TERRACE ENERGY CORP.
CONSOLIDATED FINANCIAL STATEMENTS

(Expressed in United States Dollars)

JANUARY 31, 2013 and 2012

SmytheRatcliffe
CHARTERED ACCOUNTANTS

INDEPENDENT AUDITORS' REPORT

TO THE SHAREHOLDERS OF TERRACE ENERGY CORP.

We have audited the accompanying consolidated financial statements of Terrace Energy Corp., which comprise the consolidated statements of financial position as at January 31, 2013 and 2012, and the consolidated statements of operations and comprehensive loss, changes in shareholders' equity and cash flows for the years then ended, 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 audit 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 auditors' 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 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 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 Terrace Energy Corp. as at January 31, 2013 and 2012, and its financial performance and its cash flows for the years then ended in accordance with International Financial Reporting Standards.

Smythe Ratcliffe LLP
Chartered Accountants

Vancouver, British Columbia
May 29, 2013

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TERRACE ENERGY CORP.
CONSOLIDATED STATEMENTS OF FINANCIAL POSITION
As at January 31
(Expressed in United States Dollars)

		2013		2012
				(Note 2)
ASSETS				
Current assets				
Cash	$	1,673,449	$	2,559,228
Accounts receivable (Note 12)		1,327,511		5,073
Prepaids		50,029		-
Total current assets		3,050,989		2,564,301
Non-current assets				
Operators bond		25,000		25,000
Advances for future exploration (Note 4)		459,008		1,209,163
Exploration and evaluation assets (Note 5)		6,737,039		1,754,821
Property and equipment (Note 6)		6,047,528		-
Total assets	$	16,319,564	$	5,553,285
LIABILITIES AND SHAREHOLDERS' EQUITY				
Current liabilities				
Accounts payable and accrued liabilities (Note 12)	$	571,585	$	174,129
Non-current liabilities				
Decommissioning obligations (Note 7)		8,016		-
Total liabilities		579,601		174,129
Shareholders' equity				
Capital stock (Note 8)		15,977,713		5,970,906
Stock options reserve (Note 8)		638,649		259,081
Warrants reserve (Note 8)		255,342		255,342
Translation reserve (Note 2)		396,149		299,995
Deficit		(1,527,890)		(1,406,168)
Total shareholders' equity		15,739,963		5,379,156
Total liabilities and shareholders' equity	$	16,319,564	$	5,553,285

Approved on behalf of the Board:

"Eric Boehnke"	"William McCartney"
Eric Boehnke, Director	William McCartney, Director

The accompanying notes are an integral part of these consolidated financial statements.

TERRACE ENERGY CORP.
CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME
For the years ended January 31
(Expressed in United States Dollars)

	2013	2012
		(Note 2)
REVENUE		
Oil and gas sales	$ 3,415,104	$ -
DIRECT OPERATING EXPENSES		
Production and operating	220,772	-
Royalties	164,256	-
Depreciation, depletion and accretion (Notes 6 and 7)	845,006	-
Operating Income	2,185,070	-
GENERAL AND ADMINSTRATIVE EXPENSES		
Administrative	312,111	126,742
Business investigation costs	-	94,400
Consulting	124,321	92,335
Foreign exchange loss	77,870	59,433
Impairment of exploration and evaluation assets (Note 5)	135,000	229,447
Interest income	(19,091)	(10,843)
Investor relations	345,856	-
Professional (Note 12)	195,122	179,593
Project investigation costs (Note 16)	297,961	119,857
Salaries and benefits (Note 12)	318,562	-
Share-based payments (Note 8)	393,100	280,173
Transfer agent and filing fees	39,492	70,546
Travel	86,488	23,780
	2,306,792	1,265,463
Net loss for the year	$ (121,722)	$ (1,265,463)
Basic and diluted loss per share	$ (0.00)	$ (0.03)
Weighted average number of common shares outstanding	60,348,088	38,741,924
Comprehensive loss		
Net loss for the year	$ (121,722)	$ (1,265,463)
Cumulative translation adjustment	96,154	(19,502)
Comprehensive loss for the year	$ (25,568)	$ (1,284,965)

The accompanying notes are an integral part of these consolidated financial statements.

TERRACE ENERGY CORP.
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
(Expressed in United States Dollars)

	Capital Stock						
	Shares	**Amount**	**Stock Options Reserve**	**Warrants Reserve**	**Translation Reserve**	**Deficit**	**Total Shareholders' Equity**
Balance – January 31, 2011 (Note 8)	**30,881,821**	**$ 2,548,433**	**$ (7,470)**	**$ -**	**$ 319,497**	**$ (140,705)**	**$ 2,719,755**
Private placement	19,000,000	2,819,366	-	359,005	-	-	3,178,371
Share issue costs	-	(56,771)	-	-	-	-	(56,771)
Exercise of warrants	2,887,500	524,431	-	-	-	-	524,431
Exercise of options	150,000	18,162	-	-	-	-	18,162
Fair value of options exercised	-	13,622	(13,622)	-	-	-	-
Fair value of warrants exercised	-	103,663	-	(103,663)	-	-	-
Share-based payments		-	280,173	-	-	-	280,173
Cumulative translation adjustment	-	-	-	-	(19,502)	-	(19,502)
Net loss for the year	-	-	-	-	-	(1,265,463)	(1,265,463)
Balance – January 31, 2012 (Note 8)	**52,919,321**	**5,970,906**	**259,081**	**255,342**	**299,995**	**(1,406,168)**	**5,379,156**
Private placement	10,000,000	10,024,019	-	-	-	-	10,024,019
Share issue costs	-	(48,787)	-	-	-	-	(48,787)
Exercise of options	150,000	18,043	-	-	-	-	18,043
Fair value of options exercised	-	13,532	(13,532)	-	-	-	-
Share-based payments	-	-	393,100	-	-	-	393,100
Cumulative translation adjustment	-	-	-	-	96,154	-	96,154
Net loss for the year	-	-	-	-	-	(121,722)	(121,722)
Balance – January 31, 2013	**63,069,321**	**$ 15,977,713**	**$ 638,649**	**$ 255,342**	**$ 396,149**	**$ (1,527,890)**	**$ 15,739,963**

The accompanying notes are an integral part of these consolidated financial statements.

TERRACE ENERGY CORP.
CONSOLIDATED STATEMENTS OF CASH FLOWS
For the years ended January 31
(Expressed in United States Dollars)

	2013	2012 (Note 2)
CASH FLOWS FROM OPERATING ACTIVITIES		
Net loss for the year	$ (121,722)	$ (1,265,463)
Items not involving cash:		
Depreciation, depletion and accretion	845,006	-
Share-based payments	393,100	280,173
Impairment of exploration and evaluation assets	135,000	229,447
Unrealized loss on foreign exchange	77,457	82,233
Changes in non-cash working capital items:		
Accounts receivable	(1,322,438)	(3,867)
Prepaids	(50,029)	-
Accounts payable and accrued liabilities	62,120	45,342
Net cash provided by (used in) operating activities	18,494	(632,135)
CASH FLOWS FROM INVESTING ACTIVITIES		
Restricted cash	-	2,546,510
Advances for future exploration	-	(1,209,163)
Exploration and evaluation expenditures	(9,489,036)	(628,983)
Acquisition of exploration and evaluation assets	(1,363,612)	(1,367,666)
Acquisition of property and equipment	(63,597)	-
Net cash used in investing activities	(10,916,245)	(659,302)
CASH FLOWS FROM FINANCING ACTIVITIES		
Proceeds from issuance of shares	10,024,019	3,178,371
Share issue costs	(48,787)	(56,771)
Exercise of options	18,043	18,162
Exercise of warrants	-	524,431
Net cash provided by financing activities	9,993,275	3,664,193
Foreign exchange effect on cash	18,697	(32,746)
Change in cash for the year	(885,779)	2,340,010
Cash, beginning of year	2,559,228	219,218
Cash, end of year	$ 1,673,449	$ 2,559,228

Supplemental cash flow information (Note 14)

The accompanying notes are an integral part of these consolidated financial statements.

1. NATURE OF OPERATIONS

Terrace Energy Corp. (the "Company") was incorporated on July 6, 2006 under the *Business Corporations Act* (British Columbia) and previously named Terrace Resources Inc.

The Company's head office is located at 270 – 666 Burrard Street, Vancouver, British Columbia, Canada V6C 2X8. The Company is the ultimate parent company.

The Company is classified as a "Tier 2 Oil and Gas Issuer", as those terms are defined in TSX Venture Exchange (the "Exchange") policies. Its common shares trade on the Exchange under the symbol "TZR".

These consolidated financial statements have been prepared on a going concern basis, which assumes that the Company will be able to realize its assets and discharge its liabilities in the normal course of business. The Company has a limited history of revenues and operating cash flows. The future development of the Company's oil and gas interests are therefore dependent upon its ability to raise additional capital as required and future profitable operations, neither of which is assured. These consolidated financial statements do not include adjustments to amounts and classifications of assets and liabilities that might be necessary should the Company be unable to continue operations.

2. BASIS OF PRESENTATION

Statement of compliance

These consolidated financial have been prepared in accordance with International Financial Reporting Standards ("IFRS"), as issued by the International Accounting Standards Board, and interpretations of the International Financial Reporting Interpretations Committee ("IFRIC"). The Board of Directors approved the audited consolidated financial statements on May 29, 2013.

Basis of measurement

These consolidated financial statements have been prepared on a historical cost basis, except for certain financial instruments, which are measured at fair value. In addition, these consolidated financial statements have been prepared using the accrual basis of accounting, except for cash flow information.

Functional and presentation currency

The functional currency of the Company is the Canadian dollar ("CAD"). However, these consolidated financial statements are presented in United States dollars ("USD") because substantially all of the Company's assets and operations are situated in the USA. Assets and liabilities are translated into the presentation currency using the exchange rate in effect on the consolidated statement of financial position date, shareholders' equity accounts are translated into the presentation currency using the historical exchange rate, and revenues and expenses are translated at the average rate for the year, which approximates the exchange rate in effect on the transaction date. Exchange gains and losses on translation are included as a separate component in shareholders' equity as "translation reserve".

Certain prior year amounts have been reclassified to conform to the current year presentation.

3. SIGNIFICANT ACCOUNTING POLICIES

Estimates, risks and uncertainties

The preparation of consolidated financial statements in conformity with IFRS requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the consolidated financial statements and the reported expenses during the year. Actual results could differ from these estimates, and, as such, estimates and underlying assumptions are reviewed on an ongoing basis. Revisions are recognized in the year in which the estimates are revised and in any future year affected.

Significant assumptions about the future and other sources of estimation uncertainty that management has made at the end of the reporting period that could result in a material adjustment to the carrying amounts of assets and liabilities in the event that actual results differ from assumptions made, relate to, but are not limited to, the following:

i) The inputs used in calculating the fair value for share-based payments included in operations.
ii) The recoverability of amounts recorded as exploration and evaluation assets and property and equipment.
iii) The collectability of accounts receivable.
iv) The rates of depletion and depreciation of property and equipment.
v) The determination of decommissioning obligations.

Management has applied judgment in the determination of reserve estimates. Reserve estimates affect a number of the areas referred to above, in particular the valuation of property and equipment and the calculation of depletion of property and equipment.

Principles of consolidation

The consolidated financial statements include the financial statements of the Company and its controlled subsidiaries. All intercompany transactions, balances, revenues and expenses are eliminated in full on consolidation.

Name of subsidiary	Place of Incorporation	Percentage ownership
Terrace US Holdings Inc.	USA	100%
Terrace Operating LLC	USA	100%
Terrace Cutlass LLC	USA	100%
Terrace STS LLC	USA	100%

Financial instruments

All financial instruments are classified as one of the following: held-to-maturity, loans and receivables, fair value through profit or loss (“FVTPL”), available-for-sale or other financial liabilities. Financial assets and liabilities at FVTPL are measured at fair value with gains and losses recognized in profit or loss. Financial assets held-to-maturity, loans and receivables, and other financial liabilities are measured at amortized cost using the effective interest method. Available-for-sale instruments are measured at fair value with unrealized gains and losses recognized in other comprehensive loss and reported in shareholders’ equity.

Transaction costs that are directly attributable to the acquisition or issue of financial instruments that are classified as other than FVTPL, which are expensed as incurred, are included in the initial carrying value of such instruments.

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

Financial instruments (Continued)

Fair value hierarchy

Fair value measurements of financial instruments are required to be classified using a fair value hierarchy that reflects the significance of inputs in making the measurements. The levels of the fair value hierarchy are defined as follows:

Level 1 – Quoted prices (unadjusted) in active markets for identical assets or liabilities.
Level 2 – Inputs other than quoted prices included within 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.

Foreign currency translation

Transactions denominated in foreign currencies are translated to the respective functional currencies of the Company's entities at exchange rates in effect at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are translated to the functional currency at the exchange rate prevailing at that date.

Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are retranslated to the functional currency at the exchange rate prevailing at the date that the fair value was determined. Non-monetary items denominated in a foreign currency that are measured based on historical cost are translated using the exchange rate in effect at the date of the transaction.

Foreign currency differences arising on retranslation are recognized in profit or loss.

Property and equipment and exploration and evaluation assets

Pre-exploration ("project investigation costs") expenditures

Expenditures made by the Company before acquiring the legal right to explore in a specific area do not meet the definition of an asset, and therefore are expensed by the Company as incurred.

Exploration and evaluation expenditures

Costs incurred once the legal right to explore has been acquired are capitalized as exploration and evaluation assets. These assets include, but are not limited to, exploration license expenditures, leasehold property acquisition costs, evaluation costs, including drilling costs directly attributable to an identifiable well and directly attributable general and administrative costs. These costs are accumulated in cost centers by property and are not subject to depletion until technical feasibility and commercial viability has been determined.

Exploration and evaluation assets are assessed for impairment when facts and circumstances suggest that the carrying amount exceeds the recoverable amount.

The technical feasibility and commercial viability of extracting petroleum resources is considered to be determinable when proved and 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 probable reserves have been discovered. Upon determination of proved and probable reserves, exploration and evaluation assets attributable to these reserves are tested for impairment and reclassified to oil and gas properties.

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

Property and equipment and exploration and evaluation assets (Continued)

Development and production costs

Items of property and equipment, which include oil and gas development and production assets, are measured at cost less accumulated depletion and depreciation and accumulated impairment losses. Development and production assets are grouped in cash-generating units ("CGU") for impairment testing. A CGU's recoverable amount is the higher of its fair value less costs to sell and its value in use. Where the carrying amount of a CGU exceeds its recoverable amount, the asset group is considered impaired and is written down to its recoverable amount.

Gains and losses on disposal of an item of property and equipment, including oil and gas properties, are determined by comparing the proceeds from disposal with the carrying amount of property and equipment and are 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 and equipment are recognized as oil and gas properties only when they increase the future economic benefits embodied in the specific asset to which they relate. All other expenditures are recognized in profit or loss as incurred. Such capitalized expenditures generally represent costs incurred in developing proved and/or probable reserves and bringing in or enhancing production from such reserves, and are accumulated on a field or geotechnical area basis. The carrying amount of a replaced or sold component is derecognized. The costs of the day-to-day servicing of property and equipment are recognized in profit or loss as incurred.

Depletion and depreciation

Depletion of oil and gas properties is determined using the unit-of-production method based on production volumes in relation to total estimated proved developed reserves as determined annually by independent engineers and determined in accordance with National Instrument 51-101 *Standards of Disclosure for Oil and Gas Activities*. Natural gas reserves and production are converted at the energy equivalent of six thousand cubic feet to one barrel of oil.

The calculation of depletion and depreciation of production equipment is based on total capitalized costs less the estimated net realizable value of production equipment and facilities after the proved developed reserves are fully depleted.

Proved developed reserves are estimated using independent reserve engineer reports and represent the estimated quantities of crude oil, natural gas and natural gas liquids, which geological, geophysical and engineering data demonstrate with a 90% degree of certainty to be recoverable in future years from known proved developed reservoirs and which are considered commercially producible.

Such reserves may be considered commercially producible if management has the intention of developing and producing them. Such intention is based upon:

- A reasonable assessment of the future economics of such production;
- A reasonable expectation that there is a market for all or substantially all the expected oil and gas production; and
- Evidence that the necessary production, transmission and transportation facilities are available or can be made available.

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

Property and equipment and exploration and evaluation assets (Continued)

Reserves may only be considered proved developed if supported by actual production. The area of reservoir considered proved is that portion delineated by drilling and defined as oil and/or oil-water contacts, if any, or both. In the absence of information on fluid contacts, the lowest known structural occurrence of oil and gas controls the lower proved limit of the reservoir.

Depreciation of other equipment is provided for on a 14% to 20% straight-line basis. Depreciation methods, useful lives and residual values are reviewed at each reporting date.

Impairment

Exploration and evaluation assets are assessed for impairment when they are reclassified to developing and producing assets, as oil and gas properties, and also if facts and circumstances suggest that the carrying amount exceeds the recoverable amount.

Fair value less costs to sell is determined to be the amount for which the asset could be sold in an arm's length transaction. Fair value less costs to sell can be determined by using an observable market or by using discounted future net cash flows of proved and probable reserves using forecasted prices and costs. Value in use is determined by estimating the present value of the future net cash flows expected to be derived from the continued use of the asset or CGU.

Exploration and evaluation assets are grouped together with the Company's CGUs when they are assessed for impairment, both at the time of any triggering facts and circumstances as well as upon their eventual reclassification to producing assets (oil and gas properties).

An impairment loss is recognized if the carrying amount of an asset or its CGU exceeds its estimated recoverable amount. Impairment losses are recognized in profit or loss. Impairment losses recognized in respect of CGUs are allocated first to reduce the carrying amount of goodwill, if any, allocated to the units and then to reduce carrying amounts of other assets in the unit (group of units) on a pro rata basis.

Impairment losses recognized in prior years 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. An impairment loss is reversed 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 or amortization, if no impairment loss had been recognized.

Decommissioning obligations

The Company recognizes the fair value of a provision for a decommissioning obligation in the year in which it is incurred when a reasonable estimate of fair value can be made. The carrying amount of the related long-lived asset is increased by the same amount as the liability. Changes in the liability for a decommissioning obligation due to the passage of time will be measured by applying an interest method of allocation. The amount will be recognized as an increase in the liability and an accretion expense in the consolidated statement of operations. Changes resulting from revisions to the timing or the amount of the original estimate of undiscounted cash flows are recognized as an increase or a decrease to the carrying amount of the liability and the related long-lived asset.

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

Share-based payments

Share-based payments to employees are measured at the fair value of the instruments issued and recognized over the vesting periods. Share-based payments to non-employees are measured at the fair value of the goods or services received or the fair value of the equity instruments issued, if it is determined the fair value of the goods or services cannot be reliably measured, and are recorded at the date the goods or services are received. The offset to the recorded cost is to stock options reserve. Consideration received on the exercise of stock options is recorded as capital stock and the related amount originally recorded in stock options reserve is transferred to capital stock. Upon expiry, related fair value calculated is transferred from stock options reserve to deficit.

Income taxes

The Company uses the financial position method for accounting for income taxes. Under this method of tax allocation, deferred income tax assets and liabilities are determined based on differences between the financial statement carrying values and their respective income tax basis (temporary differences). Deferred income tax assets and liabilities are measured using the tax rates expected to be in effect when the temporary differences are likely to reverse. The effect on deferred income tax assets and liabilities of a change in tax rates is included in operations in the period in which the change is enacted or substantially assured. The amount of deferred income tax assets recognized is limited to the amount of the benefit that is more likely than not to be realized. Deferred income 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.

Capital stock

Proceeds from the issue of units is allocated between common shares and share purchase warrants on a relative fair value basis, based on the fair value of common shares being the market value on the date of announcement of the placement and the value of share purchase warrants, as determined using the Black-Scholes option pricing model.

Basic and diluted loss per share

Basic loss per share is calculated using the weighted average number of common shares outstanding during the year. The Company uses the treasury stock method to compute the dilutive effect of options, warrants and similar instruments. Under this method the dilutive effect on loss per share is calculated presuming the exercise of outstanding options, warrants and similar instruments.

It assumes that the proceeds of such exercise would be used to repurchase common shares at the average market price during the year. However, the calculation of diluted loss per share excludes the effects of various conversions and exercise of options and warrants that would be anti-dilutive.

Shares held in escrow, other than where their release is subject to the passage of time, are not included in the calculation of the weighted average number of common shares outstanding.

Revenue recognition

Revenue from the sale of oil and gas is recorded when title passes to an external party and is based on volumes delivered to customers at contractual delivery points, and rates and collectability are reasonably assured. Delivery is generally at the time the product enters the pipeline. The costs associated with the delivery, including operating and maintenance costs, transportation and production based royalty expenses, are recognized during the same period in which the related revenue is earned and recorded.

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

Joint interest operations

Some of the Company's oil and gas exploration and production activities are conducted jointly with others, and, accordingly, the consolidated financial statements reflect only the Company's proportionate interest in such activities.

New accounting pronouncements

All of the new and revised standards described below may be early-adopted.

IAS 27 *Separate Financial Statements* (2011)

This amended version now only deals with the requirements for separate financial statements, which have been carried over largely unamended from IAS 27 *Consolidated and Separate Financial Statements*. Requirements for consolidated financial statements are now contained in IFRS 10 *Consolidated Financial Statements*.

Applicable to annual periods beginning on or after January 1, 2013. If early-adopted, must be adopted together with IFRS 10, IFRS 11, IFRS 12 and IAS 28 (2011).

IAS 28 *Investments in Associates and Joint Ventures* (2011)

This standard supersedes IAS 28 *Investments in Associates* and prescribes the accounting for investments in associates and sets out the requirements for the application of the equity method when accounting for investments in associates and joint ventures.

The standard defines "significant influence" and provides guidance on how the equity method of accounting is to be applied (including exemptions from applying the equity method in some cases). It also prescribes how investments in associates and joint ventures should be tested for impairment.

Applicable to annual periods beginning on or after January 1, 2013. If early-adopted, must be adopted together with IFRS 10, IFRS 11, IFRS 12 and IAS 27 (2011).

IFRS 9 *Financial Instruments* (2009)

IFRS 9 introduces new requirements for classifying and measuring financial assets, as follows:

- Debt instruments meeting both a "business model" test and a "cash flow characteristics" test are measured at amortized cost (the use of fair value is optional in some limited circumstances)
- Investments in equity instruments can be designated as "fair value through other comprehensive income" with only dividends being recognized in profit or loss
- All other instruments (including all derivatives) are measured at fair value with changes recognized in profit or loss
- The concept of "embedded derivatives" does not apply to financial assets within the scope of the standard and the entire instrument must be classified and measured in accordance with the above guidelines.

This standard is only applicable if it is optionally adopted for annual periods beginning before January 1, 2015. For annual periods beginning on or after January 1, 2015, the Company must adopt IFRS 9 (2010).

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

IFRS 9 *Financial Instruments* (2010)

This is a revised version incorporating revised requirements for the classification and measurement of financial liabilities, and carrying over the existing de-recognition requirements from IAS 39 *Financial Instruments: Recognition and Measurement*.

The revised financial liability provisions maintain the existing amortized cost measurement basis for most liabilities. New requirements apply where an entity chooses to measure a liability at fair value through profit or loss – in these cases, the portion of the change in fair value related to changes in the entity's own credit risk is presented in other comprehensive income rather than within profit or loss.

Applies to annual periods beginning on or after January 1, 2015. This standard supersedes IFRS 9 (2009). However, for annual periods beginning before January 1, 2015, an entity may early-adopt IFRS 9 (2009) instead of applying this standard.

IFRS 10 *Consolidated Financial Statements*

Requires a parent to present consolidated financial statements as those of a single economic entity, replacing the requirements previously contained in IAS 27 *Consolidated and Separate Financial Statements* and SIC-12 *Consolidation - Special Purpose Entities*.

The standard identifies the principles of control, determines how to identify whether an investor controls an investee and therefore must consolidate the investee, and sets out the principles for the preparation of consolidated financial statements.

The standard introduces a single consolidation model for all entities based on control, irrespective of the nature of the investee (i.e., whether an entity is controlled through voting rights of investors or through other contractual arrangements as is common in “special purpose entities”). Under IFRS 10, control is based on whether an investor has power over the investee, exposure, or rights, to variable returns from its involvement with the investee, and the ability to use its power over the investee to affect the amount of the returns.

Applicable to annual periods beginning on or after January 1, 2013. If early-adopted, must be adopted together with IFRS 11, IFRS 12, IAS 27 (2011) and IAS 28 (2011).

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

IFRS 11 ***Joint Arrangements***

Replaces IAS 31 *Interests in Joint Ventures*. Requires a party to a joint arrangement to determine the type of joint arrangement in which it is involved by assessing its rights and obligations and then account for those rights and obligations in accordance with that type of joint arrangement.

Joint arrangements are either joint operations or joint ventures:

- A **joint operation** is a joint arrangement whereby the parties that have joint control of the arrangement (joint operators) have rights to the assets, and obligations for the liabilities, relating to the arrangement. Joint operators recognize their assets, liabilities, revenue and expenses in relation to its interest in a joint operation (including their share of any such items arising jointly)
- A **joint venture** is a joint arrangement whereby the parties that have joint control of the arrangement (joint venturers) have rights to the net assets of the arrangement. A joint venturer applies the equity method of accounting for its investment in a joint venture in accordance with IAS 28 *Investments in Associates and Joint Ventures* (2011). Unlike IAS 31, the use of "proportionate consolidation" to account for joint ventures is not permitted.

Applicable to annual periods beginning on or after January 1, 2013. If early-adopted, must be adopted together with IFRS 10, IFRS 12, IAS 27 (2011) and IAS 28 (2011).

IFRS 12 ***Disclosure of Interests in Other Entities***

Requires the extensive disclosure of information that enables users of financial statements to evaluate the nature of, and risks associated with, interests in other entities and the effects of those interests on its financial position, financial performance and cash flows.

In high-level terms, the required disclosures are grouped into the following broad categories:

- **Significant judgments and assumptions** - such as how control, joint control, significant influence has been determined
- **Interests in subsidiaries** - including details of the structure of the group, risks associated with structured entities, changes in control, and so on
- **Interests in joint arrangements and associates** - the nature, extent and financial effects of interests in joint arrangements and associates (including names, details and summarized financial information)
- **Interests in unconsolidated structured entities** - information to allow an understanding of the nature and extent of interests in unconsolidated structured entities and to evaluate the nature of, and changes in, the risks associated with its interests in unconsolidated structured entities

IFRS 12 lists specific examples and additional disclosures which further expand upon each of these disclosure objectives, and includes other guidance on the extensive disclosures required.

Applicable to annual periods beginning on or after January 1, 2013. If early-adopted, must be adopted together with IFRS 10, IFRS 11, IAS 27 (2011) and IAS 28 (2011).

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

IFRS 13 *Fair Value Measurement*

Replaces the guidance on fair value measurement in existing IFRS accounting literature with a single standard.

This IFRS defines fair value, provides guidance on how to determine fair value and requires disclosures about fair value measurements. However, IFRS 13 does not change the requirements regarding which items should be measured or disclosed at fair value.

IFRS 13 applies when another IFRS requires or permits fair value measurements or disclosures about fair value measurements (and measurements, such as fair value less costs to sell, based on fair value or disclosures about those measurements). With some exceptions, the standard requires entities to classify these measurements into a "fair value hierarchy" based on the nature of the inputs:

- **Level 1** - quoted prices in active markets for identical assets or liabilities that the entity can access at the measurement date
- **Level 2** - inputs other than quoted market prices included within Level 1 that are observable for the asset or liability, either directly or indirectly
- **Level 3** - unobservable inputs for the asset or liability

Entities are required to make various disclosures depending upon the nature of the fair value measurement (e.g., whether it is recognized in the financial statements or merely disclosed) and the level in which it is classified.

Applicable to annual periods beginning on or after January 1, 2013.

IAS 19 *Employee Benefits* (2011)

This is an amended version with revised requirements for pensions and other post-retirement benefits, termination benefits and other changes.

The key amendments include:

- Requiring the recognition of changes in the net defined benefit liability (asset) including immediate recognition of defined benefit cost, disaggregation of defined benefit cost into components, recognition of re-measurements in other comprehensive income, plan amendments, curtailments and settlements (eliminating the "corridor approach" permitted by the existing IAS 19)
- Introducing enhanced disclosures about defined benefit plans
- Modifying accounting for termination benefits, including distinguishing benefits provided in exchange for service and benefits provided in exchange for the termination of employment and affect the recognition and measurement of termination benefits
- Clarifying various miscellaneous issues, including the classification of employee benefits, current estimates of mortality rates, tax and administration costs and risk-sharing and conditional indexation features
- Incorporating other matters submitted to the IFRIC.

Applicable to annual periods beginning on or after January 1, 2013.

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

Presentation of Items of Other Comprehensive Income **(Amendments to IAS 1)**

Amends IAS 1 *Presentation of Financial Statements* to revise the way other comprehensive income is presented.

The amendments:

- Preserve the amendments made to IAS 1 in 2007 to require profit or loss and other comprehensive income to be presented together, i.e., either as a single "statement of profit or loss and comprehensive income", or a separate "statement of profit or loss' and a 'statement of comprehensive income" – rather than requiring a single continuous statement as was proposed in the exposure draft
- Require entities to group items presented in other comprehensive income based on whether they are potentially reclassifiable to profit or loss subsequently, i.e., those that might be reclassified and those that will not be reclassified
- Require tax associated with items presented before tax to be shown separately for each of the two groups of other comprehensive income items (without changing the option to present items of other comprehensive income either before tax or net of tax).

Applicable to annual periods beginning on or after July 1, 2012.

Disclosures — Offsetting Financial Assets and Financial Liabilities **(Amendments to IFRS 7)**

Amends the disclosure requirements in IFRS 7 *Financial Instruments: Disclosures* to require information about all recognized financial instruments that are set-off in accordance with paragraph 42 of IAS 32 *Financial Instruments: Presentation*.

The amendments also require disclosure of information about recognized financial instruments subject to enforceable master netting arrangements and similar agreements even if they are not set off under IAS 32.

Applicable to annual periods beginning on or after January 1, 2013 and interim periods within those periods.

Offsetting Financial Assets and Financial Liabilities **(Amendments to IAS 32)**

Amends IAS 32 *Financial Instruments: Presentation* to clarify certain aspects because of diversity in application of the requirements on offsetting, focused on four main areas:

- the meaning of "currently has a legally enforceable right of set-off"
- the application of simultaneous realization and settlement
- the offsetting of collateral amounts
- the unit of account for applying the offsetting requirements.

Applicable to annual periods beginning on or after January 1, 2014.

3. SIGNIFICANT ACCOUNTING POLICIES (Continued)

Annual Improvements 2009-2011 Cycle

Makes amendments to the following standards:

- **IFRS 1** — Permit the repeated application of IFRS 1, borrowing costs on certain qualifying assets
- **IAS 1** — Clarification of the requirements for comparative information
- **IAS 16** — Classification of servicing equipment
- **IAS 32** — Clarify that tax effect of a distribution to holders of equity instruments should be accounted for in accordance with IAS 12 *Income Taxes*
- **IAS 34** — Clarify interim reporting of segment information for total assets in order to enhance consistency with the requirements in IFRS 8 *Operating Segments*

Applicable to annual periods beginning on or after January 1, 2013.

Consolidated Financial Statements, Joint Arrangements and Disclosure of Interests in Other Entities: Transition Guidance

Amends IFRS 10 *Consolidated Financial Statements*, IFRS 11 *Joint Arrangements* and IFRS 12 *Disclosure of Interests in Other Entities* to provide additional transition relief by limiting the requirement to provide adjusted comparative information to only the preceding comparative period. Also, amendments to IFRS 11 and IFRS 12 eliminate the requirement to provide comparative information for periods prior to the immediately preceding period.

Applicable to annual periods beginning on or after January 1, 2013.

4. ADVANCES FOR FUTURE EXPLORATION

The Company owns varying interests in oil and gas properties subject to joint operating agreements, which provide, among other things, that the Company make advance payments from time to time to fund estimated exploration and evaluation costs. The amount of funds advanced, less the Company's share of actual costs incurred by the project operators, was $459,008 at January 31, 2013 (2012 - $1,209,163), which consists of advances for future exploration on the Company's STS Olmos project. The advances made as at January 31, 2012 were reclassified to conform to the current period presentation.

5. EXPLORATION AND EVALUATION ASSETS

	Los Patos	STS Olmos	Cutlass	Total
Balance - January 31, 2011	**$ -**	**$ -**	**$ -**	**$ -**
Acquisition costs	-	1,000,000	367,666	1,367,666
Exploration and evaluation	369,410	65,526	194,047	628,983
Impairment charge	(229,447)	-	-	(229,447)
Incidental sales	(4,963)	(7,418)	-	(12,381)
Expenditures during the year	135,000	1,058,108	561,713	1,754,821
Balance - January 31, 2012	**135,000**	**1,058,108**	**561,713**	**1,754,821**
Acquisition costs	-	1,269	1,362,343	1,363,612
Exploration and evaluation	-	6,732,483	3,842,044	10,574,527
Transfer to property and equipment	-	(6,820,921)	-	(6,820,921)
Impairment charge	(135,000)	-	-	(135,000)
Expenditures during the year	(135,000)	(87,169)	5,204,387	4,982,218
Balance - January 31, 2013	**$ -**	**$ 970,939**	**$ 5,766,100**	**$ 6,737,039**

Los Patos

In June 2011, the Company entered into an agreement to earn, through a wholly-owned subsidiary, an 87.5% working interest and a 65.187% net revenue interest in certain leases and farm-out lands in Wharton County, Texas, by funding all costs associated with the re-fracture, stimulation and completion of an existing, primarily gas, well. The Company fulfilled its obligations under the agreement in 2011 and earned its interests in all of the project acreage. The well ceased production in October 2012, and the Company made the decision to abandon the well and allow the mineral leases to terminate. As a result, the Company incurred an impairment charge of $135,000 during the current period.

STS Olmos

In November 2011, the Company entered into an agreement, through a wholly-owned subsidiary, to acquire varying working and net revenue interests, which average 26.88% and 20.16%, respectively, in LaSalle and McMullen counties, Texas, and an evaluation well. The purchase price was $1,000,000.

The Company's share of the aggregate costs during the period, to drill, complete and place into production three wells was $6,760,921. These costs and $60,000 of the acreage lease acquisition cost were transferred from "exploration and evaluation assets" to "property and equipment".

The Company has secured its working and net revenue interests in all of the project acreage subject to participation in the development of additional wells proposed from time to time by the project's operator. The Company and the operator have formulated a project development plan for fiscal 2014.

Cutlass

In November 2011, the Company entered into an agreement, through a wholly-owned subsidiary, to earn a 25% working interest and an 18.75% net revenue interest in certain leases in Dimmit and LaSalle counties, Texas, for $367,666 and a commitment to participate in a two-well drilling program. In February 2012, the Company acquired an additional 5% working interest and 3.75% net revenue interest for an additional $234,097.

5. EXPLORATION AND EVALUATION ASSETS (Continued)

In order to earn the net revenue interests (22.5% in aggregate), the Company agreed to pay 33.33% of all costs, including acreage leases, prospect fees, site preparation and drilling, until the completion of two wells, and thereafter 30% of all costs relating to the lease payments, prospect fees and infrastructure costs (the "Dimmit County Acreage").

Drilling of the first well on the Dimmit County Acreage was substantially completed in June 2012. The Company's share of well and infrastructure costs to January 31, 2013 was $2,797,291. The Company expects the well to be fracture stimulated and, if successful, placed into production at an estimated cost to the Company of $1,604,500.

The Company must participate in the development of a second well on the Dimmit County Acreage at an estimated cost of $1,190,333. Work on this well is currently scheduled for the second quarter of calendar 2013.

After the drilling and technical evaluation of the first well on the Dimmit County Acreage, the Company exercised its option to earn a 22.5% net revenue interest (the "LaSalle County Acreage") at a cost of $570,462. The Company was obligated to fund 33.33% of the cost of an initial well on the La Salle County Acreage.

Drilling of the initial well commenced in late June 2012. A vertical hole was completed and results are under analysis. Completion plans for this well and plans for additional development wells will be formulated during the first quarter of 2014 based on analysis of petrophysical and geological information gathered from the well. The Company's share of well and infrastructure costs to January 31, 2013 was $1,783,338.

6. PROPERTY AND EQUIPMENT

Cost	**Other Equipment**	**Oil and Gas**	**Total**
Balance – January 31, 2012 and 2011	$ **-**	$ **-**	$ **-**
Additions	63,597	-	63,597
Transfer from exploration and evaluation	-	6,820,921	6,820,921
Change in value of decommissioning obligations	-	7,294	7,294
Balance – January 31, 2013	$ **63,597**	$ **6,828,215**	$ **6,891,812**

Accumulated depreciation and depletion	**Other Equipment**	**Oil and Gas**	**Total**
Balance – January 31, 2012 and 2011	$ **-**	$ **-**	$ **-**
Charge for year	11,274	833,010	844,284
Balance – January 31, 2013	$ **11,274**	$ **833,010**	$ **844,284**

Net book value	**Other Equipment**	**Oil and Gas**	**Total**
Balance – January 31, 2012	$ **-**	$ **-**	$ **-**
Balance – January 31, 2013	$ **52,323**	$ **5,995,205**	$ **6,047,528**

7. DECOMMISSIONING OBLIGATIONS

The Company's decommissioning obligations result from its ownership interest in oil and gas assets including well sites and gathering systems. The total decommissioning obligation is 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.

		2013		2012
Balance, beginning of the year	$	-	$	-
Increase in estimated future obligations		7,294		-
Accretion expense		722		-
Balance, end of the year	$	8,016	$	-

8. CAPITAL STOCK

On January 31, 2013, the Company had unlimited authorized common shares, without par value and 63,069,321 (2012 - 52,919,321) shares outstanding.

Share issues

During the year ended January 31, 2013, the Company issued common shares as follows:

a) In May 2012, the Company closed a private placement of 10,000,000 common shares at a purchase price of $1.00 per share for gross proceeds of CAD $10,000,000. Share issue costs of CAD $48,670 were paid in relation to the private placement.

b) In July 2012, the Company issued 150,000 common shares on the exercise of stock options at an exercise price of $0.12 per share for gross proceeds of CAD $18,000.

During the year ended January 31, 2012, the Company issued common shares as follows:

a) In June 2011, the Company closed a private placement of 10,000,000 units at a purchase price of $0.09 per unit for gross proceeds of CAD $900,000. Each unit consisted of one common share and one common share purchase warrant, which entitled the holder to acquire one additional common share for a period of five years at an exercise price of $0.18.

   The Company allocated CAD $544,200 of the subscription proceeds to capital stock and CAD $355,800 to warrant reserve based on their relative fair values as of the placement announcement date. The valuation of the warrants was estimated using the Black-Scholes valuation model with a weighted expected volatility of 100%, risk-free interest rate of 2.19%, expected life of 5 years and a dividend yield of 0%. The Company paid CAD $56,264 of share issue costs in relation to the private placement.

b) In December 2011, the Company closed a private placement of 9,000,000 common shares at a purchase price of $0.25 per share for gross proceeds of CAD $2,250,000.

8. CAPITAL STOCK (Continued)

Restricted shares and warrants

Of the common shares issued, 11,184,345 are subject to an escrow agreement and may not be transferred without the consent of the Exchange. The escrow agreement provides, among other things, that a total of 3,827,115 common shares will be released from escrow on June 23, 2013 and the same amount will be released every six months thereafter, until such time all such shares are released from escrow.

Of the common shares underlying the outstanding warrants, 2,587,500 are subject to an escrow agreement and cannot be transferred without the consent of the Exchange. The escrow agreement provides that a total of 862,500 warrants will be released from escrow on June 23, 2013 and the same amount will be released every six months thereafter, until such time all such shares are released from escrow.

Included in the issued common shares and warrants are 2,250,000 common shares and 1,350,000 warrants that are subject to a voluntary pooling agreement. The agreement provides that 750,000 common shares and 450,000 warrants will be released from trading restrictions on June 23, 2013 and the same amount will be released every six months thereafter, until such time all such shares are free of trading restrictions.

Stock options

The Company has an incentive stock option plan, which provides that the Board of Directors of the Company may from time to time, in its discretion, and in accordance with Exchange requirements, grant to directors, officers, employees and technical consultants to the Company, non-transferable options to purchase common shares, provided that the number of common shares reserved for issuance will not exceed 10% of the issued and outstanding common shares. The number of common share reserves for issuance pursuant to options granted to all technical consultants will not exceed 2% of the issued and outstanding common shares. The number of options granted to any one person cannot exceed 5% of the issued and outstanding common shares. Such options may be exercisable for a period of up to 10 years from the date of grant. Vesting terms will be determined at the time of grant by the Board of Directors.

Share-based payments

The Company uses a fair value method of accounting for all share-based payments arising from the grant of stock options. Under this method, the Company recorded share-based payments expense of $393,100 (2012 - $280,173) for the year ended January 31, 2013, with a corresponding credit to reserves. The fair value of the stock options granted during the year ended January 31, 2013 is estimated as at the date of grant using the Black-Scholes pricing model assuming the following weighted average assumptions:

	2013	2012
Risk-free interest rate	1.16%	1.18%-2.19%
Expected life	5 years	5 years
Annualized volatility	107.49%	100.0%
Pre-vest forfeiture rate	0%	0%
Dividend rate	0%	0%

During the year ended January 31, 2013, the Company granted 150,000 (2012 - 3,050,000) options with a fair value of $150,185 (2012 - $594,473), which is being expensed over the vesting periods of the options.

8. CAPITAL STOCK (Continued)

Outstanding stock options and warrants

Stock option transactions and the number of stock options outstanding are summarized as follows:

	Number of Stock Options	Weighted Average Exercise Price (CAD)
Balance - January 31, 2011	-	$ -
Granted	3,050,000	$ 0.20
Exercised	(150,000)	$ 0.12
Balance - January 31, 2012	2,900,000	$ 0.20
Granted	150,000	$ 1.35
Exercised	(150,000)	$ 0.12
Balance - January 31, 2013	2,900,000	$ 0.27

The following stock options were outstanding as at January 31, 2013:

Number of Options	Number of Options Exercisable	Exercise Price (CAD)	Expiry Date	Weighted Average Remaining Contractual Life (Years)
1,650,000	1,650,000	$ 0.12	June 22, 2016	3.39
250,000	137,500	$ 0.19	July 15, 2016	3.45
250,000	100,000	$ 0.21	September 16, 2016	3.60
250,000	100,000	$ 0.19	October 18, 2016	3.72
100,000	60,000	$ 0.53	November 25, 2016	3.82
250,000	100,000	$ 0.67	December 16, 2016	3.88
150,000	37,500	$ 1.35	July 8, 2017	4.44
2,900,000	2,185,000			3.55

8. CAPITAL STOCK (Continued)

The following stock options were outstanding as at January 31, 2012:

Number of Options	Number of Options Exercisable	Exercise Price (CAD)	Expiry Date	Weighted Average Remaining Contractual Life (Years)
1,800,000	1,800,000	$ 0.12	June 22, 2016	4.39
250,000	62,500	$ 0.19	July 15, 2016	4.45
250,000	25,000	$ 0.21	September 16, 2016	4.60
250,000	25,000	$ 0.19	October 18, 2016	4.72
100,000	20,000	$ 0.53	November 25, 2016	4.82
250,000	25,000	$ 0.67	December 16, 2016	4.88
2,900,000	1,957,500			4.50

Warrant transactions and the number of warrants outstanding are summarized as follows:

	Number of Warrants	Weighted Average Exercise Price (CAD)	Expiry Date
Balance - January 31, 2011	-	-	
Issued	10,000,000	$ 0.18	June 21, 2016
Exercised	(2,887,500)	$ 0.18	
Balance - January 31, 2012 and 2013	7,112,500	$ 0.18	

9. FINANCIAL INSTRUMENTS

The Company has classified its financial instruments as follows:

- Cash – as FVTPL;
- Accounts receivable and operators bond – as loans and receivables; and
- Accounts payable and accrued liabilities – as other financial liabilities.

The Company's risk exposure and the impact on the Company's financial instruments are summarized below:

Fair value

The carrying values of cash, accounts receivable, and accounts payable and accrued liabilities approximate their fair values due to the short-term maturity of these financial instruments. The fair value of the operators bond also approximates its carrying value.

Credit risk

Credit risk is the risk of potential loss to the Company if the counterparty to a financial instrument fails to meet its contractual obligations.

The Company's credit risk is primarily attributable to its cash and accounts receivable. The credit risk associated with cash is mitigated since the cash is held at major financial institutions with high credit ratings. Accounts receivable consists primarily of trade receivables outstanding from operators of its oil and gas interests. To mitigate this risk, the Company regularly reviews the collectability of accounts receivable to ensure there is no indication that these amounts will not be fully recoverable.

Market risk

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate due to changes in the market prices. Market risk is comprised of three types of risk: interest rate risk, foreign currency risk and other price risk.

(i) Interest rate risk

To the extent that payments made or received on the Company's monetary assets and liabilities are affected by changes in prevailing market interest rates, the Company is exposed to interest rate cash flow risk.

To the extent that changes in prevailing market interest rates differ from the interest rates in the Company's monetary assets and liabilities, the Company is exposed to interest rate price risk.

The Company's exposure to interest rate risk is minimal.

(ii) Foreign currency risk

Foreign currency risk is the risk that the future cash flow of financial instruments will fluctuate as a result of changes in foreign exchange rates. The Company's financing is raised in CAD, but a portion of the Company's operations is conducted in USD. Therefore, the Company is impacted by changes in the exchange rate between the Canadian and US dollars.

9. FINANCIAL INSTRUMENTS (Continued)

Market risk (Continued)

(ii) Foreign currency risk (Continued)

The following assets and liabilities represent the Company's exposure to foreign currency risk:

		2013 (USD)		**2012 (USD)**
Cash	$	1,502,509	$	110,408
Accounts receivable		1,302,356		3,707
Operators bond		25,000		25,000
Accounts payable and accrued liabilities		(483,690)		(145,134)
Net	$	2,346,275	$	(6,019)
Canadian dollar equivalent	CAD$	2,344,399	CAD$	(6,050)

Based on the above net exposures as at January 31, 2013, a 5% change in the Canadian/US exchange rate would impact the Company's net loss and comprehensive loss by approximately $117,000.

(iii) Other price risk

Other price risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate due to changes in the market prices, other than those arising from interest rate risk or foreign currency risk. The Company is not exposed to significant other price risk.

Liquidity risk

Liquidity risk is the risk that the Company will encounter difficulty in satisfying financial obligations as they become due. The Company manages liquidity risk through maintaining sufficient cash on hand to meet its obligations as they become due. As at January 31, 2013, the Company had cash of $1,673,449, accounts receivable of $1,327,511 and accounts payable and accrued liabilities of $571,585 due within three months of year-end.

The Company owns varying interests in oil and gas properties subject to joint operating agreements, which provide, among other things, that the Company make advance payments from time to time to fund its share of estimated exploration and evaluation costs. The Company may not have sufficient working capital and future cash flow from operations to fund its share of the agreed-upon estimated costs of proposed development activities. As a consequence, the Company may have to secure new sources of capital, which is not assured, to maintain its interests in such proposed development.

10. CAPITAL DISCLOSURES

The Company considers its capital under management to be shareholders' equity. The Company's capital management objectives are to ensure the Company continues as a going concern, as well as to maintain optimal returns to shareholders and benefits for other stakeholders. The Board of Directors does not establish quantitative criteria for management, but rather relies on management expertise to sustain future development. Management will adjust the capital structure as necessary to achieve the objectives.

The Company's capital management strategy has not changed from January 31, 2012. As at January 31, 2013, the Company is not subject to any externally imposed capital requirements.

11. COMMITMENT

The Company has a commitment to make monthly rental payments pursuant to an office rental agreement. The agreement expires June 30, 2014 and will require total payments in the remaining fiscal years of $72,183 for January 31, 2014 and $30,076 for January 31, 2015.

12. RELATED PARTY TRANSACTIONS

Key management personnel include executive officers and directors of the Company. Compensation of the Company's key management personnel is comprised of the following:

	2013	2012
Short-term compensation	$ 390,865	$ 187,238
Share-based payments	56,648	207,236
	$ 447,513	$ 394,474

As at January 31, 2013:

(a) Included in accounts receivable are advances to key management personnel totalling $21,230 (2012 - $nil).

(b) Included in accounts payable and accrued liabilities are amounts payable to key management personnel totalling $42,368 (2012 - $42,394).

During the year, the Company:

(a) Entered into an employment agreement dated May 1, 2012 with the President of the Company providing a base salary of $300,000 per annum.

(b) Paid or accrued legal fees and share issue costs totalling $56,013 (2012 - $175,924) to a law firm of which the former corporate secretary of the Company is a principal.

13. SEGMENTED INFORMATION

The Company has one operating segment, which is the acquisition and exploration of oil and gas properties. Geographic segmentation of the Company's non-current assets is as follows:

	2013		
	USA	**Canada**	**Total**
Advances for future exploration	$ 459,008	$ -	$ 459,008
Exploration and evaluation assets	6,737,039	-	6,737,039
Property and equipment	6,047,528	-	6,047,528
	$ 13,243,575	$ -	$ 13,243,575

	2012		
	USA	**Canada**	**Total**
Advances for future exploration	$ 1,209,163	$ -	$ 1,209,163
Exploration and evaluation assets	1,754,821	-	1,754,821
	$ 2,963,984	$ -	$ 2,963,984

The Company's operating expenses are incurred evenly between the US and Canada. Exploration and development activities are located in the US and oil and gas revenues are in the US.

14. SUPPLEMENTAL CASH FLOW INFORMATION

During the year ended January 31 2013, the Company:

(a) transferred $6,820,921 from exploration and evaluation assets to property and equipment;

(b) transferred $13,532 from equity reserve to capital stock on the exercise of the stock options; and

(c) had accounts payable and accrued liabilities of $437,045 related to exploration and evaluation expenditures.

During the year ended January 31, 2012, the Company:

(a) transferred $103,663 from equity reserve to capital stock on the exercise of the warrants;

(b) transferred $13,622 from equity reserve to capital stock on the exercise of the stock options; and

(c) had accounts payable and accrued liabilities of $101,709 related to exploration and evaluation expenditures.

15. INCOME TAXES

(a) Income tax expense differs from the amount that would be computed by applying the Canadian statutory income tax rate of 25.0% (2012 - 26.5%) to income before income taxes. The reasons for the differences are as follows:

		2013		2012
Loss before tax	$	(121,722)	$	(1,265,463)
Statutory income tax rate		25.0%		26.50%
Expected income tax		(30,430)		(335,348)
Items not deductible for tax purposes		107,994		74,245
Temporary differences		32,136		(25,524)
Effect of change in tax rates		11,691		-
Changes in unrecognized deferred income tax assets		(121,391)		286,627
	$	-	$	-

(b) The Company recognizes tax benefits on losses or other deductible amounts generated in countries where the probable criteria for the recognition of deferred tax assets has been met.

The significant components of the Company's deferred tax assets and liabilities are as follows:

		2013		2012
Non-capital losses	$	249,010	$	69,297
Resource properties		(249,010)		(69,297)
	$	-	$	-

The US tax loss carry-forward of $721,243 expires in 2032 and is recognized above.

As at January 31, 2013, the unrecognized deductible temporary differences consist of Canadian tax losses with the following expiry dates:

2027	$	10,176
2028		29,833
2029		75,237
2030		120,741
2031		133,774
2032		236,179
2033		318,761
	$	924,701

16. EVENTS AFTER THE REPORTING PERIOD

Subsequent to year-end, the Company announced:

(a) The completion of a non-brokered private placement of convertible, unsecured promissory notes in the aggregate principal amount of CAD $25,000,000. The convertible notes have a term of five years, earn 8% per annum and have a conversion price of $2.00 per share. The Company paid a 5% finder's fee in the aggregate amount of CAD $704,250.

(b) It decided not to exercise the option to acquire certain mineral leases in Finney County, Kansas. The non-refundable option payment of $225,150 made in December 2012 was expensed as project investigation costs.

(c) The Exchange's approval of a binding agreement with BlackBrush Oil & Gas, LP to organize a special purpose limited partnership to acquire a 50% working interest in certain oil and gas leases in south Texas, USA. In March 2013, the Company paid a deposit of $1,500,000 pursuant to the agreement.