	30,824	99,721	54,667	253,749
December 31, 2014	45,453	25,001	105,098	42,320	217,872

KOOTENAY SILVER INC.
(Expressed in Canadian dollars)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2014 and 2013

6 Mineral Properties:

	MEXICO				Mexico Total	CANADA			Canada Total	2014 Total	2013 Total
	Promontorio	Sonora Anomalies	Cervantes	San Diego*		Nechako Region	Silver Fox	Other			
	\$	\$	\$	\$	\$	\$	\$	\$	\$	\$	
Acquisition Costs											
Balance, beginning	3,658,642	591,681	-	-	4,250,323	145,630	32,500	1,126,535	1,304,665	5,554,988	5,442,488
Incurred	-	-	-	17,189	17,189	-	-	57,550	57,550	74,739	112,500
Balance, ending	3,658,642	591,681	-	17,189	4,267,512	145,630	32,500	1,184,085	1,362,215	5,629,727	5,554,988
Exploration Expenditures											
Balance, beginning	24,749,904	6,216,987	127,774	2,602	31,097,267 ¹	448,806	441,029	5,608,197	6,498,032	37,595,299 ¹	31,633,425 ¹
Assaying and Lab	135,811	8,717	-	8,337	152,865	3,999	2,393	6,073	12,465	165,330	574,885
Camp Costs	200,837	4,691	13,847	5,129	224,504	-	-	-	-	224,504	739,725
Drafting	85,794	36,132	7,225	10,972	140,123	5,500	20,515	28,070	54,085	194,208	212,154
Drilling	471,316	-	-	-	471,316	-	-	-	-	471,316	3,000,729
Geological mapping	69,461	40,560	2,440	9,182	121,643	-	28,420	1,272	29,692	151,335	207,035
Geophysics	9,610	-	-	-	9,610	-	-	-	-	9,610	128,842
Maintenance	104,226	89,235	2,418	5,643	201,522	1,729	13,181	19,458	34,368	235,890	744,453
Miscellaneous	12,674	5,576	-	-	18,250	-	-	-	-	18,250	78,008
Prospecting	225,735	48,098	2,879	31,295	308,007	21,198	22,850	28,222	72,270	380,277	447,041
Rock Sampling	72,000	-	-	-	72,000	-	-	-	-	72,000	76,476
Metallurgical testing	-	-	-	-	-	-	-	-	-	-	30,578
Incurred	1,387,464	233,009	28,809	70,558	1,719,840	32,426	87,359	83,095	202,880	1,922,720	6,239,926
Balance, ending	26,137,368	6,449,996	156,583	73,160	32,817,107	481,232	528,388	5,691,292	6,700,912	39,518,019	37,873,351
Total property balance	29,796,010	7,041,677	156,583	90,349	37,084,619	626,862	560,888	6,875,377	8,063,127	45,147,746	43,428,339
Recovery of costs	-	(3,466,284)	-	-	(3,466,284)	-	-	(2,616,148)	(2,616,148)	(6,082,432)	(6,071,939)
Mineral exploration refund	-	-	-	-	-	-	(624)	(212,083)	(212,707)	(212,707)	-
Proceeds from sale	-	-	-	-	-	-	-	(230,000)	(230,000)	(230,000)	-
Option payment received	-	(8,000)	-	-	(8,000)	-	-	(84,000)	(84,000)	(92,000)	(86,000)
Impaired or disposed	(290,896)	(2,612,954)	(14,034)	-	(2,917,884)	(555,187)	-	(3,359,983)	(3,915,170)	(6,833,054)	(3,552,638)
Cumulative mineral property	29,505,114	954,439	142,549	90,349	30,692,451	71,675	560,264	373,163	1,005,102	31,697,553	33,717,768

¹Includes foreign exchange related to translation of foreign operations

*Earn-in option agreement

KOOTENAY SILVER INC.
(Expressed in Canadian dollars)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2014 and 2013

6 Mineral Properties *(continued)*:

Promontorio - Sonora State, Mexico

The Company entered into an agreement on October 20, 2006 with Siete Campanas de Plata, S.A de C.V. ("Siete"), Exploration Canada De Oro, SA de CV ("ECO") and the Mexican Government Agency ("FIFOMI") to acquire an unencumbered 100% registered and beneficial interest in the Promontorio Concession, which includes the former producing Promontorio Mine Site. Upon completion of a bankable feasibility study or commencement of production, the Company must pay the remaining cash balance of US\$210,000 to Siete and ECO. The Promontorio claims now cover approximately 56,000 hectares, and are located in the historic silver and gold producing Sierra Madre Region of Northwest Mexico.

A 1% net smelter royalty is payable to Siete on the core claims of Promontorio of which the Company can purchase 50% of this net smelter royalty at any time for US\$500,000. The Company also has a first right of refusal to purchase the remaining 50% of this royalty. Additionally, a 2% net smelter royalty is payable to ECO on the core and surrounding claims. The Company may upon commencement of commercial production or sooner purchase 50% of this net smelter return for US\$1,000,000. The Company also has a right of first refusal on the remaining 50% of this royalty.

Sonora Concessions – Northwest Sonora Mexico

Santa Lucia - Southern Sonora State, Mexico

On May 1, 2006, amended September 27, 2006, the Company entered into an agreement and acquired a 100% interest in two mineral claims comprised of 9,350 hectares. During the year ended December 31, 2014, the Company abandoned one of the claims totalling 9,330 hectares. A 2% net smelter return is payable on the remaining claim. The Company may purchase 50% of the net smelter return for US\$1,000,000 and has the right of first refusal on the remaining 50%.

San Diego – Northwest Sonora, Mexico

On April 8, 2014, the Company entered into an option agreement to acquire an undivided interest in the San Diego concession from an arms-length party. Under the terms of the agreement, the Company must issue 100,000 common shares of the Company; and make total cash payments of US\$480,000 within a four-year period. During the year ended December 31, 2014, the Company made an initial payment of US\$15,000. The optionee retains a 2% net smelter return, which can be purchased by the Company for US\$750,000 for each percentile.

Unless specifically stated otherwise, all Sonora Concessions have been staked by the Company directly.

Other Properties – Southern British Columbia

Copley Property – Nechako Plateau, British Columbia

On February 23, 2010, the Company entered into an option agreement whereby it was granted the right to earn a 100% undivided interest in 10 mineral tenures totaling approximately 2,927 hectares collectively named as the Copley Property. Under the agreement the Company must make total cash payments of \$80,000; issue an aggregate total of 130,000 common shares and make a cash payment of \$5 per metre drilled to a maximum of 100,000 metres. The Company has issued 90,000 shares with a fair value of \$66,400, including 30,000 issued with a fair value of \$12,300 during the year ended December 31, 2014. The Company has paid \$55,000, including \$15,000 paid during the year ended December 31, 2014.

KOOTENAY SILVER INC.
(Expressed in Canadian dollars)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2014 and 2013

6 Mineral Properties *(continued)*:

The Fox and Two Times Fred Properties – Nechako Plateau, British Columbia

On July 8, 2014, the Company entered into a letter agreement with Theia Resources Ltd. (“Theia”), whereby the Company granted the right to Theia to earn a 60% undivided interest in the Fox and Two Times Fred Properties (the “Properties”). Under the terms of the agreement, Theia must issue an aggregate total of 750,000 common shares of Theia to the Company; and finance an aggregate \$2,500,000 of exploration expenditures on the Properties within a five-year period.

The Two Times Fred property is being optioned by the Company effective July 1, 2014, pursuant to a grubstake agreement. To maintain its option, the Company must make total cash payments of \$80,000; issue an aggregate total of 130,000 common shares and make a cash payment of \$5 per metre drilled to a maximum of 100,000 metres. Subsequent to December 31, 2014, an initial payment of \$5,000 has been made.

During the year ended December 31, 2011, the Company optioned the Fox property pursuant to a grubstake agreement. To maintain its option, the Company must make total cash payments of \$80,000; issue an aggregate total of 130,000 common shares and make a cash payment of \$5 per metre drilled to a maximum of 100,000 metres. The Company has made cash payments of \$55,000, including \$20,000 paid during the year ended December 31, 2014 and issued 65,000 shares with a fair value of \$66,850. Of the total 65,000 shares issued, 25,000 shares with a fair value of \$10,250 were issued during the year ended December 31, 2014.

Additional properties have been staked and are currently being evaluated to determine the viability of further exploration or development. This includes the Silver Fox Property, which also falls under the Kennedy Grubstake Agreement whereby a NSR was granted to the Kennedy Group eliminating the need for share issuance.

During the year ended December 31, 2014, the Company expensed \$94,618 (2013 - \$253,803) related to other property investigation expense and recorded an aggregate total impairment expense of \$3,215,783 (2013 - \$944,199) related to mineral properties located in both Mexico and Canada. Once the Company has made its evaluations, the properties will be either be abandoned or acquired under the terms of the Grubstake Agreements.

Title to Mineral Property Interests

Although the Company has taken steps to verify the title to mineral properties in which it has an interest, in accordance with industry standards for the current stage of exploration of such properties, these procedures do not guarantee the Company’s title. Property title may be subject to unregistered prior agreements or transfers and title may be affected by undetected defects.

7 Share Capital and Reserves:

Authorized:

The authorized share capital of the Company is an unlimited number of common shares without par value and an unlimited number of preferred shares without par value. All issued shares, consisting of only common shares are fully paid.

KOOTENAY SILVER INC.
(Expressed in Canadian dollars)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2014 and 2013

7 Share Capital and Reserves *(continued)*:

Options and Warrants:

Stock option and share purchase warrant transactions are summarized as follows:

	Warrants		Options	
	Number	Weighted Average Exercise Price	Number	Weighted Average Exercise Price
Outstanding, January 1, 2013	7,048,100	\$ 1.30	5,199,750	\$ 1.11
Granted	3,125,000	1.08	1,952,000	0.66
Expired/Cancelled	(1,221,500)	1.15	(1,065,000)	1.72
Outstanding, December 31, 2013	8,951,600	\$ 1.24	6,086,750	\$ 0.86
Granted	9,366,833	0.56	-	-
Expired/Cancelled	(1,896,600)	1.39	(944,750)	0.65
Outstanding, December 31, 2014	16,421,833	\$0.84	5,142,000	\$ 0.89

Warrants

As at December 31, 2014, the Company had outstanding share purchase warrants, enabling holders to acquire common shares as follows:

	Number of Shares	Exercise Price	Expiry Date
	3,125,000	1.08	April 26, 2015
	3,430,000	1.30	October 25, 2015
	500,000	1.30	October 30, 2015
	5,433,500	0.55	July 18, 2016
	1,803,333	0.55	August 18, 2016
	2,120,000	0.60	December 23, 2016
	16,421,833		

The weighted average remaining life of the outstanding warrants is 1.20 years (2013 – 0.89 years).

The fair value of warrants is estimated using the Black Scholes option-pricing model. Warrants are included in contributed surplus until exercised, at which time they are transferred into share capital.

During the year ended December 31, 2014, the Company completed a non-brokered private placement of 7,246,833 units at a price of \$0.30 per unit consisting of one common share and one transferable share purchase warrant, for gross proceeds of \$2,174,050. Each whole warrant entitles the holder to acquire one common share at an exercise price of \$0.55. The private placement was completed in two tranches with the first tranche of 5,433,500 units closed July 18, 2014 and the final tranche of 1,803,333 units closed on August 18, 2014, with the applicable warrants expiring on July 18, 2016 and August 18, 2016, respectively. The Company paid total share issuance costs of \$29,550 and cash finder's fees of \$86,490.

On December 23, 2014, the Company closed the initial tranche of its December 10, 2014 announced non-brokered private placement. A total of 2,120,000 units were issued at a price of \$0.35 per unit consisting of one common share and one transferable share purchase warrant, for gross proceeds of \$742,000. Each whole warrant entitles the holder to acquire one common share at an exercise price of \$0.60 expiring December 23, 2016. The Company paid total share issuance costs of \$7,390. The second tranche of 2,388,214 units for gross proceeds of \$835,875 closed subsequent to December 31, 2014 (see Subsequent Events - Note 17).

KOOTENAY SILVER INC.
(Expressed in Canadian dollars)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2014 and 2013

7 Share Capital and Reserves *(continued)*:

On October 10, 2014, the Company amended the expiration of 3,430,000 and 500,000 share purchase warrants exercisable at \$1.30 from October 25, 2014 and October 30, 2014, respectively by an additional 12 months. In all other respects, the terms of these warrants remain unchanged. As a result of this amendment, the Company reclassified \$13,805 of the fair value of the outstanding warrants from share capital to contributed surplus.

During the year ended December 31, 2013, the Company closed a \$4,750,000 investment by Agnico-Eagle Mines Limited ("Agnico-Eagle") through a non-brokered private placement. A total of 6,250,000 units were issued. As a result of the transaction Agnico-Eagle owns 9.96% of the Company's issued and outstanding shares on a non-diluted basis. Each unit was priced at \$0.76 per Unit and consisted of one common share and one half of one common share purchase warrant. Each whole warrant entitles the holder to purchase one common share at a purchase price of \$1.08 per share expiring April 26, 2015. Subject to certain conditions, Agnico-Eagle has the right to participate in any future equity offerings by the Company in order to maintain its pro rata investment in the Company. The Company paid share issuance costs of \$52,132. Subsequent to December 31, 2014, the 3,125,000 warrants issued expired unexercised.

The following assumptions were used for the Black-Scholes valuation of warrants issued and amended during 2014 and 2013:

	2014	2013
Risk-free interest rate	1.01% – 1.10%	0.94%
Expected life of warrants	12 - 24 months	24 months
Fair value per warrant issued	\$0.004 - \$0.102	\$0.22
Annualized volatility	71% - 83%	67%
Dividend rate	0.00%	0.00%

Option pricing models require the input of highly subjective assumptions, including the expected price volatility. The Company has used historical volatility in its share price to estimate expected volatility. Changes in the subjective input assumptions can materially affect the fair value estimated.

Options

The Company has adopted an incentive stock option plan under the rules of the TSX Venture Exchange ("TSXV") pursuant to which it is authorized to grant options to executive officers, directors, employees and consultants, enabling them to acquire up to 10% of the issued and outstanding common shares of the Company. Under the plan, the exercise price of each option is equal to the market price of the Company's shares on the date of grant. The options can be granted for a maximum term of 10 years and generally vest 25% in specified increments. No individual may hold options to purchase common shares of the Company exceeding 5% of the total number of common shares outstanding from time to time. Pursuant to the policies of the TSXV, shares issued on exercise of options are restricted from trading during the four month period subsequent to the date of grant.

For the year ended December 31, 2014, the Company did not grant any share purchase options.

During the year ended December 31, 2013, the Company granted a total of 1,952,000 share purchase options to officers, directors, employees and consultants. Each share purchase option is exercisable for a period of 5 years from grant date at an exercise price of \$0.66. The share purchase options vest in increments from the grant date and will be fully vested in 18 months.

Share based payments totalling \$557,762 (2013 - \$1,436,764) were expensed during the year ended December 31, 2014. As at December 31, 2014, 4,654,000 options (2013 - 4,072,750) with a weighted average exercise price of \$0.92 per option (2013 - \$0.90) were fully vested and exercisable. During the year ended December 31, 2014, 944,750 (2013 - 860,000) options expired and nil (2013 - 205,000) options were forfeited.

KOOTENAY SILVER INC.
(Expressed in Canadian dollars)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2014 and 2013

7 Share Capital and Reserves *(continued)*:

As at December 31, 2014, the Company had outstanding stock options enabling holders to acquire common shares of the Company as follows:

Number of Shares	Exercise Price	Expiry Date
120,000	0.77	November 14, 2015
750,000	1.00	March 23, 2016
200,000	1.20	December 11, 2016
2,120,000	1.05	November 26, 2017
1,952,000	0.66	September 18, 2018
5,142,000		

The weighted average remaining life of the options is 2.88 years (2013 – 3.36 years).

For stock options granted to employees, officers, directors and consultants, share based payment expense is measured at fair value and recognized over the vesting period from the date of grant. The fair value of stock options granted during the year ended December 31, 2013 was estimated using the Black-Scholes option-pricing model with the following weighted-average assumptions:

	2013
Risk-free interest rate	1.90%
Expected life of options	5 years
Fair value per option granted	\$0.52
Annualized volatility	94%
Forfeiture rate	0.00%
Dividend rate	0.00%

Option pricing models require the input of highly subjective assumptions, including the expected price volatility. The Company has used historical volatility in its share price to estimate expected volatility. Changes in the subjective input assumptions can materially affect the fair value estimated.

Earnings per share

The calculation of basic loss per share for the year ended December 31, 2014 was based on the loss of \$5,889,605 (2013 - \$4,838,647) and the weighted average number of common shares outstanding of 66,064,625 (2013 – 60,805,535) respectively. The Company does not have any instruments that would give rise to a dilution effect as of December 31, 2014. The Company has 5,142,000 options and 16,421,833 warrants that are anti-dilutive and thus, not included in diluted loss per share as of December 31, 2014.

KOOTENAY SILVER INC.
(Expressed in Canadian dollars)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2014 and 2013

8 Receivables:

The Company's receivables are as follows:

	December 31, 2014	December 31, 2013
IVA/GST receivable	\$ 609,290	\$ 606,280
Receivable	94,960	227,997
Advances receivable	20,391	11,804
Total	\$ 724,641	\$ 846,081

9 Income Taxes:

The following table reconciles the expected income tax expense (recovery) at the Canadian statutory income tax rates to the amounts recognized in the consolidated statements of operations and comprehensive loss for the years ended December 31, 2014 and 2013:

	2014	2013
Loss before taxes	(5,889,605)	(4,838,647)
Statutory tax rate	26.00%	25.75%
Expected income tax recovery	(1,531,297)	(1,245,952)
Non-deductible items	(136,884)	557,630
Change in estimates	3,283	69,008
Other	-	-
Change enacted tax rate	43,499	(194,115)
Functional currency adjustments	(1,002,845)	(560,563)
Foreign Tax Rate Difference	(155,530)	(37,468)
Change in Deferred tax asset not recognized	2,779,774	1,411,460
Total income taxes (recovery)	-	-

The British Columbia corporate tax rate has increased during the year, resulting in an increase in the Company's combined statutory tax rate.

KOOTENAY SILVER INC.
(Expressed in Canadian dollars)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2014 and 2013

9 Income Taxes *(continued)*:

Deferred taxes reflect the tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and their tax values. Deferred tax assets (liabilities) at December 31, 2014 and 2013 are comprised of the following:

Canada

	2014	2013
Non-capital loss carryforwards	3,932,968	3,231,062
Exploration and evaluation assets	1,287,752	1,062,300
Capital losses	103,361	113,088
Property and equipment	40,053	29,929
Financial instrument	63,590	73,428
Financing costs	128,918	160,298
	5,556,642	4,670,105
Deferred tax asset not recognized	5,556,642	4,670,105
Net deferred tax asset (liability)	-	-

Mexico

	2014	2013
Net operating loss carryforwards	6,980,599	6,294,003
Property and equipment	49,761	34,286
Financial instrument	-	(134,670)
Exploration and evaluation assets	(3,911,394)	(5,101,796)
	3,118,966	1,091,823
Deferred tax asset not recognized	3,118,966	1,091,823
Net deferred tax asset (liability)	-	-

KOOTENAY SILVER INC.

(Expressed in Canadian dollars)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2014 and 2013

9 Income Taxes (continued):

The Company has non capital loss carryforwards of approximately \$15,126,797 (2013: \$12,427,157), which may be carried forward to apply against future year income tax for Canadian income tax purposes, subject to the final determination by taxation authorities, expiring in the following years:

Canadian	
	2014
2025	197,017
2026	424,974
2027	630,148
2028	1,176,346
2029	1,925,432
2030	2,031,522
2031	2,200,884
2032	1,645,917
2033	1,901,800
2034	2,992,757
TOTAL	15,126,797

In addition, the Company has capital losses of \$869,911, which may be carried forward indefinitely and applied to reduce future Canadian capital gains.

The Company has net operating loss carryforwards of approximately \$23,268,657 (2013: \$20,980,007) which may be carried forward to apply against future year income for Mexican tax purposes, expiring in the following years:

Mexican	
	2014
2015	139,177
2016	-
2017	3,559,596
2018	6,828,094
2019	1,308,119
2020	2,816,616
2021	7,811,597
2022	207,844
2023	212,472
2024	385,142
TOTAL	23,268,657

KOOTENAY SILVER INC.
(Expressed in Canadian dollars)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2014 and 2013

10 Supplemental Disclosure of Cash and Non-Cash Activities:

The following transactions incurred during the year did not include cash:

	2014	2013
Acquisition of shares as proceeds from option of mineral property	\$ (6,000)	\$ (84,000)
Issuance of share capital for acquisition mineral property interests	22,550	52,500
Shares received as proceeds on sale of mineral property	(230,000)	-
Receivable and advances for mineral property costs	(5,365)	(23,592)
Mineral property costs included in accounts payable	44,475	175,131

11 Related Party Transactions and Balances:

Except as disclosed elsewhere in these consolidated financial statements the following related party transactions were incurred in the normal course of business and were measured at the exchange amount:

	2014	2013
Management fees charged by companies controlled by a director and/or officers	\$ 503,000	\$ 503,000
Consulting, administrative and geological fees charged by a company with common officers	120,000	120,000

The Company has entered into a consulting agreement with Makwa Exploration Ltd. for the services of James McDonald to act as the Company's President and CEO, and with Manly Capital Corp. for the services of Kenneth Berry to act as the Company's Chairman. The base monthly fee is \$15,000 under each agreement. The consulting agreement was effective as of January 1, 2008 and expired on December 31, 2009; on expiration, the agreement extends in increments of 24 months, until terminated.

Effective September 1, 2008, the Company entered into an administrative services agreement with Touchstone Capital Corp. a private company indirectly related to two common officers of the Company. Touchstone provides services to the Company including assisting in professional analysis and planning of exploration programs, promotional materials; providing access to secretarial services and providing such other additional instructions and directions as the Company may require. For the year ended December 31, 2014, the Company incurred expenses of \$120,000 (2013 - \$120,000) under the administrative services contract.

In addition to the above:

- a) Included in marketable securities as at December 31, 2014 is \$111,000 (2013 - \$322,000) market value of shares received from companies with directors in common.
- b) Included in exploration recovery of costs as at December 31, 2014 is \$1,151,524 (2013 - \$1,141,026) received from joint venture partners who have a common director and a common officer.
- c) Included in accounts receivable as at December 31, 2014 is \$55,685 (2013 - \$183,272) from companies who have common directors or officers.
- d) Included in accounts payable as at December 31, 2014 is \$130,921 (2013 - \$32,976) to companies who have common directors or officers.
- e) Included in prepaid expenses as at December 31, 2014 is \$nil (2013 - \$1,845) related to office deposits charged by a company with common directors.
- f) For the year ended December 31, 2014, the Company incurred \$60,000 (2013 - \$63,000) for compensation to directors. As at December 31, 2014, \$48,000 (2013 - \$48,000) is held in accounts payable.
- g) For the year ended December 31, 2014, the Company incurred \$30,000 (2013 - \$120,000) for consulting service fees charged by a director.
- h) For the year ended December 31, 2014, the Company incurred \$268,035 (2013 - \$785,050) for share based payment expenses to related parties.

KOOTENAY SILVER INC.
(Expressed in Canadian dollars)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2014 and 2013

12 Contingent Liabilities:

The Company's mineral properties are affected by the laws and regulations concerning environmental protection that exist in the various jurisdictions. It is not possible to estimate the future impact on operating results, if any, as a result of, future changes in regulations or developments.

13 Segmented Information:

The Company has one reportable operating segment, being the acquisition and exploration and future development of mineral properties.

The Company's current assets, non-current assets, current liabilities, and mineral properties and deferred costs by geographic location are as follows:

	December 31, 2014	December 31, 2013
Canada:		
Current asset	\$ 2,587,241	\$ 3,507,543
Mineral property	1,005,102	1,936,814
Other Non-current asset	193,279	188,757
Current liability	(399,216)	(283,338)
	\$ 3,386,406	\$ 5,349,776

	December 31, 2014	December 31, 2013
Mexico:		
Current asset	\$ 740,429	\$ 857,445
Mineral property	30,692,451	31,780,954
Other Non-current asset	130,593	153,492
Current liability	(17,636)	(253,097)
	\$ 31,545,837	\$ 32,538,794

14 Commitments:

The Company entered into a contract for office rent, which commenced January 1, 2013 and expires December 31, 2015. The following table summarizes the Company's total annual obligations under this agreement as at December 31, 2014:

2015	38,028
	\$ 38,028

KOOTENAY SILVER INC.

(Expressed in Canadian dollars)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

December 31, 2014 and 2013

14 Commitments (continued):

The Company entered into a contract for additional office rent, which commenced August 1, 2013 and expires July 31, 2018. The following table summarizes the Company's total annual obligations under this agreement as at December 31, 2014:

2015	4,068
2016	37,066
2017	37,066
2018	21,622
	<u>\$ 99,822</u>

During the year ended December 31, 2014, the Company subleased its additional office lease, reducing its monthly commitment from \$2,967 to \$339 per month until December 31, 2015.

15 Financial Instruments and Financial Risk Management:

The Company's financial instruments include cash and cash equivalents, receivable and advances, marketable securities, advances and deposits, and accounts payable and accrued liabilities. The carrying values of these financial instruments approximate their fair values due to their relatively short periods to maturity and due to the insignificant carrying values of long term financial instruments except for marketable securities, which are measured at fair value through other comprehensive income at each reporting period end.

The Company's risk management policies are established to identify and analyze the risks faced by the Company, to set appropriate risk limits and controls, and to monitor risks and adherence to market conditions and the Company's activities. The Company has exposure to credit risk, liquidity risk and market risk as a result of its use of financial instruments.

This note presents information about the Company's exposure to each of the above risks and the Company's objectives, policies and processes for measuring and managing these risks. Further quantitative disclosures are included throughout these consolidated financial statements. The Board of Directors has overall responsibility for the establishment and oversight of the Company's risk management framework. The Board has implemented and monitors compliance with risk management policies.

(a) Credit risk:

Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its contractual obligations. The Company's accounts receivable relates to receivables from exploration partners who are earning a right to the Company's property via earn-in option agreements, Goods and Services Tax input tax credits and IVA credits (Mexican Value Added Tax refunds) from the Mexican Government. Accordingly, the Company views credit risk on accounts receivable as minimal, being the refund of tax credits in Canada and Mexico to moderate being receivables from exploration partners.

(b) Liquidity risk:

Liquidity risk is the risk that the Company will incur difficulties meeting its financial obligations as they are due. The Company's approach to managing liquidity is to ensure, as far as possible, that it will have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions without incurring unacceptable losses or risking harm to the Company's reputation.

KOOTENAY SILVER INC.
(Expressed in Canadian dollars)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2014 and 2013

15 Financial Instruments and Financial Risk Management *(continued)*:

The Company prepares annual expenditure budgets, which are regularly monitored and updated as considered necessary. To facilitate its expenditure program, the Company raises funds through private equity placements.

The Company anticipates it will have adequate liquidity to fund its financial liabilities through future equity contributions.

As at December 31, 2014, the Company's financial liabilities were comprised of accounts payable and accrued liabilities, which have a maturity of less than one year.

(c) Market risk:

Market risk consists of currency risk, commodity price risk and interest rate risk. The objective of market risk management is to manage and control market risk exposures within acceptable limits while maximizing returns.

(i) Currency risk:

Foreign currency exchange rate risk is the risk that the fair value or future cash flows will fluctuate as a result of changes in foreign exchange rates. Although the Company is considered to be in the exploration stage and has not yet developed commercial mineral interests, the underlying market prices in Canada for minerals are impacted by changes in the exchange rate between the Canadian dollar, the United States dollar and the Mexican Peso. The Company's transactions are denominated in Canadian dollars, United States dollars and the Mexican Peso. The Company has not entered into any arrangements to hedge currency risk but does maintain cash balances within each currency with a predominate balance held in Canadian Dollars. Canadian dollars are exchanged when needed to meet foreign denominated liabilities.

The balances denominated in foreign currency are as follows:

	December 31, 2014	December 31, 2013
	US\$	US\$
Cash	270,685	35,203
Trade accounts payable and accrued liabilities	21,007	-
	Mexican Peso	Mexican Peso
Cash	1,197,494	932,103
Receivables and advances	7,259,702	6,821,319
Trade accounts payable and accrued liabilities	224,237	592,504

The Company has completed a sensitivity analysis to estimate the impact of the change in the foreign exchange rates on net loss for the period. The result of the sensitivity analysis shows a change in +/- 10% in the Mexican Peso exchange rate could have an impact of approximately +/- \$56,000 on the Company's net loss. This result arises primarily because the Company has Mexican Peso denominated cash accounts, accounts receivable and short term liabilities. The actual results of a change in foreign exchange rates would depend on the foreign currency denominated assets and liabilities at the time and could cause the impact on the Company's results to differ from above.

KOOTENAY SILVER INC.
(Expressed in Canadian dollars)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2014 and 2013

15 Financial Instruments and Financial Risk Management *(continued)*:

(ii) Commodity price risk:

Commodity price risk is the risk that the fair value or future cash flows will fluctuate as a result of changes in commodity prices. Commodity prices for minerals are impacted by world economic events that dictate the levels of supply and demand as well as the relationship between the Canadian and United States dollar, as outlined above. The Company is exposed to the price volatilities for precious and base metals that could significantly impact its future operating cash flow. As part of its routine activities, management is closely monitoring the trend of international metal prices.

(iii) Interest rate risk:

Interest rate risk is the risk that future cash flows will fluctuate as a result 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 of cash and cash equivalents is limited because of their short-term investment nature. A variable rate of interest is earned on cash and cash equivalents, changes in market interest rates at the year-end would not have a material impact on the Company's consolidated financial statements.

d) Fair value of financial instruments

The Company classifies its financial instruments measured at fair value at one of three levels according to the relative reliability of the inputs used to estimate the fair value:

December 31, 2014		Level 1	Level 2	Level 3	Total
Marketable securities	\$	173,815	\$ -	\$ -	173,815
Cash and Cash Equivalents	\$	2,360,822	\$ -	\$ -	2,360,822
December 31, 2013		Level 1	Level 2	Level 3	Total
Marketable securities	\$	382,140	\$ -	\$ -	382,140
Cash and Cash Equivalents	\$	2,804,423	\$ -	\$ -	2,804,423

Level 1 – quoted prices (unadjusted) in active markets for identical assets or liabilities;

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

Level 3 – Inputs for the asset or liability that are not based on observable market data (unobservable inputs).

KOOTENAY SILVER INC.
(Expressed in Canadian dollars)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
December 31, 2014 and 2013

16 Capital Management:

The Company's objectives when managing capital are to safeguard the Company's ability to continue as a going concern and to maintain a flexible capital structure which will allow it to pursue the development of its mineral properties. Therefore, the Company monitors the level of risk incurred in its mineral property expenditures relative to its capital structure.

The Company's capital structure includes working capital and shareholders' equity. The Company monitors its capital structure and makes adjustments in light of changes in economic conditions and the risk characteristics of the underlying assets. In order to facilitate the management of capital and the development of its mineral properties, the Company prepares annual expenditure budgets, which are regularly monitored and updated as considered necessary.

To maintain or adjust the capital structure, the Company may issue new equity if available on favourable terms, option its mineral properties for cash and/or expenditure commitments from optionees, enter into joint venture arrangements, or dispose of mineral properties.

The Company's investment policy is to hold cash in interest bearing, Schedule I bank accounts and highly liquid short-term interest bearing investments, with maturities of one year or less which can be liquidated at any time without penalties.

The Company is not subject to externally imposed capital requirements. There has been no change in the Company's approach to capital management during the year ended December 31, 2014.

17 Subsequent Events:

On February 5, 2015, the Company announced that it had closed the final tranche of its December 10, 2014 announced non-brokered private placement and raised gross proceeds of \$835,875 by issuing a total of 2,388,214 units at a purchase price of \$0.35 per unit. Each unit consists of one common share of the Company and one transferable share purchase warrant. Each whole warrant will entitle the holder to acquire one common share at an exercise price of \$0.60 and expire on February 2, 2017. All securities issued in connection with the private placement are subject to a four-month hold period from the date of issue. The Company raised gross aggregate total proceeds of \$1,577,875 with an aggregate total of 4,508,214 units issued. The initial tranche of the placement closed on December 23, 2014, with an issuance of 2,120,000 units for gross proceeds of \$742,000.

On February 23, 2015, the Company announced the issuance of an aggregate total of 2,485,000 incentive stock options to directors, officers, employees and consultants of the Company. The incentive stock options expire on February 24, 2020 and have an exercise price of \$0.35.