CANADIAN SPIRIT RESOURCES INC.

Financial Statements of

Canadian Spirit Resources Inc.

December 31, 2010

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Canadian Spirit Resources Inc.

REPORT OF MANAGEMENT

April 21, 2011

The accompanying financial statements of Canadian Spirit Resources Inc., for each of the years ended December 31, 2010 and 2009, are the responsibility of management.

Management has prepared the financial statements in accordance with accounting principles generally accepted in Canada. If alternative accounting methods exist, management has chosen those it deems most appropriate in the circumstances. Financial statements are not precise since they include certain amounts based on estimates and judgments. Management has ensured that the financial statements are presented fairly in all material respects.

Canadian Spirit Resources Inc. maintains internal accounting and administrative controls designed to provide reasonable assurance that the financial information is relevant, reliable and accurate and that assets are appropriately accounted for and adequately safeguarded.

The Board of Directors is responsible for reviewing and approving the financial statements and Management Discussion and Analysis and, primarily through its Audit Committee, ensures that management fulfills its responsibilities for financial reporting.

The Audit Committee is appointed by the Board of Directors and is entirely composed of directors who are independent of the Corporation. The Audit Committee meets regularly with management, and periodically with the external auditors, to discuss internal controls and reporting issues and to satisfy itself that each party is properly discharging its responsibilities. It reviews the financial statements and the external auditor's report. The Audit Committee also considers, for review by the Board of Directors and approval by the shareholders, the engagement or reappointment of the external auditors.

PricewaterhouseCoopers LLP, the external auditors, have audited the financial statements, for each of the years ended December 31, 2010 and 2009, in accordance with auditing standards generally accepted in Canada on behalf of the shareholders. PricewaterhouseCoopers LLP have full and free access to the Audit Committee.

(signed) "Donald R. Gardner"

Donald R. Gardner,
Chief Executive Officer

(signed) "Dean G. Hill"

Dean G. Hill,
Chief Financial Officer

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April 21, 2011

Independent Auditor's Report

To the Shareholders of Canadian Spirit Resources Inc.

We have audited the accompanying financial statements of Canadian Spirit Resources Inc., which comprise the balance sheets as at December 31, 2010 and 2009 and the statements of operations, comprehensive loss and deficit, and cash flows for the years then ended, and the related notes including a summary of significant accounting policies.

Management's responsibility for the financial statements
Management is responsible for the preparation and fair presentation of these financial statements in accordance with Canadian generally accepted accounting principles, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's responsibility
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 comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained in our audits is sufficient and appropriate to provide a basis for our audit opinion.

Opinion
In our opinion, the financial statements present fairly, in all material respects, the financial position of Canadian Spirit Resources Inc. as at December 31, 2010 and 2009 and the results of their operations and their cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

PricewaterhouseCoopers LLP

Chartered Accountants

Canadian Spirit Resources Inc.

BALANCE SHEETS

As at December 31	2010	2009
ASSETS		
Current assets:		
Cash and cash equivalents	$ 33,941,607	$ 9,647,890
Accounts receivable	262,515	203,995
Prepaid expenses and other	81,586	51,290
	34,285,708	9,903,175
Long term assets:		
Property, plant and equipment (note 3)	55,078,821	35,251,948
	$ 89,364,529	$ 45,155,123
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable and accrued trade liabilities	$ 13,284,179	$ 418,095
Long term liabilities:		
Asset retirement obligation (note 4)	445,066	288,095
Shareholders' equity:		
Common shares (note 5)	90,792,004	56,775,426
Share purchase warrants (note 5)	-	1,940,927
Contributed surplus (note 5)	6,179,344	5,865,418
Deficit	(21,336,064)	(20,132,838)
	75,635,284	44,448,933
	$ 89,364,529	$ 45,155,123

Nature of operations and basis of presentation (note 1)
Commitments (note 7)

ON BEHALF OF THE BOARD:

(signed) "Philip H. Grubbe"
Director

(signed) "J.R. Richard Couillard"
Director

Canadian Spirit Resources Inc.

STATEMENTS OF OPERATIONS, COMPREHENSIVE LOSS AND DEFICIT

For the year ended December 31	2010	2009
Revenue		
Interest and other income	$ 92,509	$ 45,809
Expenses		
Consulting fees	82,850	120,917
Salaries and benefits	782,621	845,056
Other general administration	805,339	674,262
Stock-based compensation (note 5)	554,015	372,160
Accretion (note 4)	39,465	23,651
Depreciation and amortization	25,266	25,261
	2,289,556	2,061,307
Loss before income taxes	(2,197,047)	(2,015,498)
Recovery of future taxes (note 6)	993,821	-
Net loss and comprehensive loss	(1,203,226)	(2,015,498)
Deficit, beginning of year	(20,132,838)	(18,117,340)
Deficit, end of year	$ (21,336,064)	$ (20,132,838)
Net loss and comprehensive loss per share (basic & diluted)	$ (0.02)	$ (0.04)

Nature of operations and basis of presentation (note 1)

Canadian Spirit Resources Inc.

STATEMENTS OF CASH FLOWS

For the year ended December 31	2010	2009
Operating Activities:		
Net loss and comprehensive loss	$ (1,203,226)	$ (2,015,498)
Add (deduct) items not affecting cash:		
Depreciation and amortization	25,266	25,261
Accretion (note 4)	39,465	23,651
Recovery of future taxes (note 6)	(993,821)	-
Stock-based compensation (note 5)	554,015	372,160
	(1,578,301)	(1,594,426)
Changes in non-cash working capital items	(26,097)	232,143
	(1,604,398)	(1,362,283)
Financing Activities:		
Common shares issued for cash (note 5)	36,512,624	558,900
Common shares re-purchased and cancelled (note 5)	(1,865,297)	(641,835)
Share issue costs (note 5)	(2,028,168)	(15,699)
	32,619,159	(98,634)
Investing Activities:		
Computer and office equipment, furniture and fixtures	(7,486)	(9,244)
Expenditure of exploration and development costs	(15,247,048)	(441,323)
Acquisition and retention of natural gas rights	(4,269,875)	(88,981)
	(19,524,409)	(539,548)
Changes in non-cash working capital items	12,803,365	430,593
	(6,721,044)	(108,955)
Change in cash and cash equivalents	24,293,717	(1,569,872)
Cash and cash equivalents, beginning of year	9,647,890	11,217,762
Cash and cash equivalents, end of year	$ 33,941,607	$ 9,647,890
Income taxes paid	$ -	$ -
Interest paid	$ -	$ -

See the accompanying notes to the financial statements

1. NATURE OF OPERATIONS AND BASIS OF PRESENTATION

Canadian Spirit Resources Inc. ("CSRI" or the "Corporation") is incorporated in the province of British Columbia and is a public company listed on the TSX Venture Exchange (the "Exchange").

CSRI's principal business activity is the acquisition, exploration, development and production of petroleum and natural gas resources. Since May 2002, the Corporation has been evaluating the resource potential of certain unconventional natural gas properties in northeastern British Columbia.

These financial statements have been prepared in accordance with Canadian generally accepted accounting principles. All amounts presented in these financial statements, and the notes thereto, are expressed in Canadian dollars unless otherwise indicated.

2. SIGNIFICANT ACCOUNTING POLICIES

Use of Estimates

The preparation of financial statements in conformity with Canadian generally accepted accounting principles ("GAAP") requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. The amounts recorded for amortization, asset retirement obligation, impairment of unproved properties, stock-based compensation and future taxes are based upon estimates. Actual results could differ from those estimates.

Joint Interests

Exploration, development and production activities are conducted jointly with external parties and, accordingly, the Corporation only reflects its proportionate interest in such activities.

Cash and Cash Equivalents

Cash and cash equivalents include investments with an original maturity of three months or less.

Financial Instruments and Derivatives

(a) Classification:

GAAP requires that all financial instruments be classified either as held-for-trading financial assets or liabilities, available-for-sale financial assets, held-to-maturity financial assets, loans and receivables or other financial liabilities.

The Corporation has classified each of its financial instruments as a) cash and cash equivalents as held-for-trading financial assets; b) accounts receivable as loans and receivables; and c) accounts payable and accrued trade liabilities as other financial liabilities.

The Corporation does not have any other financial assets or financial liabilities, nor does it have any embedded derivative financial instruments or contracts.

(b) Recognition and Measurement:
GAAP requires that all financial instruments including derivatives and most embedded derivatives be measured initially at fair value and then subsequently at amortized cost, with the exception of loans and receivables, debt securities classified as held-to-maturity financial assets, and other financial liabilities which may be measured at amortized cost from inception.

Financial assets and liabilities classified as held-for-trading are measured at fair value with changes in fair value recognized against earnings. The Corporation uses the trade-date method of accounting to record all purchases or sales of financial assets.

The Corporation does not have any financial instruments designated as hedges and therefore does not present a separate statement of other comprehensive income.

Property, Plant and Equipment

(a) Natural Gas Interests:
The Corporation follows the full cost method of accounting for exploration and development expenditures whereby all costs relating to the acquisition of, exploration for and development of natural gas reserves including net operating costs (after offsetting revenues) before planned principal operations have commenced, are capitalized. Such costs include lease acquisitions, geological and geophysical expenses, lease rentals on undeveloped properties, drilling both productive and non-productive wells, production equipment, and overhead charges directly related to acquisition, exploration and development activities. Proceeds received from disposals of properties and equipment are credited against capitalized costs unless the disposal would alter the rate of depletion and amortization by more than 20%, in which case a gain or loss on disposal is recorded.

Upon commencement of commercial production all costs of acquisition, exploration and development of natural gas reserves, associated tangible plant and equipment costs, asset retirement obligations and estimated costs of future development of proved undeveloped reserves are depleted and/or amortized by the unit of production method based on estimated gross proved reserves before royalties as determined by independent evaluators. Whenever necessary or appropriate, natural gas reserves are converted to equivalent oil units using their relative energy content of six thousand cubic feet of natural gas to one barrel of oil.

The costs of acquiring and evaluating unproved properties are excluded from costs subject to depletion calculations. These properties are assessed annually or when there are indicators of impairment to ascertain whether impairment has occurred. When proved reserves are assigned or the property is considered to be impaired, the cost of the property or the amount of the impairment is added to the costs subject to depletion.

Natural gas assets are evaluated annually or when events or conditions dictate to determine that the costs are recoverable and do not exceed the fair value of the properties. The costs are assessed to be recoverable if the sum of the undiscounted cash flows expected from the production of proved reserves plus the lower of cost and market of unproved properties exceed the carrying value of the petroleum and natural gas assets. If the carrying value of the petroleum and natural gas assets is not assessed to be recoverable, an impairment loss is recognized to the extent that the carrying value exceeds the sum of the discounted cash flows expected from the production of proved and probable reserves and the lower of cost and market of unproved properties. The cash flows are estimated using future product prices and costs and are discounted using the risk-free interest rate.

(b) Mineral Property:
Expenditures incurred on properties identified as having development potential are recorded at cost and are deferred on a project basis until the viability of the project is determined. If a project is successful, the project costs are amortized using the unit of production method based on recoverable mineral reserves. If a project is abandoned or it is determined that the mineral property is uneconomic to produce, the accumulated project costs are charged to earnings in the period in which the determination is made.

(c) Office Equipment:
Computer and office equipment are recorded at cost and amortized on a straight line basis over their estimated useful life of three years. Furniture and fixtures are recorded at cost and amortized on a straight line basis over their estimated useful life of five years.

Asset Retirement Obligation

The Corporation follows the accounting methodology outlined in Section 3110 of the Canadian Institute of Chartered Accountants ("CICA") Handbook with respect to asset retirement obligations. The Corporation records the present value of legal obligations associated with the retirement of long-lived tangible assets, such as producing well sites and natural gas processing plants, in the period in which they are incurred with a corresponding increase in the carrying amount of the related long-lived asset. The liability accretes until the Corporation settles the retirement obligation. The carrying amounts of the long-lived assets are depleted using the unit of production method unless related to unproved properties. Actual costs to retire tangible assets are deducted from the liability as incurred.

Revenue Recognition

Revenues from the sale of natural gas and other hydrocarbons are recorded when title passes to an external party and when collectability is reasonably assured.

Stock-based Compensation

(a) Stock Options:
Stock options are accounted for based on the fair value method. The fair value is measured at the grant date and charged to earnings or capitalized over the vesting period with a corresponding increase to contributed surplus. Consideration paid to the Corporation on exercise of all options is credited to share capital.

(b) Performance Units:
Compensation costs attributable to performance units are recognized as a charge to stock-based compensation expense when the likelihood of payout based on inherent performance factors is determined to be probable.

Comprehensive Income
Comprehensive Income is defined as the change in equity from transactions and other events from non-owner sources and other comprehensive income comprises revenues, expenses, gains and losses that, in accordance with GAAP, are recognized in comprehensive income but excluded from net earnings or loss.

Earnings per Share
Basic earnings per common share are calculated on net earnings using the weighted average number of shares outstanding during the fiscal period. Diluted earnings per share information is calculated using the treasury stock method which assumes that proceeds obtained upon exercise of options and warrants would be used to purchase common shares at the average market price for the period. No adjustment to diluted earnings per share is made if the result of this calculation is anti-dilutive.

Flow-Through Shares
The Corporation has from time to time financed a portion of its exploration and development activities through the issue of Flow-Through Shares. Under the terms of these share issues, the related resource expenditure deductions for income tax purposes are renounced to investors. Accordingly, when the expenditures are renounced and upon filing of documents with the taxation authorities, share capital is reduced and a recovery of future income taxes is recorded by the estimated value of the renounced tax deductions.

Income Taxes
The Corporation follows the asset and liability method of accounting for income taxes. Under this method, future tax liabilities and assets are recognized for the estimated tax consequences attributable to differences between the amounts reported in the financial statements and their respective tax bases, using enacted or substantively enacted income tax rates. The effect of a change in tax rates on future tax liabilities and assets is recognized in income in the period the change occurs. A valuation allowance is recorded against any future income tax asset if it is more likely than not that such asset will not be realized.

Changes in Accounting Policies and Practices
The following new accounting pronouncements have been adopted with effect from January 1, 2010:

CICA Handbook: Section 1582, *Business Combinations*

Section 1582, which replaces the previous business combinations standard, requires assets and liabilities acquired in a business combination, contingent consideration and certain acquired contingencies to be measured at their fair values as of the date of acquisition. In addition, acquisition-related and restructuring costs are to be recognized separately from the business combination and included in the statement of operations, comprehensive loss and deficit. The adoption of this standard has had no material impact on the Corporation's December 31, 2010 annual financial statements.

CICA Handbook: Section 1601, *Consolidated Financial Statements and*
Section 1602, *Non-controlling Interests*

Sections 1601 and 1602, which together replace the previous consolidated financial statements standard, establish the requirements for the preparation of consolidated financial statements and the accounting for a non-controlling interest in a subsidiary in consolidated financial statements subsequent to a business combination. Section 1602 requires that a non-controlling interest in a subsidiary be classified as a separate component of equity, and that net income or loss as well as components of other comprehensive income are attributed to both the parent and the non-controlling interest. The adoption of this standard has had no material impact on the Corporation's December 31, 2010 annual financial statements.

3. PROPERTY, PLANT AND EQUIPMENT

	2010	2009
Unproved natural gas properties	$ 56,231,872	$ 36,387,219
Mineral property	1	1
Computer and office equipment, furniture and fixtures	242,002	234,516
	56,473,875	36,621,736
Accumulated depreciation, amortization and impairment	(1,395,054)	(1,369,788)
Total property, plant and equipment	$ 55,078,821	$ 35,251,948

During the year ended December 31, 2010, the Corporation capitalized $468,998 (2009: $435,887) of overhead directly related to exploration and development activities. During the year ended December 31, 2010, the Corporation also capitalized $210,224 (2009: $Nil) of stock-based compensation expense for those employees of the Corporation directly involved in exploration and development activities.

The Corporation's Gething project produced nominal volumes of sales gas from June 2009 until July 2010. Under the terms of a joint venture agreement, operating and transportation costs less 100% of net sales revenue were the responsibility of the operator and were therefore applied against the financial amount committed by the operator. As of December 31, 2010 no royalties were accrued since the production levels were minimal and revenue was less than credits earned under the applicable British Columbia royalty regime.

On June 18, 2010, the Gething project operator provided written notice to the Corporation that, pursuant to the terms of the joint venture agreement, it elected not to continue with the project. The Corporation has therefore received title to all wellbores drilled and facilities constructed by the joint venture partner at no cost, and as at December 31, 2010 the Corporation was operator of the project.

Since the Corporation had no reported production revenue, nor proved reserves as at December 31, 2010 and 2009, there was no depletion charge for the 2010 nor 2009 years. There has been no impairment of unproved natural gas properties during the years ended December 31, 2010 nor 2009.

The Corporation's mineral property refers to a Wollastonite project where the Corporation holds a 100% undivided interest, subject to a 10% profits interest, in a mineral claim covering 450 hectares in the Iskut River area of the Liard Mining Division, British Columbia. In a prior year, the book value of the mineral property was written down to $1 to reflect its present economic value.

4. ASSET RETIREMENT OBLIGATION

		2010		2009
Balance, beginning of year	$	288,095	$	211,848
Liabilities incurred		9,226		24,149
Revisions to estimated future obligation		108,280		28,447
Accretion		39,465		23,651
Liabilities settled		-		-
Balance, end of year	$	445,066	$	288,095

The total future asset retirement obligation including costs to reclaim and abandon wells and facilities plus the years in which such costs are expected to be incurred, is estimated by management. At December 31, 2010 the estimated total future liability of $2,221,099 (2009: $1,411,083) had a present value of $445,066 (2009: $288,095) assuming the liability is settled in approximately 21 years, using an estimated credit-adjusted risk-free interest rate of 9.0%, and an inflation rate of 2.25%.

The revision to the estimated future asset retirement obligation for the year ended December 31, 2010 results from the Corporation's assumption of the balance of the reclamation and abandonment costs related to the Gething project effective upon the Corporation receiving title to certain assets, and assuming operatorship.

5. SHAREHOLDERS' EQUITY

The Corporation has authorized share capital of an unlimited number of common shares of no par value. The Corporation has closed the following share issuances since January 1, 2009:

On June 29, 2010 the Corporation issued 3,000,000 Flow-Through Shares at a price of $1.40 per share. The Flow-Through Shares entitle the holder to certain income tax benefits in the form of Canadian Development Expense. The full proceeds of the Flow-Through Shares placement, or $4,200,000, has been allocated to common shares and was fully expended on eligible development costs by the end of fiscal 2010. Incurred in relation to this issuance were $224,716 of share issue costs, $56,179 of which were recorded as an offset against the future tax recovery of the Flow-Through Shares (see note 6).

On December 14, 2010 the Corporation closed a public offering of common shares of the Corporation by way of a short form prospectus. The offering included 16,670,000 common shares issued on a bought deal basis at $1.50 per share for gross proceeds of $25,005,000. The underwriters of the offering also exercised their over-allotment option to purchase an additional 780,500 common shares of the Corporation for gross proceeds of $1,170,750, thereby bringing the aggregate total to 17,450,500 common shares for total gross proceeds of $26,175,750. The Corporation paid a fee equal to 6% of the total gross proceeds, or $1,570,545, to the underwriters of the offering resulting in total net proceeds to the Corporation of $24,605,205. The Corporation also incurred additional share issue costs of $232,907 in relation to this public offering.

Common Shares

The common shares of the Corporation issued and outstanding are summarized as follows:

	2010		2009	
	Number of shares	Amount of shares	Number of shares	Amount of shares
Outstanding, beginning of year	48,653,401	$ 56,775,426	48,555,401	$ 57,075,145
Common shares issued for cash:				
Exercise of stock options	197,500	135,550	702,500	358,900
Private placements	3,000,000	4,200,000	-	-
Public financings	17,450,500	26,175,750	-	-
Exercise of share purchase warrants	6,566,660	6,001,324	250,000	200,000
Common shares cancelled:				
Issuer bid share repurchases	(1,269,200)	(1,479,444)	(854,500)	(1,008,015)
Credit from contributed surplus		64,460		106,595
Credit from share purchase warrants	-	1,940,927	-	58,500
Share issue costs	-	(2,028,168)	-	(15,699)
Tax effect of flow-through shares	-	(993,821)	-	-
Outstanding, end of year	74,598,861	$ 90,792,004	48,653,401	$ 56,775,426

Normal Course Issuer Bids

The Corporation received approval from the Exchange on December 2, 2008 to make a Normal Course Issuer Bid (the “2008-2009 NCIB”) consisting of the acquisition and cancellation of up to 1.0 million common shares of the Corporation’s stock, representing 2.1% of the total number of common shares outstanding at the commencement of the 2008-2009 NCIB. On September 24, 2009, the Corporation received approval from the Exchange to increase the 2008-2009 NCIB to 1.6 million common shares, or 3.3% of the total number of common shares outstanding at the commencement of the 2008-2009 NCIB. The 2008-2009 NCIB commenced on December 8, 2008 and closed on November 30, 2009. During 2009, the Corporation purchased for cancellation a total of 854,500 common shares of the Corporation for total cash consideration of $641,835 (at an average price of $0.75 per common share), representing 1.8% of the total number of common shares outstanding at the commencement of the 2008-2009 NCIB. Since the average carrying value of common shares outstanding at the time of repurchase was higher than the actual repurchase price per common share during the course of the 2008-2009 NCIB, the calculated difference per common share for the year ended December 31, 2009 of $366,180 was recorded as an increase to contributed surplus.

On April 14, 2010, the Corporation received approval from the Exchange to commence a subsequent Normal Course Issuer Bid (the "2010-2011 NCIB") through the facilities of the Exchange beginning on April 16, 2010. Pursuant to the 2010-2011 NCIB, the Corporation had the ability to acquire up to 2.5 million common shares of the Corporation, representing 4.6% of the total number of common shares outstanding at the commencement of the 2010-2011 NCIB, until April 16, 2011. From April 16, 2010 to December 31, 2010, the Corporation purchased for cancellation a total of 1,269,200 common shares of the Corporation for total cash consideration of $1,865,297 (at an average price of $1.47 per common share), representing 2.3% of the total number of common shares outstanding at the commencement of the 2010-2011 NCIB. Since the average carrying value of common shares outstanding at the time of repurchase was lower than the actual repurchase price per common share, the calculated difference per common share for the year ended December 31, 2010 of $385,853 was recorded as a decrease to contributed surplus.

On April 18, 2011, the Corporation received approval from the Exchange to commence a further Normal Course Issuer Bid (the "2011-2012 NCB") through the facilities of the Exchange beginning on April 19, 2011. Pursuant to the 2011-2012 NCIB, the Corporation may acquire up to 3.7 million common shares of the Corporation until April 18, 2012. Purchases in the market will be conducted by CIBC World Markets in accordance with the Exchange rules and all common shares acquired under the 2011-2012 NCIB will be cancelled.

For each of the Corporation's Normal Course Issuer Bids, all common shares of the Corporation purchased during any given month are returned to treasury and cancelled in the month subsequent to acquisition.

Share Purchase Warrants
In conjunction with previous financings, the Corporation issued warrants with terms between one to two years to acquire common shares at specific exercise prices as summarized below:

	2010		2009	
	Number of warrants	Amount of warrants	Number of warrants	Amount of warrants
Outstanding, beginning of year	6,566,660	$ 1,940,927	6,816,660	$ 1,999,427
Issued through private placements	-	-	-	-
Exercised prior to expiry	(6,566,660)	(1,940,927)	(250,000)	(58,500)
Expired unexercised	-	-	-	-
Outstanding, end of year	-	$ -	6,566,660	$ 1,940,927

Issue Date	Weighted Average Exercise Price	Number of Warrants Outstanding at December 31, 2010	Weighted Average Fair Value (Rounded)	Weighted Average Fair Value at December 31, 2010	Expiry Date
Feb. 19, 2008	$0.80	-	$0.234	$ -	Feb. 19, 2010 (2)
July 9, 2008	$1.40	-	$0.559	$ -	August 9, 2010 (1) (3)
	$ -	-	$ -	$ -	

Notes:

(1) Effective December 23, 2009, the expiry date of the $1.40 warrants was extended by the Exchange from January 9, 2010 to July 9, 2010, and effective June 29, 2010 the expiry date was further extended by the Exchange from July 9, 2010 to August 9, 2010.

(2) Prior to expiry, all remaining 5,320,000 of the $0.80 warrants were exercised by holders resulting in gross proceeds to the Corporation of $4,256,000.

(3) Prior to expiry, all remaining 1,231,660 of the $1.40 warrants were exercised by holders resulting in gross proceeds to the Corporation of $1,724,324.

Stock Options

The Corporation has a stock option plan for directors, executive officers, employees and consultants which provides for the granting of options to acquire common shares. Under the terms of the plan, options vest over periods as determined by the Corporation and expire after a maximum of five years.

At December 31, 2010, there were 5,350,000 (2009: 3,268,500) common shares reserved for issuance under the plan. Options to acquire 2,444,500 (2009: 2,267,000) common shares were outstanding at December 31, 2010, of which 2,147,000 (2009: 1,891,998) had vested and 297,500 (2009: 375,002) remained unvested, as follows:

	2010		2009	
	Number of options	Weighted Average Exercise Price	Number of options	Weighted Average Exercise Price
Outstanding, beginning of year	2,267,000	$ 1.34	3,057,000	$ 1.53
Granted	725,000	1.80	795,000	0.69
Exercised prior to expiry	(197,500)	0.69	(702,500)	0.51
Forfeited, cancelled or expired	(350,000)	4.57	(882,500)	2.09
Outstanding, end of year	2,444,500	$ 1.06	2,267,000	$ 1.34
Vested, end of year	2,147,000	$ 0.96	1,891,998	$ 1.46

The following table summarizes the information about stock options outstanding and vested as at December 31, 2010:

	Options Outstanding				Options Exercisable			
Range of Exercise Price	Number of Options Outstanding	Remaining Contractual Life (in Yrs)		Weighted Average Exercise Price	Number of Vested Options	Remaining Vested Contractual Life (in Yrs)		Weighted Average Exercise Price
$0.40 - $0.79	1,419,500	2.58	$	0.62	1,419,500	2.58	$	0.62
$0.80 - $1.72	190,000	1.90		0.94	187,500	1.87		0.94
$1.73 - $3.65	835,000	3.57		1.85	540,000	3.32		1.87
	2,444,500	2.87	$	1.06	2,147,000	2.70	$	0.96

Options granted are accounted for using the fair value method. The total gross compensation cost, prior to capitalization of $210,224 (2009: $Nil), charged against earnings for stock option expense during the twelve months ended December 31, 2010 was $764,239 (2009: $372,160).

The fair value of all option grants during 2010 and 2009 are estimated on the date of grant using the Black-Scholes pricing model with the following annualized weighted average assumptions:

	2010	2009
Risk free interest rate	2.48%	1.56%
Expected dividend yield	0%	0%
Expected stock price volatility	82.67%	82.46%
Expected time to exercise	4.2 years	3.7 years

Fair value of options granted	$1.20	$0.40
Term of options granted	5.0 years	4.6 years

Performance Units

The Corporation has a Performance Unit Incentive Plan for executive officers and directors of the Corporation. As at December 31, 2010, there were no performance units vested or outstanding.

A performance factor ranging from zero to three is determined for each performance period based on the average closing price of the Corporation's shares over the last 10 trading days of each performance period relative to a share price scale established at the date of grant. Upon each vesting date the units either pay out or expire. Awards under this plan are paid in cash within 60 days of the end of each performance period. Payments for vested units are determined by multiplying the number of units vested by the performance factor achieved during that performance period and multiplying the product by the 10 day average closing price of the Corporation's shares at the end of the performance period.

The performance units granted to date were comprised of two separate grants: the first for 55,000 units with performance factors based on minimum and maximum 10 day average closing share prices of $2.50 and $5.00 per share respectively for all performance periods, and the second for 119,000 units with performance factors based on minimum and maximum 10 day average closing share prices of $1.75 and $4.25 per share respectively for all performance periods. Prior to 2009, 57,100 performance units expired based on performance factors of zero determined for those performance periods. Based on the 10 day average closing share price on the Exchange as at December 31, 2009 of $1.35 per share, the resultant performance factor equaled zero and therefore the total compensation expense for all performance units for the year ended December 31, 2009 was $Nil. The 50,400 performance units outstanding as at December 31, 2009 expired unexercised on March 2, 2010.

The performance units are summarized below:

	2010		2009	
	Number of units	Weighted Average Minimum Vesting Price	Number of units	Weighted Average Minimum Vesting Price
Outstanding, beginning of year	50,400	$ 1.75	116,900	$ 1.94
Granted	-	-	-	-
Exercised prior to expiry	-	-	-	-
Forfeited, cancelled or expired	(50,400)	$ 1.75	(66,500)	$ 2.08
Outstanding, end of year	-	$ -	50,400	$ 1.75
Vested, end of year	-	$ -	-	$ 1.75

Contributed Surplus

	2010	2009
Balance, beginning of year	$ 5,865,418	$ 5,233,673
Stock-based compensation, prior to capitalization	764,239	372,160
Stock options exercised and transferred to common shares	(64,460)	(106,595)
Issuer bid share repurchases	(385,853)	366,180
Share purchase warrants expired unexercised	-	-
Balance, end of year	$ 6,179,344	$ 5,865,418

Per Share Amounts

The weighted average number of common shares outstanding during the year ended December 31, 2010 was basic 55,894,890 (2009: 48,534,525) and diluted 57,307,439 (2009: 49,008,803).

For the twelve months ended December 31, 2010, the existence of stock options and warrants affects the calculation of loss per share on a diluted basis. As the effect of this dilution is to reduce the reported loss per share, diluted loss per share equals basic loss per share.

6. FUTURE TAXES

The provision for future taxes differs from the amount computed by applying the combined statutory Canadian Federal and Provincial tax rates to losses before income taxes. The reasons for these differences are as follows:

	2010	2009
Loss before income taxes	$ (2,197,047)	$ (2,015,498)
Rate	28.0%	29.0%
Computed / expected income taxes	(615,173)	(584,494)
Increase (decrease) in income taxes resulting from:		
Non-deductible stock-based compensation	155,124	107,926
Non-deductible expenses	11,938	9,702
Effect of change in future tax rate	48,012	64,396
Unrecognized future tax benefits	(593,722)	402,470
Recovery of future taxes	$ (993,821)	$ -

Related to the June 2010 Flow-Through Share issuance, the Corporation recorded in the fourth quarter 2010 a recovery of future taxes in the amount of $1,050,000 related to the renouncement of $4,200,000 of Canadian Development Expense expenditures. Offsetting this recovery is the future tax effect of $56,179 related to the corresponding share issue costs of $224,716 incurred with the issuance, therefore resulting in a net future tax recovery of $993,821.

The Corporation had estimated net future tax assets at December 31, 2010 of $2,560,735 (2009: $2,817,587) against which a valuation allowance has been applied as follows:

	2010	2009
Property, plant and equipment	$ (493,385)	$ 611,195
Asset retirement obligation	111,267	72,024
Share issue costs	465,816	118,753
Tax loss carryforwards	2,477,037	2,015,615
	2,560,735	2,817,587
Valuation allowance	(2,560,735)	(2,817,587)
Future income tax asset	$ -	$ -

The following estimated tax pools were available as deductions against future taxable income as at December 31, 2010:

	2010
Non-capital losses	$ 9,879,828
Capital losses	25,932
Canadian exploration expense	3,691,301
Canadian development expense	30,927,695
Canadian oil and gas property expense	17,334,835
Foreign exploration and development expense	120,908
Undepreciated capital cost	820,314
Cumulative eligible capital	2,389
Equity instruments issue costs	1,863,268
	$ 64,666,470

Non-capital losses as at December 31, 2010 available to reduce future taxable income are as follows, until the end of:

2014	$ 592,574
2015	543,450
2026	1,166,271
2027	1,424,041
2028	1,916,596
2029	1,935,055
2030	2,301,841
	$ 9,879,828

7. COMMITMENTS

The Corporation has an office sub-lease agreement which expires on May 30, 2011. Under the terms of the sub-lease agreement, the Corporation is obligated to pay base annual rent of $28.00 per square foot plus operating costs on 6,793 square feet.

In January 2011, the Corporation signed an office lease agreement for the same premises as described above for a subsequent two year period, expiring May 31, 2013, at a base annual rent of $12.00 per square foot plus operating costs on 7,187 square feet.

8. FINANCIAL INSTRUMENTS

The Corporation has exposure to the following risks from its use of financial instruments: credit risk, market risk and liquidity risk.

Credit risk is the risk of financial loss to the Corporation if a counterparty to a financial instrument fails to meet its contractual obligations. The maximum exposure to credit risk at December 31, 2010 is the carrying amount of the Corporation's accounts receivable balances. The Corporation did not incur any write-offs relating to accounts receivable balances during 2010. The accounts receivable balance as at December 31, 2010 is comprised of amounts due from the Corporation's joint venture partners, and is proactively collected by the Corporation on a timely basis.

Market risk is the risk that changes in market indices, such as foreign exchange rates and interest rates, will affect the Corporation's income or the value of its held financial instruments. Since, as at December 31, 2010, the Corporation held no debt, held its cash and cash equivalents in the form of bank deposits and had limited dealings with foreign currency exchange, the Corporation's exposure to market risk is minimal.

Liquidity risk is the risk that the Corporation will not be able to meet its obligations as they become due. The Corporation manages its liquidity risk by synchronizing its forecasted cash requirements for operations with its anticipated capital financing activities and maintaining significant cash balances. The impacts on the Corporation's liquidity risk due to current equity and commodity price market conditions include a) increased uncertainty in raising additional funds on reasonable terms for future capital projects and b) a reduction in the Corporation's ability to generate sufficient revenues from the sale of natural gas to cover administrative and operating costs. As such, the Corporation held significant cash balances as at December 31, 2010, sufficient to cover the budgeted capital spending for the upcoming fiscal year.

Fair Value of Financial Instruments

Financial instruments held-for-trading include cash and cash equivalents, loans and receivables include accounts receivable and other financial liabilities include accounts payable and accrued trade liabilities. The fair value of cash and cash equivalents and accounts receivable approximate their carrying values due to the short term nature of these instruments. The fair value of accounts payable and accrued trade liabilities is significantly less than the carrying value due to the credit risk of the Corporation.

9. CAPITAL MANAGEMENT

The Corporation defines capital as Shareholders' equity and working capital based on the Corporation's financial statements as follows:

	2010	2009
Working capital		
Current assets	$ 34,285,708	$ 9,903,175
Current liabilities	(13,284,179)	(418,095)
	21,001,529	9,485,080
Shareholders' equity	75,635,284	44,448,933
Total captial	$ 96,636,813	$ 53,934,013

The current objectives of the capital management process are to maximize long term shareholder value by (i) ensuring sufficient funding to enable the Corporation's unconventional natural gas resource project to reach the stage of reserves, production and funds from operations and by (ii) minimizing the Corporation's cost of capital consistent with a low level of financial and liquidity risk.

The policies followed by the Corporation in managing its capital include:

(a) targeting a minimum working capital position of $4.0 million that covers all budgeted capital commitments, anticipated administration and field operating costs for a minimum period of three months, current reclamation obligations, and other non-contingent financial liabilities;

(b) funding 100% of capital requirements through the issue of equity instruments until such time as cash generated from operations exceeds anticipated overhead expenses prior to capitalization; and

(c) holding the proceeds of equity funding in deposit accounts of major financial institutions providing for immediate access.

The Corporation manages its capital by continuously monitoring the quality and level of working capital and the amount of its financial commitments and current obligations. An annual funding plan is approved by the Board of Directors in conjunction with the capital budget process and capital commitments are made based on a quarterly budget review and approval process. The capital management process takes into account exploration and development results, economic conditions, cost inflation, commodity prices and capital market conditions.