KEY ENERGY SERVICES INC
Form 8-K
May 19, 2010

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 8-K

CURRENT REPORT
Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

Date of Report (Date of earliest event reported): May 19, 2010 (May 13, 2010)

KEY ENERGY SERVICES, INC.
(Exact name of registrant as specified in its charter)

Maryland	**001-08038**	**04-2648081**
(State or other Jurisdiction of Incorporation)	(Commission File Number)	(IRS Employer Identification No.)

1301 McKinney Street, Suite 1800	
Houston, Texas	**77010**
(Address of Principal Executive Offices)	(Zip Code)

Registrant's telephone number, including area code: **713/651-4300**

(Former name or former address if changed since last report.)
Check the appropriate box below if the Form 8-K filing is intended to simultaneously satisfy the filing obligation of the registrant under any of the following provisions:

o Written communications pursuant to Rule 425 under the Securities Act (17 CFR 230.425)

o Soliciting material pursuant to Rule 14a-12 under the Exchange Act (17 CFR 240.14a-12)

o Pre-commencement communications pursuant to Rule 14d-2(b) under the Exchange Act (17 CFR 240.14d-2(b))

o Pre-commencement communications pursuant to Rule 13e-4(c) under the Exchange Act (17 CFR 240.13e-4(c))

Item 1.01. Entry into a Material Definitive Agreement.

Key Energy Services, Inc., a Maryland corporation (the "Company"), sold its marine well service barges and related assets, along with certain other ancillary assets, for cash consideration of $17.9 million pursuant to an Asset Purchase Agreement (the "APA"), dated and effective as of May 13, 2010, by and among Key Energy Services, LLC, a Texas limited liability company, and Key Marine Services, LLC, a Delaware limited liability company (both wholly-owned subsidiaries of the Company), as seller, Moncla Companies, L.L.C., a Texas limited liability company, and Moncla Marine, L.L.C., a Louisiana limited liability company (collectively, "Purchaser"), L. Charles Moncla, Jr., Moncla Family Partnership, Ltd., L. Charles Moncla, Jr. Charitable Remainder Trust, Michael Moncla, Matthew Moncla, Marc Moncla, Christopher Moncla, Bipin A. Pandya, Thomas Sandahl, Rhonda Moncla, Cain Moncla, Andrew Moncla, and Kenneth Rothstein (collectively, the "Original Sellers"), Second 4 M Ltd., a Texas limited partnership, and Leon Charles Moncla, Jr., as payment agent for the Original Sellers.

Substantially all of the marine well service assets sold to the Purchaser under the APA were originally acquired by the Company pursuant to a Stock and Membership Interest Purchase Agreement, dated as of September 19, 2007 (as amended, the "2007 Agreement"), between and among a wholly-owned subsidiary of the Company, the Original Sellers, Moncla Well Service, Inc. and certain other affiliated companies named therein. In connection with the 2007 Agreement, the Company employed some of the Original Sellers, one of whom continues to be employed with the Company. The business acquired under the 2007 Agreement included land-based well service rigs, marine well service barges and ancillary equipment operated in the southeastern United States. The Company retained its land-based well service rig assets originally acquired under the 2007 Agreement.

The marine well service barges sold under the APA contributed approximately 1.2% of the Company's total U.S. rig hours during 2009, and approximately 2.0% of the of the Company's total U.S. rig hours during the first quarter of 2010.

The foregoing description of the APA and the 2007 Agreement does not purport to be complete and is qualified in its entirety by reference to (i) the APA filed as Exhibit 10.1 to this Current Report on Form 8-K and incorporated into this Item 1.01 by reference; (ii) the 2007 Agreement filed as Exhibit 10.1 of the Company's Current Report on Form 8-K filed on September 20, 2007 and incorporated into this Item 1.01 by reference; (iii) the First Amendment to the 2007 Agreement filed as Exhibit 10.3 to the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2007 and incorporated into this Item 1.01 by reference; and (iv) the Second Amendment to the 2007 Agreement filed as Exhibit 10.31 to the Company's Annual Report on Form 10-K for the year ended December 31, 2008 and incorporated into this Item 1.01 by reference.

Item 9.01. Financial Statements and Exhibits

(d) Exhibits.

10.1 Asset Purchase Agreement, dated May 13, 2010, by and among Key Energy Services, LLC, a Texas limited liability company, Key Marine Services, LLC, a Delaware limited liability company, Moncla Companies, L.L.C., a Texas limited liability company, and Moncla Marine, L.L.C., a Louisiana limited liability company, L. Charles Moncla, Jr., Moncla Family Partnership, Ltd., L. Charles Moncla, Jr. Charitable Remainder Trust, Michael Moncla, Matthew Moncla, Marc Moncla, Christopher Moncla, Bipin A. Pandya, Thomas Sandahl, Rhonda Moncla, Cain Moncla, Andrew Moncla, Kenneth Rothstein, Second 4 M Ltd., a Texas limited partnership, and Leon Charles Moncla, Jr., as payment agent.

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SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned hereunto duly authorized.

KEY ENERGY SERVICES, INC.

Date: May 19, 2010

By: /s/ Kimberly R. Frye

Kimberly R. Frye
Senior Vice President and General Counsel

Exhibit Index

Exhibit No.	Description
10.1	Asset Purchase Agreement, dated May 13, 2010, by and among Key Energy Services, LLC, a Texas limited liability company, Key Marine Services, LLC, a Delaware limited liability company, Moncla Companies, L.L.C., a Texas limited liability company, and Moncla Marine, L.L.C., a Louisiana limited liability company, L. Charles Moncla, Jr., Moncla Family Partnership, Ltd., L. Charles Moncla, Jr. Charitable Remainder Trust, Michael Moncla, Matthew Moncla, Marc Moncla, Christopher Moncla, Bipin A. Pandya, Thomas Sandahl, Rhonda Moncla, Cain Moncla, Andrew Moncla, Kenneth Rothstein, Second 4 M Ltd., a Texas limited partnership, and Leon Charles Moncla, Jr., as payment agent.

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Balance – December 31, 2001 (unaudited)

93,567,608

149,183

10,987,798

(8,940,174

)

2,196,807

Issuance of common stock and warrants for cash

156,800

250

49,750

-

50,000

Exercise of stock options and warrants

156,800

250

22,750

-

23,000

Issuance of common stock not previously recognized

31,360

50

(50
)

-

-

Net (loss) for the year ended December 31, 2002

-

-

-

(2,224,775
)

(2,224,775
)

Balance – December 31, 2002 (unaudited)

93,912,568

149,733

11,060,248

(11,164,949
)

45,032

Issuance of common stock and warrants for cash

3,606,400

5,750

604,250

610,000

Exercise of stock options and warrants

3,333,568

5,315

157,685

163,000

Modifications of options and warrants

-

-

1,506,427

1,506,427

Issuance of common stock not previously recognized

156,800

250

(250
)

-

Net (loss) for the year ended December 31, 2003

-

-

-

(2,569,534
)

(2,569,534
)

Balance – December 31, 2003 (unaudited)

101,009,336

$

161,048

$

13,328,360

$

(13,734,483

)

$

(245,075

)

Issuance of common stock and warrants for cash

1,991,360

3,175

254,576

257,751

Loan conversion into stock

54,880

88

6,913

7,000

Issuance of options to non-employees for services

-

-

351,253

-

351,253

Net (loss) for the year ended December 31, 2004

-

-

-

(974,674
)

(974,674
)

Balance – December 31, 2004 (unaudited)

103,055,576

$
164,311

$
13,941,101

$
(14,709,158
)
$
(603,746
)
Issuance of common stock and warrants for cash

2,069,697

3,300

257,692

260,992

Loan conversion into stock

337,904

539

42,561

43,100

Issuance of options to non-employees for services

-

-

303,055

-

303,055

Net (loss) for the year ended December 31, 2005

-

-

-

(760,504
)

(760,504
)

Balance – December 31, 2005

105,463,177

$
168,149

$
14,544,410

$
(15,469,662
)
$
(757,103
)

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Thorium Power, Ltd.
(A Development Stage Company)
Consolidated Statements of Changes in Stockholders' Deficiency (Continued)
From January 8, 1992 (Inception) to December 31, 2006

	Common Stock Shares	Common Stock Amount	Additional Paid-in Capital	Accumulated (Deficit) Accumulated During the Development Stage	Stock Committed Future Issuance	Accumulated Comprehensive Income	Deferred Stock Compensation	Treasury Stock	Stockhold Equity
Balance - December 31, 2005	105,463,177	$ 168,149	$ 14,544,410	$ (15,469,662)	$ 0	$ 0	$ 0	$	$ (757,
Issuance of common stock and warrants for cash	15,319,674	24,426	2,165,248						2,189,
Loan conversion into stock	32,144	51	4,049						4,
Cashless exercise of stock options and warrants	20,385,474	32,502	(32,502)						
Exercise of stock options and warrants for cash	407,680	650	12,350						13,
Issuance of stock for services	627,200	1,000	104,000						105,
Cancellation of shares-held by Thorium Power Ltd (pursuant to merger)	(6,597,495)	(10,506)	10,506						
Recapitalization - 10/6/06 reverse merger*	124,101,637	43,467	(3,035,878)				(306,000)		(3,298,
Extension of investor warrants terms - 6 months			963,387						963,
Stock Option Expense			1,055,648						1,055,
Issuance of stock for services	204,341	205	226,284						226,

Cashless exercise of stock options and warrants	49,333	49	(49)						
Stock issued - settlement expense	307,534	308	91,952						92,
Share issue and merger costs			(441,553)						(441,
Shares retired, redeemed for payroll taxes on stock-based compensation	(3,008,990)	(3,009)	3,009						
Net (loss) for the year ended December 31, 2006				(11,708,327)					(11,708,
Unrealized gains on marketable securities						18,861			18,
Amortization of deferred stock compensation costs							20,800		20,
Allocation of expenses from Thorium Power Ltd.			7,477,700						7,477,
Buyback of stock - 850,000 shares to treasury stock	(850,000)							(255,850)	(255,
Stock based compensation - shares committed for future issuance					1,200,000				1,200,
Balance - December 31, 2006	256,441,709	$ 257,292	$ 23,148,560	$ (27,177,989)	$ 1,200,000	$ 18,861	$ (285,200)	$ (255,850)	$ (3,094,

* See footnote 1 regarding the recapitalization of Thorium Power Inc.

Shares subject to continuing registration rights is shown on the balance sheet as temporary equity, not shareholders deficiency

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

Thorium Power, Ltd.
(A Development Stage Company)
Notes to the Consolidated Financial Statements
December 31, 2006
(Restated)

INTRODUCTORY NOTE

RESTATEMENT OF PREVIOUSLY ISSUED FINANCIAL STATEMENTS

Subsequent to the issuance of the December 31, 2006 and 2005 consolidated financial statements, the Company determined that it needed to restate its 2006 and 2005 financial statements in order to correct earlier disclosures made so that they are in accordance with generally accepted accounting principles. The first item restated was to reclassify the cash flow impact of common stock issue costs, total $441,553 from operating activities to financing activities in the statement of cash flows. This change in the statement of cash flows had no impact on the total net cash flows reported for the periods presented. It was also found that the company needs to change its presentation of the capital stock transactions in the statement of stockholders deficiency from January 8, 1992 (inception) to December 31, 2006. This change was made to reflect the equivalent number of Thorium Power Ltd. shares for each capital transaction, calculated by using the ratio of Thorium Power Ltd shares that were issued in the reverse merger to Thorium Power Inc. stockholders, to the outstanding shares held by the Thorium Power Inc. stockholders at the merger date (10/6/06). This change had no impact on the total number of common shares reported as outstanding as of December 31, 2006 on the statement of stockholders deficiency as well as the balance sheet. A restatement was made to increase the weighted average shares outstanding at December 31, 2006 and 2005. The loss per share reported for the year ended December 31, 2006 decreased from $0.09 to $0.08 per share. Additional footnote disclosures in the financial statements were madeto clarify certain other disclosures. The cumulative financial numbers presented, required to be presented for all development stage companies, from inception (January 8, 1992) to December 31, 2006, reported on the statement of operations and statement of stockholders deficiency are now marked as unaudited, as it was not practicable for us to obtain permission from the prior auditor to reissue their audit report, which was for the periods up to December 31, 2001 and for the cumulative period January 8, 1992 to December 31, 2001.

Accordingly, these accompanying 2006 consolidated financial statements have been restated, for the items mentioned above, from the amounts previously reported. There were no changes on the balance sheet at December 31, 2006 and 2005 and the reported net loss for the years ended December 31, 2006 and 2005.

Thorium Power, Ltd.
(A Development Stage Company)
Notes to the Consolidated Financial Statements
December 31, 2006

1. NATURE OF OPERATIONS AND MERGER WITH THORIUM POWER INC.

Radkowsky Thorium Power Corp., incorporated in the state of Delaware on January 8, 1992 (“Inception”), changed its name to Thorium Power, Inc. in Apri1 2001. Thorium Power, Inc. is engaged in the development, promotion and marketing of its three patented nuclear fuel designs: (1) Thorium/uranium nuclear fuel, (2) Thorium/reactor-grade plutonium disposing fuel, and (3) Thorium/weapons-grade plutonium disposing fuel. These fuels are designed to be used in existing light water reactors. Presently, we are focusing most of our efforts on demonstrating and testing our nuclear fuel technology for the Russian designed VVER-1000 reactors.

Once our reactor fuels are further developed and tested, we plan to license our intellectual property rights to fuel fabricators, nuclear generators, and governments for use in commercial light water nuclear reactors, or sell the technology to a major nuclear company or government contractor or some combination of the two. We anticipate having our technology fully developed for VVER-1000 reactors and our fuel tested in a VVER-1000 operating reactor in the next three years. Presently all our research, testing and demonstration activities are being conducted in Russia. Our research operations are subject to various political, economic, and other risks and uncertainties inherent in Russia.

We participate in a highly regulated industry that is characterized by governmental regulation. Our results of operations are affected by a wide variety of factors including general economic conditions, decreases in the use or public favor of nuclear power, the ability of our technology, the ability to safeguard the production of nuclear power and safeguarding our patents and intellectual property from competitors. Due to these factors, we may experience substantial period-to-period fluctuations in our future operating results.

We may in the future be designated as a potentially responsible party (PRP) by federal and state agencies with respect to certain sites with which we may have direct or indirect future involvement. Such designations can be made regardless of the extent of our involvement.

Operations to date have been devoted primarily to continued development of our fuel designs filing for certain patents relating to our technology, developing strategic relationships within the nuclear industry, securing political and some financial support from the United States and Russian governments, and administrative functions. We, therefore, based on our current operations, prepare our accompanying consolidated financial statements as a Development Stage Enterprise.

Merger Agreement

On February 14, 2006 Novastar Resources Ltd. (“Novastar”), entered into an Agreement and Plan of Merger (the “Merger Agreement”) with Thorium Power, Inc. and TP Acquisition Corp., a direct wholly-owned subsidiary of Thorium Power, Ltd. which was formed in connection with the merger transaction contemplated by the Merger Agreement. (Collectively after the merger, all entities are referred to as the “Company"). Concurrently therewith, Thorium Ltd (1) adopted its 2006 Stock Plan, (2) entered into an employment agreement with Seth Grae, President and Chief Executive Officer of Thorium Power, Inc. to also become President and Chief Executive Officer of Thorium Power, Ltd., which granted certain nonqualified stock options to Mr. Grae and (3) also entered into a subscription agreement with Thorium Power, Inc. for the purchase of 6,597,495 shares for $0.13 per share (equivalent to $4.00 per Thorium Power Inc share price), subsequently these 6,597,495 shares were cancelled at the Merger date, October 6, 2006.

The Merger was consummated pursuant to the terms of an Agreement and Plan of Merger among the parties that was entered into on February 14, 2006 and then subsequently the original merger terms were amended on June 12, 2006 and August 8, 2006. On October 6, 2006, subsequent to the merger, Novastar changed its name to Thorium Power Ltd. ("Thorium Power, Ltd.")

Thorium Power, Ltd.
(A Development Stage Company)
Notes to the Consolidated Financial Statements
December 31, 2006

Under the Merger Agreement each common share of Thorium Power, Inc. was converted into common stock securities of Thorium Power, Ltd. such that Thorium Power, Inc.'s current stockholders owned approximately 54.5% of the combined company (prior to dilution from common stock and warrants issued in connection with the May 2006 private placement), and each share of Thorium Power, Ltd.'s common stock will remain outstanding. In addition, Thorium Power, Ltd. appointed new directors and officers following the merger. The combined company is headquartered in McLean, Virginia, where the Company's operations are presently based.

In accordance with the terms of the Merger Agreement, the following occurred with respect to the outstanding common shares, stock options and warrants of Thorium Power, Inc. at the closing of the Merger:

i) all of the shares of common stock of Thorium Power, Inc. were cancelled and each registered owner of outstanding shares of Thorium Power, Inc. common stock automatically became the registered owner of 31.36 shares of common stock of Thorium Power, Ltd., for each share of Thorium Power, Inc. common stock that they previously owned (recapitalization ratio for reverse merger accounting purposes). In accordance to the Merger Agreement, each holder of non-compensatory options or warrants of Thorium Power, Inc. that had an exercise price of $5.00 or $1.00, received from Thorium Ltd 12.315 shares and 22.965 shares of Thorium Power, Ltd. respectively, for each option or warrant owned. There were 135,637,854 total common shares issued to the Thorium Power, Inc. stockholders in the aggregate. There was a total of 160,761,474 of common shares outstanding in Thorium Power Ltd. prior to the merger, of which 124,101,637 shares are being shown as permanent equity in the statement of changes in stockholders' deficiency and 36,659,837 as shown on the balance sheet as temporary equity. As a result of the merger, there were 296,399,328 common shares outstanding on October 6, 2006 (including the 36,659,837 shares of common stock shown as temporary equity).

ii) all of other outstanding warrants and options of Thorium Power, Inc. were assumed by Thorium Power, Ltd. and became exercisable for Thorium Power, Ltd. common stock in an amount and at an exercise price that is consistent with the exchange ratio described above for the conversion of Thorium Power, Inc. common stock. There were 22,539,083 Thorium Power, Ltd., stock purchase warrants and 22,567,242 Thorium Power, Ltd., stock options assumed by Thorium Power, Inc. as of the date of the merger.

For financial reporting purposes, this merger transaction was recorded as a recapitalization of Thorium Power, Inc. whereby Thorium Power, Inc. is deemed to be the continuing, surviving entity for accounting purposes, but through reorganization, has deemed to have adopted the capital structure of Thorium Power, Ltd.

Accordingly, all references to common shares of Thorium Power, Inc.'s common stock have been restated to reflect the equivalent number of Thorium Power, Ltd.'s common shares. In other words, the 4,325,447 Thorium Power, Inc. shares outstanding (net of the 210,119 shares held by Thorium Power Ltd. that were cancelled at the Merger date) are restated as 135,637,854 common shares, as of October 6, 2006. Each share of Thorium Power Inc. is restated to 31.36 shares of Thorium Power Ltd, which includes the shares issued to holders of non-compensatory options or warrants of Thorium Power, Inc. that had an exercise price of $5.00 or $1.00, as mentioned above.

A summary of assets and liabilities that, for accounting purposes, were deemed to have been acquired by Thorium Power, Inc. from Thorium Power Ltd, book value as of the date of acquisition (October 6, 2006) were as follows:

Total assets - consisting of cash of $12,742,408, prepaid and other receivables, $117,384	$ 12,859,792

Temporary Equity Transfer		(12,041,373)
Total Liabilities-consisting of warrant liabilities of $3,080,024 and other payables	$	(4,116,830)
Book Value of Thorium Power, Ltd. - transferred to stockholders equity	$	(3,298,411)

For the purpose of disclosing the non-cash transactions for the statement of cash flows for the years ended December 31, 2006 and 2005, these assets acquired at book value represent the non-cash transactions. Also the company acquired $12,742,408 of cash at the merger date (October 6, 2006). Due to this merger being recorded as a recapitalization of Thorium Power, Inc., this cash received was recorded as a financing activity on the Statement of Cash Flows.

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(A Development Stage Company)
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In accordance with the Security and Exchange Commissions Staff Accounting Bulletin SAB.T.1B1, an allocation of expenses attributable to Thorium Power, Inc., was made to Thorium Power, Inc. from Thorium Power, Ltd. for periods prior to the merger date of October 6, 2006. The total expenses allocated to Thorium Power, Inc. up to October 6, 2006 (merger date) were $7,477,700, which consisted of $875,602 of general and administrative expenses and $6,602,098 of stock based compensation from Thorium Power, Ltd. These total allocated expenses of approximately $7.5 million were recorded as deemed capital contributions to Thorium Power Inc. by Thorium Power Ltd.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

a) Consolidation

These financial statements include the accounts of Thorium Ltd (a Nevada corporation) and our wholly-owned subsidiaries, Thorium Power, Inc. (a Delaware corporation) and TP Acquisition Corp., (a Delaware corporation). Due to the accounting treatment of the reverse merger mentioned above, the operating results reported are those of Thorium Power Inc. from January 1, 2006 to October 6, 2006 and the operating results of Thorium Power Inc., Thorium Power Ltd and TP Acquisition Corp consolidated, from October 6, 2006 (merger date) to December 31, 2006.

All significant intercompany transactions and balances have been eliminated in consolidation.

b) Use of Estimates

The preparation of financial statements, in conformity with accounting principles generally accepted in the United States of America, requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

Thorium Power, Ltd.
(A Development Stage Company)
Notes to the Consolidated Financial Statements
December 31, 2006

These consolidated financial statements include some amounts that are based on management's best estimates and judgments. The most significant estimates relate to valuation of stock grants, stock options and stock purchase warrants, allocation of certain expenses incurred by Thorium Power, Ltd. that were attributable to Thorium Power, Inc., accrued liquidation damages pursuant to the Registration Right Agreement for the May 4, 2006 private placement, and various contingent liabilities. These above-mentioned estimates and others may be adjusted as more current information becomes available, and any adjustment could be significant in future reporting periods.

c) Prior Year Reclassifications

Certain reclassifications have been made to our prior years' financial statements in order to conform to the current year presentation. On our Statement of Operations, certain general and administrative expenses were combined into the one expense caption called general and administrative expenses. These reclassifications had no effect on previously reported results of operations or accumulated deficit of Thorium Power, Inc.

d) Cash and Cash Equivalents

Cash and cash equivalents consists of cash on deposit, money market accounts, and investment grade commercial paper that are readily convertible into cash and purchased with original maturities of three months or less.

As part of its cash management program, the Company from time to time maintains a portfolio of marketable investment securities. The securities are investment grade and include tax and tax exempt securities and have a term to earliest maturity of less than 3 months. These marketable securities, classified as either available for sale, or trading securities are recorded at market value.

Concentration of Credit Risk

Cash in bank accounts is at risk to the extent that it exceeds Federal Deposit Insurance Corporation insured amounts. To minimize risk, the Company places its cash with high credit quality institutions. Substantially all cash is deposited in two prominent U.S. financial institutions.

Investment Securities

Trading and available-for-sale securities are recorded at fair value. Unrealized holding gains and losses on trading securities are included in the net income. Unrealized holding gains and losses, net of the related tax effect, on available for sale securities are excluded from net income and are reported as a separate component of other comprehensive income until realized. Realized gains and losses from the sale of available-for-sale securities are determined on a specific-identification basis.

A decline in the market value of any available-for-sale security below cost that is deemed to be other-than-temporary results in a reduction in carrying amount to fair value. The impairment is charged as an expense to the statement of income and comprehensive income and a new cost basis for the security is established. To determine whether an impairment is other-than-temporary, the Company considers whether it has the ability and intent to hold the investment until a market price recovery and considers whether evidence indicating the cost of the investment is recoverable outweighs evidence to the contrary. Evidence considered in this assessment includes the reasons for the impairment, the severity and duration of the impairment, changes in value subsequent to year end, and forecasted performance of the investee.

e) Property and Equipment

Property, Plant and Equipment is comprised of an automobile, computer and office equipment and is stated at cost less accumulated depreciation. Depreciation of furniture, computer and office equipment is computed over the estimated useful life of the asset, generally five and seven years respectively, utilizing the double declining balance methodology. Depreciation for the leasehold improvements is computed using the straight-line method over the 5 year term of the lease. Upon disposition of assets, the related cost and accumulated depreciation are eliminated and any gain or loss is included in the statement of income. Expenditures for major improvements are capitalized. Maintenance and repairs are expensed as incurred.

Thorium Power, Ltd.
(A Development Stage Company)
Notes to the Consolidated Financial Statements
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f) Income Taxes

Income taxes are accounted for under the asset and liability method in accordance with SFAS No. 109 "Accounting for Income Taxes." Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carry forwards. Deferred tax assets and liabilities are measured using 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 deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. Deferred tax assets are reduced by a valuation allowance to the extent that the recoverability of the asset is unlikely to be recognized. The Company did not provide any current or deferred income tax provision or benefit for any periods presented to date because the Company has continued to experience a net operating loss since inception.

g) Stock-Based Compensation

In December 2004, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 123R (FAS-123R), Share-Based Payment, which is a revision of Statement of Financial Accounting Standards No. 123 (FAS-123), Accounting for Stock-Based Compensation. In addition to requiring supplemental disclosures, FAS-123R addresses the accounting for share-based payment transactions in which a company receives goods or services in exchange for (a) equity instruments of the company or (b) liabilities that are based on the fair value of the company's equity instruments or that may be settled by the issuance of such equity instruments. FAS-123R focuses primarily on accounting for transactions in which a company obtains employee services in share-based payment transactions. The Statement eliminates the ability to account for share-based compensation transactions using Accounting Principles Board Opinion No. 25 (APB-25), Accounting for Stock Issued to Employees, and generally requires that such transactions be accounted for using a fair value based method. Accordingly, pro-forma disclosure is no longer an alternative.

Under FAS-123R, the Company is required to recognize compensation cost for the portion of outstanding awards previously accounted for under the provisions of APB-25 for which the requisite service had not been rendered as of the adoption date for this Statement. The Statement also requires companies to estimate forfeitures of stock compensation awards as of the grant date of the award.

A “modified prospective” method is used in which compensation cost is recognized beginning with the effective date (a) based on the requirements of FAS-123R for all share-based payments granted after the effective date and (b) based on the requirements of FAS-123 for all awards granted to employees prior to the effective date of FAS-123R that remain unvested on the effective date; or

The Company adopted FAS-123R on January 1, 2006, using the modified prospective method. The valuation of the stock issued to consultants for consulting services are valued as of the date of the agreements with the various consultants, which in all cases is earlier than the dates when the services are committed to be performed by the various consultants.

References to the issuances of restricted stock is stock issued to individuals whom are eligible to sell all or some of their shares of restricted common stock by means of ordinary brokerage transactions in the open market pursuant to Rule 144, promulgated under the Securities Act ("Rule 144"), subject to certain limitations. In general, pursuant to

Rule 144, a stockholder (or stockholders whose shares are aggregated) who has satisfied a one-year holding period may, under certain circumstances, sell within any three-month period a number of securities which does not exceed the greater of 1% of the then outstanding shares of common stock or the average weekly trading volume of the class during the four calendar weeks prior to such sale. Rule 144 also permits, under certain circumstances, the sale of securities, without any limitations, by a non-affiliate of our company that has satisfied a two-year holding period.

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(A Development Stage Company)
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December 31, 2006

h) Warrants

Warrants issued in conjunction with equity financing were accounted for under the Emerging Issues Task Force FSP ("EITF") Issue No. 00-19, `Accounting for Derivative Financial Instruments Indexed to and Potentially Settled in a Company's Own Stock'. In December 2006, the FASB approved FSP EITF 00-19-2 Accounting for Registration Payment Arrangements, which establishes the standard that contingent obligations to make future payments under a registration rights arrangement shall be recognized and measured separately in accordance with Statement 5 and FASB Interpretation No. 14, Reasonable Estimation of the Amount of a Loss. The Company has currently evaluating the effect of how FSP EITF 00-19-2 and FSP EITF Topic D-98 will affect future financial statements. The adoption of this pronouncement on January 1, 2007 will change the classification of the warrant liability, $1,132,440 at December 31, 2006, to equity (additional paid in capital).

i) Basic and Diluted Loss per Share

In accordance with Financial Accounting Standards Board ("FASB") Statement of Financial Accounting Standard No. 128 ("SFAS 128"), "Earnings Per Share", the basic loss per common share is computed by dividing net loss available to common stockholders by the weighted average number of common shares outstanding. Diluted loss per common share is computed similar to basic loss per common share except that the denominator is increased to include the number of additional common shares that would have been outstanding if the potential common shares had been issued and if the additional common shares were dilutive. At December 31, 2006 and 2005, the Company stock equivalents were anti-dilutive and excluded in the loss per share computation.

j) Impairment Charges

Unlike goodwill and indefinite-lived intangible assets, the accounting rules do not provide for an annual impairment test in determining whether property, plant, and equipment and finite-lived intangible assets (e.g., patents) are impaired. Instead, they require that a triggering event occur before testing an asset for impairment. Examples of such triggering events include current-period operating or cash flow loss combined with a history of operating or cash flow losses, a significant disposal of a portion of such assets, an adverse change in the market involving the business employing the related asset, a significant decrease in the benefits realized from an acquired business, difficulties or delays in integrating the business and a significant change in the operations of an acquired business.

Once a triggering event has occurred, the impairment test employed is based on whether the intent is to hold the asset for continued use or to hold the asset for sale. If the intent is to hold the asset for continued use, the impairment test involves a comparison of undiscounted cash flows against the carrying value of the asset as an initial test. If the carrying value of such asset exceeds the undiscounted cash flow, the asset would be deemed to be impaired. Impairment would then be measured as the difference between the fair value of the fixed or amortizing intangible asset and the carrying value to determine the amount of the impairment. The Company generally determines fair value by using the discounted cash flow method. If the intent is to hold the asset for sale and certain other criteria are met (i.e., the asset can be disposed of currently, appropriate levels of authority have approved sale, and there is an actively pursuing buyer), the impairment test is a comparison of the asset's carrying value to its fair value less costs to sell. To the extent that the carrying value is greater than the asset's fair value less costs to sell, an impairment loss is recognized for the difference. The Company conducted an impairment test of its Patent at December 31, 2006 and determined that the future undiscounted cash flows associated with the Patent rights were sufficient to recover its carrying value. Assets held for sale are separately presented on the balance sheet and are no longer depreciated.

In November 2005, FASB issued FSP FAS 115-1 and FAS 124-1, The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments (“FSP 115-1 and 124-1”), which clarifies when an investment is considered impaired, whether the impairment is other than temporary, and the measurement of an impairment loss. It also includes accounting considerations subsequent to the recognition of an other-than-temporary impairment and requires certain disclosures about unrealized losses that have not been recognized as other-than-temporary impairments. FSP 115-1 and 124-1 are effective for all reporting periods beginning after December 15, 2005. Implementation of these statements is not expected to have a significant impact on the Company's consolidated financial position or results of operations.

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k) Comprehensive Income

Comprehensive income consists of net income and other gains and losses affecting shareholders' equity that, under generally accepted accounting principles are excluded from net income. For the Company, such items consist primarily of unrealized gains and losses on marketable debt securities, which the Company has classified as cash equivalents, as their maturities are three months or less.

l) Development Stage Enterprise

The Company's consolidated financial statements are prepared using the accrual method of accounting and according to the provisions of Statement of Financial Accounting Standards No. 7 (“SFAS 7”), “Accounting and Reporting for Development Stage Enterprises,” as we are devoting substantially all of our efforts to developing our nuclear fuel designs. Until such designs are developed and significant revenue is derived from these nuclear fuel designs or other revenue sources, we will continue to prepare our consolidated financial statements and related disclosures in accordance with entities in the development stage.

m) Revenue Recognition

All of the Company's revenue to date from January 8, 1992 (Inception) to December 31, 2006 had been derived from licensing fees from nuclear industry commercial partners.

Once the company's Thorium nuclear fuel designs has advanced to a commercially usable stage the company will seek to license its technology to major government contractors or nuclear companies, working for the US and other governments. We expect that our revenue from license fees will be recognized on a straight-line basis over the expected period of the related license term.

Total subsidies and grants from the US government totaled approximately $5.45 million, cumulative from January 8, 1992 (Inception) to December 31, 2006. These amounts were not paid to us but paid directly from the US government to third party research and development companies that worked on our nuclear project, as well as other projects.

n) Government Grants

Receipts of government grants to encourage research and development activities which are non-refundable will be credited to deferred income upon receipt. Government grants are used either for purchases of assets or to subsidize the research and development expenses incurred.

For purchases of assets, government grants are deducted from the carrying amount of the assets. For the research and development expenses, the Company matches and offsets the government grants with the expenses of the research and development activities as specified in the grant approval document in the corresponding period when such expenses incurred.

o) Segment Reporting

The Company uses the “management approach” in determining reportable operating segments. The management approach considers the internal organization and reporting used by the Company's chief operating decision maker for making operating decisions and assessing performance as the source for determining the Company's reportable segments. The Company has determined that the Company has one operating segment as defined by SFAS 131, “Disclosures about Segments of an Enterprise and Related Information”.

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p) Commitments and Contingencies

Liabilities for loss contingencies arising from various claims, assessments, litigation, fines and penalties and other sources are recorded when it is probable that a liability has been incurred and the amount of the assessment can be reasonably estimated.

q) Recently Issued Accounting Standards

FASB Interpretation No. ("FIN") 48, Accounting for Uncertainty in Income Taxes--an Interpretation of FASB Statement No. 109. In July 2006, the FASB issued FIN 48, Accounting for Uncertainty in Income Taxes--an Interpretation of FASB Statement No. 109, which clarifies the accounting for uncertainty in tax positions. This Interpretation requires the Company recognizes in its consolidated financial statements the impact of a tax position if that position is more likely than not of being sustained on audit, based on the technical merits of the position. The provisions of FIN 48 are effective for the Company on January 1, 2007, with the cumulative effect of the change in accounting principle, if any, recorded as an adjustment to opening retained earnings. The Company does not believe FIN 48 will have an impact on its consolidated financial statements.

SFAS 157, Fair Value Measurements. In September 2006, the FASB issued SFAS 157, Fair Value Measurements, which defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. SFAS 157 applies under other accounting pronouncements that require or permit fair value measurements, where fair value is the relevant measurement attribute. The standard does not require any new fair value measurements. SFAS 157 is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The Company is currently evaluating the impact of adopting SFAS 157 on its consolidated financial statements.

Staff Accounting Bulletin ("SAB") No. 108

In September 2006, the SEC issued SAB No. 108, which provides guidance on the process of quantifying financial statement misstatements. In SAB No. 108, the SEC staff establishes an approach that requires quantification of financial statement errors, under both the iron-curtain and the roll-over methods, based on the effects of the error on each of the Company's financial statements and the related financial statement disclosures. SAB No.108 is generally effective for annual financial statements in the first fiscal year ending after November 15, 2006. The transition provisions of SAB No. 108 permits existing public companies to record the cumulative effect in the first year ending after November 15, 2006 by recording correcting adjustments to the carrying values of assets and liabilities as of the beginning of that year with the offsetting adjustment recorded to the opening balance of retained earnings. Management does not expect that the adoption of SAB No.108 would have a material effect on the Company's consolidated financial statements.

The Company is currently evaluating the effect of other new accounting pronouncements on its future statements of financial position and results of operations.

r) Intangible Assets - Patents

Patents are stated in the balance sheet at cost less accumulated amortization. The costs of the patents are amortized on a straight-line basis over their estimated useful lives. The amortization period for our patents range between 17-20 years.

s) Retirement 401K Plan

We have a 401(k) savings plan that was set up in 2006 covering substantially all of our employees. Eligible employees may contribute through payroll deductions. There were no Company matching contributions made to the 401(k) savings plan in 2006.

3. Financial Status of the Company - December 31, 2006

Management anticipates, based on its current projected working capital requirements, that it will have enough working capital funds to sustain its current operations at its current operating level, until sometime during the first quarter of 2008. The Company will have future issuances of its stock or incur debt, in order to provide funds to continue its operations into 2008 and beyond.

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4. Research and Development Costs

Research and development costs, included under the caption "general and administrative expenses" in the statement of operations amounted to $34,400 and $17,500 for the years ended December 31, 2006 and 2005, respectively and $3,926,558 from January 8, 1992 (Inception) to December 31, 2006

5. Property Plant and Equipment

The following represents the detail of the Company's property, plant and equipment at December 31, 2006 and 2005:

		2006		2005
Furniture, computer and office equipment	$	24,840	$	13,879
Automobile		22,217		22,217
Total Cost		47,057		36,096
Accumulated Depreciation		(25,767)		(14,881)
Net Book Value	$	21,290	$	21,215

Depreciation expense for the years ended December 31, 2006 and 2005 were $10,886, and $5,434, respectively.

6. Intangible Assets - Patents

Patents represent legal fees and filing costs that are capitalized and amortized over their estimated useful lives of 17-20 years. There were no patents placed in service for the year ended December 31, 2006.

The following table summarizes the lives and carrying values of the Company's patents at December 31, 2006 and 2005:

		2006		2005
Patents	$	411,669	$	405,005
Accumulated Amortization		(193,794)		(193,794)
Net Book Value	$	217,875	$	211,211

Amortization expense of patents was $- and $17,270 for the years ended December 31, 2006 and 2005 and $193,794 for the cumulative period from January 8, 1992 (Inception) to December 31, 2006.

7. Stockholders' Equity

Total Common stock outstanding at December 31, 2006 was 293,101,546 (including 36,659,837 shares of common stock with registration rights). There were also 850,000 shares that were held as Treasury stock at December 31, 2006, bringing the total number of shares issued to 293,951,546. At December 31, 2006, there were 25,282,745 stock purchase warrants and 34,578,993 stock options outstanding, all totaling 352,963,284 of total stock and stock equivalents outstanding at December 31, 2006.

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a). Common Stock Issuances

STOCK ISSUANCES PRIOR TO THE MERGER DATE (10/6/06)

During the year ended December 31, 2006, Thorium Power Inc., sold 8,354,919 (equivalent to 326,010 shares of Thorium Power Inc) shares of common stock to 22 investors for $1,539,678. Thorium Power, Inc. also sold, pursuant to the Merger Agreement, 4,164,518 shares (equivalent to 162,500 shares of Thorium Power Inc.) of common stock to Novastar, at a stock price of $0.1561 per share (equivalent to $4.00 per Thorium Power Inc share price), total proceeds of $650,000. These shares were subsequently cancelled after the merger. Thorium Power, Inc., also received $13,000 from the exercise of 333,161 stock options (equivalent to 13,000 Thorium Power Inc.stock options) at $0.0435 per share (equivalent to $1.00 price per Thorium Power Inc share). Total proceeds from the issuance of the above 12,852,598 shares (equivalent to 501,510 shares of Thorium Power Inc. was $2,202,678. Thorium Power, Inc., also issued 26,268 shares (equivalent to 1,025 shares of Thorium Power Inc. common stock at $0.1561 per share (equivalent to $4.00 per stock price of Thorium Power Inc.) shares in repayment of a loan from a director, which totaled $4,100. Thorium Power, Inc. also issued 512,556 shares (equivalent to 20,000 shares of Thorium Power Inc. common stock to directors, for director service rendered at $0.2049 per share (equivalent to $5.25 per Thorium Power Inc.) share price, total value of the services recorded was $105,000. Thorium Power, Inc., was a private company, so the value of the stock issued for services was determined by the price paid by the investors mentioned above, where 21 out of the 22 of these investors paid $0.2049 per share (equivalent to Thorium Power Inc. price of $5.25 per share). There were also 16,659,275 (equivalent to 650,047 Thorium Power Inc.shares) of Thorium Power, Inc. shares issued to stock option holders, who exercised their stock options through the cashless exercise feature in accordance to their individual stock option agreements. All of these option holders had an exercise price of $0.039 per share (equivalent to $1.00 per Thorium Power Inc. share price and the numbers of shares issued in the cashless exercise were based on the market price of $0.2049 per share (equivalent to Thorium Power Inc. $5.25 per share).

STOCK ISSUANCES-PURSUANT TO THE MERGER AGREEMENT-MERGER DATE - 10/6/2006

On October 6, 2006, the Company completed the merger, as more fully described in note 1, and issued 135,637,854 shares of Thorium Power, Ltd., stock to the stockholders of Thorium Power, Inc. For accounting purposes, Thorium Power Inc. is the continuing accounting entity, therefore Thorium Power Inc. is deemed to have issued these shares to its stockholders pursuant to the Merger Agreement. An additional 307,534 shares were issued pursuant to the Merger Agreement, after the merger date, for Thorium Power, Inc. shareholders that were not reflected in the Thorium Power, Inc. stockholders list, at the merger date. This stock issuance of 307,534 shares was recorded as a stock settlement expense which totaled $92,260, valued at the stock price of $0.30 per share, valued at the date the Company was first made aware of these shares being outstanding, that were not accounted for in their stock records. The Company reviewed these share certificates and determined that they were valid stock certificates and settled this matter, post merger, by issuing the equivalent Thorium Power Ltd. shares to these stockholders.

STOCK ISSUANCES AFTER THE MERGER DATE-After October 6, 2006

The Board of Directors of the Thorium Power, Ltd. increased the size of the board to five members and appointed two Independent Directors: Jack D. Ladd and Daniel B. Magraw, Jr., as a members of the Board of Directors of the Company, effective October 23, 2006. Pursuant to terms of the Independent Director's Contracts, dated October 23, 2006, between Mr. Ladd and the Company and Mr. Magraw and the Company Mr. Ladd and Mr. Magraw will each receive a fee of $20,000 per year in cash, as well as such number of restricted shares, issued quarterly, equal to $5,000 each quarter, to be paid to each Director for the respective quarter based on the average closing price of the Company's common stock, as quoted on the trading market on which the Company's securities are traded, over the thirty day period prior to the first day of the applicable quarter. On December 27, 2006, a total of 22,050 shares were issued to the directors for their services. Additionally, the Director Contracts grant to Messrs. Ladd and Magraw for each year of service on the Board of Directors non-qualified options to purchase up to 500,000 shares of the common stock of the Company (the “Director Options”), which shall vest with respect to 13,889 shares on November 23, 2006 and the remaining 486,111 shares will subsequently vest in equal monthly installments of 13,889 shares on each one month anniversary of the grant until all shares underlying the Director Options have vested. The third independent Director, Victor Alessi, was appointed as a director in August, 2006 and received 500,000 stock options, term 5 years, vesting equally over 36 month period. On October 11, 2006, 182,291 shares were issued pursuant to a legal settlement. On November 6, 2006, 491,333 shares were issued, pursuant to a cashless stock option exercise of 140,953 shares, strike price was $0.195 per share and market value of the stock was $0.30 per share.

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In November, 2006 the company redeemed 3,008,990 shares of common stock from its two executive officers in order to satisfy the payroll tax withholding obligations of the Company owed on their stock based compensation.

b). Common Stock Buyback Program - Treasury Stock

On October 17, 2006, the Company announced that its Board of Directors authorized a share buyback program for an aggregate of $1,000,000 over the next 12 months, with $250,000 of stock to be repurchased immediately. At the discretion of the CEO Seth Grae, the Company may effect further share repurchases over the course of the year depending on valuation of the Company reflected in the share price. As of the date of this report 850,000 shares had been repurchased pursuant to this program at the average approximate price of $0.30 per share. The Company valued all shares issued in the twelve month period ended December 31, 2006 using the traded quoted market price of the Company's common stock as of the applicable agreement date. These shares are being held as Treasury Stock as of December 31, 2006.

c). Common Stock Issued With Registration Rights - Temporary Equity

On May 4, 2006, the Company completed a private placement with certain investors in which it sold an aggregate of 36,659,837 units, consisting of 36,659,837 shares of its restricted common stock and 18,329,98 common stock purchase warrants for $15,580,431. Each unit consists of one share of common stock and one-half of a non-transferable share purchase warrant. Each whole warrant entitles the holder of the warrant to acquire one additional share of common stock at a price of $0.65 per share and expires twelve months from the closing date of the subscription expiration date or term subsequently extended 6 months.

Under the terms of the sale, the investors were granted registration rights in which the Company agreed to timely file a registration statement to register the common shares and the shares underlying the warrants, obtain effectiveness of the registration statement by the SEC on or before September 1, 2006, and maintain the effectiveness of this registration statement for a pre-set time thereafter. In the event the Company failed to timely perform under the registration rights agreement, the Company agreed to pay the investors liquidated damages in an amount equal to 2% of the aggregate amount invested by the investors for each 30-day period or pro rata for any portion thereof following the date by which the registration statement should have been effective. The initial registration statement was timely filed, however it was not declared effective by the SEC within the allowed time. Accordingly, the Company is liable to the investors for liquidated damages under the registration rights agreement. The Company recognized in other income and expenses, in its statements of operatons under the caption Registration Rights Expense, an amount of approximately $354,000 for unpaid liquidated damages at December 31, 2006.

The EITF is currently reviewing the accounting for securities with liquidated damages clauses as stated in EITF 05-04, The Effect of a Liquidated Damages Clause on a Freestanding Financial Instrument subject to EITF 00-19. There are currently several views as to how to account for this type of transaction and the EITF has not yet reached a consensus. In accordance with EITF 00-19, Accounting for Derivative Financial Instruments Indexed To, and Potentially Settled in the Company's Own Stock, and EITF 05-04, because of the potential liquidated damages for failure to obtain and maintain an effective registration statement is substantial, the value of the common stock subject to such registration rights should be classified as temporary equity. Additionally, in accordance with EITF 00-19 and the terms of the above warrants, the fair value of the warrants should be recorded as a liability, with an offsetting reduction to shareholders' equity. The warrant liability is initially measured at fair value using the Black Scholes option pricing model, and is then re-valued at each reporting date, with changes in the fair value reported as non-cash charges or credits to earnings reported as gain/loss on fair value of warrant derivatives.

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The SEC concluded that under EITF 00-19, common stock and warrants subject to registration rights where significant liquidated damages could be required to be paid to the holder of the instrument in the event the issuer fails to maintain the effectiveness of a registration statement for a preset time period, the common stock subject to such liquidated damages does not meet the tests required for shareholders' equity classification, and accordingly must be reflected between liabilities and shareholders' equity in the balance sheet until the conditions are eliminated. In analyzing instruments under EITF 00-19, the likelihood or probability related to the failure to maintain an effective registration statement is not a factor.

Based on the above interpretation, as of May 4, 2006, the Company classified $12,041,373 for the value of common stock subject to registration rights as temporary equity instead of shareholders' equity. In addition, the Company measured the initial fair value of the warrants on May 4, 2006 at $3,539,058 and classified at that date the fair value of the warrants as warrant liability instead of shareholders' equity.

At the end of each reporting period, the value of these warrants is re-measured based on the fair value of the underlying shares, and changes to the warrant liability and related “gain or loss in fair value of the warrants” is recorded as a non-cash charge or credit to earnings. The warrant liability will be reclassified to shareholders' equity when the Company is no longer subject to all of its performance obligations under the registration rights agreement, or under FSP 00-19-2 as equity in 2007.

At December 31, 2006, the warrant liability decreased to $1,132,440 due to changes in the fair value of the warrants. The fair value of the warrants was estimated using the Black Scholes option-pricing model, with the following assumptions for the year ended December 31, 2006: risk-free interest rate of 3.86% dividend yield of 0%, expected life of .9 year and volatility of 106% were used. We expect to reclassify this warrant liability, in accordance with FSP 00-19-2 to stockholders' equity, additional paid in capital, at January 1, 2007.

For the period ended October 6, 2006 to December 31, 2006, the non-cash gain on fair value of warrants, or deduction in warrant liability, was $1,902,286. The gain recorded on the change in the fair value of derivative instruments was due principally to the decrease in the volatility factor used in the Black Scholes valuation of the warrants. The date range used to calculate this volatility factor was from January 5, 2006, date of announcement of Thorium Power, Ltd. and Thorium Power, Inc. merger, to December 31, 2006. The stock volatility factor for the fourth quarter of 2006 was low, as the stock trading price remained primarily at $0.30 per share for this period of time. The non-cash gain on fair value of warrants, recorded as gain on fair value of warrant derivatives, has no effect on the Company's cash flows or liquidity.

d) Share-based Compensation

The Company has in place a stock-based compensation plan to reward for services rendered by officers, directors, employees and consultants. On July 17, 2006, the Company amended this stock plan. The Company has reserved 75,000,000 shares of common stock of its unissued share capital for the stock plan. Other limitations are as follows:

i). No more than 37,500,000 options can be granted for the purchase of restricted common shares.

ii). No more than 8,000,000 options can be granted to any one person.

iii). No more than 5,000,000 options can be granted to any one person for the purchase of restricted common shares.

On January 1, 2006, the Company adopted FAS-123R. In March 2005, the SEC staff expressed their views with respect to FAS-123R in Staff Accounting Bulletin No. 107, Share-Based Payment ("SAB 107"). SAB 107 provides guidance on valuing options. The impact of adopting FAS-123R for the year ended December 31, 2006 was to record a non-cash compensation expense of $2,184,001, of which $937,619 was allocated prior to the merger from Thorium Power, Ltd. for services rendered on behalf of Thorium Power, Inc. . Prior to January 1, 2006, the Company accounted for share-based payments under the recognition and measurement provisions of APB Opinion No. 25, Accounting for Stock Issued to Employees ("APB 25"), and related Interpretations, as permitted by FAS-123. In accordance with APB 25, no compensation cost was required to be recognized for options granted that had an exercise price equal to the market value of the underlying common stock on the date of grant. The Company adopted FAS-123R using the modified-prospective-transition method. Under that transition method, compensation cost recognized in future interim and annual reporting periods includes: a) compensation cost for all share-based payments granted prior to, but not yet vested as of January 1, 2006, based on the grant-date fair value estimated in accordance with the original provisions of FAS-123, and b) compensation cost for all share-based payments granted subsequent to January 1, 2006, based on the grant-date fair value estimated in accordance with the provisions of FAS-123R.

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The adoption of FAS-123R had no effect on cash flow from operations or cash flow from financing activities for the three months ended September 30, 2006. FAS-123R requires the cash flows from tax benefits resulting from tax deductions in excess of the compensation cost recognized for those options (“excess tax benefits”) to be classified as financing cash flows. Prior to the adoptions of FAS-123R, excess tax benefits would have been classified as operating cash inflows. The Company has not recognized, and does not expect to recognize in the near future, any tax benefit related to stock-based compensation costs as a result of the full valuation allowance on our net operating loss carry forwards.

The Company recognizes share-based compensation expense for all service-based awards with graded vesting schedules on a straight-line basis over the requisite service period for the entire award. Initial accruals of compensation expense are based on the estimated number of shares for which requisite service is expected to be rendered. Estimates are revised if subsequent information indicates that forfeitures will differ from previous estimates, and the cumulative effect on compensation cost of a change in the estimated forfeitures is recognized in the period of the change.

For awards with service conditions and graded vesting that were granted prior to the adoption of FAS-123R, the Company estimates the requisite service period and the number of shares expected to vest and recognize compensation expense for each tranche on a straight-line basis over the estimated requisite service period of the award or over a period ending with an employee's eligible retirement date, if earlier. Adjustments to compensation expense as a result of revising the estimated requisite service period are recognized prospectively.

Total stock options outstanding at December 31, 2006 were 34,578,993 (22,567,242 were assumed by Thorium Power Inc. in accordance with the Merger Agreement with Thorium Power, Ltd. and remain outstanding) and 16,325,523 of these total options were vested at December 31, 2006.

Stock option transactions to the employees, directors, advisory board members and consultants are summarized as follows:

	2006	2005
Stock Options Outstanding		
Assumed by the Merger	22,567,242	-
Thorium Power Inc. Options Outstanding	12,011,751	-
Expired	-	-
Forfeited	-	-
Outstanding end of the year	34,578,993	-
Options exercisable at the end of the year	16,325,523	-

The above table includes options issued as of December 31, 2006 as follows:

i). A total of 2,150,000 non-qualified 10 year options have been issued by Thorium Power, Ltd., to advisory board members at exercise prices of $0.51 to $0.64 per share.

ii). A total of 5,500,000 non-qualified 5 year options have been issued to advisory board members at an exercise price of $0.445 per share and a weighted average of $0.445; and

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iii). A total of 14,917,242 non-qualified 10 year options have been issued to directors and officers of the Company, at exercise prices of $0.30 to $0.80 per share. From this total, 7,200,000 options were issued to Chief Executive Officer who is also a director, on February 14, 2006, with a remaining contractual life of 9.1 years. All other options issued have a remaining contractual life ranging from 4.75 years to 9.9 years.

The following table provides certain information with respect to the above-referenced stock options that are outstanding and exercisable at December 31, 2006:

	Stock Options Outstanding		Stock Options Vested	
Exercise Prices	**Weighted Average Remaining Contractual Life - Years**	**Number of Awards**	**Number of Awards**	**Weighted Average Exercise Price**
$0.16 - $0.20	3.1	6,650,415	6,650,415	$ 0.16
$0.30-$0.39	1.2	6,853,578	4,478,277	$ 0.37
$0.45-$0.51	7.2	11,875,000	1,627,085	$ 0.48
$0.64-$0.80	9.2	9,200,000	2,083,334	$ 0.77
Total	5.9	34,578,993	16,325,523	$ 0.48

Assumptions used in the Black Scholes option-pricing model are as follows:

The aggregate intrinsic value of stock options outstanding at December 31, 2006 was $931,058 of which $931,058 relates to vested awards. Intrinsic value is calculated based on the difference between the exercise price of the underlying awards and the quoted price of our common stock as of the reporting date ($0.30 per share as of December 31, 2006)

	December 31, 2006
Average risk-free interest rate	4.18% - 4.45%
Average expected life	5 years
Expected volatility	108% - 275%
Expected dividends	0%

During the year ended December 31, 2006, $9,131,746 was recorded as stock-based compensation expense in the statement of operations. The result of all the above stock option grants that occurred after January 1, 2006 for Thorium Power Inc and stock option grants for Thorium Power Ltd that were recorded in the statement of operations totaled $2,719,496 (non-deductible for tax purposes, may provide a tax deduction for the Company when exercised). Stock compensation to executive officers totaled $6,138,250, one bonus at year end recorded to common stock reserved for issuance totaled $1,200,000, and the other stock compensation to officers in accordance with their employment agreements totaled $4,938,250. From this total amount of stock-based compensation of $9,131,746, $6,602,098 was recorded on Novastar Resources Ltd. books for the period January 1, 2006 to October 6, 2006, but all of this compensation amount was incurred for Thorium Power Inc.'s benefit, thus allocated to Thorium Power Inc. statement of operations for the year ended December 31, 2006. The remaining stock-based compensation expense was to directors of $105,000 and the amortization of deferred stock compensation of $169,000. Some volatility factors used by Novastar, for five option grants in its fiscal year ended June 30, 2006 calculated the volatility factor for Black Scholes using the term of the option, which is general practice, not from the announcement date of the merger, January 5, 2006, which was later determined to be a more applicable date range due to the announcement date being the date the stock market reflected the merger in the valuation of the Company's stock. This difference in these volatility factors for these five option grants is not material to these financial statements, therefore, no current adjustment to the volatility factors was made to these financial statements for these five option grants and we have decided to continue to use these factors for future expense recognition of options under SFAS #123R.

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e). Warrants

During the year ended December 31, 2006, there were 25,282,745 warrants outstanding as of December 31, 2006.

At December 31, 2006 the range of warrant prices for shares under warrants and the weighted-average remaining contractual life are as follows:

	Warrants Outstanding and Exercisable	
Warrants - Exercise Price	**Number of Warrants**	**Weighted Average Remaining Contractual Life - Years**
$0.30 (Assumed from Thorium Power Ltd.)	2,104,999	.4
$0.39	2,743,662	.6
$0.50 (Assumed from Thorium Power Ltd.)	2,104,166	.8
$0.65 (Assumed from Thorium Power Ltd.)	18,329,918	.9
Total	25,282,745	

The investors in the November 23, 2005, March 30, 2006 and May 4, 2006 private placements received detachable warrants for the purchase of 2,104,999, 2,104,166 and 18,329,918 shares of common stock, respectively, which were valued at $127,467, $281,117 and $3,539,058, respectively. For purposes of estimating the intrinsic fair value of each warrant as of dates of the private placements, the Company utilized the Black Scholes option-pricing model. The Company estimated the fair value of the warrants assuming no expected dividends and the following weighted-average assumptions:

	December 31, 2006
Average risk-free interest rate	2.86% - 4.30%
Average expected life	1 year
Expected volatility	142% - 153%
Expected dividends	0%

On November 17, 2006 the Board of Directors of Thorium Power, Ltd., authorized the extension of the expiration date of all common stock purchase warrants above by six months from the expiration date identified on the respective warrants. This extension of the warrant terms resulted in an expense of $963,387, recorded under the caption warrant expense in the statement of operations in the category other income and expenses.

f). Common Stock and Warrants reserved for Future Issuance

Common stock and warrants reserved for future issuance consists of:

	Shares of	**Stock**

	Common Stock	Purchase Warrants	Amount
Stock-based Compensation	4,000,000	0	$ 1,200,000

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The Compensation Committee of the Board of Directors on December 18, 2006 had unanimously voted to issue 4 million shares of restricted stock as a year end 2006 bonus to its CEO and Executive VP of International Nuclear Operations. The price was to value these shares was the market price as of the date of the stock grant. In a subsequent capital transaction, in order for the company to remit the required payroll tax obligations related to this stock grant to the Federal and State taxing authorities, the Company redeemed 1,620,000 shares of this stock grant from the two executives, at a price of $0.20 per share (price determined by applying a lack of marketability discount). The Company, in January 2007, paid a total of $347,690 for primarily payroll tax withholdings (as a result of redeeming 1,620,000 shares of stock) and payroll tax expense due on these stock compensation issuances.

8. Income Taxes

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities recognized for financial reporting and the amounts recognized for income tax purposes. The significant components of deferred tax assets (at a 40% effective tax rate) as of December 31, 2006 are as follows:

	Total Amount	Deferred Tax Asset Amount
Assets		
Stock-based compensation	$ 2,719,496	$ 1,087,798
Approximate net operating loss	24,458,493	9,783,397
Less: valuation allowance	(27,177,989)	(10,871,196)
	$ -	$ -

Management believes that it is more likely than not that the forecasted taxable income will not be sufficient to utilize the tax carryforwards of approximately $24,458,493, before its expiration in 2012 and 2026 to fully recover the asset. As a result, the amount of the deferred tax assets considered realizable was reduced 100% by a valuation allowance. In the near term, if estimates of future taxable income are increased, such an increase will change the valuation allowance. The Company has no other deferred tax assets or liabilities.

9. Research Agreement

The Company is party to an agreement whereby all of its current research is being performed by the Russian Research Centre, known as the Kurchatov Institute (“RRC”), on the Company's fuel designs. All the funding under this agreement is supplied by the Company. As of March 12, 2007, the Company fulfilled all of its financial obligations under that agreement.

The Company is now in the final stage of negotiations over a new Cooperative Research Agreement (CRA) with an entity closely affiliated with the Russian Atomic Energy Agency (RosAtom) that will provide a necessary legal mechanism for the next phase of research and demonstration activities leading to lead test assembly testing in an operating VVER-1000 reactor in Russia. The initial scope of work under the new CRA is expected to cost approximately $5,000,000 over a 15 month period.

10. Commitments and Contingencies

Firm Price Commitments

The Company entered into a firm price commitment agreement with the University of Texas of the Permian Basin ("UTPB"), in connection with its participation in the pre-conceptual design phase for the construction of a high-temperature test and research reactor in Texas. The agreement had created a commitment by the Company for a minimum of $1.25 million financial contribution toward the project. A minimum payment of $50,000 on the agreement was due and paid on February 22, 2006, with 10 additional conditional contributions totaling $1.2 million due by December 31, 2006. A total of $550,000 has been paid as of December 31, 2006 and these amounts were recorded as donations, under the caption general and administrative expenses.

The terms of this agreement allow either party to terminate the agreement at any time upon giving written notice of termination. The Company, after having further detailed discussions with UTPB regarding the use of the $550,000 donations that were made to UTPB in 2006 and the terms of the agreement, it was understood between the parties that if future donations were to be given, they would be given at the discretion of Thorium Power based on the future use of these funds. Therefore, it is management's assessment and opinion, that under the terms of this agreement, the Company has no further obligations to fund the additional $675,000 to UTPB project; any future funding will be made at the discretion of Thorium Power, subject to the condition that the proceeds are directed by UTPB to the Company's nuclear research or other development work related to its Thorium based fuel designs, as agreed to by the parties.

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Lease Commitments

i) The Company leases office space. Future estimated rental payments under these operating leases are as follows:

		Dollars
Year ending December 31, 2007	$	70,000
Year ending December 31, 2008	$	35,000

COMMITMENTS AND CONTRACTUAL OBLIGATIONS

The Company has employment agreements with its executive officers, the terms of which expire at various times. Such agreements provide for minimum compensation levels, as well as incentive bonuses that are payable if specified management goals are attained. Under each of the agreements, in the event the officer's employment is terminated (other than voluntarily by the officer or by the Company for cause or upon the death of the officer), the Company, if all provisions of the employment agreements are met, is committed to pay certain benefits, including specified monthly severance.

THORIUM POWER, LTD.

112,544,149 shares of common stock

PROSPECTUS

October 11, 2007

Dealer Prospectus delivery obligation

Until 90 days from the date of this prospectus, all dealers that effect transactions in these securities, whether or not participating in this offering, may be required to deliver a prospectus. This is in addition to the dealers' obligation to deliver a prospectus when acting as underwriters and with respect to their unsold allotments or subscriptions.