IVANHOE ENERGY INC
Form 10-Q
August 09, 2012
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

Form 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(D)

OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended June 30, 2012

Commission file number: 000-30586

Ivanhoe Energy Inc.

(Exact name of registrant as specified in its charter)

Yukon, Canada	**98-0372413**
(State or other jurisdiction of incorporation or organization)	**(IRS Employer Identification No.)**

654-999 Canada Place

Vancouver, BC, Canada V6C 3E1

(604) 688-8323

(Address and telephone number of the registrant s principal executive offices)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. x Yes ¨ No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). ¨ Yes ¨ No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definitions of large accelerated filer , accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer	¨	Accelerated filer	x
Non-accelerated filer	¨	Smaller reporting company	¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). ¨ Yes x No

As at July 31, 2012, Ivanhoe Energy Inc. had 344,139,428 Common Shares outstanding with no par value.

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PART I FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

IVANHOE ENERGY INC.

Condensed Consolidated Statements of Financial Position

(Unaudited)

(US$000s)	Note	June 30, 2012	December 31, 2011
Assets			
Current Assets			
Cash and cash equivalents	3	27,416	16,890
Restricted cash	4	20,500	20,500
Accounts receivable		5,377	7,859
Note receivable		225	227
Prepaid and other		1,282	1,411
Assets held for sale	5	52,660	41,902
		107,460	88,789
Intangible	6	295,723	273,986
Property, plant and equipment	7	49,002	46,979
Long term receivables		5,295	3,956
		457,480	413,710
Liabilities and Shareholders Equity			
Current Liabilities			
Accounts payable and accrued liabilities		34,181	15,548
Debt	8	38,348	
Derivative instruments	9		183
Income taxes		947	641
		73,476	16,372
Long term debt	8	62,235	61,892
Long term derivative instruments	9, 10	60	1,617
Long term provisions		2,727	1,919
Deferred income taxes		18,041	17,773
		156,539	99,573
Shareholders Equity			
Share capital	12	586,108	586,108
Contributed surplus	13	28,693	26,524
Accumulated deficit		(313,860)	(298,495)
		300,941	314,137
		457,480	413,710

Nature of operations and going concern	**1**

(See accompanying Notes to the Unaudited Condensed Consolidated Financial Statements)

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IVANHOE ENERGY INC.

Condensed Consolidated Statements of Loss and Comprehensive Loss

(Unaudited)

		Three Months Ended		Six Months Ended	
		June 30,		June 30,	
(US$000s, except share and per share amounts)	Note	2012	2011	2012	2011
Revenue					
Oil		**11,292**	9,389	**19,200**	17,508
Interest		**5**	143	**11**	210
		11,297	9,532	**19,211**	17,718
Expenses and other					
Operating	**15**	**4,846**	5,339	**9,494**	9,862
Exploration and evaluation	**6**	**152**		**152**	
General and administrative		**10,400**	11,744	**20,887**	25,161
Depletion and depreciation	**7**	**2,401**	1,891	**4,237**	3,722
Foreign currency exchange gain		**(1,760)**	(238)	**(794)**	(463)
Derivative instruments gain	**9**	**(1,262)**	(6,071)	**(1,732)**	(7,200)
Finance		**470**	359	**586**	367
Other expenses	**8**			**309**	
		15,247	13,024	**33,139**	31,449
Loss before income taxes		**(3,950)**	(3,492)	**(13,928)**	(13,731)
Recovery of (provision for) income taxes					
Current		**(821)**	(477)	**(1,169)**	(799)
Deferred		**68**	(142)	**(268)**	(707)
		(753)	(619)	**(1,437)**	(1,506)
Net loss and comprehensive loss		**(4,703)**	(4,111)	**(15,365)**	(15,237)
Net loss per common share, basic and diluted		**(0.01)**	(0.01)	**(0.04)**	(0.04)
Weighted average number of common shares					
Basic and diluted (000s)		**344,139**	338,432	**344,139**	341,197

(See accompanying Notes to the Unaudited Condensed Consolidated Financial Statements)

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IVANHOE ENERGY INC.

Condensed Consolidated Statements of Changes in Equity

(Unaudited)

		Share Capital				
(US$000s, except share amounts)	Note	Shares (000s)	Amount	Contributed Surplus	Accumulated Deficit	Total
Balance January 1, 2011		**334,365**	**550,562**	**23,141**	**(273,219)**	**300,484**
Net loss and comprehensive loss					(15,237)	(15,237)
Exercise of stock options		984	4,164	(2,231)		1,933
Exercise of purchase warrants		8,621	31,047			31,047
Share-based compensation expense	13			3,235		3,235
Balance June 30, 2011		**343,970**	**585,773**	**24,145**	**(288,456)**	**321,462**

		Share Capital				
(US$000s, except share amounts)	Note	Shares (000s)	Amount	Contributed Surplus	Accumulated Deficit	Total
Balance January 1, 2012		**344,139**	**586,108**	**26,524**	**(298,495)**	**314,137**
Net loss and comprehensive loss					(15,365)	(15,365)
Funding of equity-settled share-based awards				(54)		(54)
Share-based compensation expense	13			2,223		2,223
Balance June 30, 2012		**344,139**	**586,108**	**28,693**	**(313,860)**	**300,941**

(See accompanying Notes to the Unaudited Condensed Consolidated Financial Statements)

IVANHOE ENERGY INC.

Condensed Consolidated Statements of Cash Flows

(Unaudited)

(US$000s)	Note	Three Months Ended June 30, 2012	Three Months Ended June 30, 2011	Six Months Ended June 30, 2012	Six Months Ended June 30, 2011
Operating Activities					
Net loss		**(4,703)**	(4,111)	**(15,365)**	(15,237)
Adjustments to reconcile net loss to cash from operating activities					
Depletion and depreciation	**7**	**2,401**	1,891	**4,237**	3,722
Exploration and evaluation expense	**6**	**152**		**152**	
Share-based compensation expense	**13**	**1,003**	1,471	**2,239**	3,247
Unrealized foreign currency exchange loss (gain)		**(1,669)**	(1,553)	**(620)**	(1,780)
Unrealized derivative instruments gain	**9**	**(1,262)**	(6,071)	**(1,732)**	(7,200)
Current income tax expense		**821**	477	**1,169**	799
Deferred income tax expense		**(68)**	142	**268**	707
Finance expense		**470**	359	**586**	367
Finance costs			269		269
Other expenses	**8**			**309**	
Other		**(2)**	(106)	**(1)**	(12)
Current income tax paid		**(381)**	(267)	**(864)**	(324)
Interest paid		**(302)**		**(302)**	
Share-based payments		**(110)**		**(166)**	
Changes in non-cash working capital items	**16**	**(534)**	1,044	**(986)**	1,978
Net cash used in operating activities		**(4,184)**	(6,455)	**(11,076)**	(13,464)
Investing Activities					
Intangible expenditures		**(19,509)**	(13,906)	**(28,050)**	(23,772)
Property, plant and equipment expenditures		**(5,110)**	(3,514)	**(5,494)**	(7,463)
Long term receivables		**(964)**	(316)	**(1,338)**	(463)
Interest paid		**(2,553)**	15	**(2,553)**	(1,003)
Changes in non-cash working capital items	**16**	**17,538**	1,082	**21,673**	4,578
Net cash used in investing activities		**(10,598)**	(16,639)	**(15,762)**	(28,123)
Financing Activities					
Debt proceeds, net of transaction costs	**8**		72,914	**37,282**	72,914
Proceeds from exercise of options and warrants			59		29,873
Changes in non-cash working capital items	**16**		(28)		(47)
Net cash provided by financing activities			72,945	**37,282**	102,740
Foreign exchange gain on cash and cash equivalents held in a foreign currency		**(62)**	2,659	**82**	3,838
(Decrease) increase in cash and cash equivalents, for the period		**(14,844)**	52,510	**10,526**	64,991
Cash and cash equivalents, beginning of period		**42,260**	80,798	**16,890**	68,317
Cash and cash equivalents, end of period		**27,416**	133,308	**27,416**	133,308

(See accompanying Notes to the Unaudited Condensed Consolidated Financial Statements)

IVANHOE ENERGY INC.

Notes to the Unaudited Condensed Consolidated Financial Statements

(tabular amounts in US$000s, except share and per share amounts)

1. NATURE OF OPERATIONS AND GOING CONCERN

Ivanhoe Energy Inc. (the Company or Ivanhoe) is a publicly listed company incorporated in Canada, with limited liability under the legislation of the Yukon. Ivanhoe s common shares are listed on the Toronto Stock Exchange (TSX) and the NASDAQ Stock Market (NASDAQ). The head office and principal address of the Company are located at 999 Canada Place, Suite 654, Vancouver, British Columbia, Canada, V6C 3E1. The registered and records office of the Company is located at 300-204 Black Street, Whitehorse, Yukon, Canada, Y1A 2M9.

Ivanhoe is an independent international heavy oil development and production company focused on pursuing long term growth in its reserves and production. Ivanhoe plans to utilize advanced technologies, such as its HTL technology, that are designed to improve recovery of heavy oil resources. In addition, the Company seeks to expand its reserve base and production through conventional exploration and production of oil and gas.

The June 30, 2012 unaudited condensed consolidated financial statements (Financial Statements) have been prepared using International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB), applicable to a going concern, which contemplates the realization of assets and settlement of liabilities in the normal course of business as they become due and assumes that Ivanhoe will be able to meet its obligations and continue operations for at least its next fiscal year. Realization values may be substantially different from carrying values as shown and these Financial Statements do not give effect to adjustments that may be necessary to the carrying values and classification of assets and liabilities should the Company be unable to continue as a going concern. Such adjustments could be material.

At June 30, 2012, Ivanhoe had an accumulated deficit of $313.9 million and working capital deficit of $18.7 million, excluding assets held for sale. In the six months ended June 30, 2012, cash used in operating activities was $11.1 million and the Company expects to incur further losses in the development of its business. Continuing as a going concern is dependent upon attaining future profitable operations to repay liabilities arising in the normal course of operations and accessing additional capital to develop the Company s properties. Ivanhoe intends to finance its future funding requirements through a combination of strategic investors and/or public and private debt and equity markets, either at a parent company level or at the project level, and through the sale of interests in existing oil and gas properties. There is no assurance that the Company will be able to obtain such financing, or obtain it on favorable terms. Without access to additional financing or other cash generating activities in 2012, there is material uncertainty that casts substantial doubt that the Company will be able to continue as a going concern.

The June 30, 2012 Financial Statements were approved by the Board of Directors and authorized for issue on July 27, 2012.

The Financial Statements are presented in US dollars and all values are rounded to the nearest thousand dollars except where otherwise indicated.

2. BASIS OF PRESENTATION

2.1 Statement of Compliance

The Financial Statements have been prepared in accordance with IAS 34, Interim Financial Reporting (IAS 34), using accounting policies consistent with IFRS as issued by the IASB. The Financial Statements are not subject to qualification relating to the application of IFRS as issued by the IASB.

The Financial Statements should be read in conjunction with the Company s annual financial statements for the year ended December 31, 2011 prepared in accordance with IFRS. The same accounting policies, presentation and methods of computation have been followed in these Financial Statements as were applied in the Company s first annual IFRS consolidated financial statements for the year ended December 31, 2011.

2.2 Basis of Presentation

The Financial Statements have been prepared on an historical cost basis, except derivative instruments, which are measured at fair value.

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2.3 Standards and Interpretations Issued But Not Yet Adopted

The Company has reviewed new and revised accounting pronouncements listed below, that have been issued, but are not yet effective. The Company has not yet evaluated the impact of these changes on its financial statements.

i. IFRS 9 Financial Instruments (IFRS 9)

IFRS 9 was issued in November 2009 and is intended to replace IAS 39, Financial Instruments: Recognition and Measurement (IAS 39) in phases. IFRS 9 uses a single approach to determine whether a financial asset is measured at amortized cost or fair value, as opposed to the multiple rules in IAS 39. The approach is based on how an entity manages its financial instruments given its business model and the contractual cash flow characteristics of the financial assets. The standard also requires a single impairment method to be used, replacing the multiple impairment methods in IAS 39. IFRS 9 is effective for reporting periods beginning on or after January 1, 2015.

ii. IFRS 10 Consolidated Financial Statements (IFRS 10)

IFRS 10 was issued in May 2011 and sets a single basis for consolidation, that being control of an entity. IFRS 10 replaces portions of IAS 27, Consolidated and Separate Financial Statements and Standing Interpretations Committee 12, Special Purpose Entities that provide a single model on how entities should prepare consolidated financial statements. This standard is effective for reporting periods on or after January 1, 2013, with earlier adoption permitted.

iii. IFRS 11 Joint Arrangements (IFRS 11)

IFRS 11, issued in May 2011, establishes principles for financial reporting by entities involved in a joint arrangement and distinguishes between joint operations and joint ventures. IFRS 11 supersedes the current IAS 31, Interests in Joint Ventures and Standing Interpretations Committee 13, Jointly Controlled Entities-Non Monetary Contributions by Venturers and is effective for reporting periods beginning on or after January 1, 2013, with earlier adoption permitted.

iv. IFRS 12 Disclosure of Interests in Other Entities (IFRS 12)

IFRS 12, issued in May 2011, establishes a single set of disclosure objectives, and requires minimum disclosures designed to meet those objectives, regarding interests in subsidiaries, joint arrangements, associates or unconsolidated structured entities. IFRS 12 is intended to combine the disclosure requirements on interests in other entities currently located throughout different standards. This standard is effective for reporting periods on or after January 1, 2013, with earlier adoption permitted.

v. IFRS 13 Fair Value Measurements (IFRS 13)

IFRS 13, issued in May 2011, defines fair value, sets out a single IFRS framework for measuring fair value and requires disclosures about fair value measurements. IFRS 13 applies to IFRS that require or permit fair value measurements or related disclosures, except in specified circumstances. IFRS 13 is to be applied for reporting periods beginning on or after January 1, 2013, with earlier adoption permitted.

vi. IAS 28 Investments in Associates and Joint Ventures (IAS 28)

IAS 28 was amended in 2011 and prescribes the accounting for investments in associates and sets out the requirements for the application of the equity method when accounting for investments in associates and joint ventures. IAS 28 is effective for reporting periods beginning on or after January 1, 2013, with earlier adoption permitted.

There are no other standards or interpretations issued, but not yet adopted, that are anticipated to have a material effect on the reported loss or net assets of the Company.

3. CASH AND CASH EQUIVALENTS

	June 30, 2012	December 31, 2011
Cash at banks and on hand	**27,416**	16,867
Restricted cash		23
	27,416	16,890

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4. RESTRICTED CASH

	June 30, 2012	December 31, 2011
Ecuador performance bond	**500**	500
Zitong performance bond	**20,000**	20,000
	20,500	20,500

In December 2011, Ivanhoe was required to post a $20.0 million performance bond as part of the completion and signing of a supplementary agreement to the Contract for Exploration, Development and Production in Zitong Block, Sichaun Basin with China National Petroleum Corporation (CNPC) for the Zitong block.

5. ASSETS HELD FOR SALE

Sunwing Zitong Energy (SZE), a wholly owned subsidiary of the Company, signed a binding Memorandum of Understanding to assign 100% of its participating interest in the Zitong Production Sharing Contract (PSC) to Shell China Exploration and Production Company Limited (Shell). The transaction is subject to government approvals and other prescribed conditions. There is no assurance that this transaction will close on the terms presently contemplated or at all.

In exchange for SZE s interest in the Zitong block, Ivanhoe will receive a cash payment of up to $85.0 million as reimbursement for past qualified and recoverable costs incurred. In addition, Ivanhoe will receive a further cash payment contingent on the timing of the receipt of full government approvals and third-party consents and waivers for the transaction. If the transaction closes after June 30, 2012, but on or before September 30, 2012, the Company will receive an additional $50.0 million. If the transaction closes after September 30, 2012, but on or before December 31, 2012, the Company will receive an additional $20.0 million. Failure to reach completion of the transaction prior to December 31, 2012 will give either party the right to terminate the transaction.

Should SZE receive government approval for the transaction, Shell will become liable for the performance bond posted in 2011, resulting in a release of restricted cash back to the Company.

The carrying value of the Zitong asset, which is comprised of exploration and evaluation (E&E) expenditures, was $52.7 million at June 30, 2012 (December 31, 2011 $41.9 million); the property was previously reported in the Asia segment.

6. INTANGIBLE ASSETS

	Exploration and Evaluation Assets					
	Asia	Canada	Latin America	Total	HTL Technology	Total Intangible Assets
Cost						
Balance January 1, 2011	38,135	123,755	19,525	181,415	92,153	273,568
Additions	23,094	9,697	12,303	45,094		45,094
Exploration and evaluation expense	(2,124)		(650)	(2,774)		(2,774)
Assets reclassified as held for sale	(41,902)			(41,902)		(41,902)
Balance December 31, 2011	17,203	133,452	31,178	181,833	92,153	273,986
Additions	229	4,877	16,783	21,889		21,889
Exploration and evaluation expense		(152)		(152)		(152)
Balance June 30, 2012	**17,432**	**138,177**	**47,961**	**203,570**	92,153	**295,723**

In the six months ended June 30, 2012, $0.9 million (year ended December 31, 2011 $2.1 million) of employee benefits directly attributable to E&E assets were capitalized. In addition, in the six months ended June 30, 2012, nil (year ended December 31, 2011 $0.3 million) related to share-based compensation costs were capitalized to E&E assets.

Amortization of the HTL technology has not commenced and its carrying value had not been impaired since it was acquired in 2005.

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7. PROPERTY, PLANT AND EQUIPMENT

	Oil and Gas Property and Equipment					
	Asia	Canada	Latin America	Total	Other Assets	Total PP&E
Cost						
Balance January 1, 2011	35,939			35,939	13,009	48,948
Additions	12,923			12,923	1,471	14,394
Disposals					(3)	(3)
Balance December 31, 2011	48,862			48,862	14,477	63,339
Additions	6,144			6,144	116	6,260
Balance June 30, 2012	**55,006**			**55,006**	**14,593**	**69,599**
Accumulated Depletion and Depreciation						
Balance January 1, 2011	6,196			6,196	2,134	8,330
Depletion and depreciation	6,899			6,899	1,132	8,031
Disposals					(1)	(1)
Balance December 31, 2011	13,095			13,095	3,265	16,360
Depletion and depreciation	3,676			3,676	561	4,237
Balance June 30, 2012	**16,771**			**16,771**	**3,826**	**20,597**
Net Book Value						
As at December 31, 2011	35,767			35,767	11,212	46,979
As at June 30, 2012	**38,235**			**38,235**	**10,767**	**49,002**

Oil and Gas Property and Equipment

In the six months ended June 30, 2012, $0.1 million (year ended December 31, 2011 $0.1 million) of employee benefits directly attributable to property, plant and equipment (PP&E) were capitalized.

Other Assets

Other assets include the Company s Feedstock Test Facility (FTF) at the Southwest Research Institute in San Antonio, Texas, and general furniture and fixtures.

Security

Should Ivanhoe receive government and other approvals necessary to develop the northern border of one of the Company s oil sands leases in the Athabasca region of Canada (Tamarack), the Company will make a cash payment to Talisman Energy Canada (Talisman) of up to Cdn$15.0 million, as a contingent, final payment for the 2008 acquisition of the oil sands leases (Note 11). The contingent payment is secured by a first fixed charge and security interest in favor of Talisman, including over the oil sands leases, and a general security interest in all of the Company s present and after acquired property, other than equity interests in the Company s subsidiaries (through which it holds assets in China, Mongolia and Ecuador and the HTL technology). Talisman has agreed to subordinate its security interest in the Tamarack oil sands leases and related assets to UBS Securities LLC and certain of its affiliates (UBS) until the loan provided by UBS to the Company through a credit agreement signed in March 2012 (Note 8) is repaid.

8. DEBT

Interest incurred for all outstanding debt was recorded as follows:

	Three months ended June 30,		Six months ended June 30,	
	2012	**2011**	**2012**	**2011**
Interest expense	**475**	352	**572**	352
Capitalized to E&E	**2,010**	677	**3,723**	1,374
Capitalized to PP&E	**463**		**729**	
Total interest incurred	**2,948**	1,029	**5,024**	1,726

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8.1 Short Term Debt

In March 2012, the Company signed a credit agreement with UBS providing for a $50.0 million loan from UBS (UBS Loan). The UBS Loan includes an initial draw of $30.0 million and Ivanhoe may elect to draw an additional $20.0 million of principal. Subsequent to quarter end, the Company elected to draw an additional $20.0 million of principal in July 2012. Borrowed amounts incur interest at a per annum rate equal to one month Libor plus 10% for the first six months of the UBS Loan which escalates by 1% per month thereafter; interest is payable monthly. The UBS Loan matures on March 23, 2013 and is secured by the Tamarack oil sands leases and related assets, and by a charge over the shares of three of the Company s subsidiaries: Sunwing Holding Corporation, Sunwing Energy Ltd. and Sunwing Zitong Energy Ltd.

8.2 Convertible Short Term Debt

Ivanhoe entered into an unsecured loan agreement on December 30, 2011 with Ivanhoe Capital Finance Ltd. (ICFL), a company wholly owned by Robert Friedland, for a $10.0 million loan (ICFL Loan). The funds were advanced to the Company on January 3, 2012. The outstanding balance is subordinate in repayment to all amounts owing under the UBS Loan. Interest on the loan is 10% per annum, calculated monthly and due upon maturity.

On March 14, 2012, the ICFL Loan agreement was amended to provide that, at ICFL s option, the outstanding principal may be converted into 10,484,375 common shares of the Company, at a price of Cdn$0.96 per common share, and the maturity date was extended to March 31, 2013. The debt component is carried at amortized cost and, on the date of amendment, the equity option was valued at nil using the residual method. The amendment was treated as an extinguishment of the original loan with recognition of the amended loan resulting in the remaining deferred financing costs of $0.3 million being expensed in the first quarter of 2012.

8.3 Convertible Debentures

On June 9, 2011, the Company issued Cdn$73.3 million in 5.75% convertible unsecured subordinated debentures at a price of Cdn$1,000 per debenture (Convertible Debentures). Cdn$50.0 million of the Convertible Debentures were issued in a public offering. The remaining Cdn$23.3 million were issued in a private placement on the same terms as the public offering.

The Convertible Debentures mature on June 30, 2016, pay interest semi-annually on June 30 and December 31 and are convertible at a price of Cdn$3.36 per share. They are redeemable after June 30, 2014 at Ivanhoe s option with the redemption price being settled using either cash or common shares.

The Canadian dollar denominated debt is considered an embedded derivative since the functional currency of the Company is the US dollar and, as such, the option was bifurcated and recognized at fair value as a long term derivative liability (Note 10) with changes in value recorded each period in the statement of loss. The carrying amount of the debt component of the Convertible Debentures at June 30, 2012 was $62.2 million (December 31, 2011 $61.9 million). The June 30, 2012 carrying value of the unamortized bifurcated derivative and transaction costs was $9.2 million.

9. FINANCIAL INSTRUMENTS

9.1 Fair Value of Financial Instruments Measured at Amortized Cost

Except as detailed below, the fair value of the Company s financial instruments recognized at amortized cost approximates their carrying value due to the short term maturity of these instruments.

	June 30, 2012	December 31, 2011
Short Term Debt		
Carrying amount	**38,348**	
Fair value	**39,340**	
Long Term Debt		
Carrying amount	**62,235**	61,892
Fair value	**49,323**	51,901

The fair value of the liability component of the Convertible Debentures was estimated using the closing price of the publicly traded debentures at June 30, 2012.

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9.2 Financial Instruments Measured at Fair Value Through Profit and Loss

The Company classifies its financial instruments according to the fair value hierarchy outlined in IFRS 7, Financial Instruments: Disclosures, as described below:

Level 1 using quoted prices in active markets for identical assets or liabilities.

Level 2 using inputs for the asset or liability, other than quoted prices, that are observable either directly (i.e. as prices) or indirectly (i.e. derived from prices).

Level 3 using inputs for the asset or liability that are not based on observable market data, such as prices based on internal models or other valuation methods.

The following table presents the Company s derivative instruments measured at fair value through profit or loss (FVTPL):

	Level 1		Level 2		Level 3	
	2006 Purchase Warrants	2009 & 2010 Purchase Warrants	2008 Convertible Component of Debt	2011 Convertible Component of Debentures	Subsidiary Option	Total Fair Value
Balance January 1, 2011	5,615	1,616	1,216			8,447
Issuance of convertible debentures				9,852		9,852
Exercise of options	(2)	(3,107)				(3,109)
Derivative (gains) losses through profit and loss	(3,267)	2,968	(1,216)	(7,810)	183	(9,142)
Expiration of purchase warrants through profit and loss	(2,346)	(1,477)				(3,823)
Foreign exchange gains				(425)		(425)
Balance December 31, 2011				1,617	183	1,800
Derivative gains through profit and loss				(1,549)		(1,549)
Expiration of derivatives through profit or loss					(183)	(183)
Foreign exchange gains				(8)		(8)
Balance June 30, 2012				**60**		**60**

The gain on derivative instruments of $1.7 million for the six months ended June 30, 2012 (six months ended June 30, 2011 $7.2 million, year ended December 31, 2011 $13.0 million) originated from the expiration and revaluation of derivative instruments measured at FVTPL.

9.3 Risks Arising from Financial Instruments

Ivanhoe is exposed in varying degrees to normal market risks inherent in the oil and gas industry, including commodity price risk, foreign currency exchange rate risk, credit risk, interest rate risk and liquidity risk. The Company recognizes these risks and manages its operations to minimize the exposure to the extent practicable. There have not been any significant changes to the Company s exposure to risks, or processes to manage these risks as described in the Company s 2011 Form 10-K, except as noted below:

Interest Rate Risk

As at June 30, 2012, the Company had borrowed $30.0 million under the UBS Loan. Subsequent to quarter end, the Company elected to draw an additional $20.0 million of principal in July 2012. Borrowed amounts incur interest at a rate of one month Libor plus 10% for the first six months and escalate by 1% per month thereafter. Borrowings issued at variable rates expose Ivanhoe to interest rate risk. The Company s goal is to minimize its interest expense; however, the Company does not anticipate using hedging contracts in 2012 to manage its interest rate risk.

If the interest rate on the UBS Loan were to increase by 1%, the Company s net loss would increase by approximately $25,000 per month. Similarly, a 1% decrease in the interest rate on the UBS Loan would decrease Ivanhoe s net loss by approximately $25,000 per month.

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10. DERIVATIVE INSTRUMENTS

The Company issued Cdn$73.3 million in Convertible Debentures in the second quarter of 2011. The outstanding principal amount is convertible into common shares of the Company. The fair value of the convertible component was $0.1 million at June 30, 2012, calculated with the Black-Scholes valuation method using a risk-free interest rate of 1.25%, a dividend yield of 0.0%, a weighted average volatility factor of 40% and an expected life of 4.0 years.

If the volatility used to fair value the convertible component decreased by 10%, the fair value would decrease by $0.1 million. If volatility increased by 10%, the fair value of the convertible option would increase by $0.2 million.

11. COMMITMENTS AND CONTINGENCIES

11.1 Operating Lease Arrangements

In the six months ended June 30, 2012, the Company expended $0.8 million (2011 $0.9 million) on operating leases relating to the rental of office space, which expire between 2012 and 2017.

At June 30, 2012, future net minimum payments for operating leases were:

2012	967
2013	1,432
2014	595
2015	401
After 2015	502
	3,897

11.2 Other

Should Ivanhoe receive government and other approvals necessary to develop the northern border of one of the Tamarack leases, the Company will make a cash payment to Talisman of up to Cdn$15.0 million, as a contingent, final payment for the 2008 purchase of the Tamarack leases.

From time to time, Ivanhoe enters into consulting agreements whereby a success fee may be payable if and when either a definitive agreement is signed or certain other contractual milestones are met. Under the agreements, the consultant may receive cash, common shares, stock options or some combination thereof. Similarly, agreements entered into by the Company may contain cancellation fees or liquidated damages provisions for early termination. These fees are not considered to be material.

The Company may provide indemnities to third parties, in the ordinary course of business, that are customary in certain commercial transactions, such as purchase and sale agreements. The terms of these indemnities will vary based upon the contract, the nature of which prevents Ivanhoe from making a reasonable estimate of the maximum potential amounts that may be required to be paid. The Company s management is of the opinion that any resulting settlements relating to indemnities are not likely to be material.

In the ordinary course of business, the Company is subject to legal proceedings being brought against it. While the final outcome of these proceedings is uncertain, the Company believes that these proceedings, in the aggregate, are not reasonably likely to have a material effect on its financial position.

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12. SHAREHOLDERS EQUITY

12.1 Share Capital

Authorized	Unlimited common shares with no par value
	Unlimited preferred shares with no par value
Issued and Outstanding	344,139,428 common shares (December 31, 2011 344,139,428)
	Nil preferred shares (December 31, 2011 nil)

See the Unaudited Condensed Consolidated Statements of Changes in Equity for the change in common shares issued in the six months ended June 30, 2012 and 2011.

12.2 Contributed Surplus

Contributed surplus at June 30, 2012 consisted solely of share-based compensation expense from equity settled awards.

13. SHARE-BASED PAYMENTS

Share-based transactions were charged to earnings, as general and administrative or operating expenses, or capitalized to E&E assets as follows:

	Three months ended June 30,		Six months ended June 30,	
	2012	**2011**	**2012**	**2011**
Share-based expense related to				
Equity settled transactions	**1,069**	1,459	**2,223**	3,235
Cash settled transactions	**(66)**	12	**16**	12
Total share-based expense	**1,003**	1,471	**2,239**	3,247
Share-based payments capitalized as E&E assets		335		335

13.1 Stock Option Plan

Details of transactions under the Company s stock option plan are as follows:

	June 30, 2012		December 31, 2011	
	Number of Stock Options (000s)	**Weighted Average Exercise Price (Cdn$)**	**Number of Stock Options (000s)**	**Weighted Average Exercise Price (Cdn$)**
Outstanding, beginning of period	**15,748**	**2.14**	16,927	2.24
Granted	**2,783**	**0.96**	2,924	2.06
Exercised			(1,687)	2.44
Expired	**(463)**	**2.22**	(710)	2.90
Forfeited	**(871)**	**2.20**	(1,706)	2.46

Outstanding, end of period	**17,197**	**1.95**	15,748	2.14
Exercisable, end of period	**8,949**	**2.13**	8,231	2.13

Shares authorized for issue under the option plan at June 30, 2012 were 24.1 million (December 31, 2011 24.1 million).

There were no stock options exercised in the six months ended June 30, 2012. The weighted average share price per option at the date of exercise for stock options exercised in the six months ended June 30, 2011 was Cdn$3.28.

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The weighted average fair value of stock options granted from the stock option plan during the six months ended June 30, 2012 was Cdn$0.69 (2011 Cdn$1.61) per option at the grant date using the Black-Scholes option pricing model. The weighted average assumptions used for the calculation were:

Six months ended June 30,	**2012**	**2011**
Expected life (in years)	**6.3**	6.3
Volatility [1]	**73.8%**	74.5%
Dividend yield		
Risk-free rate	**1.7%**	2.7%
Estimated forfeiture rate	**7.9%**	6.0%

(1) Expected volatility factor based on historical volatility of the Company s publicly traded common shares.

The following table summarizes information in respect of stock options outstanding and exercisable at June 30, 2012:

Range of Exercise Prices (Cdn$)	**Outstanding (000s)**	**Weighted Average Remaining Contractual Life (years)**	**Weighted Average Exercise Price (Cdn$)**
0.86 to 1.29	3,698	6.7	0.95
1.30 to 1.89	3,943	1.3	1.61
1.90 to 2.79	8,341	4.1	2.36
2.80 to 3.44	1,215	4.5	3.26
	17,197	4.0	1.95

13.2 Restricted Share Unit Plan

The Company adopted a restricted share unit (RSU) plan in the second quarter of 2011 under which it may issue restricted share units to eligible employees. RSUs vest in equal increments over three years and are settled in shares or cash on the anniversary date. RSUs do not entitle the holder to exercise voting rights until they have vested and the underlying shares have been delivered to the participant.

Details of transactions under the Company s RSU plan are as follows:

	June 30, 2012		**December 31, 2011**	
	Number of RSUs (000s) [1]	**Weighted Average Fair Value (Cdn$)**	Number of RSUs (000s) [1]	Weighted Average Fair Value (Cdn$)
Outstanding, beginning of period	**937**	**1.53**		
Granted	**2,498**	**0.69**	1,115	1.62
Vested	**(283)**	**1.14**		
Forfeited	**(143)**	**1.10**	(178)	2.08
Outstanding, end of period	**3,009**	**0.77**	937	1.53

(1) Includes RSUs that will be withheld on behalf of employees to satisfy statutory tax withholding requirements.

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The weighted average fair value of RSU s granted during the six months ended June 30, 2012 was Cdn$0.69 per RSU at the grant date using the Black-Scholes option pricing model. The weighted average assumptions used for the calculation were:

Six months ended June 30,	2012	2011
Expected life (in years)	**2.0**	3.0
Volatility [(1)]	**68.9%**	62.7%
Dividend yield		
Risk-free rate	**1.2%**	1.7%
Estimated forfeiture rate	**20.0%**	6.1%

(1) Expected volatility factor based on historical volatility of the Company s publicly traded common shares.

The liabilities arising from the RSUs to be settled by way of cash payments and the intrinsic value of those liabilities are:

	June 30, 2012
Current liabilities related to RSUs	**107**
Long term liabilities related to RSUs	**67**
Intrinsic value of vested RSUs	**164**

14. SEGMENT INFORMATION

Ivanhoe s organizational structure reflects its various operating activities and the geographic areas in which it operates. Oil and gas operations are divided into three geographic segments: Asia, Canada and Latin America. Asian operations capture the Company s oil production in Dagang and Daqing and exploration at Zitong in China, as well as exploration in Mongolia. The Canadian segment comprises activities from Ivanhoe s oil sands development project at Tamarack. Latin America consists of exploration and development of Block 20 in Ecuador.

The Technology Development area captures costs incurred to develop, enhance and identify improvements in the application of the Company s HTL technology. The Corporate area consists of costs that are not directly allocable to operating projects, such as executive officers, corporate financings and other general corporate activities.

The accounting policies of the segments are the same as the Company s consolidated accounting policies. Segment results include transactions between business segments. Corporate activities undertaken on behalf of a segment are allocated at cost. Oil revenue is classified according to the geographic location of the production. Segment liabilities include intercompany balances.

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The following tables present the Company s segment loss, capital investments and identifiable assets and liabilities.

	Asia	Canada	Latin America	Technology Development	Corporate	Total
Segment revenue [(1)]						
For the three months ended June 30, 2012	11,292				5	11,297
For the three months ended June 30, 2011	9,391				141	9,532
For the six months ended June 30, 2012	19,201				10	19,211
For the six months ended June 30, 2011	17,511				207	17,718
Segment income (loss)						
For the three months ended June 30, 2012	1,116	(1,028)	(1,600)	(2,061)	(1,130)	(4,703)
For the three months ended June 30, 2011	461	(979)	(2,160)	(2,759)	1,326	(4,111)
For the six months ended June 30, 2012	940	(2,456)	(2,543)	(4,190)	(7,116)	(15,365)
For the six months ended June 30, 2011	(1,711)	(2,286)	(3,867)	(5,007)	(2,366)	(15,237)
Segment assets [(2)]						
As at June 30, 2012	122,972	138,675	60,022	102,201	33,610	457,480
As at December 31, 2011	107,902	133,880	40,216	102,435	29,277	413,710
Segment liabilities [(3)]						
As at June 30, 2012	154,750	151,779	84,210	91,778	(325,978)	156,539
As at December 31, 2011	140,621	144,531	64,362	87,822	(337,763)	99,573
Capital investments Intangible						
For the three months ended June 30, 2012	9,488	642	9,379			19,509
For the three months ended June 30, 2011	7,607	1,806	4,493			13,906
For the six months ended June 30, 2012	10,094	2,751	15,205			28,050
For the six months ended June 30, 2011	14,106	3,847	5,819			23,772
Capital investments Property, plant and equipment						
For the three months ended June 30, 2012	5,110					5,110
For the three months ended June 30, 2011	2,755		(5)	764		3,514
For the six months ended June 30, 2012	5,419			34	41	5,494
For the six months ended June 30, 2011	6,301		58			