



International Frontier Resources Corporation  
Consolidated Financial Statements  
December 31, 2007

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## Auditors' Report

To the Shareholders of  
**International Frontier Resources Corporation**

We have audited the consolidated balance sheet of **International Frontier Resources Corporation** as at December 31, 2007 and the consolidated statements of operations, comprehensive loss and deficit and cash flows for the year then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of International Frontier Resources Corporation as at December 31, 2007 and the results of its operations and cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

The comparative financial statements as at and for the year ended December 31, 2006 presented for comparative purposes were audited by another firm of Chartered Accountants which expressed an opinion without reservation on those financial statements in their report dated April 17, 2007.

(Signed) "*Deloitte & Touche LLP*"

Calgary, Alberta  
March 21, 2008

Chartered Accountants

# International Frontier Resources Corporation

## Consolidated Balance Sheets

December 31 2007 2006

### Assets

#### Current

Cash and cash equivalents (Note 15)	\$ 25,316,940	\$ 11,853,540
Receivables	1,227,990	456,190
Inventory	-	82,125
Prepays	<u>162,690</u>	<u>31,590</u>

**26,707,620** 12,423,445

Restricted cash on deposit (Note 5)	2,267,175	1,538,125
Property and equipment (Note 6)	17,504,875	12,237,085
Inventory (Note 4)	82,125	-
Intangibles (Note 7)	<u>35,000</u>	<u>40,000</u>

**\$ 46,596,795** \$ 26,238,655

### Liabilities

#### Current

Payables and accruals	\$ 4,207,115	\$ 1,075,270
Convertible debentures (Note 10)	62,650	-
Current portion of asset retirement obligations (Note 8)	<u>30,000</u>	<u>-</u>
	<b>4,299,765</b>	1,075,270

Asset retirement obligations (Note 8)	306,020	239,045
Future income taxes (Note 9)	1,141,630	1,655,510
Convertible debentures (Note 10)	<u>-</u>	<u>62,650</u>
	<b>5,747,415</b>	3,032,475

### Shareholders' Equity

Share capital (Note 11)	44,121,725	26,410,600
Warrants (Note 11)	3,757,090	-
Contributed surplus (Note 11)	6,732,940	4,474,570
Equity component of convertible debentures (Note 10)	2,350	2,350
Deficit	<u>(13,764,725)</u>	<u>(7,681,340)</u>
	<b>40,849,380</b>	23,206,180
	<b>\$ 46,596,795</b>	\$ 26,238,655

Commitments and contingencies (Note 14)  
Nature of operations (Note 1)

On behalf of the Board

**(Signed) "Wm. Patrick Boswell"** Director **(Signed) "W.J. McNaughton"** Director

See accompanying notes to the interim consolidated financial statements.

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**International Frontier Resources Corporation**  
**Consolidated Statements of Operations, Comprehensive Loss and Deficit**

Years ended December 31,	2007	2006
Revenue		
Oil	\$ 787,020	\$ 965,370
Less: Royalties	<u>(179,530)</u>	<u>(219,005)</u>
	607,490	746,365
Interest income	1,154,975	449,095
Prospect fee income	<u>194,755</u>	<u>172,500</u>
	<u>1,957,220</u>	<u>1,367,960</u>
Expenses		
Field operating costs	508,025	398,785
Depletion, depreciation and impairments (Note 6)	4,459,275	1,222,010
Accretion (Note 8)	16,775	21,560
Foreign exchange loss	265,165	-
General and administration	872,790	833,955
Stock based compensation (Note 11)	<u>1,851,725</u>	<u>729,830</u>
	<u>7,973,755</u>	<u>3,206,140</u>
Loss before income taxes	(6,016,535)	(1,838,180)
Future income tax expense (recovery) - (Note 9)	<u>66,850</u>	<u>(608,535)</u>
Net loss and comprehensive loss	\$ (6,083,385)	\$ (1,229,645)
Deficit, beginning of year	<u>(7,681,340)</u>	<u>(6,451,695)</u>
Deficit, end of year	<u>\$ (13,764,725)</u>	<u>\$ (7,681,340)</u>
<hr/>		
Net loss per share (Note 12)		
Basic and diluted	\$ <u>(0.11)</u>	\$ <u>(0.03)</u>

See accompanying notes to the consolidated financial statements.

# International Frontier Resources Corporation

## Consolidated Statements of Cash Flows

Years ended December 31

2007

2006

<b>Operating</b>		
Net loss	\$ (6,083,385)	\$ (1,229,645)
Non Cash Items:		
Depletion, depreciation and impairments	4,459,275	1,222,010
Accretion	16,775	21,560
Stock based compensation	1,851,725	729,830
Future income tax expense	66,850	(608,535)
Asset retirement liabilities settled	<u>(223,145)</u>	<u>(5,960)</u>
	88,095	129,260
Change in non-cash operating working capital (Note 15)	<u>340,855</u>	<u>977,365</u>
	<u>428,950</u>	<u>1,106,625</u>
<b>Investing</b>		
Additions to property and equipment	(9,016,845)	(6,433,410)
Proceeds from disposition of property and equipment	4,770	-
Restricted cash on deposit	(729,050)	(96,800)
Change in non-cash investing working capital (Note 15)	<u>1,888,090</u>	<u>1,384,560</u>
	<u>(7,853,035)</u>	<u>(5,145,650)</u>
<b>Financing</b>		
Shares and warrants issued for cash	22,890,000	2,990,565
Share issue costs	<u>(2,002,515)</u>	<u>(3,915)</u>
	<u>20,887,485</u>	<u>2,986,650</u>
Net increase (decrease) in cash and cash equivalents	13,463,400	(1,052,375)
Cash and cash equivalents,		
Beginning of year	<u>11,853,540</u>	<u>12,905,915</u>
End of year	<u>\$ 25,316,940</u>	<u>\$ 11,853,540</u>

See accompanying notes to the consolidated financial statements.

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# International Frontier Resources Corporation

## Notes to the Consolidated Financial Statements

December 31, 2007 and 2006

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### 1. Nature of operations and basis of presentation

The Company, since inception, is engaged primarily in the exploration for and development of petroleum and natural gas reserves. These activities are conducted in two geographical areas, being Canada and the United Kingdom.

The consolidated financial statements include the accounts of the Company, its wholly owned United Kingdom subsidiary, Britcana Energy Ltd. and its 50% jointly controlled interest in Sidox Chemicals Canada Ltd. ("Sidox Canada") accounted for on the proportionate consolidation method. All inter-company transactions and balances are eliminated upon consolidation.

The consolidated financial statements of the Company have been prepared in accordance with Canadian generally accepted accounting principles within the framework of the accounting policies summarized below.

The costs associated with the acquisition and development thereon to date is recognized in these consolidated financial statements in accordance with the accounting policies outlined in this note. Accordingly, their carrying value represents costs incurred to date and do not necessarily reflect present or future values. The recoverability of these amounts is dependent upon the existence of economically recoverable petroleum and natural gas reserves.

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### 2. Significant accounting policies

#### Measurement uncertainty

The preparation of consolidated financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates that affect the reported amounts of assets, liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the amounts of revenues and expenses during the reporting period. Accordingly, actual results may differ from estimated amounts as future confirming events occur.

The most significant estimate is related to the recoverability of petroleum and natural gas properties. Amounts recorded for depletion and depreciation, asset retirement obligations and amounts used in impairment test calculations are based upon estimates of petroleum and natural gas reserves and future costs to develop those reserves. By their nature, these estimates of reserves, costs and related future cash flows are subject to uncertainty, and the impact on the consolidated financial statements of future periods could be material.

The calculation of asset retirement obligations include estimates of the ultimate settlement amounts, inflation factors, credit adjusted discount rates and timing of settlement. The impact of future revisions to these assumptions on the consolidated financial statements of future periods could be material.

The amounts recorded relating to the fair value of stock options issued are based on estimates of the future volatility of the Company's share price, expected lives of the options, expected dividends and other relevant assumptions.

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# International Frontier Resources Corporation

## Notes to the Consolidated Financial Statements

December 31, 2007 and 2006

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### 2. Summary of significant accounting policies (Continued)

#### Measurement uncertainty (continued)

The Company may from time to time issue flow-through shares to finance a portion of its capital expenditure program. The income tax deductions associated with the expenditures funded by flow-through arrangements are renounced to investors in accordance with the appropriate tax legislation. To recognize the foregone tax benefits to the Company, share capital is reduced and a future tax liability is recorded equal to the estimated amount of future income taxes when the expenditure renouncements are filed.

The capital expenditures classification made with respect to the renouncement of flow-through shares is based on estimates from geological and geophysical information obtained and the classification of the expenditures may be challenged by the taxation authorities and in this regard the assessments may be different from that of management. By their nature, these estimates are subject to measurement uncertainty and the effect on the financial statements of changes of estimates in future periods could be significant.

#### Property and equipment

The Company follows the full cost method of accounting for petroleum and natural gas operations as determined by the Canadian Institute of Chartered Accountants ("CICA"), Accounting Guideline 16, whereby all costs of exploration for and development of petroleum and natural gas reserves are capitalized in a cost centre for each country in which the Company has operations. Costs include lease acquisition costs, geological and geophysical expenses, costs of drilling both successful and unsuccessful wells and overhead charges directly related to exploration activities. Proceeds from the sale of oil and gas properties will be applied against the capitalized costs, with no gain or loss recognized, unless such a sale would significantly alter the rate of depletion and depreciation.

Depletion of exploration and development costs and depreciation of production equipment is provided using the unit-of-production method based upon estimated proved petroleum and natural gas reserves before royalties as determined by independent engineers. The costs of significant undeveloped properties are excluded from costs subject to depletion until it is determined whether or not proved reserves are attributable to the properties or impairment has occurred. Estimated future costs to be incurred in developing proved reserves are included in costs subject to depletion.

At each reporting period, the Company performs an impairment test to determine the recoverability of capitalized costs associated with reserves. An impairment loss is recognized in net earnings when the carrying amount of a cost centre exceeds its fair value. The carrying amount of the cost centre is not recoverable if the carrying amount exceeds the sum of the undiscounted cash flows from proved reserves plus the costs of unproved properties. If the sum of the cash flows is less than the carrying amount, the impairment loss is limited to the amount by which the carrying amount exceeds the sum of the fair value of proved and probable reserves and the costs of unproved properties that have been subject to a separate impairment test and contain no probable reserves.

Depreciation of office furniture and equipment is provided on a diminishing balance basis over the estimated useful lives of those assets at rates ranging from 20% to 30% per annum.

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# International Frontier Resources Corporation

## Notes to the Consolidated Financial Statements

December 31, 2007 and 2006

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### 2. Summary of significant accounting policies (Continued)

#### Asset retirement obligations

The Company recognizes the fair value of estimated asset retirement obligations on the consolidated balance sheet when a reasonable estimate of fair value can be made. Asset retirement obligations include those legal obligations where the Company will be required to retire tangible long lived assets such as well sites, pipelines and facilities. The asset retirement cost, equal to the initially estimated fair value of the asset retirement obligation, is capitalized as part of the cost of the related long lived asset. Changes in the estimated obligation resulting from revisions to estimated timing or amount of undiscounted cash flows are recognized as a change in the asset retirement obligation and the related asset retirement cost.

Asset retirement costs are amortized using the unit-of-production method and are included in depletion and depreciation in the consolidated statements of loss and deficit. Increases in the asset retirement obligations resulting from the passage of time are recorded as accretion of asset retirement obligations in the consolidated statements of loss and deficit. Actual expenditures incurred are charged against the accumulated obligation.

#### Joint venture operations

Substantially all of the Company's exploration and production activities are conducted jointly with others and accordingly the accounts reflect only the Company's proportionate interest in such activities.

#### Flow-through common shares

Resource expenditure deductions for income tax purposes related to exploration and development activities funded by flow-through share arrangements are renounced to investors in accordance with income tax legislation. The estimated tax benefits transferred to shareholders upon renouncement are recorded as an increase to future income taxes and a reduction to share capital at the time the resource expenditure deductions are renounced.

#### Cash and cash equivalents

Cash and cash equivalents include cash on hand, balances with banks and short-term deposits with original maturities of three months or less earning an average interest rate of 4.00% in 2007 (2006 – 3.20%)

#### Inventory

Inventory is comprised of chemical inventory that is stated at the lower of cost and net realizable value. Cost is determined on a weighted average cost basis.

#### Intangible assets

The Company's proportionate share of an exclusive licensing agreement for the Sidox product in Canada is held by Sidox Chemicals Canada Ltd. The agreement covering an exclusive license for Canada has a ten-year term and costs related thereto are being amortized on a straight line basis over the period. Intangible assets are subject to an annual impairment test whenever events or changes in circumstances indicate that the carrying value may not be recoverable.

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# International Frontier Resources Corporation

## Notes to the Consolidated Financial Statements

December 31, 2007 and 2006

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### 2. Summary of significant accounting policies (Continued)

#### Convertible debentures

The debt component of convertible debentures outstanding represents the present value of the payment obligations, interest and principal, to be satisfied in cash, discounted at the rate of interest that would be applicable to a debt-only instrument of comparable term and risk. The residual amount of the debenture represents the equity component and is presented in shareholders' equity. These component parts have been measured at their respective estimated fair values at the time the convertible debentures were originally issued.

#### Income taxes

Income taxes are recorded using the liability method. Future income taxes are calculated based on temporary differences arising from the difference between the tax basis of an asset and liability and its carrying value using substantively enacted income tax rates. Changes in income taxes rates that are substantively enacted are reflected in the period the change occurs. A valuation allowance is recorded against any future income tax asset if the Company is not "more likely than not" to be able to utilize the associated tax deductions.

#### Per share amounts

Basic earnings per share is computed by dividing the earnings for the period by the weighted average number of common shares outstanding during the year. Diluted earnings per share reflects the potential dilution that could occur if potentially dilutive securities were exercised or converted to common stock. The dilutive effect of options and warrants and their equivalent is computed by application of the treasury stock method and the effect of convertible securities by the "if converted" method. Diluted amounts are not presented when the effect of the computations are anti-dilutive due to the losses incurred. Accordingly, there is no difference in the amounts presented for basic and diluted loss per share.

#### Stock-based compensation

The Company has a stock option plan as described in Note 11(d). The Company uses the fair value method of accounting for stock options granted to employees and directors. Fair values are determined using the Black-Scholes option pricing model. Compensation costs are recognized in the statement of operations at the date of grant as the options vest immediately. Compensation expense is adjusted for the estimated amount of forfeitures at the time compensation expense is recognized.

#### Revenue recognition

Revenue associated with the production and sales of crude oil, natural gas and natural gas liquids owned by the Company are recognized when title passes from the Company to its customer. Other revenue is recognized in the period that the service is provided to the customer or when income is earned.

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# International Frontier Resources Corporation

## Notes to the Consolidated Financial Statements

December 31, 2007 and 2006

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### 2. Summary of significant accounting policies (Continued)

#### Foreign currency translation

Monetary assets and liabilities denominated in a foreign currency are translated at the exchange rate prevailing at the balance-sheet date. Non-monetary assets and liabilities and transactions denominated in a foreign currency are translated at the exchange rates in effect at the transaction date.

Integrated foreign subsidiaries are accounted for using the temporal method. Under this method, monetary assets and liabilities are translated at the exchange rate in effect at the balance-sheet date. Non-monetary assets are translated at historical rates. Revenue and expenses are translated at average rates for the period. Foreign exchange gains and losses are included in net loss in the period in which they arise.

#### 3. New accounting policies

Effective January 1, 2007, the Company adopted the Canadian Institute of Chartered Accountants ("CICA") Section 1530, "Comprehensive Income", Section 3855, "Financial Instruments – Recognition and Measurement", Section 3861, "Financial Instruments – disclosure and Presentation" and Section 3865, "Hedges". The Company has adopted these standards retrospectively without restatement.

Upon adoption of Section 3855, all financial instruments are classified into one of the following five categories: held-for-trading, loans and receivables, held-to-maturity investments, available-for-sale financial assets or other financial liabilities. Subsequent measurement of the financial instruments is based on their initial classification. Held-for-trading financial assets are measured at fair value and changes in fair value are recognized in net income. Available-for-sale financial instruments are measured at fair value with changes in fair value recorded in other comprehensive income until the instrument is derecognized or impaired.

All derivative instruments are recorded in the balance sheet at fair value unless they qualify for the normal sale and normal purchase exemption. All changes in their fair value are recorded in net income unless cash flow hedge accounting is used, in which case changes in fair value are recorded in other comprehensive income until the underlying hedged transaction is recognized in net income. Any hedge ineffectiveness is immediately recognized in net income. The other categories of financial instruments are recognized at amortized cost using the effective interest rate method.

Upon adoption of these standards, the Company classified its cash and cash equivalents as held-for-trading, which are measured at fair value. Accounts receivable are classified as loans and receivables, which are measured at cost. Accounts payable and notes payable are classified as other financial liabilities, which are measured at amortized cost.

For financial assets and financial liabilities that are not classified as held-for-trading, the transaction costs that are directly attributable to the acquisition or issue of a financial asset or financial liability are adjusted to the fair value initially recognized for that financial instrument. These costs are expensed using the effective interest rate method.

The adoption of Section 1530 has no material impact on the consolidated financial statements of the Company.

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# International Frontier Resources Corporation

## Notes to the Consolidated Financial Statements

December 31, 2007 and 2006

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### 3. New accounting policies (continued)

The Company currently does not utilize hedges or other derivative financial instruments in its operations, and as a result of the adoption of Section 3865 had no material impact on the consolidated financial statements of the Company.

The adoption of these new standards had no impact on the Company's opening deficit as at January 1, 2007.

The new standards establish a new statement of comprehensive income, which is comprised of net earnings and other comprehensive income. The Company currently has no other comprehensive income items.

The Company has also adopted Section 3251, "Equity" and Section 1506, "Accounting Changes". Section 3251 replaces Section 3250, "Surplus" and describes standards for the presentation of equity and changes in equity for reporting periods as a result of the application of Section 1530, "Comprehensive Income". The only impact of Section 1506, "Accounting Changes", is to provide disclosure of when an entity has not applied a new source of GAAP that has been issued but is not yet effective. This is the case with Section 3862, "Financial Instruments Disclosures" and Section 3863, "Financial Instruments Presentations" which are required to be adopted for fiscal years beginning on or after October 1, 2007. The Company will adopt these standards on January 1, 2008 and it is expected the only effect on the Company will be additional disclosures regarding the significance of financial instruments for the entity's financial position and performance; and the nature, extent and management of risks arriving from financial instruments to which the entity is exposed.

The Company is assessing the new and revised accounting pronouncements that have been issued that are not yet effective:

- As of January 1, 2008, the Company will be required to adopt two new CICA standards, Section 3862 "Financial Instruments – Disclosures" and Section 3863 "Financial Instruments – Presentation," which will replace Section 3861 "Financial Instruments – Disclosure and Presentation." The new disclosure standard increases the emphasis on the risks associated with both recognized and unrecognized financial instruments and how those risks are managed. The new presentation standard carries forward the former presentation requirements. The new financial instruments presentation and disclosure requirements were issued in December 2006 and the Company is assessing the impact on its consolidated financial statements.
- As of January 1, 2008, the Company will be required to adopt Section 1535 "Capital Disclosures," which will require companies to disclose their objectives, policies and processes for managing capital. In addition, disclosures are to include whether companies have complied with externally imposed capital requirements. The new capital disclosure requirements were issued in December 2006 and the Company is assessing the impact on its consolidated financial statements.
- The Company will be required to adopt CICA Handbook Section 3031, Inventories. This new accounting standard is effective for interim and annual financial statements for fiscal years beginning on or after January 1, 2008. This new standard is not expected to have a material impact on the Company's consolidated financial statements.

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# International Frontier Resources Corporation

## Notes to the Consolidated Financial Statements

December 31, 2007 and 2006

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### 3. New accounting policies (continued)

- The CICA Accounting Standards Board (“AcSB”) adopted a strategic plan for the direction of accounting standards in Canada. As part of that plan, accounting standards in Canada for public companies are expected to converge with International Financial Reporting Standards (“IFRS”) by the end of 2011. The Company continues to monitor and assess the impact of convergence of Canadian GAAP and IFRS.
  
- In February 2008, the Canadian Institute of Chartered Accountants (“CICA”) issued Section 3064, Goodwill and intangible assets, replacing Section 3062, Goodwill and other intangible assets and Section 3450, Research and development costs. Various changes have been made to other sections of the CICA Handbook for consistency purposes. The new Section will be applicable to financial statements relating to fiscal years beginning on or after October 1, 2008. Accordingly, the Company will adopt the new standards for its fiscal year beginning January 1, 2009. It establishes standards for the recognition, measurement, presentation and disclosure of goodwill subsequent to its initial recognition and of intangible assets by profit-oriented enterprises. Standards concerning goodwill are unchanged from the standards included in the previous Section 3062. The Company does not expect that the adoption of this new Section will have a material impact on its consolidated financial statements.

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### 4. Investment in Sidox Chemicals Canada Ltd.

The investment in Sidox Canada is subject to joint control and accordingly has been proportionately consolidated in these financial statements at December 31, 2007.

Company’s proportionate share of balances included in these consolidated financial statements related to Sidox Canada is:

	<u>2007</u>	<u>2006</u>
Assets		
Cash	\$ 49,990	\$ 49,990
Receivables	12,265	12,265
Inventory	82,125	82,125
Intangibles	<u>35,000</u>	<u>40,000</u>
	<u>179,380</u>	184,380
Liabilities		
Payables	<u>87,730</u>	<u>77,455</u>
Net assets	\$ <u>91,650</u>	\$ <u>106,925</u>
Revenues	\$ -	\$ -
Expenditures	<u>15,275</u>	<u>19,990</u>
Net Loss	\$ <u>15,275</u>	\$ <u>19,990</u>

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## International Frontier Resources Corporation

### Notes to the Consolidated Financial Statements

December 31, 2007 and 2006

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#### 5. Restricted cash on deposit

As at December 31, 2007, the Company has provided an assignment of cash totaling \$2,267,175 (2006 - \$1,538,125) as security on the irrevocable standby letters of credit for the Northwest Territories Exploration Licenses (see Note 14) as follows:

	<u>2007</u>	<u>2006</u>
EL – 423	\$ 509,180	\$ 310,000
EL – 429	781,250	781,250
EL – 432	250,000	250,000
EL – 441	352,440	196,875
EL – 445	68,750	-
EL – 443	<u>305,555</u>	<u>-</u>
	<u>\$ 2,267,175</u>	<u>\$ 1,538,125</u>

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#### 6. Property and equipment

##### December 31, 2007

	<u>Cost</u>	<u>Accumulated Depletion, Depreciation and Impairments</u>	<u>Net Book Value</u>
Petroleum and natural gas properties	\$ 24,919,340	\$ 7,434,515	\$ 17,484,825
Office furniture and equipment	<u>82,480</u>	<u>62,430</u>	<u>20,050</u>
Petroleum and natural gas properties	<u>\$ 25,001,820</u>	<u>\$ 7,496,945</u>	<u>\$ 17,504,875</u>

##### December 31, 2006

	<u>Cost</u>	<u>Accumulated Depletion, Depreciation and Impairments</u>	<u>Net Book Value</u>
Petroleum and natural gas properties	\$ 15,197,280	\$ 2,985,915	\$ 12,211,365
Office furniture and equipment	<u>82,480</u>	<u>56,760</u>	<u>25,720</u>
Petroleum and natural gas properties	<u>\$ 15,279,760</u>	<u>\$ 3,042,675</u>	<u>\$ 12,237,085</u>

During the year, \$411,450 (2006 - \$135,230) of overhead expenses directly related to exploration activities in the Northwest Territories and \$614,150 (2006 - \$425,045) related to exploration and prospect generation in the North Sea were capitalized. Of these amounts, \$6,175 (2006 - \$6,175) related to interest expense capitalized for activities the Northwest Territories and \$Nil (2006 - \$Nil) related to the activities in the North Sea.

Included in the above amounts are, \$294,800 (2006 - \$Nil) of stock option costs recognized in the period that were capitalized to undeveloped properties in the Northwest Territories and \$111,835 (2006 - \$Nil) of stock option costs recognized in the period were capitalized to petroleum and natural gas properties in the North Sea.

# International Frontier Resources Corporation

## Notes to the Consolidated Financial Statements

December 31, 2007 and 2006

### 6. Property and equipment (continued)

As at December 31, 2007 the Company has accumulated capital expenditures for land, seismic, and drilling in the Central Mackenzie Valley, Northwest Territories of \$13,805,330 (2006 - \$10,251,460). In the North Sea (UKCS) the Company has incurred capital expenditures, at December 31, 2007, of \$2,413,000 (2006 - \$1,105,265). These costs have been included in petroleum and natural gas properties as undeveloped properties but have not been included in the respective cost centers for purposes of calculating depletion.

In 2007, \$Nil (2006 - \$1,000,620) impairment of petroleum and natural gas assets has been recorded as part of depletion to reflect the excess carrying amount of assets over fair value of future reserves in Canada. In addition, in 2007, \$4,280,860 (2006 - \$Nil) impairment of petroleum and natural gas assets in the North Sea has been recorded as part of depletion.

The prices used in the impairment test evaluation of the Company's petroleum properties were as follows:

	<u>2008</u>	<u>2009</u>	<u>2010</u>	<u>2011</u>	<u>2012</u>	<u>2013</u>	Increase Thereafter
Crude oil (\$C/Bbl)	\$55.30	\$53.20	\$50.50	\$48.70	\$48.00	\$47.20	2.0%

### 7. Intangible assets

#### December 31, 2007

	<u>Cost</u>	<u>Accumulated Depreciation</u>	<u>Net Book Value</u>
Sidox license	\$ <u>50,000</u>	\$ <u>15,000</u>	\$ <u>35,000</u>

#### December 31, 2006

	<u>Cost</u>	<u>Accumulated Amortization</u>	<u>Net Book Value</u>
Sidox license	\$ <u>50,000</u>	\$ <u>10,000</u>	\$ <u>40,000</u>

### 8. Asset retirement obligations

The Company's asset retirement obligations result from net ownership interest in petroleum and natural gas assets including well sites, gathering systems and processing facilities. The Company estimates the total undiscounted amount of cash flows required to settle its asset retirement obligations is approximately \$832,500 (2006 - \$472,500). A credit-adjusted risk-free rate of 9% and inflation rate of 2% was used to calculate the fair value of the asset retirement obligations. A reconciliation of the asset retirement obligations is provided below:

	<u>2007</u>	<u>2006</u>
Balance, beginning of year	\$ <u>239,045</u>	\$ 201,390
Change in estimate	<u>303,345</u>	-
Liabilities incurred	-	22,055
Liabilities settled	<u>(223,145)</u>	(5,960)
Accretion expense	<u>16,775</u>	<u>21,560</u>
	<u>336,020</u>	239,045
Less: current portion	<u>(30,000)</u>	-
Balance, end of year	\$ <u>306,020</u>	\$ <u>239,045</u>

It is expected that this obligation will be funded from the Company's general resources at the time the costs are incurred with the majority of costs expected to occur between 2008 and 2018.

# International Frontier Resources Corporation

## Notes to the Consolidated Financial Statements

December 31, 2007 and 2006

### 9. Income taxes

- a) The total provision for income taxes differs from the expected amount calculated by applying the combined federal and provincial tax rates of approximately 30.12% (2006 - 32.49%) to loss before income taxes in Canada and tax rate of approximately 30% (2006 – 30%) in the U.K.. This difference results from the following items:

#### December 31, 2007

	<u>Canada</u>	<u>U.K.</u>	<u>Total</u>
Loss before income taxes	\$ (1,631,510)	\$ (4,385,025)	\$ (6,016,535)
Expected tax recovery of combined Federal and provincial statutory rates	(491,410)	(1,320,770)	(1,812,180)
Increase (decrease) resulting from:			
Statutory rate change	520	243,950	244,470
Stock based compensation	557,740	-	557,740
Foreign exchange loss	-	33,000	33,000
Change in valuation allowance	-	1,043,820	1,043,820
	-	1,043,820	1,043,820
Future income tax expense	\$ <u>66,850</u>	\$ <u>-</u>	\$ <u>66,850</u>

#### December 31, 2006

	<u>Canada</u>	<u>U.K.</u>	<u>Total</u>
Loss before income taxes	\$ (1,811,310)	\$ (26,870)	\$ (1,838,180)
Expected tax recovery of combined Federal and provincial statutory rates	(589,165)	(8,060)	(597,225)
Increase (decrease) resulting from:			
Statutory rate change	(271,690)	-	(271,690)
Resource Allowance	11,200	-	11,200
Stock based compensation	237,120	-	237,120
Other	12,060	-	12,060
	12,060	-	12,060
Future income tax recovery	\$ <u>(600,475)</u>	\$ <u>(8,060)</u>	\$ <u>(608,535)</u>

- b) Future income taxes consist of the following temporary differences:

#### December 31, 2007

	<u>Canada</u>	<u>U.K.</u>	<u>Total</u>
Excess of carry value of property and equipment over tax values	\$ (2,171,510)	\$ 1,070,215	\$ (1,101,295)
Asset retirement obligations	84,005	-	84,005
Share issue costs	472,070	-	472,070
Non-capital loss carry-forwards	473,805	32,510	506,315
	(1,141,630)	1,102,725	(38,905)
Valuation allowance	-	(1,102,725)	(1,102,725)
	-	(1,102,725)	(1,102,725)
Future income tax liability	\$ <u>(1,141,630)</u>	\$ <u>-</u>	\$ <u>(1,141,630)</u>

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## International Frontier Resources Corporation

### Notes to the Consolidated Financial Statements

December 31, 2007 and 2006

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#### 9. Income taxes (continued)

##### December 31, 2006

	<u>Canada</u>	<u>U.K.</u>	<u>Total</u>
Excess of carry value of property and equipment over tax values	\$ (2,310,000)	\$ -	\$ (2,310,100)
Asset retirement obligations	69,320	-	69,320
Share issue costs	151,360	-	151,360
Non-capital loss carry-forwards	400,290	8,060	408,350
Other	<u>25,460</u>	-	<u>25,560</u>
Future income tax liability	<u>\$ (1,663,570)</u>	<u>\$ 8,060</u>	<u>\$ (1,655,510)</u>

#### c) Tax losses

The Company has incurred losses for income tax purposes of approximately \$2,433,880 (2006 - \$1,681,00) in Canada and \$130,000 (2006 - \$27,000) in the United Kingdom. The related benefit of these losses has been recognized in the consolidated financial statements by reducing future income taxes. Unless sufficient taxable income is earned these losses will expire as follows:

	<u>Canada</u>	<u>U.K.</u>	<u>Total</u>
2008	\$ 9,000	\$ -	\$ 9,000
2009	90,000	-	90,000
2010	66,000	-	66,000
2011	265,000	-	265,000
2012	508,000	-	508,000
2015	593,000	-	593,000
2026	268,000	27,000	295,000
2027	<u>634,880</u>	<u>103,000</u>	<u>737,880</u>
	<u>\$ 2,433,880</u>	<u>\$ 130,000</u>	<u>\$ 2,563,880</u>

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#### 10. Convertible debentures

At December 31, 2007, the Company has \$65,000 of convertible debentures remaining. The debentures pay interest at a rate of 9.5% per year and are convertible into common shares at \$0.70 per share to June 2007 and \$0.75 per share to June 2008 at which time they expire.

The Company's convertible debentures were presented in their component parts. The debt component of \$62,650 (2006 - \$62,650) represents the present value of the payment obligations, interest and principal, to be satisfied in cash, discounted at the rate of interest that would be applicable to a debt-only instrument of comparable term and risk. The residual amount of the debenture is \$2,350 (2006 - \$2,350) which represents the equity component and is presented in shareholders' equity. These component parts have been measured at their respective estimated fair values at the time the convertible debentures were originally issued.

There were no debentures converted during the years ended December 31, 2007 and 2006. A total of 86,667 shares will be issued if the remainder of the debentures are converted at June 30, 2008. The debentures are secured by a floating charge on the Company's assets.

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## International Frontier Resources Corporation

### Notes to the Consolidated Financial Statements

December 31, 2007 and 2006

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#### 11. Share capital

a) **Authorized:**

Unlimited common shares  
Unlimited preferred shares

b) **Issued:**

	December 31, 2007		December 31, 2006	
	Number of Shares	Amount	Number of Shares	Amount
<b>Common shares</b>				
Beginning of year	42,041,465	\$ 26,410,600	40,245,215	\$ 25,111,255
Issued for cash	12,400,000	15,500,000	-	-
Issued for services	100,000	125,000		
Value attributed to warrants (Note 11(e))	-	(3,757,090)	-	-
Issued upon exercise of warrants	-	-	1,521,250	2,814,315
Issued upon exercise of options	-	-	275,000	359,625
Flow-through shares	5,037,500	7,390,000	-	(1,870,680)
Share issue costs, net of tax effect	-	(1,546,785)	-	(3,915)
Balance, end of year	59,578,965	\$ 44,121,725	42,041,465	\$ 26,410,600

(i) In conjunction with a bought deal financing on February 22, 2007 the Company issued 12,400,000 units at a price of \$1.25 per unit, for gross proceeds of \$15,500,000. Each unit is comprised of one common share and one-half warrant. One full warrant entitles the holder thereof with the right to purchase one common share at \$1.60.

(ii) In conjunction with the above financing, the Company issued 100,000 Corporate Finance Units to the underwriter. Each unit consists of one common share and one warrant. At December 31, 2007, \$125,000 has been included in share capital to reflect the value of these shares at the date of issue.

(iii) On February 22, 2007, the Company also issued 4,800,000 flow-through shares at a price of \$1.50 per share, for gross proceeds of \$7,200,000.

(iv) On December 13, 2007 in conjunction with a non-brokered private placement, the Company issued 237,500 flow-through shares at a price of \$0.80 per share, for gross proceeds of \$190,000. The shares issued are subject to a hold period which expires on April 20, 2008.

# International Frontier Resources Corporation

## Notes to the Consolidated Financial Statements

December 31, 2007 and 2006

**11. Share capital** (continued)

**c) Flow-through share obligation information:**

	<u>2007</u>	<u>2006</u>
Balance, beginning of year	\$ -	\$ 5,337,725
Flow-through share proceeds	<b>7,390,000</b>	-
Expenditures incurred	<u>(3,891,975)</u>	<u>(5,337,725)</u>
Balance, end of year	<b>\$ <u>3,498,025</u></b>	<b>\$ <u>-</u></b>

**d) Stock options:**

The Company has a stock option plan available to consultants, officers, directors, and employees of the Company. The Option Plan allows directors, employees and consultants to be granted incentive based compensation under the Option Plan while allowing a rolling maximum of 10% of the number of issued and outstanding shares from time-to-time to be granted under the Option Plan. The exercise price of each option approximates the market price for the common shares on the date the option was granted. As at December 31, 2007, 5,855,000 common shares were reserved for issuance under the plan. Options granted under the plan vest upon granting and have a term of five years to expiry.

**Outstanding and exercisable**

	<u>2007</u>		<u>2006</u>	
	<u>Number of Options</u>	<u>Weighted Average Exercise Price</u>	<u>Number of Options</u>	<u>Weighted Average Exercise Price</u>
Balance, beginning of year	3,355,000	\$ 1.42	3,320,000	\$ 1.34
Granted	2,500,000	\$ 0.97	500,000	\$ 1.57
Expired	-	\$ -	(190,000)	\$ 1.37
Exercised	-	\$ -	(275,000)	\$ 0.64
Balance, end of year	<b><u>5,855,000</u></b>	<b><u>\$ 1.23</u></b>	<b><u>3,355,000</u></b>	<b><u>\$ 1.42</u></b>

**Expiry dates**

	<u>2007</u>		<u>2006</u>	
	<u>Number of Options</u>	<u>Price</u>	<u>Number of Options</u>	<u>Price</u>
December 23, 2008	465,000	\$ 0.45	465,000	\$ 0.45
January 26, 2009	90,000	\$ 0.50	90,000	\$ 0.50
April 1, 2009	75,000	\$ 0.45	75,000	\$ 0.45
November 16, 2009	525,000	\$ 1.50	525,000	\$ 1.50
December 23, 2009	800,000	\$ 1.60	800,000	\$ 1.60
February 11, 2010	800,000	\$ 1.85	800,000	\$ 1.85
September 15, 2010	100,000	\$ 1.35	100,000	\$ 1.35
January 5, 2011	150,000	\$ 1.95	150,000	\$ 1.95
June 30, 2011	350,000	\$ 1.40	350,000	\$ 1.40
January 9, 2012	800,000	\$ 1.30	-	\$ -
June 26, 2012	<u>1,700,000</u>	<u>\$ 0.82</u>	-	\$ -
	<b><u>5,855,000</u></b>	<b><u>\$ 1.23</u></b>	<b><u>3,355,000</u></b>	<b><u>\$ 1.42</u></b>

# International Frontier Resources Corporation

## Notes to the Consolidated Financial Statements

December 31, 2007 and 2006

### 11. Share capital (continued)

#### d) Stock options (continued)

##### December 31, 2007

Exercise Price	Options Outstanding			Options Exercisable	
	Options Outstanding	Weighted Average Contractual Life (years)	Weighted Average Exercise Price	Options Exercisable	Weighted Average Exercisable Price
\$0.45 - \$0.50	630,000	1.03`	\$ 0.46	630,000	\$ 0.46
\$0.82 - \$1.30	2,500,000	4.34`	\$ 0.97	2,500,000	\$ 0.97
\$1.35 - \$1.95	<u>2,725,000</u>	<u>2.28</u>	<u>\$ 1.64</u>	<u>2,725,000</u>	<u>\$ 1.64</u>
	<u>5,855,000</u>	<u>3.03</u>	<u>\$ 1.23</u>	<u>5,855,000</u>	<u>\$ 1.23</u>

##### December 31, 2006

Exercise Price	Options Outstanding			Options Exercisable	
	Options Outstanding	Weighted Average Contractual Life (years)	Weighted Average Exercise Price	Options Exercisable	Weighted Average Exercisable Price
\$0.45 - \$0.50	630,000	2.03`	\$ 0.46	630,000	\$ 0.46
\$1.30 - \$1.95	<u>2,725,000</u>	<u>3.28</u>	<u>\$ 1.64</u>	<u>2,725,000</u>	<u>\$ 1.64</u>
	<u>3,355,000</u>	<u>3.04</u>	<u>\$ 1.42</u>	<u>3,355,000</u>	<u>\$ 1.42</u>

The weighted average fair market value of options granted in the year ended December 31, 2007 is \$0.92 per option (2006 - \$1.46 per option). The fair value of each option granted was estimated on the date of grant using the Black-Scholes option pricing model with the following assumptions:

	<u>2007</u>	<u>2006</u>
Risk-free interest rate	4.37%	4.20%
Expected life of options	5 years	5 years
Volatility	163%-170%	143%-155.00%
Dividend yield rate	0%	0%

#### e) Warrants:

Warrants outstanding are as follows:

	<u>2007</u>		<u>2006</u>	
	Number of Warrants	Amount	Number of Warrants	Amount
Balance, beginning of year	-	\$ -	1,637,500	\$ -
Issued	7,504,000	3,757,090	-	-
Exercised	-	-	(1,521,250)	-
Expired	-	-	(116,250)	-
Balance, end of year	<u>7,504,000</u>	<u>\$ 3,757,090</u>	<u>-</u>	<u>\$ -</u>

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# International Frontier Resources Corporation

## Notes to the Consolidated Financial Statements

December 31, 2007 and 2006

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### 11. Share capital (continued)

#### e) Warrants (continued)

(i) In conjunction with a bought deal unit financing on February 22, 2007 the Company raised proceeds of \$15,500,000. Each unit is comprised of one common share and one-half warrant. One full warrant entitles the holder, on exercise to purchase one additional non-flow through share at a price of \$1.60 per share. The Company received approval from the TSX-V to extend the expiry date of the warrants from February 22, 2008 to May 22, 2008. Subsequent to year end none of the warrants had been exercised.

(ii) Concurrently with the issuance of the units, the Company issued 1,204,000 underwriter warrants which entitle the holder, on exercise, to purchase one common share at a price of \$1.60 on or before February 22, 2008. In addition, the Company issued 100,000 Corporate Finance Units to the underwriter. Each unit consists of one common share and one warrant. One warrant entitles the holder the right to acquire one common share at a price of \$1.60 on or before February 22, 2008. The underwriter warrants and corporate finance warrants expired unexercised on February 22, 2008

The weighted average fair market value of warrants granted in the year ended December 31, 2007 is \$0.50 per warrant (2006 – \$Nil). The fair value of each warrant granted was estimated on the date of grant using the Black-Scholes option pricing model with the following assumptions:

	<u>2007</u>	<u>2006</u>
Risk-free interest rate	4.11%	-
Expected life of options	1 year	-
Volatility	82%	-
Dividend yield rate	0%	0%

#### f) Contributed surplus:

	<u>2007</u>	<u>2006</u>
Balance, beginning of year	\$ 4,474,570	\$ 3,928,115
Value attributed to stock options granted	2,258,370	729,830
Value of stock options exercised	<u>-</u>	<u>(183,375)</u>
Balance, end of year	<u>\$ 6,732,940</u>	<u>\$ 4,474,570</u>

At December 31, 2007, \$406,640 (2006 – \$Nil) of the value attributed to stock options granted in the year were capitalized to petroleum and natural gas properties.

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## International Frontier Resources Corporation

### Notes to the Consolidated Financial Statements

December 31, 2007 and 2006

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#### 12. Per share

	<u>2007</u>	<u>2006</u>
Net loss	\$ (6,083,385)	\$ (1,229,645)
Weighted average number of shares	<u>56,889,170</u>	<u>41,409,880</u>
Basic loss per share	<u>\$ (0.11)</u>	<u>\$ (0.03)</u>
Weighted average number of shares	<b>56,889,170</b>	41,409,880
Dilutive effect of stock options	<u>634,260</u>	<u>706,936</u>
Dilutive weighted average number of shares	<u><b>57,523,430</b></u>	<u>42,116,816</u>

In calculating diluted common share amounts for the year ended December 31, 2007, the Company excluded 3,525,000 (2006 – 3,432,000) options and 7,504,000 (2006 – Nil) warrants because the exercise price was greater than the average market price of its common shares during the year. In addition, at December 31, 2007, Nil (2006 – Nil) convertible debentures were included in the amount used in calculating diluted common share amounts.

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#### 13. Related party transactions

a) During the year, the Company paid consulting fees to certain officers and directors as follows:

	<u>2007</u>	<u>2006</u>
Director's fees and other compensation	\$ 47,000	\$ 282,500
Royalty incentive program	<u>10,510</u>	<u>12,690</u>
	<u>\$ 57,510</u>	<u>\$ 295,190</u>

At December 31, 2007, \$10,510 (2006 – \$85,190) of the above amounts were included in payables and accruals.

b) During the year, \$30,725 (2006 - \$43,600) was paid to a law firm in which a Director of the Company is a partner. Of this amount, \$Nil is included in payables and accruals at December 31, 2007. These costs are included in general and administrative expenses on the consolidated statements of operations and deficit.

c) During the year, certain officers and directors of the Company participated in share offerings purchasing 20,400 flow through shares at a price of \$1.50 per share in February 2007 and 62,500 flow through shares at a price of \$0.80 per share in December 2007.

The above transactions were incurred in the normal course of operations of the Company and have been recorded at the exchange amounts that were established and agreed upon by the related parties.

# International Frontier Resources Corporation

## Notes to the Consolidated Financial Statements

December 31, 2007 and 2006

### 14. Commitments and contingencies

a) The Company has letters of credit for its share of refundable deposits on Northwest Territories Exploration Licenses. The letters of credit are secured by a total assignment of cash of \$2,267,175 (2006 – \$1,538,125) – (Note 5). The Company is contingently liable under the letters of credit for its proportionate share of the refundable deposit of \$2,267,175 (2006 - \$1,538,125). The deposits are refundable to the Company upon the Company meeting its work commitments, in whole or in part in the amount of \$9,068,700. The deposits will be refunded by \$1 for every \$4 spent on qualified expenditures on each Exploration License. A refund of \$182,138 was approved on February 29, 2008.

b) The Company is party to an agreement to lease its premises until December 31, 2011. The annual rent of premises consists of a minimum rent plus occupancy costs. Minimum rent payable for premises until the end of the lease are as follows:

2008	\$	86,570
2009	\$	86,570
2010	\$	86,570
2011	\$	86,570

c) The Company has established a Royalty Incentive Agreement for employees, consultants and directors. Under the plan, the compensation committee issues units on an annual basis to employees, consultants and directors. The units entitle the holder to receive an annual payment based on 2% of the Company's annual production revenue, net of transportation and processing fees. Under the terms of the agreement once the Company has recovered payout of 100% of its cumulative annual capital expenditures the payment to employees, consultants and directors is based on 4% of the Company's annual production revenue.

### 15. Supplemental cash flow information

Changes in non-cash working capital items increase (decrease) cash as follows:

	2007	2006
Receivables	\$ (771,800)	\$ 1,474,400
Prepays	(131,100)	100,820
Payables and accruals	<u>3,131,845</u>	<u>786,705</u>
	<u>\$ 2,228,945</u>	<u>\$ 2,361,925</u>
Operating activities	\$ 340,855	\$ 977,365
Investing activities	1,888,090	1,384,560
Financing activities	-	-
	<u>\$ 2,228,945</u>	<u>\$ 2,631,925</u>
Interest paid	<u>\$ 6,175</u>	<u>\$ 17,805</u>
Cash and cash equivalents are comprised of:		
Cash	\$ 3,242,150	\$ 496,340
Short term banker's acceptances		
(bearing interest rates ranging from 3.81% - 4.61% (2006: 2.55% - 3.85%))	<u>22,074,790</u>	<u>11,357,200</u>
	<u>\$ 25,316,940</u>	<u>\$ 11,853,540</u>

# International Frontier Resources Corporation

## Notes to the Consolidated Financial Statements

December 31, 2007 and 2006

### 16. Segmented information

The Company's activities are conducted in two geographic segments: Canada and the United Kingdom. All activities relate to exploration for and development of petroleum and natural gas.

#### a) Earnings (Loss)

<u>December 31, 2007</u>	<u>Canada</u>	<u>U.K.</u>	<u>Total</u>
Oil revenues, net	\$ 787,020	\$ -	\$ 787,020
Less: royalties	<u>(179,530)</u>	<u>-</u>	<u>(179,530)</u>
	607,490	-	607,490
Interest income	1,120,040	34,935	1,154,975
Prospect fee income	<u>194,755</u>	<u>-</u>	<u>194,755</u>
	<u>1,922,285</u>	<u>34,935</u>	<u>1,957,220</u>
Expenses			
Field operating costs	508,025	-	508,025
Depletion, depreciation and impairments	178,415	4,280,860	4,459,275
Accretion	16,775	-	16,775
Foreign exchange gain (loss)	132,555	132,610	265,165
General and administration	866,300	6,490	872,790
Stock based compensation	<u>1,851,725</u>	<u>-</u>	<u>1,851,725</u>
	<u>3,553,795</u>	<u>4,419,960</u>	<u>7,973,755</u>
Loss before income taxes	(1,631,510)	(4,385,025)	(6,016,535)
Future income tax expense	66,850	-	66,850
Net loss	<u>\$ (1,698,360)</u>	<u>\$ (4,385,025)</u>	<u>\$ (6,083,385)</u>
<u>December 31, 2006</u>	<u>Canada</u>	<u>U.K.</u>	<u>Total</u>
Oil revenues, net	\$ 965,370	\$ -	\$ 965,370
Less: royalties	<u>(219,005)</u>	<u>-</u>	<u>(219,005)</u>
	746,365	-	746,365
Interest income	449,095	-	449,095
Prospect fee income	<u>172,500</u>	<u>-</u>	<u>172,500</u>
	<u>1,367,960</u>	<u>-</u>	<u>1,367,960</u>
Expenses			
Field operating costs	398,785	-	398,785
Depletion, depreciation and impairments	1,222,010	-	1,222,010
Accretion	21,560	-	21,560
General and administration	807,085	26,870	833,955
Stock based compensation	<u>729,830</u>	<u>-</u>	<u>729,830</u>
	<u>3,179,270</u>	<u>26,870</u>	<u>3,206,140</u>
Loss before income taxes	(1,811,310)	(26,870)	(1,838,180)
Future income tax expense	608,535	-	608,535
Net loss	<u>\$ (1,202,775)</u>	<u>\$ (26,870)</u>	<u>\$ (1,229,645)</u>

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## International Frontier Resources Corporation

### Notes to the Consolidated Financial Statements

December 31, 2007 and 2006

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#### 16. Segmented information (continued)

##### b) Property and equipment

<u>December 31, 2007</u>	<u>Canada</u>	<u>U.K.</u>	<u>Total</u>
Capital expenditures			
Cash expenditures	\$ 3,834,760	\$ 5,177,305	\$ 9,012,065
Asset retirement provision	303,345	-	303,345
Stock options costs	<u>294,800</u>	<u>111,835</u>	<u>406,635</u>
	<u>\$ 4,432,905</u>	<u>\$ 5,289,140</u>	<u>\$ 9,722,045</u>
 Property and equipment	 <u>\$ 15,391,060</u>	 <u>\$ 2,113,815</u>	 <u>\$ 17,504,875</u>
<u>December 31, 2006</u>	<u>Canada</u>	<u>U.K.</u>	<u>Total</u>
Capital expenditures			
Cash expenditures	\$ 5,504,000	\$ 929,410	\$ 6,433,410
Asset retirement provision	-	-	-
Stock options costs	<u>-</u>	<u>-</u>	<u>-</u>
	<u>\$ 5,504,000</u>	<u>\$ 929,410</u>	<u>\$ 6,433,410</u>
 Property and equipment	 <u>\$ 11,131,820</u>	 <u>\$ 1,105,265</u>	 <u>\$ 12,237,085</u>

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#### 17. Financial Instruments

As disclosed in Note 2, the Company holds various forms of financial instruments. The nature of these instruments and the Company's operations expose the Company to fair value, foreign currency and industry credit risks. The Company manages its exposure to these risks by operating in a manner that minimizes its exposure to the extent practical.

##### a) Commodity price risk

The Company will be subject to commodity price risk for the delivery of natural gas and crude oil.

##### b) Credit risk

Substantially all of the Company's accounts receivable are with customers and joint venture partners in the oil and gas industry and are subject to normal industry credit risks.

##### c) Foreign currency risk

Foreign currency risk is the risk that a variation in exchange rates between the Canadian dollar and foreign currencies will affect the Company's operating and financial results. The Company is exposed to foreign currency risk as the Company holds cash and cash equivalents on hand that are denominated in United States currency and is exposed to foreign currency fluctuations on its operations in the United Kingdom as these are denominated in British pounds. At December 31, 2007, there were no contracts in place to fix the exchange rates on these transactions.

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# **International Frontier Resources Corporation**

## **Notes to the Consolidated Financial Statements**

December 31, 2007 and 2006

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### **17. Financial Instruments (continued)**

#### **c) Fair Values**

The Company's financial instruments included on the balance sheets as at December 31, 2007 and 2006 are comprised of cash and cash equivalents, accounts receivable, payables and accruals and convertible debentures. The fair values of these financial instruments approximate their carrying value due to the short-term nature of those instruments.

#### **d) Interest Rate Risk**

The Company is exposed to interest rate cash flow risk to the extent the changes in market interest rates will impact the Company's interest rate price risk to the extent that the convertible debentures have a fixed interest rate.

**International Frontier Resources Corporation  
Management's Discussion and Analysis  
2007 Annual and Fourth Quarter Results**



International Frontier Resources Corporation is engaged in the exploration for and development of petroleum and natural gas reserves in the frontier regions of the Northwest Territories, Canada and the UK sector of the North Sea.

The following is management's discussion and analysis ("MD&A") of International Frontier Resources Corporation's ("International Frontier" or "IFR" or "Britcana" or the "Company") operating and financial results for the year ended December 31, 2007, as well as information concerning the Company's future outlook based on currently available information. This MD&A should be read in conjunction with the Company's December 31, 2007 audited consolidated financial statements and related notes and the Company's 51-101 report filed on Sedar.

The MD&A and the annual consolidated financial statements and accompanying notes have been prepared by management and approved by the Audit Committee of the Board of Directors.

The quarterly financial statements have not been reviewed or audited on behalf of the shareholders by the Company's independent external auditors.

All financial measures presented in this Annual Report are expressed in Canadian dollars unless otherwise indicated.

**Liquidity, capital resources and financing activities**

At December 31, 2007 cash and cash equivalents were \$25,316,940 (2006 - \$11,853,540), and working capital was \$22,407,855 (2006 - \$11,348,175). The increase in working capital at December 31, 2007 as compared to 2006 is the result of funds raised in a non-brokered private placement completed in the first quarter of 2007. The Company does not have any exposure to asset backed securities

**Annual Results**

The following table summarizes results for the years 2007, 2006, and 2005.

	<b>2007</b>	<b>2006</b>	<b>2005</b>
Sales volumes – BOE/day (Canada)	38	48	50
Oil Revenues, net (Canada)	\$ 607,490	\$ 746,365	\$ 656,080
Interest income			
Canada	\$ 1,120,040	\$ 449,095	\$ 219,135
United Kingdom	34,935	-	-
Consolidated interest income	<u>\$ 1,154,975</u>	<u>\$ 449,095</u>	<u>\$ 219,135</u>
Net loss and comprehensive loss			
Canada	\$ (1,698,360)	\$ (1,202,775)	\$ (1,837,235)
United Kingdom	<u>(4,385,025)</u>	<u>(26,870)</u>	<u>-</u>
Consolidated net loss and comprehensive loss	<u>\$ (6,083,385)</u>	<u>\$ (1,229,645)</u>	<u>\$ (1,837,235)</u>
Net loss per share – basic and diluted	\$ (0.11)	\$ (0.03)	\$ (0.05)
Property and equipment			
Canada	\$ 15,391,060	\$ 11,131,820	\$ 6,822,780
United Kingdom	2,113,815	1,105,265	175,855
Consolidated property and equipment	<u>\$ 17,504,875</u>	<u>\$ 12,237,085</u>	<u>\$ 6,998,635</u>
Total assets	\$ 46,596,795	\$ 26,238,655	\$ 23,536,000
Working capital	\$ 22,407,855	\$ 11,348,175	\$ 14,762,475
Flow through share obligations	\$ 3,498,025	\$ -	\$ 5,337,725

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**Annual Results (continued)**

***Sales volumes***

Sales volumes for 2007 were 38 Bbl/day per day down 10 Bbl/day compared to 2006 and down 22 Bbl/day compared to 2005. The decrease in sales volumes in 2007 can be attributed to natural decline rates as forecasted in the Company's engineering report.

***Gross revenues and royalties***

Gross oil revenues in 2007 were \$787,020 a decrease of \$138,875 or 18% as compared to revenues in 2006 of \$965,370 (2005 - \$866,190). Decrease in revenues as compared to years ended December 31, 2006 and 2005 is due to decline in production mitigated by an increase in price in 2006 and 2007. Decrease in net oil revenues in 2007 of \$175,235 or 23% as compared to net oil revenues of \$746,365 in 2006 (2005 - \$656,080) is a result of decline in production mitigated by an increase in the average price received in 2006 of 2% from \$55.24 per Bbl for the year ended December 31, 2006 to \$56.20 per Bbl for the same period in 2007.

Gross overriding royalty costs were \$164,520 or 21% of gross revenues in 2007 as compared with \$200,880 or 21% of gross revenues in 2006 and \$180,340 or 21% of gross revenues in 2005. The decrease in royalties in 2007 of \$36,360 or 18% is due to a decrease in production received in during the year ended December 31, 2007 as compared to the same period in 2006.

For the period ending December 31, 2007 the Company paid royalties of \$15,010 (2006 - \$18,125 and 2005 - \$29,770) to certain officers, directors and consultants in accordance with the Company's Royalty Incentive Plan.

***Field operating costs***

During 2007 the Company incurred operating expenses of \$508,025, an increase of \$109,240 or 27% as compared to operating expenses incurred in year ended December 31, 2006 of \$398,785 (2005 - \$409,000). Operating costs per Bbl increased in 2007 by 59% averaging \$36.30 per Bbl as compared \$22.80 Bbl throughout 2006 (2005 - \$22.40 per Bbl). The increase in operating costs in 2007 is the result of further Sidox field testing coupled with natural production declines.

***Interest income***

In 2007 interest income from short term investments was \$1,120,040 compared to interest income in 2006 of \$449,100 and interest income in 2005 of \$219,135. The variance in annual interest income earned is a result of annual cash balances invested during the year. The Company does not have any exposure to asset backed securities. Interest income at December 31, 2007 also includes \$34,935 (2006 - \$Nil, 2005 - \$Nil) of interest earned from cash balances in the U.K.

***Prospect Fees***

At December 31, 2007 the Company earned prospect fees of \$194,755 (2006 - \$172,500, 2005 - \$Nil) related to prospect fees earned by the Company in the fourth quarter of 2007 and the third quarter of 2006 respectively.

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**Annual Results (continued)**

**Depletion and depreciation**

Depletion, depreciation and impairments at December 31, 2007 and 2006 consist of the following

**December 31, 2007**

<b>Depletion, depreciation and impairments</b>	<b>Canada</b>	<b>U.K</b>	<b>Total</b>
Depletion of natural gas properties	\$ 167,745	\$ -	\$ 167,745
Impairment of natural gas properties	-	4,280,860	4,280,860
Amortization of Sidox license	5,000	-	5,000
Depreciation of equipment	5,670	-	5,670
	<u>\$ 178,415</u>	<u>\$ 4,280,860</u>	<u>\$ 4,459,275</u>

**December 31, 2006**

<b>Depletion, depreciation and impairments</b>	<b>Canada</b>	<b>U.K</b>	<b>Total</b>
Depletion of natural gas properties	\$ 210,050	\$ -	\$ 210,050
Impairment of natural gas properties	1,000,620	-	1,000,620
Amortization of Sidox license	5,000	-	5,000
Depreciation of equipment	6,340	-	6,340
	<u>\$ 1,222,010</u>	<u>\$ -</u>	<u>\$ 1,222,010</u>

Depletion of petroleum and natural gas assets in Canada at December 31, 2007 decreased by \$42,305 or 20%. The depletion rate of \$12.00 per Bbl remained consistent in 2007 as compared to 2006. The decrease in depletion in 2007 can be attributed to the decline in production during 2007 coupled with increased future reserves as evaluated by reserve engineers at December 31, 2007.

In 2007 the carrying value of properties in the exploration stage in the Northwest Territories increased to \$13,805,330, from \$10,251,500 in 2006 and in the North Sea the book value of properties in the exploration stage increased to \$2,413,000 from \$1,105,000 in 2006. These amounts were excluded from the depletion calculation at December 31, 2007.

As at December 31, 2007, \$Nil (2006 - \$1,000,620) impairment of petroleum and natural gas assets has been recorded as part of depletion to reflect the excess carrying amount of assets over fair value of future reserves in Canada. In addition, at December 31, 2007 \$4,280,860 (2006 - \$Nil) relating to the cost of three dry holes was included as an impairment of petroleum and natural gas assets in the North Sea and were recorded as part of depletion.

**Accretion of asset retirement obligation**

The accretion of asset retirement obligations December 31, 2007 of \$16,775 decreased by \$4,785 or 22% as compared to \$21,560 (2005 - \$21,710) for the year ended December 31, 2006.

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**Annual Results (continued)**

**General and administrative expenses**

	2007	2006	2005
Investor relations	\$ 107,180	\$ 36,170	\$ 50,650
Filing and transfer fees	39,310	33,580	26,445
Professional fees	176,785	143,480	151,875
Consulting fees - gross	446,195	373,550	326,195
Consulting fees - capitalized	(154,350)	(82,800)	(105,625)
Rent and office costs	257,670	214,140	151,100
Part 12.6 Tax	-	115,835	37,810
	<u>\$ 872,790</u>	<u>\$ 833,955</u>	<u>\$ 638,450</u>

In 2007 general and administrative expenses increased by \$38,835 or 5% and \$234,340 and 37% to \$872,790 for the year ended December 31, 2007 as compared to \$ 833,955 for 2006 and \$638,450 for 2005 respectively. The increase in G&A costs in 2007 is a result of legal and accounting fees relating to the Company's financing as well as increases in filing and transfer fees relating to corporate equity financings plus a general increase in office costs and salaries. Included in general and administrative expenses is \$6,490 (2006 - \$26,870) of legal expenses incurred in the North Sea.

**Stock based compensation**

Stock based compensation costs increased from \$1,562,450 in the year ended December 31, 2006 to \$1,851,725 in the same period in 2007 due to an increased number of options issued to officers, directors, employees and consultants during the year.

**Net earnings (loss)**

International Frontier recorded a consolidated net loss of \$3,644,345 (\$0.06 loss per share) for the year ended December 31, 2007 as follows:

<b>Net earnings (loss):</b>	<b>2007</b>	<b>2006</b>	<b>2005</b>
Canada	\$(1,698,360)	\$ (1,202,775)	\$ (1,837,235)
United Kingdom	(4,385,025)	(26,870)	-
<b>Consolidated net loss</b>	<b>\$(6,083,385)</b>	<b>\$ (1,229,645)</b>	<b>\$ (1,837,325)</b>
<b>Loss per share</b>	<b>\$ (0.11)</b>	<b>\$ (0.03)</b>	<b>\$ (0.05)</b>

During the year ended December 31, 2007 loss before tax increased Canada due to a future income tax expense of \$66,850 at December 31, 2007 as compared to a recovery of \$608,535 for the year ended December 31, 2006. Net loss at December 31, 2007 was mitigated by an increase of interest income earned on cash balances in the year as compared to 2006. The increase in net loss in the United Kingdom can be attributed to an impairment of petroleum and natural gas properties in the amount of \$4,280,860 (2006 - \$Nil) related to the drilling of three dry holes.

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**Annual Results (continued)**

***Funds flow from operations***

Funds flow from operations is not a recognized measure under Canadian generally accepted accounting principles ("GAAP"). Management believes that funds flow from operations is a useful measure of financial performance. For the purposes of funds flow from operations calculations, the following table reconciles the non-GAAP financial measures "funds flow from operations" to "net income," the most comparable measure calculated in accordance with GAAP:

	2007	2006	2005
Net loss	\$(6,083,385)	\$ (1,229,645)	\$ (1,837,235)
Non-cash items			
Depletion, depreciation and impairments	4,459,275	1,222,010	203,435
Accretion	16,775	21,560	21,710
Stock based compensation	1,851,725	729,830	1,562,450
Gain on sale of investment	-	-	(4,745)
Write off of investment	-	-	52,875
Future income tax recovery	66,850	(608,535)	(175,880)
Asset retirement obligation	(223,145)	(5,960)	(69,610)
<b>Funds flow from operations</b>	<b>\$ 88,095</b>	<b>\$ 129,260</b>	<b>\$ (247,000)</b>

**Financial Instruments**

International Frontier has not entered into any commodity or financial instrument hedges. The Company carries various forms of financial instruments, all of which are recognized in International Frontier's audited consolidated financial statements at December 31, 2007. Unless otherwise denoted in the December 31, 2007 audited consolidated financial statements it is management's opinion that the Company is not exposed to significant interest, currency or credit risks arising from these financial instruments. The fair values of financial instruments approximate their carrying value. The Company has no unrecognized gains or losses in its financial statements.

**Investing Activities**

Year ended December 31,	2007	2006	2005
Capital expenditures			
Canada	\$ 3,834,760	\$ 5,504,000	\$ 2,647,025
United Kingdom	5,177,305	929,410	175,855
	<u>\$ 9,012,065</u>	<u>\$ 6,433,410</u>	<u>\$ 2,822,880</u>

Capital expenditures for the period ending December 31, 2007 were \$9,012,065 (2006 – \$6,433,410) of which \$3,834,760 or 43% (2006 – 86%, 2005 – 94%) is related to exploration activities in the Central Mackenzie Valley, NWT and \$5,177,305 or 57% (2006 – 14%, 2005 – 6%) is related to exploration activities in the U.K. North Sea. Operations in these areas are expensive and of a high risk nature that could create conditions that could alter the plans of the Company and its partners. Further, should commercial quantities of petroleum and natural gas be proven to exist in the areas, the timing of revenue generation is dependent on a variety of factors not within control of the Company.

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**Obligations**

Under the terms of the flow-through agreements undertaken in 2007, the Company had flow-through share spending obligations of \$3,498,025 (2006 - \$Nil, 2005 - \$5,337,725) at December 31, 2007. The Company has sufficient working capital to meet its flow through share obligations. The Company is party to an agreement to lease its premises until December 31, 2011. The annual rent of premises consists of a minimum rent payment of \$86,570 plus occupancy costs. Minimum rent payable for premises until the end of the lease will be \$86,570 per year to the end of December 31, 2011.

**Related Party Transactions**

Certain officers and directors and consultants provide professional, consulting and management services to the Company and are eligible to receive royalties pursuant to the Company's Royalty Incentive Plan. Total amounts paid to officers and directors during the year ended December 31, 2007 in respect of consulting fees and royalties were \$59,750 (2006 - \$295,190, 2005 - \$206,835). Of the total consulting fees paid to related parties during the year \$6,950 (2006 - \$82,800, 2005 - \$93,375) was capitalized to property and equipment at December 31, 2007. In addition, during the year \$30,725 (2006 - \$43,600, 2005 - \$8,400) was paid to a law firm in which a Director is a partner. These costs are included in general and administrative expenses on the consolidated statements of loss, deficit and comprehensive loss at December 31, 2007. During the year certain officers and directors purchased 20,400 flow through shares at a price of \$1.50 per share in February 2007 and 62,500 flow through shares at a price of \$0.80 per share in December 2007.

**Summary of Quarterly Results**

The quarterly results have been prepared without audit or review by the Company's independent external auditors. The following table summarized the Company's financial and operating highlights for the past eight quarters:

<b>Unaudited:</b>	<b>March 31, 2006</b>	<b>June 30, 2006</b>	<b>Sept. 30, 2006</b>	<b>Dec. 31, 2006</b>	<b>March 31, 2007</b>	<b>June 30, 2007</b>	<b>Sept. 30, 2007</b>	<b>Dec. 31, 2007</b>
Sales volumes – Bbl/ day	50	52	46	42	36	35	44	38
Revenues, net (\$)	240,305	246,080	209,995	133,490	130,035	134,605	186,915	155,930
Net earnings (loss) - (\$)	(217,450)	(135,290)	(472,900)	(404,005)	(415,770)	(1,060,295)	21,290	(4,334,515)
Net loss per share– basic & diluted - (\$)/share	(0.01)	(0.00)	(0.01)	(0.01)	(0.01)	(0.02)	(0.00)	(0.08)
Total assets	23,440,490	26,402,100	25,928,020	26,238,655	47,245,705	46,772,450	47,572,995	46,596,795
Working capital (\$)	12,555,475	13,439,825	13,540,290	11,348,175	32,305,425	31,204,960	29,631,060	22,407,855
Restricted cash on deposit (\$)	2,016,225	1,596,700	1,538,125	1,538,125	1,538,125	1,912,430	1,912,430	2,267,175
Funds flow form operations (\$)	2,535	97,655	287,250	(258,170)	2,529	(60,650)	72,510	54,340



## **Fourth Quarter Results**

The following summarizes the results for the three months ended December 31, 2007 compared with the same period in 2006.

### ***Sales Volumes***

Sales volumes in the fourth quarter of 2007 were 38 Bbl/day a decrease of 4 Bbl/day or 10% as compared to the same period in 2006 with sales volumes of compared to 42 Bbl/day in 2006. The decline in sales volumes in 2007 as compared to 2006 is due to natural decline rates as forecasted in the Company's engineering report.

### ***Gross revenues and royalties***

Gross revenues were \$218,500 in the fourth quarter of 2007, an increase of \$27,315 or 14% as compared to \$191,185 for the same period in 2006. The increase in gross revenues in the fourth quarter of 2007 is a direct result of a 25% increase in average price per Bbl received of in the three months ended December 31, 2007 at \$61.34 per Bbl as compared to \$49.10 per Bbl in the third quarter of 2006, which was slightly mitigated by a decrease in production of 4 Bbl per day or 10%.

Gross overriding royalty costs were relatively consistent with \$47,560 or 22% in the fourth quarter of 2007 as compared with \$39,570 or 21% in the same quarter in 2006.

### ***Interest income***

In the fourth quarter of 2007 interest income from short term investments was \$347,595 up from \$207,445 or 148% as compared to \$140,150 for the three months ended December 31, 2006. The increase in interest income received is a result of a larger cash balance in the period. Interest income earned in the fourth quarter of December 31, 2007 also includes \$28,190 (2006 - \$Nil) of interest earned from cash balances in the U.K. in that period.

### ***Field operating costs***

Operating expenses were \$100,180 or \$25.75 per Bbl for the three months ended December 31, 2006 as compared with \$145,425 or \$40.85 per BOE in 2007. This increase of \$45,245 or 45% in the fourth quarter of 2007 as compared to the same period in 2006 was due primarily to increased operating costs, well workovers and facility turn arounds.

### ***Depletion and Depreciation***

Consolidated depletion, depreciation and impairments on oil and gas properties was \$4,346,390 in the fourth quarter of 2007 as compared to \$286,650 in the same period in 2006. Included in this amount was depletion of oil and gas properties in Canada of \$63,000 or \$17.70 per Bbl which is comparable to \$16.60 per Bbl or \$64,625 in the fourth quarter of 2006.

In addition for the fourth quarter ended December 31, 2007 consolidated depletion, depreciation and impairments includes a \$Nil (2006 - \$1,000,620) impairment of petroleum and natural gas assets which has been recorded as part of depletion to reflect the excess carrying amount of assets over fair value of future reserves in Canada. At December 31, 2007 a \$4,280,860 (2006 - \$Nil) impairment of petroleum and natural gas assets in the North Sea was incurred relating to the costs of three dry holes. These costs were recorded as part of depletion.

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**Fourth Quarter Results (continued)**

**General and Administrative Costs**

General and administrative expenses in the fourth quarter of 2007 were \$285,545 a decrease of \$149,580 or 34% as compared to \$423,500 for the fourth quarter of 2006. This decrease is primarily a result of Part 12.6 tax accrued at December 31, 2006 with respect to flow through shares issued in 2005. There were no such costs incurred in the same period in 2007.

**Stock based compensation**

There were no stock options issued or exercised in the fourth quarter of 2007, therefore, no stock based compensation costs were booked for the three months ended December 31, 2007, which is consistent with the three months ended December 31, 2006.

**Net earnings (loss)**

International Frontier recorded a consolidated net loss of \$1,895,475 (\$0.03 loss per share) for the quarter ended December 31, 2007 as follows:

<b>Net earnings (loss):</b>	<b>Q4 - 2007</b>	<b>Q4 - 2006</b>
Canada	\$ 3,505	\$ (396,135)
United Kingdom	(4,338,020)	(7,870)
<b>Consolidated net loss</b>	<b>\$ (4,334,515)</b>	<b>\$ (404,005)</b>
<b>Loss per share</b>	<b>\$ (0.08)</b>	<b>\$ (0.01)</b>

The increased earnings in Canada for the fourth quarter ended December 31, 2007 can be attributed to a larger cash balance resulting in an increase in interest income earned in the period. The increase in net loss in the United Kingdom can be attributed to impairment of petroleum and natural gas properties in the North Sea of \$4,280,860 (2006 - \$Nil) booked in the fourth quarter of 2007.

**Other Items**

**Outstanding shares, options and warrants**

The Company's share capital structure is as follows:

<b>As of:</b>	<b>December 31, 2007</b>	<b>April 8, 2008</b>
Common shares outstanding	58,578,965	59,241,546
Warrants outstanding	7,504,000	6,200,000
Options outstanding	5,855,000	5,855,000
Convertible debentures	86,667	86,667
<b>Fully diluted</b>	<b>72,024,632</b>	<b>70,720,632</b>

Additional details on the shares, options and warrants outstanding at December 31, 2007 are available in the Notes to the December 31, 2007 audited consolidated financial statements.



### ***Accounting Policy Changes***

On January 1, 2007, the Company adopted the new Canadian accounting standards for financial instruments – recognition and measurement, financial instruments – presentations and disclosures, hedging and comprehensive income. Prior periods have not been restated. Additional disclosure requirements for financial instruments and accounting changes have been approved by the Canadian Institute of Chartered Accountants and will be required disclosure beginning January 1, 2008. These new standards have no material impact on the Company's financial statements.

#### ***Financial Instruments – Recognition and Measurement***

This new standard requires all financial instruments within its scope, including all derivatives, to be recognized on the balance sheet initially at fair value. Subsequent measurement of all financial assets and liabilities except those held-for-trading and available for sale are measured at amortized cost determined using the effective interest rate method. Held for– trading financial assets are measured at fair value with changes in fair value recognized in earnings. Available-for-sale financial assets are measured at fair value with changes in fair value recognized in other comprehensive income and reclassified to earnings when derecognized or impaired. There were no changes to the measurement of existing financial assets and liabilities at the date of adoption.

Cash and cash equivalents are designated as “held-for-trading” and are measured at carrying value, which approximates fair value due to the short-term nature of these instruments. Accounts receivable are designated as “loans and receivables” and accounts payable and accrued liabilities and bank loans are designated as “other liabilities”, all of which are measured at carrying value, which approximates fair value due to the short-term nature of these instruments. Risk management assets and liabilities are derivative financial instruments classified as “held-for-trading” unless designated for hedge accounting. The Company has no commodity contracts or fixed-price physical contracts in place at this time.

#### ***Derivatives***

The Company may use various types of derivative financial instruments to manage risks associated with crude oil and natural gas fluctuations. These instruments are not used for trading or speculative purposes. Proceeds and costs realized from holding the related contracts are recognized in petroleum and natural gas revenues at the time that each transaction under a contract is settled. For the unrealized portion of such contracts, the Company utilized the fair value method of accounting. The fair value is based on an estimate of the amounts that would have been paid to or received from counterparts to settle these instruments given quoted future market prices and other relevant factors. The method requires the fair value of the derivative financial instruments to be recorded at each balance sheet date with unrealized gains or losses on these contracts recorded through net earnings. The Company had no derivatives in 2007.

#### ***Embedded Derivatives***

On adoption, the Company elected to recognize, as separate assets and liabilities, only for those embedded derivatives in hybrid instruments issued, acquired or substantively modified after January 1, 2003. The Company did not identify any material embedded derivatives which require separate recognition and measurement.

#### ***Other Comprehensive Income***

The new standards establish a new statement of comprehensive income, which is comprised of net earnings and other comprehensive income. The Company currently has no other comprehensive income items.

Beginning January 1, 2007 the Company adopted Section 1506 “Accounting Changes” the only impact of which is to provide disclosure of when an entity has not applied a new source of GAAP



### ***Accounting Policy Changes (continued)***

#### ***Other Comprehensive Income***

that has been issued but is not yet effective. This is the case with Section 3862 "Financial Instruments - Disclosures" and Section 3863 "Financial Instruments - Presentation" which are required to be adopted for fiscal years beginning on or after October 1, 2007. The Company will adopt these standards on January 1, 2008 and it is expected the only effect on the Company will be incremental disclosures regarding the significance of financial instruments for the entity's financial position and performance and the nature, extent and management of risks arising from financial instruments to which the entity is exposed.

As of January 1, 2008, the Company will be required to adopt CICA Handbook Section 1535 "Capital Disclosures", which requires entities to disclose their objectives, policies and processes for managing capital, and in addition, whether the entity has complied with any externally imposed capital requirements. The Company is assessing the impact of this new standard on its financial statements and anticipates that the main impact will be in terms of additional disclosures required.

As of January 1, 2008, the Company will be required to adopt CICA Handbook Section 3031, "Inventories". This new standard will have no impact on the Company's financial statements. In February 2008, the CICA issued Section 3064, "Goodwill and Intangible Assets", replacing Section 3062, "Goodwill and Other Intangible Assets" and Section 3450, "Research and Development Costs". Various changes have been made to other sections of the CICA Handbook, for consistency purposes. The new Sections will be applicable to financial statements relating to fiscal years beginning on or after October 1, 2008. Accordingly, the Company will adopt the new standards for

### ***Critical Accounting Estimates***

Management is required to make judgments, assumptions and estimates in the application of Canadian generally accepted accounting principles that have a significant impact on the financial results of the Company. Reserve estimates are a key component in the calculation of depletion, depreciation and accretion costs. A change in reserve quantity estimates will result in a corresponding change in DD&A costs. In addition, if capitalized costs are determined to be in excess of the calculated ceiling, which is based on reserve quantities and values, the excess must be written off as an expense. Asset retirement costs are estimated, discounted and carried on the balance sheet as a liability. A change in estimated future asset restoration costs will change the liability on the balance sheet and the amortization of the asset retirement costs included in property and equipment.



## **Forward Looking Statements**

This Management Discussion and Analysis (MD&A) contains forward-looking or outlook information which reflects management's expectations regarding the Company's growth, results of operations, performance and business prospects and opportunities. The use of words such as "anticipate", "continue", "estimate", "expect", "may", "project", "should", "believe", "outlook", "forecast" and similar expressions are intended to identify forward-looking statements. These statements reflect management's current beliefs and are based on information currently available to management. Forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause actual results of events to differ materially from those anticipated in these forward-looking statements. Although management believes the expectations reflected in these forward-looking statements are reasonable, there can be no assurance that actual results will be consistent with these forward-looking statements. Readers should not put undue reliance on forward-looking information. These statements are made as of the date hereof and management assumes no obligation to update or revise these statements to reflect new events or circumstances.

Our actual results could differ materially from those anticipated in these forward-looking statements as a result of the risk factors set forth below and elsewhere in this management discussion and analysis.

- Volatility in market prices for oil and natural gas;
- Risks inherent in our operations;
- Geological, technical, drilling and processing problems;
- General economic conditions;
- Industry conditions, including fluctuation in the price of oil and natural gas;
- Governmental regulation;
- Fluctuation in foreign exchange and interest rates;
- Unanticipated events that can reduce production or cause production to be shut-in or delayed;
- Failure to obtain industry partner and other third party consents and approvals, when required;
- The need to obtain required approvals from regulatory authorities; and
- The other factors discussed under "Operational and Other Business Risks" in this management discussion and analysis.

## **Operational and other business risks**

### ***Need to Replace and Grow Reserves***

The future oil and natural gas production of International Frontier, and therefore future cash flows, are highly dependent upon ongoing success in exploring its current and future undeveloped land base, exploiting the current producing properties, and acquiring or discovering additional reserves. Without reserve additions through exploration, acquisition or development activities, reserves and production will decline over time as reserves are depleted.

The business of discovering, developing, or acquiring reserves is capital intensive. To the extent cash flows from operations are insufficient and external sources of capital become limited or unavailable, the ability of International Frontier to make the necessary capital investments to maintain and expand its oil and natural gas reserves may be impaired.

There can be no assurance that International Frontier will be able to find and develop or acquire additional reserves to replace and grow production at acceptable costs.



### ***Exploration, Development and Production Risks***

Oil and natural gas exploration involves a high degree of risk, which even with a combination of experience, knowledge and careful evaluation may not be able to overcome. There is no assurance that expenditures made on future exploration by International Frontier will result in new discoveries of oil and natural gas in commercial quantities. It is difficult to project the costs of implementing an exploratory drilling program due to the inherent uncertainties of drilling in unknown formations, the costs associated with encountering various drilling conditions such as over pressured zones, tools lost in the hole and changes in drilling plans and locations as a result of prior exploratory wells or additional seismic data and interpretations thereof.

The long-term commercial success of International Frontier depends on its ability to find, acquire, develop and commercially produce oil and natural gas reserves. No assurance can be given that International Frontier will be able to continue to locate satisfactory properties for acquisition or participation. Moreover, if such acquisitions or participation are identified, International Frontier may determine that current markets, terms of acquisition and participation or pricing conditions make such acquisitions or participations uneconomic.

Future oil and gas exploration may involve unprofitable efforts, not only from dry wells, but from wells that are productive but do not produce sufficient net revenues to return a profit after drilling, operating and other costs. Completion of a well does not assure a profit on the investment or recover of drilling, completion and operating cost. In addition, drilling hazards or environmental damage could greatly increase the cost of operations, and various field operating conditions may adversely affect the production from successful wells. These conditions include delays in obtaining governmental approvals or consents, shut-ins of connected wells resulting from extreme weather conditions, insufficient storage or transportation capacity or other geological and mechanical conditions. While diligent well supervision and effective maintenance operations can contribute to maximizing production rate over time, production delays and declines from normal field operating conditions cannot be eliminated and can be expected to adversely affect revenue and cash flow levels to varying degrees.

In addition, oil and gas operations are subject to the risks of exploration, development and production of oil and natural gas properties, including encountering unexpected formations or pressures, premature declines of reservoirs, blowouts, sour gas releases, fires and spills. Losses resulting from the occurrence of any of these risks could have a materially adverse effect on future results of operations, liquidity and financial condition.

### ***Reserve Estimates***

The production forecast and recoverable estimates contained in International Frontier's engineering report are only estimates and the actual production and ultimate recoverable reserves from the properties may be greater or less than the independent estimates of McDaniel & Associates Consultants Ltd.

There are numerous uncertainties inherent in estimating quantities of reserves and cash flows to be derived thereof, including many factors that are beyond the control of International Frontier. The reserve and cash flow information set forth herein represent estimates only. The reserves and estimated future net cash flow from the assets of International Frontier have been independently evaluated effective December 31, 2007 by McDaniel & Associates Consultants Ltd. These evaluations include a number of assumptions relating to factors such as initial production rates, production decline rates, ultimate recovery of reserves, timing and amount of capital expenditure, marketability of production, future prices of oil and natural gas, operating costs and royalties and other government levies that may be imposed over the producing life of the reserves. These assumptions were based on price forecasts in use at the date the relevant

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evaluations were prepared and many of these assumptions are subject to change and are beyond the control of International Frontier. Actual production and cash flows derived thereof will vary from these evaluations, and such variations could be material. The foregoing evaluations are based in part on the assumed success of exploitation activities intended to be undertaken in future years. The reserves and estimated cash flows to be derived thereof contained in such evaluations will be reduced to the extent that such exploitation activities do not achieve the level of success assumed in the evaluations.

***Volatility of Oil and Natural Gas Prices***

The operational results and financial condition of International Frontier will be dependent on the prices received for oil and natural gas production. Oil and natural gas prices have fluctuated widely during recent years and are determined by supply and demand factors, including weather and general economic conditions, as well as conditions in other oil and natural gas regions. Any decline in oil and natural gas prices could have an adverse effect of the operations, proved reserves, and financial conditions of International Frontier and could result in a reduction of the net production revenue of the Company causing a reduction in its oil and gas acquisition and development activities. In addition, bank borrowings which might be made available to the Company are typically determined in part by the borrowing base of the reserves of International Frontier. A sustained material decline in prices from historical average prices could reduce the borrowing base of International Frontier, therefore reducing the bank credit available to International Frontier and could require that a portion of such bank debt be repaid.

International Frontier uses the full cost method of accounting for oil and natural gas properties. Under this accounting method, capitalized costs are reviewed on a quarterly basis for impairment to ensure that the carrying amount of these costs is recoverable based on expected future cash flows.

***Operational Hazards and Other Uncertainties***

Oil and natural gas exploration operations are subject to all the risks and hazards typically associated with such operations, including hazards such as fire, explosion, blowouts, and oil spills, each of which could result in substantial damage to oil and natural gas wells, production facilities, other property and the environment or in personal injury. In accordance with industry practice, International Frontier is not fully insured against all of these risks, nor is all such risks insurable. Although International Frontier will maintain liability insurance, where available, in an amount which it considers adequate and consistent with industry practice, the nature of these risks is such that liabilities could exceed policy limits, in which event International Frontier could incur significant costs that could have a material adverse affect upon its financial condition. Business interruption insurance may also be purchased for selected facilities, to the extent that such insurance is available. Oil and natural gas production operations are also subject to all the risks typically associated with such operations, including premature decline of reservoirs and the invasion of water into producing formations.

Oil and natural gas exploration and development activities are dependent on the availability of drilling and related equipment in the particular areas where such activities will be conducted. Demand for such equipment or access restrictions may affect the availability and/or cost of such equipment to International

Frontier and may delay exploration and development activities. To the extent International Frontier is not the operator of its oil and gas properties, the Company will be dependent on other operators for timing of activities related to non-operating properties and will be largely unable to direct or control the activities of the operators.

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Although property title reviews will be done according to industry standards prior to the purchase of most oil and natural gas producing properties or the commencement of drilling wells, such reviews do not guarantee or certify that an unforeseen defect in the chain of title will not arise to defeat the claim of International Frontier which could result in reduction of the revenue received by the Company.

***Competition***

There is strong competition relating to all aspects of the oil and natural gas industry. International Frontier will actively compete for capital, skilled personnel, undeveloped land, reserve acquisitions, access to drilling rigs, service rigs and other equipment, access to processing facilities and pipeline and refining capacity, and in all other aspects of its operations with a substantial number of other organizations, many of which may have greater technical and financial resources than does International Frontier.

***Key Personnel***

The success of International Frontier will depend in large measure on certain key personnel. The loss of the services of such key personnel could have a material adverse affect on International Frontier. International Frontier does not have key person insurance in effect for management. The contributions of these individuals to the immediate operations of International Frontier are likely to be of central importance. In addition, the competition for qualified personnel in the oil and natural gas industry is intense and there can be no assurance that International Frontier will be able to continue to attract and retain all personnel necessary for the development and operation of its business.

***Environmental Risks***

The oil and natural gas industry is subject to environmental regulation pursuant to a variety of international conventions and Canadian federal, provincial and municipal laws, regulations, and guidelines. A breach of such regulations may result in the imposition of fines or issuances of clean up orders in respect of International Frontier or its assets. Such regulation may be changed to impose higher standards and potentially more costly obligations on International Frontier. There can be no assurance that future environmental costs will not have a material adverse affect on International Frontier.

***Other information***

Additional information regarding International Frontier Corporation's reserves and other data is available on SEDAR at [www.sedar.com](http://www.sedar.com)