United Hunter Oil & Gas Corp.

Consolidated Financial Statements

(expressed in US dollars)

December 31, 2011 and 2010

Collins Barrow
Chartered Accountants

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INDEPENDENT AUDITORS' REPORT

To the Shareholders of United Hunter Oil & Gas Corp.

We have audited the accompanying consolidated financial statements of United Hunter Oil & Gas Corp. and its subsidiaries, which comprise the consolidated statements of financial position as at December 31, 2011, December 31, 2010 and January 1, 2010 and the consolidated statements of loss and comprehensive loss, changes in equity, and cash flows for the years ended December 31, 2011 and December 31, 2010 and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated 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 audits to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated 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 consolidated 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 controls. 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 consolidated 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 consolidated financial statements present fairly, in all material respects, the financial position of United Hunter Oil & Gas Corp. and its subsidiaries as at December 31, 2011, December 31, 2010 and January 1, 2010, and its financial performance and its cash flows for the years ended December 31, 2011 and December 31, 2010 in accordance with International Financial Reporting Standards.

Emphasis of matter

Without qualifying our opinion, we draw attention to Note 2 in the consolidated financial statements which indicates the existence of material uncertainties that may cast significant doubt about the company's ability to continue as a going concern.

Collins Barrow Toronto LLP

Collins Barrow Toronto LLP
Licensed Public Accountants
Chartered Accountants
April 23, 2012

United Hunter Oil & Gas Corp.
Consolidated Statements of Financial Position
(expressed in US dollars)

	Note	As at December 31, 2011 $	As at December 31, 2010 $ (note 15)	As at January 1, 2010 $ (note 15)
Assets				
Current				
Cash and cash equivalents		413,967	3,641,755	2,252
Accounts receivable		118,587	84,952	-
Due from joint venture partner	6	-	128,901	-
Prepaid expenses		145,015	68,617	-
		677,569	3,924,225	2,252
Exploration and evaluation	6	4,745,297	5,523,580	1,200,000
Property, plant and equipment	7	717,879	-	-
		6,140,745	9,447,805	1,202,252
Liabilities				
Current				
Accounts payable and accrued liabilities		347,021	875,656	75,000
Due to joint venture partner	6	25,507	-	-
Consideration payable	8	800,000	800,000	-
Warrant liability	9	-	432,389	-
		1,172,528	2,108,045	75,000
Decommissioning liabilities		52,749	-	
		1,225,277	2,108,045	75,000
Shareholders' equity				
Share capital	9	7,519,574	7,519,574	2,252
Warrants	9	403,783	403,783	-
Contributed surplus		1,959,250	1,594,094	1,200,000
Deficit		(4,967,139)	(2,177,691)	(75,000)
		4,915,468	7,339,760	1,127,252
		6,140,745	9,447,805	1,202,252
Going-concern	2			
Subsequent events	16			

Approved by the Board:

Arthur Halleran — **Director**

Daniel Bloch — **Director**

United Hunter Oil & Gas Corp.
Consolidated Statements of Loss and Comprehensive Loss
Years ended December 31

(expressed in US dollars)

	Note	2011 $	2010 $ (note 15)
Revenues			
Oil sales	11	315,196	-
Expenses			
Operating and transportation		394,880	-
Depletion	7	210,843	-
Impairment losses	7	735,130	-
Professional fees		165,487	101,737
Management fees		48,750	70,000
Salaries and wages		586,037	276,600
Consulting fees		192,060	565,879
Share-based compensation	9	365,156	394,094
Premises		44,629	51,000
General and administrative		57,139	31,617
Public company costs		25,544	24,879
Investor relations		155,808	141,006
Travel		69,375	77,386
Permitting		193,642	25,630
Transaction costs	5	-	1,226,384
Interest income		(15,774)	(19,366)
Gain on revaluation of warrant liablility	9	(432,389)	(1,206,084)
Loss on sale of exploration and evaluation	6	326,829	-
Foreign exchange gain (loss)		(18,502)	68,753
		3,104,644	1,829,515
Net loss and comprehensive loss		(2,789,448)	(1,829,515)
Basic and diluted loss per share		(0.02)	(0.02)
Weighted average number of shares outstanding - basic and diluted		120,302,722	95,425,318

United Hunter Oil & Gas Corp.
Consolidated Statements of Changes in Equity
Years ended December 31

(expressed in US dollars)

	Note	Share capital $	Warrants $	Contributed surplus $	Deficit $	Total $
Balance, January 1, 2010		2,252	21,439	1,200,000	(75,000)	1,148,691
Acquisition of 4% membership interest in Excelaron	6	367,570	-	-	-	367,570
Corporate finance fee	5	937,606	-	-	-	937,606
Private placement of units	5	9,008,100	-	-	-	9,008,100
Fair value of warrants issued	9	(2,020,817)	382,344	-	-	(1,638,473)
Share issue costs	9	(775,137)	-	-	-	(775,137)
Share-based compensation	9	-	-	394,094	-	394,094
Net liabilities assumed	5	-	-	-	(273,176)	(273,176)
Loss		-	-	-	(1,829,515)	(1,829,515)
Balance, December 31, 2010		7,519,574	403,783	1,594,094	(2,177,691)	7,339,760
Share-based compensation	9	-	-	365,156	-	365,156
Loss		-	-	-	(2,789,448)	(2,789,448)
Balance, December 31, 2011		7,519,574	403,783	1,959,250	(4,967,139)	4,915,468

United Hunter Oil & Gas Corp.
Consolidated Statements of Cash Flows
Years ended December 31

(expressed in US dollars)

	2011 $	2010 $ (note 15)
Cash flow from operating activities		
Loss	(2,789,448)	(1,829,515)
Items not affecting cash		
Depletion	210,843	-
Impairment losses	735,130	-
Share-based compensation	365,156	394,094
Transaction costs settled in common shares	-	937,606
Gain on revaluation of warrant liablility	(432,389)	(1,206,084)
Loss on sale of exploration and evaluation	326,829	-
Unrealized foreign exchange gain	-	(16,263)
Changes in non-cash working capital		
Accounts receivable	(33,635)	(84,952)
Due from joint venture partner	128,901	(128,901)
Prepaid expenses	(76,398)	(68,617)
Accounts payable and accrued liabilities	(528,635)	192,241
Due to joint venture partner	25,507	-
	(2,068,139)	(1,810,391)
Cash flow from financing activities		
Issue of common shares	-	9,008,100
Share issue costs	-	(775,137)
	-	8,232,963
Cash flow from investing activities		
Cash acquired upon amalgamation with Vesta	-	10,810
Acquistion of membership interest in Excelaron	-	(1,789,542)
Proceeds on sale of exploration and evaluation	300,000	-
Exploration and evaluation expenditures	(1,459,649)	(1,020,599)
	(1,159,649)	(2,799,331)
Net change in cash and cash equivalents	(3,227,788)	3,623,241
Cash and cash equivalents, beginning of year	3,641,755	2,252
Unrealized foreign exchange gain on cash held in foreign operations	-	16,262
Cash and cash equivalents, end of year	413,967	3,641,755
Cash and cash equivalents consist of the following:		
Cash	413,967	193,440
Short-term investments	-	3,448,315
	413,967	3,641,755
Supplementary information		
Interest paid	-	-
Interest received	15,744	19,306
Income taxes paid	-	-

1. Nature of operations

United Hunter Oil & Gas Corp. (the "Company") is a public company engaged in the exploration and development of oil and gas properties. The Company owns a 65% indirect joint venture interest in Excelaron, LLC ("Excelaron"), an exploration stage company based in San Luis Obispo, California; a 45% joint venture interest in Alamo Creek Oil LLC ("Alamo"), an exploration stage company based in San Luis Obispo, California; and interests in oil and gas properties in Alberta.

The Company was incorporated under the Business Corporations Act of Ontario on February 22, 2008 and its registered office is located at 181 Bay Street, Suite 1800, Toronto, ON M5J 2T9.

2. Going concern

The consolidated financial statements were prepared on a going concern basis, which assumes that the Company will continue in operation for the foreseeable future and will be able to realize its assets and discharge its liabilities and commitments in the normal course of business.

The Company has financed its operations through the issue of equity. At December 31, 2011, the Company had a working capital deficit of $494,959 (December 31, 2010 – working capital of $1,816,180; January 1, 2010 - working capital deficit of $72,748) and for the year ended December 31, 2011, the Company incurred losses of $2,789,448 (2010 - $1,829,515) and negative cash flows from operations of $2,068,139 (2010 - $1,810,391). The working capital deficiency and losses limit the Company's ability to fund operations and the exploration and development of oil and gas properties. In addition, there is uncertainty whether the Company will secure conditional use permits for its planned exploration and development of the Huasna property and in the event the conditional use permits are secured, the Company is committed to make a payment of $800,000. As a result, there is significant doubt about the Company's ability to continue as a going concern.

The continuation of the Company as a going concern is dependent on completing an equity financing and securing conditional use permits for its Huasna property. The Company will work to raise the necessary financing and secure the conditional use permits, but the outcome of these efforts cannot be predicted at this time.

The consolidated financial statements do not reflect the adjustments to the carrying values of assets and liabilities and the reported expenses and balance sheet classifications that would be necessary were the going concern assumption inappropriate.

3. Basis of presentation and adoption of International Financial Reporting Standards ("IFRS")

Statement of compliance

The consolidated financial statements are prepared in accordance with IFRS as issued by the International Accounting Standards Board.

These are the Company's first annual consolidated financial statements prepared in accordance with IFRS and IFRS 1 *First-time Adoption of International Financial Reporting Standards.* In previous years, the Company prepared its consolidated financial statements in accordance with Canadian generally accepted accounting principles ("Canadian GAAP"). See note 15 for details on the impact of the transition from Canadian GAAP to IFRS.

The consolidated financial statements were approved and authorized for issue by the Board of Directors on April 23, 2012.

Basis of measurement

These consolidated financial statements have been prepared on the historical cost basis, except for the warrant liability, which is measured at fair value.

Functional and presentation currency

These consolidated financial statements are presented in US dollars, which is the functional currency of the Company and its subsidiaries.

Use of estimates
The preparation of financial statements in conformity with IFRS requires the Company's management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the year in which the estimates are revised and in any future years affected.

Judgments
The key judgments made in applying accounting policies that have the most significant effect on the amounts recognized in these consolidated financial statements are as follows:

Identification of cash generating units
Cash generating units ("CGUs") are defined as the lowest grouping of integrated assets that generate identifiable cash inflows that are largely independent of the cash inflows of other assets or groups of assets. The classification of assets into cash generating units requires significant judgment and interpretations with respect to shared infrastructure, geographical proximity, petroleum type and similar exposure to market risk and materiality. See note 7.

Fair value of warrant liability
The fair value of the warrant liability is not observable in an active market, and as such, is determined using valuation methods. The Company uses judgment to select the method used to determine the fair value and uses directly and indirectly observable inputs. See note 9.

Estimates
Information about assumptions and estimation uncertainties that have a significant risk of resulting in a material adjustment within the next financial year are as follows:

Impairment of exploration and evaluation
Expenditures on exploration and evaluation are initially capitalized with the intent to establish commercially viable reserves. The Company makes estimates about future events and circumstances in determining whether the carrying amount of exploration and evaluation exceeds its recoverable amount.

Estimates of oil and natural gas reserves
Depletion and depreciation as well as the amounts used in impairment calculations are based on estimates of oil reserves. Reserves estimates are based on engineering data, estimated future prices, expected future rates of production and the timing of future capital expenditures, all of which are subject to many uncertainties and interpretations. At least once per year, a reserves estimate is prepared by independent qualified reserves evaluators. The Company expects that, over time, its reserves estimates will be revised upward or downward based on updated information such as the results of future drilling, testing and production levels, and may be affected by changes in commodity prices. See note 7.

Recoverable amounts of CGUs
The recoverable amount of a CGU used in the assessment of impairment of property, plant and equipment is the greater of its value in use ("VIU") and its fair value less costs to sell ("FVLCTS"). VIU is determined by estimating the present value of the future net cash flows from the continued use of the CGU, and is subject to the risks associated with estimating the value of reserves. FVLCTS refers to the amount obtainable from the sale of a CGU in an arm's length transaction between knowledgeable, willing parties, less costs of disposal.

Recoverable amounts of the Company's CGUs were based on their estimated VIU. The key assumptions and estimates of the value of oil reserves are valid at the time of reserves estimation and market assessment and are subject to change as new information becomes available. Changes in international and regional factors including supply and demand of commodities, inventory levels, drilling activity, currency exchange rates, weather, geopolitical and general economic environment factors may result in significant changes to the estimated recoverable amounts of CGUs. See note 7.

Decommissioning liabilities
Decommissioning liabilities are estimated based on the Company's net ownership interest in all wells and facilities, estimated costs to reclaim and abandon these wells and facilities and the estimated timing of the costs to be incurred in future years, based on current legal and constructive requirements and technology. The estimated liabilities and actual costs may change significantly due to changes in regulations, technology, timing of the expenditure, and the discount rates used to determine the net present value of the obligations.

Deferred income taxes
Deferred income tax assets and liabilities are measured using enacted or substantively enacted tax rates at the reporting date in effect for the period in which the temporary differences are expected to be recovered or settled. The effect on deferred income tax assets and liabilities of a change in tax rates is recognized as part of the provision for income taxes in the period that includes the enactment date. The recognition of deferred income tax assets is based on the assumption that it is probable that taxable profit will be available against which the deductible temporary differences can be utilized. See note 12.

Warrant liability and share-based compensation
The Company uses the Black-Scholes option pricing model in determining warrant liability and share-based compensation, which requires a number of assumptions to be made, including the risk-free interest rate, expected life, forfeiture rate and expected share price volatility. Consequently, the actual share-based compensation expense may vary from the amount estimated. See note 9.

4. Significant accounting policies and future accounting changes

The accounting policies set out below have been applied consistently to all years presented in these consolidated financial statements.

Basis of consolidation

Subsidiaries
Subsidiaries are entities controlled by the Company. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

Jointly controlled operations
Many of the Company's activities are conducted jointly with others. The consolidated financial statements include the Company's proportionate share of the joint ventures.

Transactions eliminated on consolidation
All intercompany transactions and balances are eliminated on consolidation.

Foreign currencies
Transactions in foreign currencies are translated to US dollars at exchange rates in effect on the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies are translated to US dollars at the period end exchange rate. Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are translated to US dollars at the exchange rate in effect on the date that the fair value was determined. Foreign currency differences arising on translation are recognized in the consolidated statement of loss and comprehensive loss.

Financial instruments
Non-derivative financial assets
The Company initially recognizes loans and receivables and deposits on the date that they are originated. All other financial assets (including assets designated at fair value through profit or loss) are recognized initially on the trade date, which is the date that the Company becomes a party to the contractual provisions of the instrument.

The Company derecognizes a financial asset when the contractual rights to the cash flows from the asset expire, or it transfers the rights to receive the contractual cash flows on the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred. Any interest in transferred financial assets that is created or retained by the Company is recognized as a separate asset or liability.

Financial assets and liabilities are offset and the net amount presented in the statement of financial position when, and only when, the Company has a legal right to offset the amounts and intends either to settle on a net basis or to realize the asset and settle the liability simultaneously.

The Company classifies non-derivative financial assets into the following categories: financial assets at fair value through profit or loss, held-to-maturity financial assets, loans and receivables and available-for-sale financial assets.

Financial assets at fair value through profit or loss
A financial asset is classified at fair value through profit or loss if it is classified as held for trading or is designated as such upon initial recognition. Financial assets are designated at fair value through profit or loss if the Company manages such investments and makes purchase and sale decisions based on their fair value in accordance with the Company's documented risk management or investment strategy. Attributable transaction costs are recognized in profit or loss as incurred. Financial assets at fair value through profit or loss are measured at fair value, and changes therein are recognized in profit or loss.

The Company has not classified any financial asset as fair value through profit or loss.

Held-to-maturity financial assets
If the Company has the positive intent and ability to hold debt securities to maturity, then such financial assets are classified as held-to-maturity. Held-to-maturity financial assets are recognized initially at fair value plus any directly attributable transaction costs. Subsequent to initial recognition held-to-maturity financial assets are measured at amortized cost using the effective interest method, less any impairment losses.
The Company has not classified any financial asset as held-to-maturity.

Loans and receivables
Loans and receivables are financial assets with fixed or determinable payments that are not quoted in an active market. Such assets are recognized initially at fair value plus any directly attributable transaction costs. Subsequent to initial recognition, loans and receivables are measured at amortized cost using the effective interest method, less any impairment losses.

The Company has classified cash and cash equivalents and due from joint venture partner as loans and receivables.

Available-for-sale financial assets
Available-for-sale financial assets are non-derivative financial assets that are designated as available for sale or are not classified in any of the above categories of financial assets. Subsequent to initial recognition, they are measured at fair value and changes therein, other than impairment losses and foreign currency differences on available-for-sale assets, are recognized in other comprehensive income and presented in the fair value reserve in equity. When an investment is derecognized, the gain or loss accumulated in equity is reclassified to profit or loss.

The Company has not classified any financial asset as available-for-sale.

Non-derivative financial liabilities
The Company initially recognizes debt securities issued and subordinated liabilities on the date that they are originated. All other financial liabilities (including liabilities designated at fair value through profit or loss) are recognized initially on the trade date, which is the date that the Company becomes a party to the contractual provisions of the instrument.

The Company derecognizes a financial liability when its contractual obligations are discharged, cancelled or expire. Financial assets and liabilities are offset and the net amount presented in the statement of financial position when, and only when, the Company has a legal right to offset the amounts and intends either to settle on a net basis or to realize the asset and settle the liability simultaneously.

The Company classifies non-derivative financial liabilities into the other financial liabilities category. Such financial liabilities are recognized initially at fair value plus any directly attributable transaction costs. Subsequent to initial recognition, these financial liabilities are measured at amortized cost using the effective interest method.

The Company has classified accounts payable and accrued liabilities and due to joint venture partner as other financial liabilities.

Derivative financial liabilities

Derivative financial liabilities, including warrant liability, are recorded at "fair value through profit or loss" and accordingly recorded on the balance sheet date at fair value. Unrealized gains and losses on derivatives held for trading are recorded as part of other gains or losses in earnings. Fair values for derivative instruments are determined using valuation techniques, using assumptions based on market conditions existing at the balance sheet date.

The Company has classified warrant liability as a derivative liability.

Impairment of non-derivative financial assets

A financial asset is assessed at each reporting date to determine whether there is objective evidence that it is impaired. A financial asset is impaired if objective evidence indicates that a loss event has occurred after the initial recognition of the asset, and that the loss event had a negative effect on the estimated future cash flows of that asset that can be estimated reliably.

Financial assets carried at amortized cost

An impairment loss in respect of a financial asset measured at amortized cost is calculated as the difference between its carrying amount and the present value of the estimated future cash flows discounted at the asset's original effective interest rate. The carrying amount of the financial asset is reduced by the amount of the impairment loss and the impairment loss is recognized in profit or loss. When a subsequent event causes the amount of impairment loss to decrease, the decrease in impairment loss is reversed through profit or loss.

Available-for-sale financial assets

An impairment loss in respect of a financial asset classified as available-for-sale is calculated as the difference between the acquisition cost and the current fair value, less any impairment loss recognized previously in profit or loss. The impairment loss is recognized by reclassifying the loss from equity to profit or loss. When a subsequent event causes the amount of impairment loss to decrease, the decrease in impairment loss is reversed through profit or loss, except in the case of equity investments where the decrease in impairment loss is recognized in other comprehensive income.

Cash and cash equivalents

Cash and cash equivalents consist of cash in the bank and short-term deposits with a maturity of less than three months.

Exploration and evaluation

Recognition and measurement

Pre-license costs are expensed when incurred.

Exploration and evaluation, including the costs of acquiring licenses and directly attributable general and administrative costs, initially are capitalized as exploration and evaluation. The costs are accumulated in cost centres by well, field or exploration area pending determination of technical feasibility and commercial viability.

Impairment

Exploration and evaluation are assessed for impairment if (i) sufficient data exists to determine technical feasibility and commercial viability, and (ii) facts and circumstances suggest that the carrying amount exceeds the recoverable amount. For purposes of impairment testing, exploration and evaluation is tested at a well level.

The technical feasibility and commercial viability of extracting an oil and gas resource is considered to be determinable when proved and/or probable reserves are determined to exist. A review of each exploration license or field is carried out, at least annually, to ascertain whether proved and/or probable reserves have been discovered. Upon determination of proved and/or probable reserves, exploration and evaluation attributable to those reserves are first tested for impairment and then reclassified from exploration and evaluation to property, plant and equipment or expensed to the statement of loss and comprehensive loss to the extent of any impairment.

Property, plant and equipment

Recognition and measurement

Property, plant and equipment, including costs incurred to develop oil reserves and maintain or enhance production and directly attributable general and administration costs, are measured at cost less accumulated depletion and accumulated impairment losses.

The gain or loss on disposal of property, plant and equipment is determined by comparing the proceeds from disposal with the carrying amount of the property, plant and equipment, and is recognized in profit or loss.

Subsequent costs

Costs incurred subsequent to the determination of technical feasibility and commercial viability and the costs of replacing parts of property, plant and equipment are recognized as oil and natural gas interests only when they increase the future economic benefits embodied in the specific asset to which they relate. All other expenditures are recognized in earnings as incurred. Capitalized oil and natural gas interests generally represent costs incurred in developing proved and/or probable reserves and bringing on or enhancing production from such reserves, and are accumulated on a field or geotechnical area basis.

Depletion and depreciation

The net carrying value of development or production assets is depleted on a field by field basis using the unit of production method by reference to the ratio of production in the year to the related proven and probable reserves, taking into account estimated future development costs necessary to bring those reserves into production. Future development costs are estimated taking into account the level of development required to produce the reserves. These estimates are reviewed by independent reserve engineers at least annually.

Impairment

The carrying amounts of property, plant and equipment are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, the estimated recoverable amount is calculated. For the purpose of impairment testing, assets are grouped together into CGUs, the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups of assets. The recoverable amount of an asset or a CGU is the greater of its VIU and its FVLCTS.

In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money. Value in use is generally computed by reference to the present value of the future cash flows expected to be derived from production of proved and probable reserves.

Exploration and evaluation are allocated to the related CGU's to assess for impairment, both at the time of any triggering facts and circumstances as well as upon their eventual reclassification to producing assets (oil interests in property, plant and equipment). When significant parts of an item of property, plant and equipment, including oil interests, have different useful lives, they are accounted for as separate items (components).

An impairment loss is recognized in the statement of loss and comprehensive loss if the carrying amount of an asset or its CGU exceeds its estimated recoverable amount.

Impairment losses previously recognized are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of accumulated depletion and depreciation, if no impairment loss had been recognized.

Decommissioning liabilities

The Company's activities give rise to dismantling, decommissioning and site disturbance remediation activities. Provision is made for the estimated cost of site restoration. Decommissioning obligations are measured at the present value of management's best estimate of expenditures required to settle the present obligation at the balance sheet date. The fair value of the estimated obligation is recorded as a liability with a corresponding increase in the carrying amount of the related asset. The obligation is subsequently adjusted at the end of each period to reflect the passage of time and changes in the estimated future cash flows underlying the obligation. The increase in the provision due to the passage of time is recognized as accretion costs whereas increases or decreases due to changes in the estimated future cash flows or changes in the discount rate are capitalized. Actual costs incurred upon settlement of the decommissioning obligations are charged against the provision to the extent the provision was established.

Warrant liability

Warrants representing an obligation to issue shares for a price that is not in the Company's functional currency that do not qualify as a rights offering to all shareholders of that class, are classified as a derivative liability and measured at fair value at each balance sheet date with changes recognized in the statement of loss and comprehensive loss.

Share capital

Common shares are classified as equity. Incremental costs directly attributable to the issue of common shares are recognized as a deduction from equity, net of any tax effects.

Revenue and expenses from the sale of oil

Revenue from the sale of oil is recognized based on volume delivered at contractual delivery points and rates.

Expenses associated with the delivery, including operating, transportation and production-based royalties, are recognized in the period that the related revenue is recognized.

Share-based payments

The Company offers a stock option plan for its employees. The fair value of stock options for each vesting period is determined using the Black-Scholes option pricing model and is recorded over the vesting period as an increase to stock-based compensation and contributed surplus. A forfeiture rate is estimated on the grant date and is adjusted to reflect the actual number of options that vest. Upon the exercise of stock options, the proceeds received by the Company and the related contributed surplus are recorded as an increase to share capital. In the event that vested stock options expire, previously recognized share-based compensation is not reversed. In the event that stock options are forfeited, previously recognized share-based compensation associated with the unvested portion of the stock options forfeited is reversed.

The fair value of share-based payment transactions to non-employees and other share-based payments are based on the fair value of the goods and services received. If the fair value cannot be estimated reliably, the share-based payment transaction is measured at the fair value of the equity instruments granted at the date the Company receives the goods or services.

Provisions

A provision is recognized if, as a result of a past event, the Company has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the liability. The unwinding of the discount is recognized as a finance cost.

Income tax
Income tax expense comprises current and deferred tax. Current tax and deferred tax is recognized in profit or loss except to the extent that it relates to a business combination, or items recognized directly in equity or in other comprehensive income.

Current tax is the expected tax payable or receivable on the taxable income or loss for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years. Current tax payable also includes any tax liability arising from the declaration of dividends.

Deferred tax is recognized in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognized for:

- temporary differences on the initial recognition of assets or liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable profit or loss;
- temporary differences related to investments in subsidiaries and jointly controlled entities to the extent that it is probable that they will not reverse in the foreseeable future; and
- taxable temporary differences arising on the initial recognition of goodwill.

Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date.

Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax liabilities and assets, and they relate to income taxes levied by the same tax authority on the same taxable entity, or on different tax entities, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realized simultaneously.

A deferred tax asset is recognized for unused tax losses, tax credits and deductible temporary differences, to the extent that it is probable that future taxable profits will be available against which they can be utilized. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realized.

Loss per share
The Company presents basic and diluted loss per share data for its common shares. Basic earnings per share is calculated by dividing the loss attributable to ordinary shareholders of the Company by the weighted average number of common shares outstanding during the period, adjusted for own shares held. Diluted earnings per share is determined by adjusting the loss attributable to common shareholders and the weighted average number of common shares outstanding, adjusted for own shares held, for the effects of all dilutive potential ordinary shares, which comprise outstanding warrants and stock options.

New standards and interpretations not yet adopted
A number of new standards, amendments to standards and interpretations are effective for periods beginning on or after January 1, 2013.

IFRS 9, Financial Instruments ("IFRS 9")
IFRS 9 addresses classification and measurement of financial assets and replaces the multiple category and measurement models in IAS 39 for debt instruments with a new mixed measurement model having only two categories: amortized cost and fair value through profit or loss. IFRS 9 also replaces the models for measuring equity instruments, and such instruments are either recognized at fair value through profit or loss or at fair value through other comprehensive income. Where such equity instruments are measured at fair value through other comprehensive income, dividends are recognized in profit or loss to the extent not clearly representing a return of investment; however, other gains and losses (including impairments) associated with such instruments remain in accumulated comprehensive income indefinitely.

Requirements for financial liabilities were added in October 2010 and they largely carried forward existing requirements in IAS 39, *Financial Instruments - Recognition and Measurement*, except that fair value changes due to credit risk for liabilities designated at fair value through profit and loss would generally be recorded in other comprehensive income.

IFRS 10, Consolidation ("IFRS 10")
IFRS 10 requires an entity to consolidate an investee when it is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. Under existing IFRS, consolidation is required when an entity has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. IFRS 10 replaces SIC-12 Consolidation—Special Purpose Entities and parts of IAS 27 Consolidated and Separate Financial Statements.

IFRS 11, Joint Arrangements ("IFRS 11")
IFRS 11 requires a venturer to classify its interest in a joint arrangement as a joint venture or joint operation. Joint ventures will be accounted for using the equity method of accounting whereas for a joint operation the venturer will recognize its share of the assets, liabilities, revenue and expenses of the joint operation. Under existing IFRS, entities have the choice to proportionately consolidate or equity account for interests in joint ventures. IFRS 11 supersedes IAS 31, Interests in Joint Ventures, and SIC-13, Jointly Controlled Entities—Non-monetary Contributions by Venturers.

IFRS 12, Disclosure of Interests in Other Entities ("IFRS 12")
IFRS 12 establishes disclosure requirements for interests in other entities, such as joint arrangements, associates, special purpose vehicles and off balance sheet vehicles. The standard carries forward existing disclosures and also introduces significant additional disclosure requirements that address the nature of, and risks associated with, an entity's interests in other entities.

IFRS 13, Fair Value Measurement ("IFRS 13")
IFRS 13 is a comprehensive standard for fair value measurement and disclosure requirements for use across all IFRS standards. The new standard clarifies that fair value is the price that would be received to sell an asset, or paid to transfer a liability in an orderly transaction between market participants, at the measurement date. It also establishes disclosures about fair value measurement.

Under existing IFRS, guidance on measuring and disclosing fair value is dispersed among the specific standards requiring fair value measurements and in many cases does not reflect a clear measurement basis or consistent disclosures.

Amendments to other standards
In addition, there have been amendments to existing standards, including IAS 27, Separate Financial Statements (IAS 27), and IAS 28, Investments in Associates and Joint Ventures (IAS 28). IAS 27 addresses accounting for subsidiaries, jointly controlled entities and associates in non-consolidated financial statements. IAS 28 has been amended to include joint ventures in its scope and to address the changes in IFRS 10-13.

Effect of new standards
IFRS 9, IFRS 10 and IFRS 11 are expected to have an effect on the consolidated financial statements of the Company. The Company has not determined the extent of the impact these standards and does not plan to early adopt these new standards.

5. Reverse takeover transaction
On April 23, 2010, Vesta Capital Corp. (“Vesta”), a capital pool company, completed its qualifying transaction by way of an amalgamation among Vesta, United Hydrocarbon Corporation (“UHC”) and a wholly owned subsidiary of Vesta (“Amalgamation”).

Pursuant to the Amalgamation, Vesta issued 1.7754 common shares for each UHC common share outstanding, 1.33 common shares for each UHC Class A common share outstanding, 1.33 warrants for each UHC Warrant outstanding and 1 warrant for each UHC Compensation Warrants outstanding.

(expressed in US dollars)

Since the former UHC shareholders owned greater than 50% of the combined entity after the completion of the Amalgamation, the Amalgamation was accounted for as a reverse-takeover transaction that did not constitute a business combination, and therefore, was accounted for as though UHC acquired Vesta using the purchase method of accounting. Although Vesta was the legal parent company and UHC was the legal subsidiary, for accounting purposes, UHC was considered to be the acquirer. The combined entity subsequently changed its name to United Hunter Oil & Gas Corp.

Details of the acquisition were as follows:

Assets	**$**
Cash	10,810
Receivables	124,516
Prepaid expenses	25,022
	160,348
Liabilities	
Accounts payable and accrued liabilities	412,085
Warrants	21,439
	433,524
Net liabilities assumed	(273,176)

Net liabilities assumed were recorded as a deficit adjustment. Transaction costs of $1,226,384 were expensed, of which, $937,606 related to the fair value of 5,746,999 UHC common shares issued for a corporate finance fee (note 9). In addition, $411,316 of transaction costs were incurred in Vesta prior to the Amalgamation and therefore have been included in accounts payable in the above purchase equation.

6. Exploration and evaluation

	Huasna $	Atlee Buffalo $	Leduc Woodbend $	Porter Ranch $	Total $
Balance, January 1, 2010	1,200,000	–	–	–	1,200,000
Acquisition	3,300,499	105,140	–	50,000	3,455,639
Additions	164,639	371,160	332,142	–	867,941
Balance, December 31, 2010	4,665,138	476,300	332,142	50,000	5,523,580
Additions	23,299	1,187,551	189,282	6,860	1,406,992
Disposition	–	–	(521,424)	–	(521,424)
Transfers to property, plant and equipment	–	(1,663,851)	–	–	(1,663,851)
Balance, December 31, 2011	4,688,437	–	–	56,860	4,745,297

Exploration and evaluation consists of the Company's exploration projects which are pending the determination of proved or probable reserves. Additions represent the Company's share of costs incurred on exploration and evaluation during the period.

Huasna
The Company holds an indirect 65% joint venture interest in Excelaron, which holds a 100% interest in an oil and natural gas property consisting of 260 acres on the western edge of the Huasna Basin, an existing California Department of Oil, Gas and Geothermal Resources designated oilfield within the Meridian Anticline located in Arroyo Grande, California.

On January 1, 2009, the Company acquired a 21% joint venture interest in Excelaron from a shareholder of the Company, for a 5% assignable gross overriding royalty. The royalty is payable on all amounts received directly or indirectly by the

(expressed in US dollars)

Company that can be attributed to the Company's 65% joint venture interest in Excelaron. The joint venture interest, net of the gross overriding royalty was recorded at fair value as a capital contribution increasing contributed surplus.

On April 23, 2010, the Company increased its joint venture interest in Excelaron from 21% to 65%. The Company acquired an additional 4% joint venture interest in Excelaron in exchange for 2,253,001 common shares valued at C$0.163 per common share for total consideration of $367,570 (C$367,239). The Company acquired an additional 40% joint venture interest in Excelaron for cash of $1,000,900 (C$1,000,000), a capital contribution to Excelaron of US$1,075,000 and a commitment to pay US$800,000 when Excelaron secures its permits for its planned operations on its oil and gas properties. In the event that Excelaron does not secure such permits or the Company does not pay the US$800,000, the Company's 65% joint venture interest in Excelaron will be reduced to a 40% joint venture interest.

These acquisitions are accounted for as follows:

	$
Investment in Excelaron	
Acquisition of 4% joint venture interest	
2,253,001 UHC common shares	367,570
Acquisition of 40% joint venture interest	
Cash of C$1,000,000	1,000,900
Members' capital contribution in cash	1,075,000
Consideration payable	800,000
	3,243,470
Net assets acquired	
Cash	286,358
Accounts receivable	12,100
Exploration and evaluation	3,300,499
Property, plant and equipment	2,482
	3,601,439
Accounts payable	357,969
	3,243,470

Although the Company holds a 65% joint venture interest in Excelaron, the joint operating agreement has established joint control over Excelaron by all parties with a joint venture interest t.

As at and for the years ended December 31, the consolidated financial statements included the following amounts related to the Company's joint venture interest in Excelaron (2011 – 65%; 2010 – 65%):

	2011 $	2010 $
Statements of financial position		
Current assets	21,668	11,772
Exploration and evaluation	1,143,547	1,121,171
Current liabilities	85,435	55,323
Statements of loss and comprehensive loss		
Expenses	340,406	246,527
Net loss	340,406	246,527
Statements of cash flows		
Cash flow from operating activities	(308,828)	(402,917)
Cash flow from financing activities	318,489	868,689
Cash flow from investing activities	(22,376)	(474,859)

(expressed in US dollars)

See note 16 for subsequent event.

Atlee Buffalo

The Company acquired a working interest in Atlee Buffalo for fair value of $105,140 from a company controlled by a director and officer of the Company. The working interest in Atlee Buffalo is subject to gross overriding royalties of 2% payable to a company controlled by a director and officer of the Company and to a director and officer of the Company.

Production commenced at Atlee Buffalo and the related costs were transferred to property, plant and equipment.

Leduc Woodbend

Pursuant to a farm-in and operating agreement dated December 9, 2010, the Company acquired the right to earn a 100% interest in each 40 acre spacing in which it completes a well, subject to a 10% convertible overriding royalty, which can be converted into a 30% working interest after 60 days of production. Pursuant to a joint interest agreement, the Company granted a joint interest partner the right to acquire a 20% interest in the property by paying 28.5% of the costs of the re-completion program. In the event that the overriding royalty is converted to a 30% working interest, the interest of the joint interest partner will be reduced to 20%. The interest in Leduc Woodbend is subject to a gross overriding royalty of 2% payable to two directors and officers of the Company.

On November 2, 2011, the Company sold its interest in Leduc Woodbend for cash of C$300,000 and a 12% gross overriding royalty (“GOR”) on the production from the test well completed by the Company. The purchaser has agreed to tie in the test well and attempt production. To the extent that the tie in costs exceeds C$200,000, the purchaser will be entitled to recover up to C$150,000 of the costs as a reduction to the GOR payable to the Company. In the event that the purchaser has not tied in the test well and attempted production within 8 months of the sale, the purchaser will pay C$150,000 to the Company as an advance royalty, which will be deducted from the GOR payable to the Company. Provided that the purchaser has tied in the test well and pursued production for 6 months after the tie-in and the test well is not capable of economic production, the purchaser’s obligation to continue production will terminate. As a result of the sale, the Company recorded a loss on the sale of exploration and evaluation of $326,829.

Porter Ranch

The Company acquired a 45% joint venture interest in Alamo Creek Oil LLC (“Alamo”), at which time, leased 4,068 acres adjacent to the Santa Maria Basin and south east of the Company's Huasna property (“Porter Ranch”). Subsequently, Alamo leased an additional 4,983 acres increasing the acreage under lease to 9,051 acres. See note 16 for subsequent event.

7. Property, plant and equipment

Cost

	$
Balance, January 1, 2010 and December 31, 2010	–
Transfer from exploration and evaluation	1,663,851
Balance, December 31, 2011	1,663,851

Accumulated depletion and impairment losses

	$
Balance, January 1, 2010 and December 31, 2010	–
Depletion	210,843
Impairment losses	735,130
Balance, December 31, 2011	945,973

Carrying amounts

	$
At January 1, 2010 and December 31, 2010	–
At December 31, 2011	717,879

(expressed in US dollars)

Impairment losses

During the year ended December 31, 2011, the Company recorded impairment losses of $735,130 based upon VIU using reserve estimates from its independent qualified reserve evaluators, a discount rate of 10% and the following estimated oil prices:

Year	$ per bbl
2012	72.49
2013	72.49
2014	73.18
2015	74.58

At December 31, 2011, if the discount rate had been 5% higher or lower, the impairment losses recognized would have been revised as follows:

	$
Reduction of impairment loss using 5% discount rate	27,725
Additional impairment using 15% discount rate	26,454

8. Consideration payable

Pursuant to its acquisition of Excelaron (note 6), the Company is committed to pay US$800,000 when Excelaron secures its permits for its planned operations on its oil and gas properties. In the event that Excelaron does not secure such permits or the Company does not pay the US$800,000, the Company's 65% Membership Interest in Excelaron will be reduced to a 40% Membership Interest.

9. Share capital

Authorized

An unlimited number of common shares
Unlimited number of preference shares, issuable in series.

(expressed in US dollars)

Outstanding

	Share capital Number of shares	Amount $	Warrant liability $	Warrants $
Vesta common shares				
Balance, January 1, 2010	6,303,000	832,296	–	21,439
UHC common shares (note 5)				
Balance, January 1, 2010	22,500,000	2,252	–	–
Acquisition of 4% membership interest in Excelaron	2,253,001	367,570	–	–
Corporate finance fee	5,746,999	937,606	–	–
	30,500,000	1,307,428	–	–
UHC Class A shares (note 5)				
Private placement of common share units	45,000,000	9,008,100	–	–
Fair value of UHC Warrants	–	(1,638,473)	1,638,473	–
Fair value of UHC Compensation Warrants	–	(382,344)	–	382,344
Share issue costs	–	(775,137)	–	–
	45,000,000	6,212,146	1,638,473	382,344
Adjustment to reflect the issue of 1.7754 common shares of Vesta for each UHC common share outstanding (note 5)	23,649,722	–	–	–
Adjustment to reflect the issue of 1.33 common shares of Vesta for each UHC Class A share outstanding (note 5)	14,850,000	–	–	–
Adjustment to reflect the elimination of share capital and contributed surplus of Vesta (note 5)	–	(832,296)	–	–
Change in value of fair value of warrants	–	–	(1,206,084)	–
Share-based compensation	–	–	–	–
Balance, December 31, 2010	120,302,722	7,519,574	432,389	403,783
Change in value of fair value of warrants	–	–	(432,389)	–
Balance, December 31, 2011	120,302,722	7,519,574	–	403,783

In connection with the Amalgamation, Vesta issued 22,662,892 common shares to directors and parties related to them in exchange for 12,764,950 UHC Class A shares.

Concurrent with the closing of the Amalgamation, UHC completed a private placement of 45,000,000 common share units at a price of C$0.20 per unit for gross proceeds of $9,008,100 (C$9,000,000) ("Private Placement"). Each unit consisted of one Class A common share and one-half of one warrant, with each whole warrant entitling the holder to purchase one Class A common share at a price of C$0.40 per Class A share until April 23, 2012 ("UHC Warrant"). In the event that the UHC Class A common shares trade at or above C$0.80 for more than 20 consecutive days, the warrants must be exercised after written notice is provided by UHC or they will expire. In respect of the Private Placement, UHC issued 3,600,000 broker compensation warrants entitling the holder to purchase one Class A common share at a price of C$0.20 per Class A common share until April 23, 2012 ("UHC Compensation Warrants"); issued 5,746,999 common shares with a value of $937,606 in respect of a corporate finance fee recorded in transaction costs, of which, 4,310,249 common shares were issued to a company controlled by a director of the Company; and paid $683,307 for the agent's commissions, legal fees and out-of-pocket expenses.

The fair value of the UHC Warrants of $1,638,473 and the UHC Compensation Warrants of $382,344 was calculated using the Black-Scholes option pricing model with the following assumptions:

(expressed in US dollars)

Risk-free interest rate	1.98%
Expected volatility	100%
Expected life of warrants	2 years
Expected dividend yield	Nil

The fair value of the UHC Compensation Warrants was measured using the Black-Scholes option pricing model as the fair value of the services received by the Company could not be reasonably estimated.

Warrants
A summary of the Company's warrants is presented below:

	Number of warrants	Weighted-average exercise price C$
Balance, January 1, 2010	200,000	0.20
UHC Warrants issued	22,500,000	0.40
Adjustment to reflect the issue of 1.33 warrants of Vesta for each UHC Warrant outstanding (note 5)	7,425,000	–
UHC Compensation Warrants issued (note 5)	3,600,000	0.20
Warrants expired	(200,000)	0.20
Balance, December 31, 2010 and December 31, 2011	33,525,000	0.38

A summary of the Company’s outstanding warrants at December 31, 2011 is presented below:

Exercise price	Expiry date	Options outstanding
C$0.40	April 23, 2012	29,925,000
C$0.20	April 23, 2012	3,600,000
		33,525,000

In the event that the Company’s common shares trade at or above C$0.80 for more than 20 consecutive days, the 29,925,000 warrants must be exercised after written notice is provided by the Company or they will expire.

Subsequent to December 31, 2011, the expiry date of the 29,925,000 warrants was extended to August 31, 2012.

Stock options
Under its stock option plan, the Company may grant options to its employees to acquire up to 10% of the issued and outstanding common shares at the time of the grant. As at December 31, 2011, there were 12,030,272 common shares available for issuance under the stock option plan.

A summary of the Company's stock options is presented below:

(expressed in US dollars)

	Number of options	Weighted-average exercise price C$
Balance, January 1, 2010	380,000	0.20
Granted	9,775,000	0.15
Cancelled	(380,000)	0.20
Balance, December 31, 2010	9,775,000	0.15
Granted	1,600,000	0.15
Expired	(1,000,000)	0.15
Balance, December 31, 2011	10,375,000	0.15
Options exercisable	4,125,000	0.15

Pursuant to the terms of the Amalgamation, the 380,000 stock options of Vesta outstanding at the closing date of the Amalgamation were cancelled.

A summary of the Company's outstanding stock options at December 31, 2011 is presented below:

Exercise price	Expiry date	Options outstanding	Options exercisable
C$0.15	May 12, 2015	6,350,000	2,116,667
C$0.15	July 28, 2012	1,000,000	333,333
C$0.15	July 20, 2015	1,000,000	1,000,000
C$0.15	August 31, 2015	425,000	141,667
C$0.15	January 18, 2016	650,000	216,667
C$0.15	May 5, 2016	600,000	200,000
C$0.15	September 19, 2016	350,000	116,666
		10,375,000	4,125,000

The weighted average remaining contractual life of outstanding stock options is 3.54 years.

A summary of the stock options granted and the assumptions for the calculation of the fair value of those stock options using the Black-Scholes option pricing model is presented below:

	May 12, 2010	July 20, 2010	August 31, 2010
Options granted	8,350,000	1,000,000	425,000
Exercise price	C$0.15	C$0.15	C$0.15
Share price	C$0.14	C$0.12	C$0.12
Expiry date	May 12, 2015	July 20, 2015	August 31, 2015
Fair value	$856,000	$85,000	$35,000
Risk-free interest rate	2.96%	2.61%	2.05%
Expected volatility	100%	100%	100%
Expected life of options	5 years	5 years	5 years
Expected dividend yield	Nil	Nil	Nil
Forfeiture rate	Nil	Nil	Nil
Vesting	3 annual instalments	On date of grant	3 annual instalments

(expressed in US dollars)

	January 18, 2011	May 5, 2011	September 19, 2011
Options granted	650,000	600,000	350,000
Exercise price	C$0.15	C$0.15	C$0.15
Share price	C$0.08	C$0.12	C$0.085
Expiry date	January 18, 2016	May 5, 2016	September 19, 2016
Fair value	$35,000	$54,000	$20,000
Risk-free interest rate	2.58%	2.50%	1.43%
Expected volatility	100%	100%	100%
Expected life of options	5 years	5 years	5 years
Expected dividend yield	Nil	Nil	Nil
Forfeiture rate	Nil	Nil	Nil
Vesting	1/3 on date of grant and 1/3 each in 2 annual instalments		

Expected volatility was based on historical volatility of securities of comparable companies. The weighted-average grant date fair value of stock options granted during year was $0.07 per stock option (2010 - $0.10).

10. Determination of fair values

A number of the Company's accounting policies and disclosures require the determination of fair value, for both financial and non-financial assets and liabilities. Fair values have been determined for measurement and/or disclosure purposes based on the following methods. When applicable, further information about the assumptions made in determining fair values is disclosed in the notes specific to that asset or liability.

Cash and cash equivalents, accounts receivable, due from joint venture partner, accounts payable and accrued liabilities, due to joint venture partner and consideration payable

The fair values of cash and cash equivalents, accounts receivable, due from joint venture partner, accounts payable and accrued liabilities, due to joint venture partner and consideration payable are estimated as the present value of future cash flows, discounted at the market rate of interest at the reporting date. At December 31, 2011, December 31, 2010 and January 1, 2010, the fair value of these balances approximated their carrying value due to their short term to maturity.

Exploration and evaluation and property, plant and equipment

The Company estimated the VIU to determine the recoverable amounts of the Company's CGUs for impairment testing based on consideration of the following:

- net present value of proved plus probable reserves using a pre-tax discount rate of 10% as determined by independent qualified reserves evaluators;
- management's estimate of the fair value of undeveloped land; and
- a review of the values indicated by the metrics of recent market transactions of similar assets within the oil and gas industry.

The market value of other items of exploration and evaluation and property, plant and equipment is based on the quoted market prices for similar items.

Warrant liability and stock options

The fair value of warrant liability and employee stock options is measured using a Black-Scholes option pricing model. Measurement inputs include share price on grant date, exercise price, expected volatility (based on historical volatility of securities of comparable companies), weighted average expected life and forfeiture rate (both based on historical experience and general option holder behaviour), expected dividends, and the risk-free interest rate (based on government bonds).

Classification of fair value of financial instruments

The Company classified the fair value of its financial instruments measured at fair value according to the following hierarchy based on the amount of observable inputs used to value the instrument:

(expressed in US dollars)

- Level 1 - quoted prices in active markets for identical assets and liabilities;
- Level 2 - inputs, other than the quoted prices included in Level 1, that are observable for the asset or liability, either directly or indirectly;
- Level 3 - inputs for the asset or liability that are not based on observable market data

The carrying value of cash and cash equivalents, due from joint venture partner, accounts payable and accrued liabilities, due to joint venture partner and consideration payable approximate fair value due to their short-term nature. Other financial instruments measured at fair value classified using the fair value hierarchy:

As at December, 31, 2011	**Carrying value $**	**Fair value $**	**Level 1 $**	**Level 2 $**	**Level 3 $**
Derivative financial liabilities					
Warrant liability	–	–	–	–	–

As at December, 31, 2010	**Carrying value $**	**Fair value $**	**Level 1 $**	**Level 2 $**	**Level 3 $**
Derivative financial liabilities					
Warrant liability	432,389	432,389	–	–	432,389

11. Revenues

For the year ended December 31, 2011, revenues of $315,196 were derived from one external customer.

12. Income taxes

The Company's effective income tax rate differs from the amount that would be computed by applying the federal and provincial statutory rate of 28.25% (2010 – 31%) to the loss for the year. The reasons for the difference are as follows:

	2011 $	**2010 $**
Income tax reduction based on statutory rate	(788,019)	(557,087)
Other	(83,816)	–
Change in future tax rates	131,610	69,833
Non-deductible expenses	101,753	–
Deferred income tax assets not recognized	638,472	487,254
	–	–

Deferred income tax liability
A continuity of the net deferred income tax liability is as follows:

	2011 $	**2010 $**
Oil and gas properties	286,802	–
Non-capital losses	1,492,985	980,578
Share issue costs	141,799	194,439
Consideration payable	200,000	200,000
Warrant liability	–	108,097
Benefit of deferred income taxes not recognized	(2,121,586)	(1,483,114)
	–	–

Due to losses incurred in the current year with respect to the Company's Canadian operations, and expected future operating results, management has determined that it is probable that the deferred income tax assets will not be realized.

Losses carried forward
At December 31, 2011, the Company had non-capital loss carryforwards of approximately $5,490,000 which expire between 2028 and 2031.

13. Financial risk management

The Company's activities expose it to a variety of financial risks that arise as a result of its exploration, development, production and financing activities, including credit risk, liquidity risk and market risk.

This note presents information about the Company's exposure to each of the above risks, the Company's objectives, policies and processes for measuring and managing risk, and the Company's management of capital. Further quantitative disclosures are included throughout these consolidated financial statements.

The Board of Directors oversees management's establishment and execution of the Company's risk management framework. Management has implemented and monitors compliance with risk management policies. The Company's risk management policies are established to identify and analyze the risks faced by the Company, to set appropriate risk limits and controls, and to monitor risks and adherence to market conditions and the Company's activities.

Credit risk
Credit risk is the risk of financial loss to the Company if a counterparty to a financial instrument fails to meet its contractual obligations. Credit risk arises principally from the Company's cash balances and receivables. The maximum exposure to credit risk is equal to the balances of cash and cash equivalents and due from joint venture partner.

The Company's limits its exposure to credit risk on its cash and cash equivalents by holding its cash balances in deposits with a high credit quality Canadian chartered bank.

Liquidity risk
Liquidity risk is the risk that the Company will encounter difficulty in meeting its financial liabilities that are settled in cash or other financial assets. The Company's approach to managing liquidity risk is to ensure, as far as possible, that it will have sufficient liquidity to meet is liabilities as they come due. The amounts for accounts payable and accrued liabilities, due to joint venture partner and consideration payable are due in less than one year.

Market risk
Market risk is the risk that changes in market prices, such as equity prices, foreign exchange rates, and interest rates will affect the Company's income or the value of its financial instruments.

Equity price risk
Equity risk arises from the effect of changes in the market value of the Company's common shares on the determination of fair value of the warrant liability as calculated using the Black-Scholes option pricing model.

Currency risk
Currency risk arises from the Company's financial instruments and purchases that are denominated in a currency other than the US dollar, the Company's functional currency. As at December 31, 2011, the Company had the following monetary assets and liabilities denominated in Canadian dollars:

(expressed in US dollars)

	C$
Assets	
Cash and cash equivalents	377,910
Accounts receivable	92,160
	470,070
Liabilities	
Accounts payable and accrued liabilities	188,134
Due to joint venture partner	18,436
	206,570

As at December 31, 2011, a 5% change in the exchange rate between the US dollar and Canadian dollar would have resulted in an impact on operations of $13,175.

Interest rate risk
The Company's exposure to interest rate risk is limited due to the short-term nature of its financial instruments.

Capital management
Capital of the Company consists of share capital, warrants, contributed surplus and deficit. The Company's objective when managing capital is to safeguard the Company's ability to continue as a going concern so that it can acquire, explore and develop oil and gas properties for the benefit of its shareholders. The Company manages its capital structure and makes adjustments based on the funds available to the Company in light of changes in economic conditions. The Board of Directors has not established quantitative return on capital criteria for management, but rather relies on the expertise of the Company's management to sustain the future development of the Company. In order to facilitate the management of its capital requirements, the Company prepares annual expenditure budgets that consider various factors, including successful capital deployment and general industry conditions. Management reviews its capital management approach on an ongoing basis and believes that this approach, given the relative size of the Company, is reasonable.

The Company's principal source of capital is from the issue of common shares. In order to achieve its objectives, the Company intends to raise additional funds as required.

The Company is not subject to externally imposed capital requirements and there were no changes to the Company's approach to capital management during the year.

14. Related party transactions

	Years ended December 31, 2011 $	2010 $
Atlee Buffalo acquisition costs		
Acquired a 95% working interest from a company controlled by an officer (note 5)	–	105,140
Legal fees		
Paid to a firm, of which, a director is a partner	84,172	310,725
Consulting fees		
Paid to a director and officer in his capacity as an President	–	67,778
Paid to a company controlled by an officer in his capacity as Vice President	–	12,865
Paid to a company controlled by an officer for geological consulting services	–	13,600
Rent		

Paid to a company controlled by a director for office premises	12,643	36,457
Paid to a company controlled by an officer for office premises	17,700	15,009

	Years ended December 31, 2011 $	2010 $
Office		
Paid to a person related to a director for administration services	31,859	7,075
Paid to a company controlled by an officer for office services	–	2,269
Transaction costs		
Issued 4,310,249 common shares in respect of corporate finance fees to a company controlled by a director (note 5)	–	703,203

These transactions were in the normal course of business and recorded at fair value.

Compensation of key management personnel
The Company considers its directors and officers to be key management personnel. Transactions with key management personnel are set out as follows:

	Years ended December 31, 2011 $	2010 $
Salaries	473,339	252,535
Short-term employee benefits	–	–
Share-based payments, representing amortization of share-based compensation	289,333	198,090
	762,672	450,625

15. First-time adoption of IFRS

These financial statements are the first annual consolidated financial statements prepared in accordance with IFRS. The accounting policies set out in note 3 have been applied in preparing the consolidated financial statements for the years ended December 31, 2011 and December 31, 2010 and the opening statement of financial position at January 1, 2010.

First-time adoption exemptions applied
IFRS 1 allows first-time adopters certain exemptions from retrospective application of certain IFRS. The Company has applied the following optional exemptions to full retrospective application of IFRS and has made the following adjustments to transition from Canadian GAAP to IFRS:

Historical cost as deemed cost
The Company elected an IFRS 1 exemption whereby the Canadian GAAP full cost pool was measured upon transition to IFRS at the amount determined under Canadian GAAP as at January 1, 2010. Cost included in the full cost pool on January 1, 2010 were allocated on a pro-rata basis to the underlying assets on the basis of proved and probable reserves values as at January 1, 2010. The exploration and evaluation assets were reclassified from the full cost pool to exploration and evaluation assets at the amount that was recorded under Canadian GAAP.

Business Combinations
IFRS 1 allows for IFRS 3, *Business Combinations*, to be applied retrospectively or prospectively. The Company elected to adopt IFRS 3 prospectively to business combinations subsequent to the date of transition. Accordingly, all business combinations after January 1, 2010 will be accounted for in accordance with IFRS 3.

(expressed in US dollars)

Share-based payment transactions
IFRS 1 allows that full retrospective application may not apply to certain share-based instruments depending on the grant date and vesting terms. The Company has elected to not apply IFRS 2 to share-based payments granted after November 7, 2002 that vested before the date of transition to IFRS. Accordingly, the Company has applied IFRS 2 only to unvested stock options outstanding as at January 1, 2010.

Reconciliation of equity at the date of IFRS transition – January 1, 2010

	Note	Canadian GAAP $	Effect of transition to IFRS $	IFRS $
Assets				
Current				
Cash and cash equivalents		2,252	–	2,252
Exploration and evaluation	15(d)	1,854,203	(654,203)	1,200,000
		1,856,455	(654,203)	1,202,252
Liabilities				
Current				
Accounts payable and accrued liabilities		75,000	–	75,000
Deferred income tax liability	15(d)	628,348	(628,348)	–
		703,348	(628,348)	75,000
Shareholders' equity				
Share capital		2,252	–	2,252
Contributed surplus		1,200,000	–	1,200,000
Deficit	15(d)	(49,145)	(25,855)	(75,000)
		1,153,107	(25,855)	1,127,252
		1,856,455	(654,203)	1,202,252

(expressed in US dollars)

Reconciliation of equity at the end of the last reporting year under Canadian GAAP – December 31, 2010

	Note	Canadian GAAP $	Effect of transition to IFRS $	IFRS $
Assets				
Current				
Cash and cash equivalents		3,641,755	–	3,641,755
Accounts receivable		84,952	–	84,952
Due from joint venture partner		128,901	–	128,901
Prepaid expenses		68,617	–	68,617
		3,924,225	–	3,924,225
Exploration and evaluation	15(a)	5,377,783	800,000	5,523,580
	15(d)		(654,203)	
		9,302,008	145,797	9,447,805
Liabilities				
Current				
Accounts payable and accrued liabilities		875,656	–	875,656
Consideration payable	15(a)	□	800,000	800,000
Warrant liability	15(b)	□	432,389	432,389
		875,656	1,232,389	2,108,045
Deferred income tax liability	15(d)	530,131	(530,131)	–
		1,405,787	702,258	2,108,045
Shareholders' equity				
Share capital		7,519,574	–	7,519,574
Warrants	15(b)	2,042,256	(1,638,473)	403,783
Contributed surplus	15(c)	1,453,370	140,724	1,594,094
Deficit	15(b), (c) and (d)	(3,118,979)	941,288	(2,177,691)
		7,896,221	(556,461)	7,339,760
		9,302,008	145,797	9,447,805

(expressed in US dollars)

Reconciliation of comprehensive loss for the last reporting year under Canadian GAAP – December 31, 2010

	Note	Canadian GAAP $	Effect of transition to IFRS $	IFRS $
Expenses				
Professional fees		101,737	–	101,737
Management fees		70,000	–	70,000
Salaries and wages		276,600	–	276,600
Consulting fees		565,879	–	565,879
Stock-based compensation	15(c)	253,370	140,724	394,094
Premises		51,000	–	51,000
General and administrative		31,617	–	31,617
Public company costs		24,879	–	24,879
Investor relations		141,006	–	141,006
Travel		77,386	–	77,386
Permitting		25,630	–	25,630
Transaction costs		1,226,384	–	1,226,384
Interest income		(19,366)	–	(19,366)
Gain on revaluation of warrant liability	15(b)	–	(1,206,084)	(1,206,084)
Foreign exchange gain		68,751	–	68,753
		2,894,873	(1,065,360)	1,829,515
Loss and comprehensive loss before income taxes	15(c)	(2,894,873)	1,065,360	(1,829,515)
Deferred income tax reduction	15(d)	98,217	(98,217)	–
Net loss and comprehensive loss		(2,796,656)	(967,143)	(1,829,515)
Basic and diluted loss per share		(0.03)	□	(0.02)

Impact on statement of cash flows for the last reporting year under Canadian GAAP – December 31, 2010

There was no effect on cash flow from operations, financing activities or investing activities as a result of transition to IFRS.

Reconciliation notes

a) Contingent liability

The Company is committed to pay $800,000 at such time as Excelaron secures its conditional use permits for its planned operations on its oil and gas properties.

Under IFRS, a contingent liability resulting from a business combination is recognized if it is a present obligation that arises from past events and its fair value can be measured reliably.

Under Canadian GAAP, when the outcome of a contingency cannot be determined without reasonable doubt, a contingent liability is not recognized until the contingency is resolved and the consideration is issued.

The following table summarizes the adjustments resulting from the recognition of the contingent liability:

	January 1, 2010 $	December 31, 2010 $
Consolidated statements of financial position		
Exploration and evaluation	–	800,000
Consideration payable	–	800,000

b) Warrants

The Company has outstanding common share purchase warrants denominated in Canadian dollars.

Under IFRS, an obligation to issue shares for a price that is not in the Company's functional currency, and that does not qualify as a rights offering to all shareholders of that class, must be classified as a derivative liability and measured at fair value at each balance sheet date with changes recognized in the statement of comprehensive income.

Under Canadian GAAP, warrants were classified as equity and changes in fair value were not recognized.

The following table summarizes the adjustments resulting from the reclassification and revaluation the warrants:

	January 1, 2010 $	December 31, 2010 $
Consolidated statements of financial position		
Warrant liability	–	432,389
Warrant	–	(1,638,473)
Deficit	–	1,206,084

	December 31, 2010 $
Consolidated statements of loss and comprehensive loss	
Gain on revaluation of warrant liability	1,206,084

c) Share based payments

Under IFRS, the Company is required to recognize the expense over the individual vesting periods for the graded vesting awards and estimate a forfeiture rate.

Under Canadian GAAP, the Company recognized stock-based compensation related to issue of stock options on a straight-line basis through the date of full vesting and did not incorporate a forfeiture multiple.

The following table summarizes the adjustments resulting from the recognition of the stock-based compensation in accordance with IFRS:

	January 1, 2010 $	December 31, 2010 $
Consolidated statements of financial position		
Contributed surplus	–	140,724
Deficit	–	(140,724)

(expressed in US dollars)

	December 31, 2010 $
Consolidated statements of loss and comprehensive loss	
Stock-based compensation	140,724

d) Deferred income taxes

Under IFRS, there is a provision for an exemption from recording a deferred income tax liability on initial recognition when the acquisition of assets is not a business combination and, at the time of the transaction, affects neither accounting profit/loss nor tax profit/loss. As the acquisition of Excelaron meets the IFRS exemption criteria, the Company did not recognize the deferred income tax liability.

Under Canadian GAAP, the Company recognized deferred income tax on temporary differences arising on acquisition of assets where the carrying amount of the assets acquired exceeded the tax base.

The following table summarizes the adjustments resulting from the de-recognition of deferred income taxes in accordance with IFRS:

	January 1, 2010 $	December 31, 2010 $
Consolidated statements of financial position		
Exploration and evaluation	(654,203)	(654,203)
Deferred income tax liability	(628,348)	(628,348)
Deficit	(25,855)	(25,855)

	December 31, 2010 $
Consolidated statements of loss and comprehensive loss	
Deferred income tax reduction	(98,217)

16. Subsequent events

Amalgamation

On January 1, 2012, the Company amalgamated with its wholly-owned subsidiary UHC.

Huasna

On March 8, 2012 the San Luis Obispo County Planning Commission voted to deny the granting of conditional use permits to the Company for the Huasna. The decision has been appealed to the San Luis Obispo County Board of Supervisors for the final decision.

Porter Ranch

Subsequent to December 31, 2011, the Company declined to pay its share of a cash call and its joint venture interest in Alamo was reduced from 45% to 25%.