

**RARE ELEMENT RESOURCES LTD.**  
CONSOLIDATED FINANCIAL STATEMENTS  
For the six months ended December 31, 2007  
(UNAUDITED)

**RARE ELEMENT RESOURCES 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 standards established by the Canadian Institute of Chartered Accountants for a review of interim financial statements by an entity's auditor.

**RARE ELEMENT RESOURCES LTD.**  
**CONSOLIDATED BALANCE SHEETS**  
*(Expressed in US Dollars)*

	<b>December 31 2007</b>	<b>June 30 2007</b>
	<b>(Unaudited)</b>	<b>(Audited)</b>
<b>ASSETS</b>		
<b>CURRENT</b>		
Cash	\$ 2,171,452	\$ 1,085,337
Accounts receivable	19,947	44,428
Prepaid expenses	30,538	49,651
	2,221,937	1,179,416
<b>Equipment</b> (Note 4)	6,268	673
<b>Investment</b> (Note 5)	15,083	15,083
<b>Mineral properties and deferred exploration costs</b> (Note 3)	929,415	764,147
<b>Reclamation bond</b> (Note 6)	10,000	10,000
	\$ 3,182,703	\$ 1,969,319
<b>LIABILITIES</b>		
<b>CURRENT</b>		
Accounts payable and accrued liabilities	\$ 13,192	\$ 16,456
Due to related parties (Note 8)	15,853	8,257
	29,045	24,713
<b>SHAREHOLDERS' EQUITY</b>		
<b>SHARE CAPITAL</b> (Note 7)	6,407,896	4,973,386
<b>CONTRIBUTED SURPLUS</b> (Note 7)	278,704	240,729
<b>DEFICIT</b>	(3,532,942)	(3,269,509)
	3,153,658	1,944,606
	\$ 3,182,703	\$ 1,969,319
<b>CONTINUANCE OF OPERATIONS</b> (Note 1)		
<b>SUBSEQUENT EVENTS</b> (Note 11)		

APPROVED BY THE BOARD OF DIRECTORS:

*“Donald E. Ranta”*

\_\_\_\_\_  
Donald E. Ranta

*“Mark T. Brown”*

\_\_\_\_\_  
Mark T. Brown

See accompanying notes to consolidated financial statements

**RARE ELEMENT RESOURCES LTD.**  
**CONSOLIDATED STATEMENTS OF OPERATIONS AND DEFICIT**  
*(Expressed in US Dollars)*  
**(Unaudited)**

	<b>For the three months ended</b>		<b>For the six months ended</b>	
	<b>December 31</b>		<b>December 31</b>	
	<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
<b>EXPENSES</b>				
Audit and legal	\$ 4,174	\$ 9,918	\$ 6,491	\$ 10,636
Accounting and administrative fees (Note 8)	22,214	17,792	48,784	45,744
Amortization	-	64	83	64
Bank charges	677	253	823	640
Foreign-exchange loss (gain)	39,669	49,282	(152,581)	52,752
Investor relations and shareholder communication	58,805	74,271	78,723	142,057
Management fees (Note 8)	53,320	19,133	73,391	37,193
Office and miscellaneous	11,619	8,514	18,827	16,203
Rent (Note 8)	2,298	2,050	4,448	3,985
Stock-based compensation	65,369	106,247	155,698	194,982
Transfer and listing fees	17,180	13,732	19,303	21,229
Travel	14,712	8,565	16,856	11,694
	<u>290,037</u>	<u>309,821</u>	<u>270,846</u>	<u>537,179</u>
Interest income	<u>7,413</u>	<u>-</u>	<u>7,413</u>	<u>-</u>
<b>NET LOSS FOR THE PERIOD</b>	(282,624)	(309,821)	(263,433)	(537,179)
<b>DEFICIT, BEGINNING OF PERIOD</b>	<u>(3,250,318)</u>	<u>(2,745,371)</u>	<u>(3,269,509)</u>	<u>(2,518,013)</u>
<b>DEFICIT, END OF PERIOD</b>	<u>\$ (3,532,942)</u>	<u>\$ (3,055,192)</u>	<u>\$ (3,532,942)</u>	<u>\$ (3,055,192)</u>
<b>LOSS PER SHARE – BASIC AND DILUTED</b>	<u>\$ (0.01)</u>	<u>\$ (0.01)</u>	<u>\$ (0.01)</u>	<u>\$ (0.03)</u>
<b>WEIGHTED AVERAGE NUMBER OF SHARES OUTSTANDING</b>	<u>22,746,328</u>	<u>20,788,751</u>	<u>22,356,156</u>	<u>19,672,588</u>

See accompanying notes to consolidated financial statements

**RARE ELEMENT RESOURCES LTD.**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
*(Expressed in US Dollars)*  
**(Unaudited)**

	<b>For the three months ended</b>		<b>For the six months ended</b>	
	<b>December 31</b>		<b>December 31</b>	
	<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
<b>CASH PROVIDED BY (USED IN) OPERATIONS</b>				
Net loss for the period	\$ (282,624)	\$ (309,821)	\$ (263,433)	\$ (537,179)
Items not involving cash:				
Amortization	-	64	83	64
Stock-based compensation	65,369	106,247	155,698	194,982
	(217,255)	(203,510)	(107,652)	(342,133)
Changes in non-cash working-capital items:				
Accounts receivable	11,846	(6,963)	24,481	10,686
Prepaid expenses	27,966	12,636	19,113	12,050
Accounts payable and accrued liabilities	(30,653)	(3,231)	(3,264)	(13,279)
Due to related parties	14,886	12,420	7,596	2,864
	(193,210)	(188,648)	(59,726)	(329,812)
<b>INVESTING ACTIVITIES</b>				
Deferred exploration costs	(162,936)	(12,984)	(165,268)	(49,043)
Purchase of equipment	(5,678)	-	(5,678)	(868)
	(168,614)	(12,984)	(170,946)	(49,911)
<b>FINANCING ACTIVITIES</b>				
Cash received for common shares	1,186,430	197,950	1,332,303	1,169,367
Share issue costs	(15,516)	-	(15,516)	-
	1,170,914	197,950	1,316,787	1,169,367
<b>INCREASE (DECREASE) IN CASH</b>	<b>809,090</b>	<b>(3,682)</b>	<b>1,086,115</b>	<b>789,644</b>
<b>CASH, BEGINNING OF PERIOD</b>	<b>1,362,362</b>	<b>1,221,593</b>	<b>1,085,337</b>	<b>428,267</b>
<b>CASH, END OF PERIOD</b>	<b>\$ 2,171,452</b>	<b>\$ 1,217,911</b>	<b>\$ 2,171,452</b>	<b>\$ 1,217,911</b>

See accompanying notes to consolidated financial statements

**RARE ELEMENT RESOURCES LTD.**  
**CUMULATIVE SCHEDULE OF MINERAL PROPERTY COSTS**  
*(Expressed in US Dollars)*

	Balance June 30, 2006	Expenditures for the year	Balance June 30, 2007	Expenditures for the period	Balance December 31, 2007
	(Audited)		(Audited)		(Unaudited)
<b>Bear Lodge Property</b>					
Property acquisition costs	\$ 17,721	\$ -	\$ 17,721	\$ -	\$ 17,721
Exploration expenditures					
Assays	7,637	114	7,751	2,310	10,061
Assessments and taxes	20,104	-	20,104	-	20,104
Drilling	250,409	73,513	323,922	136,038	459,960
Geological consulting	121,983	46,785	168,768	26,030	194,798
Geophysical	300	-	300	-	300
Metallurgical testing	-	38,530	38,530	-	38,530
Overhead expenses	8,489	1,190	9,679	810	10,489
Staking	17,949	-	17,949	-	17,949
Survey	34,338	-	34,338	-	34,338
Travel expenses	23,935	-	23,935	80	24,015
Wages	99,734	-	99,734	-	99,734
Total exploration expenditures on Bear Lodge property	602,599	160,132	762,731	165,268	927,999
<b>Kipawa Property</b>					
Exploration expenditures					
Geological consulting	4,949	-	4,949	-	4,949
Staking	1,308	-	1,308	-	1,308
Write-down of property	-	(4,841)	(4,841)	-	(4,841)
Total exploration expenditures on Kipawa property	6,257	(4,841)	1,416	-	1,416
<b>TOTAL EXPENDITURES</b>	<b>\$ 608,856</b>	<b>\$ 155,291</b>	<b>\$ 764,147</b>	<b>\$ 165,268</b>	<b>\$ 929,415</b>

See accompanying notes to consolidated financial statements

**RARE ELEMENT RESOURCES LTD.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

December 31, 2007  
*(Expressed in US Dollars)*  
*(Unaudited)*

**1. NATURE OF OPERATIONS**

Rare Element Resources Ltd. (“Rare Element” or “the Company”) was incorporated under the laws of the Province of British Columbia on June 3, 1999.

These consolidated 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 continuing operations of the Company are dependent upon its ability to continue to raise adequate financing and to commence profitable operations in the future.

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**Interim financial statements**

These interim consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles and follow the same accounting policies and methods of application as the annual financial statements. These interim consolidated financial statements do not include in all respects the annual disclosure requirements of generally accepted accounting principles and should be read in conjunction with the most recent annual statements.

**Basis of presentation and principles of consolidation**

These consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles and are inclusive of the accounts of the Company and Paso Rico Resources Ltd. (“Paso Rico”), together with those of Paso Rico’s wholly-owned subsidiaries, Minera Santa Regina, S.A. de C.V., Compania Minera Real de las Lomas, S.A. de C.V. and Paso Rico (USA), Inc. The Company is in the process of winding down the two Mexican companies.

**Use of estimates**

The preparation of these consolidated financial statements requires the use of 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 consolidated financial statements, and the reported amounts of revenues and expenses during the reported period. Actual results could differ from these estimates.

**Foreign currency translation**

The Company’s reporting currency is the US Dollar. The Company’s Canadian operations are considered to be integrated with foreign currency transactions translated into US Dollars as follows:

- monetary assets and liabilities at the rates of exchange prevailing at the balance sheet dates;
  - other assets and liabilities at the applicable historical exchange rates;
  - revenues and expenses at the average rates of exchange for the period, and;
  - gains and losses arising from the conversion of foreign-currency balances and transactions are reported in income as they occur.
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**RARE ELEMENT RESOURCES LTD.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

December 31, 2007  
*(Expressed in US Dollars)*  
*(Unaudited)*

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, Continued**

**Mineral properties and deferred exploration costs**

The cost of mineral properties and related exploration expenditures are deferred until the properties are placed into production, sold or abandoned. These deferred costs will be amortized over the estimated useful life of the properties following the commencement of production, or written-off if the properties, allowed to lapse, or abandoned.

Cost includes the cash consideration and the fair market value of shares issued for the acquisition of mineral properties. Properties acquired under option agreements are recorded in the accounts at such time as payments are made. Proceeds from options granted are applied to the cost of the related property and any excess is included in income for the period.

The recorded amounts of mineral claim acquisition costs and their related deferred exploration costs represent actual expenditures incurred and are not intended to reflect present or future values.

The Company reviews capitalized costs on its mineral properties periodically and will recognize an impairment in value based upon current exploration results and upon management's assessment of the future probability of profitable revenues from the property or from the sale of the property. Management's assessment of a property's estimated current fair market value may also be based upon a review of other property transactions that have occurred in the same geographic area as that of the property under review.

**Amortization**

The Company provides for amortization on its computer equipment at 45% and software at 100% declining balance (one-half of the rate is taken in the year of acquisition and disposition).

**Income taxes**

The Company accounts for, and measures future tax assets and liabilities in accordance with the liability method, where future income-tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amount of existing assets and liabilities and their respective tax bases. Future tax assets and liabilities are measured using enacted or substantively enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on future tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the date of enactment or substantive enactment of the change. When the future realization of income tax assets does not meet the test of being more likely than not to occur, a valuation allowance in the amount of the future benefit is taken and no asset is recognized. Such an allowance applies fully to all potential income tax assets of the Company.

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**RARE ELEMENT RESOURCES LTD.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

December 31, 2007  
*(Expressed in US Dollars)*  
*(Unaudited)*

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, Continued**

**Loss per share**

The loss per share is computed using the weighted average number of shares outstanding during the period. Diluted loss per share is not presented as the effect on the basic loss per share would be anti-dilutive.

**Comparative figures**

Certain of the prior period's figures have been reclassified to conform with the current period's financial statement presentation.

**Stock-based compensation**

The Company recognizes compensation expense for all stock options granted using the fair value based method of accounting. Any cash paid on the exercise of stock options is added to the stated value of common shares.

**Asset retirement obligations**

The Company recognizes a liability for an asset retirement obligation when it is determinable and calculates the liability based upon undiscounted future payments. A corresponding amount is added to the carrying amount of the related long-lived asset, and this amount is subsequently allocated to expenses over its expected life. Adjustments will also be made in subsequent periods to changes in asset retirement obligations due to changes in estimates. As at December 31, 2007, the Company did not have any asset retirement obligations.

**Retirement of long-lived assets**

Long-lived assets are assessed for impairment when events and circumstances warrant, when the carrying amounts of the assets exceeds its estimated undiscounted net cash flow from use or its fair value, at which time the impairment is charged to earnings.

**RARE ELEMENT RESOURCES LTD.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

December 31, 2007  
*(Expressed in US Dollars)*  
*(Unaudited)*

**2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES, Continued**

**New Accounting Policies**

Effective July 1, 2007, the Company adopted the new recommendations of the Canadian Institute of Chartered Accountants (CICA) Handbook Section 1530, Comprehensive Income; Section 3251, Equity; Section 3855, Financial Instruments - Recognition and Measurement; and Section 3865, Hedges, retroactively without restatement. These new Handbook Sections, which apply to fiscal years beginning on or after October 1, 2006, provide requirements for the recognition and measurement of financial instruments and on the use of hedge accounting. Section 1530 establishes standards for reporting and presenting comprehensive income, which is defined as the change in equity from transactions and other events from non-owner sources. Other comprehensive income refers to items recognized in comprehensive income that are excluded from net income calculated in accordance with generally accepted accounting principles. Under the new standards, policies followed for periods prior to the effective date generally are not reversed and therefore, the comparative figures have not been restated. The adoption of these Handbook Sections had no impact on opening deficit.

Under Section 3855, financial instruments must be classified into one of the following five categories: held-for-trading, held-to-maturity, loans and receivables, available-for-sale financial assets or other financial liabilities. All financial instruments, including derivatives, are measured in the balance sheet at fair value except for loans and receivables, held-to-maturity investments and other financial liabilities which are measured at amortized cost. Subsequent measurement and changes in fair value will depend on their initial classification, as follows: held-for-trading, financial assets are measured at fair value and changes in fair value are recognized in net income; available-for-sale financial instruments are measured at fair value with changes in fair value recorded in other comprehensive income until the investment is derecognized or impaired at which time the amounts would be recorded in net income.

Upon adoption of these new standards, the Company designated its cash and cash equivalents as held-for-trading, which are measured at fair value. Accounts receivable and income taxes receivable are classified as loans and receivables, which are measured at amortized cost. Accounts payable, accrued liabilities, due to/from related parties and joint venture partners are classified as other financial liabilities. The Company had neither available-for-sale, nor held-to-maturity instruments during the six months ended December 31, 2007.

The Company had no "other comprehensive income or loss" transactions during the six months ended December 31, 2007 and no opening or closing balances for accumulated other comprehensive income or loss.

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**RARE ELEMENT RESOURCES LTD.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

December 31, 2007  
(Expressed in US Dollars)  
(Unaudited)

**3. MINERAL PROPERTIES AND DEFERRED EXPLORATION COSTS**

The amounts shown represent costs incurred to date, and do not necessarily represent present or future values as they are entirely dependent upon the economic recovery of future ore reserves. A breakdown of carrying values by period is as follows:

	December 31 2007	June 30 2007
Bear Lodge Property	\$ 927,999	\$ 762,731
Kipawa Property	1,416	1,416
	<u>\$ 929,415</u>	<u>\$ 764,147</u>

**Bear Lodge Property**

The Company, through its wholly owned subsidiary, Paso Rico (USA), Inc., holds a 100% interest in a group of unpatented mineral claims, known as the Bear Lodge Property. The property is situated in the Bear Lodge Mountains of northeast Wyoming. These claims were, in part, acquired from Phelps Dodge Exploration Company ("Phelps Dodge") by way of a "Mineral Lease and Option for Deed". Some of the claims and a portion of a defined area of influence surrounding the claims are subject to a production royalty of 2% of Net Smelter Returns ("NSR") payable to Phelps Dodge. Paso Rico (USA), Inc. owns a portion of the claim group outright and these claims are not subject to the NSR.

In September 2005, the Company staked 20 additional claims at the property. The property now comprises 90 federal unpatented mineral claims and a 640-acre Wyoming state lease for a total of approximately 2,100 acres.

On June 1, 2006, Paso Rico (USA), Inc. and Newmont North America Exploration Limited ("Newmont"), a subsidiary of Newmont Mining Corporation, signed an agreement to establish a gold-exploration venture on the Company's Bear Lodge, Wyoming property ("Venture"). Under the term sheet, Newmont has the right to earn a 65% participating interest in the Bear Lodge property, excluding any rights to the rare-earth elements and uranium, but including rights to gold and other metals, if Newmont spends \$5 million on property exploration by 2011.

Newmont also has the right to earn an additional 15% participating interest by completing a positive feasibility study. If the Company's interest is reduced to 20% for any reason, the Company shall have a financing option by which it may elect for Newmont to carry the Company's share of Venture expenditures, without further dilution to the Company, until commencement of mining on the property. The funds advanced by Newmont under the financing option, plus interest at LIBOR plus 3%, shall be recouped from 90% of the Company's portion of the proceeds from production.

Newmont staked an additional 116 Federal lode mineral claims, which are included as part of the Venture's property.

**RARE ELEMENT RESOURCES LTD.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

December 31, 2007  
(Expressed in US Dollars)  
(Unaudited)

**3. MINERAL PROPERTIES AND DEFERRED EXPLORATION COSTS, Continued**

**Bear Lodge Property, Continued**

Newmont is the operator of the gold-exploration program. The Company will continue to operate its rare-earth-element exploration program; however, if the two exploration programs conflict, the Venture, under Newmont, may choose to operate both programs.

All claims are located on federal lands and are subject to annual maintenance fees payable to the United States Bureau of Land Management. These fees are now paid by Newmont as long as the Newmont agreement remains in effect.

**Kipawa Property**

In April 2006, the Company acquired by staking 26 claims, totaling approximately 1,531 hectares. The property is located in Quebec, 90 km northwest of North Bay, Ontario. The Company wrote off \$4,841 in fiscal 2007 in light of the sale of the property. On October 12, 2007, the Company sold the property for \$1,500 CDN (\$1,416) (subsequently received, Note 11).

**4. EQUIPMENT**

	December 31 2007	June 30 2007
Computer equipment	\$ 5,211	\$ 864
Software	1,331	-
Accumulated amortization	(274)	(191)
Net book value	<u>\$ 6,268</u>	<u>\$ 673</u>

**5. INVESTMENT**

During fiscal 2007, the Company sold to Almaden Minerals Ltd. ("Almaden") its 2% Net Smelter Return royalty ("NSR") on a Mexican property which has been previously written off by the Company. The NSR was sold for \$20,000 and 25,000 Almaden warrants exercisable at a price of \$3.00 CDN until March 20, 2010. A fair value of \$15,083 was assigned to these warrants and was estimated using the Black-Scholes Option Pricing Model based on the following assumptions: A risk free interest rate of 3.98%, a volatility rate of 52.42% and an expected time to exercise of 3 years.

Almaden has a common officer with the Company.

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**RARE ELEMENT RESOURCES LTD.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

December 31, 2007  
*(Expressed in US Dollars)*  
*(Unaudited)*

**6. RECLAMATION BOND**

The Company was required to post a reclamation bond which covers the cost to reclaim the ground disturbed during its exploration programs at the Bear Lodge Property. On July 23, 2004, \$10,000 was transferred to the Wyoming Department of Environmental Quality for the bond required to cover the exploration program. The Company must complete certain reclamation work for these funds to be released, but may leave the bond in place for future exploration programs, even if such work is completed.

In August 2006, an additional bond of \$10,000 was set up in the name of Paso Rico (USA), Inc., but it was paid by Newmont and covers Newmont's gold-exploration reclamation work. It will revert to Newmont, if and when Newmont completes its reclamation.

**7. SHARE CAPITAL**

Authorized – unlimited number of common shares without par value.

Issued and outstanding:	Number of Shares	Amount	Contributed Surplus
Balance as at June 30, 2006	18,273,425	\$ 3,463,293	\$ 116,579
Issued for cash:			
Private placement (Note 7a)	1,666,698	897,917	-
Exercise of warrants (Notes 7a and b)	1,076,766	337,550	-
Exercise of options (Note 7c)	687,500	158,634	-
Fair value of the options exercised	-	115,992	(115,992)
Stock-based compensation	-	-	240,142
Balance as at June 30, 2007	21,704,389	4,973,386	240,729
Issued for cash:			
Private placement (Note 7e)	1,075,000	1,150,358	-
Exercise of warrants (Note 7a)	46,667	34,595	-
Exercise of options (Note 7d)	356,500	147,350	-
Fair value of the options exercised	-	117,723	(117,723)
Share issue costs	-	(15,516)	-
Stock-based compensation	-	-	155,698
Balance as at December 31, 2007	23,182,556	\$ 6,407,896	\$ 278,704

- (a) During the year ended June 30, 2007, the Company closed a non-brokered private placement of 1,666,698 units at \$0.60 CDN per unit for gross proceeds of \$897,917 (\$1,000,021 CDN). Each unit comprises one common share and one-half of a non-transferable share purchase warrant. A whole warrant may be exercised to purchase one additional common share of the Company at \$0.75 CDN per share until March 22, 2008. 129,166 of these warrants were exercised during fiscal 2007, and 46,667 warrants were exercised in the period ended December 31, 2007.

**RARE ELEMENT RESOURCES LTD.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

December 31, 2007  
*(Expressed in US Dollars)*  
*(Unaudited)*

**7. SHARE CAPITAL, Continued**

- (b) During the year ended June 30, 2007, 947,600 warrants were exercised at \$0.30 CDN.
- (c) During the year ended June 30, 2007, a total of 687,500 options at prices ranging from \$0.20 CDN to \$0.55 CDN were exercised. A fair value of \$115,992 was recognized on these exercised options.
- (d) During the period ended December 31, 2007, a total of 356,500 options at prices ranging from \$0.25 CDN to \$0.55 CDN were exercised. A fair value of \$117,723 was recognized on these exercised options.
- (e) On November 5, 2007, the Company completed a non-brokered private placement for \$1,075,000 CDN. The offering consists of 1,075,000 units at \$1.00 CDN per unit. Each unit comprises one common share and one-half of a non-transferable share-purchase warrant. A whole warrant may be exercised to purchase one additional common share of the Company at \$1.35 CDN per share until May 5, 2009.

**Stock Options**

The following table summarizes the Company's stock option activity:

	Number of Shares	Weighted Average Exercise Price (CDN\$)
Outstanding, June 30, 2006	2,580,000	0.37
Granted	440,000	0.55
Cancelled	(250,000)	0.55
Exercised	(687,500)	0.26
Outstanding, June 30, 2007	2,082,500	0.42
Granted	725,000	1.00
Exercised	(356,500)	0.42
Outstanding, December 31, 2007	2,451,000	0.60

At December 31, 2007, the following options were outstanding:

Expiry Date	Number of Options	Exercise Price (CDN\$)
October 31, 2008*	770,000	0.35
July 24, 2010	200,000	0.25
April 28, 2011	350,000	0.55
January 10, 2012**	406,000	0.55
September 1, 2012	350,000	1.00
October 12, 2012	350,000	1.00
October 15, 2012	25,000	1.00
	2,451,000	

\* Subsequently, 10,000 of these options were exercised.

\*\* Subsequently, 10,000 of these options were exercised.

**RARE ELEMENT RESOURCES LTD.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

December 31, 2007  
*(Expressed in US Dollars)*  
*(Unaudited)*

**7. SHARE CAPITAL, Continued**

**Stock-based compensation**

The fair value of options reported as compensation expense has been estimated using the Black-Scholes Option Pricing Model using the following assumptions:

Risk-free interest rate	4.08%
Annualized volatility	88%
Expected dividend yield	Nil
Expected option life in years	4 years

Based on these variables, stock-based compensation expense for the options vested during the period ended December 31, 2007 was \$155,698 (2006 – \$194,982).

Option pricing models require the input of highly subjective assumptions, particularly as to the expected price volatility of the stock. Changes in these assumptions can materially affect fair value estimates and, therefore, it is management's view that the existing models do not necessarily provide a single reliable measure of the fair value of the Company's stock-option grants.

**Warrants**

The following table summarizes the Company's warrant activity:

	Number of Shares	Weighted Average Exercise Price (CDN\$)
Outstanding, June 30, 2006	947,600	0.30
Exercised	(1,076,766)	0.35
Granted	833,349	0.75
Outstanding, June 30, 2007	704,183	0.75
Exercised	(46,667)	0.75
Granted	537,500	1.35
Outstanding, December 31, 2007	1,195,016	1.02

At December 31, 2007, the following warrants were outstanding:

Expiry Date	Number of Warrants	Exercise Price (CDN\$)
March 22, 2008*	657,516	0.75
May 5, 2009	537,500	1.35
	1,195,016	

\* Subsequently, 20,000 of these warrants were exercised.

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*(Expressed in US Dollars)*  
*(Unaudited)*

**8. RELATED PARTY TRANSACTIONS**

During the six months ended December 31, 2007, \$47,891 (2006 - \$37,193) was charged for management fees by a private company controlled by the former president. As at December 31, 2007, \$Nil (June 30, 2007 - \$Nil) was owed to this private company.

During the six months ended December 31, 2007, \$25,500 (2006 - \$Nil) was charged for management fees by the president. As at December 31, 2007, \$8,500 (June 30, 2007 - \$Nil) was owed.

During the six months ended December 31, 2007, \$53,232 (2006 - \$49,729) was charged by a private company controlled by one of the directors for accounting, administrative fees and rent. As at December 31, 2007, \$7,353 (June 30, 2007 - \$8,257) was owed to this private company.

Related party transactions are measured at the fair value amount as determined by management. The amounts bear no interest and are unsecured with no repayment terms.

**9. COMMITMENTS AND CONTINGENCIES**

**Potential environmental contingency**

The Company's mining and exploration activities are subject to various federal, provincial and state laws and regulations governing the protection of the environment. These laws and regulations are continually changing and generally becoming more restrictive. The Company conducts its operations so as to protect public health and the environment, and believes its operations are materially in compliance with all applicable laws and regulations. The Company has made, and expects to make in the future, expenditures to comply with such laws and regulations. The ultimate amount of reclamation and other future site-restoration costs to be incurred for existing mining interests is uncertain.

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**10. SEGMENTED INFORMATION**

The Company operates in a single reportable operating segment, being exploration and development of mineral properties.

Summarized financial information for the geographic segments the Company operates in are as follows:

	Canada	United States	Total
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<u>As at December 31, 2007</u>			
Assets	\$ 2,229,620	\$ 953,083	\$ 3,182,703
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<u>As at June 30, 2007</u>			
Assets	\$ 1,156,505	\$ 812,814	\$ 1,969,319
<hr/>			
	Canada	United States	Total
<hr/>			
<u>For the six months ended</u> <u>December 31, 2007</u>			
Loss for the period	\$ (262,629)	\$ ( 804)	\$ (263,433)
Capital expenditures	\$ 5,678	\$ 165,268	\$ 170,946
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<u>For the six months ended</u> <u>December 31, 2006</u>			
Loss for the period	\$ (536,889)	\$ (290)	\$ (537,179)
Capital expenditures	\$ 868	\$ 49,403	\$ 49,911
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**11. SUBSEQUENT EVENT**

In January 2008, the Company received \$1,500 CDN for the sale of Kipawa property.