
**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549**

FORM 10-Q

Quarterly report pursuant to section 13 or 15(d) of the Securities Exchange Act of 1934

For the quarterly period ended June 30, 2007

or

Transition report pursuant to section 13 or 15(d) of the Securities Exchange Act of 1934

For the transition period from _____ to _____

Commission File No. 0-51669

STERLING MINING COMPANY

(Exact name of registrant as specified in its charter)

IDAHO
(State or other jurisdiction of
incorporation or organization)

82-0300575
(IRS Employer
Identification No.)

609 Bank Street, Wallace, ID 83873
(Address of principal executive offices and Zip Code)

(208) 556-0227
(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer.

Large Accelerated Filer Accelerated Filer Non-Accelerated Filer

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date: 32,237,202 shares of common stock as of August 9, 2007.

STERLING MINING COMPANY

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Part I – Financial Information

Item 1 Consolidated Financial Statements

**STERLING MINING COMPANY AND SUBSIDIARY
CONSOLIDATED BALANCE SHEETS**

| | June 30 2007 (unaudited) | December 31 2006 (audited) |
|--|--------------------------------|----------------------------------|
| ASSETS | | |
| CURRENT ASSETS | | |
| Cash | \$ 201,413 | \$ 3,054,582 |
| Marketable securities | 881,483 | 790,514 |
| Accounts receivable | 55,071 | 64,043 |
| Inventories | 429,523 | 313,467 |
| Prepaid expenses and deposits | 622,557 | 225,787 |
| Other current assets | 265,063 | 242,211 |
| Total current assets | <u>2,455,110</u> | <u>4,690,605</u> |
| INVESTMENTS | | |
| Investment in Chester Mining Company | 2,860,432 | 2,808,238 |
| Long-term Investments and Other Investments | 870,009 | 782,253 |
| Total investments | <u>3,730,441</u> | <u>3,590,491</u> |
| PROPERTY AND EQUIPMENT | | |
| Property, plant and equipment | 17,658,805 | 11,720,178 |
| Less accumulated depreciation | (133,210) | (72,603) |
| Total property and equipment | <u>17,525,595</u> | <u>11,647,575</u> |
| OTHER ASSETS | | |
| Prepaid long-term leases | 947,540 | 990,096 |
| Other assets | 12,911 | 1,600 |
| TOTAL ASSETS | <u>\$ 24,671,597</u> | <u>\$ 20,920,367</u> |
| LIABILITIES AND STOCKHOLDERS' EQUITY (DEFICIT) | | |
| CURRENT LIABILITIES | | |
| Accounts payable | \$ 2,441,484 | \$ 1,464,102 |
| Accrued expenses | 409,399 | 192,206 |
| Notes payable-current portion | 27,862 | 13,931 |
| Unearned revenue | 89,000 | 134,172 |
| Other current liabilities | — | 4,057,245 |
| Total current liabilities | <u>2,967,745</u> | <u>5,861,656</u> |
| LONG-TERM LIABILITIES | | |
| Notes payable | 505,832 | 519,763 |
| Total long-term liabilities | <u>505,832</u> | <u>519,763</u> |
| STOCKHOLDERS' EQUITY | | |
| Common stock, \$.05 par value; 80,000,000 shares authorized. 30,190,828, and 24,877,568 shares issued and outstanding at June 30, 2007 and December 31, 2006, respectively | 1,509,541 | 1,243,878 |
| Additional paid in capital | 45,764,694 | 32,674,757 |
| Common stock issuable | — | 400,000 |
| Accumulated deficit | (25,876,562) | (19,955,554) |
| Accumulated comprehensive income | (199,653) | 175,867 |
| TOTAL STOCKHOLDERS' EQUITY | <u>21,198,020</u> | <u>14,538,948</u> |
| TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY | <u>\$ 24,671,597</u> | <u>\$ 20,920,367</u> |

The accompanying condensed notes are an integral part of these interim financial statements

STERLING MINING COMPANY AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE LOSS

| | 3 Months Ended June 30 2007 (unaudited) | 3 Months Ended June 30 2006 (unaudited) | Six Months June 30 2007 (unaudited) | Six Months June 30 2006 (unaudited) |
|--|---|---|--|--|
| REVENUES | \$ 854,151 | \$ 316,509 | \$ 1,045,488 | \$ 597,033 |
| COSTS AND EXPENSES | | | | |
| Production costs applicable to sales | 265,208 | 303,985 | 513,369 | 528,433 |
| Exploration | 642,663 | 1,151,966 | 940,046 | 1,700,370 |
| Mine rehabilitation | 1,751,972 | — | 2,996,321 | — |
| General and administrative | 1,731,038 | 479,316 | 2,677,810 | 885,977 |
| Depreciation and amortization | 46,358 | 26,356 | 60,607 | 32,250 |
| Professional services | — | 219,997 | — | 312,967 |
| Total expenses | <u>4,437,239</u> | <u>2,181,622</u> | <u>7,188,153</u> | <u>3,459,997</u> |
| (LOSS) FROM OPERATIONS | <u>(3,583,088)</u> | <u>(1,865,112)</u> | <u>(6,142,665)</u> | <u>(2,862,964)</u> |
| OTHER INCOME (EXPENSE) | | | | |
| Gain (loss) on investments | 39,643 | 17,333 | 276,988 | 57,366 |
| Interest and dividends | 17,553 | 17,979 | 53,640 | 21,702 |
| Interest (expense) | (18,566) | (19,410) | (35,151) | (27,739) |
| Gain (loss) on derivative instruments | — | 146,958 | — | (59,467) |
| Gain (loss) on exchange | 6,394 | 63,960 | (73,628) | 6,220 |
| Other income | — | — | (746) | — |
| Total Other Income (Expense) | <u>45,024</u> | <u>226,820</u> | <u>221,103</u> | <u>(1,919)</u> |
| LOSS BEFORE INCOME TAXES | <u>(3,538,064)</u> | <u>(1,638,292)</u> | <u>(5,921,562)</u> | <u>(2,864,883)</u> |
| INCOME TAXES | <u>—</u> | <u>—</u> | <u>—</u> | <u>—</u> |
| LOSS FROM CONTINUING OPERATIONS | <u>(3,538,064)</u> | <u>(1,638,292)</u> | <u>(5,921,562)</u> | <u>(2,864,883)</u> |
| GAIN (LOSS) FROM INVESTMENT IN CHESTER MINING COMPANY | <u>(1,062)</u> | <u>—</u> | <u>554</u> | <u>—</u> |
| NET LOSS | <u>(3,539,126)</u> | <u>(1,638,292)</u> | <u>(5,921,008)</u> | <u>(2,864,883)</u> |
| OTHER COMPREHENSIVE INCOME (LOSS) | | | | |
| Unrealized gain (loss) on investments | (516,587) | (279,641) | (375,520) | 168,059 |
| COMPREHENSIVE INCOME (LOSS) | <u>\$ (4,055,713)</u> | <u>\$ (1,917,933)</u> | <u>\$ (6,296,528)</u> | <u>\$ (2,696,824)</u> |
| Basic and Fully Diluted Loss per Share | <u>\$ (0.12)</u> | <u>\$ (0.08)</u> | <u>\$ (0.20)</u> | <u>\$ (0.14)</u> |
| Basic and fully diluted weighted average shares outstanding | <u>29,890,900</u> | <u>20,105,300</u> | <u>29,578,000</u> | <u>19,821,400</u> |

The accompanying condensed notes are an integral part of these interim financial statements

**STERLING MINING COMPANY AND SUBSIDIARY
CONSOLIDATED STATEMENTS OF CASH FLOW**

| | Six Months ended June 30 2007 (unaudited) | Six Months ended June 30 2006 (unaudited) |
|---|---|---|
| CASH FLOWS FROM OPERATING ACTIVITIES: | | |
| Net income (loss) | \$ (5,921,008) | \$(2,864,883) |
| Adjustments to reconcile net loss to net cash used by operating activities: | | |
| Depreciation | 60,607 | 32,250 |
| Amortization of discount on debentures | — | 84,755 |
| Stock and options issued for services | 431,130 | — |
| (Gain) loss on investments | (276,988) | (57,366) |
| (Gain) loss on investment in Chester Mining Company | (554) | — |
| (Gain) loss on derivatives | — | 59,467 |
| Payments for lease expenses with stock | 25,346 | 1,005,000 |
| Payment of general & admin. expenses with stock | — | 5,200 |
| (Increase) decrease in: | | |
| Accounts receivable | 8,972 | (53,624) |
| Inventories | (116,056) | (23,058) |
| Prepaid expenses | (354,213) | (883,368) |
| Other current assets | (69,660) | (99,675) |
| Increase (decrease) in: | | |
| Accounts payable | 977,382 | 158,356 |
| Accrued expenses | 217,193 | (197,622) |
| Other current liabilities | (157,245) | (8,490) |
| Net cash used by operating activities | <u>(5,175,094)</u> | <u>(2,842,879)</u> |
| CASH FLOWS FROM INVESTING ACTIVITIES: | | |
| Purchase of investments | (644,696) | (276,703) |
| Proceeds from investments | 484,555 | 122,758 |
| Investment in property plant and equipment | (8,876,127) | (1,208,716) |
| Net cash provided (used) by investing activities | <u>(9,036,268)</u> | <u>(1,362,661)</u> |
| CASH FLOWS FROM FINANCING ACTIVITIES: | | |
| Proceeds from sales of common stock net of costs | 11,339,443 | 2,460,000 |
| Proceeds from exercise of stock options and warrants | 18,750 | 582,331 |
| Proceeds from debentures payable | — | 875,000 |
| Net cash provided by financing activities: | <u>11,358,193</u> | <u>3,917,331</u> |
| Net increase (decrease) in cash and cash equivalents | (2,853,169) | (288,209) |
| Cash beginning of period | <u>3,054,582</u> | <u>1,270,849</u> |
| Cash at end of period | <u>\$ 201,413</u> | <u>\$ 982,640</u> |
| SUPPLEMENTAL CASH FLOW DISCLOSURES: | | |
| Income taxes paid | \$ — | \$ — |
| Interest paid | \$ 35,151 | \$ 27,739 |
| NON-CASH INVESTING AND FINANCING ACTIVITIES: | | |
| Common stock issued for equipment | \$ — | \$ 90,000 |
| Common stock issued for leases | \$ 156,500 | \$ 1,005,000 |
| Common stock issued for land | \$ 1,362,500 | \$ — |
| Common stock and options issued for services | \$ 431,130 | \$ 5,200 |

The accompanying condensed notes are an integral part of these interim financial statements

STERLING MINING COMPANY AND SUBSIDIARY

CONDENSED NOTES TO FINANCIAL STATEMENTS JUNE 30, 2007

Sterling Mining Company is engaged in the business of acquiring, exploring, and developing mineral properties, primarily those containing silver and associated base and precious metals. It is operating the Barones silver plant and mining surface material at the San Acacio mine in Zacatecas, Mexico and is preparing the Sunshine Mine for production in Idaho. The Company was incorporated under the laws of the State of Idaho on February 3, 1903. The Company is headquartered at 609 Bank Street, Wallace, ID 83873.

Note 1: Basis of Presentation of Financial Statements

In the opinion of management, the accompanying unaudited consolidated balance sheet, consolidated statements of operations and comprehensive income (loss), consolidated statements of cash flows and notes to interim consolidated financial statements contain all adjustments necessary to present fairly, in all material respects, the financial position of Sterling Mining Company and its consolidated subsidiaries (the "Company"). Management has made all adjustments necessary for a fair statement of the results for the interim periods presented. These unaudited interim consolidated financial statements should be read in conjunction with our audited consolidated financial statements and related footnotes as set forth in our annual report filed on Form 10-K for the year ended December 31, 2006 as it may be amended from time to time.

The results of operations for the periods presented may not be indicative of those which may be expected for a full year. Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles in the United States ("GAAP") have been condensed or omitted as permitted by GAAP.

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities as of the date of the financial statements, the reported amounts of revenues and expenses during the reporting period and the disclosures of contingent liabilities. Accordingly, ultimate results could differ materially from those estimates.

Note 2: Summary of Significant Accounting Policies

This summary of significant accounting policies is presented to assist in understanding the financial statements. The financial statements and notes are representations of the Company's management, which is responsible for their integrity and objectivity. These accounting policies conform to accounting principles generally accepted in the United States of America and have been consistently applied in the preparation of the financial statements.

Accounting Method

The Company's financial statements are prepared using the accrual basis of accounting in accordance with accounting principles generally accepted in the United States of America.

Accounts Receivable

The Company carries its accounts receivable at net realizable value. On a periodic basis, the Company evaluates its accounts receivable and determines if an allowance for doubtful accounts is necessary, based on a history of past write-offs and collections and current credit conditions.

Asset Retirement Obligations

The Company accounts for asset retirement obligations and conditional asset retirement obligations in accordance with SFAS 143, FIN 47 and U.S. GAAP.

Cash and Cash Equivalents

The Company considers all highly liquid investments with an original maturity of three months or less to be cash equivalents.

Compensated Absences

Employees of the Company may be paid vacation, sick, and personal days off. The Company did not accrue compensated absences expense during the quarter because no policy on compensated absences had been adopted at June 30, 2007 and 2006, and management has deemed that any liability arising from these provisions in the future would be immaterial.

Concentration of Risk

The Company maintains its domestic cash in several commercial banks in Coeur d'Alene and Wallace, Idaho. Accounts are guaranteed by the Federal Deposit Insurance Corporation (FDIC) up to \$100,000. The Company also maintains cash in a Mexican bank. The Mexican accounts, one denominated in dollars and one denominated in pesos, are considered to be un-insured.

Derivative Instruments

The Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and Hedging Activities," (hereinafter "SFAS No. 133") as amended by SFAS No. 137, "Accounting for Derivative Instruments and Hedging Activities – Deferral of the Effective Date of FASB No. 133", and SFAS No. 138, "Accounting for Certain Derivative Instruments and Certain Hedging Activities" and SFAS No. 149, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities." These statements establish accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging activities. They require that an entity recognize all derivatives as either assets or liabilities in the consolidated balance sheet and measure those instruments at fair value. In February 2006, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 155, "Accounting for Certain Hybrid Financial Instruments, an Amendment of FASB Standards No. 133 and 140." (See Recent Accounting Pronouncements.)

If certain conditions are met, a derivative may be specifically designated as a hedge, the objective of which is to match the timing of gain or loss recognition on the hedging derivative with the recognition of (i) the changes in the fair value of the hedged asset or liability that are attributable to the hedged risk or (ii) the earnings effect of the hedged forecasted transaction. For a derivative not designated as a hedging instrument, the gain or loss is recognized in income in the period of change.

Historically, the Company has not entered into derivatives contracts to hedge existing risks.

The Company has issued convertible debt and accounts for that debt according to SFAS 133 and subsequent pronouncements. Consequently, management recognizes the convertible debt contract as a derivative instrument and accounted for the derivative according to U.S. GAAP. The Company had no derivative instruments at June 30, 2007 or December 31, 2006. The Company did issue a convertible debenture subsequent to June 30, 2007 as disclosed in Note 12.

Earnings Per Share

The Company has adopted Statement of Financial Accounting Standards No. 128, which provides for calculation of “basic” and “diluted” earnings per share.

Equity Method

The Company applies the equity method to account for investments for which it has significant influence upon the investee, according to APB Opinion 18 and subsequent pronouncements. During 2006 the Company acquired significant influence in Chester Mining Company and began accounting for its investment in Chester Mining Company using the equity method. The value of the Company’s investment in Chester Mining Company was approximately \$2.8 million at June 30, 2007. Sterling owns 45% of the voting shares of common stock issued and outstanding by Chester. The difference between the carrying value of the investment in Chester and the underlying equity in the net assets of Chester Mining Company is \$1,706,166. Consequently, management considers \$1,706,166 of its investment in Chester to be goodwill. Management has evaluated the investment in Chester Mining Company and does not consider it to be impaired.

Estimates

The preparation of financial statements in conformity with GAAP 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 revenues and expenses during the reporting period. Actual results could differ from those estimates.

Exploration Costs

In accordance with accounting principles generally accepted in the United States of America, the Company expenses exploration costs as incurred.

At least annually, management reviews the reserves used to estimate the quantities and grades of ore at our mines which management believes can be recovered and sold economically. Management’s calculations of proven and probable ore reserves are based on in-house engineering and geological assessments using current operating costs, metals prices and, when applicable, third-party audits of our reserves.

Fair Value of Financial Instruments

The Company’s financial instruments, as defined by Statement of Financial Accounting Standards No. 107, “Disclosures about Fair Value of Financial Instruments,” include cash, marketable securities, investments in stocks, purchase options, purchase warrants, receivables, payables and accrued expenses. Cash, receivables, payables and accrued expenses are accounted for on a historical cost basis, which, due to the short maturity of these financial instruments, approximate fair value at June 30, 2007 and 2006. Marketable securities, investments in stocks, purchase options and purchase warrants are accounted for by market prices when available, or by other valuation methods described in these notes when market prices are not available.

Foreign Currency Transactions

The Company created a Mexican subsidiary during 2004 for the purpose of exploration and exploitation of silver bearing minerals in Mexico. The Company records in United States dollars the assets and liabilities of its Mexico subsidiary according to GAAP. The Company translates into United States dollars the revenues, expenses, gains and losses of its Mexican subsidiary at the transaction

date and records them according to GAAP. Management has concluded that for the purposes of financial reporting, the functional currency of the Mexican subsidiary is the United States dollar. Consequently, management uses the temporal method of foreign currency translation.

Inventories

Metals inventories are carried at the lower of current market value or average unit cost. Production costs include the cost of direct labor and materials, depreciation, amortization, and overhead costs relating to mining and processing activities. Materials and supplies inventories are valued at the lower of average cost or net realizable value. Net realizable value is determined by market conditions and the cost to bring inventory to production. Sterling de Mexico had an inventory adjustment for the month of June, 2007 when average unit cost exceeded net realizable value. The inventories balances at June 30, 2007 and December 31, 2006 represented supplies inventory in Mexico and Idaho, minerals inventory in Mexico and the value of silver coins and other inventory in Idaho.

Mineral Development Costs

The Company will capitalize property acquisition costs for undeveloped mineral interests that have significant potential to develop an economic ore body. The Company will amortize the capital costs based on proven and probable ore reserves if an economic ore body is developed. If an economic ore body is not discovered, previously capitalized costs are expensed in the period in which it is determined that the property does not contain an economic ore body. Costs to develop new mines, to define further mineralization in existing ore bodies, and to expand the capacity of operating mines, are capitalized and will be amortized on a unit of production basis over proven and probable reserves. Gains and losses on the sales or retirement of assets are recorded as other income or expense.

Prepaid Expenses

The Company's current prepaid expenses primarily consist of prepaid insurance premiums, specialty equipment, prepaid lease payments which are paid for up to a year in advance and other pre-payments. Prepaid lease payments for periods beyond one year are considered other non-current assets. Non-current assets are primarily comprised of the Sunshine Mine lease and the Barones lease which was prepaid in 2004 and is being amortized over the 20 year lease term.

Minority Interest

The Company owns 99% of its Mexico subsidiary, Sterling Mining de Mexico S.A. de C.V. The 1% minority in the subsidiary is owned by an individual. A minority interest is not shown on the balance sheet because there is a negative value to the capital account of the minority interest holder. Additionally, the minority holder is not expected to make additional capital contributions.

Principles of Consolidation

The consolidated financial statements include the accounts of the Company and its majority-owned subsidiary after elimination of inter-company accounts and transactions. The majority-owned subsidiary of the Company is named above.

Property and Equipment

Property and equipment is recorded at cost. Depreciation of property and equipment is calculated using the straight-line method over the estimated useful lives of the assets, which range from three to ten years.

Provision for Taxes

Income taxes are provided based upon the liability method of accounting pursuant to Statement of Financial Accounting Standards No. 109, "Accounting for Income Taxes." Under this approach, deferred income taxes are recorded to reflect the tax consequences in future years of differences between the tax basis of assets and liabilities and their financial reporting amounts at each year-end. A valuation allowance is recorded against deferred tax assets if management does not believe the Company has met the "more likely than not" standard imposed by SFAS No. 109 to allow recognition of such an asset.

Recent Accounting Pronouncements

In September 2006, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 157, "Fair Value Measurement". Management does not expect the adoption of this statement to have a material impact on its consolidated financial position or results of operations when FAS 157 becomes effective, after November 15, 2007.

In February 2006, the FASB issued SFAS No. 155 "Accounting for Certain Hybrid Financial Instruments," which amends SFAS No. 133 "Accounting for Derivative Instruments and Hedging Activities" and SFAS No. 140 "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities." SFAS No. 155 resolves issues addressed in Statement 133 Implementation Issue No. D1 "Application of Statement 133 to Beneficial Interests in Securitized Financial Assets," and permits:

- Fair value remeasurement for any hybrid financial instrument that contains an embedded derivative that otherwise would require bifurcation;
- Clarifies which interest-only strips are not subject to the requirements of SFAS 133;
- Establishes a requirement to evaluate interests in securitized financial assets to identify interests that are freestanding derivatives or that are hybrid financial instruments that contain an embedded derivative requiring bifurcation;
- Clarifies that concentrations of credit risk in the form of subordination are not embedded derivatives; and
- Amends SFAS No. 140 to eliminate the prohibition on a qualifying special-purpose entity from holding a derivative financial instrument that pertains to a beneficial interest other than another derivative financial instrument.

FAS No. 155 is effective for all financial instruments acquired, issued or subject to a remeasurement event occurring after the beginning of an entity's first fiscal year that begins after September 15, 2007. The adoption of SFAS No. 155 is not expected to have a material effect on our consolidated financial statements.

In February 2006, the FASB issued FSP No. 123(R)-4 "Classification of Options and Similar Instruments Issued as Employee Compensation That Allow for Cash Settlement upon the Occurrence of Contingent Event." FSP 123(R)-4 amends paragraphs 32 and A229 of SFAS No. 123(R) to incorporate the concept that a cash settlement feature that can be exercised only upon the occurrence of a contingent event that is outside the employee's control does not meet the condition in paragraphs 32 and A229 until it becomes probable that the event will occur, and that an option or similar instrument that is classified as equity, but subsequently becomes a liability because the contingent cash settlement event is probable of occurring, shall be accounted for similar to a modification from an equity to liability award. FSP 123(R)-4 became effective when the Company adopted SFAS 123(R) and is not expected to have a material effect on the Company's consolidated financial statements.

In September 2005, the FASB issued Emerging Issues Task Force ("EITF") Issue No. 04-13 "Accounting for Purchases and Sales of Inventory with the same Counterparty." The scope of EITF No. 04-13 includes guidance on the circumstances under which two or more inventory purchases and sales transactions with the same counterparty should be viewed as a single exchange transaction under the scope of Opinion 29 "Accounting for Nonmonetary Transactions," and whether there are circumstances under which nonmonetary exchanges of inventory within the same line of business should be recognized at fair value. EITF No. 04-13 is effective for new arrangements entered into, or modifications or renegotiations of existing arrangements, beginning in the first interim or annual reporting period beginning after March 15, 2006. The adoption of EITF Issue No. 04-13 is not expected to have a material effect on our consolidated financial statements.

Note 3: Marketable Securities and Investments

The Company's investment portfolio consists primarily of small-cap mining stocks, options and warrants.

The Company's investments in securities are classified as either trading, held to maturity, or available-for-sale in accordance with Statement of Financial Accounting Standards No. 115. During the three months ended June 30, 2007 and 2006, the Company did not own any securities classified as trading or held to maturity, but did own securities classified as available-for-sale. Available-for-sale securities consist of equity securities not classified as trading securities or as securities to be held to maturity.

Unrealized holding gains and losses, net of tax, on available-for-sale securities are reported as a net amount in a separate component of other comprehensive income. Gains and losses on the sale of available-for-sale securities are determined using the average cost method and are included in earnings. The Company determines the gain or loss on investment securities held as available-for-sale, based upon the accumulated cost basis of specific investment accounts.

On the Company's balance sheet, short-term available for sale securities are classified as "marketable securities." Long-term available-for-sale securities and other investments are classified as "investments."

Options and warrants are recorded at fair market value, calculated using a conventional Black Scholes pricing model. Assumptions made in estimating the fair value include the risk-free interest rate, volatility and expected life. For the three months ended June 30, 2007, the average volatility ranged from 49% to 67%. Expected life used was the number of days to expiration. The risk-free interest

rate used was the Federal Reserve Boards risk-free rate most closely corresponding to the option or warrant lifetime. Management used risk free rates between 4.95% and 5.29 % for the three months ended June 30, 2007.

The changes in marketable securities, long-term investments, and investments-other during the three and six months ended June 30, 2007 are as follows:

| <u>Three Months ended June 30, 2007</u> | <u>Fair Value at March 31, 2007</u> | <u>Plus Purchases</u> | <u>Less Sales at Cost</u> | <u>Plus (Less) Unrealized Gain (Loss)</u> | <u>Fair Value at June 30, 2007</u> |
|---|---|---------------------------|-------------------------------|---|--|
| Investments Long-Term | \$ 638,286 | \$ 65,951 | \$ (32,216) | \$(134,620) | \$ 537,401 |
| Investment in Chester Mining Company | 2,859,510 | — | — | 922 | 2,860,432 |
| Investments Other | 424,014 | — | — | (91,406) | 332,608 |
| Total-Investments | 3,921,810 | 65,951 | (32,216) | (225,104) | 3,730,441 |
| Marketable Securities | 1,073,378 | 195,651 | (96,062) | (291,483) | 881,483 |
| Total-Marketable Securities and Investments | <u>\$ 4,995,188</u> | <u>\$261,602</u> | <u>\$(128,278)</u> | <u>\$(516,587)</u> | <u>\$4,611,924</u> |

At June 30, 2007 the total cost basis of marketable securities and investments was \$4,811,577.

Total accumulated losses were \$199,653 and the total fair market value was \$4,611,924.

Note 4: Income Tax

Income taxes are provided based upon the liability method of accounting pursuant to Statement of Financial Accounting Standards No. 109, "Accounting for Income Taxes." Under this approach, deferred income taxes are recorded to reflect the tax consequences in future years of differences between the tax basis of assets and liabilities and their financial reporting amounts at each year-end. A valuation allowance is recorded against deferred tax assets if management does not believe the Company has met the "more likely than not" standard imposed by SFAS No. 109 to allow recognition of such an asset.

At June 30, 2007, the Company had net deferred tax assets, calculated at an expected rate of 34%, of approximately \$6,720,000, principally arising from net operating loss carryforwards for income tax purposes. As management of the Company cannot determine that it is more likely than not that the Company will realize the benefit of the net deferred tax asset, a valuation allowance equal to the net deferred tax asset has been established at June 30, 2007.

The Company's deferred tax assets are estimated as follows:

| | <u>June 30, 2007</u> | <u>December 31, 2006</u> |
|--|--------------------------|------------------------------|
| Net operating loss carryforward | <u>\$19,760,000</u> | <u>\$14,290,000</u> |
| Deferred tax asset | <u>\$ 6,720,000</u> | <u>\$ 4,860,000</u> |
| Deferred tax asset valuation allowance | <u>\$(6,720,000)</u> | <u>\$(4,860,000)</u> |

At June 30, 2007, the Company has net operating loss carryforwards of approximately \$19,760,000, which expire in the years 2017 through 2026. The change in the allowance account from December 31, 2006 to June 30, 2007, was approximately \$1,860,000.

Note 5: Inventories

The Company uses the first-in-first-out method of inventory valuation.

Inventories in the United States consist of silver coins, rounds and bullion. Inventories in Mexico consist primarily of silver in precipitate form. Other components of inventory are gold in precipitate form as well as copper, thiosulfite and gravel used in the processing of mineral bearing ore. At June 30, 2007 and December 31, 2006 the Company reported the following inventories:

| | <u>June 30, 2007</u> | <u>December 31, 2006</u> |
|---|--------------------------|------------------------------|
| United States | | |
| Coins, rounds and bullion | \$ 58,086 | \$ 62,829 |
| Pyromorphite and other | 42,910 | 20,000 |
| Supply inventory for the Sunshine Mine | <u>31,471</u> | <u>58,546</u> |
| US Total | <u>132,467</u> | <u>141,375</u> |
| Mexico | | |
| Silver and gold precipitate & concentrate | 215,586 | 108,809 |
| Supplies and other inventory | <u>81,470</u> | <u>63,283</u> |
| Mexico Total | <u>297,056</u> | <u>172,092</u> |
| Consolidated Total | <u>\$429,523</u> | <u>\$ 313,467</u> |

At June 30, 2007 and December 31, 2006, the precipitate and concentrate in Mexico was either on-site, in transit, or at the refinery.

Note 6: Commitments and Contingencies

Mineral Leases

The Company has secured leases of a number of mineral properties. Each of the leases is subject to lease payments as shown in the table below.

| <u>Mineral Leases</u> | <u>Production Royalties Payable (1)</u> | <u>2007 Annual Lease Fees</u> |
|---|---|---------------------------------------|
| Barones Concession (2) | Yes | \$ — |
| Chester Claim Group (3) | Yes | 7,200 |
| J.E. Prospect | Yes | 12,500 |
| Jestec | Yes | 15,000 |
| Merger Mines Claim Group | Yes | 2,500 |
| Metropolitan Mines Claim Group | Yes | 12,000 |
| Mineral Mountain Claim Group | Yes | 3,600 |
| Montana Revett Claim Group (4) | Yes | — |
| San Acacio Concession (5) | Yes | — |
| Sunshine Mine and Infrastructure, ARI lease | Yes | 120,000 |
| Timberline Resources (6) | Yes | 20,000 |
| Rock Creek-Idaho (7) | Yes | 6,000 |
| Jimenez de Teul (8) | Yes | — |
| Cuatro Cienegas (9) | Yes | \$ — |

(1) All leases are subject to production royalties

- (2) \$375,000 in cash and \$100,000 in the Company's common stock were prepaid in 2004 to apply to the life of the Barones lease of 240 months. There are no annual lease fees.
- (3) The Chester Claim Group lease also requires an annual payment of 50,000 shares of the Company's common stock.
- (4) Production royalties are not payable to lessor, but are payable to third parties.
- (5) \$150,000 paid by Source Minerals in June 2007.
- (6) Timberline annual lease fee of \$20,000 began on June 1, 2007.
- (7) The lease includes a \$50,000 per year work commitment and payments of \$500 a month, which can be credited against the 25% net profits royalty.
- (8) The lease includes a \$50,000 work commitment in 2007 and additional work commitments of \$100,000 for each of the next four years.
- (9) The lease includes payments of \$100,000 per year for each of the next five years.

The total value of shares issued for leases and lease amendments for the three and six months ended June 30, 2007 was \$156,500. The total number of shares of common stock issued for leases for the three and six months ended June 30, 2007 was 50,000.

Other Leases

The Company entered into a lease for office space in Coeur d'Alene, Idaho for \$1,763 per month through November 2007.

The Company's obligations under mineral agreements and office space operating lease agreements as of June 30, 2007 are as follows:

| Year Ending: | |
|-------------------------------------|---------------------------|
| December 31, 2007 | \$ 115,788 |
| December 31, 2008 | 280,176 |
| December 31, 2009 | 300,176 |
| December 31, 2010 | 300,176 |
| December 31, 2011 | 300,176 |
| Total minimum lease payments | <u>\$1,296,492</u> |

Compliance with Environmental Regulations

The Company is subject to a variety of federal, state and local statutes, rules and regulations designed to protect human health and the environment in the vicinity of its mining operations. Activities at the Company's mining operations include continual efforts to meet

or exceed these statutes, rules and regulations. These regulations include “permitting” or pre-operating approval requirements designed to ensure the environmental integrity of a proposed mining facility, operating requirements to mitigate the effects of discharges into the environment during mining operations, and reclamation or post-operation requirements designed to remediate the lands affected by a mining facility. The Company is diligently working with the regulatory agencies for the necessary environmental and bonding requirements to comply with the regulations.

Other Taxes

The Company assumed certain property taxes in arrears as part of the Company’s obligation in the lease of the Sunshine Mine. The Company has paid property taxes in arrears for the years 1999 through 2004. Estimated tax liabilities including penalties and interest outstanding are shown below.

| | |
|--------------------------------|-------------------------|
| Tax Year: | |
| 2005 | \$ 37,762 |
| 2006 | 38,400 |
| 2007 | 20,000 |
| Accrued Penalties and Interest | <u>10,700</u> |
| Balance, June 30, 2007 | <u><u>\$106,862</u></u> |

Note 7: Notes Payable

At June 30, 2007, the Company had three notes payable as follows: \$400,000 to Western Continental for a land purchase, \$50,000 to Diversified Machine Technology (DMT) for a land purchase and \$83,694 to Microsoft Corporation for the purchase of computer hardware and software. The notes payable current portion on the balance sheet is \$27,862 representing the current portion of the Microsoft note. Notes payable long-term on the balance sheet is \$505,832, the sum of the \$400,000 Western Continental note, the \$50,000 DMT note and \$55,832 from the long-term portion of the Microsoft note.

The notes payable have the following terms: The Western Continental note has a 7.25% interest rate, monthly interest payments of \$2,417, with payment of the principal due in full on November 6, 2008. The DMT note has a maturity date of October 6, 2008, when the principal is due in full. No payment is due until the maturity date. The Microsoft note has monthly payments of \$50 for six months and then \$2,803 for the succeeding 36 months. Interest and principal are scheduled to be paid in full on July 1, 2010. Each note is collateralized by the asset acquired.

Note 8: Common Stock, Options and Warrants

During the second quarter of 2007 the Company issued 1,422,260 shares of common stock as follows: 550,000 shares, with warrants attached, for \$1,980,000; and 250,000 shares for land. 475,260 warrants were exercised during the quarter of 2007 for a total of \$1,619,704 and 310,000 warrants were granted. The warrants were valued at \$311,857 at June 30, 2006 and the weighted average exercise price of the warrants is \$4.50. The Company granted 850,000 options during the quarter to officers, directors, employees and consultants.

During the second quarter of 2006, the Company issued 1,158,608 shares of common stock as follows: 435,000 shares for \$1,100,000 in cash; 40,000 shares for lease expense and equipment; and 665,108 shares upon the exercise of \$0.75 per share stock options that were granted in June of 2003. 17,500 warrants were exercised during the quarter for \$70,000 and 572,500 warrants, valued at \$722,287, were granted at a weighted average exercise price of \$6.41.

Note 9: Loss per Common Share

The Company is authorized to issue 80,000,000 shares of common stock, \$0.05 par value per share, of which 30,190,828 shares were issued at June 30, 2007. The weighted average shares of common stock outstanding for the quarter ended June 30, 2007 were 29,890,900.

The Company has adopted Statement of Financial Accounting Standards No. 128, which provides for calculation of “basic” and “diluted” earnings per share. Basic earnings per share includes no dilution and is computed by dividing net income available to common shareholders by the weighted average common shares outstanding for the period. Diluted earnings per share reflect the potential dilution of securities that could share in the earnings of an entity similar to fully diluted earnings per share. Although there were common stock equivalents outstanding June 30, 2007, they were not included in the calculation of earnings per share because they would have been considered anti-dilutive.

As of June 30, 2007, the Company had issued and outstanding 9,984,480 warrants, 850,000 options, commitments to issue 40,294 shares, and convertible debt that could be converted to 80,000 shares of common stock. Earnings would be fully diluted by 10,954,774 shares if the Company had earnings to report.

Note 10: Business Segments

The Company began reporting two business segments during 2004. One segment is the exploration segment in the United States of America. The Company engages in the acquisition and exploration of mineral properties in the U.S.A. in this segment. The Company’s other segment, acquired in 2004, is the Mexico exploration segment. The Company acquired the Mexican operation in 2004 and began reporting two segments subsequent to the acquisition. Due to this change in the composition of reportable segments, all prior periods have been restated.

The Mexico segment includes the Company’s 99% owned subsidiary Sterling Mining De Mexico, S.A. De C.V. The Mexico segment engages in the acquisition exploration and operation of mineral properties in Mexico. The Company’s objective in each segment is to place those properties that can be operated at a profit into production. The following table presents information about reportable segments for the three and six months ended June 30, 2007 and 2006:

| | Three Months Ended June 30 | | Six Months Ended June 30 | |
|--------------------------------------|----------------------------|----------------------|--------------------------|----------------------|
| | 2007 | 2006 | 2007 | 2006 |
| Revenues: | | | | |
| United States | \$ 224,935 | \$ 37,133 | \$ 232,917 | \$ 47,951 |
| Mexico | 629,216 | 279,375 | 812,571 | 549,082 |
| Total | <u>\$ 854,151</u> | <u>\$ 316,509</u> | <u>\$ 1,045,488</u> | <u>\$ 597,033</u> |
| Income (loss) from operations | | | | |
| United States | \$(3,432,625) | \$(1,628,431) | \$(5,803,437) | \$(2,611,252) |
| Mexico | (150,463) | (236,681) | (339,228) | (251,712) |
| Total | <u>\$(3,583,088)</u> | <u>\$(1,865,112)</u> | <u>\$(6,142,665)</u> | <u>\$(2,862,964)</u> |
| Net Income (Loss) | | | | |
| United States | \$(3,394,476) | \$(1,424,624) | \$(5,506,542) | \$(2,618,578) |
| Mexico | (144,650) | (213,668) | (414,466) | (246,305) |
| Total | <u>\$(3,539,126)</u> | <u>\$(1,638,292)</u> | <u>\$(5,921,008)</u> | <u>\$(2,864,883)</u> |
| Identifiable Assets: | | | | |
| United States | \$ Same as | Same as | \$22,881,200 | \$ 5,429,085 |
| Mexico | 6 mo. | 6 mo. | 1,790,397 | 643,772 |
| Total | <u>Column</u> | <u>Column</u> | <u>\$24,671,597</u> | <u>\$ 6,072,857</u> |
| Capital Expenditures: | | | | |
| United States | \$ 3,498,256 | \$ 1,012,597 | \$ 5,534,763 | \$ 1,148,902 |
| Mexico | 184,459 | 113,408 | 403,864 | 149,814 |
| Total | <u>\$ 3,682,715</u> | <u>\$ 1,126,005</u> | <u>\$ 5,938,627</u> | <u>\$ 1,298,716</u> |

Note 11: Significant Customers

During the three and six months ended June 30, 2007 all sales were to one refinery, Met-Mex Penoles.

Note 12: Subsequent Events

In July of 2007 the Company issued one debenture for a total of \$100,000, prior to completing its recent private placement offerings. The debenture included a provision for the conversion of the debt, at a conversion price of \$4.25, to a total of 23,529 shares of the Company's common stock. The debenture expires after eighteen months and is convertible after twelve months. The Company is paying the holder of the debenture a monthly interest payment at an annual percentage rate of 12.0 %.

On August 2, 2007 the Company closed two private placement offerings that in the aggregate raised a total of \$24,734,755.50.

In a brokered offering, the offering consisted of 5,585,792 special warrants at a price of \$3.25 per special warrant. Each special warrant is convertible into one common share of the Company and one-half of one common share purchase warrant. Conversion shall occur upon the issuance of a receipt for a final prospectus in Canada that qualifies the common shares and warrants. Each whole warrant is exercisable for one common share at an exercise price of \$4.10 for 24 months following the closing date of the brokered offering. The brokered offering was completed on a best-efforts basis with TD Securities Inc. and Blackmont Capital Inc. of Toronto, Canada, who were engaged as co-agents.

In a second offering in the United States and elsewhere, the offering consisted of 2,024,902 units at the same price of \$3.25 per Unit. Each unit is comprised of one common share of the Company and one-half of one common share purchase warrant. Each warrant is similarly exercisable for one Common Share at an exercise price of \$4.10 for 24 months following the closing date of the Offering.

In connection with the Brokered Offering, the Company paid a cash commission of 7% of the gross proceeds of the private placement, and issued non-transferable compensation options to purchase 391,005 special warrants, equal to 7% of the special warrants sold under the private placement, exercisable at \$3.25 per special warrant for a period of 24 months after the closing date of the Offering.

In connection with the second offering, the Company paid cash commissions, and issued similar non-transferable compensation options to purchase units, common shares and warrants not exceeding 7% of the gross proceeds.

Item 2: Management's Discussion and Analysis of Financial Condition and Results of Operations

Statements contained in this Form 10-Q, including in "Management's Discussion and Analysis of Financial Condition and Results of Operations" and "Quantitative and Qualitative Disclosure About Market Risk", are intended to be covered by the safe harbor provided for under Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. Our forward-looking statements include our current expectations and projections about future results, performance, results of litigation, prospects and opportunities. We have tried to identify these forward-looking statements by using words such as "may," "will," "expect," "anticipate," "believe," "intend," "feel," "plan," "estimate," "project," "forecast" and similar expressions. These forward-looking statements are based on information currently available to us and are expressed in good faith and believed to have a reasonable basis. However, our forward-looking statements are subject to a number of risks, uncertainties and other factors that could cause our actual results, performance, prospects or opportunities to differ materially from those expressed in, or implied by, these forward-looking statements.

These risks, uncertainties and other factors include, but are not limited to, those set forth under Part I, Item 1A – Risk Factors in our annual report filed on Form 10-K for the year ended December 31, 2006. Given these risks and uncertainties, readers are cautioned not to place undue reliance on our forward-looking statements. All subsequent written and oral forward-looking statements attributable to Sterling Mining Company or to persons acting on our behalf are expressly qualified in their entirety by these cautionary statements. Except as required by federal securities laws, we do not intend to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

Overview

Sterling Mining Company is a minerals, exploration, development and a producing company traded on the over the counter market in the United States. As is typical with such companies, losses are incurred in the stages of exploration and development, which typically need to be funded through equity or debt financing. Sterling has expanded rapidly its range of activities since 2003 and this has generated funding requirements for

- the initiation of and advancing of rehabilitation, maintenance, exploration and mine planning at the Sunshine Mine,

- the initial entry into Mexico, acquisition costs of projects, and the financing and construction of the Barones plant, and
- increasing both administrative and operational staff to manage the increased scope of Sterling's activities.

Our main focus is the Sunshine Mine project where we are engaged in maintenance, rehabilitation, exploration and mine planning. We also have exploration interests in Idaho, Montana, and in Mexico. We have a land position of early stage prospects in Idaho, Montana and Mexico that we are evaluating to determine whether to hold and explore or seek the participation of industry partners.

The Company's operating mines are the Barones silver project and the San Acacio mine in Zacatecas, Mexico. Total production for the quarter was 18,843 ounces of silver and 18 ounces of gold compared to 23,618 ounces of silver and 53 ounces of gold in the second quarter of 2006. At the Barones silver project in Mexico, silver production was 12,502 ounces of silver and 15 ounces of gold in the second quarter of 2007. San Acacio ore processed at an outsourced concentrating facility resulted in additional silver production of 6,341 ounces of silver and 3 ounces of gold during the quarter. The company realized a price of \$13.00 per ounce of silver and \$656.84 per ounce of gold in the second quarter of 2007 compared to \$11.93 and \$617.88 respectively in the second quarter of 2006.

Management anticipates that by bringing the Barones crusher facility into operation in July of 2007, recoveries and profitability will improve. As of June 30, 2007, the jaw and cone crusher had been installed and remaining infrastructure was complete. The electrical permits have been received and start-up testing began on July 28, 2007. The Company is currently stockpiling San Acacio ore at the mill for processing once the crusher is fully operational.

The Company's principal project is the Sunshine Mine in the State of Idaho. Management expects to begin production in December 2007. Rehabilitation and development expenses of the Sunshine Mine during the second quarter of 2007 were approximately \$4.2 million. Expenditures on the Sterling Tunnel were \$2.5 million in the quarter ended June 30, 2007, all of which was capitalized.

The Sterling Tunnel project initiated in January 2006 and completed in April 2007 now provides access for exploration and a corridor for ventilation, services and travel between the Big Creek and Rosebud Creek sides of the mine. In addition the tunnel provides the required secondary escapeway serving both the Silver Summit hoistroom and Sterling Tunnel exploration areas. The Company continued underground diamond drilling during the quarter and completed development of a 750 foot cross-cut project designed to access the Polaris stope and intersect an un-mined projection of the Sunshine vein. Drifting on the vein structure to determine its extent and mineral content along strike will begin in late August. Sterling crews also resumed work on a rail serviced cross-cut into un-mined ground east of the Polaris workings to expose projected vein structures and establish a drill platform to explore the Yankee Girl vein 1,200 feet to the south.

The Company hired twenty-three employees at the Sunshine Mine during the quarter resulting in a total workforce of sixty-four. Work neared completion on the Silver Summit hoist which began final commissioning activities in July 2007. Rehabilitation of the Silver Summit shaft at the top station began as the first step to re-establish the shaft as a secondary escapeway required by law in order to commence production from "lower country" areas of the mine.

Dewatering in the Jewell shaft began and the water level lowered approximately 50 feet during the quarter. A major substation and ventilation drift necessary to reduce 13,200 volt primary feed power to 2,400 volt level feed power were excavated on the 3,100 level adjacent to the Jewell shaft. Mill crews worked through the crushing circuit, conveyors and ore storage bins and began work required to renovate the grinding and floatation circuits. Number 5 compressor was returned to service to meet increasing compressed air demand. Underground diesel equipment started arriving on site and will initially be used in Sterling Tunnel exploration and development. The Company continued to order and receive equipment and supplies as well as re-stock its mine warehouse to meet the ongoing development plan.

The Company has exploration projects in Idaho, Montana and Mexico. During the second quarter of 2007, Sterling Mining Company continued acquisition and assessment of exploration properties in Mexico. The Company intends to enter into joint ventures with other junior exploration companies on several of its projects while advancing other projects by itself. Drilling on the properties near Ojo Caliente is scheduled for early August 2007.

The results of the Company's operations are significantly affected by the market prices of silver which may fluctuate widely and are affected by many factors beyond the Company's control including, without limitation, interest rates, expectations regarding inflation, currency values, governmental decisions regarding the disposal of precious metals stockpiles, global and regional political and economic conditions, and other factors. The average prices of silver (London Final) and gold (London Final) for the three months ended June 30, 2007 were \$13.23 and \$667.58 per ounce, respectively. The average prices of silver (London Final) and gold (London Final) for the three months ended June 30, 2006 were \$12.23 and \$627.58 per ounce, respectively.

Comparative Results of Operations

For the three and six months ended June 30, 2007 compared to three and six months ended June 30, 2006:

Revenues

Lease and contract income for the six months ended June 30 was \$641,885 in 2007 and \$12,100 in 2006. The increase was primarily due to revenues from the 2007 agreements with Source Minerals, Silver Fields and Aura Silver.

Sales of metal from continuing operations in the second quarter and first six months of 2006 consisted of sales of silver and gold from the refinery in Zacatecas, Mexico and coin revenues in the USA from the sale of coins, rounds and bullion. Total sales for the quarter were \$212,266 in 2007 and \$316,509 in 2006. Total sales for the six months ended June 30, 2007 were \$403,603 in 2007 and \$597,033 in 2006. Sales in the second quarter in Mexico were \$209,231 in 2007 and \$279,376 in 2006. Sales for the six months ended June 30 in Mexico were \$392,586 in 2007 and \$549,082 in 2006. Revenue was lower than expected, largely due to a delay in sales. May production was encouraging but concentrate and precipitate produced in May had not been sold as of June 30.

Sales in the second quarter in the USA were \$4,384 in 2007 and \$37,133 in 2006. Sales for the six months ended June 30 in the USA were \$11,017 in 2007 and \$47,951 in 2006. Decrease in sales revenue in the USA was due to decreased sales volume, as staff spent more time preparing for the opening of the Sunshine Mine and less time on coin sales.

Costs and Expenses

The cost of production for the quarter was slightly less in Mexico and in the US compared to one year ago. The decrease was due to a decrease in sales in both countries. The Company reported "Production Costs Applicable to Sales" of \$265,208 in the second quarter of 2007 and \$303,985 in the second quarter of 2006. "Production Costs Applicable to Sales" for the six months ended June 30 was \$513,369 in 2007 and \$528,433 in 2006. "Production Costs Applicable to Sales" for the second quarter in Mexico was \$262,435 in 2007 and \$289,260 in 2006. "Production Costs Applicable to Sales" for the six months ended June 30 in Mexico was \$503,010 in 2007 and \$507,305 in 2006. The Cost of Revenues for coin sales in the U.S. was \$2,773 and \$14,726 in the second quarters of 2007 and 2006 respectively. The Cost of Revenues for coin sales in the U.S. was \$10,359 and \$21,128 for the six months ended June 30 of 2007 and 2006 respectively.

Total operating expenses increased from \$2,181,622 in the second quarter of 2006 to \$4,437,239 in 2007, as the Company accelerated its activity to prepare the Sunshine Mine for operation. As a result, the loss from operations increased from \$1,865,112 in the second quarter of 2006 to \$3,583,088 in 2007 and the net loss for the quarter increased from \$1,638,292 in 2006 to \$3,538,064 in 2007.

For the six months ended June 30 operating expenses increased from \$3,459,997 in 2006 to \$7,188,153 in 2007. As a result, the loss from operations increased from \$2,862,964 in 2006 to \$6,142,665 in 2007 and the net loss for the six month period increased from \$2,864,883 in 2006 to \$5,921,562 in 2007. The reason for the increase is the same as above, an acceleration of activities to prepare the Sunshine Mine for operations.

Other Income and Expenses

Other income and expense for the quarter resulted in a net gain of \$45,024 in 2007 and \$226,820 in 2006. The largest component of that income in the second quarter of 2007 was gain on the sale of investments. The largest component of that income in the second quarter of 2006 was gain on derivative instruments.

Other income and expense for the six months ended June 30 resulted in a net gain of \$221,103 in 2007 and a net expense of \$1,919 in 2006. The largest component of other income in those six months of 2006 was gain on the sale of investments. The largest component of other income in those six months of 2006 was loss on derivative instruments.

Income Taxes

Sterling Mining Company has a substantial net operating loss for U.S. income tax purposes. Sterling de Mexico has a net tax asset of IVA tax refundable in Mexico of approximately \$216,000.

Liquidity and Capital Resources

The Company's cash balance at June 30, 2007 was \$201,413. During the three and six months ended June 30, 2007, the Company received cash upon the exercise of options and warrants, and private placement of common stock. Total cash provided by financing activities was approximately \$3.5 million in the second quarter and \$11.4 million in the six months ended June 30, 2007.

Although the Company had negative working capital at June 30, the Company closed an equity financing for gross proceeds of approximately \$24.7 million on August 2, 2007. We believe that this funding will be sufficient to meet our operating and capital needs in 2007. Whether we will need to seek additional financing from external sources in 2008 will depend on a number of factors,

including, when production begins at the Sunshine Mine, the level of production and silver prices, whether production from our properties in Mexico increases, and other circumstances that are difficult to predict until Sterling has completed its development activities and achieved a sustained period of production. Management has been successful in raising capital through private equity offerings and may seek additional debt and/or equity funding for future operations if needed. There can be no assurances that financing will be available through private equity or debt offerings, if needed.

The Company has received conditional approval from the Toronto Stock Exchange (“TSX”) to list its common shares on the TSX, subject to fulfilling all requirements of the TSX and filing of customary documentation on or prior to October 30, 2007.

The Company’s use of funds has been growing due to increasing exploration activities both in Mexico and at the Sunshine Mine in Idaho. Rehabilitation of the Sunshine Mine has been the primary use of funds for capital expenditures. The installation of the crusher at the Barones silver plant was the second largest capital expenditure during the quarter. Corporate General and Administrative expense has grown since the second quarter of 2006 as the Company expanded its operational and administrative staff. As the Company grows and prepares for the operation of the Sunshine Mine, management anticipates further capital improvements, equipment purchases and staff increases.

Management has been successful in raising capital through private equity offerings and may seek additional debt and/or equity funding for future operations if needed. While the Company believes its cash, cash equivalents and short-term investments and cash from operations will be adequate to meet its obligations in 2007. There can be no assurances that financing will be available through private equity or convertible debt offerings, if needed.

The financing requirements of the Company will grow as the Sunshine Mine project advances during the next stages in 2007. To achieve internal objectives and timetables will require approximately \$20 million to bring the mine into production. Gross proceeds of approximately \$24.7 million in financing were secured in August of 2007. Should the mine fail to produce positive operating cash flows, there is no assurance the Company will be successful in its fund raising efforts in future years, or that its Mexican operations can generate significant excess cash to help fund operating expenses.

The capital requirements of the Company’s Mexican operations will be dependent on the profits and cash flow from Barones and San Acacio operations, results of economic and technical studies on our other projects and any exploration projects the Company may select for advancement.

Contractual Obligations

The Company is obligated under certain contractual arrangements for future cash expenditures. The following table sets forth our contractual obligations for the periods shown:

| | Total | Payments due by period | | | |
|--------------------------|--------------------|------------------------|--------------------|------------------|------------------|
| | | Less than 1 Year | 1-3 Years | 3-5 Years | After 5 Year |
| Notes Payable | \$ 533,694 | \$ 27,862 | \$ 505,832 | — | — |
| Operating Leases: | | | | | |
| J.E. Prospect | \$ 65,000 | \$ 12,500 | \$ 12,500 | \$ 20,000 | \$ 20,000 |
| Jestec | 130,000 | 15,000 | 15,000 | 50,000 | 50,000 |
| American Reclamation | 480,000 | 120,000 | 120,000 | 120,000 | 120,000 |
| Chester Mining Company | 27,000 | 5,400 | 7,200 | 7,200 | 7,200 |
| Mineral Mountain | 14,400 | 3,600 | 3,600 | 3,600 | 3,600 |
| Merger Mines | 15,000 | 2,500 | 2,500 | 5,000 | 5,000 |
| Timberline Resources | 80,000 | 20,000 | 20,000 | 20,000 | 20,000 |
| Metropolitan Mines | 47,000 | 11,000 | 12,000 | 12,000 | 12,000 |
| Rock Creek Mining | 23,500 | 5,500 | 6,000 | 6,000 | 6,000 |
| San Acacio | — | — | — | — | — |
| Jimenez de Teul | 600,000 | 50,000 | 350,000 | 200,000 | — |
| Cuatro Cienegas | 500,000 | — | 200,000 | 300,000 | — |
| Sub-total Leases | \$1,981,900 | \$245,500 | \$ 748,800 | \$743,800 | \$243,800 |
| Total Obligations | \$2,515,594 | \$273,362 | \$1,254,632 | \$743,800 | \$243,800 |

Critical Accounting Policies and Estimates

The Company has determined from the significant accounting policies as disclosed in our financial statements, that the following two disclosures are critical accounting policies.

Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

At least annually, management reviews the reserves used to estimate the quantities and grades of ore at our mines which management believes can be recovered and sold economically. Management's calculations of proven and probable ore reserves are based on in-house engineering and geological assessments using current operating costs, metals prices and, when applicable, on third-party audits of our reserves.

Reserve estimates will change as existing reserves are depleted through production and as production costs and/or metals prices change. A significant drop in metals prices may reduce reserves by making some portion of such ore uneconomic to develop and produce. Changes in reserves may also reflect that actual grades of ore processed may be different from stated reserve grades because of variation in grades in areas mined, mining dilution and other factors. Estimated reserves, particularly for properties that have not yet commenced production, may require revision based on actual production experience.

Declines in the market prices of metals, increased production or capital costs, reduction in the grade or tonnage of the deposit or an increase in the dilution of the ore or reduced recovery rates may render ore reserves uneconomic to exploit. If our realized price for the metals we produce were to decline substantially below the levels set for calculation of reserves for an extended period, there could be material delays in the development of new projects, net losses, reduced cash flow, restatements or reductions in reserves and asset write-downs in the applicable accounting periods. Reserves should not be interpreted as assurances of mine life or of the profitability of current or future operations. No assurance can be given that the estimate of the amount of metal or the indicated level of recovery of these metals will be realized.

Mineral Exploration and Development Costs

The Company has been engaged in exploration since 1998.

In accordance with GAAP, the Company expenses exploration costs as incurred. Significant property acquisition costs for undeveloped mineral interests that have significant potential to develop an economic ore body are capitalized. The Company will amortize the capital costs based on proven and probable ore reserves if an economic ore body is developed. If an economic ore body is not discovered previously capitalized costs are expensed in the period in which it is determined that the property does not contain an economic ore body. Costs to develop new mines, to define further mineralization in existing ore bodies, and to expand the capacity of operating mines are capitalized and will be amortized on units of production basis over proven and probable reserves. Gains and losses on the sales or retirement of assets are recorded as other income or expense.

The Company expects to have reserves in the future on any development it deems commercially viable. The essential nature of any reserves acquired or discovered will be estimates based upon ore body information presented to and reviewed by professionals. The enterprise of exploration and mining are subject to substantial uncertainties in development and operations. The Company continues to recruit a team of operational professionals, with the highest standards for reporting always being in the forethought of management.

Any estimates arising out of our exploration, development and operational activities will be expected to be reviewed under current internal policies. Our current environment has had only a short period of active operations and management believes that all exploration, development and operating policies are being accurately maintained. Our future operations will be heavily dependent on the market values of precious metals and our estimated costs of production. As these determinants change we would expect analysis by management of both short-term and long-term conditions, which could have a negative impact on the Company's choices concerning development and operations of its existing and future acquired properties.

Recent Accounting Pronouncements

In September 2006, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards No. 157, "Fair Value Measurement". Management does not expect the adoption of this statement to have a material impact on its consolidated financial position or results of operations when FAS 157 becomes effective, after November 15, 2007.

In February 2006, the FASB issued SFAS No. 155 "Accounting for Certain Hybrid Financial Instruments," which amends SFAS No. 133 "Accounting for Derivative Instruments and Hedging Activities" and SFAS No. 140 "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities." SFAS No. 155 resolves issues addressed in Statement 133 Implementation Issue No. D1 "Application of Statement 133 to Beneficial Interests in Securitized Financial Assets," and permits:

- Fair value remeasurement for any hybrid financial instrument that contains an embedded derivative that otherwise would require bifurcation;
- Clarifies which interest-only strips are not subject to the requirements of SFAS 133;
- Establishes a requirement to evaluate interests in securitized financial assets to identify interests that are freestanding derivatives or that are hybrid financial instruments that contain an embedded derivative requiring bifurcation;

- Clarifies that concentrations of credit risk in the form of subordination are not embedded derivatives; and
- Amends SFAS No. 140 to eliminate the prohibition on a qualifying special-purpose entity from holding a derivative financial instrument that pertains to a beneficial interest other than another derivative financial instrument.

Amends SFAS No. 140 to eliminate the prohibition on a qualifying special-purpose entity from holding a derivative financial instrument that pertains to a beneficial interest other than another derivative financial instrument.

FAS No. 155 is effective for all financial instruments acquired, issued or subject to a remeasurement event occurring after the beginning of an entity's first fiscal year that begins after September 15, 2006. The adoption of SFAS No. 155 is not expected to have a material effect on our consolidated financial statements.

In February 2006, the FASB issued FSP No. 123(R)-4 "Classification of Options and Similar Instruments Issued as Employee Compensation That Allow for Cash Settlement upon the Occurrence of Contingent Event." FSP 123(R)-4 amends paragraphs 32 and A229 of SFAS No. 123(R) to incorporate the concept that a cash settlement feature that can be exercised only upon the occurrence of a contingent event that is outside the employee's control does not meet the condition in paragraphs 32 and A229 until it becomes probable that the event will occur, and that an option or similar instrument that is classified as equity, but subsequently becomes a liability because the contingent cash settlement event is probable of occurring, shall be accounted for similar to a modification from an equity to liability award. FSP 123(R)-4 became effective when we adopted SFAS 123(R) and is not expected to have a material effect on our consolidated financial statements.

In September 2005, the FASB issued Emerging Issues Task Force ("EITF") Issue No. 04-13 "Accounting for Purchases and Sales of Inventory with the same Counterparty." The scope of EITF No. 04-13 includes guidance on the circumstances under which two or more inventory purchases and sales transactions with the same counterparty should be viewed as a single exchange transaction under the scope of Opinion 29 "Accounting for Nonmonetary Transactions," and whether there are circumstances under which nonmonetary exchanges of inventory within the same line of business should be recognized at fair value. EITF No. 04-13 is effective for new arrangements entered into, or modifications or renegotiations of existing arrangements, beginning in the first interim or annual reporting period beginning after March 15, 2006. The adoption of EITF Issue No. 04-13 is not expected to have a material effect on our consolidated financial statements.

Item 3 Quantitative and Qualitative Disclosures About Market Risk

Market risk is the potential loss arising from adverse changes in market rates and prices, such as foreign currency exchange, interest rates, and commodity prices. The Company's operations in Mexico could potentially be affected by a change in the exchange rate of Mexican pesos into American dollars.

Item 4 Controls and Procedures

The Company's disclosure controls and procedures are designed to provide reasonable assurance that information required to be disclosed by it in its periodic reports filed with the Securities and Exchange Commission is recorded, processed, summarized and reported, within the time periods specified in the Commission's rules and forms. Based on an evaluation of the Company's disclosure controls and procedures conducted by the Company's Chief Executive Officer and Chief Financial Officer, such officers concluded at June 30, 2007, that the Company's disclosure controls and procedures were effective.

Based on an evaluation by the Company's Chief Executive Officer and Chief Financial Officer, such officers concluded that there was no change in the Company's internal control over financial reporting during the three months ended June 30, 2007 that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II – OTHER INFORMATION

Item 1 Legal Proceedings

As initially reported in our report on for 10-Q for the quarter ended June 30, 2006, in September 2005, James D. Christianson and several small entities whom Christianson represents filed a lawsuit in the United States District Court for the Western District of Washington against several parties, including two directors of the Company, Carol Stephan and Ray De Motte. Mr. De Motte is also an officer of the Company. The original complaint alleged, among other things, that De Motte and Stephan made misrepresentations and omitted information in connection with the plaintiffs' purchases of stock in the Company and in other entities with which they alleged De Motte and/or Stephan are associated. The Company was not a party to the original complaint. Claims against several parties were dismissed without prejudice on jurisdictional grounds and venue of the case was later transferred to the Northern Division of the District of Idaho.

The plaintiffs requested, and were granted leave to amend their complaint, and their amended complaint included new claims against the Company and others. The plaintiffs' amended complaint asserts, with respect to the Company, that it and others made misrepresentations and omitted information in connection with the plaintiffs' purchases of the Company's stock. It asserts claims for civil RICO under Idaho law, and for securities fraud, misrepresentation and other causes of action. The Company and the other defendants responded by moving to dismiss the amended complaint on various grounds. The motions to dismiss remain pending. Plaintiffs have, in March 2007, filed a motion for a second amendment to their complaint adding several third parties. The court has not yet ruled on this motion. The parties participated in court ordered mediation during June 2007. A settlement was not reached. If the case is not dismissed and settlement is not reached in the short term, the Company intends to aggressively defend and is likely to bring counterclaims against Mr. Christianson and the other plaintiffs. If trial is required, it is currently scheduled to begin on June 10, 2008.

Item 1A Risk Factors

The Company has no material changes to report to add to the risk factors previously disclosed in our 2006 annual report on Form 10-K filed on March 14, 2007.

Item 2 Unregistered Sales of Equity Securities and Use of Proceeds

During the three months ended June 30, 2007 the Company issued an aggregate of 1,422,260 shares of common stock for aggregate proceeds of \$3,599,704 and for non-cash value of \$962,500 including:

475,260 warrants were exercised for a total of \$1,619,704, and 250,000 shares were issued for land.

Item 3 Defaults Upon Senior Securities

None

Item 4 Submission of Matters to a Vote of Security Holders

The Company held an annual shareholders' meeting on May 17, 2007 for the purpose of amending the Company's Articles of Incorporation to increase the number of authorized shares to 80 million, to approve the Company's 2006 Employee Stock Purchase Plan, to approve the auditors to perform the 2007 financial audit, and, to approve the Company's 2006 Equity Incentive Plan, to

elect six (6) directors. The following directors were appointed: Raymond K. DeMotte, Kevin G. Shiell, Carol Stephan, Dave J. Waisman, Roger A. VanVoorhees, and J. Kenny Berscht. The respective votes cast for and against each nominee were as follows: Raymond DeMotte, 20,155,728 for, 174,430 against; Kevin Shiell, 20,158,336 for, 343,598 against; Carol Stephan, 20,168,436 for, 161,722 against; Dave Waisman, 19,986,560 for, 343,598 against, Roger A. VanVoorhees 20,169,136 for, 161,022 against, and J. Kenny Berscht 20,168,836 for, 161,322 against.

Item 5 Other Information

None

Item 6 Exhibits

| <u>Exhibit</u> | <u>Description</u> |
|----------------|--|
| 31.1 | Certification of Chief Executive Officer |
| 31.2 | Certification of Chief Financial Officer |
| 32.1 | Certification of Chief Executive Officer |
| 32.2 | Certification of Chief Financial Officer |

SIGNATURES

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 thereunto duly authorized.

STERLING MINING COMPANY

By: /s/ Raymond DeMotte

Raymond DeMotte, Chief Executive Officer

Date: 8/14/07

By: /s/ James N. Meek

James N. Meek, Chief Financial Officer

Date: 8/14/07

**CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER
PURSUANT TO RULE 13a—14(a) OF THE
SECURITIES EXCHANGE ACT OF 1934, AS AMENDED,
AS ADOPTED PURSUANT TO
SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Raymond DeMotte, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Sterling Mining Company.

2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report.

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report.

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a -15(e) and 15d -15(e)) for the registrant and have:

a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

b) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures as of the end of the period covered by this report based on such evaluation; and

c) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):

a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 14, 2007

By: /s/ RAYMOND DEMOTTE

Raymond DeMotte

President and Chief Executive Officer

**CERTIFICATION OF PRINCIPAL FINANCIAL OFFICER
PURSUANT TO RULE 13a—14(a) OF THE
SECURITIES EXCHANGE ACT OF 1934, AS AMENDED,
AS ADOPTED PURSUANT TO
SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, James N. Meek, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Sterling Mining Company.

2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report.

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report.

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a -15(e) and 15d -15(e)) for the registrant and have:

a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

b) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures as of the end of the period covered by this report based on such evaluation; and

c) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):

a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 14, 2007

By: /s/ JAMES N. MEEK

James N. Meek

Vice-President and Chief Financial Officer

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350

In connection with the Quarterly Report of Sterling Mining Company (the "Company") on Form 10-Q for the quarter ended June 30, 2007, as filed with the Securities and Exchange Commission on the date hereof (the "Quarterly Report"), I, Raymond DeMotte, President and Chief Executive Officer of the Company, hereby certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to the best of my knowledge:

- a. the Quarterly Report fully complies with the requirements of Section 13(a) of the Securities Exchange Act of 1934; and
- b. the information contained in the Quarterly Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Raymond DeMotte

Raymond DeMotte,
President and Chief Executive Officer
Date: August 14, 2007

**CERTIFICATION OF PRINCIPAL FINANCIAL OFFICER
PURSUANT TO 18 U.S.C. SECTION 1350
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of Sterling Mining Company (the "Company") on Form 10-Q for the quarter ended June 30, 2007, as filed with the Securities and Exchange Commission on the date hereof (the "Quarterly Report"), I, James N. Meek, Vice-President and Chief Financial Officer of the Company, hereby certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to the best of my knowledge:

- a. the Quarterly Report fully complies with the requirements of Section 13(a) of the Securities Exchange Act of 1934; and
- b. the information contained in the Quarterly Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ James N. Meek

James N. Meek,
Vice-President and Chief Financial Officer
Date: August 14, 2007