

CORTEZ GOLD CORP.
FINANCIAL STATEMENTS
February 28, 2011
(Stated in Canadian Dollars)



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INDEPENDENT AUDITORS' REPORT

To the Shareholders,
Cortez Gold Corp.

We have audited the accompanying financial statements of Cortez Gold Corp. , which comprise the balance sheets as at February 28, 2011 and 2010, and the statements of operations and deficit and cash flows for the years then ended, and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Canadian Generally Accepted Accounting Principles, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the 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 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 presentation of the financial statements.

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

Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of Cortez Gold Corp. as at February 28, 2011 and 2010 and the results of its operations and its cash flows for the years then ended, in accordance with Canadian Generally Accepted Accounting Principles.

Emphasis of Matter

Without qualifying our opinion, we draw attention to Note 1 in the financial statements, which indicates that the Company has not yet achieved profitable operations and has accumulated losses of \$1,828,342 since its inception and its working capital deficit as at February 28, 2011 was \$334,521. These conditions, along with other matters as set forth in Note 1, indicate the existence of a material uncertainty that may cast significant doubt upon the Company's ability to continue as a going concern.

(signed) "BDO Canada LLP"

Chartered Accountants
Vancouver, Canada
June 21, 2011

CORTEZ GOLD CORP.
BALANCE SHEETS
February 28, 2011 and 2010
(Stated in Canadian Dollars)

	2011	2010
<u>ASSETS</u>		
Current		
Cash and cash equivalents – Note 3	\$ 6,435	\$ 558,501
Taxes recoverable	169,215	14,247
Prepaid expenses – Notes 5 and 7	17,962	-
	193,612	572,748
Capital Assets – Note 4	44,968	-
Interests in mineral property options – Note 5	1,740,771	29,299
	\$ 1,979,351	\$ 602,047
<u>LIABILITIES</u>		
Current		
Accounts payable and accrued liabilities – Note 7	\$ 528,133	\$ 29,977
Asset retirement obligation – Note 5	24,285	-
Future income tax liability – Note 10	48,053	-
	600,471	29,977
<u>SHAREHOLDERS' EQUITY</u>		
Share capital – Note 6	2,836,390	1,454,846
Contributed surplus – Note 6	370,832	61,545
Deficit	(1,828,342)	(944,321)
	1,378,880	572,070
	\$ 1,979,351	\$ 602,047

Nature of Operations and Ability to Continue as a Going Concern – Note 1
Commitments – Notes 5 and 6
Subsequent Events – Notes 5 and 6

APPROVED ON BEHALF OF THE BOARD:

<u>“Robert Eadie”</u> Robert Eadie	Director	<u>“Gary Arca”</u> Gary Arca	Director
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CORTEZ GOLD CORP.
STATEMENTS OF OPERATIONS AND DEFICIT
For the years ended February 28, 2011 and 2010
(Stated in Canadian Dollars)

	2011	2010
Expenses		
Accounting and audit fees – Note 7	\$ 11,211	\$ 37,611
Amortization	8,558	-
Bank charges and interest	2,698	1,388
Consulting fees – Note 7	121,315	100,712
Legal and corporate services	78,603	126,954
Management services – Note 7	20,000	-
Office and administration – Note 7	95,104	21,308
Rent – Note 7	30,500	18,000
Property investigation costs	3,178	-
Stock-based compensation – Note 6	181,941	-
Shareholder communications – Note 7	124,344	54,854
Transfer agent and filing fees	44,032	38,632
Travel	129,074	79,269
Loss before other items	(850,558)	(478,728)
Other items:		
Interest income	420	148
Foreign exchange loss	(4,584)	(15,340)
Write-off of investigation cost – Note 9	-	(222,749)
Write-down of mineral property option – Note 5	(29,299)	-
Loss and comprehensive loss for the year	(884,021)	(716,669)
Deficit, beginning of the year	(944,321)	(227,652)
Deficit, end of the year	\$ (1,828,342)	\$ (944,321)
Basic and diluted loss per share	\$ (0.07)	\$ (0.14)
Weighted average number of shares outstanding	12,756,680	5,068,220

CORTEZ GOLD CORP.
STATEMENTS OF CASH FLOWS
For years ended February 28, 2011 and 2010
(Stated in Canadian Dollars)

	2011	2010
Operating Activities		
Net loss for the year	\$ (884,021)	\$ (716,669)
Non cash items:		
Amortization	8,558	-
Stock-based compensation	181,941	-
Write-down of deferred acquisition cost	-	222,749
	(693,522)	(493,920)
Changes in non-cash working capital items:		
Taxes recoverable	(154,968)	(11,816)
Prepaid expenses	(17,962)	-
Accounts payable and accrued liabilities	70,436	11,928
Cash used in operating activities	(796,016)	(493,808)
Investing Activities		
Capital assets	(53,526)	-
Mineral property investigation	-	(675,550)
Mineral properties	(841,414)	(25,000)
Recovery of deferred property investigation	-	452,801
Cash used in (provided by) investing activities	(894,940)	(247,749)
Financing Activities		
Issuance of common shares	1,200,000	1,010,000
Share issue costs	(61,110)	(76,764)
Cash provided by financing activities	1,138,890	933,236
Increase (decrease) in cash during the year	(552,066)	191,679
Cash and cash equivalents, beginning of the year	558,501	366,822
Cash and cash equivalents, end of the year	\$ 6,435	\$ 558,501
Supplementary disclosure of cash flow information:		
Cash paid for:		
Interest	\$ -	\$ -
Income taxes	\$ -	\$ -
Mineral property expenditures included in accounts payable and accrued liabilities	\$ 427,720	\$ 4,299

Non-cash Transactions – Note 5 and 6

CORTEZ GOLD CORP.
NOTES TO THE FINANCIAL STATEMENTS
February 28, 2011
(Stated in Canadian Dollars)

Note 1 **Nature of Operations and Ability to Continue as a Going Concern**

The Company was incorporated in the Province of British Columbia on March 29, 2007 under the Business Corporations Act of British Columbia as 0786996 BC Ltd., changed its name to Cortez Resources Corp. on April 13, 2007 and again changed its name to Cortez Gold Corp. on September 18, 2009. The Company is listed on the TSX Venture Exchange (the “Exchange”) as a Tier 2 issuer.

The recoverability of the amounts shown in the balance sheet for expenditures on mineral properties is dependent upon the existence of economically recoverable reserves, maintaining beneficial interest in the property and the underlying mining claims, obtaining the necessary regulatory approvals and permits, the ability to obtain the necessary financing to fulfil its obligations as they arise, the ability to complete the development of the claims, and achieving profitable production or receiving proceeds from the disposition of the property.

These financial statements have been prepared in accordance with Canadian generally accepted accounting principles (“Canadian GAAP”) applicable to a going concern, under which material uncertainties that may cast significant doubt upon the Company’s ability to continue as a going concern must be disclosed. As at February 28, 2011, the Company has not yet achieved profitable operations and has accumulated losses of \$1,828,342 since its inception. Its ability to continue as a going concern is dependent upon the ability of the Company to obtain necessary financing to meet the Company’s liabilities as they become payable and ultimately to generate profitable future operations. Working capital deficit at February 28, 2011 was \$334,521. These financial statements do not give effect to adjustments that would be necessary should the Company be unable to continue as a going concern and, therefore, be required to realize its assets and liquidate its liabilities and commitments in other than the normal course of operations, and at amounts different from those in the accompanying consolidated financial statements.

Note 2 **Significant Accounting Policies**

Management has prepared the financial statements of the Company in accordance with Canadian GAAP. The preparation of financial statements in conformity with Canadian GAAP requires management to make estimates and assumptions that affect amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates. These financial statements have been prepared within the framework of the significant accounting policies summarized below.

CORTEZ GOLD CORP.

Notes to the Financial Statements

February 28, 2011

(Stated in Canadian Dollars)

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Note 2 Significant Accounting Policies – (cont'd)

a) Use of Estimates

Because a precise determination of many assets and liabilities is dependent upon future events, the preparation of these financial statements requires management to make estimates and assumptions. The most significant estimates include, but are not limited to: the recoverability of amounts receivable; the future cost of asset retirement obligations; the anticipated costs of reclamation and closure cost obligations; the amounts of contingencies; and assumptions used in the accounting for stock-based compensation such as volatility, expected term and risk free interest rate. Using these estimates and assumptions, management makes various decisions in preparing the financial statements including:

- Whether long-lived assets; equipment; mineral properties and deferred exploration costs are impaired, and if so, estimates of the fair value of those assets and any corresponding impairment charge;
- The ability to realize future income tax assets;
- The useful lives of long-lived assets and the measurement of amortization;
- The fair value of reclamation and closure cost obligations, where estimable;
- The likelihood of loss contingencies occurring and the amount of any potential loss; and
- The amount of stock-based compensation expense.

As the estimation process is inherently uncertain, actual future outcomes could differ from present estimates and assumptions, potentially having material future effects on the financial statements.

b) Basic and Diluted Loss per Share

Basic loss per share is computed by dividing the loss for the period by the weighted average number of common shares outstanding during the period. Diluted loss per share reflects the potential dilution that could occur if potentially dilutive securities were exercised or converted to common stock. The dilutive effect of options and warrants and their equivalent is computed by application of the treasury stock method. Fully diluted amounts are not presented when the effect of the computations are anti-dilutive due to the losses incurred. Accordingly, there is no difference in the amounts presented for basic and diluted loss per share.

Potentially dilutive common shares (relating to options and warrants outstanding at year-end) totalling 3,040,800 (2010: 315,000) were not included in the computation of loss per share because their effect was anti-dilutive.

CORTEZ GOLD CORP.

Notes to the Financial Statements

February 28, 2011

(Stated in Canadian Dollars)

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Note 2 Significant Accounting Policies – (cont'd)

c) Income Taxes

The Company follows the asset and liability method of accounting for income taxes. Under this method, current income taxes are recognized for the estimated income taxes payable for the current period. Future income tax assets and liabilities are determined based on differences between the tax and accounting basis of assets and liabilities. The future tax assets or liabilities are calculated using the tax rates for the period in which the differences are expected to be settled. Future tax assets are recognized to the extent that they are considered more likely than not to be realized.

d) Stock-based Compensation

The Company has a stock-based compensation plan, whereby stock options are granted in accordance with the policies of regulatory authorities. The fair value of all share purchase options granted are expensed over their vesting period with a corresponding increase to contributed surplus. Upon exercise of share purchase options, the consideration paid by the option holder, together with the amount previously recognized in contributed surplus, is recorded as an increase to share capital.

The Company uses the Black-Scholes valuation model to determine the fair value of share purchase options at the date of grant. Option pricing models require the input of highly subjective assumptions, including the expected price volatility. Changes in these assumptions can materially affect the fair value.

e) Share issue costs

Share issue costs, which include commissions, professional and regulatory fees are charged directly to share capital.

f) Financial Instruments

All financial instruments are classified into one of the following five categories: held for trading, held-to-maturity investments, loans and receivables, available-for-sale assets or other financial liabilities. All financial instruments, including derivatives, are included on the balance sheet and are measured at fair market value upon inception with the exception of certain related party transactions. Subsequent measurement and recognition of changes in the fair value of financial instruments depends on their initial classification. Held-for-trading financial investments are measured at fair value and all gains and losses are included in operations in the period in which they arise. Available-for-sale financial instruments are measured at fair value with revaluation gains and losses included in other comprehensive income (loss) until the asset is removed from the balance sheet. Loans and receivables, investments held to maturity and other financial liabilities are measured at amortized cost using the effective interest method. Gains and losses upon inception, derecognition, impairment write-downs and foreign exchange translation adjustments are recognized immediately. Transaction costs related to debt financings will be expensed in the period incurred.

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Notes to the Financial Statements

February 28, 2011

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Note 2 Significant Accounting Policies – (cont'd)

f) Financial Instruments – (cont'd)

The Company has entered into agreements which provide an option to purchase an equity interest in private companies (Note 5), which constitute derivative financial instruments. Derivative financial instruments that are linked to and must be settled by delivery of equity instruments of another entity whose fair value cannot be reliably measured are classified as held-for-trading and are measured at cost.

The Company's financial instruments consist of cash and cash equivalents, which is classified as held-for-trading, derivative financial instrument which is classified as held for trading, and accounts payable, which is classified as other financial liabilities. It is management's opinion that the Company is not exposed to significant interest, currency or credit risks arising from these financial instruments.

Section 3862, "Amendment to Financial Instruments – Disclosures" requires disclosures about the inputs to fair value measurements, including their classification within a hierarchy that prioritizes the inputs to fair value measurement. The three levels of the fair value hierarchy are:

Level 1 – Unadjusted quoted prices in active markets for identical assets or liabilities;

Level 2 – Inputs other than quoted prices that are observable for the asset or liability either directly or indirectly; and

Level 3 – Inputs that are not based on observable market data

All of the financial instruments measured at fair value on the balance sheet are included in Level 1.

g) Mineral Properties

The Company defers the cost of acquiring, maintaining its interest, exploring and developing mineral properties until such time as the properties are placed into production, abandoned, sold or considered to be impaired in value. Costs of producing properties will be amortized on a unit of production basis and costs of abandoned properties are written-off. Proceeds received on the sale of interests in mineral properties are credited to the carrying value of the mineral properties, with any excess included in operations. Write-downs due to impairment in value are charged to operations.

The Company is in the process of exploring and developing its mineral properties and has not yet determined the amount of reserves available. Management reviews the carrying value of mineral properties on an annual basis and will recognize impairment in value based upon current exploration results, the prospect of further work being carried out by the Company, the assessment of future probability of profitable revenues from the property or from the sale of the property. Amounts shown for properties represent costs incurred net of write-downs and recoveries, and are not intended to represent present or future values.

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Notes to the Financial Statements

February 28, 2011

(Stated in Canadian Dollars)

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Note 2 Significant Accounting Policies – (cont'd)

h) Asset Retirement Obligations

The Company records the fair value of an asset retirement obligation as a liability in the period in which it incurs a legal obligation associated with the retirement of tangible long-lived assets that results from the acquisition, construction, development, and/or normal use of the assets. The obligation is measured initially at fair value using present value methodology and the resulting costs are capitalized into the carrying amount of the related asset. In subsequent periods, the liability will be adjusted for any changes in the amount or timing of the underlying future cash flows. Capitalized asset retirement costs are depreciated on the same basis as the related asset and the discounted accretion of the liability is included in determining the results of operations. As at February 28, 2011 the Company has accrued asset retirement obligations in the amount of \$24,285 (2010: \$Nil) (Note 5).

It is possible that the Company's estimates of its ultimate asset retirement obligations could change as a result of changes in regulations, the extent of environmental remediation required, and the means of reclamation or of cost estimates. Changes in estimates are accounted for prospectively from the period the estimate is revised.

i) Impairment of Long-lived Assets

Canadian GAAP requires that long-lived assets and intangibles to be held and used by the Company be reviewed for possible impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. If changes in circumstances indicate that the carrying amount of an asset that an entity expects to hold and use may not be recoverable, future cash flows expected to result from the use of the asset and its disposition must be estimated. If the undiscounted value of the future cash flows is less than the carrying amount of the asset, impairment is recognized. With the exceptions of the Seabridge Acquisition costs, which were written down during the year ended February 28, 2010 and the Timber Property, which was written off during the year ended February 28, 2011, management believes there has been no impairment of the Company's long-lived assets as at February 28, 2011 and 2010.

j) Foreign Currency Translation

Monetary assets and liabilities denominated in other than Canadian dollars are translated using the exchange rates prevailing at the balance sheet date and non-monetary assets and liabilities are translated at exchange rates prevailing at the transaction dates. Foreign currency denominated expenses are translated at exchange rates prevailing at the transaction dates. Gains and losses on foreign currency transactions are recorded in operations in the current year.

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Notes to the Financial Statements

February 28, 2011

(Stated in Canadian Dollars)

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Note 2 Significant Accounting Policies – (cont'd)

k) Capital Assets

Capital assets are recorded at cost. The Company provides for amortization using the declining balance method at the following annual rates:

Vehicles	30%
Computer equipment	45%

l) Warrants

The Company accounts for warrants issued as part of units in a private placement using the residual value method whereby the difference, if any, between the price paid for the units and the market price of the shares on the date of issuance, is attributable to the warrants.

m) Future Accounting Changes

International Financial Reporting Standards (“IFRS”)

In 2006, the Canadian Accounting Standards Board (“AcSB”) published a new strategic plan that will significantly affect financial reporting requirements for Canadian companies. The AcSB strategic plan outlines the convergence of Canadian generally accepted accounting principles with IFRS over an expected five-year transitional period. In February 2008, the AcSB announced that 2011 is the changeover date for publicly-listed companies to use IFRS, replacing Canada’s own generally accepted accounting principles. The effective date for the Company is for interim and annual financial statements relating to fiscal years beginning on or after March 1, 2012. This transition will require the restatement, for comparative purposes, of amounts reported by the Company for the year ended February 28, 2011. The Company does not expect any significant adjustment to the financial statements as a result of the impact of the convergence of Canadian GAAP and IFRS.

Note 3 Cash and Cash Equivalents

At February 28, 2011, the Company had no GICs. At February 28, 2010, cash equivalents included GICs with a market value of \$421,136, earning interest income at approximately 0.25% per annum and maturing on December 1, 2010. All of the Company’s cash is held at one financial institution and as such the Company is exposed to the risks of that financial institution.

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Notes to the Financial Statements

February 28, 2011

(Stated in Canadian Dollars)

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Note 4 Capital Assets

	February 28,			
	2011			2010
	Cost	Accumulated Amortization	Net	Net
Vehicles	\$ 51,943	\$ 8,402	\$ 43,541	\$ -
Computer equipment	1,583	156	1,427	-
	\$ 53,526	\$ 8,558	\$ 44,968	\$ -

Note 5 Interests in Mineral Property Options

	Timber Property	Guadalupe Property	Petlacala Property	Total
Acquisition Cost:				
Balance February 28, 2010	\$ 25,000	\$ -	\$ -	\$ 25,000
Cash payments and advances	-	108,321	1,070,236	1,178,557
500,000 common shares at \$0.31	-	-	125,000	125,000
100,000 common shares at \$0.31	-	-	25,000	25,000
1,000,000 common shares at \$0.275	-	220,000	-	220,000
Acquisition costs during the period	25,000	328,321	1,220,236	1,573,557
Exploration Cost:				
Balance February 28, 2010	4,299	-	-	4,299
Geological consulting	-	-	66,338	66,338
Assays and sampling	-	-	53,538	53,538
Site restoration	-	-	24,285	24,285
Expenditures during the period	-	-	144,161	148,460
Future income tax liability	-	-	48,053	48,053
Subtotal before write-down	29,299	328,321	1,412,450	1,770,070
Write-down	(29,299)	-	-	(29,299)
Mineral Properties, February 28, 2011	\$ -	\$ 328,321	\$ 1,412,450	\$ 1,740,771

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Notes to the Financial Statements

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(Stated in Canadian Dollars)

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Note 5 **Interests in Mineral Property Options** – (cont'd)

	Timber Property	Guadalupe Property	Petlacala Property	Total
Balance, February 28, 2009	\$ -	\$ -	\$ -	\$ -
Acquisition Cost:				
Property payments	25,000	-	-	25,000
Exploration cost:				
Geological consulting	4,299	-	-	4,299
Mineral Properties, February 28, 2010	\$ 29,299	\$ -	\$ -	\$ 29,299

Timber Property

The Company entered into a letter of agreement with Strategic Metals Ltd. (“Strategic”) dated January 14, 2010 under which the Company had the right and option to earn an undivided 50% interest in the Timber Property located in southeast Yukon Territory. The Option Agreement provided that the Company pay to Strategic an aggregate of \$150,000 in cash and commit to \$1,000,000 in exploration expenditures over a three-year period, in order to earn its interest.

Subsequent to February 28, 2011 the Company terminated the proposed acquisition of the Timber Property. Consequently, the Company recorded a write-down of \$29,299 in the statement of operations and deficit for the year ended February 28, 2011 relating to payments and expenditures on this property.

Petlacala Property

On April 9, 2010 the Company entered into non-binding agreement, pursuant to a Letter of Intent (the “LOI”) with Cortez Minera Mexicana, S.A. de C.V. (“Minera Mexicana”), a private Mexican company. The LOI sets out the terms upon which the Company can acquire 100% of the issued and outstanding shares of Minera Mexicana. Minera Mexicana holds an option to purchase a 100% interest in the Petlacala gold-silver project in Guerrero State, Mexico, under an option agreement dated April 2, 2010 with the property vendor, Minera Petlacala, S.A. de C.V. (“Minera Petlacala”).

Effective August 6, 2010 the Company executed the Definitive Agreement with Minera Mexicana and its shareholders formalizing the transaction. In order to acquire the shares of Minera Mexicana, the Company must make cash payments of US\$1,700,000 over 48 months and issue 4,000,000 shares of the Company over 24 months as follows:

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Notes to the Financial Statements

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(Stated in Canadian Dollars)

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Note 5 **Interests in Mineral Property Options** – (cont'd)

- (i) US \$50,000 upon signing of the Letter of Intent (paid);
- (ii) US \$50,000 upon signing a definitive agreement*;
- (iii) an additional US \$100,000 and issue 2,000,000 shares of the Company by August 6, 2011;
- (iv) an additional US \$300,000 and issue 2,000,000 shares of the Company by August 6, 2012;
- (v) an additional US \$400,000 by August 6, 2013; and
- (vi) an additional US \$800,000 by August 6, 2014.

In order to acquire a 100% interest in the Petlacala property from Minera Petlacala, Minera Mexicana must conduct a 3,000 meter drill program (completed) and make payments as follows:

- (i) \$7,950,000 in cash over 48 months of signing the agreement (US \$75,000 paid during the year ended February 28, 2011 and US \$75,000 paid subsequent February 28, 2011) ;
- (ii) Issuance of 4,000,000 shares (500,000 issued) of Minera Mexicana (which may be substituted with shares of the Company); and
- (iii) Completion of staged exploration expenditures in the aggregate amount of \$7,000,000 over 48 months.

Under the terms of the Share Purchase Agreement, the Company has agreed to fund the above cash, share and expenditure commitments required by Minera Mexicana to earn an interest in the Petlacala property.

In addition, Minera Petlacala will retain a 2% Net Profit Royalty. The Company has issued 100,000 shares as a finder's fee.

*As at February 28, 2011, the US\$50,000 due upon signing of a definitive agreement had not yet been paid, however Minera Mexicana has not demanded payment or given notice of default and has confirmed the agreement is still in good standing. This amount was due August 6, 2010. This amount had been accrued and was included in accounts payable and accrued liabilities as at February 28, 2011.

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Note 5 **Interests in Mineral Property Options** – (cont'd)***Real de Guadalupe Property***

On November 1, 2010 the Company entered into a letter of agreement (the "Agreement") with Minera Ligia, S.A. de C.V. ("Minera Ligia"), a private Mexican company at arm's length to the Company. The Agreement sets out the terms upon which the Company can acquire 100% of the issued and outstanding shares of Minera Ligia which holds an option to purchase a 100% interest in the Real de Guadalupe polymetallic gold-silver-copper-zinc-lead project in Guerrero State, Mexico, 40 under an option agreement dated March 12, 2010 with the current property vendors.

The Agreement provides the Company with the exclusive right to conduct due diligence on the property and on Minera Ligia, for the purpose of finalizing the agreement to purchase the shares of Minera Ligia, for cash payments of US \$800,000 over 48 months, the issue of 5,000,000 shares of the Company and expenditure of a minimum of \$1,800,000 on exploration expenses over a period of 4 years from the effective date of November 19, 2010, as follows:

- (i) Pay US \$50,000 upon signing of the Letter Agreement (paid);
- (ii) Pay US \$50,000 (paid) and issue 1,000,000 shares (issued) on November 19, 2010;
- (iii) expend \$200,000 on exploration expenditures by November 19, 2011;
- (iv) Pay US \$100,000, issue 1,000,000 shares and incur exploration expenditures of \$300,000 by November 19, 2012;
- (v) Pay US \$100,000, issue 1,000,000 shares and incur exploration expenditures of \$500,000 by November 19, 2013; and
- (vi) Pay US \$500,000, issue 2,000,000 shares and incur exploration expenditures of \$800,000 by November 19, 2014.

Environmental Protection Practices and Asset Retirement Obligation

The Company is subject to laws and regulations relating to environmental matters in all jurisdictions in which it operates, including provisions relating to property reclamation, discharge of hazardous material and other matters. The Company may also be held liable should environmental problems be discovered that were caused by former owners and operators of its properties and properties in which it has previously had an interest. The Company is not aware of any existing environmental problems related to any of its current or former properties that may result in a material liability to the Company, other than the amount accrued.

Included in the carrying value of interests in mineral property options is \$24,285 (US\$25,000) (2010: \$Nil) accrued as estimated reclamation costs arising as a result of trenching work completed on the Company's Petlacala property.

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Note 6 Share Capital and Contributed Surplusa) Authorized

Unlimited common shares without par value

b) Shares issued and Contributed Surplus

	Number	Amount	Contributed Surplus
Balance, February 28, 2009	4,050,001	\$ 517,166	\$ 65,989
Issued for cash pursuant to:			
Private placement at \$0.20	5,000,000	1,000,000	-
Exercise of agent's warrants at \$0.20	50,000	10,000	-
Share issue costs	-	(76,764)	-
Transfer from contributed surplus on exercise of agent's warrants	-	4,444	(4,444)
Balance, February 28, 2010	9,100,001	1,454,846	61,545
Issued for cash pursuant to:			
Private placement at \$0.30	4,000,000	1,087,720	112,280
Issued for acquisition of mineral property at \$0.25	500,000	125,000	-
Issued for acquisition of mineral property at \$0.22	1,000,000	220,000	-
Issued for finder's fee for acquisition of mineral property at \$0.25	100,000	25,000	-
Share issue costs	-	(76,176)	15,066
Stock-based compensation	-	-	181,941
Balance, February 28, 2011	14,700,001	\$ 2,836,390	\$ 370,832

During the year ended February 28, 2011, the Company completed two private placements for proceeds of \$1,200,000 pursuant to the issue of 4,000,000 units at \$0.30 per unit. Each Unit consists of one common share and one-half of one warrant, with each whole warrant entitling the holder to acquire an additional common share at \$0.45 per share until May, 2012 and December, 2012, respectively.

The shares issued in this private placement had a weighted average value of \$0.27 per share or \$1,087,720, which was equal to the market price on the date the shares were issued. The intrinsic fair value of the warrants was calculated to be \$0.03 per one-half warrant, or \$112,280, which was credited to contributed surplus.

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Notes to the Financial Statements

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Note 6 Share Capital and Contributed Surplus – (cont'd)b) Shares issued and Contributed Surplus – (cont'd)

An aggregate of \$61,110 in cash was paid to various finders for that portion of the financing attributable to these finders' efforts. In addition, a total of 160,800 in agents' warrants were issued, each warrant being exercisable at \$0.31 until May 18, 2011. Share issue costs include \$15,066 for the fair value of the agent's warrants.

The fair value of agents' warrants was determined using the Black-Scholes model with the following assumptions:

Dividend rate	0%
Risk-free interest rate	1.62%
Expected life	1 Year
Expected annual volatility	155%

During the year ended February 28, 2011, the Company issued 500,000 common shares valued at \$0.25 per share pursuant to the Petlacala Property acquisition (Note 5), The Company also issued 100,000 common shares as finder's fees in that acquisition. These shares are valued at \$125,000 and \$25,000, respectively, using the quoted market price of the Company's shares on the date of issuance and have been excluded from the statement of cash flows.

During the year ended February 28, 2011, the Company issued 1,000,000 common shares valued at \$0.22 per share pursuant to the Real de Guadalupe Property acquisition (Note 5). These shares are valued at \$220,000 using the quoted market price of the Company's shares on the date of issuance and have been excluded from the statement of cash flows.

During the year ended February 28, 2010, the Company completed a \$1,000,000 financing consisting of 5,000,000 common shares at \$0.20 per share. Pursuant to this private placement, the Company paid share issue costs of \$76,764.

During the year ended February 28, 2010, the Company issued 50,000 common shares pursuant to the exercise of agent's warrants at \$0.20 per share. The fair value of these warrants, \$4,444, transferred from contributed surplus to share capital on exercise, has been excluded from the statement of cash flows. The remaining 100,000 agent's warrants expired unexercised during the year.

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Note 6 **Share Capital and Contributed Surplus** – (cont'd)c) Stock-based Compensation

The Company, in accordance with the policies of the Exchange, is authorized to grant options to directors, officers, and employees to acquire up to 10% of common stock outstanding. Options may be granted for a maximum term of 5 years. Optioned shares will vest when granted except where granted for investor relations activities which vest and may be exercised in accordance with the vesting provisions as to ¼ of the options each 3 months.

During the year ended February 28, 2011, the Company granted incentive stock options to directors, key employees and consultants to acquire up to 595,000 shares at \$0.35 per share until April 15, 2015. The fair value of the 595,000 options granted was estimated to be \$181,941, using the Black-Scholes option pricing model with the following weighted average assumptions at date of grant:

Dividend rate	0%
Risk-free interest rate	2.55%
Expected life	5 Years
Expected annual volatility	198%

During the year ended February 28, 2011, 30,000 of the stock options granted during the year ended February 28, 2008 were forfeited following the resignation of a director.

No stock options were granted during the year ended February 28, 2010. During the year ended February 28, 2010, 85,000 options were forfeited following the resignation of a director.

A summary of the Company's outstanding stock options as of February 28, 2011 and 2010 and the changes during the years then ended is presented below:

	Number of Options	Weighted Average Exercise Price
Outstanding at February 28, 2009	400,000	\$0.20
Forfeited	(85,000)	\$0.20
Outstanding at February 28, 2010	315,000	\$0.20
Granted	595,000	\$0.35
Forfeited	(30,000)	\$0.20
Outstanding and exercisable at February 28, 2011	880,000	\$0.30

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Note 6 **Share Capital and Contributed Surplus** – (cont'd)c) Stock-based Compensation – (cont'd)

As at February 28, 2011, 880,000 stock options were outstanding, entitling the holders thereof to purchase one common share for each option held as follows:

Number of Shares	Number Exercisable	Exercise Price	Expiry Date	Contractual Life Remaining
275,000	275,000	\$0.20	August 20, 2012	1.48 years
10,000	10,000	\$0.20	August 20, 2017	6.48 years
595,000	595,000	\$0.35	April 15, 2015	4.13 years
880,000	880,000	\$0.30		3.33 years

d) Warrants Outstanding

A summary of the Company's outstanding share purchase warrants as at February 28, 2011 and 2010 and the changes during the years then ended is presented below:

	Number of Warrants	Weighted Average Exercise Price
Outstanding at February 28, 2009	150,000	\$0.20
Exercised	(50,000)	\$0.20
Expired	(100,000)	\$0.20
Outstanding at February 28, 2010	-	-
Issued	2,160,800	\$0.44
Outstanding at February 28, 2011	2,160,800	\$0.44

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Note 6 Share Capital and Contributed Surplus – (cont'd)d) Warrants Outstanding – (cont'd)

At February 28, 2011, there were 2,160,800 warrants exercisable to purchase one common share for each option held as follows:

Number of Shares	Exercise Price	Expiry Date
1,288,000	\$0.45	May 18, 2012
160,800	\$0.31	May 18, 2011
462,000	\$0.45	May 31, 2012
250,000	\$0.45	December 7, 2012
2,160,800	\$0.44	

Subsequent to February 28, 2011, 160,800 agent warrants at \$0.31 expired.

e) Escrow shares

At February 28, 2011, 1,200,001 (February 28, 2010: 1,800,001) shares were held in escrow subject to an escrow agreement and are being released in accordance with CPC policy guidelines.

Note 7 Related Party Transactions

During the year ended February 28, 2011, the Company paid rent of \$30,500 (2010: \$18,000), office and administration fees of \$62,144 (2010: \$18,000) and shareholders communications of \$14,000 (2010: \$Nil) to two companies controlled by a director of the Company. The Company also paid management services fees of \$20,000 (2010: \$Nil) and consulting fees of \$31,750 (2010: \$Nil) to directors.

Included in prepaid expenses at February 28, 2011, is \$8,000 (2010: \$Nil) for prepaid rent and refundable expenses advance with a company controlled by a director.

Included in accounts payables and accrued liabilities at February 28, 2011 is \$78,548 (2010: \$Nil) due to two directors and to a company with a director in common.

These charges were measured at the exchange amount, which is the amount agreed upon by the transacting parties.

Note 8 Capital Management

The Company's objective when managing capital is to safeguard the Company's ability to continue as a going concern, so that it can continue to provide returns for shareholders and benefits for other stakeholders.

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Note 8 Capital Management – (cont'd)

The Company considers the items included in shareholders' equity as capital. The Company manages the capital structure and makes adjustments to it in light of changes in economic conditions and the risk characteristics of the underlying assets. In order to maintain or adjust the capital structure, the Company may issue new shares through private placements, sell assets to reduce debt or return capital to shareholders. The Company is not subject to externally imposed capital requirements.

There have been no changes in the Company's approach to capital management during the year ended February 28, 2011.

Note 9 Seabridge Agreement

The Company entered into a letter agreement dated March 25, 2009, and amended July 9, 2009, and September 30, 2009, as well as an Asset Purchase agreement dated July 31, 2009 and amended September 30, 2009 (the "Agreement") with Seabridge Gold Inc. ("Seabridge") to acquire various mineral claims in Nevada (the "Seabridge Acquisition") held by Seabridge's wholly-owned subsidiaries.

During the year ended February 28, 2010, the agreement was terminated and a write-down of \$222,749 relating to deposits and property investigation costs, was reported on the statement of operations. The US\$409,925 was recovered and is included in cash at February 28, 2010.

Note 10 Income taxes

A reconciliation of the income tax provision computed at statutory rates to the reported income tax provision is as follows:

	February 28, 2011	February 28, 2010
Loss before income taxes	\$ (884,021)	\$ (716,669)
Basic statutory and provincial income tax rate	28.20%	29.75%
Expected tax recovery on net loss, before income tax	(249,000)	(213,200)
Differences due to recognition of items for tax purposes:		
Permanent differences	72,000	2,900
Effect of reduction in statutory rate	20,000	36,100
Share issue costs	(15,000)	(19,200)
Increase in valuation allowance	172,000	193,400
Future income tax expense	\$ -	\$ -

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Note 10 **Income taxes** – (cont'd)

Significant components of the Company's future tax assets and liabilities are as follows:

	February 28, 2011	February 28, 2010
Future income tax assets		
Non-capital losses carried forward	\$ 345,000	\$ 181,000
Mineral property expenditures	62,000	56,000
Investment in target companies	(48,000)	-
Undeducted financing cost	28,000	23,000
Capital assets	(3,000)	-
	384,000	260,000
Less: valuation allowance	(432,000)	(260,000)
Future income tax liability	\$ (48,000)	\$ -

The Company has recorded a valuation allowance against its future income tax assets based on the extent that it is more likely-than-not that sufficient and appropriate taxable income will not be realized during the carry forward periods to utilize all the future tax assets.

At February 28, 2011, the Company has accumulated non-capital losses totalling approximately \$1,380,000, which may be applied against future years' taxable income. The non-capital losses expire in various amounts from 2028 to 2031.

Note 11 **Financial Instruments**a) Interest rate risk

The Company's cash earns interest at a variable interest rate. Because of the nature of this financial instrument, fluctuations in market rates do not have a significant impact on estimated fair values as of February 28, 2011. Future cash flows from interest income on cash will be affected by interest rate fluctuations. Interest rate risk consists of two components:

- (i) To the extent that payments made or received on the Company's monetary assets and liabilities are affected by changes in the prevailing market interest rates, the Company is exposed to interest rate cash flow risk.
- (ii) To the extent that changes in prevailing market interest rates differ from the interest rates in the Company's monetary assets and liabilities, the Company is exposed to interest rate price risk.

The Company's exposure to interest rate fluctuations is minimal.

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Note 11 **Financial Instruments** – (cont'd)

b) Credit risk

Credit risk is the risk that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss. The Company is exposed to credit risk with respect to its cash, the balance of which at February 28, 2011 is \$6,435. Cash is held at a chartered Canadian financial institution.

c) Liquidity risk

Liquidity risk arises from the excess of financial obligations over available financial assets due at any point in time. The Company's objective in managing liquidity risk is to maintain sufficient readily available reserves in order to meet its liquidity requirements. The Company achieves this by maintaining sufficient cash reserves. As at February 28, 2011, the Company was holding cash of \$6,435. The Company's accounts payable and accrued liabilities are due in the short term.

d) Currency risk

Currency risk is the risk that funds held in currencies other than the operating currency will fluctuate negatively, resulting in a foreign exchange loss. The Company is exposed to currency risk with respect to its cash, the balance of which at February 28, 2011 was \$6,435. Of the cash balance, US Dollars of \$5,742 (CDN\$5,578) is held at a Canadian financial institution.