



Second Quarter Report

June 30, 2006

Notice to Readers

The interim unaudited consolidated financial statements of Augusta Resource Corporation (the "Company") for the three and six months ended June 30, 2006 ("Financial Statements") have been prepared by management and have not been reviewed by the Company's auditors. The Financial Statements should be read in conjunction with the Company's restated audited consolidated financial statements for the year ended December 31, 2005 which are available at the SEDAR website at www.sedar.com.

Directors' Report to Our Shareholders

For the first half of 2006, management continued to focus its efforts on advancing its properties, in particular the development of the 100% owned Rosemont copper/molybdenum project in Arizona. During the first quarter of 2006, the Company raised the largest ever financing in its history to complete the acquisition of the Rosemont property on March 31, 2006 and advance exploration, development and permitting activities. The Company commenced a 20,000 meter drill program during the latter part of the second quarter with emphasis on moving inferred resources into the measured and indicated category. The drill program and a concurrent program of re-logging and re-assay of historic drill core will define potential oxide copper zones and quantify a silver resource for the deposit.

On June 14, 2006 the Company released the results of a Preliminary Assessment ("PA") on the Rosemont project. It is our belief that these results, while still preliminary, suggest that the Rosemont deposit may well be one of the best undeveloped open pit copper projects in the United States. Also in June, the Company obtained a sustainable water supply source for Rosemont when it signed two contracts with the Central Arizona Water Conservation District (CAWCD). These contracts are significant because they address the water supply question ahead of the Environmental Impact Statement Review process, which removes a significant amount of uncertainty regarding project impacts to the region.

On August 1, 2006 the Company filed a "Plan of Operations" for the Rosemont project with the United States Forest Service, the first formal step signifying start of the Environmental Impact Statement and Public Review Processes of that plan - two key activities in the permitting process. Concurrently, the Company commenced a full feasibility study on Rosemont. M3 Engineering and Technology Corporation of Tucson, Arizona was awarded the contract for the feasibility study after a due bidding and selection process. The study is scheduled for completion by the end of the first quarter of 2007.

In addition, the Company continued exploration activity on its Mount Hamilton and Shell Deposit properties in Nevada. During the quarter management announced the start of a Pre-Feasibility Study at Mount Hamilton to evaluate development of the Centennial Deposit as well as a 10,000-foot Phase I Exploratory Drilling Program on the Shell molybdenum/tungsten deposit.

On August 10, 2006 the Company graduated to the Toronto Stock Exchange with the symbol "AZC". The move to Canada's major stock exchange is a further step in our strategic plan to maximize the value of the Company's assets by expanding awareness within the global investment community.

Financing

On March 17, 2006 the Company closed a \$44,099,000 equity financing which will fulfill our funding requirements for 2006 and into 2007. On June 1, 2006 the Company retired the remaining \$3,000,000 convertible debenture issued in June 2005.

Personnel

The Company announced the appointment of Mr. Bruce Nicol as Senior Vice-President and Chief Financial Officer of Augusta, effective September 1, 2006. Mr. Nicol is a Chartered Accountant with 15-years of professional experience in the international mining industry, working with Placer Dome as an officer in senior financial roles. Mr. Nicol will replace Donald B. Clark, who has been Chief Financial Officer of Augusta since June 2002. Mr. Clark will continue as a Director of Augusta, a position he has held since February 1996.

On August 2, 2006 the Company announced the appointments of Mr. Lance Newman as Vice-President, Metallurgical Operations and Mr. Mark Stevens as Chief Project Geologist. Both Mr. Newman and Mr. Stevens are seasoned members of the team with proven track records in project development and operations.

Mr. Newman has 19 years of concentrating, smelting and refining operations experience with several successful startups in base and precious metals plant operations. In addition to holding a Bachelor of Science (honours) in Chemistry from Rhodes University, Mr. Newman is also Chairman of the Palladium

Research Group and an Advisory Board Member for the Process Plant Technology faculty at the Montana State University College of Technology.

Mr. Stevens joins Augusta with 25 years of technical and managerial experience in the exploration, evaluation, and mining of base and precious metals. Mr. Stevens holds his Bachelor of Science in Geology from Colorado State University, and his Masters of Science in Geology from the University of Utah.

The Company also announced the appointment of Mrs. Marlo Hamer-Jackson as Manager, Investor Relations and Corporate Communications, and Ms. Tracey Brix-Nielsen as Controller, to its management team. Mrs. Hamer-Jackson and Ms. Brix-Nielsen bring to the Company extensive knowledge and experience in the resource sector working with Goldcorp Inc., Placer Dome Inc. and Teck Cominco Ltd.

Project Updates

Rosemont Property – The 2006 Rosemont Deposit Mineral Resource Statement (excluding satellite deposits) was announced in the first quarter of 2006, reporting significant improvements when compared with the historic resource reported by Anamax (Pincock, Allen and Holt – 1977). The mineral resource estimation work was performed by or under the direction of Mr. William L. Rose, P.E., Principal Mining Engineer of WLR Consulting, Inc. (WLRC) of Lakewood, Colorado. Mr. Rose is an independent Qualified Person under the standards set forth by Canadian National Instrument 43-101. Details of the Mineral Resource Estimate can be found in the technical report entitled Mineral Resource Estimate, Revised Technical Report for the Rosemont Deposit dated April 21, 2006 filed on SEDAR (www.sedar.com) and also available on the Company's website.

Following up on the new resource estimate, the Company announced the commencement of a 20,000-meter diamond drill program at Rosemont on March 27, 2006. The program is designed to meet the following objectives:

- Increase the current measured and indicated resource by upgrading the existing inferred resource at the Rosemont deposit;
- Provide better definition of near surface oxide-copper mineralization;
- Provide better definition of silver and gold mineralization in the Rosemont deposit;
- Acquire geotechnical data to support pit slope designs;
- Initiate exploration for additional resources in the Broadtop Butte area.

Initial drill results from four holes of the current 30-hole 20,000 meter program at Rosemont were announced on July 19, 2006. Highlights include 190.5 m at 0.51% Cu, 140.21m at 1.32% Cu, 111.25m at 0.82% Cu and 163m at 0.72% Cu. The company has 5 drill rigs active on the property, and is expecting to complete the program by the end of September.

In early May the Company announced positive results from metallurgical test work that would impact production and process techniques at Rosemont. The new findings had a major positive impact on flow sheet design and the financial performance of the project. The Company published the PA in June 2006, which demonstrated that the Rosemont copper/molybdenum deposit may be developed as a low cost open pit mine with potentially robust project economics. With the positive project economics noted in the PA and the continued buoyant market for these strategic metals, management decided to move the Rosemont project to full feasibility study. M3 Engineering was awarded the contract in early August, and is expected to deliver the study by the end of the first quarter of 2007.

The Company obtained a sustainable water supply source for Rosemont when it signed two contracts with the Central Arizona Water Conservation District (CAWCD) in June. One contract allows Augusta to become a water user in the CAWCD system, allowing Augusta to request up to 10,000 acre-feet of water per year for the five-year term of the contract. The second contract allows the Company to store the water in the Pima Mine Storage and Retrieval Facility in Pima County, Arizona. The pre-stored water will accumulate in a water-bank account to offset groundwater removed from the aquifer once mine operations

begin on the Rosemont property. The planned mine operations at Rosemont will incorporate water-miser design principles and are expected to use 5,000 acre-feet per year or less.

The Company also commenced the permitting process when it filed Rosemont's "Plan of Operations" with the US Forest Service in early August. The Plan of Operations allows the Company to move forward with the Environmental Impact Statement and Public Review Processes.

White Pine County Properties – The Company announced the acquisition of the Mount Hamilton property located in Nevada in December 2004, and announced the option of the Shell Deposit property in January 2005. The Shell Deposit property is situated in close proximity to the Mount Hamilton property, approximately 35 miles west of Ely, Nevada.

The Mount Hamilton property contains a historical resource of gold, molybdenum, tungsten and copper and the Shell Deposit property contains a historical resource of molybdenum, gold and tungsten. Compilation of data from prior programs has been completed and an updated geological model developed.

On May 11, 2006, the Company announced it had retained Pincock, Allen & Holt, to conduct a Pre-Feasibility Study at Mount Hamilton, due for completion during the third quarter of 2006. The study is evaluating the development of the Centennial Deposit as an open-pit heap leach gold mine. The Mount Hamilton project contains 405,000 ounces gold ("Au") and 2,153,000 ounces silver ("Ag") in an Indicated Resource of 12 million tons at 0.034 ounces ("oz") per ton Au and 0.18 oz per ton Ag, using a cut-off grade of 0.016 per ton Au. Mineralization appears to be open in several directions, and potentially amenable to open pit mining.

Also in May, the Company announced a 10,000-foot Phase I Exploratory Drilling Program at the Shell Deposit. The drilling program commenced in August.

Lone Mountain Property – On May 15, 2006 the Company announced that after completing a detailed geological assessment, the Company has elected not to pursue its option to purchase the Lone Mountain project located in Grant County, South Western New Mexico.

Management continues to build a strong foundation from which your Company can grow. The Rosemont, Mount Hamilton, and the Shell projects are valuable assets. We remain committed to develop these assets in order to realize significant value for all of our shareholders. For further details please refer to our Financial Statements and Management Discussion and Analysis.

On behalf of the Board,

/S/ Gil Clausen

Gil Clausen
President & Chief Executive Officer

August 28, 2006

AUGUSTA RESOURCE CORPORATION
CONSOLIDATED BALANCE SHEETS
(UNAUDITED)
As at June 30, 2006 and December 31, 2005

(See Note 1 - Basis of presentation)

	Notes	June 30 2006	December 31 2005
ASSETS			
			(restated, note 2)
CURRENT			
Cash and cash equivalents		\$ 20,546,630	\$ 2,252,044
Accounts receivable	10	278,068	28,470
Prepaid expenses		173,684	48,334
Deferred debt issuance costs	6	-	272,796
		20,998,382	2,601,644
OFFICE EQUIPMENT	3	7,516	9,042
MINING ASSETS			
	4		
Land and Mining properties		31,223,501	15,161,604
Deferred exploration expenses		6,118,149	3,035,560
		37,341,650	18,197,164
		\$ 58,347,548	\$ 20,807,850
LIABILITIES			
CURRENT			
Accounts payable and accrued liabilities	10	\$ 946,313	\$ 813,931
Current portion of convertible debenture	6	-	2,204,032
Current portion of notes and advances	5	1,524,208	1,136,895
		2,470,521	4,154,858
LONG-TERM			
Future income taxes		2,200,000	2,200,000
Notes, advances and other	5	18,490	1,492,267
		4,689,011	7,847,125
Commitments	12		
SHAREHOLDERS' EQUITY			
Share capital	7	59,199,668	18,437,248
Contributed surplus	7	13,896,195	6,226,110
Deficit		(19,437,326)	(11,702,633)
		53,658,537	12,960,725
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY		\$ 58,347,548	\$ 20,807,850

On Behalf of the Board of Directors

/S/ Richard W. Warke

Richard W. Warke – Director
See accompanying Notes to the Consolidated Financial Statements

/S/ Gil Clausen

Gil Clausen - Director

AUGUSTA RESOURCE CORPORATION
CONSOLIDATED STATEMENTS OF OPERATIONS AND DEFICIT
(UNAUDITED)
For the Three and Six months ended June 30, 2006 and 2005

	Three Months Ended June 30		Six Months Ended June 30	
	2006	2005	2006	2005
		(restated, note 2)		(restated, note 2)
EXPENSES				
Accounting and audit	\$ 26,900	\$ -	\$ 62,400	\$ -
Administration (note 10)	7,500	7,500	15,000	15,000
Amortization	681	-	1,526	-
Consulting and communication	20,556	(154,576)	45,411	38,752
Debt issuance costs (note 6)	109,118	45,178	272,796	45,178
Filing and regulatory	29,771	76,351	48,936	114,846
Fiscal and advisory services	21,811	16,506	40,018	17,023
Foreign exchange (gain)	(105,937)	2,248	(115,197)	2,440
Investor relations	15,623	33,236	73,437	33,236
Legal fees	56,571	5,146	76,710	5,251
Office and sundry	123,815	100,764	175,873	130,714
Insurance	-	-	74,341	-
Recruitment fees	-	-	-	45,174
Salaries, benefits and bonuses	650,176	155,108	891,643	211,427
Stock based compensation	787,510	223,008	1,018,056	345,525
Write-off of mining assets	309,550	-	309,550	-
Travel	97,920	20,170	146,019	20,170
Other expenses	58,990	(8,847)	58,990	(8,847)
	<u> </u>	<u> </u>	<u> </u>	<u> </u>
Loss from operations	(2,210,555)	(521,792)	(3,195,509)	(1,015,889)
Interest and other income	233,839	6,039	305,822	7,420
Interest and finance charges	(460,167)	(345,309)	(1,073,677)	(343,627)
	<u> </u>	<u> </u>	<u> </u>	<u> </u>
LOSS FOR THE PERIOD	(2,436,883)	(861,062)	(3,963,364)	(1,352,096)
Deficit, beginning of the period	(16,747,320)	(5,586,037)	(11,702,633)	(4,991,105)
Share issue expenses	(253,123)	(1,086,277)	(3,771,329)	(1,190,175)
	<u> </u>	<u> </u>	<u> </u>	<u> </u>
DEFICIT, END OF PERIOD	<u>\$ (19,437,326)</u>	<u>\$ (7,533,376)</u>	<u>\$ (19,437,326)</u>	<u>\$ (7,533,376)</u>
BASIC & DILUTED LOSS PER SHARE	<u>\$ (0.04)</u>	<u>\$ (0.03)</u>	<u>\$ (0.08)</u>	<u>\$ (0.05)</u>
WEIGHTED AVERAGE NUMBER				
OF SHARES OUTSTANDING	<u>57,210,694</u>	<u>30,542,602</u>	<u>48,660,225</u>	<u>27,896,450</u>

See accompanying Notes to the Consolidated Financial Statements

AUGUSTA RESOURCE CORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED)
For the Three and Six months ended June 30, 2006 and 2005

	Three Months Ended June 30		Six Months Ended June 30	
	2006	2005	2006	2005
		(restated, note 2)		(restated, note 2)
NET INFLOW (OUTFLOW) OF CASH RELATED TO THE FOLLOWING:				
OPERATING				
Net loss for the period	\$ (2,436,883)	\$ (861,062)	\$ (3,963,364)	\$ (1,352,096)
Items not affecting cash:				
Discount interest on debt	413,131	-	957,624	-
Debt issuance costs	109,118	45,178	272,796	45,178
Amortization	681	-	1,526	-
Accrued interest on debt	-	296,724	-	297,943
Unrealized foreign exchange	(65,148)	-	(80,232)	-
Write-off of mining assets	309,550	-	309,550	-
Stock based compensation	787,510	223,008	1,018,056	345,525
Other	(1,202)	(8,847)	(2,470)	(8,847)
	(883,243)	(304,999)	(1,486,514)	(672,297)
Net changes in non-cash working capital items: (note 8)	29,764	7,036	44,095	(263,121)
	(853,479)	(297,963)	(1,442,419)	(935,418)
FINANCING				
Issuance of common shares	1,765,025	9,713,661	2,410,259	10,823,661
Issuance of convertible debt security	-	6,000,000	-	6,000,000
Repayment of notes and advances	(1,165,420)	(14,950)	(1,165,420)	(14,950)
Repayment of convertible debt security	(3,000,000)	-	(3,000,000)	-
Issuance of special warrants	-	-	44,099,000	-
Share issue expense	(113,863)	(708,668)	(2,866,139)	(708,668)
Subscriptions for common shares	-	(727,500)	-	(1,050,000)
	(2,514,258)	14,262,543	39,477,700	15,050,043
INVESTING				
Acquisition of DHI Minerals Inc.	-	(4,000)	-	(4,000)
Investment in mining properties, net of related payables	(81,021)	(8,565,468)	(16,333,132)	(8,590,461)
Investment in fixed assets	-	(10,636)	-	(10,636)
Deferred exploration expenses, net of related payables	(2,606,896)	(205,600)	(3,407,563)	(234,557)
	(2,687,917)	(8,785,705)	(19,740,695)	(8,839,654)
NET CASH INFLOW (OUTFLOW)	(6,055,654)	5,178,875	18,294,586	5,274,971
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD	26,602,284	1,085,895	2,252,044	989,799
CASH AND CASH EQUIVALENTS, END OF PERIOD	\$ 20,546,630	\$ 6,264,770	\$ 20,546,630	\$ 6,264,770
SUPPLEMENTAL INFORMATION				
Interest Paid	\$ 135,000	\$ -	\$ 135,000	\$ -
Interest Received	\$ 61,699	\$ 6,039	\$ 109,201	\$ 7,420

See accompanying Notes to the Consolidated Financial Statements

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)
JUNE 30, 2006 AND 2005

1. BASIS OF PRESENTATION

The accompanying interim consolidated financial statements of Augusta Resource Corporation (the “Company”) have been prepared in accordance with Canadian generally accepted accounting principles for interim financial statements and accordingly do not include all disclosures required for annual financial statements.

These interim consolidated financial statements follow the same significant accounting policies and methods of application as the Company’s annual restated consolidated financial statements for the year ended December 31, 2005 (the “Annual Financial Statements”). The interim consolidated financial statements should be read in conjunction with the Annual Financial Statements.

In the opinion of management, all adjustments (including normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for interim periods are not necessarily indicative of the result that may be expected for the full fiscal year ending December 31, 2006.

2. RESTATEMENT

During the preparation of the Form 40-F filing document, a requirement of an American Stock and Options Exchange (AMEX) listing the Company is pursuing, the Company discovered non-cash errors relating to its financial statements (including the audited year end financial statements) for the first quarter ended March 31, 2006 as well as for the each quarter of 2005. In the previously released financial statements the Company had not properly accounted for the convertible debenture issued on June 1, 2005. Canadian Institute of Chartered Accountants (“CICA”) Handbook Section 3860 requires that the proceeds received from the issuance of convertible debt be allocated between its equity and debt components. The Company had treated all the proceeds as debt. Further, upon review of the option pricing model (Black-Scholes) used for valuing stock options and warrants issued during 2005, the Company concluded that the time period used to calculate the volatility assumption required adjustment.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)
JUNE 30, 2006 AND 2005

2. RESTATEMENT (continued)

Through June 30, 2005 and as at December 31, 2005 the impact of the restatement was:

	As previously reported	Adjustments	As restated
<u>December 31, 2005</u>			
<u>Balance Sheet</u>			
Deferred debt Issuance costs	1,132,792	(859,996)	272,796
Current portion of convertible debt	3,000,000	(795,968)	2,204,032
Share capital	17,392,510	1,044,738	18,437,248
Contributed surplus	7,177,811	(951,701)	6,226,110
Deficit	(11,545,568)	(157,065)	(11,702,633)
<u>June 30, 2005</u>			
<u>Statement of operations</u>			
Debt issuance costs	-	45,178	45,178
Interest and finance charges	68,681	274,946	343,627
Stockbased compensation	1,441,128	(1,095,603)	345,525
Net loss for the period	(2,127,575)	775,479	(1,352,096)
Share issue expenses	(2,323,104)	1,132,929	(1,190,175)
Deficit, end of period	(9,441,784)	1,908,408	(7,533,376)
<u>Statement of cash flows</u>			
Net loss for the period	(2,127,575)	775,479	(1,352,096)
Accrued interest on debt	22,997	274,946	297,943
Debt issuance costs	-	45,178	45,178
Stock based compensation	1,441,128	(1,095,603)	345,525

3. OFFICE EQUIPMENT

	<u>June 30, 2006</u>			<u>December 31, 2005</u>
	Cost	Accumulated Amortization	Net Book Value	Net Book Value
Computer hardware	\$ 10,636	\$ 3,120	\$ 7,516	\$ 9,042

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)
JUNE 30, 2006 AND 2005

4. MINING ASSETS

On March 31, 2006 the Company exercised its option to purchase the Rosemont property in Pima County, Arizona with a payment of \$16.1 million. Augusta now owns a 100% interest in the Rosemont property subject to a 3% NSR.

The purchase price has been allocated based on the fair value of the consideration provided which equates the fair value of the Rosemont property land and mineral rights acquired based on management's best estimates and takes into account all available information at the time these consolidated financial statements were prepared. The process has been conducted in accordance with the recent accounting pronouncement relating to "Mining Assets – Impairment and Business Combinations" (Emerging Issue Committee Abstract 152).

On May 15, 2006 the Company announced that after completing a detailed geological assessment, the Company has elected not to pursue its option to purchase the Lone Mountain project.

	Mining Properties Cost		Deferred Exploration Expenses	
	June 30 2006	December 31 2005	June 30 2006	December 31 2005
Mining assets:				
Rosemont property	\$24,437,454	\$ 8,315,611	\$ 5,879,898	\$ 2,831,281
Mt. Hamilton property	6,574,757	6,574,757	225,463	142,543
Lone Mountain property	-	271,236	-	48,947
Shell property	211,290	-	12,788	12,789
	<u>\$31,223,501</u>	<u>\$15,161,604</u>	<u>\$ 6,118,149</u>	<u>\$ 3,035,560</u>
Mining properties:	2006	2005		
Balance, beginning of period	\$15,161,604	\$ 285,064		
Acquisition costs	16,333,132	15,124,447		
Lone Mountain cost adjustment	(24,993)			
Write-offs	(246,242)	(247,907)		
Balance, June 30, 2006 and December 31, 2005	<u>\$31,223,501</u>	<u>\$15,161,604</u>		
Deferred exploration expenses:				
Balance, beginning of period	\$ 3,035,560	\$ 19,785		
Geologists, consultants and professional services	3,145,897	3,019,369		
Write-offs	(63,308)	(3,594)		
Balance, June 30, 2006 and December 31, 2005	<u>\$ 6,118,149</u>	<u>\$ 3,035,560</u>		

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)
JUNE 30, 2006 AND 2005

5. LONG TERM NOTES AND ADVANCES

	June 30 2006	December 31 2005
Notes and advances	\$ 41,778	\$ 44,692
Long term notes	1,500,920	2,584,470
	1,542,698	2,629,162
Less: Current portion	(1,524,208)	(1,136,895)
Total long term notes and advances	<u>\$ 18,490</u>	<u>\$1,492,267</u>

The purchase of the Mount Hamilton property included cash consideration of \$3,000,000 USD (\$3,103,438 CDN). The initial installment payment of \$500,000 USD (\$620,100 CDN) was accrued in April 2005 and paid. On the purchase of the Mount Hamilton property two non-interest bearing US\$ notes were given totaling \$2,500,000 USD (\$2,655,695 CDN) and were discounted using an interest rate of 15%. On April 30, 2006 the USD \$1,000,000 note was repaid.

	Amount USD\$	Discounted USD\$	Discounted CDN\$
April 30, 2007 (current portion of long term note)	1,500,000	1,344,669	1,500,920
Total long term notes	<u>\$ 1,500,000</u>	<u>\$ 1,344,669</u>	<u>\$ 1,500,920</u>

Other notes and advances do not provide for specific terms of repayment and are unsecured.

6. CONVERTIBLE DEBENTURE

On June 1, 2005, in connection with the Rosemont acquisition, the Company issued a convertible debenture for \$6,000,000. The debenture has a one-year term, with half due within six-months, and is convertible at the option of the lender into 2,181,818 common shares of the Company at a price of \$2.75 per share. The convertible debenture bears an interest rate of 9% annually and the Company has the option to repay the convertible debenture on the specified repayment dates in cash or stock. The convertible debenture was issued with 363,363 common shares of the Company to the lender at a fair market value at the date of the transaction of \$2.805 per common share (after a discount of 15% to reflect a hold period expiring on October 2, 2005.).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)
JUNE 30, 2006 AND 2005

6. CONVERTIBLE DEBENTURE (continued)

In accordance with CICA Handbook Section 3860, and following the fair value allocation approach, the Company allocated the proceeds as follows:

Common shares	\$1,019,233
Convertible debenture	
Equity component	1,478,083
Debt component	<u>3,502,684</u>
	\$6,000,000

The difference between the debt allocation of \$3,502,684 and the repayment amount of \$6,000,000 is interest expense, which is accrued over the term of the debenture. Through June 30, 2006, \$2,497,316 of the interest expense had been accrued including \$347,838 for the second quarter of 2006.

On November 17, 2005 the Company renegotiated the terms of its convertible debenture to allow for repayment in the form of cash and stock, as opposed to cash or stock. As consideration, the Company agreed to issue 750,000 warrants with an exercise price of \$1.44 expiring in one year, for which regulatory approval was received on March 15, 2006. The fair value of the warrants issued was \$288,938, which was allocated to debt (\$203,193) and equity (\$85,745).

On December 1, 2005, the Company retired \$3,000,000 of the convertible debenture plus interest of \$270,000 through payment of \$1,620,000 in cash and the issuance of 1,500,000 common shares at a price of \$1.10 per share. As the shares were issued at discount of 20% to the market value in accordance with the terms of the convertible debenture agreement, a loss on repayment of the convertible debenture of \$390,000 occurred which was recorded in the statement of operations.

In connection with the issuance of the convertible debenture and common shares, the Company also paid a fee in the amount of 6% cash and 218,181 warrants. The fair value of the warrants of \$247,769 was allocated to debt (\$144,643) and equity (\$103,126). Each warrant is exercisable to acquire one common share at \$2.75 per warrant for a period of one year expiring on June 14, 2006. The warrants had a hold period expiring on October 15, 2005.

The remaining debenture was retired on June 1, 2006 with the payment of \$3 million cash.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)
JUNE 30, 2006 AND 2005

6. CONVERTIBLE DEBENTURE (continued)

	June 30 2006	December 31 2005
Convertible debenture, beginning of period	\$2,204,032	\$ -
Convertible debenture issued	-	3,502,684
Accretion of discount interest	795,968	1,701,348
Repayment of debenture	(3,000,000)	(3,000,000)
Convertible debenture, end of period	<u>\$ -</u>	<u>\$2,204,032</u>
Deferred debt issuance costs, beginning of period	\$ 272,796	\$ -
Debt issuance costs - incurred	-	598,424
Debt issuance costs - amortized	(272,796)	(325,628)
Deferred debt issuance costs, end of period	<u>\$ -</u>	<u>\$ 272,796</u>

7. SHARE CAPITAL

- (a) Authorized:** Unlimited number of common shares without par value.
- (b) Issued:** Changes in the Company's share capital were as follows:

	Number of Shares	Amount
Common shares, Balance at December 31, 2003	9,164,555	\$ 4,081,331
Issued for finder's fees	140,000	7,000
Issued for cash	10,460,000	523,000
Common shares, Balance at December 31, 2004	19,764,555	\$ 4,611,331
Issued to convertible debenture holder	363,363	1,019,233
Issued for convertible debenture repayment	1,500,000	2,040,000
Issued for property acquisitions	4,100,000	885,000
Issued for cash	8,998,500	8,370,551
Issued for fractional rounding due to share consolidation	9	-
Issued for options exercised	445,833	75,873
Issued for warrants exercised	4,342,333	1,435,260
Common shares, Balance at December 31, 2005	39,514,593	\$ 18,437,248
Issued for warrants exercised	2,068,807	2,634,405
Issued for options exercised	5,000	500
Issued for special warrants exercised	23,210,000	38,127,515
Common shares, Balance at June 30, 2006	64,798,400	\$ 59,199,668

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
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7. **SHARE CAPITAL (continued)**

(c) **Private Placement**

The proceeds from the following special warrants were allocated to special warrants and contributed surplus based on the relative fair value of the underlying common shares and warrants at the dates of issuance.

On March 17, 2006 the Company closed a brokered private placement of 23,210,000 special warrants with gross proceeds of \$44,099,000.

Each Special Warrant is convertible, without payment of additional consideration, into a unit consisting of one common share (23,210,000 shares) and one-half transferable common share purchase warrant (11,605,000 warrants). Each whole warrant will entitle the holder to acquire, at any time within two years, one common share of the Company at a price of \$3.10 expiring on March 17, 2007 and \$4.10 expiring on March 17, 2008.

The Company filed and obtained a receipt for a short form prospectus, which qualifies the distribution of the common shares and warrants underlying the Special Warrants effective April 28, 2006.

In consideration for their services, the agents received a cash commission equal to 6% of the gross proceeds, totaling \$2,645,940 from the offering and 1,392,600 agent's warrants exercisable into common shares which is equal to 6% of the number of Special Warrants sold. Each agent's warrant will entitle the holder to acquire one common share of the Company at a price of \$3.10 expiring March 17, 2007 and \$4.10 expiring March 17, 2008. Fair value of the agent's warrants is \$905,190. The fair value of the warrants was calculated using the Black-Scholes option pricing model for warrant valuation, assuming an average volatility of 97% on the underlying shares, a risk free interest rate of 4.00%, a two year term to expiry and no annual dividends.

(d) **Options**

On June 30, 2006, certain directors and officers of the Company held 4,269,334 stock options, and certain employees of the Company held 422,500 stock options to purchase common shares of the Company.

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8. SHARE CAPITAL (continued)

(d) Options (continued)

The following table summarizes the status of the Company's stock option plans as at June 30, 2006:

	2006	
	Number of Shares	Average Exercise Price
Outstanding at beginning of year	3,226,834	\$ 1.35
Granted	1,470,000	\$ 2.13
Exercised	(5,000)	\$ 0.10
Outstanding at end of year	4,691,834	\$ 1.71
Options exercisable at June 30, 2006	1,086,834	\$ 1.36

The following table summarizes stock options outstanding at June 30, 2006:

Options Outstanding and Exercisable					
Exercise Prices	Number Outstanding at June 30, 2006	Weighted Average Remaining Contractual Life	Weighted Average Exercise Prices	Number Exercisable at June 30, 2006	Weighted Average Exercise Prices
\$ 0.30	87,667	0.5 Years	\$ 0.30	87,667	\$ 0.30
\$ 0.33	66,667	0.9 Years	\$ 0.33	66,667	\$ 0.33
\$ 0.10	207,500	3.4 Years	\$ 0.10	207,500	\$ 0.10
\$ 2.05	450,000	3.8 Years	\$ 2.05	225,000	\$ 2.05
\$ 1.96	125,000	3.8 Years	\$ 1.96	62,500	\$ 1.96
\$ 2.30	100,000	4.1 Years	\$ 2.30	100,000	\$ 2.30
\$ 1.56	2,035,000	4.2 Years	\$ 1.56	200,000	\$ 1.56
\$ 1.55	150,000	4.3 Years	\$ 1.55	37,500	\$ 1.55
\$ 2.07	816,000	4.8 Years	\$ 2.07	-	\$ 2.07
\$ 2.20	654,000	4.8 Years	\$ 2.20	100,000	\$ 2.20
	4,691,834		\$ 1.71	1,086,834	\$ 1.36

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
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7. SHARE CAPITAL (continued)

(e) Warrants

The following table summarizes information about warrants outstanding at June 30, 2006. Each warrant is exercisable into one common share.

Currency	Exercise Price	Expiry Dates	Outstanding at December 31,2005	Issued	Exercised	Expired	Outstanding at June 30, 2006
CDN	\$ 0.45	March 3, 2006	685,000	-	685,000	-	-
CDN	\$ 1.25	April 15, 2006	729,807	-	704,807	25,000	-
CDN	\$ 2.50	April 15, 2006	832,155	-	229,000	603,155	-
CDN	\$ 2.75	June 14, 2006	218,181	-	-	218,181	-
CDN	\$ 0.10	September 7, 2006	7,460,000	-	-	-	7,460,000
CDN	\$ 1.44	April 28, 2007	-	750,000	450,000	-	300,000
USD	\$ 0.16	May 6, 2007	3,750,000	-	-	-	3,750,000
CDN	\$ 3.00	June 29, 2007	2,200,000	-	-	-	2,200,000
CDN	\$ 3.10	March 17, 2008	-	12,997,600	-	-	12,997,600
			15,875,143	13,747,600	2,068,807	846,336	26,707,600

The Company obtained approval on March 15, 2006 to issue 750,000 warrants with an exercise price of \$1.44 in consideration of the debenture renegotiation.

(f) Contributed Surplus

On June 30, 2006, the contributed surplus was as follows:

	<u>2006</u>
Balance - Beginning of period	\$ 6,226,110
Stock-based compensation expense for the year	1,018,056
Fair value of warrants issued on private placements	5,971,485
Fair value of warrants issued on share issuance	905,190
Transfer to share capital upon exercise of warrants	<u>(224,646)</u>
Balance - End of period	<u>\$13,896,195</u>

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
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8. CHANGES IN NON-CASH WORKING CAPITAL ITEMS

The following table summarizes the changes in non-cash working capital items:

	Three Months Ended June 30		Six Months Ended June 30	
	2006	2005	2006	2005
Net changes in non-cash working capital items:				
Accounts receivable	\$(221,775)	\$ 74,844	\$ (249,598)	\$ 64,803
Prepaid items	(134,215)	(14,602)	(125,350)	(14,601)
Accounts payable & accrued liabilities	385,754	(53,206)	419,043	(313,323)
	<u>\$ 29,764</u>	<u>\$ 7,036</u>	<u>\$ 44,095</u>	<u>\$ (263,121)</u>

9. SUPPLEMENTAL CASH FLOW INFORMATION

	Three Months Ended June 30		Six Months Ended June 30	
	2006	2005	2006	2005
Special warrants converted into common shares	\$ 38,127,515	\$ -	\$ 38,127,515	\$ -
Warrants issued as share issue expenses	\$ -	\$ 120,000	\$ 905,190	\$ 120,000
Acquisition of DHI Minerals Ltd.	\$ -	\$ 4,760,601	\$ -	\$ 4,760,601

10. RELATED PARTY TRANSACTIONS

During the period ended June 30, 2006, the Company incurred expenses of \$15,000 (2005 - \$15,000) for administrative services provided by a company in which a director of the Company has a 25% interest. During the period ended June 30, 2006, the Company incurred salaries and bonuses of \$227,500 (2005 - \$75,000) to the Chairman of the Company, \$299,800 (2005 - \$57,012) to the President and CEO of the Company, \$73,543 (2005 - \$32,065) to the Vice President Exploration and \$95,000 (2005 - \$37,500) to the CFO.

At June 30, 2006, \$1,467 of accounts payable (2005 - \$5,743 of accounts receivable) is due to a related company, which share office space and certain common directors with the Company. At June 30, 2006, \$150,000 of accounts payable (2005 - \$Nil) is due to the Chairman of the Company, \$170,000 of accounts payable (2005 - \$37,500) is due to the CFO of the Company for salaries and bonuses accrued in the current and prior year. Also, included in accounts receivable at June 30, 2006 is an amount of \$33,827 (2005 - \$75,950) due from a related company with common directors.

All related party transactions are recorded at the exchange value.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
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11. FINANCIAL INSTRUMENTS

The carrying values of cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities, notes, advances and convertible debenture as reflected in the balance sheet approximate their fair values. The company has no significant concentrations of credit risk.

12. COMMITMENTS

The Company entered into a lease agreement for office space in Denver, the term of the lease expires June 30, 2009. The future minimum lease payments are as follows:

Year	
2007	\$ 95,253
2008	96,180
2009	<u>48,322</u>
Total	<u>\$ 239,755</u>

13. SUBSEQUENT EVENTS

On August 2, 2006 the Company granted 365,000 stock options to officers and employees of the Company at an exercise price of \$1.78 per share for a period of five years expiring on August 2, 2011.

On August 10, 2006 the Company commenced trading on the Toronto Stock Exchange (“TSX”) under the symbol “AZC” and will no longer trade on the TSX Venture Exchange.

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Richard Warke ~ Vice President Corporate Development
Donald B. Clark ~ Chief Financial Officer
Mike Clarke ~ Vice President Exploration
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SHARES LISTED

Toronto Stock Exchange
Trading Symbol ~ AZC