



2005

ANNUAL REPORT

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## Directors' Letter to Shareholders

April 17, 2006

Dear Shareholders,

2005 was a very constructive year for Canasil. During the past year, we actively pursued the acquisition of new projects in Mexico, and initiated a systematic process to compile and evaluate the extensive database on the Brenda gold-copper project in British Columbia, Canada. The results from the implementation of both objectives have been very positive, and we have experienced a significant improvement in our share price and liquidity.

Our focus in Mexico was to aggressively pursue the acquisition of new exploration projects with potential for silver, gold, zinc and copper. With increasing metal prices there was strong competition from explorers for attractive exploration targets in Mexico, and it was important to act promptly and effectively to acquire prospective exploration projects. Establishing our wholly owned operating subsidiary, Minera Canasil S.A. de C.V. in Durango, Mexico, with experienced local technical and administrative staff under the direction of Erme Enriquez, provided us with the capability to identify and evaluate numerous project opportunities. As a result we were able to acquire a number of large, well located, exploration projects within the prolific mining districts in Durango, Sinaloa and Zacatecas States, all relatively close to our operating base in Durango.

The extensive portfolio of exploration projects we acquired in Mexico in 2005 and early 2006 cover over 19,000 hectares. They provide excellent exploration potential for silver, gold, zinc, copper and lead. The majority of the projects have been acquired through direct staking of the claim areas. As a result we have 100% title without the high property acquisition payments common in agreements for acquisition of projects from third parties in Mexico. The majority of our future investments can therefore be committed to exploration programs, maximizing the opportunities for adding value to our projects. All our projects have excellent road access and are in the proximity of infrastructure required for cost effective exploration, and if warranted later development of mining operations. They provide us with the opportunity to create significant added value through our planned exploration programs in Mexico.

In British Columbia, Canada, compilation and mapping of the Brenda gold-copper project data, including geology, geochemistry, ground and aerial geophysics, satellite imaging and over 8,000 metres of drilling in 58 drill holes, has confirmed a large porphyry gold-copper mineralizing system and indicated several significant untested target zones for further drilling. The excellent access and infrastructure at the Brenda project, located 25km northwest of the 300,000 oz gold per year Kemess mine, and the strong evidence of a large gold-copper mineralizing system in the project area make this a very attractive advanced exploration prospect. With the current high prices of gold and copper, this project now has the potential for creating significant future value.

We have also started recompilation of the data on the Vega copper-gold project in B.C., Canada. This is an earlier stage exploration project located in the Quesnel Trough geologic formation, neighbouring the Lorraine project operated by Eastfield Resources Ltd. and Lysander Minerals Corp., under option to Teck Corp. The local geology, regional geophysics and geochemistry, and a strong gold-copper geochemical signature in the project area indicate favourable prospects for future exploration for copper-gold mineralized systems at the Vega project.



## Directors' Letter to Shareholders April 17, 2006, (contd.)

As a result of the completion of the above initiatives during 2005, Canasil is now in a strong position with a significant portfolio of high potential mineral exploration projects in two very attractive jurisdictions. Our data compilation and review has established drill targets for the Brenda gold-copper project. Our objective in British Columbia for 2006 is to implement a drill program of 2,000 to 3,000 metres at the Brenda project to test the main targets. This will be done either through a joint venture agreement with a partner with strong technical and financial capabilities, or directly by Canasil depending on progress with our plans for funding our 2006 exploration programs. We also plan to review, and where warranted, advance the other exploration projects in B.C.

Our initial objective in Mexico for 2006 is to complete the geologic mapping and sampling of all of our new exploration projects in order to define drill targets. As a result we will have six drill ready exploration projects in Mexico. We plan to start drill programs at these projects, based on the completion of our financing plans, and on our review of target priorities for these projects. We have also received interest in joint venture cooperation for advancing exploration programs on the Mexican projects, which we will evaluate as part of our program. The potential for multiple drill programs in Mexico presents further opportunities for significant added value in our Mexican exploration projects during 2006.

During the fourth quarter of 2005 and first quarter of 2006, we have had a very active mapping and sampling program on the Mexican projects. These have consistently returned encouraging surface sampling results and defined drill targets on the Sandra gold-silver, La Esperanza silver-zinc-lead and Colibri zinc-silver-copper-lead projects. We plan to complete similar programs at the Los Azules copper-gold and Salamandra zinc-silver projects during the second quarter 2006.

During the first quarter of 2006 we have initiated an active investor relations program and exhibited at the Vancouver Resource Investment Conference, the Vancouver Mineral Exploration Roundup, and for the first time at the Prospectors and Developers Association of Canada convention in Toronto. The positive exploration results from Mexico, together with the potential at the Brenda gold-copper project in BC, have generated a very positive response. As a result we have experienced improving share prices and trading volumes during the first quarter of 2006, providing the opportunity to arrange funding for our future exploration programs with favourable terms and lower shareholder dilution, which is one of our important priorities.

The completion of additional exploration funding and potential for joint venture agreements leading to progress with our exploration projects, including drill programs on projects in B.C. and Mexico, will provide the Company with important opportunities for creating shareholder value during 2006. Your Company now offers significant exposure to exploration potential for gold, silver, copper, zinc and lead in Mexico and British Columbia, Canada, two politically and economically stable environments with proven mineral and mining potential. All these metals are currently trading at high historical price levels. We look forward to the implementation of, and results from our exploration programs during 2006, and their impact on our share prices and trading volumes.

We thank all our shareholders for their continued support,

On behalf of the Board,

*"Bahman Yamini"*

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Bahman Yamini, President, CEO & Director

**CANASIL RESOURCES INC.**

**CONSOLIDATED FINANCIAL STATEMENTS**

**DECEMBER 31, 2005**

## **AUDITORS' REPORT**

To the Shareholders of  
Canasil Resources Inc.

We have audited the consolidated balance sheets of Canasil Resources Inc. as at December 31, 2005 and 2004 and the consolidated statements of operations and deficit and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. 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 plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as, evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2005 and 2004 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

**“DAVIDSON & COMPANY LLP”**

Vancouver, Canada

Chartered Accountants

April 15, 2006

A Member of *SC INTERNATIONAL*

**CANASIL RESOURCES INC.**  
**CONSOLIDATED BALANCE SHEETS**  
**AS AT DECEMBER 31**

	2005	2004
<b>ASSETS</b>		
<b>Current</b>		
Cash	\$ 204,920	\$ 681,818
Receivables	59,698	30,058
Prepaid expenses	<u>4,347</u>	<u>191</u>
	268,965	712,067
<b>Equipment</b> (Note 3)	6,692	2,240
<b>Resource properties</b> (Note 4)	1,827,000	1,650,561
<b>Reclamation bond</b>	<u>13,000</u>	<u>13,000</u>
	<u>\$ 2,115,657</u>	<u>\$ 2,377,868</u>

**LIABILITIES AND STOCKHOLDERS' EQUITY**

<b>Current</b>		
Accounts payable and accrued liabilities	<u>\$ 44,917</u>	<u>\$ 21,947</u>
<b>Stockholders' equity</b>		
Capital stock (Note 5)	5,762,048	5,762,048
Contributed surplus (Note 5)	449,081	414,403
Deficit	<u>(4,140,389)</u>	<u>(3,820,530)</u>
	<u>2,070,740</u>	<u>2,355,921</u>
	<u>\$ 2,115,657</u>	<u>\$ 2,377,868</u>

**Nature and continuance of operations** (Note 1)

**Subsequent events** (Note 12)

**On behalf of the Board:**

"Bahman Yamini"

Director

"Alvin Jackson"

Director

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

**CANASIL RESOURCES INC.**  
**CONSOLIDATED STATEMENTS OF OPERATIONS AND DEFICIT**  
**YEAR ENDED DECEMBER 31**

	2005	2004
<b>EXPENSES</b>		
Accounting and audit	\$ 13,052	\$ 15,427
Amortization	992	524
Directors fees	18,000	15,000
Foreign exchange	16,806	4,124
General exploration	121,139	6,903
Investor relations	26,604	24,965
Legal fees	7,806	15,428
Management fees	60,000	60,000
Office services and supplies	12,558	10,347
Registration, licence and filing	8,086	9,575
Stock-based compensation (Note 6)	34,678	66,973
Stock transfer fees	3,325	5,826
Telephone	4,220	5,053
Travel and conferences	<u>2,577</u>	<u>3,852</u>
<b>Loss before other item</b>	<b>(329,843)</b>	<b>(243,997)</b>
<b>OTHER ITEM</b>		
Interest income	<u>9,984</u>	<u>21,619</u>
<b>Loss for the year</b>	<b>(319,859)</b>	<b>(222,378)</b>
<b>Deficit, beginning of year</b>	<u><b>(3,820,530)</b></u>	<u><b>(3,598,152)</b></u>
<b>Deficit, end of year</b>	<u><b>\$ (4,140,389)</b></u>	<u><b>\$ (3,820,530)</b></u>
<b>Basic and diluted loss per share</b>	<b>\$ (0.02)</b>	<b>\$ (0.01)</b>
<b>Weighted average number of shares outstanding</b>	<b>18,432,342</b>	<b>18,432,342</b>

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

**CANASIL RESOURCES INC.**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**YEAR ENDED DECEMBER 31**

	2005	2004
<b>CASH FLOWS USED IN OPERATING ACTIVITIES</b>		
Loss for the year	\$ (319,859)	\$ (222,378)
Items not affecting cash:		
Amortization	992	524
Stock-based compensation	34,678	66,973
Changes in non-cash working capital items:		
Increase in receivables	(29,640)	(25,478)
(Increase) decrease in prepaid expenses	(4,156)	233
Increase (decrease) in accounts payable and accrued liabilities	<u>3,648</u>	<u>(77,001)</u>
Net cash used in operating activities	<u>(314,337)</u>	<u>(257,127)</u>
<b>CASH FLOWS USED IN INVESTING ACTIVITIES</b>		
Resource property option payment received	-	5,000
Resource property costs and deferred exploration costs	(157,117)	(326,842)
Equipment	<u>(5,444)</u>	<u>(285)</u>
Net cash used in investing activities	<u>(162,561)</u>	<u>(322,127)</u>
<b>Decrease in cash during the year</b>	(476,898)	(579,254)
<b>Cash, beginning of year</b>	<u>681,818</u>	<u>1,261,072</u>
<b>Cash, end of year</b>	<u>\$ 204,920</u>	<u>\$ 681,818</u>

**Supplemental disclosure with respect to cash flows (Note 8)**

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

**CANASIL RESOURCES INC.**  
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS  
DECEMBER 31, 2005

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**1. NATURE AND CONTINUANCE OF OPERATIONS**

Canasil Resources Inc. (the "Company") is considered to be in the exploration stage with respect to its interest in resource properties. Based on the information available to date, the Company has not yet determined whether these properties contain economically recoverable ore reserves.

The recovery of the amounts comprising resource properties and deferred exploration costs is dependent upon the confirmation of economically recoverable reserves, the ability of the Company to obtain necessary financing to successfully complete its exploration and development and upon future profitable production.

These financial statements have been prepared on a going concern basis which assumes that the Company will be able to realize its assets and discharge its liabilities in the normal course of business for the foreseeable future. The financial statements do not include adjustments to amounts and classifications of assets and liabilities that might be necessary should the Company be unable to continue. The continuing operations of the Company are dependent upon its ability to continue to raise adequate financing and to commence profitable operations in the future.

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	2005	2004
Deficit	\$ (4,140,389)	\$ (3,820,530)
Working capital	224,048	690,120

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**2. SIGNIFICANT ACCOUNTING POLICIES**

**Principles of consolidation**

These consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles. These consolidated financial statements include the accounts of the Company and its wholly-owned subsidiary, Minera Canasil, S.A. de C.V., a company incorporated in Mexico on November 8, 2004. All significant intercompany transactions and balances have been eliminated.

**Use of estimates**

The preparation of financial statements in accordance with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amount of revenues and expenses during the year. Actual results could differ from these estimates.

**Equipment and amortization**

Equipment, being furniture and equipment, is recorded at cost and amortized over its estimated useful life using the declining balance method at 20% per annum.

**2. SIGNIFICANT ACCOUNTING POLICIES (cont'd...)**

**Resource properties**

All costs related to the acquisition, exploration and development of resource properties are capitalized by property. If economically recoverable ore reserves are developed, capitalized costs of the related property are reclassified as mining assets and amortized using the unit of production method. When a property is abandoned, all related costs are written off to operations. If, after management review, it is determined that the carrying amount of a resource property is impaired, that property is written down to its estimated net realizable value. A resource property is reviewed for impairment whenever events or changes in circumstances indicate that its carrying amount may not be recoverable.

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

From time to time, the Company may acquire or dispose of properties pursuant to the terms of option agreements. Due to the fact that options are exercisable entirely at the discretion of the optionee, the amounts payable or receivable are not recorded. Option payments are recorded as mineral property costs or recoveries when the payments are made or received.

**Asset retirement obligations**

Asset retirement obligations are legal obligations associated with the retirement of tangible long-lived assets that the Company is required to settle. The Company recognizes the fair value of liabilities for asset retirement obligations in the period in which they occur or in the period in which a reasonable estimate of such costs can be made. Liabilities include those liabilities related to environmental protection and rehabilitation due to environmental law or contracts. The asset retirement obligation is recorded as a liability with a corresponding increase to the carrying amount of the related long-lived asset.

**Foreign currency translation**

The Company's subsidiary is an integrated foreign operation and is translated into Canadian dollars using the temporal method. Monetary items are translated at the exchange rate in effect at the balance sheet date and non-monetary items are translated at historical exchange rates. Income and expense items are translated at rates approximating those in effect at the time of the transactions. Translation gains and losses are reflected in the statement of operations for the year.

**Future income taxes**

Future income taxes are recorded using the asset and liability method whereby future tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Future tax assets and liabilities are measured using the enacted or substantively enacted tax rates expected to apply when the asset is realized or the liability settled. The effect on future tax assets and liabilities of a change in tax rates is recognized in income in the year that substantive enactment or enactment occurs. To the extent that the Company does not consider it more likely than not that a future tax asset will be recovered, it provides a valuation allowance against the excess.

**2. SIGNIFICANT ACCOUNTING POLICIES (cont'd...)**

**Loss per share**

The Company uses the treasury stock method to compute the dilutive effect of options, warrants and similar instruments. Under this method the dilutive effect on loss per share is recognized on the use of the proceeds that could be obtained upon exercise of options, warrants and similar instruments. It assumes that the proceeds would be used to purchase common shares at the average market price during the year. Basic loss per share is calculated using the weighted-average number of shares outstanding during the year. Existing stock options and share purchase warrants have not been included in the computation of diluted loss per share because to do so would be anti-dilutive.

**Stock-based compensation**

The Company uses the fair value method whereby the Company recognizes compensation costs for the granting of all stock options and direct awards of stock. Any consideration paid by the option holders to purchase shares is credited to capital stock.

**Comparative figures**

Certain comparative figures have been reclassified to conform with the current year's presentation.

**3. EQUIPMENT**

	2005			2004		
	Cost	Accumulated Amortization	Net Book Value	Cost	Accumulated Amortization	Net Book Value
Furniture and equipment	\$ 14,971	\$ 8,279	\$ 6,692	\$ 9,527	\$ 7,287	\$ 2,240

**4. RESOURCE PROPERTIES**

Title to resource properties involves certain inherent risks due to the difficulties of determining the validity of certain claims as well as the potential for problems arising from the frequently ambiguous conveyancing history characteristic of many resource properties. The Company has investigated title to all of its resource properties and, to the best of its knowledge, title to all of its properties is in good standing.

**Brenda Claims, Canada**

The Company owns twenty-two mineral claims in North Central British Columbia.

**Lil Claim, Canada**

The Company owns two mineral claims in the Omineca Mining division of British Columbia.

**4. RESOURCE PROPERTIES (cont'd...)**

**Vega Claims, Canada**

The Company owns twelve mineral claims in the Omineca Mining division of British Columbia.

**Tres Marias and Cebollas properties, Mexico**

During fiscal 2003, the Company entered into an option agreement with Wheaton River Minerals Ltd. ("Wheaton") and its wholly-owned subsidiary Minas Luismin S.A. de C.V. to earn a 51% interest in the Tres Marias and Cebollas gold-silver properties located in Durango State, Mexico. In 2005 Wheaton merged with Goldcorp Inc.

In accordance with the terms of the agreement, the Company issued 50,000 common shares at a value of \$8,000 and must also incur exploration expenditures of US\$1,000,000 over five years. The Company's interest may be increased to 75% in the sixth year by incurring an additional US\$700,000 in exploration expenditures. Goldcorp Inc. may buy back a 35% interest in the properties for US\$1,700,000 after the Company has acquired a 75% interest. The property is subject to a 3% net smelter returns royalty ("NSR").

**Los Azules project, Mexico**

During fiscal 2005, the Company acquired, through staking, claims in Sinaloa State, Mexico.

**Sandra and Nora project, Mexico**

During fiscal 2005, the Company acquired, through staking, claims located in Durango State, Mexico.

**San Francisco project, Mexico**

During fiscal 2005, the Company acquired through staking, claims in Durango State, Mexico.

**La Esperanza project, Mexico**

During the current year, the Company entered into an option agreement to purchase a 100% interest in the La Esperanza project, subject to a Net Smelter Return royalty of up to 1.5%. The claims are located in Zacatecas State, Mexico. Under the terms of a subsequent definitive agreement, the Company has the right to acquire these claims by making option payments over a period of three years totaling \$174,000 (U.S.\$150,000).

**Colibri project, Mexico**

During fiscal 2005, the Company acquired through staking, claims located in Durango State, Mexico.

**Granite Claims, Canada**

The Company owns one mineral claim in the Omineca Mining division of British Columbia.

**CANASIL RESOURCES INC.**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2005**

**4. RESOURCE PROPERTIES (cont'd...)**

**Schedule of Deferred Exploration Expenses**

	Brenda Claims, Canada	Lil Claim, Canada	Vega Claims, Canada	Tres Marias and Cebollas, Mexico	Los Azules, Mexico	Sandra and Nora, Mexico	San Francisco, Mexico	La Esperanza, Mexico	Colibri, Mexico	Total
<b>Total - December 31, 2003</b>	\$ 1,301,652	\$ -	\$ -	\$ 27,067	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 1,328,719
Assays	-	-	-	9,773	-	-	-	-	-	9,773
Drilling	-	-	-	159,485	-	-	-	-	-	159,485
Geological and field costs	-	-	-	76,547	-	-	-	-	-	76,547
Land holding costs	-	-	-	54,477	-	-	-	-	-	54,477
Mapping and surveying	-	-	-	18,556	-	-	-	-	-	18,556
Transportation and rentals	-	-	-	8,004	-	-	-	-	-	8,004
Total expenditures	-	-	-	326,842	-	-	-	-	-	326,842
Cost recoveries	(5,000)	-	-	-	-	-	-	-	-	(5,000)
<b>Total - December 31, 2004</b>	1,296,652	-	-	353,909	-	-	-	-	-	1,650,561
Administration	25	-	-	544	-	126	126	-	-	821
Assays	-	-	-	1,852	207	3,929	-	2,120	-	8,108
Geological and field costs	4,196	-	-	37,893	6,484	28,971	697	13,036	11,134	102,411
Land holding costs	-	441	1,441	-	11,365	3,193	1,308	6,696	4,747	29,191
Mapping and surveying	12,832	-	-	4,857	22	-	-	-	-	17,711
Transportation and rentals	-	-	-	11,422	-	2,777	366	3,172	460	18,197
Total expenditures	17,053	441	1,441	56,568	18,078	38,996	2,497	25,024	16,341	176,439
<b>Total - December 31, 2005</b>	\$ 1,313,705	\$ 441	\$ 1,441	\$ 410,477	\$ 18,078	\$ 38,996	\$ 2,497	\$ 25,024	\$ 16,341	\$ 1,827,000

**CANASIL RESOURCES INC.**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2005**

**5. CAPITAL STOCK AND CONTRIBUTED SURPLUS**

	Number of Shares	Capital Stock	Contributed Surplus
Authorized			
Unlimited common voting shares, without par value			
Common shares issued			
Balance, December 31, 2003	18,432,342	\$ 5,762,048	\$ 347,430
Stock-based compensation	-	-	66,973
Balance, December 31, 2004	18,432,342	5,762,048	414,403
Stock-based compensation	-	-	34,678
Balance, December 31, 2005	18,432,342	\$ 5,762,048	\$ 449,081

**6. STOCK OPTIONS AND WARRANTS**

The Company has an Incentive Stock Option Plan (the "Plan") which complies with the rules set forth for such plans by the TSX Venture Exchange ("TSX-V") in that at no time may more than 5% of the outstanding issued common shares be reserved for incentive stock options granted to any one individual. The Plan provides for the issuance of options to directors, officers, employees and consultants of the Company and its subsidiary to purchase common shares of the Company. The stock options may be issued at the discretion of the Board of Directors and may be exercisable during a period not exceeding five years. Stock options granted under the Plan will vest in equal quarterly tranches over a period of not less than 18 months. At no time will more than 2,000,000 shares be under option pursuant to the Plan. The exercise price will not be lower than, the greater of, the market price of the shares on the TSX-V at the time of grant or \$0.10 per share.

At December 31, 2005, the Company had outstanding stock options, enabling holders to acquire common shares as follows:

Number of Shares	Exercise Price	Expiry Date
100,000	\$ 0.23	April 17, 2007
650,000	0.26	November 6, 2008
150,000	0.10	August 31, 2010

**CANASIL RESOURCES INC.**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2005**

**6. STOCK OPTIONS AND WARRANTS (cont'd...)**

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

	Warrants		Options	
	Number	Weighted Average Exercise Price	Number	Weighted Average Exercise Price
Balance, December 31, 2003	2,770,500	\$ 0.35	1,235,000	\$ 0.27
Cancelled/expired	(520,500)	0.35	(185,000)	0.41
Balance, December 31, 2004	2,250,000	0.35	1,050,000	0.27
Cancelled/expired	(2,250,000)	0.35	(300,000)	0.32
Granted	-	-	150,000	0.10
Balance, December 31, 2005	-	\$ -	900,000	\$ 0.23
Exercisable, December 31, 2005	-	\$ -	787,500	\$ 0.26

**Stock-based compensation**

During the current fiscal year, the Company granted incentive stock options to a consultant to acquire up to 150,000 common shares with a weighted fair value \$0.03 per share. One quarter of these options (37,500) vested during the current period resulting in stock-based compensation expense under the Black Scholes option pricing model of \$1,191 being recognized. During the 2003 fiscal year, the Company granted 650,000 stock options. Three-quarters of these options (487,500) vested in prior years and one-quarter (162,500) vested during the current year resulting in stock-based compensation expense under the Black-Scholes option-pricing model of \$33,487 (2004 - \$66,973) being recognized.

The following weighted average assumptions were used for the Black-Scholes valuation of stock options granted:

	2005
Risk-free interest rate	3.3%
Expected life of options	2 year
Annualized volatility	60%
Dividend rate	0.00%

**CANASIL RESOURCES INC.**  
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS  
DECEMBER 31, 2005

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**7. RELATED PARTY TRANSACTIONS**

The Company entered into the following transactions with related parties:

- a) Paid or accrued \$48,000 (2004 - \$48,000) for management fees to a company controlled by a director.
- b) Paid or accrued \$7,804 (2004 - \$14,895) for legal services to a law firm in which an officer of the Company is a partner.
- c) Paid or accrued \$18,000 (2004 - \$15,000) to a director and to two companies each controlled by a director for directors' fees.
- d) Paid or accrued \$Nil (2004 - \$7,500) for geological consulting fees to a director and a company controlled by a director.
- e) Paid or accrued \$14,638 (2004 - \$15,176) to a company controlled by an officer of the Company for accounting and management fees.

These transactions were in the normal course of operations and were measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties.

Included in accounts payable at December 31, 2005 is \$2,334 (2004 - \$7,369) due to directors or to companies controlled by directors and to a law firm in which an officer of the Company is a partner.

**8. SUPPLEMENTAL DISCLOSURE WITH RESPECT TO CASH FLOWS**

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	2005	2004
Cash paid during the year for interest	\$ -	\$ -
Cash paid during the year for income taxes	\$ -	\$ -

Significant non-cash transactions for the year ended December 31, 2005 consists of the Company accruing mineral property expenditures in accounts payable and accrued liabilities of \$19,322 at December 31, 2005.

There were no significant non-cash transactions for fiscal 2004.

**9. FINANCIAL INSTRUMENTS**

The Company's financial instruments consist of cash, receivables, a reclamation bond and accounts payable and accrued liabilities. Unless otherwise noted, it is management's opinion that the Company is not exposed to significant interest, currency or credit risks arising from these financial instruments. The fair value of these financial instruments approximates their carrying value, unless otherwise noted.

**CANASIL RESOURCES INC.**  
**NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS**  
**DECEMBER 31, 2005**

**10. INCOME TAXES**

A reconciliation of income taxes at statutory rates with the reported taxes is as follows:

	2005	2004
Loss for the year	\$ (319,859)	\$ (222,378)
Expected income tax (recovery)	\$ (105,805)	\$ (79,166)
Non-deductible expenses	47,616	18,387
Unrecognized benefit of non-capital losses	<u>58,189</u>	<u>60,779</u>
Actual income tax recovery	<u>\$ -</u>	<u>\$ -</u>

The significant components of the Company's future income tax assets are as follows:

	2005	2004
Future income tax assets:		
Non-capital loss carryforwards	\$ 203,501	\$ 168,470
Resource properties	752,080	738,779
Financing costs	11,310	17,702
Equipment	<u>10,818</u>	<u>10,874</u>
	977,709	935,825
Valuation allowance	<u>(977,709)</u>	<u>(935,825)</u>
Net future income tax assets	<u>\$ -</u>	<u>\$ -</u>

The Company has available for deduction against future taxable income non-capital losses of approximately \$596,500. These losses, if not utilized, will expire commencing in 2006. Subject to certain restrictions, the Company also has resource expenditures available of approximately \$4,031,000 to reduce taxable income in future years. Future tax benefits which may arise as a result of these non-capital losses, resource deductions and other tax assets have been offset by a valuation allowance and have not been recognized in these financial statements.

**CANASIL RESOURCES INC.**  
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS  
DECEMBER 31, 2005

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**11. SEGMENTED INFORMATION**

The Company's one reportable operating segment is the acquisition and exploration of resource properties. Geographic information is as follows:

The Company's assets are located in the following geographic locations:

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	2005	2004
Canada	\$ 1,521,328	\$ 2,021,684
Mexico	<u>594,329</u>	<u>356,184</u>
	<u>\$ 2,115,657</u>	<u>\$ 2,377,868</u>

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**12. SUBSEQUENT EVENTS**

Subsequent to December 31, 2005, the Company:

- a) Granted 800,000 incentive stock options exercisable at \$0.20 per share over five years.
- b) Signed a letter of intent to enter into an option agreement, subject to regulatory approval, to purchase a 100% interest in the Salamandra project, subject to a Net Smelter Return royalty of 2%. Under the terms of the proposed agreement, the Company has the right to acquire these claims by making option payments over a period of three years totaling \$552,000 (U.S.\$475,000).

This Management's Discussion and Analysis (MD&A) for Canasil Resources Inc. ("the Company") is dated April 17, 2006 and provides information on the Company's activities for the year ended December 31, 2005 and from the end of the 2005 fiscal year to the date of this report. The following discussion and analysis of the financial position of the Company should be read in conjunction with the audited financial statements and related notes for the year ended December 31, 2005.

### **Business of the Company**

The Company was incorporated in 1984 and is engaged in the exploration and development of mineral properties hosting copper-gold, gold, silver, zinc and lead prospects located in Durango, Sinaloa and Zacatecas States, Mexico, and in British Columbia, Canada. During 2005, the company actively pursued the acquisition of new projects in Mexico, and initiated a systematic process to compile and evaluate the extensive database on the Brenda gold-copper project in B.C., Canada. The results from the implementation of both objectives have been very positive.

### **Overall Performance**

The Company's focus in Mexico is to aggressively pursue the acquisition of new exploration projects with potential for silver, gold, zinc and copper deposits. With increasing metal prices there is strong competition from explorers for attractive exploration targets in Mexico, and it is important to act promptly and effectively to acquire prospective exploration projects. Our wholly-owned operating subsidiary, Minera Canasil S.A. de C.V. in Durango, Mexico, was strengthened with experienced local technical and administrative staff, providing the capability to identify and evaluate numerous project opportunities. As a result we were able to acquire a number of large, well-located, exploration projects within the prolific mining districts in Durango, Sinaloa and Zacatecas States, all relatively close to our operating base in Durango. General exploration expenditures for the project evaluation and acquisition program in Mexico during 2005 were \$121,139 (2004 - \$6,903).

The extensive portfolio of exploration projects we acquired in Mexico in 2005 cover over 19,000 hectares. They provide excellent exploration potential for silver, gold, zinc, copper and lead. The majority of the projects have been acquired through direct staking of the claim areas. As a result we have 100% title without the high property acquisition payments common in agreements for acquisition of projects from third parties in Mexico. The majority of our future expenditures can therefore be committed to exploration programs, maximizing the opportunities for adding value to our projects. All our projects have excellent road access and are in the proximity of infrastructure required for cost effective exploration, and if warranted later, development of mining operations. These projects provide us with the opportunity to create significant added value through our planned exploration programs in Mexico.

During the fourth quarter of 2005, the Company completed the geologic mapping and surface sampling programs at the Sandra and La Esperanza projects. These programs consistently returned encouraging surface sampling results and defined drill targets on the Sandra gold-silver and the La Esperanza silver-zinc-lead projects. The exploration program has been continued in 2006 with the Colibri zinc-silver-copper-lead project, and we plan to complete similar programs at the Los Azules copper-gold and Salamandra zinc-silver projects during the second quarter of 2006. Deferred exploration expenditures on the Mexican projects in 2005 were \$157,504.

In October 2003, the Company signed option and joint venture agreements with Wheaton River Minerals ("Wheaton River"), now Goldcorp Inc. ("Goldcorp") and Luismin S.A. de C.V. ("Luismin") to acquire up to a 75% interest in the Tres Marias and Cebollas silver-gold properties in Durango State, Mexico. The Company completed an initial diamond drill and evaluation program on these projects between November 2004 and January 2005 for a total of 8 drill holes for 1,219 metres with 2005 expenditures of \$56,568 (2004 - \$326,842). The drill program returned mixed results with some excellent high-grade silver-gold intercepts in upper zone at the Cebollas project. However the lower intercepts at Cebollas did not return similarly high-grade intercepts, and drilling at Tres Marias was not conclusive due to difficulties with positioning drill pads close enough to the mineralized structure. There is potential for further drilling at Tres Marias and Cebollas to further investigate the silver-gold vein system. The Company's obligations under the agreements with Goldcorp and Luismin have been fulfilled to October 2006.

In British Columbia, Canada, the Company undertook a program to compile and incorporate the Brenda gold-copper project data, including geology, geochemistry, ground and aerial geophysics, satellite imaging and over 8,000 metres of drilling in 58 drill holes, in a comprehensive geologic information system. This now allows us to generate layered compilation maps with the various data elements for review and analysis of exploration targets. This program has indicated several large untested target zones for further drilling. Total 2005 expenditures on the Brenda project were \$17,053 (2004 - Nil). The excellent access and infrastructure at the Brenda project, located 25km northwest of the 300,000 oz gold per year Kemess mine, and the strong evidence of a large gold-copper mineralizing system in the project area make this a very attractive advanced exploration prospect. With the current high prices of gold and copper, this project now has the potential for creating significant future value. The Company holds 100% interest in the Brenda project with all claims in good standing to May 31, 2015.

We have also started recompilation of the data on the Vega copper-gold project in B.C., Canada. This is an earlier stage exploration project located in the Quesnel Trough geologic formation, and neighbouring the Lorraine project of Eastfield Resources Ltd. and Lysander Minerals Corp., which is under option to Teck Corp. The local geology, regional geophysics and geochemistry, and a strong gold-copper geochemical signature in the project area indicate favourable prospects for future exploration for copper-gold mineralized structures at the Vega project. All other mineral claims in British Columbia were maintained in good standing.

The Company exhibited at the Vancouver Resource Investment Conference and Vancouver Mineral Exploration Roundup in January 2005. Investor relations expenditures in 2005 were \$26,604 (2004 – \$24,965)

#### **Financial Condition, Results of Operations and Cash Flows**

The Company's working capital as at December 31, 2005, was \$224,048 (2004 - \$690,120). The Company has sufficient working capital to meet current operating requirements and planned expenditures for exploration and maintenance of its mineral property interests for the first half of 2006. The Company will require additional funding for continued exploration programs and for working capital thereafter. Operating expenditures in 2005 were \$329,843 (2004 - \$243,997) and the Company earned interest income of \$9,984 (2004 - \$21,619). The operating expenditures for 2005 include general exploration expenses of \$121,139 (2004: \$6,903) and non-cash stock-based compensation of \$34,678 (2004 - \$66,973) for 200,000 stock options that vested during the year. Net cash used for operating activities increased to \$314,337 (2004 - \$257,127). This increase was primarily due to the increase to general exploration expenses that were incurred in the identification of prospective property acquisitions. Cash used for deferred exploration expenditures and acquisition costs on resource properties during the year was \$157,117 (2004 – \$326,842). These costs were incurred primarily for the acquisition and exploration of new projects in Mexico (\$100,936), evaluation of the Tres Marias and Cebollas project (\$56,568), and for data compilation for the Brenda project (\$17,053). There was no cash flow from financing activities in 2005 or 2004.

#### ***Mineral Properties***

The Company acquired the following mineral exploration projects in Mexico during 2005 and to the date of this report:

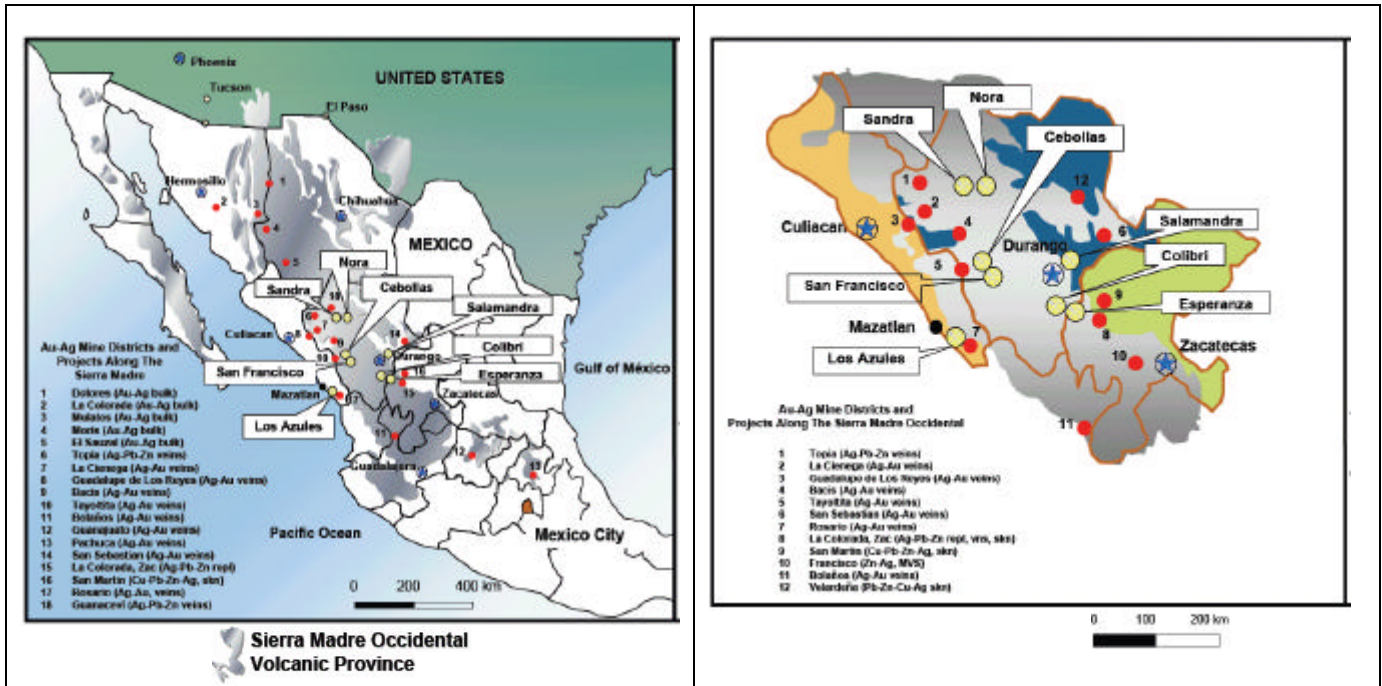
- Sandra and Nora gold-silver project – 100%
- San Francisco gold-silver project – 100%
- Los Azules copper gold project – 100%
- La Esperanza silver zinc lead project – option to earn 100%
- Colibri silver zinc lead copper project – 100%
- Salamandra zinc silver project (March 2006) – option to earn 100%

Under option and joint venture agreements signed in 2003 with Goldcorp and Luismin, the Company holds an option to earn up to a 75% interest in the Tres Marias and Cebollas silver-gold properties in the San Dimas District, Durango State, Mexico.

The Company holds 100% interest in the following mineral properties located in the Omineca Mining District, in North-central British Columbia, Canada:

- Brenda, gold-copper property
- Vega, gold-copper property
- Granite, gold property
- LIL, silver property

**Exploration projects in Mexico**



**Tres Marias and Cebollas silver-gold properties, Durango State, Mexico**

The Tres Marias and Cebollas properties, covering 3,163 hectares, are located 150 km west of the city of Durango and 14 km southeast of Luismin's San Dimas/Tayoltita mine.

In October 2003, the Company signed option and joint venture agreements with Wheaton River now Goldcorp and Luismin to acquire up to a 75% interest in these projects. Canasil can earn an initial 51% interest in the properties by issuing 50,000 shares to Wheaton River/Luismin and incurring US\$1,000,000 in exploration expenditures over five years. Canasil's interest may be increased to 75% in the sixth year by incurring a further US\$700,000 in exploration expenditures. Wheaton River/Luismin retains an option to buy back a 35% interest in the properties for US\$1,700,000 after Canasil has acquired a 75% interest.

Underground sampling was carried out in 2004 to investigate the Tahuehueto, Rosario and Los Laureles vein systems on the project area. This sampling returned significant high grade gold and silver assays with grades of up to 2,300 g/t silver and 30.3 g/t gold observed. A diamond drill program of 8 drill holes for a total of 1,219 metres was completed between November 2004 and January 2005. Total deferred acquisition and exploration expenditures on these projects during 2005 were \$56,568 (2004 \$326,842), as detailed in Schedule of Consolidated Deferred Exploration Expenses included with the audited financial statements for the fiscal year ended December 31, 2005.

Drill hole TAH-1 at the Tahuehueto vein returned assays of 329 g/t silver and 6.28 g/t gold over 2.14 metres above the underground workings. Drill holes TAH-2, TAH-3 and TAH-4 below the workings returned low silver and gold values. Drill hole ROS-1 returned assays of 120 g/t silver and 0.97 g/t gold over 2.05 metres, and 76 g/t silver and 0.94 g/t gold over 1.40 metres. Drill holes LAU-1 (177.15 metres) and LAU-2 (210.95 metres) did not intersect the vein structure due to the difficult access for a drill set-up close enough to the workings, although they did intersect quartz veins and breccias with widths from 0.50 to 4.08 metres with anomalous gold and silver values, indicating that the mineralized structure found in the 'main level' workings extends beyond a depth of 140 metres. Both the Tahuehueto-Rosario and Los Laureles structures require further evaluation and drill testing along strike and at depth. The Company plans to evaluate additional drill programs depending on the availability of funding and priorities based on the results from the other exploration projects.

**CANASIL RESOURCES INC.**  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
For the Year ended December 31, 2005

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*Sandra and Nora silver-gold project, Durango State, Mexico*

The Sandra project covers 1,200 hectares, located 183 km northeast of the city of Durango in Durango State, Mexico, and benefits from excellent infrastructure and access. The Company has 100% title to the Sandra claims, which were acquired by staking and are located immediately south of a large claim group controlled by Pan American Silver Corp. The initial surface sampling and geological mapping program during the third quarter 2005 identified a number of mineralized veins over an area of approximately 2,000 x 750 metres in the central area of the Sandra claims. Rock and chip samples from these veins returned encouraging grades of up to 9.74 g/t gold, 635 g/t silver, 2.46% copper and 20.06% lead as announced on November 2, 2005.

Subsequent trench sampling during the first quarter of 2006 confirmed silver and gold mineralization observed in earlier surface samples from the Barite, Maria Fernanda, and Encino veins. Assay results returned silver grades of up to 888 g/t (25.9 oz/t) silver over 0.7 metres at the Barite vein, and up to 9.95 g/t (0.29 oz/t) gold and 365 g/t (10.65 oz/t) silver over 0.5 metres at the Maria Fernanda vein, where trench samples indicate consistent silver/gold mineralization over a strike length of approximately 300 metres. These results now confirm and define targets for drilling at the Sandra project in order to explore extensions of these veins along strike and at depth. The silver and gold grades observed in samples taken across the entire width of the mineralized structures are encouraging because they confirm the high grades seen in the earlier surface sampling program. A diamond drill program is now warranted to test these vein systems at depth. 2005 expenditures on the Sandra and Nora project were \$38,996.

*La Esperanza silver-zinc-lead project, Zacatecas State, Mexico*

During the year, the Company entered into an option agreement to purchase a 100% interest in the La Esperanza project, subject to a Net Smelter Return royalty of up to 1.5%. Under the terms of the agreement, the Company has the right to acquire these claims by making option payments over a period of three years totalling \$174,000 (U.S.\$150,000).

The La Esperanza project, covering 335 hectares, is located 100 km SSE of the city of Durango in Zacatecas State on the border with Durango State. The project site is easily accessible from Canasil's operating base in Durango and the area is well served with power lines, water access and services for supporting exploration and mining operations. The project is also close to a number of prominent silver mines – San Martin mine operated by Grupo Mexico, the La Colorada mine of Pan American Silver and La Parrilla mine of First Majestic Resource Corp.

The mineralization observed at La Esperanza occurs in a principal low sulphidation vein, which can be traced for a distance of approximately 300 metres, striking N50°W and dipping at 65°-75°. The mineralization consists of galena, argentiferous galena, silver sulphides and sphalerite, contained in grey and white crystalline quartz. There are a number of small dumps with ore left over from past mining operations around the vein and mine area. During an initial geologic mapping and sampling program, undertaken in November 2005, 38 samples were taken from dumps close to the vein and from surface pits over the vein. The highest grades observed in these samples were 1,820 g/t silver, 10.05% lead and 8.66% zinc. 31 samples returned assays with over 100 g/t silver, with an average grade of 413 g/t silver, 2.17% lead and 3.08% zinc. The La Esperanza vein occurs within rhyolitic volcanics of the Upper Volcanic Series. Mapping shows andesitic volcanics of the Lower Volcanic Series outcrop lower in elevation and to the south of the La Esperanza Vein. There is good potential to outline mineralization, or additional blind mineralized vein structures, at depth within the lower volcanic sequence, which is the main host rock for this type of mineralization. A diamond drill program is now warranted to test for mineralized structures below the old mine workings. 2005 expenditures on the La Esperanza project were \$25,024.

*Colibri gold-silver-zinc-copper-lead project, Durango State, Mexico*

The Company acquired the Colibri claims, covering a total of 6,413 hectares, through direct staking of the claim blocks, giving the Company 100% title. The Colibri district covered by the claims is on the eastern border of Sierra Madre Occidental volcanic province, and hosts a number of prospects with epithermal-mesothermal vein type mineralization carrying gold, silver, lead, zinc and copper. The project site is located 70 km southeast of the city of Durango with a travel time of approximately 1:30 hours. The infrastructure at the property is excellent with access to power, water and all required services.

The geology of the area consists of Lower Volcanic Group Eocene andesites and scarce intercalated rhyolites. These units are overlain by Upper Volcanic Group Oligocene rhyolitic tuffs and ignimbrites. The Lower Volcanic Group formations are intruded by grandiorites and diorites. A number of mineralized structures are observed in the project area, occurring in epithermal to mesothermal fault controlled veins with silver sulphides, and lead and zinc minerals. Historical records indicate samples from these structures carried significant silver, lead and zinc values with gold credits. Observations during the initial project evaluation visits also indicate the possibility for disseminated silver mineralization. There has been no recent systematic exploration in the project area. The Company started a geologic mapping and surface sampling program in March 2006. Initial results have outlined a broad, banded, mineralized structure with a strike length of over 400 metres and widths up to 30 – 50 metres. Specific zones within this structure returned high silver, zinc, copper and lead values. The sampling program is continuing and will lead to definition of drill targets for further exploration. 2005 expenditures on the Colibri claims were \$16,341.

**CANASIL RESOURCES INC.**  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
For the Year ended December 31, 2005

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*Los Azules gold-silver-copper project, Sinaloa State, Mexico*

The Company acquired a 100% interest in the Los Azules claims in Sinaloa State, Mexico, covering 7,844 hectares, by direct staking between May and August 2005. The claims host prospects for epithermal low sulphidation vein type mineralization carrying gold, silver and copper.

The Los Azules property is located 60 km southeast of the city of Mazatlan. The infrastructure at the property is excellent with the new Mazatlan-Escuinapa highway providing direct and easy access to the City and port facilities of Mazatlan. Power and water are available throughout the district. The mineralization consists of epithermal low sulphidation veins with gold, silver and copper mineralization, hosted by volcanic and intrusive rocks of Tertiary age. The area has shown possibilities for the occurrence of Tourmaline-gold breccias, similar to the mineralization at Los Brasiles, located 15 km northeast of the property. An initial exploratory trench used to strip overburden and evaluate the structure of mineralization on the property identified a mineralized vein over a distance of 40 metres, with a width of approximately 2.40 metres. The alteration zone surrounding the vein covers a distance of approximately 25 metres. Intrusive rocks with quartz stockwork are observed in this alteration zone.

18 samples collected to evaluate and define the boundaries of the claims returned encouraging results in gold, silver and copper, with grades up to 2.71 g/t gold, 60 g/t silver and 4.49% copper observed in various samples with widths of 1.0 – 1.5 metres. The Los Azules project is a significant acquisition covering a large prospective area with potential for the occurrence of gold-silver-copper mineralization. It is extremely well located offering opportunities for cost effective exploration, and if warranted further development, as well as low acquisition and maintenance costs. The Company will be conducting the initial phase of geologic evaluation and sampling to define drill targets and determine the potential for this project. 2005 expenditures on the Los Azules claims were \$18,078.

*Salamandra zinc-silver project, Durango State, Mexico*

Subsequent to the end of the year, the Company signed a letter of intent to enter into an option agreement to purchase a 100% interest in the Salamandra project, subject to a Net Smelter Return royalty of 2%. Under the terms of the proposed agreement, the Company has the right to acquire these claims by making option payments over a period of three years totalling \$552,000 (U.S.\$475,000).

The Salamandra silver-zinc project, covering 900 hectares in Durango State, is located 35 km NE of the city of Durango in the El Guadiana valley in Durango State, with good access from Durango via paved and gravel roads. The Company has acquired a further 2,000 hectares by staking ground surrounding the existing claims, making the total claim area covered by the project 2,900 hectares. The access, infrastructure, climate and topography at Salamandra provide favourable conditions for exploration and development.

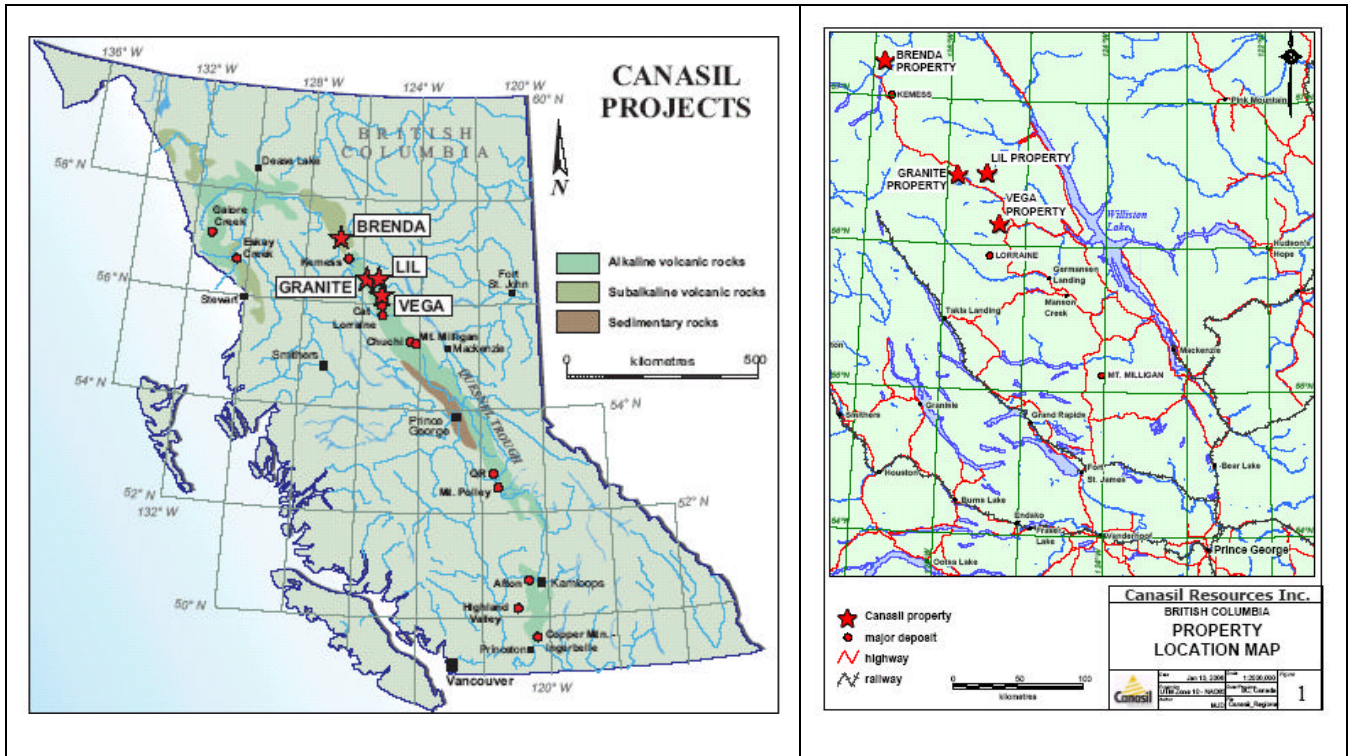
The geological setting and mineralization at Salamandra is similar to the San Martin Mine of Grupo Mexico, located approximately 80 kilometres to the southeast. The San Martin Mine is the largest underground zinc-copper-silver mine in Mexico and currently operates at 5,600 tonnes per day. Chip and grab samples at the Salamandra project contain encouraging grades of zinc and silver mineralization, grading up to 7.84% zinc and 25g/t silver over 3.2 metres. The mineralization is associated with fault and fracture replacement zones within a thin band of argillically altered and silicified siltstones and interbedded limestones along the southern contact of a rhyolite porphyry intrusive. The principal mineralized target area at the Salamandra project is a flat covered area to the south of the mineralized sediment outcrops covered by shallow gravel and basalt. A program of geological mapping and soil geochemical sampling is planned, followed by an induced polarization-resistivity survey to define targets for drilling.

*San Francisco gold-silver project, Durango, Mexico*

The San Francisco property, covering 500 hectares, is located approximately 104 km West of the city of Durango, and approximately 12 km south of the Company's Tres Marias and Cebollas silver-gold projects, located 14 km southeast of the Tayoltita mine in the San Dimas mining district of Durango. The claims are within view of the community of San Francisco. The access road cuts through the centre of the property, as does the main power line supplying the Tayoltita mine.

Mineralization observed on the San Francisco property consists of epithermal low sulphidation quartz veins hosted by volcanic rocks of the Upper Volcanic Group. Veins observed at surface over a strike length of over 400 metres range between 4 metres to 20 metres in width. Surface samples returned high values of Mercury (between 1,000 ppb to 7,000 ppb) indicating the higher levels of a potential epithermal mineralized system. The project will require a program of geologic mapping and surface sampling to identify and establish drill targets over the wide structure observed. 2005 expenditures on the San Francisco claims were \$2,497.

**Exploration projects in British Columbia, Canada**



*Brenda gold-copper property, British Columbia, Canada*

The Company holds 100% interest in the Brenda property which consists of 178 claim units, covering 4,450 hectares (44.5 square kilometres), is located in the core of the Kemsess-Toodoggone porphyry copper-gold district in the Omineca Mining Division, approximately 450 kilometres northwest of Prince George, B.C. All claims are currently in good standing to May 30, 2015.

The Brenda property is an advanced gold-copper exploration project located centrally in the highly prospective Kemsess-Toodoggone district. There has been over \$3,000,000 in cumulative exploration expenditures on the property, covering geologic mapping, geochemistry, ground and aerial geophysics, satellite imaging and over 8,000 metres of drilling in 58 drill holes. In 2005 the Company undertook a program to compile and incorporate the Brenda gold-copper project data into a comprehensive geologic information system. This now allows us to generate layered compilation maps with the various data elements for review and analysis of exploration targets.

This program has indicated several large untested target zones for further drilling. Total 2005 expenditures on the Brenda project were \$17,053. The excellent access and infrastructure at the Brenda project, located 25km northwest of the 300,000 oz gold per year Kemsess mine, and the strong evidence of a large gold-copper mineralizing system in the project area make this a very attractive advanced exploration prospect. With the current high prices of gold and copper, this project now has the potential for creating significant future value. The Company's objective for the Brenda project for 2006 is to implement a drill program of 2,000 to 3,000 metres to test the main targets. The drill program will be carried out either through a joint venture agreement with a partner with strong technical and financial capabilities, or directly by Canasil depending upon plans for funding the 2006 exploration programs.

**CANASIL RESOURCES INC.**  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
For the Year ended December 31, 2005

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*Vega gold/copper property, British Columbia, Canada*

The 100% owned Vega claims are located in the Omineca Mining Division of British Columbia, 300 km northwest of Prince George. Access to the property is via the Omineca Mines Access Road and logging roads. The claim area was increased by staking in August, 2005 to cover 5,154 Hectares. The project now covers a large area located in the Quesnel Trough geologic formation, neighbouring the Lorraine project operated by Eastfield Resources Ltd. and Lysander Minerals Corp., and under option to Teck Corp. The local geology, regional geophysics and geochemistry, and a strong gold-copper geochemical signature in the project area indicate favourable prospects for mineralized systems hosting large copper-gold porphyry deposits. The Company has started recompilation of the data on the Vega project to determine the program for further exploration covering geologic mapping, sampling and geophysics to define drill targets.

*LIL property, British Columbia, Canada*

The 100% owned LIL claims, covering 873 hectares, are located in the Omineca Mining Division, 350 kilometres northwest of Prince George, British Columbia. Logging roads provide four-wheel drive access to within 2km of the property. Mineralization on the property consists of narrow high-grade, silver bearing quartz veins and breccia zones, which have been identified over a distance of 300 metres, with grades ranging from 4.3 ounces/ton to 325.54 ounces/ton silver over 0.20 to 0.90 meters. Large silver bearing floats, found downstream in LIL Creek, indicate a possibility of wider mineralized veins on the property.

Tests carried out by BC Research Inc., Vancouver, in September 2001 on a sample of silver ore from the LIL property concluded that the composite sample contained a very high silver grade of over 100 oz/ton and that high rates of recovery (94% - 98%) were readily obtained through flotation using a very simple processing flow sheet. Potential contaminants such as mercury, cadmium and selenium were well below problem levels. There was no active exploration on the Lil property during 2005. The Company is undertaking a review to determine future exploration programs at the LIL project.

*Granite property, British Columbia, Canada*

The 100% owned Granite gold-silver claim, covering 500 hectares in the Johansson Lake area, Omineca Mining Division of British Columbia, is located 360 km northwest of Prince George. The Omineca Resource Access Road and auxiliary roads provide four-wheel drive access to the property.

Historical exploration records reported encouraging assays from trenches with grades of up to 10.3 g/t gold across 10 meters and sampling in the old underground workings with a grade of 6.86 g/t gold over 12.2 meters including 14.4 g/t gold over 3.0 meters. Three mineralized shear zones with gold/silver mineralization have been identified to date on the property, with rock samples ranging in grade from 1.99 g/t to 43.88 g/t gold and 9.94 g/t to 546.77 g/t silver. Soil and rock geochemistry completed in 1994 outlined a broad 300 metres by 2.0 kilometres gold soil anomaly.

In 1995 Hemlo Gold Mines Inc reported trench sample assays averaging 6.8 g/t gold over 7.5 meters and drill hole 95-2 (88.4 meters) intersected 9.1 meters of mineralization averaging 3.36 g/t gold and 11.7 g/t silver, of which 3.1 meters showed values of 8.9 g/t gold and 28.4 g/t silver. In 1996 further trenching and channel sampling returned average gold and silver values between 1.82 g/t to 9.44 g/t gold and 19.87 g/t to 43.10 g/t silver over widths of 3.0 to 11.0 meters. A diamond drill program of 500 metres completed by Canasil in 1997 intersected several sections with anomalous gold and silver values, however failed to locate sections corresponding in grade to the many samples recovered from these zones. There was no active exploration on the Granite property in 2005. The project is being reviewed to determine future exploration potential.

A discussion of general conditions, trends, and competitive and environmental factors affecting the Company's business and operations is included following the financial and other information.



During the fourth quarter, the Company incurred general exploration expenditures of \$23,954 compared with \$807 for the same period in 2004. In addition, the Company incurred deferred exploration expenditures of \$43,566 compared with no expenditures in 2004. The increases reflects the Company's level of activity in 2005 compared with the prior year. No stock-based compensation was recorded in the fourth quarter 2005 compared with the \$33,487 that was recorded for the fourth quarter of 2004.

### **Liquidity and Capital Resources**

The Company has sufficient financial resources to undertake currently planned exploration programs and operating expenditures during the first two quarters of 2006. Future exploration and subsequent development of the Company's properties beyond planned expenditures will depend on the Company's ability to obtain additional financing. The Company has limited financial resources and there is no assurance that additional funding will be available to allow the Company to fulfil its obligations on existing exploration (or joint venture) properties. Failure to obtain financing could result in the delay or indefinite postponement of further exploration and the possible partial or total loss of interest in certain properties.

The Company is dependent on raising funds by the issuance of shares or disposing of interests in its mineral properties (by options, joint ventures or outright sale) in order to finance further acquisitions, undertake exploration and development of mineral properties and meet general and administrative expenses in the immediate and long term. There can be no assurance that the Company will be successful in securing the required financing.

The Company had working capital at December 31, 2005 of \$224,048 (2004 - \$690,120). The Company had no material income from operations and the improvement in working capital results from the issuance of share capital.

As at December 31, 2005, the Company had no long-term debt.

For the year ended December 31, 2005, the Company experienced negative cash flow of \$476,898 (2004 - \$579,254) from operating, investing and financing activities. This was comprised of cash used in operating activities of \$314,337 (2004 - \$257,127) and net cash used in investing activities of \$162,561 (2004 - \$322,127).

2,250,000 share purchase warrants, each entitling the holders to purchase one common share of the Company at \$0.35 by June 30, 2005, expired unexercised during the year.

### **Other Information and Disclosures**

#### ***Related Party Transactions***

During 2005 the Company paid or accrued a total of \$88,442 (2004 - \$100,571) to related parties covering Directors' and management fees and geological and legal services. In addition the Company recorded stock based compensation expense amounting to \$33,491 (2004 - \$66,974) with respect to the vesting in 2005 of 162,500 stock options that were granted to directors and officers of the Company in the 2003 fiscal year. One quarter of these options (162,500) vested during 2003, and one half (325,000) vested during 2004.

#### ***Off-Balance Sheet Arrangements***

The Company does not have any off-balance sheet arrangements and does not contemplate such arrangements in the foreseeable future. There are no contingent liabilities.

#### ***Critical Accounting Estimates***

The preparation of financial statements in accordance with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amount of assets and liabilities, the disclosure of commitments and contingencies at the date of the financial statements, and the reported amount of revenue and expenses during the period. The most significant accounting estimates for the Company relate to the carrying value of its mineral property assets and accounting for stock-based compensation. The Company's accounting policies are set out in full in note 2 to the consolidated audited financial statements.

**CANASIL RESOURCES INC.**  
MANAGEMENT'S DISCUSSION AND ANALYSIS  
For the Year ended December 31, 2005

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*Mineral Property Costs*

The Company is in the exploration stage and defers all expenditures related to its mineral properties until such time as the properties are put into commercial production, sold or abandoned. Under this method, all amounts shown as mineral properties represent costs incurred to date less amounts amortized and/or written off and do not necessarily represent present or future values.

If the properties are put into commercial production, the expenditures will be depleted based upon the proven reserves available. If the properties are sold or abandoned, the expenditures will be charged to operations. The Company does not accrue the estimated future costs of maintaining in good standing its mineral properties.

In the event that reserves are determined, the carrying values of mineral interests, on a property-by-property basis, will be reviewed by management at least annually to determine if they have become impaired. If impairment is deemed to exist, the mineral property will be written down to its net recoverable value. The ultimate recoverability of the amounts capitalized for the mineral properties is dependent upon the delineation of economically recoverable ore reserves, the Company's ability to obtain the necessary financing to complete their development and realize profitable production or proceeds from the disposition thereof. Management's estimates of recoverability of the Company's investment in various projects have been based on current conditions. However, it is reasonably possible that changes could occur in the near term which could adversely affect management's estimates and may result in future write-downs of capitalized property carrying values.

From time to time, the Company may acquire or dispose of properties pursuant to the terms of option agreements. Due to the fact that options are exercisable entirely at the discretion of the optionee, the amounts payable or receivable are not recorded. Option payments are recorded as mineral property costs or recoveries when the payments are made or received.

*Stock-based Compensation*

The fair value of stock options is determined by the Black-Scholes option pricing model, which require the input of highly subjective assumptions, including the expected price volatility of the Company's common shares and the expected life of the options. Changes in the subjective input assumptions can materially affect the fair value estimate, and therefore, the model does not necessarily provide a reliable single measure of the fair value of the Company's stock options granted/vested during the year.

**New Accounting Pronouncements**

*Variable Interest Entities*

The CICA has issued Accounting Guideline 15, "Consolidation of Variable Interest Entities", which became effective for annual and interim periods beginning on or after November 1, 2004. This guideline addresses the application of consolidation principles to entities that are subject to control on a basis other than ownership of voting interests. The Company adopted the guideline on January 1, 2005. The adoption of this guideline did not have any impact on the Company's consolidated financial statements.

**Financial Instruments**

The Company's financial instruments consist of cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities. It is management's opinion that the Company is not exposed to significant interest, currency or credit risks arising from its cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities. The fair value of these financial instruments approximates their carrying value due to their short-term maturity.

**Outstanding Share Data as at April 17, 2006**

(a) Authorized and issued shares as at December 31, 2004 are as follows:

<u>Class</u>	<u>Par Value</u>	<u>Authorized</u>	<u>Issued</u>	<u>Amount</u>
Common	Without par value	100,000,000	18,432,342	\$5,762,048

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- (b) As at April 17, 2006, a total of 1,700,000 incentive stock options were outstanding of which 987,500 incentive stock options were exercisable.

Number of Shares	Exercise Price	Expiry Date
100,000	0.23	April 17, 2007
650,000	0.26	November 6, 2008
150,000	0.10	August 31, 2010
800,000	0.20	March 15, 2011
1,700,000		

- (c) No shares are subject to escrow or pooling arrangements.

### ***Investor Relations***

The Company maintains a website, [www.canasil.com](http://www.canasil.com), with detailed corporate information and information covering its mineral exploration projects and operations. For 2005 the Company exhibited at the Vancouver Resource Investment Conference and the Vancouver Exploration Roundup in January 2005. During, 2005 investor relations expenditures were \$26,604 (2004 - \$24,965).

### ***Recent developments***

Subsequent to December 31, 2005, the Company has signed a letter of intent for an option to acquire 100% interest in the Salamandra zinc-silver project, completed a trench sampling program at the Sandra and Nora project in Durango, Mexico, and started a geologic mapping and surface sampling program at the Colibri project in Durango, Mexico.

The Company has also been discussing potential joint venture agreements for the Brenda gold-copper project in British Columbia, Canada, and planning for a financing to fund the 2006 exploration programs and to strengthen working capital.

In March 2006, Dr. Andre Panteleyev and Mr. Arthur Freeze agreed to join the Company as advisors to the Board of Directors. Both Dr. Panteleyev and Mr. Freeze are recognized figures in the mineral exploration industry and their contributions will have a significant impact on the Company's future exploration and development programs.

The company exhibited at the Vancouver Resource Investment Conference and Vancouver Exploration Roundup in January 2006, and at the Prospectors and Developers Association of Canada convention in Toronto in March 2006. The Company had a significantly more active Investor Relations program during the first quarter of 2006.

### ***General Conditions Affecting the Company's Operations***

#### ***General Trends***

The principal business of the Company is the acquisition, exploration and, if warranted, development of natural resource properties of merit. The Company is not geographically limited to any particular region but in recent years has focused attention on natural resource properties in Canada and Mexico.

There has been a trend towards improving base and precious metal prices over the past year, particularly for gold, silver and copper. This trend is forecasted to continue over the coming year. The mining and minerals industry is experiencing increased demand for minerals and metals, in particular from economic growth in Asia. This has resulted in greater interest from the financial community in financing mineral exploration and development projects

#### ***Competitive Conditions***

Significant competition exists for natural resource acquisition opportunities. As a result the Company may be unable to acquire rights to exploit additional attractive mining properties on terms it considers acceptable

#### *Environmental Protection*

Environmental legislation is evolving in a manner such that standards, enforcement, fines and penalties for non-compliance are becoming stricter. Environmental assessments of proposed projects carry a heightened degree of responsibility for companies and directors, officers and employees. The cost of compliance with changes in government regulations has the potential to reduce the profitability of future operations. To the Company's knowledge, it is in compliance with all environmental laws and regulations affecting its operations.

#### *Number of Employees*

As of December 31, 2004, the Company had no employees. All administrative and certain geological services are provided to the Company by consultants or companies controlled by related parties.

#### *Acquisition and Disposition of Resource Properties*

During the year ended December 31, 2003, the Company entered into option and joint venture agreements to acquire up to a 75% interest in the Tres Marias and Cebollas silver-gold properties in Durango, Mexico, as detailed above. During 2004 the area covered by these properties was increased to 3,163 hectares through option agreements to acquire neighbouring claims and through staking of additional claim blocks.

#### **Risk Factors Relating to the Company's Business**

The Company's ability to generate revenue and profit from its natural resource properties, or any other resource property it may acquire, is dependent upon a number of factors, including, without limitation, the following:

##### *Precious and Base Metal Price Fluctuations*

The Company's ability to finance its mineral property acquisition, exploration and eventual development is dependent upon the market price of certain precious and base metals. The price of such metals has fluctuated widely and is affected by numerous economic and political factors, consumption patterns, speculative activities, levels of supply and demand, increased production due to new mine developments and productivity, metal substitutes and stock levels. These fluctuations may result in the Company not receiving an adequate return on invested capital or the investment retaining its value.

##### *Operating Hazards and Risks*

Mining operations generally involve a high degree of risk, which even a combination of experience, knowledge and careful evaluation may not be able to overcome. Operations in which the Company has a direct or indirect interest will be subject to all the hazards, risks and liabilities normally incidental to exploration, development and production of precious and base metals. The Company presently carries no liability insurance, and any liabilities arising from its operations may have a material, adverse effect on the Company's financial position.

##### *Exploration and Development*

There is no known body of commercial ore on the Company's mineral properties. Development of the Company's properties will only follow upon obtaining satisfactory exploration results. Mineral exploration and development involves a high degree of risk and few exploration properties are ultimately developed into producing mines. There is no assurance that the Company's mineral exploration and development activities will result in any commercially viable discoveries.

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

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

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*Calculation of Reserves and Mineralization and Precious and Base Metal Recovery*

There is a degree of uncertainty attributable to the calculation of reserves and mineralization and corresponding grades being mined or dedicated to future production. In addition, there can be no assurance that precious or other metal recoveries in small-scale laboratory tests will be duplicated in larger scale tests under on-site conditions or during production.

*Government Regulation*

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

*Environmental Factors*

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

*Title to Assets*

Although the Company has or will receive title opinions for any properties in which it has a material interest, there is no guarantee that title to such properties will not be challenged or impugned. The Company has not conducted surveys of the claims in which it holds direct or indirect interests and therefore, the precise area and location of such claims may be in doubt. The Company's claims may be subject to prior unregistered agreements or transfers or native land claims and title may be affected by undetected defects.

*Foreign Operations*

The Company operates in Mexico and has acquired four mineral properties, through staking, and has option agreements to acquire interests in two other mineral properties. The Company and is currently engaged in exploration activities on these properties. Subsequent to the end of the fiscal year, the Company has made a commitment to option another mineral property.

*Management and Directors*

The Company is dependent on a small number of directors and officers: Alvin Jackson, Michael McInnis, Gary Nordin, Bahman Yamini, Iain MacPhail and Graham Scott. The loss of any of these persons could have an adverse effect on the Company. The Company does not maintain key person insurance on any of its management.

*Conflicts of Interest*

Certain officers and directors of the Company are officers and/or directors of other natural resource companies that acquire interest in mineral properties. Such associations may give rise to conflicts of interest from time to time. The directors are required by law to act honestly and in good faith with a view to the best interests of the Company and its shareholders. They are also required to disclose any personal interest in any material transaction, which is proposed to be entered into with the company, and to abstain from voting as a director for the approval of any such transaction.

*Limited Operating History - Losses*

The Company has experienced losses in all years of its operations. There can be no assurance that the Company will operate profitably in the future. As of December 31, 2005, the Company's accumulated deficit was \$4,140,389.

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*Price Fluctuations and Share Price Volatility*

In recent years the securities markets in the United States and Canada have experienced a high level of price and volume volatility. The market price of securities of many mineral exploration companies have experienced wide fluctuations in price, which has not necessarily been related to their operating performance, underlying asset value or prospects. During the twelve months ended December 31, 2005, the price of the Company's shares fluctuated from a low of \$0.06 to a high of \$0.13 per share. There can be no assurance that continued fluctuations in price will not occur.

*Shares Reserved for Future Issuance - Dilution*

As at March 31, 2006, a total of 18,432,342 common shares of the Company were issued and outstanding. There were 1,700,000 stock options outstanding pursuant to which additional common shares may be issued in the future, which would result in further dilution to the Company's shareholders and pose a dilutive risk to potential shareholders.

**Forward-Looking Statements**

Any statements in this discussion, other than statements of historical facts, that address future production, reserve potential, exploration activities and events or developments that the Company expects, are forward-looking statements. Although the Company believes the expectations expressed in such forward-looking statements are based on reasonable assumptions, such statements are not guarantees of future performance. Actual results and developments may differ materially from those in the forward-looking statements. Factors that could cause actual results to differ materially from those in forward-looking statements include market prices, exploration results, availability of capital and financing, and general economic, market and business conditions.

**Corporate Disclosures**

The Company maintains a system of internal controls to provide reasonable assurance that assets are safeguarded and financial information is accurate and reliable. The Board of Directors has responsibility for developing and implementing the Company's approach to governance issues. Committees of the Board presently consist of an Audit Committee and a Management Compensation Committee. The Audit Committee consists of two unrelated, outside directors and one related director. The role of the audit committee is to oversee the Company's financial reporting obligations, systems and disclosure and to act as a liaison between the Board and the Company's auditors. The Board has also appointed a Management Compensation Committee that consists of three unrelated outside directors. The role of the Management Compensation Committee is to determine the remuneration of executive officers and to administer the Company's Stock Option Plan.

**Approval**

The Board of Directors of the Company has approved the disclosure contained in this annual MD&A.

A copy of this MD&A and previously published financial statements and MD&A, as well as other information is available on the SEDAR website at [www.sedar.com](http://www.sedar.com), and on the Company's website at [www.canasil.com](http://www.canasil.com)