

Terra Energy Corp.

Consolidated Financial Statements

For the three and six months ended June 30, 2008

Consolidated Balance Sheets

| AS AT JUNE 30 AND DECEMBER 31 (UNAUDITED) | 2008 | 2007 |
|---|-----------------------|-----------------------|
| Assets | | |
| Current | | |
| Cash and cash equivalents | \$ 11,304,130 | \$ – |
| Accounts receivable | 7,849,247 | 7,960,046 |
| Prepaid expenses | 877,763 | 1,076,879 |
| Future income taxes | 3,853,882 | – |
| | 23,885,022 | 9,036,925 |
| Oil and gas properties | 104,967,264 | 157,024,959 |
| | \$ 128,852,286 | \$ 166,061,884 |
| Liabilities and Shareholders' Equity | | |
| Current | | |
| Bank overdraft (NOTE 5) | \$ 2,844,948 | \$ 1,828,943 |
| Accounts payable and accrued liabilities | 10,585,553 | 21,485,964 |
| Asset retirement obligation | 337,172 | 398,798 |
| Financial instruments (NOTE 3) | 12,846,273 | 567,483 |
| | 26,613,946 | 24,281,188 |
| Deferred credit | 149,460 | 182,670 |
| Long-term financing (NOTE 5) | – | 54,631,003 |
| Asset retirement obligation | 5,023,312 | 5,166,555 |
| Future income taxes | 20,032,121 | 12,933,520 |
| | 51,818,839 | 97,194,936 |
| Shareholders' Equity | | |
| Share capital and warrants (NOTE 6) | 68,571,949 | 65,195,721 |
| Contributed surplus (NOTE 7) | 9,826,949 | 9,365,272 |
| Deficit | (1,365,451) | (5,694,045) |
| | 77,033,447 | 68,866,948 |
| | \$ 128,852,286 | \$ 166,061,884 |

Approved on behalf of the Board:



Theodore Anderson, Director



Robert Penner, Director

Consolidated Statements of Operations, Comprehensive Income (Loss) and Deficit

For the three months and six months ended June 30 (unaudited)

| | THREE MONTHS ENDED JUNE 30 | | SIX MONTHS ENDED JUNE 30 | |
|---|----------------------------|-----------------------|--------------------------|-----------------------|
| | 2008 | 2007 | 2008 | 2007 |
| Revenue | | | | |
| Petroleum and natural gas | \$ 20,807,645 | \$ 12,268,331 | \$ 41,063,056 | \$ 22,652,456 |
| Realized gain (loss) on financial instruments (Note 3) | (614,727) | 265,801 | (868,864) | 574,894 |
| Unrealized gain (loss) on financial instruments (Note 3) | (9,243,546) | 978,907 | (12,278,790) | (1,867,739) |
| | 10,949,372 | 13,513,039 | 27,915,402 | 21,359,611 |
| Royalties | (4,279,537) | (2,533,942) | (9,018,978) | (4,756,647) |
| | 6,669,835 | 10,979,097 | 18,896,424 | 16,602,964 |
| Expenses | | | | |
| Production | 3,752,789 | 3,485,514 | 8,464,519 | 6,605,843 |
| General and administrative | 1,259,463 | 983,357 | 2,279,708 | 2,232,412 |
| Accretion of asset retirement obligation | 113,457 | 111,517 | 232,428 | 223,034 |
| Stock based compensation | 1,513,147 | 552,877 | 1,976,320 | 869,728 |
| Depletion and amortization | 4,704,465 | 3,912,799 | 10,901,118 | 7,288,313 |
| Interest on long-term debt | 369,301 | 854,725 | 1,251,833 | 1,490,101 |
| Unrealized foreign exchange loss | 18 | — | 336,438 | — |
| Realized foreign exchange loss | — | — | 6,740 | — |
| | 11,712,640 | 9,900,789 | 25,449,104 | 18,709,431 |
| Income (loss) before income taxes and other income | (5,042,805) | 1,078,308 | (6,552,680) | (2,106,467) |
| Gain on disposition of P&NG rights (Note 9) | 14,478,281 | — | 14,478,281 | — |
| Income (loss) before income taxes | 9,435,476 | 1,078,308 | 7,925,601 | (2,106,467) |
| Income tax expense (recovery) | | | | |
| Current tax | — | — | 3,605 | — |
| Future tax | 3,657,296 | 459,445 | 3,244,719 | (556,914) |
| | 3,657,296 | 459,445 | 3,248,324 | (556,914) |
| Net income (loss) and comprehensive income (loss) for the period | 5,778,180 | 618,863 | 4,677,277 | (1,549,553) |
| Deficit, beginning of period | (7,143,631) | (5,817,397) | (5,694,045) | (3,477,604) |
| Repurchase of common shares (Note 6) | — | (107,818) | (348,683) | (279,195) |
| Deficit, end of period | \$ (1,365,451) | \$ (5,306,352) | \$ (1,365,451) | \$ (5,306,352) |
| Income (loss) per share (Note 6) | | | | |
| Basic | \$ 0.08 | \$ 0.01 | \$ 0.06 | \$ (0.02) |
| Diluted | \$ 0.08 | \$ 0.01 | \$ 0.06 | \$ (0.02) |

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

Consolidated Statements of Cash Flows

For the three months and six months ended June 30 (unaudited)

| | THREE MONTHS ENDED JUNE 30 | | SIX MONTHS ENDED JUNE 30 | |
|--|----------------------------|-------------|--------------------------|----------------|
| | 2008 | 2007 | 2008 | 2007 |
| Cash flows from operating activities | | | | |
| Net income (loss) for the period | \$ 5,778,180 | \$ 618,863 | \$ 4,677,277 | \$ (1,549,553) |
| Items not affecting cash: | | | | |
| Future income taxes | 3,657,296 | 459,445 | 3,244,719 | (556,914) |
| Accretion | 113,457 | 111,517 | 232,428 | 223,034 |
| Stock based compensation | 1,513,147 | 552,877 | 1,976,320 | 869,728 |
| Unrealized loss (gain) on financial instruments (Note 3) | 9,243,546 | (978,907) | 12,278,790 | 1,867,739 |
| Unrealized loss on foreign exchange | 18 | — | 336,438 | — |
| Gain on disposition of P&NG rights | (14,478,281) | — | (14,478,281) | — |
| Asset retirement obligations settled | (62,154) | — | (156,667) | — |
| Amortization of deferred credit | (16,605) | (16,605) | (33,210) | (33,211) |
| Depletion and amortization | 4,704,465 | 3,912,799 | 10,901,118 | 7,288,313 |
| | 10,453,069 | 4,659,989 | 18,978,932 | 8,109,136 |
| Changes in non-cash working capital from operations (Note 8) | 2,248,869 | (2,275,508) | (3,369,127) | (2,438,006) |
| | 12,701,938 | 2,384,481 | 15,609,805 | 5,671,130 |
| Cash flows from financing activities | | | | |
| Proceeds from (repayment of) long-term financing | (58,173,297) | 3,788,204 | (54,967,441) | 15,426,162 |
| Increase (decrease) in bank overdraft | (177,895) | 3,148,176 | 1,016,005 | (3,501,766) |
| Issuance of common shares, net of issuance costs | 1,758,889 | 92,880 | 2,525,937 | 89,755 |
| Repurchase of common shares | — | (299,572) | (1,013,035) | (2,066,643) |
| | (56,592,303) | 6,729,688 | (52,438,534) | 9,947,508 |
| Cash flows from investing activities | | | | |
| Additions to oil and gas properties | (5,252,716) | (4,131,449) | (14,522,340) | (12,568,422) |
| Disposition of oil and gas properties | 63,863,482 | — | 69,876,568 | — |
| Changes in non-cash working capital from investing (Note 8) | (3,416,271) | (4,982,720) | (7,221,369) | (3,050,216) |
| | 55,194,495 | (9,114,169) | 48,132,859 | (15,618,638) |
| Increase in cash and cash equivalents | 11,304,130 | — | 11,304,130 | — |
| Cash and cash equivalents, beginning of period | — | — | — | — |
| Cash and cash equivalents, end of period | 11,304,130 | — | 11,304,130 | — |

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

Notes to Consolidated Financial Statements

NOTE. 1 **Basis of Presentation**

The interim financial statements of Terra Energy Corp. (the "Company") have been prepared by management in accordance with Canadian generally accepted accounting principles and are consistent with the presentation and disclosure in the audited consolidated financial statements and notes thereto for the year ended December 31, 2007 except for the changes described in note 2. The interim consolidated financial statements do not conform in all respects to the requirements of GAAP for annual financial statements. These interim consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto for the year ended December 31, 2007

The preparation of interim financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the interim financial statements and accompanying notes. Actual results could differ from those estimates. The interim financial statements have, in management's opinion, been properly prepared using careful judgements within reasonable limits of materiality.

NOTE. 2 **Adoption of New Policies**

Financial Instruments

On January 1, 2008, the Company adopted the following new CICA Handbook Sections, which were effective for interim periods beginning on or after October 1, 2007:

Section 3862 – "Financial Instruments – Disclosures", describes the required disclosure for the assessment of the significance of financial instruments to an entity's financial position and performance and of the nature and extent of risks arising from financial instruments to which the entity is exposed and how the entity manages those risks. This section and Section 3863, "Financial Instruments – Presentation" replaced Section 3861, "Financial Instruments – Disclosure and Presentation".

Section 3863 – "Financial Instruments – Presentation", establishes standards for presentation of financial instruments and non-financial derivatives.

Section 1535 – "Capital Disclosures", establishes standards for disclosing information about an entity's capital and how it is managed. It describes the disclosure requirements of the entity's objectives, policies and processes for managing capital, the quantitative data relating to what the entity regards as capital, whether the entity has complied with capital requirements, and, if it has not complied, the consequences of such non-compliance.

The CICA has amended Section 1400, "General Standards of Financial Statement Presentation", which is effective for interim periods beginning on or after January 1, 2008, to include requirements to assess and disclose the Company's ability to continue as a going concern. The adoption of this new section will not have an impact on the financial statements.

NOTE. 3 Financial and Capital Management

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

Credit Risk

Credit risk arises when a failure by counter parties to discharge their obligations could reduce the amount of future cash inflows from financial assets on hand at the balance sheet date. The Company's accounts receivable at the balance sheet date arise from crude oil, natural gas liquids and natural gas sales. Industry standard dictates that commodity sales are settled on the 25th day of the month following the month of production. The Company markets its oil and natural gas to several marketers so that the exposure to any one entity is minimized. In addition, when joint operations are conducted on behalf of a joint venture partner relating to capital expenditures, costs of such operations are paid for in advance to the Company by way of a cash call by the partner of the operation being conducted.

Joint venture receivables are generated from conducting joint operating or capital operations with joint venture partners. Collections from these operations are usually paid within three months of the joint venture bill being issued to the partner. Circumstances can arise which extend the terms of collection beyond this period as specific items on these joint venture billings need to be resolved between partners. Smaller partners may be cash called to pay for their share of costs in advance of a project. The Company has the ability to take measures such as withholding production volumes as recourse for collections on receivables as well. The Company monitors receivables accounts and actively pursues collection and payment. If any accounts are considered impaired they will be charged to an allowance for doubtful accounts. At June 30, 2008 no allowance for doubtful accounts was recorded.

The Company assesses quarterly if there should be any impairment of the financial assets of the Company. During the three and six month periods ended June 30, 2008 there was no impairment required on any of the financial assets of the Company due to historical success of collecting receivables. The Company does not have any significant credit risk exposure with respect to accounts receivable to any single counterparty or any group of counterparties having similar characteristics.

The credit risk on cash and cash equivalents is considered by management to be limited because the counterparties are financial institutions with high credit ratings assigned by international credit rating agencies

The carrying value of accounts receivable approximates its fair value due to the relatively short periods to maturity on this instrument. The maximum exposure to credit risk is represented by the carrying amount on the balance sheet. There are no material financial assets that the Company considers past due and at risk of collection.

Interest Rate Risk

Interest rate risk refers to the risk that the value of a financial instrument or cash flows associated with the instrument will fluctuate due to changes in market interest rates. The Company is exposed to interest rate risk as it can borrow funds at floating interest rates as disclosed in Note 5. The Company currently does not use interest rate hedges or fixed interest rate contracts to manage the Company's exposure to interest rate fluctuations.

Commodity Price Risk

The Company is exposed to fluctuations in commodity prices for crude oil, natural gas and natural gas liquids. Commodity prices are affected by many factors including supply and demand. The Company monitors these risks and when appropriate, utilizes financial instruments to manage its exposure to these risks.

A 10% increase or decrease is used when reporting commodity risk internally to key management personnel and represents management's assessment of the reasonably possible change in commodity prices. Assuming all other variables remain constant, a 10% increase in commodity prices would have reduced the earnings of the Company during the six month period ended June 30, 2008 by approximately \$2,455,289. Assuming all other variables remain constant, a 10% decrease in commodity prices would have increased the earnings of the Company during the six month period ended June 30, 2008 by approximately \$2,811,573.

The Company had the following outstanding derivative contracts, the terms of which are summarized below:

| Contract Type | Price | Volumes Per Day | Contract Term |
|---------------|-------------------------|-----------------|---------------------------------------|
| Financial | Sell \$92.00 per Bbl | 100 Bbls | January 1, 2008 to December 31, 2008 |
| Financial | Sell \$95.00 per Bbl | 100 Bbls | February 1, 2008 to December 31, 2008 |
| Financial | Sell \$90.55 US per Bbl | 200 Bbls | January 1, 2009 to December 31, 2009 |
| Financial | Sell \$7.84 per GJ | 2,000 GJ | July 1, 2008 to September 30, 2008 |
| Financial | Sell \$7.55 per GJ | 5,000 GJ | July 1, 2008 to September 30, 2008 |
| Financial | Sell \$8.00 per GJ | 5,000 GJ | October 1, 2008 to December 31, 2008 |
| Financial | Sell \$8.23 per GJ | 2,000 GJ | October 1, 2008 to December 31, 2008 |
| Financial | Sell \$ 8.40 per GJ | 4,000 GJ | January 1, 2009 to March 31, 2009 |
| Financial | Sell \$8.60 per GJ | 2,000 GJ | January 1, 2009 to March 31, 2009 |
| Financial | Sell \$8.60 per GJ | 1,000 GJ | January 1, 2009 to March 31, 2009 |

The mark to market adjustment of these contracts, based on price quotation in an active market, has been recognized as a liability in the amount of \$12,846,273 at June 30, 2008 (December 31, 2007 – \$567,483).

Liquidity Risk

Liquidity risk includes the risk that, as a result of the Company's operational liquidity requirements:

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

The Company's operating cash requirements, including amounts projected to complete the Company's existing capital expenditure program, are continuously monitored and adjusted as input variables change. These variables include but are not limited to, available credit, oil and natural gas production from existing wells, results from new wells drilled, commodity prices, cost overruns on capital projects and regulations relating to prices, taxes, royalties, land tenure, allowable production and availability of markets. As these variables change, liquidity risks may necessitate the Company to conduct equity issues or obtain project debt financing. The Company also mitigates liquidity risk by maintaining an insurance program to minimize exposure to insurable losses.

Following is a list of the financial liabilities at June 30, 2008 and their due dates:

| | Total | Current Within 1 Year |
|--|-------------------|-----------------------------|
| Bank overdraft | 2,844,948 | 2,844,948 |
| Accounts payable and accrued liabilities | 10,585,553 | 10,585,553 |
| Financial instruments | 12,846,273 | 12,846,273 |
| Total | 26,276,774 | 26,276,774 |

Capital Management

The Company's objectives when managing capital is to safeguard its ability to continue as a going concern, so that it can continue to provide returns to shareholders and benefits for other stakeholders. The Company manages the capital structure and makes adjustments to it in light of changes in economic conditions and the risk characteristics of the underlying assets. The Company's objective is met by retaining adequate equity to provide for the possibility that cash flows from assets will not be sufficient to meet future cash flow requirements. The Board of Directors does not establish quantitative return on capital criteria for management. The Company defines capital as the aggregate of total equity, cash and debt.

The Company is not subject to any externally imposed cash flow requirements other than covenants on its operating credit facility with its lender. At June 30, 2008 the company was in compliance with its financial covenants.

NOTE. 4 Related Party Transactions

Except as disclosed elsewhere in these consolidated financial statements, the Corporation had the following related party transactions:

a) The Corporation entered into transactions with the following related parties:

Rhodes Petroleum Corp. – controlled by an officer of the Corporation

Pioneer Land Services Ltd. – a Director is an employee of Pioneer

Borden Ladner Gervais LLP – a Director is partner with the law firm

b) Transactions

| | 2008 | 2007 |
|---|------------------|-------------------|
| Expenses | | |
| Consulting – Pioneer Land Services Ltd. | \$ – | \$ 209 |
| Legal Consulting – Borden Ladner Gervais LLP | 90,155 | 265,532 |
| | \$ 90,155 | \$ 265,741 |
| Other | | |
| Recorded as part of Oil and Gas Properties – Pioneer Land Services Ltd | \$ 13,214 | \$ 5,685 |
| Recorded as part of Share issuance cost – Borden Ladner Gervais LLP | – | 71,123 |
| Recorded as part of Oil and Gas Properties – Borden Ladner Gervais LLP | 9,602 | – |
| Recorded as part of Oil and Gas Properties – Rhodes Petroleum Corp. | 151 | – |
| | \$ 22,967 | \$ 76,808 |

- c) Revenue and expense transactions are in the normal course of operations and have been valued in these consolidated financial statements at the exchange amount which is the amount of consideration established and agreed to by the related parties and represents actual values charged to unrelated parties.

NOTE. 5 Long-term Financing

The Corporation has a revolving line of credit, with a syndicate of chartered banks, of up to \$70 million (2006 - \$55 million), which bears interest at prime plus 0.50% (2007 – 0.25%). The facility is secured by a general security agreement, a floating charge debenture in the amount of \$150 million and an unlimited liability guarantee by Terra Energy Corp. and Constar Resources.

At June 30, 2008 the revolving line of credit was not drawn upon. Outstanding cheques issued in the amount of \$2,844,948 are shown as bank overdraft until they clear against cash.

The Corporation's bank credit facility is structured as a 364 day revolving credit facility with a one year term out. If the credit facility is not renewed at maturity, the corporation is required to pay the outstanding balance one year from the maturity. In addition, the credit facility includes a change of control clause whereby in the event of any change of control, the creditor, at their discretion, may terminate the credit facility and therefore the entire amount outstanding will be due and payable upon demand.

NOTE. 6 Share Capital

- a) Authorized
- i) Unlimited number of common voting shares
- ii) Unlimited number of preferred shares
- b) Issued and outstanding

| | JUNE 30, 2008 | | DECEMBER 31, 2007 | |
|--|-------------------|---------------------|-------------------|----------------------|
| | Number of Shares | Amounts | Number of Shares | Amounts |
| Common shares | | | | |
| Balance, beginning of period | 74,297,484 | \$65,195,721 | 76,900,833 | \$ 72,570,457 |
| Issued on exercise of options | 2,118,300 | 2,525,937 | 206,000 | 214,480 |
| Tax effect of flow through share renouncement | – | – | – | (5,106,725) |
| Reclassification of contributed surplus (NOTE 7) | – | 1,514,643 | – | 90,067 |
| Shares repurchased for cancellation | (757,100) | (664,352) | (2,809,349) | (2,571,459) |
| Share issue costs | – | – | – | (1,099) |
| Balance, end of period | 75,658,684 | 68,571,949 | 74,297,484 | 65,195,721 |
| Share purchase warrants | | | | |
| Balance, beginning of period | – | – | 1,093,700 | 434,258 |
| Expired | – | – | (1,093,700) | (434,258) |
| Balance, end of period | – | – | – | – |
| Total Common Shares and Warrants | 75,658,684 | \$68,571,949 | 74,297,484 | \$ 65,195,721 |

During 2007 and 2008, the Corporation obtained permission from the TSX Venture Exchange for a Normal Course Issuer Bid to repurchase for cancellation up to 8,700,000 common shares (5.0 million in 2007 and 3.7 million in 2008).

In the six month period ended June 30, 2008, the Corporation purchased 757,100 common shares for total costs of \$1,013,035, at an average price of \$1.34 per common share. Share capital was reduced by \$664,352 and the excess of \$348,683 was charged to deficit.

No shares were purchased in the three month period ended June 30, 2008.

Of the repurchased shares, 215,400 were being held for cancellation at June 30, 2008 (December 31, 2007 – 477,849).

c) Stock Options

The Corporation's Employee Stock Option Plan provides for officers, directors, employees, and consultants to be granted options of up to 10 percent of the issued and outstanding common shares of the Corporation. These options entitle the holder to purchase common shares of the Corporation subject to various vesting periods and other terms and conditions specified in the stock option plan.

Details of all options outstanding at June 30, 2008 are as follows:

| | JUNE 30, 2008 | |
|--|----------------------|--|
| | Number of Options | Weighted average exercise price |
| Employee Stock Options | | |
| Balance, beginning of period | 6,693,000 | 1.35 |
| Granted | 2,184,300 | 1.75 |
| Exercised | (2,118,300) | (1.20) |
| Expired | (71,000) | (1.08) |
| Total Options, balance, end of period | 6,688,000 | 1.53 |

Stock Based Compensation expense of \$1,513,147 has been recorded for the three months ended June 30, 2008 (2007 - \$552,877) with the offsetting credit to contributed surplus. The fair value of share options granted in the period was \$0.98 and was estimated using the Black Scholes option-pricing model with the following assumptions: Dividend yield Nil; expected volatility at 84%; risk-free interest rate of 4.0%; weighted average term of 2.6 years.

Stock Based Compensation expense of \$1,976,320 has been recorded for the six months ended June 30, 2008 (2007 - \$869,728) with the offsetting credit to contributed surplus. The fair value of share options granted in the period was \$0.80 and was estimated using the Black Scholes option-pricing model with the following assumptions: Dividend yield Nil; expected volatility at 50% to 84%; risk-free interest rate of 4.0%; weighted average term of 2.5 years.

d) Per share amounts

The following table summarizes the calculation of basic net income (loss) and diluted net income (loss) per share.

| | THREE MONTHS ENDED JUNE 30 | | SIX MONTHS ENDED JUNE 30 | |
|--|----------------------------|------------|--------------------------|---------------|
| | 2008 | 2007 | 2008 | 2007 |
| Net income (loss) available to common shareholders | \$ 5,778,180 | \$ 618,863 | \$ 4,677,277 | \$(1,549,553) |
| Weighted-average number of common shares outstanding – basic | 74,597,170 | 75,165,101 | 74,338,591 | 75,071,384 |
| Dilutive effect of stock options | 938,502 | 693,062 | 501,261 | 351,564 |
| Weighted-average number of common shares outstanding – diluted | 75,535,672 | 75,858,163 | 74,839,852 | 75,422,948 |
| Net income (loss) per share (\$/share) | | | | |
| Basic | \$ 0.08 | \$ 0.01 | \$ 0.06 | \$ (0.02) |
| Diluted | \$ 0.08 | \$ 0.01 | \$ 0.06 | \$ (0.02) |

For the three month period ended June 30, 2008, 5,749,498 stock options (2007 – 6,469,938) and Nil warrants (2007 – 2,500,000) were anti-dilutive and have been excluded from the calculation of diluted income (loss) per share.

For the six month period ended June 30, 2008, 6,186,739 stock options (2007 – 6,811,436) and Nil warrants (2007 – 2,500,000) were anti-dilutive and have been excluded from the calculation of diluted income (loss) per share.

NOTE. 7 Contributed Surplus

The details of contributed surplus are as follows:

| | 2008 | 2007 |
|---|---------------------|--------------|
| Balance, beginning of period | \$ 9,365,272 | \$ 7,838,602 |
| Stock based compensation | 1,976,320 | 1,182,479 |
| Warrants expired | – | 434,258 |
| Reclassification resulting from exercise of options and warrants to common shares | (1,514,643) | (90,067) |
| Balance, end of period | \$ 9,826,949 | \$ 9,365,272 |

NOTE. 8 Statement of Cash Flows**Change in non-cash working capital**

| | THREE MONTHS ENDED JUNE 30 | | SIX MONTHS ENDED JUNE 30 | |
|--|----------------------------|--------------------|--------------------------|-----------------------|
| | 2008 | 2007 | 2008 | 2007 |
| Accounts receivable | \$ 3,771,447 | \$ (887,677) | \$ 110,799 | \$ (957,035) |
| Prepaid expenses | 241,807 | (117,004) | 199,116 | (92,096) |
| Accounts payable and accrued liabilities | (5,180,656) | (6,253,549) | (10,900,411) | (4,439,091) |
| | (1,167,402) | (7,258,230) | (10,590,496) | (5,488,222) |
| Change in non-cash working capital from investing | (3,416,271) | (4,982,720) | (7,221,369) | (3,050,216) |
| Change in non-cash working capital from operations | 2,248,869 | (2,275,510) | (3,369,127) | (2,438,006) |
| | \$ (1,167,402) | (7,258,230) | \$ (10,590,496) | \$ (5,488,222) |

Other information

| | THREE MONTHS ENDED JUNE 30 | | SIX MONTHS ENDED JUNE 30 | |
|---------------|----------------------------|------------|--------------------------|--------------|
| | 2008 | 2007 | 2008 | 2007 |
| Interest paid | \$ 652,018 | \$ 773,725 | \$ 1,433,224 | \$ 1,409,101 |
| Taxes paid | \$ — | \$ — | \$ 3,605 | \$ — |

NOTE. 9 Gain on Disposition of P&NG Rights

On May 13, 2008 the Corporation sold approximately 110 sections of Montney Petroleum and Natural Gas ("P&NG") rights for net proceeds received of \$65.2 million. Under full cost accounting the sale of undeveloped P&NG property uses a deemed cost of disposition, which resulted in a gain of \$14.5 million.

Full cost accounting requires a pooling of all costs, the disposition of a specific asset within that pool must be allocated an appropriate share of all costs, resulting in the use of a deemed cost of disposition in the calculation of a gain. All costs related to the exploration, acquisition and development of petroleum and natural gas reserves are initially capitalized under the full cost method of accounting. Such costs include lease acquisition costs, geological and geophysical expenditures, lease rentals on non-productive properties, costs of drilling both productive and non-productive wells, equipment costs and general and administrative expenses applicable to these activities. This calculation resulted in a deemed cost of disposition of \$47.3 million. The actual cost incurred by the Corporation to acquire these P&NG rights over the years is approximately \$3.3 million.

The closing on one section of mineral rights associated with sale remains outstanding which is expected to result in a further \$1.3 million of additional proceeds to the Corporation once certain criteria are met. The contingent consideration has not been included in the determination of the gain recognized in the second quarter of 2008. An adjustment will be recorded in a subsequent period if and when the criteria is met.