

PETAQUILLA MINERALS LTD.

CONSOLIDATED FINANCIAL STATEMENTS
(An Exploration Stage Company)

Six Months Ended

July 31, 2006 and 2005

(Unaudited – Prepared by Management)

PETAQUILLA MINERALS LTD.

NOTICE OF NO AUDITOR REVIEW OF INTERIM FINANCIAL STATEMENTS

Under National Instrument 51-102, Part 4, subsection 4.3(3)(a), if an auditor has not performed a review of the interim financial statements, they must be accompanied by a notice indicating that the financial statements have not been reviewed by an auditor.

The accompanying unaudited interim financial statements of the Company have been prepared by and are the responsibility of the Company's management. The Company's independent auditor has not performed a review of these financial statements in accordance with the standards established by the Canadian Institute of Chartered Accountants for a review of interim financial statements by an entity's auditor.

"Michael Levy"
President

"John S. Watt"
Chief Financial Officer

September 8, 2006

PETAQUILLA MINERALS LTD.
(An Exploration Stage Company)
CONSOLIDATED BALANCE SHEETS
(Expressed in Canadian Dollars)

	July 31, 2006 (Unaudited)	January 31, 2006 (Audited)
ASSETS		
Current		
Cash and cash equivalents	\$ 2,217,770	\$ 9,171,318
Receivables	51,973	32,188
Prepaid expenses	<u>229,896</u>	<u>36,650</u>
Total current assets	2,499,639	9,240,156
Property and equipment (Note 5)	1,484,075	285,005
Mineral properties (Note 6)	8,380,843	2,389,769
Restricted cash (Note 7)	<u>1,675,460</u>	<u>892,242</u>
	<u>\$ 14,040,017</u>	<u>\$ 12,807,172</u>

LIABILITIES AND SHAREHOLDERS' EQUITY

Current		
Accounts payable and accrued liabilities	\$ 1,499,561	\$ 499,261
Other accrued liabilities	45,899	51,835
Current portion of long term debt (note 8)	<u>164,019</u>	<u>-</u>
Total current liabilities	<u>1,709,479</u>	<u>551,096</u>
Long term debt (Note 8)	<u>318,816</u>	<u>-</u>
Shareholders' equity		
Capital stock (Note 9)		
Authorized		
Unlimited common shares and preference shares without par value (Note 9)		
Issued and outstanding		
73,996,167 (January 31, 2006 – 70,246,303) common shares	66,399,476	62,977,209
Contributed surplus (Note 9)	1,225,244	1,004,480
Deficit	<u>(55,446,017)</u>	<u>(51,558,632)</u>
	12,178,703	12,423,057
Treasury stock, at cost (Note 12)		
Repurchased, not cancelled		
44,200 (January 31, 2006 – 44,200) common shares	<u>(166,981)</u>	<u>(166,981)</u>
	<u>12,011,722</u>	<u>12,256,076</u>
	<u>\$ 14,040,017</u>	<u>\$ 12,807,172</u>

Nature of operations and going concern (Note 1)

Commitments (Note 14)

Subsequent events (Note 17)

On behalf of the Board:

“Michael Levy”

Director

“Richard Fifer”

Director

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

PETAQUILLA MINERALS LTD.
(An Exploration Stage Company)
CONSOLIDATED STATEMENTS OF OPERATIONS AND DEFICIT
(Expressed in Canadian Dollars)
PERIODS ENDED JULY 31

	Three months ended July 31, 2006	Three months ended July 31, 2005	Six months ended July 31, 2006	Six months ended July 31, 2005
EXPENSES				
Accounting and legal	\$ 171,793	\$ 91,881	\$ 266,106	\$ 141,198
Consulting fees	138,819	29,387	294,693	59,669
Depreciation	65,688	7,477	99,111	14,273
Filing fees	31,887	3,884	36,040	8,193
Investor relations and shareholder information	327,821	54,461	477,348	136,573
Office administration	228,506	61,962	343,018	106,682
Rent	8,322	18,757	26,159	44,683
Resource property costs	4,671	11,105	10,608	11,105
Stock-based compensation (Notes 9 & 10)	1,261,988	33,789	1,320,047	202,245
Travel	284,268	42,028	453,966	94,231
Wages and benefits	<u>580,888</u>	<u>59,431</u>	<u>746,499</u>	<u>120,177</u>
Total expenses	<u>(3,104,651)</u>	<u>(414,162)</u>	<u>(4,073,595)</u>	<u>(939,029)</u>
OTHER INCOME (EXPENSE)				
Foreign exchange (loss)	78,129	(102,700)	42,977	(15,134)
Write-down of property and equipment	-	-	-	-
Gain on sale of marketable securities	-	-	21,191	-
Interest income and amortization of discount on bond	<u>39,225</u>	<u>7,110</u>	<u>122,042</u>	<u>15,322</u>
	<u>117,354</u>	<u>(95,590)</u>	<u>186,210</u>	<u>188</u>
Loss for the period	(2,987,297)	(509,752)	(3,887,385)	(938,841)
Deficit, beginning of period	(52,458,720)	(44,572,501)	(51,558,632)	(44,143,412)
Loss on sale of treasury stock (Note 12)	<u>-</u>	<u>(1,574,015)</u>	<u>-</u>	<u>(1,574,015)</u>
Deficit, end of period	<u>\$ (55,446,017)</u>	<u>\$ (46,656,268)</u>	<u>\$ (55,446,017)</u>	<u>(46,656,268)</u>
Basic and diluted loss per share	<u>\$ (0.04)</u>	<u>\$ (0.01)</u>	<u>\$ (0.05)</u>	<u>\$ (0.02)</u>
Weighted average number of shares outstanding	<u>72,270,691</u>	<u>51,421,238</u>	<u>71,388,118</u>	<u>49,964,392</u>

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

PETAQUILLA MINERALS LTD.
(An Exploration Stage Company)
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Expressed in Canadian Dollars)
PERIODS ENDED JULY 31

	Three months ended July 31, 2006	Three months ended July 31, 2005	Six months ended July 31, 2006	Six months ended July 31, 2005
CASH FLOWS FROM OPERATING ACTIVITIES				
Loss for the period	\$ (2,987,297)	\$ (509,752)	\$ (3,887,385)	\$(938,841)
Items not affecting cash:				
Depreciation	65,688	7,477	99,111	14,273
Stock-based compensation	1,261,988	33,789	1,320,047	202,245
Gain on sale of marketable securities	-	-	(21,191)	-
Foreign exchange loss (gain) on restricted cash	(13,568)	23,916	10,140	4,511
Changes in non-cash working capital items:				
(Increase) decrease in receivables	(8,742)	10,135	(19,785)	25,989
(Increase) decrease in prepaid expenses	(112,187)	(2,907)	(193,246)	(33,419)
(Decrease) increase in accounts payable and accrued liabilities	<u>(72,000)</u>	<u>(52,222)</u>	<u>400,072</u>	<u>(571)</u>
Net cash used in operating activities	<u>(1,866,118)</u>	<u>(489,564)</u>	<u>(2,292,237)</u>	<u>(725,813)</u>
CASH FLOWS FROM FINANCING ACTIVITIES				
Net proceeds from sale of treasury stock	-	-	-	319,985
Proceeds from long term debt	25,279	-	318,816	-
Net proceeds from issuance of capital stock	<u>2,091,418</u>	<u>584,300</u>	<u>2,322,984</u>	<u>629,837</u>
Net cash provided by financing activities	<u>2,116,697</u>	<u>584,300</u>	<u>2,641,800</u>	<u>949,822</u>
CASH FLOWS FROM INVESTING ACTIVITIES				
Acquisition of property and equipment	(637,994)	(5,232)	(1,356,056)	(100,443)
Investment in mineral properties	(2,911,448)	(258,217)	(5,232,763)	(898,922)
Depreciation (deferred)	57,875	-	57,875	-
Purchase of performance bond and restricted cash	(227,908)	-	(793,358)	-
Proceeds from sale of marketable securities	<u>-</u>	<u>-</u>	<u>21,191</u>	<u>-</u>
Net cash used in investing activities	<u>(3,719,475)</u>	<u>(263,449)</u>	<u>(7,303,111)</u>	<u>(999,365)</u>
Change in cash and cash equivalents	(3,468,896)	(168,713)	(6,953,548)	(775,356)
Cash and cash equivalents, beginning of period	<u>5,686,666</u>	<u>284,905</u>	<u>9,171,318</u>	<u>891,548</u>
Cash and cash equivalents, end of period	\$ <u>2,217,770</u>	\$ <u>116,192</u>	\$ <u>2,217,770</u>	\$ <u>116,192</u>

Supplemental disclosure with respect to cash flows (Note 16)

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

PETAQUILLA MINERALS LTD.

(An Exploration Stage Company)

NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in Canadian Dollars)

JULY 31, 2006

(Unaudited – Prepared by Management)

1. NATURE OF OPERATIONS

The Company was incorporated in the Province of British Columbia and is in the business of the acquisition and exploration of resource properties and has not yet determined whether its properties contain ore reserves that are economically recoverable. To date, the Company has not earned significant revenues and is considered to be in the exploration stage.

At July 31, 2006, the Company has working capital of \$790,160 (January 31, 2006 - \$8,689,060). During the year ended January 31, 2006, the Company raised funds from a private placement but will have to raise additional funds to undertake further exploration and subsequent development of its mineral properties. Management is pursuing additional sources of financing and while it has been successful in the past there can be no assurance that it will be able to do so in the future.

These consolidated financial statements have been prepared on a going concern basis, which assumes the Company will be able to realize its assets and discharge its liabilities in the normal course of business for the foreseeable future. These consolidated financial statements do not include any adjustments relating to the recoverability and classification of recorded assets and liabilities that might be necessary should the Company be unable to continue as a going concern.

2. SIGNIFICANT ACCOUNTING POLICIES

These consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles. The significant accounting policies adopted by the Company are as follows:

Basis of consolidation

These consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries, Petaquilla Minerals, S.A. (a Panama corporation), Adrian Resources (BVI) Ltd. (a British Virgin Island corporation), Georecursos Internacional, S.A. (“Georecursos”) (a Panama corporation), Petaquilla Gold, S.A. (a Panama corporation) and Petaquilla Copper Ltd. (a British Columbia corporation). The Company proportionately consolidates its 52% interest in a joint venture investment, Minera Petaquilla S.A. (“Minera Petaquilla”) (a Panama corporation).

All significant inter-company transactions and balances have been eliminated upon consolidation.

Use of estimates

The preparation of consolidated 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 and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amount of revenues and expenses during the reporting period. Actual results could differ from these estimates.

Cash and cash equivalents

Cash is comprised of cash on hand and demand deposits.

Cash equivalents are short-term, highly liquid investments with original maturities of three months or less that are readily convertible to known amounts of cash and which are subject to an insignificant risk of change in value. To limit its credit risk exposure in excess of federally insured amounts, the Company places its deposits with financial institutions with high credit standing.

PETAQUILLA MINERALS LTD.

(An Exploration Stage Company)

NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in Canadian Dollars)

JULY 31, 2006

(Unaudited – Prepared by Management)

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

Marketable securities are carried at the lower of cost and quoted market value on an individual investment basis.

Property and equipment

Equipment is recorded at cost less accumulated depreciation, which is provided on the following capital assets on the declining balance basis at rates as follows:

Furniture and fixtures	20%
Office equipment	20%
Computer equipment	30%
Equipment	30%
Vehicles	30%
Computer software	50%
Leasehold improvements	5 year straight line

Resource properties

Acquisition costs of resource properties, together with direct exploration and development expenditures incurred thereon, are deferred until the property to which they relate is placed into production, sold or abandoned. The carrying values of resource properties are, where necessary, written down to the estimated recoverable amount based on undiscounted estimated future net cash flows. Costs relating to properties abandoned are written off when the decision to abandon is made.

The Company follows the cost reduction method of accounting for the receipt of property option and similar payments. Cash and other property payments received from the Company's exploration partners are credited to the respective property until capitalized costs are recovered; thereafter, such payments are included in income. Option payments are exercisable at the discretion of the optionee and are only recognized when received. Management fees earned for the management of properties are included in income.

On an annual basis, the Company reviews the carrying values of deferred resource property acquisition and exploration expenditures with a view to assessing whether there has been impairment in value. In the event that management determines potential reserves to be insufficient to recover the carrying value of any property, the carrying value will be written down or written off, as appropriate.

PETAQUILLA MINERALS LTD.

(An Exploration Stage Company)

NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in Canadian Dollars)

JULY 31, 2006

(Unaudited – Prepared by Management)

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

Asset retirement obligations

An asset retirement obligation is a legal obligation associated with the retirement of tangible long-lived assets that the Company is required to settle. The Company recognizes the fair value of a liability for an asset retirement obligation in the period in which it is incurred when a reasonable estimate of fair value can be made. The carrying amount of the related long-lived asset is increased by the same amount as the liability. To date, the Company has not incurred any asset retirement obligations.

Impairment of long-lived assets

A long-lived asset is tested for recoverability whenever events or changes in circumstances indicate that its carrying amount may not be recoverable. An impairment loss is recognized when the carrying amount of a long-lived asset exceeds its fair value. For purposes of recognition and measurement of an impairment loss, a long-lived asset is grouped with other assets and liabilities to form an asset group, at the lowest level for which identifiable cash flows are largely independent of the cash flows of other assets and liabilities. Estimates of future cash flows used to test recoverability of a long-lived asset include only the future cash flows that are directly associated with, and that are expected to arise as a direct result of, its use and eventual disposition.

Foreign currency translation

Integrated foreign operations are translated using the temporal method. Under this method, monetary assets and liabilities are translated at the period-end exchange rate, non-monetary assets and liabilities are translated at rates prevailing at the respective transaction dates, and revenue and expenses are translated at rates approximating those in effect at the time of the transactions. Translation gains and losses are reflected in loss for the period.

Foreign currency-denominated monetary accounts of the Company are translated at the period-end exchange rate. Exchange gains and losses on translation are recognized as a gain or loss in the period they arise.

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 period. For the periods presented, this calculation proved to be anti-dilutive.

Basic loss per share is calculated using the weighted average number of common shares outstanding during the period.

PETAQUILLA MINERALS LTD.

(An Exploration Stage Company)

NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in Canadian Dollars)

JULY 31, 2006

(Unaudited – Prepared by Management)

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

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.

Income taxes

Future income taxes are recorded using the asset and liability method under which 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 period 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.

Comparative figures

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

3. MARKETABLE SECURITIES

The Company holds shares of certain publicly traded companies with a book value of \$Nil (January 31, 2006 - \$Nil) and a market value of \$Nil (January 31, 2006 - \$15,375). During the period ended July 31, 2006, all of the Company's holdings of marketable securities were sold for net proceeds of \$21,191 and a gain of \$21,191.

PETAQUILLA MINERALS LTD.

(An Exploration Stage Company)

NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in Canadian Dollars)

JULY 31, 2006

(Unaudited – Prepared by Management)

4. INVESTMENT IN JOINT VENTURE

The Company owns a 52% joint venture interest in Minera Petaquilla, which is proportionately consolidated in the financial statements. The Company's interest is summarized as follows:

	July 31, 2006	January 31, 2006
ASSETS		
Current assets		
Cash	\$ 47,473	\$ 5,907
Due from shareholders	-	-
Receivables	6,323	5,671
Prepaid expenses	-	2,357
	<u>\$ 53,796</u>	<u>\$ 13,935</u>
LIABILITIES		
Current liabilities	\$ 5,285	\$ 9,367
Other liabilities	40,546	42,468
SHAREHOLDERS' EQUITY (DEFICIENCY)	<u>7,965</u>	<u>(37,900)</u>
	<u>\$ 53,796</u>	<u>\$ 13,935</u>

5. PROPERTY AND EQUIPMENT

	July 31, 2006			January 31, 2006		
	Cost	Accumulated Depreciation	Net Book Value	Cost	Accumulated Depreciation	Net Book Value
Computer equipment	\$ 295,107	\$ 49,409	\$ 245,698	\$ 127,650	\$ 22,329	\$ 105,321
Computer software	261,457	37,803	223,654	20,418	3,754	16,664
Equipment	749,767	74,505	675,262	74,173	15,045	59,128
Furniture and fixtures	23,375	6,204	17,171	23,375	4,330	19,045
Leasehold improvements	8,951	8,951	-	8,951	2,920	6,031
Office equipment	29,698	5,228	24,470	14,778	3,421	11,357
Vehicles	302,721	39,031	263,690	79,803	12,344	67,459
Land	<u>34,130</u>	<u>-</u>	<u>34,130</u>	<u>79,803</u>	<u>12,344</u>	<u>67,459</u>
	<u>\$ 1,705,206</u>	<u>\$ 221,131</u>	<u>\$ 1,484,075</u>	<u>\$ 349,148</u>	<u>\$ 64,143</u>	<u>\$ 285,005</u>

PETAQUILLA MINERALS LTD.

(An Exploration Stage Company)

NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in Canadian Dollars)

JULY 31, 2006

(Unaudited – Prepared by Management)

6. MINERAL PROPERTIES

Ley Petaquilla Property- Panama

The Company, through its wholly-owned subsidiary Georecursos, owns 52% of Minera Petaquilla. Minnova (Panama) Inc. (“Minnova”), a wholly-owned subsidiary of Inmet Mining Corporation (“Inmet”), owns the remaining 48% of Minera Petaquilla, a company formed during 1997 to own the Ley Petaquilla mineral concession in Panama. Pursuant to the contract law under which the Petaquilla concession was granted by the Government of the Republic of Panama, the Company has delivered a phased Mine Development Plan to the Government of Panama which was approved in September 2005. Refer also to “Molejon Property – Panama”. This approval resulted in the extension of the land tenure for an initial 20 year period commencing on September 2005, subject to the Company meeting certain other development and operational conditions on an ongoing basis. Terms of the land tenure have two additional 20 year terms that are also subject to the Company meeting certain other ongoing development and operational conditions.

Teck Cominco Limited (“Teck”) has an option to acquire 50% of the Company’s interest in Minera Petaquilla, which would result in Teck having a 26% interest in Minera Petaquilla. In order for Teck to acquire the 26% interest, it is required to:

- i) Fund 52% of the continuing exploration expenditures, as defined, of Minera Petaquilla, with Minnova to fund its 48% share, until such time as Teck either acquires its interest or its interest is terminated.
- ii) Fund 100% of and complete a final feasibility study, as defined, for the property and deliver such study by January 21, 1998 (completed).
- iii) Arrange project financing for Minera Petaquilla for completion of development of the Ley Petaquilla property and, if necessary, fund 52% (Minnova to fund 48%) of any shortfall in the total project funding requirement in excess of arranged project financing.

Teck is committed to annually make a final commitment respecting development of the concession and to deliver an update to the feasibility study of the concession. The requirement to make a final commitment or give notice of unfavorable economic conditions within 90 days of delivery of the final feasibility study applies to all subsequent annual anniversaries. Failure to make such a commitment or deliver a notice shall result in the termination of Teck’s right to acquire an interest in Minera Petaquilla.

In April 2005, the Company and Inmet agreed to waive for one year Teck’s obligation to make a final commitment respecting development of the concession and to deliver an updated feasibility study. This waiver does not affect Teck’s obligation to make a final commitment respecting development of the concession and to deliver an updated feasibility study in 2006.

PETAQUILLA MINERALS LTD.

(An Exploration Stage Company)

NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in Canadian Dollars)

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(Unaudited – Prepared by Management)

6. MINERAL PROPERTIES (cont'd...)

Ley Petaquilla Property- Panama (cont'd...)

On April 27, 2006 Teck, Inmet and PTQ, the partners in Minera Petaquilla project, agreed to proceed with an update of the January 1998 Feasibility Study to be completed by AMEC Americas Limited (“AMEC”), formerly H.A. Simons, for the Petaquilla Copper Project to more accurately reflect current prices and technological advances. September 30, 2006 is the targeted completion date for such study. The updated study by AMEC will include the following specific assessments:

- i. Reviewing the truck and shovel fleet equipment selection, with a view of utilization of larger equipment.
- ii. Reviewing the grinding capacity to determine if a single grinding line would provide the capacity required for the anticipated 120,000 tpd throughput rate.
- iii. Reviewing the flotation equipment selection in light of the larger equipment currently available.
- iv. For any of the above revised approaches that appear technically feasible, to estimate their capital and operating cost impacts on the Project to the prefeasibility level (+/- 25% to +/- 30%).

Upon Teck making a final commitment, Minnova is required to deliver a final commitment to participate in the development of the project or it will be required to dispose of its interest in Minera Petaquilla. Minnova is then required to either offer to sell its interest in the concession or accept an 8% net profit interest, as defined, in the project. The offer to sell its interest shall be made first to the Company and then to Teck at a price to be determined by Minnova. In the event that neither the Company nor Teck chooses to acquire Minnova’s interest, Minnova shall be entitled to seek an independent purchaser of its interest on terms no more favorable than those offered to the Company and Teck.

Either the Company or Minnova (the Proposer) may at any time give notice to the other parties of its intention to proceed with development of the concession in accordance with the most recently delivered Teck feasibility study. Upon receipt of such notice, Teck has 50 days in which to make a final commitment to develop the project. The other party, the Company or Minnova (the Recipient), has 60 days from the receipt of such notice to commit to develop the project.

If the Recipient has not agreed to develop the project, the Proposer may, within 70 days of the proposal, elect to exercise the “Shotgun Offer,” as defined, and either sell its interest or acquire the Recipient’s interest in Minera Petaquilla, for cash, based on the value of Minera Petaquilla as determined in accordance with the provisions of the agreement. The Recipient has 15 days from receipt of the Shotgun Offer to agree either to sell its interest or to acquire the Proposer’s interest as applicable, and in the event that the Recipient does not take action within the 15-day period, it will thereafter be deemed to have agreed to sell its interest in Minera Petaquilla.

If Minnova sells its interest, pursuant to the Shotgun Offer, the Company shall pay Minnova 48% of the value of Minera Petaquilla.

If the Company sells its interest, pursuant to the Shotgun Offer, it shall receive 29% of the value of Minera Petaquilla on condition that, in the event that Teck’s interest in the concession is terminated, the Company shall receive an additional 23% of the value of Minera Petaquilla.

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NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in Canadian Dollars)

JULY 31, 2006

(Unaudited – Prepared by Management)

6. MINERAL PROPERTIES (cont'd...)

Ley Petaquilla Property- Panama (cont'd...)

If Teck's interest in the concession is not terminated and the Company sells its interest, pursuant to the Shotgun Offer, the Company shall not be entitled to receive any further amount, in excess of the 29% of the value received on account of the sale of its interest in Minera Petaquilla.

Upon exercise of the Shotgun Offer, Teck has 130 days in which to deliver a final commitment for development of the concession or its interest shall be terminated.

Teck's interest in the concession shall terminate on the earlier of:

- i) Teck electing to terminate its interest provided it has delivered its final feasibility study, or
- ii) Teck's failure to deliver a final commitment requesting development of the concession and to deliver an updated feasibility study.

In the event that Teck's interest is terminated, Teck shall retain a net profit royalty interest in the project at a rate to be determined.

The Government of Panama passed legislation which significantly expands the size of the Panama Canal Watershed in general and, in particular, establishes an overlap of part of the Petaquilla concession. It is possible that future construction of dams within the watershed area could negatively affect the development of the Ley Petaquilla property.

In late April 2006, the government of Panama announced it will take action to repeal its present legislation to significantly expand the Panama Canal Watershed in general. This will eliminate the risk of any potential overlap of part of the Ley Petaquilla concession.

Molejon Property – Panama

In June 2005, the shareholders of Minera Petaquilla agreed to separate the gold deposit and other precious metal mineral deposits that might be developed within the Ley Petaquilla mineral concession from the copper mineral deposits within the Ley Petaquilla mineral concession. The agreement provides for the Company, through Petaquilla Gold, S.A., to own a 100% interest in the Molejon gold deposit, as well as all other gold and precious metal mineral deposits that might be developed within the Ley Petaquilla mineral concession, subject to a graduated 1% - 5% Net Smelter Return, based on the future gold price at the time of production, payable to Teck and Minova as to 35.135% and 64.865% respectively.

Approval of the phased Mine Development Plan was obtained in September 2005. Transfer of title to the Company of the Molejon gold mineral deposit, as well as the other rights as described above, is underway.

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NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in Canadian Dollars)

JULY 31, 2006

(Unaudited – Prepared by Management)

6. MINERAL PROPERTIES (cont'd...)***Molejon Property – Panama (cont'd...)***

As of July 31, 2006, the Company has incurred the following costs related to the Molejon gold deposit. These costs have been capitalized on the Company's consolidated balance sheet as mineral property costs:

	July 31, 2006	January 31, 2006
Trenching	\$ 2,039,836	\$ 811,037
Purchases, logistics and site administration	644,813	352,250
Road	2,142,147	293,407
Engineering and geology	646,487	275,372
Camp costs	370,552	197,300
Assaying	397,979	167,434
Drilling	1,604,860	106,842
Permits and licences	119,575	81,097
Data management	169,648	59,825
Community service plan	244,946	45,205
	\$ 8,380,843	\$ 2,389,769

Mineral Properties - Other

The Company holds various interests in other land concession areas adjacent to the Ley Petaquilla Property in Panama, including the Rio Belencillo and Rio Petaquilla concessions.

By an Agreement dated May 7, 2005 and amended on June 10, 2005, Gold Dragon Capital Management Ltd. ("Gold Dragon"), has an option to purchase all of the Company's interest in the Rio Belencillo and Rio Petaquilla concessions by the expenditure of \$100,000 in approved exploration costs by May 7, 2007, an additional \$400,000 in approved exploration costs by February 7, 2008 and by then paying the Company \$1,152,400. This sum is payable in shares of Gold Dragon.

During the period ended July 31, 2006, Gold Dragon exercised its option having met all the option conditions. Delivery of the final payment to the Company in shares of Gold Dragon is scheduled to complete upon the Company delivering to Gold Dragon appropriate title to the Optioned Land.

During the period ended July 31, 2006, the Company entered into an agreement with Eurogold Mining Inc. ("Eurogold"), for the exploration and development of the San Juan Concessions. The San Juan Property is adjacent to the Company's Molejon gold project and the Petaquilla porphyry copper project in west central Panama. Under the agreement, Eurogold may earn a 60% interest in the San Juan Property by incurring exploration expenditures of at least US\$60,000,000, by paying Petaquilla US\$600,000 in cash and by causing to be issued to Petaquilla 3,000,000 shares of the public company ("Pubco") to which Eurogold will assign its interest in the property, all over a period of three years. If Pubco acquires a 60% interest in the property, it may increase its interest to 70% by incurring US\$3,000,000 in additional exploration expenditures in the fourth year. The Company will be the operator of the project. The Company has received the initial cash option payment of \$112,000 (US\$100,000).

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7. RESTRICTED CASH

The Company is required to post a performance bond of US\$780,000 to maintain its interest in the Petaquilla property. As at January 31, 2004, the Company fulfilled this requirement by holding a Republic of Panama Sovereign Bond (the "Panama Bond") with a face value of US\$750,000, which the Company had purchased earlier at a discount of US\$630,000, and an additional one-year time deposit of US\$31,175. The discount on the Panama Bond was being amortized to income over the original term of the bond. The Panama Bond was also returning a portion of its principal to the Company over the term of the loan. During the fiscal year ended January 31, 2005, the Panama Bond was redeemed early resulting in a gain of \$198,142. The Company has pledged a guaranteed investment certificate in the amount of US\$780,000 as security for a letter of credit with the Bank of Nova Scotia to satisfy the requirements of the performance bond. The Canadian dollar equivalent of the US\$780,000 investment is \$882,102 as at July 31, 2006 after recognizing a foreign exchange loss of \$10,140 from the January 31, 2006 balance of \$892,242.

During the period ended July 31, 2006, the Company pledged \$370,193 (US\$325,000) by way of a term deposit with the bank as a reserve to meet statutory employer payroll obligations that will arise through the next six months ended December 31, 2006.

During the period ended July 31, 2006, the Company arranged a bank loan for \$428,403 (US\$382,400) to acquire road and mine site equipment. The bank loan is repayable in 36 equal monthly instalments of \$13,155 (US\$11,742) commencing in May 2006 and bears interest at an annual rate of 5.625%. Collateral for this equipment loan is in the form of a pledge of \$280,075 (US\$250,000) renewable term deposit and a fixed first charge on the purchased equipment.

During the period ended July 31, 2006, the Company pledged \$113,090 (US\$100,000) by way of term deposit with the bank as a performance bond with the Ministry of Commerce (Panama) for possible environmental impacts.

During the period ended July 31, 2006, the Company deposited \$30,000 with HSBC Bank to be used as collateral for the credit card used by the Company to pay ongoing travel and related costs.

	July 31, 2006	January 31, 2006
Performance bond	\$ 882,102	\$ 892,242
Payroll reserve	370,193	-
Equipment loan collateral	280,075	-
Environmental impact bond	113,090	-
Credit card collateral	30,000	-
	<u>\$ 1,675,460</u>	<u>\$ 892,242</u>

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8. LONG TERM DEBT

During the period ended July 31, 2006, the Company arranged a bank loan of \$428,403 (US\$382,400) to acquire road and mine site equipment. The loan is repayable in 36 equal monthly instalments of \$13,155 (US\$11,742) commencing in May 2006 and bears interest at an annual rate of 5.625%. Collateral for this loan is comprised of a pledge of a \$280,075 (US\$250,000) renewable term deposit and a fixed first charge on the purchased equipment. As at July 31, 2006, the current portion of the long term debt is \$136,984 and the long term portion is \$262,995.

During the period ended July 31, 2006, the Company arranged a bank loan of \$89,126 (US\$78,810) to acquire vehicles to be used for the mine site. The loan is repayable in 36 equal monthly instalments of \$2,834 (US\$2,506) commencing in May 2006 and bears interest at an annual rate of 5.75%. Collateral for this loan is comprised of a fixed first charge on the purchased equipment. As at July 31, 2006, the current portion of the long term debt is \$27,035 and the long term portion is \$55,821.

	July 31, 2006	January 31, 2006
Long term debt		
Equipment loan	\$ 399,979	\$ -
Vehicle loan	82,856	-
	482,835	-
Less: current portion	(164,019)	-
	\$ 318,816	\$ -

9. CAPITAL STOCK AND CONTRIBUTED SURPLUS

Authorized Capital

At the June 6, 2006 Annual General Meeting of the shareholders, a special resolution was authorized and approved changing the authorized capital of the Company to an unlimited number of common shares without par value and an unlimited number of preference shares without par value.

	July 31, 2006	January 31, 2006
Unlimited common shares without par value		100,000,000 common shares without par value
Unlimited preference shares without par value		20,000,000 preference shares without par value

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9. CAPITAL STOCK AND CONTRIBUTED SURPLUS (cont'd...)

	Number of Shares	Amount	Contributed Surplus
Issued			
Balance as at January 31, 2004	48,829,542	50,849,326	327,822
Exercise of stock options	2,185,497	476,209	(114,383)
Exercise of warrants	249,498	105,257	(42,883)
Stock-based compensation	-	-	716,876
Balance as at January 31, 2005	51,264,537	51,430,792	887,432
Non-brokered private placement, net of finders' fees (a)	9,965,670	8,933,334	-
Exercise of stock options	1,465,600	713,008	(241,690)
Exercise of warrants	7,550,496	1,939,187	(51,563)
Stock-based compensation	-	-	410,301
Share issuance costs	-	(39,112)	-
Balance as at January 31, 2006	70,246,303	\$ 62,977,209	\$ 1,004,480
Exercise of stock options	3,477,693	3,095,661	(1,099,283)
Exercise of warrants	272,171	326,606	-
Stock-based compensation	-	-	1,320,047
Balance as at July 31, 2006	73,996,167	\$ 66,399,476	\$ 1,225,244

- a) In January 2006, the Company completed a non-brokered private placement and issued 9,965,670 units at a price of \$0.95 per unit, for gross proceeds of \$9,467,387. Each unit consists of one common share and one-half of one non-transferable share purchase warrant aggregating 4,982,835 warrants. Each whole warrant entitles the holder to purchase one common share of the Company at a price of \$1.20 per share if exercised in the first year following the closing, and at a price of \$1.44 per share if exercised in the second year following the closing. The warrant will terminate within 20 days unless exercised in the event the Company's closing stock price meets or exceeds \$2.00 for 10 consecutive trading days and the Company issues a press release of such an event. The Company paid finders' fees of \$534,053 for net proceeds of \$8,933,334.
- b) During the fiscal year ended January 31, 2006, net proceeds from issuance of capital stock of \$11,292,276 is comprised of \$8,933,334 for the non-brokered private placement and \$2,358,942 being the cash proceeds from the exercise of stock options and warrants.
- c) During the period ended July 31, 2006, proceeds of \$2,322,984 is comprised of the net cash proceeds from the exercise of stock options and warrants.

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9. CAPITAL STOCK AND CONTRIBUTED SURPLUS (cont'd...)

- d) The Company has adopted a new shareholder rights plan, subject to regulatory and shareholder approval. Under the new Plan, the Company will issue one Right for no consideration for each outstanding common share of the Company to all holders of record of common shares as at 5:00 p.m., Pacific time, March 7, 2006. Thereafter, each common share issued by the Company during the term of the Plan will have one Right attached to it. The term of the Plan is five years unless the rights are earlier redeemed or exchanged. The Plan will be subject to review after the third year of its term.

The Rights are attached to the common shares and cannot be exercised until eight trading days after a triggering event has taken place. A triggering event is one of the following: (i) an Acquiring Person, as defined in the Plan, acquires 20% or more of the common shares of the Company; or (ii) an Acquiring Person announces his intention to make a take-over bid that would result in the person owning 20% or more of the outstanding common shares of the Company. Upon such a triggering event occurring, each Right would separate from the common share and thereafter entitle the holder to purchase common shares at 50% discount to the market price, up to the amount of the \$30 exercise price of the Right.

The Rights will not be separated from the shares if the Acquiring Person makes a Permitted Bid, defined in the Plan to mean a bid made pursuant to a take-over bid circular to all shareholders of the Company, which has a minimum deposit period of at least 60 days and pursuant to which not less than 50% of the common shares, other than those held by the Acquiring Person, are deposited and not withdrawn.

10. STOCK OPTIONS

The Company has a stock option plan which authorizes the board of directors to grant incentive stock options to directors, officers and employees whereby the maximum number of shares reserved for issuance under the Company's plan is 10,000,000 common shares of which 3,040,493 has been exercised, leaving 6,959,507 common shares available under the Plan of which 5,475,107 incentive stock options are outstanding as at July 31, 2006. The aggregate number of common shares reserved for issuance to any person may not exceed 5% of the number of outstanding common shares. The exercise price of the options will be determined by the fair market value of the shares at the closing price on the date prior to date of the grant. Options granted must be exercised no later than 10 years after the date of grant or such lesser period as may be determined by the Board. The Board may at its discretion in any granting of an option set a vesting period whereby the option may only be exercisable in pre-determined instalments.

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10. STOCK OPTIONS (cont'd...)

Stock option transactions are summarized as follows:

	Number of Shares	Weighted Average Exercise Price
Balance at January 31, 2004	3,089,297	0.18
Granted	2,770,000	0.43
Exercised	(2,185,497)	0.17
Expired	-	-
Forfeited	<u>(1,300,000)</u>	0.41
Balance at January 31, 2005	2,373,800	0.36
Granted	5,573,000	0.53
Exercised	(1,465,600)	0.32
Expired	-	-
Forfeited	<u>(450,000)</u>	0.42
Balance at January 31, 2006	6,031,200	\$ 0.53
Granted	3,730,000	1.14
Exercised	(3,477,693)	0.59
Expired	(400,000)	1.24
Forfeited	(408,400)	0.97
Balance at July 31, 2006	<u>5,475,107</u>	<u>\$ 0.79</u>
Number of stock options exercisable	<u>2,266,287</u>	<u>\$ 0.69</u>

The weighted average fair value of stock options granted and vested during the six months ended July 31, 2006 was \$0.41 (July 31, 2005 - \$0.26) per option.

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10. STOCK OPTIONS (cont'd...)

As at July 31, 2006, the following stock options were outstanding as follows:

Number of Shares Outstanding	Exercise Price	Expiry Date
110,000	\$ 0.50	September 21, 2007
279,407	0.50	April 21, 2010
1,544,700	0.50	July 11, 2010
88,000	0.385	August 23, 2010
66,000	0.50	September 13, 2010
385,000	0.62	October 5, 2010
193,000	1.00	December 31, 2010
131,000	1.00	December 31, 2010
2,478,000	1.05	February 1, 2011
200,000	1.73	April 27, 2011
5,475,107		

Total stock options granted during the six months ended July 31, 2006 are 3,730,000 of which 808,400 were forfeited during the period. Stock options granted that are not vested have been excluded from the calculation of stock-based compensation. Total stock-based compensation recognized for the fair value of stock options granted and vested during the six month period ended July 31, 2006 was \$1,320,047 (July 31, 2005 - \$202,245).

The fair value of stock options granted is estimated using the Black-Scholes option pricing model with the following assumptions:

	Six Months Ended July 31, 2006	Six Months Ended July 31, 2005
Risk-free interest	4.03 – 4.30 %	2.98 %
Expected dividend yield	-	-
Expected stock price volatility	51% - 87%	88%
Expected option life in years	5 years	5 years

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11. SHARE PURCHASE WARRANTS

Share purchase warrant transactions are summarized as follows:

	Number of Shares	Weighted Average Exercise Price
Balance at January 31, 2004	7,799,994	0.25
Issued	-	-
Exercised	(249,498)	0.25
Expired	-	-
Balance at January 31, 2005	7,550,496	0.25
Issued	4,982,835	1.20/1.44
Exercised	(7,550,496)	0.25
Expired	-	-
Balance at January 31, 2006	4,982,835	\$ 1.20/1.44
Issued	-	-
Exercised	(272,171)	1.20
Expired	-	-
Balance at July 31, 2006	4,710,664	\$ 1.20/1.44

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11. SHARE PURCHASE WARRANTS (cont'd...)

As at July 31, 2006, the following share purchase warrants were outstanding and exercisable as follows:

Number of Shares	Exercise Price	Expiry Date
3,951,760	\$ 1.20	December 19, 2006
	then at \$ 1.44	December 19, 2007
758,904	\$ 1.20	January 6, 2007
	then at \$ 1.44	January 6, 2008
4,710,664		

These warrants will terminate within 20 days unless exercised in the event the Company's closing stock price meets or exceeds \$2.00 for 10 consecutive trading days and the Company issues a press release of such an event.

Subsequent to period end, on August 31, 2006, the Company issued a press release thereby triggering September 20, 2006 as the expiry date for the warrants. The Company has received proceeds of \$90,000 from the partial exercise of the warrants between August 31, 2006 and the date of this report.

12. TREASURY STOCK

During the period ended July 31, 2005, the Company sold 500,000 of its shares held in treasury at a price of \$0.65 per share for net proceeds of \$319,985. These shares were previously issued and reacquired at a cost of \$3.79 per share by the Company some years ago pursuant to an issuer bid. The loss of \$1,574,015 resulting from the sale of these shares and related broker fees has been charged to deficit in the period ended July 31, 2005. As at July 31, 2006, 44,200 common shares were held in treasury.

13. RELATED PARTY TRANSACTIONS

During the period ended July 31, 2006:

- The Company paid consulting fees of \$103,603 (July 31, 2005 - \$53,377) to companies controlled by a director, a former director and an officer.
- The Company paid wages and benefits of \$484,303 (July 31, 2005 - \$65,600) to directors.
- The Company received \$7,573 (July 31, 2005 - \$Nil) for rent charges from a company with a common director.
- The Company paid legal fees of \$141,103 (July 31, 2005 - \$Nil) to a law firm controlled by an officer.

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13. RELATED PARTY TRANSACTIONS (cont'd...)

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

14. COMMITMENTS

During the period ended July 31, 2006, the Company entered into a five-year lease for office premises at an estimated annual cost of \$61,112 commencing September 1, 2006. Cancellation of two previous lease obligations was obtained effective May 15, 2006.

On April 20, 2006, the Company entered into an agreement for completion of a Light Detection and Ranging survey of 1.621 square kilometres of Panama, including all of the Company's concession lands with initial filed work scheduled for completion by September 30, 2006. Cost of this survey is estimated at \$919,000 of which \$184,000 has been paid. The balance of \$735,000 is payable over the data gathering and interpretation phases spanning October 2006 through February 2007.

During the period ended July 31, 2006, the Company acquired, through a series of purchase orders, three ball mills for future installation at the Molejon mill site. The cost of these assets was \$1,006,459, of which \$89,928 was paid during the period and the balance of \$916,531 was paid subsequent to the period.

15. FINANCIAL INSTRUMENTS

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

The Company is subject to financial risk arising from fluctuations in foreign currency exchange rates. The Company does not use any derivative instruments or hedging activities to reduce its exposure to fluctuations in foreign currency exchange rates.

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16. SUPPLEMENTAL DISCLOSURE WITH RESPECT TO CASH FLOWS

	Six months ended July 31, 2006	Six months ended July 31, 2005
Investment in mineral properties - cash	\$ 5,232,763	898,922
Investment in mineral properties – non-cash	758,311	-
	<u>\$ 5,991,074</u>	<u>898,922</u>

	July 31, 2006	January 31, 2006
Cash and cash equivalents consist of:		
Cash	\$ 1,115,523	\$ 1,420,258
Term deposits	1,102,247	7,751,060
	<u>2,217,770</u>	<u>9,171,318</u>

17. SUBSEQUENT EVENTS

Subsequent to July 31, 2006:

- The Company issued 1,439,215 shares on the exercise of stock options and warrants for proceeds of \$1,663,338.
- On August 30, 2006, the Company amended the terms of a July 20, 2006 private placement offering to consist of up to 9,400,000 units at a price of \$2.40 per unit for gross proceeds in the amount of \$22,560,000 (the "Offering"). The private placement is subject to regulatory approval and the satisfaction of other customary conditions.

Each unit will consist of one common share and one transferable share purchase warrant, where each warrant entitles the holder to purchase an additional common share of the Company for a period of five years at a price of \$3.00 per share.

The closing of the Offering is scheduled to occur prior to the "Effective Date" of the Plan of Arrangement between the Company and Petaquilla Copper Ltd. ("Copper") approved by the shareholders of the Company on June 6, 2006, and by the Supreme Court of British Columbia on June 19, 2006.

The warrants will contain customary anti-dilution provisions and will be transferable in accordance with the applicable legislation.

The proceeds of the private placement will be used as to \$17,560,000 on the advancement of the Company's Molejon Gold Project in Panama, to pay the expenses of the Offering and for working capital, with the remaining \$5,000,000 being invested in common shares of Copper.

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17. SUBSEQUENT EVENTS (cont'd...)

Finders' fees in the form of compensation warrants and cash will be paid in connection with the private placement.

The Company received proceeds of \$960,000 from the private placement between August 31, 2006 and the date of this report.

- c) The Company completed the acquisition of three ball mills for future installation on the Molejon mill site. Total cost of these assets was \$1,006,459 which has been paid.
- d) On August 31, 2006, the Company issued a press release thereby triggering September 20, 2006 as the expiry date for the warrants. The Company has received proceeds of \$90,000 from the partial exercise of the warrants between August 31, 2006 and the date of this report.
- e) On September 5, 2006 additional 5 Year Stock Options were granted on 1,693,425 shares at an exercise price of \$ 2.72 per share, subject to regulatory and shareholder approvals..