

South American Silver Corp.

(An Exploration Stage Company)

**Condensed Consolidated Financial Statements
Third Quarter Ended September 30, 2011**

(Unaudited – expressed in U.S. dollars)

South American Silver Corp.

(An Exploration Stage Company)

Condensed Consolidated Statements of Financial Position

(Unaudited - expressed in U.S. dollars)

| | Note | September 30, 2011 \$ | December 31, 2010 \$ |
|---|------|-----------------------------|----------------------------|
| Assets | | | |
| Current assets | | | |
| Cash and cash equivalents | | 28,636,038 | 35,687,151 |
| Receivables and prepaids | | 593,942 | 221,155 |
| | | <u>29,229,980</u> | <u>35,908,306</u> |
| Non-current assets | | | |
| Equipment | 5 | 234,580 | 78,080 |
| Mining claims and deferred exploration costs | 6 | 16,107,586 | 12,524,955 |
| | | <u>16,342,166</u> | <u>12,603,035</u> |
| Total assets | | <u>45,572,146</u> | <u>48,511,341</u> |
| Liabilities | | | |
| Current liabilities | | | |
| Accounts payable and accrued liabilities | | 607,338 | 838,525 |
| Total liabilities | | <u>607,338</u> | <u>838,525</u> |
| Equity attributable to shareholders | | | |
| Share capital | 7 | 82,116,313 | 79,482,130 |
| Contributed surplus | | 8,389,337 | 5,668,895 |
| Accumulated other comprehensive income (loss) | | (188,955) | 1,265,442 |
| Deficit | | (45,351,887) | (38,743,651) |
| Total equity | | <u>44,964,808</u> | <u>47,672,816</u> |
| Total liabilities and equity | | <u>45,572,146</u> | <u>48,511,341</u> |
| Commitments (notes 7 and 10) | | | |
| Contingencies (note 9) | | | |
| Subsequent events (note 14) | | | |

Approved by the Board of Directors:

(signed) "Paul Haber"

(signed) "John Watson"

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

South American Silver Corp.

(An Exploration Stage Company)

Condensed Consolidated Statements of Loss and Comprehensive Loss

For the three and nine months ended September 30

(Unaudited - expressed in U.S. dollars)

| | Note | Three Month Period Ended Sept. 30, 2011 \$ | Three Month Period Ended Sept. 30, 2010 \$ | Nine Month Period Ended Sept. 30, 2011 \$ | Nine Month Period Ended Sept. 30, 2010 \$ |
|--|------|---|---|--|--|
| General and administrative expenses | | | | | |
| Consulting | 8 | 22,203 | 39,087 | 157,989 | 138,091 |
| Depreciation and amortization | | 15,370 | 7,425 | 29,959 | 26,026 |
| Directors' fees | | 77,749 | 20,500 | 188,238 | 75,250 |
| Filing and transfer agent fees | | 8,889 | 10,645 | 100,889 | 95,013 |
| Office and administration | | 274,658 | 80,067 | 631,949 | 206,986 |
| Professional fees | 8 | 18,176 | 63,728 | 440,323 | 347,201 |
| Reconnaissance and sundry exploration | | 32,527 | 2,140 | 75,840 | 16,616 |
| Shareholder information and investor relations | | 413,054 | 225,032 | 1,262,825 | 498,021 |
| Share-based payments | 7c | 961,962 | 509,048 | 3,353,240 | 684,289 |
| Wages and benefits | | 236,516 | 124,548 | 610,397 | 325,528 |
| | | (2,061,104) | (1,082,220) | (6,851,649) | (2,413,021) |
| Other income (expenses) | | | | | |
| Interest and other income | | 88,616 | 1,382 | 271,644 | 3,511 |
| Foreign currency (loss) gain | | 78,233 | (171,420) | (28,231) | (160,502) |
| | | 166,849 | (170,038) | 243,413 | (156,991) |
| Net loss for the period | | (1,894,255) | (1,252,258) | (6,608,236) | (2,570,012) |
| Other comprehensive income (loss) | | | | | |
| Currency translation differences | | (2,501,189) | 156,671 | (1,454,397) | 149,335 |
| Total comprehensive loss | | (4,395,444) | (1,095,587) | (8,062,633) | (2,420,677) |
| Basic and diluted loss per share | | (0.02) | (0.02) | (0.07) | (0.04) |
| Weighted average number of shares outstanding | | 100,382,076 | 66,359,049 | 99,520,591 | 62,561,434 |

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

South American Silver Corp.

(An Exploration Stage Company)

Condensed Consolidated Statements of Changes in Equity

(Unaudited - expressed in U.S. dollars)

| | Share Capital | | Contributed Surplus | Deficit | AOCI | Total |
|---|---------------|--------------|------------------------|--------------|-------------|-------------|
| | Number | Amount \$ | | | | |
| Balance, January 1, 2011 | 98,205,720 | 79,482,130 | 5,668,895 | (38,743,651) | 1,265,442 | 47,672,816 |
| Shares issued on exercise of warrants | 1,988,693 | 1,608,211 | - | - | - | 1,608,211 |
| Shares issued on exercise of options and share appreciation rights (SAR's) | 241,139 | 34,025 | - | - | - | 34,025 |
| Shares issued on vesting of PSU's | 185,750 | 404,367 | (404,367) | - | - | - |
| Share-based payments | - | - | 3,712,389 | - | - | 3,712,389 |
| Transfer to share capital on exercise of warrants | - | 509,414 | (509,414) | - | - | - |
| Transfer to share capital on exercise of options and SAR's | - | 78,166 | (78,166) | - | - | - |
| Net loss for the period | - | - | - | (6,608,236) | - | (6,608,236) |
| Other comprehensive income: Currency translation differences | - | - | - | - | (1,454,397) | (1,454,397) |
| Balance, September 30, 2011 | 100,621,302 | 82,116,313 | 8,389,337 | (45,351,887) | (188,955) | 44,964,808 |
| Balance, January 1, 2010 | 59,582,915 | 47,251,095 | 2,801,685 | (34,656,330) | - | 15,396,450 |
| Private placements of securities | 6,350,000 | 2,884,553 | - | - | - | 2,884,553 |
| Shares issued on exercise of warrants | 15,625 | 8,912 | - | - | - | 8,912 |
| Shares issued on vesting of RSA's | 1,433,335 | 615,473 | (615,473) | - | - | - |
| Share-based payments | - | - | 775,262 | - | - | 775,262 |
| Transfer to share capital on exercise of warrants | - | 1,723 | (1,723) | - | - | - |
| Warrants issued | - | - | 585,976 | - | - | 585,976 |
| Net loss for the period | - | - | - | (2,570,012) | - | (2,570,012) |
| Other comprehensive income: Currency translation differences | - | - | - | - | 149,335 | 149,355 |
| Balance, September 30, 2010 | 67,381,875 | 50,761,756 | 3,545,727 | (37,226,342) | 149,335 | 17,230,476 |

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

South American Silver Corp.

(An Exploration Stage Company)

Condensed Consolidated Statements of Cash Flows

For the nine months ended September 30

(Unaudited - expressed in U.S. dollars)

| | 2011 \$ | 2010 \$ |
|---|--------------------|--------------------|
| Cash flows (used in) from operating activities | | |
| Net loss for the period | (6,608,236) | (2,570,012) |
| Items not affecting cash | | |
| Investor relation fees settled by warrants | - | 36,282 |
| Depreciation and amortization | 29,959 | 26,026 |
| Share-based payments | 3,353,240 | 684,289 |
| | <u>(3,225,037)</u> | <u>(1,823,415)</u> |
| Changes in non-cash operating working capital | | |
| Change in receivables and prepaids | (390,054) | (101,787) |
| Change in accounts payable and accrued liabilities | (231,213) | (205,971) |
| | <u>(3,846,304)</u> | <u>(2,131,173)</u> |
| Cash flows used in investing activities | | |
| Mining claims and deferred exploration costs | (3,206,189) | (2,284,782) |
| Purchase of equipment | (186,459) | (9,533) |
| | <u>(3,392,648)</u> | <u>(2,294,315)</u> |
| Cash flows from financing activities | | |
| Private placement of units, net of issue costs | - | 3,434,247 |
| Exercise of warrants and options | 1,642,236 | 8,912 |
| | <u>1,642,236</u> | <u>3,443,159</u> |
| Decrease in cash and cash equivalents | (5,596,716) | (982,329) |
| Foreign exchange effect on cash and cash equivalents | (1,454,397) | 149,335 |
| Cash and cash equivalents - Beginning of period | 35,687,151 | 7,013,973 |
| Cash and cash equivalents - End of period | <u>28,636,038</u> | <u>6,180,979</u> |
| Cash and cash equivalents are comprised of: | | |
| Cash | 2,379,641 | 781,411 |
| Cash equivalents | 26,256,397 | 5,399,568 |
| | <u>28,636,038</u> | <u>6,180,979</u> |

Supplemental cash flow information (note 12)

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

South American Silver Corp.

(An Exploration Stage Company)

Notes to Condensed Consolidated Financial Statements

For the three and nine months ended September 30, 2011 and 2010

(Unaudited - expressed in U.S. dollars)

1 Organization and nature of operations

South American Silver Corp. (“SASC” or the “Company”) was incorporated pursuant to the *Canada Business Corporations Act* by articles of incorporation dated September 28, 2006. The Company’s corporate head office is located at Suite 2100 – 650 West Georgia Street, Vancouver, British Columbia, Canada. The Company’s shares are listed on the Toronto Stock Exchange.

The Company’s principal activities include the acquisition, exploration and development of mineral properties. The principal countries where the Company is undertaking exploration activities are Bolivia and Chile. Property interests in these countries are held through various wholly owned subsidiaries.

The recoverability of amounts shown as mining claims and deferred exploration costs is dependent upon the discovery of economically recoverable reserves, the Company’s ability to obtain financing to develop the properties, and the ultimate realization of profits through future production or sale of the properties.

2 Basis of presentation and adoption of International Financial Reporting Standards

The Company prepares its financial statements in accordance with Canadian generally accepted accounting principles as set out in the Handbook of the Canadian Institute of Chartered Accountants (“CICA Handbook”). In 2010, the CICA Handbook was revised to incorporate International Financial Reporting Standards (“IFRS”), and require publicly accountable enterprises to apply such standards effective for years beginning on or after January 1, 2011. Accordingly, the Company commenced reporting on this basis in its 2011 interim consolidated financial statements. In these financial statements, the term “Canadian GAAP” refers to Canadian GAAP before the adoption of IFRS.

These condensed interim consolidated financial statements have been prepared in accordance with IFRS applicable to the preparation of interim financial statements, including IAS 34, *Interim Financial Reporting*, and IFRS 1, *First-time Adoption of International Financial Reporting Standards*. The accounting policies followed in these interim financial statements are the same as those applied in the Company’s interim financial statements for the period ended March 31, 2011. The Company has consistently applied the same accounting policies throughout all periods presented, as if these policies had always been in effect. Note 4 discloses the impact of the transition to IFRS on the Company’s reported equity as at September 30, 2010 and comprehensive income for the three and nine months ended September 30, 2010, including the nature and effect of significant changes in accounting policies from those used in the Company’s consolidated financial statements for the year ended December 31, 2010.

The accounting policies applied in these condensed interim consolidated financial statements are based on IFRS effective for the year ended December 31, 2011, as issued and outstanding as of November 10, 2011, the date the Board of Directors approved the statements. Any subsequent changes to IFRS that are given effect in the company’s annual consolidated financial statements for the year ending December 31, 2011 could result in restatement of these condensed interim consolidated financial statements, including transition adjustments recognized on change-over to IFRS. The condensed interim consolidated financial statements should be read in conjunction with the Company’s Canadian GAAP annual financial statements for the year ended December 31, 2010, and the Company’s condensed interim consolidated financial statements for the quarter ended March 31, 2011 prepared in accordance with IFRS applicable to interim financial statements.

South American Silver Corp.

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Notes to Condensed Consolidated Financial Statements

For the three and nine months ended September 30, 2011 and 2010

(Unaudited - expressed in U.S. dollars)

3 Accounting standards issued but not yet applied

Amendments to IFRS 7 “Financial Instruments: Disclosures”

This amendment increases the disclosure required regarding the transfer of financial assets, especially if there is a disproportionate amount of transfer transactions that take place around the end of a reporting period. This amendment is effective for annual periods beginning on or after July 1, 2011.

New standard IFRS 9 “Financial Instruments”

IFRS 9 as issued reflects the first phase of the IASB’s work on the replacement of IAS 39, “Financial Instruments: Recognition and Measurement”, and applies to the classification and measurement of financial assets as defined in IAS 39. The standard is effective for annual periods beginning on or after January 1, 2013.

New standard IFRS 10 “Consolidated Financial Statements”

IFRS 10 builds on existing principles by identifying the concept of control as the determining factor in whether an entity should be included within the consolidated financial statements. The standard provides additional guidance to assist in determining control where this is difficult to assess. This new standard might impact the entities that a group consolidates in its subsidiaries. The standard is effective for annual periods beginning on or after January 1, 2013 with early adoption permitted.

New standard IFRS 11 “Joint Arrangements”

IFRS 11 requires a venturer to classify its interest in a joint arrangement as a joint venture or joint operation. Joint ventures will be accounted for using the equity method of accounting whereas for a joint operation the venturer will recognize its share of the assets, liabilities, revenue and expenses of the joint operation. Under existing IFRS, entities have the choice to proportionately consolidate or equity account for interests in joint ventures. IFRS 11 supersedes IAS 31, Interests in Joint Ventures, and SIC-13, Jointly Controlled Entities—Non-monetary Contributions by Venturers. The standard is effective for annual periods beginning on or after January 1, 2013 with early adoption permitted.

New standard IFRS 12 “Disclosure of Interests in Other Entities”

IFRS 12 is a new standard on disclosure requirements for all forms of interests in other entities, including joint arrangements, associates, special purpose vehicles and other off balance sheet vehicles. This standard is effective for annual periods beginning on or after January 1, 2013 with early adoption permitted.

The Company has not early adopted any of these revised standards and is currently assessing the impact that these standards will have on the consolidated financial statements.

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Notes to Condensed Consolidated Financial Statements

For the three and nine months ended September 30, 2011 and 2010

(Unaudited - expressed in U.S. dollars)

4 Adoption of IFRS

Below is a reconciliation of shareholders' equity as previously reported under Canadian GAAP to IFRS.

| Note | September 30, 2010 | | |
|-----------------------------|--------------------|-----------|-------------------|
| | Cdn GAAP | Adj | IFRS |
| Shareholders' equity | | | |
| | 50,761,756 | - | 50,761,756 |
| | 3,577,941 | (32,214) | 3,545,727 |
| | - | 149,335 | 149,335 |
| | (37,109,221) | 32,214 | |
| | | (149,335) | (37,226,342) |
| | 17,230,476 | - | 17,230,476 |

There were no changes to assets and liabilities as at September 30, 2010 as previously reported.

Below is a reconciliation of net loss and comprehensive loss as previously reported under Canadian GAAP to IFRS.

| Note | Three months ended September 30, 2010 | | | Nine months ended September 30, 2010 | | |
|--|---------------------------------------|------------------|--------------------|--------------------------------------|------------------|--------------------|
| | Cdn GAAP | Adj | IFRS | Cdn GAAP | Adj | IFRS |
| General and administrative expenses | | | | | | |
| | 39,087 | - | 39,087 | 138,091 | - | 138,091 |
| | 7,425 | - | 7,425 | 26,026 | - | 26,026 |
| | 20,500 | - | 20,500 | 75,250 | - | 75,250 |
| | 10,645 | - | 10,645 | 95,013 | - | 95,013 |
| | 80,067 | - | 80,067 | 206,986 | - | 206,986 |
| | 63,728 | - | 63,728 | 347,201 | - | 347,201 |
| | 2,140 | - | 2,140 | 16,616 | - | 16,616 |
| | 225,032 | - | 225,032 | 498,021 | - | 498,021 |
| | 512,201 | (3,153) | 509,048 | 700,073 | (15,784) | 684,289 |
| | 124,548 | - | 124,548 | 325,528 | - | 325,528 |
| | (1,085,373) | 3,153 | (1,082,220) | (2,428,805) | 15,784 | (2,413,021) |
| Other income (expenses) | | | | | | |
| | 1,382 | - | 1,382 | 3,511 | - | 3,511 |
| | (14,749) | (156,671) | (171,420) | (11,167) | (149,335) | (160,502) |
| | (13,367) | (156,671) | (170,038) | (7,656) | (149,335) | (156,991) |
| | (1,098,740) | (153,518) | (1,252,258) | (2,436,461) | (133,551) | (2,570,012) |
| Other comprehensive income | | | | | | |
| | - | 156,671 | 156,671 | - | 149,335 | 149,335 |
| | (1,098,740) | 3,153 | (1,095,587) | (2,436,461) | 15,784 | (2,420,677) |

South American Silver Corp.

(An Exploration Stage Company)

Notes to Condensed Consolidated Financial Statements

For the three and nine months ended September 30, 2011 and 2010

(Unaudited - expressed in U.S. dollars)

(i) **Adjustment on share-based payments**

Under IFRS, in the determination of share-based payments expense, the Company estimates forfeitures of awards on the grant date and revises these estimates for actual experiences in subsequent periods. Under Canadian GAAP, the Company had recognized forfeitures of awards as they occurred.

(ii) **Adjustment on translation of foreign currency entity**

The Company, as a result of its interpretation of IFRS, has determined that the parent company, SASC, has a functional currency of Canadian dollars. On translation to the presentation currency, U.S. dollars, the exchange gains/losses under IFRS are charged to other comprehensive income/loss. This treatment has resulted in a currency translation difference on conversion from Canadian GAAP to IFRS.

5 Equipment

| Nine months ended September 30, 2011 | Furniture and equipment \$ | Computer hardware \$ | Computer software \$ | Vehicle \$ | Leasehold improvements \$ | Total \$ |
|---|----------------------------------|----------------------------|----------------------------|---------------|---------------------------------|----------------|
| Cost | | | | | | |
| Balance, beginning of the period | 102,720 | 35,238 | 66,074 | 27,500 | - | 231,532 |
| Additions | 36,634 | 36,192 | 20,262 | - | 93,371 | 186,459 |
| Balance, end of the period | 139,354 | 71,430 | 86,336 | 27,500 | 93,371 | 417,991 |
| Accumulated amortization | | | | | | |
| Balance, beginning of the period | 36,431 | 24,612 | 64,909 | 27,500 | - | 153,452 |
| Amortization for the period | 16,148 | 6,760 | 4,532 | - | 2,519 | 29,959 |
| Balance, end of the period | 52,579 | 31,372 | 69,441 | 27,500 | 2,519 | 183,411 |
| Net book value at September 30, 2011 | 86,775 | 40,058 | 16,895 | - | 90,852 | 234,580 |

| Year ended December 31, 2010 | Furniture and equipment \$ | Computer hardware \$ | Computer software \$ | Vehicle \$ | Total \$ |
|--|----------------------------------|----------------------------|----------------------------|---------------|---------------|
| Cost | | | | | |
| Balance, beginning of the period | 94,503 | 26,092 | 66,074 | 27,500 | 214,169 |
| Additions | 8,217 | 9,146 | - | - | 17,363 |
| Balance, end of the period | 102,720 | 35,238 | 66,074 | 27,500 | 231,532 |
| Accumulated amortization | | | | | |
| Balance, beginning of the period | 16,896 | 15,939 | 61,362 | 25,667 | 119,864 |
| Amortization for the period | 19,535 | 8,673 | 3,547 | 1,833 | 33,588 |
| Balance, end of the period | 36,431 | 24,612 | 64,909 | 27,500 | 153,452 |
| Net book value at December 31, 2010 | 66,289 | 10,626 | 1,165 | - | 78,080 |

South American Silver Corp.

(An Exploration Stage Company)

Notes to Condensed Consolidated Financial Statements

For the three and nine months ended September 30, 2011 and 2010

(Unaudited - expressed in U.S. dollars)

6 Mining claims and deferred exploration costs – Schedule 1

Mining claims and deferred exploration costs are associated with the following projects.

| | September 30, 2011 | December 31, 2010 |
|-------------------------|-----------------------|----------------------|
| | \$ | \$ |
| a) Escalones, Chile | 1,810,732 | 1,067,321 |
| b) Malku Khota, Bolivia | 14,296,854 | 11,457,634 |
| | <u>16,107,586</u> | <u>12,524,955</u> |

- a) In 2004, the Company entered into an option agreement (the “Boezio Option”) to acquire the Escalones property located in Chile. In each of 2005, 2007 and 2009, the terms were renegotiated. Pursuant to the Boezio Option, as revised, the Company has the right until June 30, 2013 to purchase the claims upon payment to the owner of \$5,000,000. As at September 30, 2011, \$1,300,000 has been paid, including \$450,000 paid during the second quarter of 2011, and \$150,000 paid by a former partner. Additional payments pursuant to the Boezio Option are due as follows: \$700,000 on June 30, 2012; and \$3,000,000 on June 30, 2013.

The Company is required to pay all amounts required to protect and maintain the property during the option period. There is a 2% net smelter royalty (“NSR”) payable on production if the price of copper is greater than \$0.75 per pound and a 1% NSR if the copper price is equal to or less than \$0.75 per pound. The NSR may be purchased for \$3,000,000 within the five years following the first sale of minerals produced and \$5,000,000 after five years of the date of the first sale of minerals produced.

If the Company purchases the concessions, the Boezio Option requires the Company to commence exploitation of the concessions within two years thereafter. Until exploitation begins, the Company is required to pay annual advance royalty payments of \$200,000 which are credited against future royalty payments. Failure to commence exploitation within the two year period triggers an obligation to make annual indemnity payments of \$300,000 until exploitation begins. In this event, the \$200,000 annual payments made from the date of exercise of the option are deemed to be indemnity payments, not advance royalty payments. Royalty payments are suspended if exploitation of the mining concessions is suspended for reasons beyond the Company’s control

- b) In 2003, the Company entered into an option agreement (the “Kempff Option”) to acquire the Malku Khota property located in west central Bolivia. During 2007, the Company completed the purchase of the central portion of the Malku Khota property. A 1% NSR is payable on all production from the property included in the Kempff Option. This NSR can be purchased at any time for \$500,000.

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For the three and nine months ended September 30, 2011 and 2010

(Unaudited - expressed in U.S. dollars)

7 Share capital

a) Authorized

An unlimited number of common shares and an unlimited number of preferred shares issuable in series.

The holders of the common shares are entitled to one vote per share. The holders of the common shares are entitled to dividends, when and if declared by the directors of the Company, and to the distribution of the residual assets of the Company in the event of the liquidation, dissolution or winding-up of the Company. No dividends have ever been declared or paid as at September 30, 2011.

b) Financings

There were no financings completed during the nine months ended September 30, 2011.

c) Stock options and performance share units ("PSU's")

(i) Changes in stock options

The Company's stock options outstanding as at September 30, 2011 and the changes for the nine months then ended are as follows:

| | Number of options | Weighted average price Cdn.\$ |
|--|----------------------|-------------------------------------|
| Balance outstanding – December 31, 2010 | 8,066,800 | 0.51 |
| Options granted | 3,325,000 | 2.09 |
| Options exercised | (287,999) | 0.51 |
| Options forfeited or cancelled | (3,333) | 0.53 |
| Balance outstanding – September 30, 2011 | <u>11,100,468</u> | <u>0.98</u> |

(ii) Changes in PSU's

The Company's PSU's outstanding as at September 30, 2011 and the changes for the nine months then ended are as follows:

| | Number of PSU's |
|--|--------------------|
| Balance outstanding – December 31, 2010 | - |
| PSU's granted | 371,500 |
| PSU's vested | <u>(185,750)</u> |
| Balance outstanding – September 30, 2011 | <u>185,750</u> |

During the nine months ended September 30, 2011, the Company granted PSU's to officers, employees and consultants which, if fully vested, will entitle them to 371,500 common shares of the Company. 50% of the PSU's vested immediately, and the remaining 50% vest on October 15, 2011. See note 14c).

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Notes to Condensed Consolidated Financial Statements

For the three and nine months ended September 30, 2011 and 2010

(Unaudited - expressed in U.S. dollars)

(iii) Share-based payments

During the nine months ended September 30, 2011, the Company recorded share-based payments of \$3,712,389 (September 30, 2010 - \$775,262) in respect of stock options, performance share units and restricted share awards. Of this amount, \$3,353,240 (September 30, 2010 - \$684,289) was recorded as a charge to operations and \$359,149 (September 30, 2010 - \$90,973) was included in deferred exploration costs and credited to contributed surplus.

During the nine months ended September 30, 2011, the Company granted stock options to employees, officers, directors and consultants of the Company for the purchase of 1,800,000 common shares at a strike price of Cdn. \$2.09 per share. These options are exercisable for a period of five years, and of these options, 650,000 granted to non-management directors vested immediately and of the balance, 33 1/3% vested immediately, with a further 33 1/3% vesting on the date which is 12 months following the date of the grant; and the final 33 1/3% vesting on the date which is 24 months following the date of the grant.

During the nine months ended September 30, 2011, the Company granted stock options to consultants for the purchase of 400,000 common shares at a strike price of Cdn. \$2.09 per share. These options are exercisable for a period of two years and vest on the first anniversary of the grant date. The Company also granted stock options to non-management directors for the purchase of 600,000 common shares at a strike price of Cdn. \$2.32 per share. These options are exercisable for a period of five years and 33 1/3% vested immediately, with a further 33 1/3% vesting on the date which is 12 months following the date of the grant; and the final 33 1/3% vesting on the date which is 24 months following the date of the grant.

During the nine months ended September 30, 2011, the Company granted stock options to consultants for the purchase of 200,000 common shares at a strike price of Cdn. \$1.85 per share. These options are exercisable for a period of two years and 33 1/3% vested immediately, with a further 33 1/3% vesting on the date which is 6 months following the date of the grant; and the final 33 1/3% vesting on the date which is 12 months following the date of the grant. The Company also granted stock options to employees and consultants for the purchase of 325,000 common shares at a strike price of Cdn. \$1.85 per share. These options are exercisable for a period of five years and 33 1/3% vested immediately, with a further 33 1/3% vesting on the date which is 12 months following the date of the grant; and the final 33 1/3% vesting on the date which is 24 months following the date of the grant.

During the comparative nine months ended September 30, 2010, the Company granted stock options to officers and directors of the Company for the purchase of 1,450,000 common shares at a strike price of Cdn. \$0.37 per share, and stock options to directors for the purchase of 400,000 common shares at a strike price of Cdn. \$0.69 per share. These options are exercisable for a period of five years, and vest as to 33 1/3% on a cumulative basis on the date which is 12, 24 and 36 months following the date of the grant. The Company also granted stock options to employees, officers, directors and consultants of the Company for the purchase of 1,775,000 common shares at a price of Cdn. \$0.63 per share. These options are exercisable for a period of five years, and of these options, 675,000 granted to directors vested immediately and 33 1/3% of the balance vested immediately and 33 1/3% vest on the date which is 12 months following the date of the grant; and the final 33 1/3% vest on the date which is 24 months following the date of the grant.

The fair value of each option grant was estimated at the time of the grant using the Black-Scholes option pricing model with assumptions for grants as follows:

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(Unaudited - expressed in U.S. dollars)

| | Nine months ended September 30, 2011 | Nine months ended September 30, 2010 |
|---|---|---|
| Weighted average exercise price | Cdn.\$2.09 | Cdn.\$0.53 |
| Weighted average grant date share price | Cdn.\$2.09 | Cdn.\$0.53 |
| Risk-free interest rate | 2.1% | 2.1% to 2.3% |
| Expected life | 2.0 to 5.0 years | 5.0 years |
| Expected volatility | 87% to 94% | 88% to 89% |
| Dividend rate | 0% | 0% |
| Expected forfeiture rate | 3.3% | 3.3% |

Grant date share price is the closing market price on the date before the options were granted. Expected volatility was determined by measuring the historical volatility of the Company's share price. The historical period used to measure historical volatility was the same as the expected life of the options granted. The weighted average grant date fair value of options granted during the nine months ended September 30, 2011 was \$1.52 (September 30, 2010 - \$0.36).

The fair value of the PSU's granted during the nine months ended September 30, 2011 was based upon the closing share price on the date of grant and amounts to \$808,735.

(iv) Options outstanding at the end of the period

Options to acquire common shares are outstanding at September 30, 2011 as follows:

| Number of options outstanding | Number of options exercisable | Exercise price Cdn. \$ | Expiry date |
|-------------------------------------|-------------------------------------|------------------------------|--------------------|
| 2,310,000 | 2,310,000 | 0.50 | February 15, 2012 |
| 590,000 | 590,000 | 0.68 | May 16, 2012 |
| 400,000 | - | 2.09 | April 15, 2013 |
| 510,000 | 510,000 | 0.53 | May 30, 2013 |
| 200,000 | 66,667 | 1.85 | August 16, 2013 |
| 906,734 | 576,734 | 0.35 | May 25, 2014 |
| 650,000 | 216,667 | 0.37 | March 26, 2015 |
| 800,000 | 266,667 | 0.37 | March 29, 2015 |
| 400,000 | 133,333 | 0.69 | June 8, 2015 |
| 1,608,734 | 1,042,067 | 0.63 | September 16, 2015 |
| 1,800,000 | 1,033,333 | 2.09 | April 15, 2016 |
| 600,000 | 200,000 | 2.32 | May 26, 2016 |
| 325,000 | 108,333 | 1.85 | August 16, 2016 |
| <u>11,100,468</u> | <u>7,053,801</u> | | |

At September 30, 2011, the outstanding options have a weighted average remaining contractual life of 2.8 years.

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d) Warrants

(i) Changes in warrants

The Company's warrants outstanding as at September 30, 2011 and the changes for the nine months then ended are as follows:

| | Number of warrants | Weighted average price Cdn.\$ |
|------------------------------|-----------------------|-------------------------------------|
| Balance – December 31, 2010 | 8,488,133 | 0.93 |
| Warrants exercised | (1,988,693) | 0.79 |
| Balance – September 30, 2011 | <u>6,499,440</u> | <u>0.95</u> |

(ii) Warrants exercised

During the nine months ended September 30, 2011, the weighted average share price for warrants exercised was Cdn. \$0.79. During the nine months ended September 30, 2010, 15,625 warrants were exercised at an exercise price of Cdn. \$0.60.

(iii) Warrants outstanding at the end of the period

Warrants to acquire common shares are outstanding at September 30, 2011 as follows:

| Number Outstanding | Exercise Price Cdn. \$ | Expiry Date |
|--------------------------|------------------------------|-------------------|
| 1,293,750 | \$0.60 | November 27, 2011 |
| 8,000 | \$0.60 | December 7, 2011 |
| 200,000 | \$0.50 | February 15, 2012 |
| 1,997,690 | \$1.16 | May 30, 2012 |
| 2,600,000 ⁽¹⁾ | \$0.95 | July 15, 2012 |
| <u>400,000</u> | <u>\$1.47</u> | November 5, 2012 |
| <u>6,499,440</u> | | |

(1) In the event that the Company's common shares trade on the Toronto Stock Exchange (the "TSX") at a price of not less than Cdn. \$1.25 for a period of 10 consecutive trading days, the Company shall be entitled to accelerate the exercise period of these warrants to a period ending at least 30 days from the date notice of such acceleration is provided to the holders of the warrants.

8 Related party transactions

The Company's related parties consist of the Company's officers or companies associated with them, and a legal firm in which a director is a partner. The Company incurred the following expenditures during the three and nine months ended September 30, 2011 and 2010 that were charged by related parties:

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| | Three months ended September 30, 2011 \$ | Three months ended September 30, 2010 \$ | Nine months ended September 30, 2011 \$ | Nine months ended September 30, 2010 \$ |
|--|---|---|--|--|
| Consulting fees | 19,950 | 21,350 | 60,095 | 62,130 |
| Legal fees | 16,419 | 20,449 | 229,471 | 226,219 |
| Legal fees in deferred share issue costs | - | 66,312 | - | 108,393 |
| Mineral property costs – consulting fees | 72,528 | 88,600 | 221,911 | 133,820 |
| | <u>108,897</u> | <u>196,711</u> | <u>511,477</u> | <u>530,562</u> |

Included in accounts payable at September 30, 2011 is an amount of \$172,452 (December 31, 2010 - \$409,095) due to related parties. These amounts are non-interest bearing and have no specific terms of repayment.

Transactions with related parties are recorded at the exchange amount, being the price agreed between the parties.

Key management includes the Chief Executive Officer and the Executive Chairman. The compensation paid or payable to key management for services is as follows:

| | Three months ended September 30, 2011 \$ | Three months ended September 30, 2010 \$ | Nine months ended September 30, 2011 \$ | Nine months ended September 30, 2010 \$ |
|----------------------|---|---|--|--|
| Wages and benefits | 113,879 | 70,456 | 329,629 | 165,417 |
| Share-based payments | 156,668 | 101,599 | 414,798 | 191,068 |
| | <u>270,547</u> | <u>172,055</u> | <u>744,427</u> | <u>356,485</u> |

9 Contingencies

The Company may be subject to various contingent liabilities that occur in the normal course of operations. The Company is not aware of any pending or threatened proceedings that would have a material adverse effect on the consolidated financial condition or future results of the Company.

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10 Commitments

The Company is committed under the terms of office lease agreements for the following approximate annual rent and estimated operating costs.

| | Amount \$ |
|--------------------------------|----------------|
| Due on or before September 30, | |
| 2012 | 148,000 |
| 2013 | 124,000 |
| 2014 | 127,000 |
| 2015 | 129,000 |
| 2016 | 118,000 |
| | <u>646,000</u> |

11 Segment information

The Company's operations are limited to a single industry segment, being mineral exploration and development. Geographic segment information of the Company's assets and liabilities is as follows:

| Identifiable assets | September 30, 2011 | December 31, 2010 |
|---------------------------------|-----------------------|----------------------|
| | \$ | \$ |
| Bolivia | 14,731,653 | 11,632,412 |
| Canada | 28,835,507 | 35,669,356 |
| Chile | 1,954,322 | 1,094,740 |
| United States and other | 50,664 | 114,833 |
| Total assets | <u>45,572,146</u> | <u>48,511,341</u> |
| Identifiable liabilities | | |
| Bolivia | 57,320 | 73,120 |
| Canada | 399,442 | 661,770 |
| Chile | 44,690 | 11,543 |
| United States and other | 105,886 | 92,092 |
| Total liabilities | <u>607,338</u> | <u>838,525</u> |

| Additions to segmented non-current assets during the nine months ended Sept. 30, 2011 | Bolivia | Canada | Chile | United States and other | Total |
|---|-------------------|----------------|------------------|-------------------------|-------------------|
| | \$ | \$ | \$ | \$ | \$ |
| Balance, December 31, 2010 | 11,525,232 | 4,402 | 1,068,597 | 4,804 | 12,603,035 |
| Additions | 2,825,870 | 161,908 | 744,943 | 6,410 | 3,739,131 |
| Balance, September 30, 2011 | <u>14,351,102</u> | <u>166,310</u> | <u>1,813,540</u> | <u>11,214</u> | <u>16,342,166</u> |

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Geographic segmentation of the Company's net loss for the period is as follows:

| | Three months ended September 30, 2011 \$ | Three months ended September 30, 2010 \$ | Nine months ended September 30, 2011 \$ | Nine months ended September 30, 2010 \$ |
|-------------------------|--|--|---|---|
| Bolivia | 21,100 | 14,772 | 78,182 | 56,551 |
| Canada | 1,662,584 | 969,465 | 5,887,898 | 1,845,399 |
| Chile | 45,321 | 26,709 | 126,618 | 83,017 |
| United States and other | 165,250 | 241,312 | 515,538 | 585,045 |
| Net loss | 1,894,255 | 1,252,258 | 6,608,236 | 2,570,012 |

12 Supplemental cash flow information

The Company conducted non-cash investing and financing activities as follows:

| | Nine months ended September 30, 2011 \$ | Nine months ended September 30, 2010 \$ |
|---|---|---|
| Investing activities | | |
| Deferred exploration costs included in accounts payable | (234,533) | (375,557) |
| Financing activities | | |
| Share-based payments included in deferred exploration costs | (359,149) | (90,973) |

13 Financial instruments

a) Fair value of financial instruments

The Company's financial instruments consist of cash and cash equivalents, receivables and accounts payable and accrued liabilities. Cash equivalents consist of bankers' acceptances and term deposits, the investment terms of which are less than three months at the time of acquisition. The Company has no asset backed commercial paper. Cash and cash equivalents are measured at fair value. Receivables and accounts payable and accrued liabilities are measured at their amortized cost which approximates their fair value due to their short-term nature.

The Company classifies fair values of financial instruments within a three-level hierarchy that prioritizes the inputs to fair value measurement and reflects the significance of the inputs used in making the fair value measurements. Fair values of assets and liabilities included in Level 1 are determined by reference to quoted prices in active markets for identical assets and liabilities. Assets and liabilities in Level 2 include valuations using inputs other than quoted prices for which all significant outputs are observable, either directly or indirectly. Level 3 valuations are based on inputs that are unobservable and significant to the overall fair value

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measurement. The Company's cash and cash equivalents have been classified as "Level 2" financial instruments.

b) Currency risk

A portion of the Company's financial assets and liabilities is denominated in foreign currencies giving rise to risks from changes in foreign exchange rates. The Company is exposed to currency exchange rate risks to the extent of its activities in Canada, Bolivia, and Chile. The Company's currency risk is presently limited to approximately \$980,000 of financial assets and liabilities denominated in U.S. dollars which are owned by the Canadian parent, or denominated in Bolivian Bolivianos or in Chilean pesos. Based on this exposure as at September 30, 2011, a 5% change in exchange rates would give rise to a change in net loss of approximately \$49,000. The Company does not use derivative financial instruments to reduce its foreign exchange exposure.

The currencies of the Company's financial instruments, based on notional amounts, were as follows:

| | September 30, 2011 | | |
|--|-------------------------------|-------------------------------|-------------------------|
| | U.S. dollar | Bolivian Boliviano | Chilean Peso |
| Cash and cash equivalents | 859,409 | 337,217 | 13,726,420 |
| Receivables | 326,963 | 216,440 | - |
| Accounts payable and accrued liabilities | (205,912) | (393,153) | (26,920,701) |
| Net balance sheet exposure | 980,460 | 160,503 | (13,194,281) |

| | December 31, 2010 | | |
|--|------------------------------|-------------------------------|-------------------------|
| | U.S. dollar | Bolivian Boliviano | Chilean Peso |
| Cash and cash equivalents | 4,297,532 | 334,922 | 4,266,851 |
| Receivables | 19,465 | 67,604 | (404,203) |
| Accounts payable and accrued liabilities | (135,875) | (552,237) | (5,406,395) |
| Net balance sheet exposure | 4,181,182 | (149,711) | (1,543,747) |

Future changes in exchange rates could have a material effect on the Company's business, financial condition and results of operations.

c) Credit risk

Credit risk is the risk of loss if a customer or third party to a financial instrument fails to meet its commercial obligations.

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The majority of the Company's cash is held through a Canadian chartered bank and accordingly, the Company's exposure to credit risk is considered to be limited. Cash equivalents consist of bankers' acceptances which have an original maturity of three months or less from the date of purchase and which are readily convertible into a known amount of cash. The Company also maintains deposits for ongoing working capital at major banks in the jurisdictions in which its foreign subsidiaries operate.

d) **Interest rate risk**

Interest rate risk is the risk that the fair value of 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 of the short term investments included in cash and cash equivalents is limited because these instruments, although available for sale, are generally held to maturity and the interest rate is fixed. The Company manages its cash according to its operational needs.

e) **Liquidity risk**

The Company manages liquidity risk by maintaining sufficient cash and cash equivalents balances to enable settlement of transactions on the due date. Accounts payable and accrued liabilities are all current.

14 Subsequent events

Subsequent to September 30, 2011:

- a) the Company received proceeds of Cdn. \$56,250 from the exercise of 93,750 warrants.
- b) the Company issued 76,056 common shares on the exercise of 110,000 SARs.
- c) 185,750 PSUs vested and were converted into 185,750 common shares in accordance with the vesting provisions.

South American Silver Corp.*(An Exploration Stage Company)***Condensed Consolidated Schedule of Deferred Exploration Costs***(Unaudited - expressed in U.S. dollars)*

| | Bolivia properties | Chile properties | Total |
|--------------------------------------|-------------------------------|-----------------------------|-------------------|
| | \$ | \$ | \$ |
| Balance at December 31, 2009 | <u>7,845,524</u> | <u>829,527</u> | <u>8,675,051</u> |
| Land and option payments | 24,104 | 157,105 | 181,209 |
| Laboratory | 659,971 | - | 659,971 |
| Field supplies | 79,873 | 366 | 80,239 |
| Consulting and supervision | 567,925 | 63,893 | 631,818 |
| Maps and reproduction | 2,645 | 38 | 2,683 |
| Community relations | 57,485 | - | 57,485 |
| Environmental | 29,108 | - | 29,108 |
| Hydrology | 22,847 | - | 22,847 |
| Petrology | 9,820 | - | 9,820 |
| Engineering | 195,353 | - | 195,353 |
| Geological consulting | 516,512 | 14,789 | 531,301 |
| Drilling | 751,041 | - | 751,041 |
| Trenching | 162,915 | - | 162,915 |
| Travel and accommodation | 166,486 | 1,418 | 167,904 |
| Share-based payments | 151,150 | - | 151,150 |
| Value added tax credits | 214,875 | 185 | 215,060 |
| | <u>3,612,110</u> | <u>237,794</u> | <u>3,849,904</u> |
| Balance at December 31, 2010 | <u>11,457,634</u> | <u>1,067,321</u> | <u>12,524,955</u> |
| Land and option payments | 17,222 | 453,655 | 470,877 |
| Laboratory | 555,829 | 35,930 | 591,759 |
| Field supplies | 134,748 | 47,956 | 182,704 |
| Consulting and supervision | 688,777 | 103,090 | 791,867 |
| Maps and reproduction | 3,511 | 5,324 | 8,835 |
| Community relations | 155,538 | - | 155,538 |
| Environmental | 20,566 | - | 20,566 |
| Petrology | 14,424 | - | 14,424 |
| Engineering | 346,760 | - | 346,760 |
| Geological consulting | 268,073 | 53,014 | 321,087 |
| Drilling | 94,091 | 654 | 94,745 |
| Trenching | 3,682 | 6,465 | 10,147 |
| Travel and accommodation | 123,624 | 24,139 | 147,763 |
| Share-based payments | 359,149 | - | 359,149 |
| Value added tax credits | 53,226 | 13,184 | 66,410 |
| | <u>2,839,220</u> | <u>743,411</u> | <u>3,582,631</u> |
| Balance at September 30, 2011 | <u>14,296,854</u> | <u>1,810,732</u> | <u>16,107,586</u> |

