International Frontier Resources Corporation

Consolidated Financial Statements

December 31, 2008

Contents

Auditors' Report

To the Shareholders of
International Frontier Resources Corporation

We have audited the consolidated balance sheets of **International Frontier Resources Corporation** as at December 31, 2008 and 2007 and the consolidated statements of operations, comprehensive loss and deficit and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits 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, 2008 and 2007 and the results of its operations and cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

(Signed) "*Deloitte & Touche LLP*"

Calgary, Alberta
April 17, 2009

Chartered Accountants

International Frontier Resources Corporation

Consolidated Balance Sheets

December 31	2008	2007
Assets		
Current		
Cash and cash equivalents (Note 15)	**$ 9,605,300**	$ 25,316,940
Receivables	**154,695**	1,227,990
Prepaids and deposits	**43,815**	162,690
` Current portion of restricted cash on deposit (Note 5)	**1,342,115**	-
	11,145,925	26,707,620
Restricted cash on deposit (Note 5)	**925,060**	2,267,175
Property and equipment (Note 6)	**26,137,890**	17,504,875
Inventory (Note 4)	**16,200**	82,125
Intangibles (Note 7)	**30,000**	35,000
	$ 38,255,075	$ 46,596,795
Liabilities		
Current		
Payables and accruals	**$ 1,257,310**	$ 4,207,115
Convertible debentures (Note 10)	**-**	62,650
Current portion of asset retirement obligations (Note 8)	**-**	30,000
	1,257,310	4,299,765
Asset retirement obligations (Note 8)	**339,615**	306,020
Future income taxes (Note 9)	**2,028,630**	1,141,630
	3,625,555	5,747,415
Shareholders' Equity		
Share capital (Note 11)	**42,064,435**	44,121,725
Warrants (Note 11)	**-**	3,757,090
Contributed surplus (Note 11)	**10,490,030**	6,732,940
Equity component of convertible debentures	**-**	2,350
Deficit	**(17,924,945)**	(13,764,725)
	34,629,520	40,849,380
	$ 38,255,075	$ 46,596,795

Commitments and contingencies (Note 14)

On behalf of the Board

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

See accompanying notes to the interim consolidated financial statements.

International Frontier Resources Corporation

Consolidated Statements of Operations, Comprehensive Loss and Deficit

Years ended December 31,	**2008**	2007
Revenue		
Oil	$ **1,229,080**	$ 787,020
Less: Royalties	**(259,020)**	(179,530)
	970,060	607,490
Interest income	**523,715**	1,154,975
Prospect fee income	**-**	194,755
	1,493,775	1,957,220
Expenses		
Field operating costs	**376,145**	508,025
Depletion, depreciation and impairments (Note 6)	**5,665,455**	4,459,275
Accretion (Note 8)	**29,450**	16,775
Foreign exchange loss	**13,900**	265,165
General and administration	**625,510**	872,790
Bad debt expense (Note 17)	**27,495**	-
Non- recoverable Sidox costs (Note 4)	**55,165**	-
Inventory write down (Note 4)	**61,875**	-
Stock based compensation (Note 11)	**-**	1,851,725
	6,854,995	7,973,755
Loss before income taxes	**(5,361,220)**	(6,016,535)
Future income tax expense (recovery) - (Note 9)	**(1,201,000)**	66,850
Net loss and comprehensive loss	$ **(4,160,220)**	$ (6,083,385)
Deficit, beginning of year	**(13,764,725)**	(7,681,340)
Deficit, end of year	$ **(17,924,945)**	$ (13,764,725)

Net loss per share (Note 12)		
Basic and diluted `	$ **(0.07)**	$ (0.11)

See accompanying notes to the consolidated financial statements.

International Frontier Resources Corporation
Consolidated Statements of Cash Flows

Years ended December 31	2008	2007
Operating		
Net loss	**$ (4,160,220)**	$ (6,083,385)
Non Cash Items:		
Depletion, depreciation and impairments	**5,665,455**	4,459,275
Accretion	**29,450**	16,775
Write down of inventory	**61,875**	-
Stock based compensation	**-**	1,851,725
Future income tax expense	**(1,201,000)**	66,850
Asset retirement liabilities settled	**(25,855)**	(223,145)
	369,705	88,095
Change in non-cash operating working capital (Note 15)	**(210,915)**	340,855
	158,790	428,950
Investing		
Additions to property and equipment	**(14,289,430)**	(9,016,845)
Proceeds from disposition of property and equipment	**-**	4,770
Increase of restricted cash on deposit	**-**	(729,050)
Change in non-cash investing working capital (Note 15)	**(1,546,710)**	1,888,090
	(15,836,140)	(7,853,035)
Financing		
Shares and warrants issued for cash	**-**	22,890,000
Share issue costs (Note 11)	**30,710**	(2,002,515)
Redemption of convertible debenture	**(65,000)**	-
	(34,290)	20,887,485
Net increase (decrease) in cash and cash equivalents	**(15,711,640)**	13,463,400
Cash and cash equivalents (Note 15)		
Beginning of year	**25,316,940**	11,853,540
End of year	**$ 9,605,300**	$ 25,316,940

See accompanying notes to the consolidated financial statements.

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. These financial statements are denoted in Canadian dollars.

The consolidated financial statements include the accounts of the Company, it's 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.
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In 2008, the global credit market crisis, the volatility in the price of oil and natural gas, the recession in Canada and the slowdown of economic growth in the rest of the world has created a substantially more volatile business environment. These conditions will limit certain of the Company's previously planned business development activities and it will continue to represent risk for the Company's future.

2. Summary of 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 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.

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.

2. Summary of significant accounting policies (Continued)

Measurement uncertainty (continued)

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.

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.

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.

At the end of each reporting period, the Company performs an impairment test with respect to the costs of its unproved properties. An impairment loss is recognized in net earnings when the carrying amount of its unproved properties exceeds their fair value assessed based on management's best estimate using the relevant information available at the time.

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.

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 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.

Financial Instruments

All financial instruments are initially recognized at fair value on the balance sheet. The Company has classified each financial instrument into one of the following categories: held-for-trading (assets and liabilities), loans and receivables, financial assets available-for-sale, financial assets held-to-maturity, and other financial liabilities. Subsequent measurement of financial instruments is based on their classification.

Cash and cash equivalents are classified 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. 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.

2. Summary of significant accounting policies (Continued)

Financial Instruments

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.

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.

Inventory

Inventory is comprised of Sidox 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.

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 are 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

2. Summary of significant accounting policies (Continued)

Per share amounts

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 12(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.

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.

The Company's foreign subsidiary is an integrated operation. 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.

Changes in accounting policies

On January 1, 2008, the Company adopted the following new accounting standards:

- CICA Section 1535, "Capital Disclosures", specifies the disclosure of an entity's objectives, policies and processes for managing capital, quantitative data about what the entity regards as capital, whether the entity has complied with any capital requirements, and if it has not complied, the consequences of such non-compliance.
- CICA Sections 3862, "Financial Instruments – Disclosures" and CICA Sections 3863, "Financial Instruments – Presentation", specify standards of presentation and enhanced disclosures on financial instruments. These Sections require the Company to increase disclosure on the nature and extent of risks arising from financial instruments and how the entity manages those risks. (Note 18)

2. Summary of significant accounting policies (Continued)

- CICA Section 3031, "Inventories", provides guidance on the method of determining the cost of the Company's materials and supplies. The new accounting standard specifies that inventories are to be valued at the lower of cost and net realizable value. The standard requires the reversal of previously recorded write downs to realizable value when there is clear evidence that net realizable value has increased. The adoption of Section 3031 "Inventories" did not impact the Company's financial statements.
- The CICA has amended Section 1400, "General Standards of Financial Statement Presentation", which is effective for interim periods beginning on or after January 1, 2008, to include requirements to assess and disclose the Company's ability to continue as a going concern.

New Accounting Pronouncements

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

- 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.
- In January 2009, the AcSB issued Section 1582, Business Combinations, which replaces former guidance on business combinations. Section 1582 establishes principles and requirements of the acquisition method for business combinations and related disclosures. This statement applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after January 2011 with earlier application permitted. The Company does not expect that the adoption of this new Section will have a material impact on its consolidated financial statements.
- In January 2009, the AcSB issued Sections 1601, Consolidated Financial Statements, and 1602, Non-controlling Interests, which replaces existing guidance. Section 1601 establishes standards for the preparation of consolidated financial statements. Section 1602 provides guidance on accounting for a non-controlling interest in a subsidiary in consolidated financial statements subsequent to a business combination. These standards are effective on or after the beginning of the first annual reporting period beginning on or after January 2011 with earlier application permitted. The Company does not expect that the adoption of this new Section will have a material impact on its consolidated financial statements.

3. Capital Management

The Company is in the business of oil and gas exploration in Canada and in the United Kingdom. Management determines the Company's capital structure and makes adjustments to it based on funds available to the Company, in order to support the acquisition, exploration and development of oil and gas properties. The Board of Directors has not established quantitative return on capital criteria for capital management but rather relies upon the expertise of the management team to sustain the future development of the business.

The majority of the properties in which the Company currently has an interest are in the exploration stage and do not generate any revenue. The Company does earn some revenue from properties owned in Alberta. The Company therefore is dependent upon partnerships with industry and external financing to fund the majority of its future exploration programs and its administrative costs. The Company will spend existing working capital and will seek additional financing as needed. The Company will continue to assess new properties and to seek to acquire an interest in additional properties if management feels there is sufficient geologic or economic potential.

Historically, the Corporation has relied on proceeds from the sale of its common shares to fund its operations. In order to accelerate the Corporation's current exploration programs the Corporation may require additional capital. The timing, pace, scope and amount of the Corporation's capital expenditures is largely dependent on the operators' capital expenditure programs and the availability of capital to the Corporation.

The Corporation may obtain funds for future capital investments from strategic alliances with other energy or financial partners, the issuance of additional Common Shares, preferred shares or debt securities, project financing, sale of property interests, or other arrangements, all of which may dilute the interest of the Corporation's existing shareholders. In the current economic environment there can be no assurances that the Company can raise capital through the sale of its shares.

In the management of capital, the Company includes shareholders' equity, cash and cash equivalents and short term portion of restricted cash less accounts payable in the definition of capital. Management reviews its capital requirements on an ongoing basis and believes that its approach, given the relative size of the Company is reasonable. As at December 31, 2008, the Company's capital as defined above was approximately $44,319,000 (2007 - $61,959,000).

4. Investment in Sidox Chemicals Canada Ltd. ("Sidox Canada")

The investment in Sidox Canada is subject to joint control and accordingly has been proportionately consolidated in these financial statements at December 31, 2008.

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

		2008		2007
Assets				
Cash	$	**8,045**	$	49,990
Receivables		**15,660**		12,265
Inventory		**16,200**		82,125
Intangibles		**30,000**		35,000
		69,905		179,380
Liabilities				
Payables		**135**		87,730
Net assets	$	**69,770**	$	91,650
Revenues	$	**-**	$	-
Expenditures		**71,880**		15,275
Net Loss	$	**71,880**	$	15,275

During 2008, the Company wrote off $55,165 of non recoverable costs, which represent its proportionate share of amounts owed to the Company by Sidox Canada at December 31, 2008 that were not collectible.

At December 31, 2008 Sidox chemical inventory was written down by $123,750 to its net realizable value of $32,400. The Company's proportionate share of this write down of $61,875 has been recorded as an expense resulting in a net realizable value of $16,200 at December 31, 2008.

5. Restricted cash on deposit

As at December 31, 2008, the Company has provided an assignment of cash totaling $2,267,175 (2007 - $2,267,175) as security on the irrevocable standby letters of credit for the Northwest Territories Exploration Licenses (see Note 14a) as follows:

		2008		2007
EL – 423	$	**509,180**	$	509,180
EL – 429		**781,250**		781,250
EL – 432		**250,000**		250,000
EL – 441		**352,440**		352,440
EL – 445		**68,750**		68,750
EL – 443		**305,555**		305,555
		2,267,175		2,267,175
Current portion		**(1,342,115)**		-
	$	**925,060**	$	2,267,175

6. Property and equipment

December 31, 2008	Cost	Accumulated Depletion, Depreciation and Impairments	Net Book Value
Petroleum and natural gas properties	$ 39,210,260	$ 13,090,385	$ 26,119,875
Office furniture and equipment	84,980	66,965	18,015
Petroleum and natural gas properties	$ 39,295,240	$ 13,157,350	$ 26,137,890

December 31, 2007	Cost	Accumulated Depletion, Depreciation and Impairments	Net Book Value
Petroleum and natural gas properties	$ 24,919,340	$ 7,434,515	$ 17,484,825
Office furniture and equipment	82,480	62,430	20,050
Petroleum and natural gas properties	$ 25,001,820	$ 7,496,945	$ 17,504,875

Canada

During 2008, $58,300 (2007 - $411,450) of overhead expenses directly related to exploration activities in the Northwest Territories were capitalized. Of these amounts, $3,600 (2007 - $6,175) related to interest expense was capitalized for activities in the Northwest Territories. Also included in the above amounts are $Nil (2007 - $294,800) of stock option costs recognized in the period that were capitalized to undeveloped properties in the Northwest Territories.

As at December 31, 2008, the Company has accumulated capital expenditures for land, seismic, and drilling in the Northwest Territories of $28,203,005 (2007 - $18,524,665). Included in this amount are costs of $19,431,260 (2007 - $13,805,330) which have been included in petroleum and natural gas properties as undeveloped properties and have not been included in the respective cost centers for purposes of calculating depletion. During 2008, the Company transferred $4,052,480 of impaired costs incurred in the Northwest Territories from the unproved properties to the full cost pool.

In 2008, $3,796,330 (2007 - $Nil) impairment of petroleum and natural gas assets in the Northwest Territories has been recorded as part of depletion to reflect the excess carrying amount of assets over fair value of future reserves in Canada. An evaluation of undeveloped properties in the Northwest Territories was performed and no impairment exists at December 31, 2008.

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

	2009	2010	2011	2012	2013	2014	Increase Thereafter
Sask Cromer Medium Crude Oil ($C/Bbl)	$56.80	$67.35	$74.10	$76.00	$78.05	$79.60	2.0%

6. Property and equipment (continued)

North Sea

During 2008, $58,300 (2007 - $614,150) of overhead expenses directly related to exploration activities in the North Sea were capitalized. Included in the above amounts are, $Nil (2007 - $111,835) of stock option costs recognized in the period that were capitalized to undeveloped properties in the North Sea.

As at December 31, 2008, the Company has accumulated capital expenditures for land, seismic, and drilling in the North Sea of $11,007,255 (2007 - $6,394,675). Included in this amount are costs of $5,291,020 (2007 - $2,113,000) which have been included in petroleum and natural gas properties as undeveloped properties.

In 2008, the Company recognized an impairment expense of $1,435,375 (2007 - $4,280,860) for dry hole costs and G&A expenses incurred in the North Sea. As at December 31, 2008, no additional impairment was identified with respect to the unproved properties

7. Intangible assets

December 31, 2008	**Cost**	**Accumulated Depreciation**	**Net Book Value**
Sidox license	**$ 50,000**	**$ 20,000**	**$ 30,000**

December 31, 2007	Cost	Accumulated Amortization	Net Book Value
Sidox license	$ 50,000	$ 15,000	$ 35,000

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 before inflation required to settle its asset retirement obligations is approximately $832,500 (2007 - $832,500). 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:

	2008	2007
Balance, beginning of year	**$ 336,020**	$ 239,045
Change in estimate	**-**	303,345
Liabilities settled	**(25,855)**	(223,145)
Accretion expense	**29,450**	16,775
Balance, end of year	**$ 339,615**	$ 336,020

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 29.50% (2007-30.12%) to loss before income taxes in Canada and tax rate of approximately 30% (2007 – 30%) in the U.K.. This difference results from the following items:

December 31, 2008

	Canada	U.K.	Total
Loss before income taxes	$ (3,923,875)	$ (1,437,345)	$ (5,361,220)
Expected tax recovery of combined federal and provincial statutory rates	(1,157,545)	(424,020)	(1,581,565)
Increase (decrease) resulting from:			
Statutory rate change	(63,600)	64,680	1,080
Other	20,145	495	20,640
Change in valuation allowance	-	358,845	358,845
Future income tax recovery	$ (1,201,000)	$ -	$ (1,201,000)

December 31, 2007

	Canada	U.K.	Total
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
Future income tax expense	$ 66,850	$ -	$ 66,850

b) Future income taxes consist of the following temporary differences and other items

December 31, 2008

	Canada	U.K.	Total
Excess of carry value of property and equipment over tax values	$ (3,003,535)	$ 1,429,060	$ (1,574,475)
Asset retirement obligations	84,905	-	84,905
Share issue costs	311,140	-	311,140
Non-capital loss carry-forwards	578,860	32,510	611,370
	(2,028,630)	1,461,570	(567,060)
Valuation allowance	-	(1,461,570)	(1,461,570)
Future income tax liability	$ (2,028,630)	$ -	$ (2,028,630)

9. Income taxes (continued)

December 31, 2007

	Canada	U.K.	Total
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)
Future income tax liability	$ (1,141,630)	$ -	$ (1,141,630)

c) Tax losses

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The Company has incurred losses for income tax purposes of approximately $2,860,000 (2007 - $2,433,880) in Canada and $132,000 (2007 - $130,000) in the United Kingdom. The related benefit of these losses in Canada has been recognized in the consolidated financial statements to reduce future income taxes. Unless sufficient taxable income is earned these losses will expire as follows:

	Canada	U.K.	Total
2009	90,000	-	90,000
2010	66,000	-	66,000
2011	265,000	-	265,000
2012	508,000	-	508,000
2013	593,000	-	593,000
2026	268,000	27,000	295,000
2027	634,000	103,000	737,000
2028	436,000	2,000	438,000
	$ 2,860,000	$ 132,000	$ 2,992,000

10. Convertible debentures

At December 31, 2008, the Company has $Nil (2007 - $65,000) of convertible debentures remaining. The debentures paid interest at a rate of 9.5% per year and were convertible into common shares at $0.70 per share to June 2007 and $0.75 per share to their scheduled expiry date of April 2008. There were no debentures converted during the years ended December 31, 2008 and 2007. On April 30, 2008 the debentures outstanding in the amount of $65,000 were repaid.

11. Share capital

a) Authorized:

Unlimited common shares
Unlimited preferred shares

b) Issued:

	December 31, 2008		December 31, 2007	
	Number of Shares	Amount	Number of Shares	Amount
Common shares				
Beginning of period	**59,578,965**	**$ 44,121,725**	42,041,465	$ 26,410,600
Issued for cash (i)	**-**	**-**	12,400,000	15,500,000
Issued for services (ii)	**-**	-	100,000	125,000
Value attributed to warrants	-	**-**	-	(3,757,090)
Flow-through shares (iii, iv)	-	-	5,037,500	7,390,000
Tax effect of flow through shares (iii), (iv)	**-**	**(2,088,000)**	-	-
Share issue costs (v)	**-**	**30,710**	-	(1,546,785)
Balance, end of year	**59,578,965**	**$ 42,064,435**	59,578,965	$ 44,121,725

(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.

(v) During 2008, the Company received a refund of $30,710 on share issue costs paid in 2007 with respect to non-brokered placement per (iv) above.

11. Share capital (continued)

c) Flow-through share obligation information:

	December 31, 2008	December 31, 2007
Balance, beginning of year	**$ 3,498,025**	$ -
Flow-through share proceeds	**-**	7,390,000
Expenditures incurred	**(3,498,025)**	(3,891,975)
Balance, end of year	**$ -**	$ 3,498,025

d) Stock options

The Company has a stock option plan available to consultants, officers, directors, and employees of the Company to be granted options of up to 10 percent of the issued and outstanding common shares of the Corporation. 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, 2008, 1,015,000 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	**December 31, 2008**		December 31, 2007	
	Number of Options	**Weighted Average Exercise Price**	Number of Options	Weighted Average Exercise Price
Balance, beginning of period	**5,855,000**	**$ 1.23**	3,355,000	$ 1.42
Granted	**-**	**$ -**	2,500,000	$ 0.97
Cancelled	**(4,840,000)**	**$ 1.31**	-	$ -
Exercised	**-**	**$ -**	-	$ -
Balance, end of year	**1,015,000**	**$ 1.16**	5,855,000	$ 1.23

December 31, 2008

	Options Outstanding			Options Exercisable	
Exercise Price	Options Outstanding	Weighted Average Contractual Life (years)	Weighted Average Exercise Price	Options Exercisable	Weighted Average Exercisable Price
$0.25 - $0.82	515,000	2.42	$ 0.71	515,000	$ 0.71
$1.35 - $1.95	500,000	1.36	$ 1.62	500,000	$ 1.62
	1,015,000	1.90	$ 1.16	1,015,000	$ 1.16

11. Share capital (continued)

d) Stock options (continued)

December 31, 2007

	Options Outstanding			Options Exercisable	
Exercise Price	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	2,725,000	2.28	$ 1.64	2,725,000	$ 1.64
	5,855,000	3.03	$ 1.23	5,855,000	$ 1.23

There were no options granted in 2008. The weighted average fair market value of options granted in 2007 was $0.92 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:

	December 31, 2007
Risk-free interest rate	4.37%
Expected life of options	5 years
Volatility	163%- 170.00%
Dividend yield rate	0%

e) Warrants:

	December 31, 2008		December 31, 2007	
	Number of Warrants	**Amount**	Number of Warrants	Amount
Balance, beginning of year	**7,504,000**	**$ 3,757,090**	-	$ -
Issued (i), (ii)	**-**	**-**	7,504,000	3,757,090
Expired	**(7,504,000)**	**(3,757,090)**	-	-
Balance, end of year	**-**	**$ -**	7,504,000	$ 3,757,090

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 was comprised of one common share and one-half warrant. One full warrant entitled 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. The warrants expired unexercised on May 22, 2008.

(ii) Concurrently with the issuance of the units, the Company issued 1,204,000 underwriter warrants which entitled 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 consisted of one common share and one warrant. One warrant entitled 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 2007 was $ 0.50. 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:

	December 31, 2007
Risk-free interest rate	4.11%
Expected life of warrants	1 year
Volatility	82%
Dividend yield rate	0%

f) Contributed surplus:

	December 31, 2008	December 31, 2007
Balance, beginning of year	**$ 6,732,940**	$ 4,474,570
Value attributed to stock options granted	**-**	2,258,370
Fair value of expired warrants	**3,757,090**	-
Balance, end of year	**$10,490,030**	$ 6,732,940

At December 31, 2008, $Nil (2007 – $406,640) of the value attributed to stock options granted in the year were capitalized to petroleum and natural gas properties.

12. Per share

	2008	2007
Net loss	**$ (4,160,220)**	$ (6,083,385)
Weighted average number of shares	**59,578,565**	56,889,170
Basic and diluted loss per share	**$ (0.07)**	$ (0.11)

13. Related party transactions

a) During 2008, the Company paid compensation to certain officers and directors as follows:

	2008	2007
Executive officers compensation	**$ 108,000**	$ 17,000
Director's fees	**14,500**	30,000
Royalty incentive program	**16,745**	10,510
	$ 139,245	$ 57,510

At December 31, 2008, $16,745 (December 31, 2007 – $10,510) of the above amounts were included in payables and accruals.

b) During 2008, $6,310 (2007 - $30,725) was paid to a law firm in which a Director of the Company is a partner. Of this amount, $675 (2007 - $Nil) is included in payables and accruals at December 31, 2008. These costs are included in general and administrative expenses on the consolidated statements of operations and deficit.

c) During 2008, two of the directors of the Company were also directors of Sidox Chemicals Canada Ltd. Details of transactions with Sidox Chemicals Canada Ltd during 2008 are disclosed in Note 4.

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.

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 (2007 – $2,267,175). The Company is contingently liable under the letters of credit for $2,267,175 (2007 - $2,267,175). The deposits will be refunded by $1 for every $4 spent on qualified expenditures on each exploration license. At December 31, 2008 the Company has met a certain portion of its work commitments on the exploration licenses which entitle it to a refund of qualified expenditures upon approval by the National Energy Board and Department of Indian Affairs. Subsequent to December 31, 2008, the Company received a refund of $746,860. In addition, a refund of $595,255 was approved on April 9, 2009. As a result the Company's letters of credit and restricted cash on deposit will be reduced to $925,060.

14. Commitments and contingencies (continued)

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 is as follows:

2009	$	53,000
2010	$	53,000
2011	$	53,000

c) The Company has established a Royalty Incentive Agreement for officers who are also Directors and consultants. Under the plan, the compensation committee issues units and pays royalties 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 gross oil and gas production revenue, net of transportation and processing fees from licenses and lands owned by the Company. Under the terms of the agreement, once the Company has recovered payout of 100% of its cumulative annual capital expenditures from licenses and lands owned by the Company, the payment to employees, consultants and directors is based on 4% of the Company's annual production revenue less transportation and processing fees. At December 31, 2008, payout of 100% of cumulative annual capital expenditures had not been reached. At December 31, 2008, the Company recorded costs of $23,920 (2007 - $15,010) with respect to this plan.

d) In 2008, the Company signed a long-lead AFE with respect to future costs to be incurred on License P.1465 in the Bowmore area of the North Sea. The Company is committed to expenditures of $1,230,000 to be incurred in the first two quarters of 2009.

15. Supplemental cash flow information

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

	2008	2007
Receivables	**$ 1,073,305**	$ (771,800)
Prepaids and deposits	**118,875**	(131,100)
Payables and accruals	**(2,949,805)**	3,131,845
	$ (1,757,625)	$ 2,228,945
Operating activities	**$ (210,915)**	$ 340,855
Investing activities	**(1,546,710)**	1,888,090
Financing activities	**-**	-
	$ (1,757,625)	$ 2,228,945
Interest paid	**$ 3,600**	$ 6,175
Cash and cash equivalents are comprised of:		
Cash	**$ 671,850**	$ 3,242,150
Short term bankers' acceptances (bearing interest rates ranging from 1.30% - 1.34% (2007: 4.33% - 4.58%)	**8,933,450**	22,074,790
	$ 9,605,300	$ 25,316,940

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)

December 31, 2008	Canada	U.K.	Total
Oil revenues, net	$ 1,229,080	$ -	$ 1,229,080
Less: royalties	(259,020)	-	(259,020)
	970,060	-	970,060
Interest income	460,895	62,820	523,715
	1,430,955	62,820	1,493,775
Expenses			
Field operating costs	376,145	-	376,145
Depletion, depreciation and impairments	4,230,080	1,435,375	5,665,455
Accretion	29,450	-	29,450
Foreign exchange (gain) loss	(21,345)	35,245	13,900
General and administration	621,595	3,915	625,510
Bad debt expenses	1,865	25,630	27,495
Non- recoverable Sidox costs	55,165	-	55,165
Write down of inventory	61,875	-	61,875
	5,354,830	1,500,165	6,854,995
Loss before income taxes	(3,923,875)	(1,437,345)	(5,361,220)
Future income tax recovery	(1,201,000)	-	(1,201,000)
Net loss	$ (2,722,875)	$ (1,437,345)	$ (4,160,220)

December 31, 2007	Canada	U.K.	Total
Oil revenues, net	$ 787,020	$ -	$ 787,020
Less: royalties	(179,530)	-	(179,530)
	607,490	-	607,490
Interest income	1,120,040	34,935	1,154,975
Prospect fee income	194,755	-	194,755
	1,922,285	34,935	1,957,220
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 loss	132,555	132,610	265,165
General and administration	866,300	6,490	872,790
Stock based compensation	1,851,725	-	1,851,725
	3,553,795	4,419,960	7,973,755
Loss before income taxes	(1,631,510)	(4,385,025)	(6,016,535)
Future income tax expense	66,850	-	66,850
Net loss	$ (1,698,360)	$ (4,385,025)	$ (6,083,385)

16. Segmented information (continued)

b) Property and equipment

December 31, 2008	**Canada**	**U.K.**	**Total**
Capital expenditures	$ 9,676,580	$ 4,612,850	$ 14,289,430
Property and equipment, net book value	$ 20,846,600	$ 5,291,290	$ 26,137,890

December 31, 2007	**Canada**	**U.K.**	**Total**
Capital expenditures			
Cash expenditures	$ 3,834, 760	$ 5,177,305	$ 9,012,065
Asset retirement provision	303,345	-	303,345
Stock options costs	294,800	111,835	406,635
	$ 4,432,905	$ 5,289,140	$ 9,722,045
Property and equipment, net book value	$ 15,391,060	$ 2,113,815	$ 17,504,875

17. Financial Instruments

The Company is exposed to financial risk in a range of financial instruments including cash and cash equivalents, trade accounts receivable, and trade accounts payable. The Company manages its exposure to financial risks by operating in a manner that minimizes its exposure to the extent practical. The main financial risks affecting the Company are discussed below:

a) Credit risk

Credit risk arises when a failure by counter parties to discharge their obligations could reduce the amount of future cash inflows from financial assets on hand at the balance sheet date. A portion of the Company's financial assets at the balance sheet date arise from crude oil sales. Industry standard dictates that commodity sales are settled on the 25th day of the month following the month of production.

At December 31, 2008, substantially all of the accounts receivable are with customers and joint venture partners in the oil and gas industry and are subject to normal industry credit risks. The Company markets its oil through one marketer the increased risk arising from exposure to one entity is mitigated by the fact that oil production is not a significant part of the Company's business at this time as the Company is engaged primarily in the exploration for and development of petroleum and natural gas reserves.

The maximum exposure to loss arising from accounts receivable at any given time is equal to their total carrying amounts on the balance sheet. During 2008, the Company wrote off $25,860 (2007 - $nil) in uncollectible amounts in its U.K. subsidiary and $1,635 in Canada.

17. Financial Instruments (continued)

The following table presents the aging the Company's accounts receivable at December 31, 2008:

Total receivables:	0 to 30 days	31 to 60 days	61 to 90 days	Greater than 90 days
$ 154,695	$ 138,060	$ -	$ -	$ 16,635

The maximum exposure to credit risk is represented by the carrying amount on the balance sheet of all the financial assets. There are no material financial assets that are past due. During the 2008, there was no allowance for doubtful accounts recorded as all amounts outstanding at December 31, 2008 are deemed collectible.

b) 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 some cash and cash equivalents on hand that are denominated in British pounds and is exposed to foreign currency fluctuations on its operations in the United Kingdom as these are denominated in British pounds. The Company's management monitors the exchange rate fluctuations on a regular basis. The Company does not use currency derivative instruments to manage the Company's exposure to foreign currency fluctuations.

At December 31, 2008, the carrying amount of the Company's U.K. pound denominated net monetary assets was approximately C$563,000. Assuming all other variables remain constant, a fluctuation of one cent in the exchange rate of the Canadian dollar to the British pound would not result in a material change in income.

c) Interest Rate Risk

Interest rate risk refers to the risk that the value of a financial instrument or cash flows associated with the instrument will fluctuate due to changes in market interest rates. 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 with respect to funds invested in short term marketable securities. As a December 31, 2008, the Company did not have any financial assets based on variable interest rates and as such the Company has no specific interest rate risk at year end. The Company does not use interest rate hedges or fixed interest rate contracts to manage the Company's exposure to interest rate fluctuations.

d) Liquidity Risk

Liquidity risk includes the risk that:

- The Company will not have sufficient funds to settle a transaction on the due date;
- The Company will be forced to sell financial assets at a value which is less than what they are worth; or
- The Company may be unable to settle or recover a financial asset at all.

17. Financial Instruments (continued)

The Company's operating cash requirements including, amounts projected to complete budgeted capital expenditures are continuously monitored and adjusted as input variables change. These variables include, but are not limited to, opening cash and cash equivalents balance, available bank lines, oil and natural gas production from existing wells, results from new wells drilled, commodity prices, cost overruns on capital projects and changes to government regulations relating to prices, taxes, royalties, land tenure, allowable production and access to equity markets. As these variables change, liquidity risks may necessitate the need for the Company to conduct equity issues or obtain project debt financing.

At December 31, 2008 the Company had cash and cash equivalents of $9,605,300 (2007 - $25,316,940), and working capital was $9,888,615 (2007 - $22,407,855). The Company has sufficient working capital to fund its share of its 2009 – 2010 budgeted firm and contingent capital expenditures from existing working capital.