

# **PanTerra Resource Corp.**

## **FINANCIAL STATEMENTS**

**For the years ended December 31, 2010 and 2009**

## Management's Responsibility

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To the Shareholders of PanTerra Resource Corp.:

Management is responsible for the preparation and presentation of the accompanying financial statements, including responsibility for significant accounting judgments and estimates in accordance with Canadian generally accepted accounting principles. This responsibility includes selecting appropriate accounting principles and methods, and making decisions affecting the measurement of transactions in which objective judgment is required.

In discharging its responsibilities for the integrity and fairness of the financial statements, management designs and maintains the necessary accounting systems and related internal controls to provide reasonable assurance that transactions are authorized, assets are safeguarded and financial records are properly maintained to provide reliable information for the preparation of financial statements.

The Board of Directors and Audit Committee are composed primarily of Directors who are neither management nor employees of the Company. The Board is responsible for overseeing management in the performance of its financial reporting responsibilities and for approving the financial information included in the financial statements. The Audit Committee has the responsibility of meeting with management and external auditors to discuss the internal controls over the financial reporting process, auditing matters and financial reporting issues. The Committee is also responsible for recommending the appointment of the Company's external auditors.

Meyers Norris Penny LLP, an independent firm of Chartered Accountants, is appointed by the shareholders to audit the financial statements and report directly to them; their report follows. The external auditors have full and free access to, and are available to meet periodically and separately with, the Board and management to discuss their audit findings.

*"signed"*

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Fred Rumak

**President & CEO**

*"signed"*

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Ron Sparrow

**CFO**

## Independent Auditors' Report

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To the Shareholders of PanTerra Resource Corp.:

We have audited the accompanying financial statements of PanTerra Resource Corp. (the "Company") which comprise the balance sheets as at December 31, 2010 and 2009, and the statements of loss, comprehensive loss and deficit and cash flows for the years then ended, and a summary of significant accounting policies and other explanatory information.

### *Management's Responsibility for the Financial Statements*

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

### *Auditors' Responsibility*

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

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

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

### *Opinion*

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

### *Emphasis of Matter - Going Concern*

In forming our opinion on the financial statements, which is not qualified, we have considered the adequacy of the disclosure made in note 2 to the financial statements concerning the Company's ability to continue as a going concern. The Company has an accumulated deficit of \$13,134,825 (2009 - \$11,135,498). This condition indicates the existence of a material uncertainty which may cast significant doubt about the Company's ability to continue as a going concern.

*Meyer Norris Penny LLP*

Calgary, Alberta  
March 17, 2011

Chartered Accountants



**PANTERRA RESOURCE CORP.**  
**BALANCE SHEETS**  
As at December 31,

	2010	2009
<b>ASSETS</b>		
<b>Current</b>		
Cash and cash equivalents (Note 4)	\$ 1,306,759	\$ 315,170
Accounts receivable	138,822	177,482
Deposits for land leases (Note 4)	-	183,541
Prepaid expenses	32,630	94,438
	1,478,211	770,631
<b>Property and equipment (Note 5)</b>	17,806,154	17,569,652
	\$ 19,284,365	\$ 18,340,283

**LIABILITIES**

<b>Current</b>		
Accounts payable and accrued liabilities	\$ 359,723	\$ 181,297
<b>Asset retirement obligation (Note 7)</b>	1,170,997	1,128,179
	1,530,720	1,309,476

**SHAREHOLDERS' EQUITY**

<b>Share capital (Note 9)</b>	27,155,164	24,843,300
<b>Contributed surplus</b>	3,733,306	3,323,005
<b>Deficit</b>	(13,134,825)	(11,135,498)
	17,753,645	17,030,807
	\$ 19,284,365	\$ 18,340,283

**Going concern (Note 2)**  
**Commitments (Note 8)**  
**Subsequent event (Note 14)**

**On behalf of the board**

Fred Rumak

Director

David Halpin

Director

**PANTERRA RESOURCE CORP.**  
**STATEMENTS OF LOSS, COMPREHENSIVE LOSS AND DEFICIT**  
**Years ended December 31,**

	2010	2009
<b>REVENUE</b>		
Oil and gas sales	\$ 1,300,364	334,899
Royalties	(142,453)	(38,826)
Interest	3,765	8,271
	<b>1,161,676</b>	<b>304,344</b>
<b>EXPENSES</b>		
Operating	1,155,254	307,724
Depletion, depreciation and accretion	748,015	231,943
Stock-based compensation	274,328	435,818
Consulting	548,484	407,414
Office and administration	247,870	239,649
Professional	137,894	86,738
Investor communications	37,135	76,254
Transfer agent	10,833	22,717
Interest	1,190	25,131
	<b>3,161,003</b>	<b>1,833,388</b>
<b>OTHER INCOME</b>		
Foreign exchange gain	-	20,351
<b>LOSS BEFORE INCOME TAXES</b>	<b>(1,999,327)</b>	<b>(1,508,693)</b>
Future Income Tax Recovery (Note 6)	-	435,029
<b>NET LOSS AND COMPREHENSIVE LOSS FOR THE YEAR</b>	<b>(1,999,327)</b>	<b>(1,073,664)</b>
<b>DEFICIT, BEGINNING OF YEAR</b>	<b>(11,135,498)</b>	<b>(10,061,834)</b>
<b>DEFICIT, END OF YEAR</b>	<b>\$ (13,134,825)</b>	<b>\$ (11,135,498)</b>
<b>Net (loss) per share</b>		
- basic	\$ (0.12)	\$ (0.11)
- diluted	(0.12)	(0.11)
<b>Weighted average number of common shares (note</b>		
- basic	17,200,386	10,014,683
- diluted	17,200,386	10,014,683

See accompanying notes to the financial statements

**PANTERRA RESOURCE CORP.**  
**STATEMENTS OF CASH FLOWS**  
Years ended December 31,

	2010	2009
<b>CASH FLOWS PROVIDED BY (USED IN)</b>		
<b>OPERATING ACTIVITIES</b>		
Net loss for the year	\$ (1,999,327)	\$ (1,073,664)
Add items not affecting cash		
Stock-based compensation	274,328	435,818
Future income tax recovery	-	(435,029)
Depletion, depreciation and accretion	748,015	231,943
Asset retirement settlement	(78,783)	-
	(1,055,767)	(840,932)
Net changes in non-cash working capital items:		
Accounts receivable	38,660	(137,844)
Prepaid expenses	61,808	(52,337)
Accounts payable and accrued liabilities	91,961	34,280
	192,429	(155,901)
	(863,338)	(996,833)
<b>INVESTING ACTIVITIES</b>		
Additions to property and equipment	(862,916)	(1,874,322)
Refund of deposits	183,541	237,591
Land deposits remitted	-	(237,591)
Changes in non-cash working capital	86,466	(18,114)
	(592,909)	(1,892,437)
<b>FINANCING ACTIVITIES</b>		
Private placement proceeds (net of issue costs)	2,447,836	(718)
<b>INCREASE (DECREASE) IN CASH &amp; CASH EQUIVALENTS</b>	991,589	(2,889,988)
<b>CASH &amp; CASH EQUIVALENTS, BEGINNING OF YEAR</b>	315,170	3,205,158
<b>CASH &amp; CASH EQUIVALENTS, END OF YEAR</b>	\$ 1,306,759	\$ 315,170
<b>CASH AND EQUIVALENTS IS COMPRISED OF:</b>		
Cash in bank	\$ 106,759	\$ 15,194
Term deposits	1,200,000	299,976
	\$ 1,306,759	\$ 315,170

See accompanying notes to the financial statements

**PanTerra Resources Corp.**  
**NOTES TO THE FINANCIAL STATEMENTS**  
December 31, 2010 and 2009

**Note 1 NATURE OF OPERATIONS**

**PanTerra Resource Corp.** (the “Company” or “PanTerra”) is an oil and gas exploration and production company with producing properties in Alberta and a shale gas resource project in Saskatchewan. The Company is headquartered in Calgary and is an Alberta-based reporting entity whose shares are listed on the TSX Venture Exchange under the symbol: V.PRC.

Effective October 13, 2009, PanTerra shares were consolidated on a one for ten basis. Accordingly, the comparative number of shares and per share amounts have been retroactively adjusted to reflect the one for ten consolidation.

**Note 2 GOING CONCERN**

These financial statements have been prepared on a going concern basis, which implies the Company will continue to realize its assets and discharge its liabilities in the normal course of business. The Company has incurred recurring losses and has not generated profitable operations to date. The Company incurred a net loss of \$1,999,328 for the year ended December 31, 2010. As of December 31, 2010, the Company has working capital of \$1,118,487 (2009 – \$589,335), an accumulated deficit of \$13,134,825 (2009 – \$11,135,498) and shareholders’ equity of \$17,753,645 (2009 – \$17,030,808). The continuation of the Company as a going concern is dependent upon the ability of the Company to obtain necessary equity or other financing to continue operations, and/or to attain sufficient profitable operations. The outcome of these matters cannot be predicted at the present time. These financial statements do not include any adjustments to the recoverability and classification of recorded asset amounts and classification of liabilities that might be necessary should the Company be unable to continue as a going concern.

**Note 3 SIGNIFICANT ACCOUNTING POLICIES**

**Revenue Recognition**

Interest income from investments, such as term deposits, is recognized on a time proportionate basis. Revenue from the sale of oil or natural gas are recorded when title passes to an external party.

**Financial Instruments, Hedges and Comprehensive Income**

The accounting standards for financial instruments require that all financial assets and liabilities, including derivatives, are classified as: held for trading, held to maturity, available for sale assets, loans and receivables or other financial liabilities.

Financial assets and financial liabilities “held for trading” are measured at fair value with changes in those fair values recognized in net income. Financial assets “available for sale” are measured at fair value, without any deduction for transaction costs incurred on sale or other disposal with changes in those fair values measured in other comprehensive income. Financial assets “held to maturity”, “loans and receivables” and “other financial liabilities” are measured at amortized cost using the effective interest method of amortization. Transactions to purchase or sell these items are recorded on the trade date, and transaction costs are immediately recognized as income and expense.

Cash and cash equivalents are classified as “held for trading”, deposits for land leases are classified as “held to maturity”, accounts receivable are classified as “loans and receivables”, and accounts payable and accrued liabilities are designated as “other liabilities”.

Accounting standards for hedges specify the criteria under which hedge accounting can be applied and that any gains or losses resulting from ineffective hedges are recognized in net income immediately. Changes in hedging derivatives are recognized in net income or other comprehensive income depending on the nature of the hedging relationship. During the years ended December 31, 2010 and December 31, 2009 the Company has not designated any financial transactions as hedges.

**PanTerra Resources Corp.**  
**NOTES TO THE FINANCIAL STATEMENTS**  
December 31, 2010 and 2009

**Note 3 SIGNIFICANT ACCOUNTING POLICIES (continued)**

**Comprehensive Income**

Comprehensive income is the change in equity of the Company during the period as a result of transactions and other events and circumstances from non-owner sources. There was no other comprehensive income or loss during the years ended December 31, 2010 and 2009; accordingly, comprehensive loss is equal to net loss.

**Cash and Cash Equivalents**

Cash and cash equivalents include cash deposits in bank accounts and investments with original maturities of three months or less.

**Property and Equipment**

The Company follows the full cost method of accounting for oil and natural gas operations whereby all costs relating to the acquisition, exploration and development of oil and natural gas reserves, including asset retirement costs, are initially capitalized in a single Canadian cost centre. Such costs include land acquisition costs, geological and geophysical expenses, carrying charges on non-producing properties, costs of drilling both productive and non-productive wells, related production equipment costs, and abandonment costs and overhead charges directly related to acquisition, exploration and development activities.

Capitalized costs, excluding costs related to unproven properties, are depleted using the unit-of-production method based on estimated proven oil and natural gas reserves before deduction of royalties as determined by independent petroleum engineers. Natural gas reserves and production are converted to equivalent barrels of oil using a ratio of six thousand cubic feet of natural gas to one barrel of oil.

Costs of acquiring and evaluating unproven properties are initially excluded from depletion calculations. These unproven properties are assessed periodically to ascertain whether impairment has occurred. When proved reserves are assigned or the property is considered to be impaired, the cost of the property or the amount of the impairment is added to costs subject to depletion.

Proceeds from the sale of petroleum and natural gas properties will be applied against capitalized costs, with no gain or loss recognized, unless such a sale would result in a greater than 20% change in the depletion and depreciation rate.

When proved reserves are assigned, associated capitalized costs will be assessed for possible impairment using a two stage ceiling test. In the first stage undiscounted future cash flows are calculated based on the independent petroleum engineer's best estimate of forward indexed prices applied to estimated future production of proved reserves plus anticipated proceeds from the sale of undeveloped properties, less estimated future operating costs, royalties and future capital development costs. When the carrying amount of a cost centre is not recoverable, the second stage of the process will determine the impairment whereby the cost centre would be written down to its fair value. The second stage requires the calculation of discounted future cash flows from proved plus probable reserves using the Company's risk free interest rate plus the cost of undeveloped land, net of any impairment. The fair value is estimated using accepted present value techniques, which incorporate risks and other uncertainties when determining expected cash flows.

Automotive, office equipment and furniture are carried at cost and amortized on a straight line basis over the estimated service lives of three to ten years.

**Joint Interest Activities**

Some of the Company's activities are conducted jointly with others. These financial statements reflect only the Company's proportionate interest in such activities. Where the Company enters into a joint venture agreement with partners and is the operator, the Company recovers a portion of its overhead costs from the non-operating partners.

**PanTerra Resources Corp.**  
**NOTES TO THE FINANCIAL STATEMENTS**  
December 31, 2010 and 2009

**Note 3 SIGNIFICANT ACCOUNTING POLICIES (continued)**

**Asset Retirement Obligations**

The Company recognizes the fair value of a liability for an asset retirement obligation in the period in which it is incurred or when a reasonable estimate of the fair value can be made, and records a corresponding increase in the carrying value of the related long-lived asset. The fair value is determined through a review of engineering studies, industry guidelines, and management's estimate on a site-by-site basis. The liability is subsequently adjusted for the passage of time, which is recognized as accretion expense in the statement of loss, comprehensive loss and deficit. The liability is also adjusted due to revisions in either the timing or the amount of the original estimated cash flows associated with the liability. Actual costs incurred upon settlement of the asset retirement obligations are charged against the asset retirement obligation to the extent of the liability recorded.

**Per Share Amounts**

The basic per share amount is computed by dividing the net loss by the weighted average number of common shares outstanding during the year. The diluted loss per share reflects the potential dilution of common share equivalents, such as outstanding stock options and outstanding warrants, in the weighted average number of common shares outstanding during the year, if dilutive. For this purpose, the "treasury stock" method is used which assumes that any proceeds received upon the exercise of in-the-money stock options and warrants would be used to purchase common shares at the average market price for the period.

**Income Taxes**

The asset and liability method is used for determining income taxes. Under this method, future tax assets and liabilities are recognized for the estimated tax recoverable or payable that would arise if assets and liabilities were covered or settled at the financial statement carrying amounts. Future tax assets and liabilities are measured using substantively enacted tax rates expected to apply to taxable income in the years in which temporary differences are expected to be recovered or settled. Changes to these balances, including changes due to changes in income tax rates, are recognized in income in the period in which they occur. The amount of the future income tax asset recognized is limited to the amount that is more likely than not to be realized.

In assessing the realization of the future tax assets, management considers whether it is more likely than not that some portion or all of the future tax assets will not be realized. The ultimate realization of future tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management considers the scheduled reversal of future tax liabilities, projected future taxable income, and tax planning strategies in making this assessment. The amount of the future tax asset considered realizable could change materially in the near term based on future taxable income during the carry-forward period. A valuation allowance has been provided against all net future tax assets as a realization of such net assets is uncertain.

**Measurement Uncertainty**

The preparation of financial statements in conformity with Canadian Generally Accepted Accounting Principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the period, including the related income and future taxes and asset retirement obligations.

The valuation of property and equipment is based on management's best estimate of the future recoverability of these assets. The amounts recorded for depletion and depreciation of property and equipment and accretion of the asset retirement obligation are based on estimates. The property and equipment impairment test is based on estimates of proved reserves, production rates, petroleum and natural gas prices, future costs and other relevant assumptions. The amounts computed with respect to stock-based compensation are based on estimates as to the expected life of options granted, the volatility of the Company's stock price and certain other variables.

**PanTerra Resources Corp.**  
**NOTES TO THE FINANCIAL STATEMENTS**  
December 31, 2010 and 2009

**Note 3 SIGNIFICANT ACCOUNTING POLICIES (continued)**

By their nature, these estimates are subject to measurement uncertainty and the effect on the financial statements of changes in such estimates in future periods could be significant. These estimates and assumptions are reviewed periodically and, as adjustments become necessary, they are reported in earnings in the periods in which they become known.

**Flow-through Shares**

Periodically the Company finances a portion of its exploration and development activities through the issuance of flow-through shares. Under the terms of the flow-through share agreements, the tax attributes of the related expenditures are renounced to the subscribers. Share capital is reduced and the future income tax liability is increased by the tax affected amount of the renounced tax deductions at the time of renouncement which is when the related documentation is filed with the appropriate government agency and there is reasonable certainty that the expenditures will be incurred.

**Stock-based Compensation**

Stock options granted to employees, consultants and directors are accounted for using the fair value method. For stock options granted to employees, consultants and directors, compensation expense is recorded in the statement of loss and deficit over the vesting period with a corresponding increase to contributed surplus. The fair value of options granted is determined at the date of grant using the Black-Scholes valuation model.

The fair value of warrants issued to agents is recorded as a share issue cost.

Upon exercise of stock options and warrants, consideration received together with the amount previously recognized in contributed surplus is recorded as an increase to share capital. The Company does not incorporate an estimated forfeiture rate for stock options and agents' warrants that will not vest, but accounts for forfeitures as they occur.

**Recent Accounting Pronouncements**

**International Financial Reporting Standards**

In February 2008, the Canadian Accounting Standards Board (AcSB) confirmed that the transition date to International Financial Reporting Standards ("IFRS") from Canadian Generally Accepted Accounting Principles ("GAAP") will be January 1, 2011 for publicly accountable enterprises. IFRS will become the generally accepted accounting principles in Canada. The adoption date of January 1, 2011 will require restatement for comparative purposes, of amounts reported by the Company for the year ended December 31, 2010, including the opening balance sheet as at January 1, 2010.

The areas of accounting differences with the highest impact on Panterra's financial statements include; exploration and evaluation expenditures, depletion expense, property plant and equipment, stock-based compensation expense, flow through shares and asset retirement obligations.

Panterra will release its first IFRS compliant interim financial statements for the first quarter of 2011.

**Note 4 CASH EQUIVALENTS**

Cash equivalents at December 31, 2010 included \$1,200,000 of term deposits at a rate of 0.9%. The December 31, 2009 balance included \$299,976 of term deposits at an annual rate of 0.10%.

**PanTerra Resources Corp.**  
**NOTES TO THE FINANCIAL STATEMENTS**  
December 31, 2010 and 2009

**Note 5 PROPERTY AND EQUIPMENT**

	December 31, 2010			December 31, 2009		
	Cost	Accumulated depletion and depreciation	Net Book Value	Cost	Accumulated depletion and depreciation	Net Book Value
Petroleum and natural gas property and equipment	\$ 18,573,812	\$ 789,350	\$ 17,784,462	\$ 17,721,201	\$ 169,881	\$ 17,551,320
Office equipment and furniture	75,252	53,560	21,692	64,947	46,615	18,332
	<u>\$ 18,649,064</u>	<u>\$ 842,910</u>	<u>\$ 17,806,154</u>	<u>\$ 17,786,148</u>	<u>\$ 216,496</u>	<u>\$ 17,569,652</u>

Unproved properties in the amount of \$13,282,230 (2009 - \$12,915,594) were excluded from the depletion calculation.

In 2009 property and equipment additions included capitalized G&A and stock based compensation in the amount of \$113,029. None was included in 2010.

The Company's Saskatchewan property exploration permits are subject to certain conditions, one of which is an annual deposit for the work commitment on each property. When actual expenditures are incurred and submitted the deposit is refunded. At December 31, 2010, no deposits (2009 - \$183,541) in relation to petroleum and natural gas properties were held by the Province of Saskatchewan as all the work commitments have taken place.

At December 31, 2010 the Company applied a ceiling test to its petroleum and natural gas assets. The application of the test required no impairment adjustment to the carrying value of the Company's petroleum and natural gas properties. The prices used in the ceiling test evaluation of the Company's oil and gas assets are summarized in the following chart:

	Crude Oil		Natural Gas
	WTI Cushing Oklahoma (\$US/bbl)	Edmonton Par Price 40 API (\$Cdn/bbl)	Alberta AECO-C Spot (\$Cdn/MMBTU)
2011	88.40	93.08	4.04
2012	89.14	93.85	4.66
2013	88.77	93.43	4.99
2014	88.88	93.54	6.58
2015	90.22	94.95	6.69
Thereafter	1.5%	1.5%	1.5%

Percentage change of 1.5% represents the change in the future prices each year after 2015 to the end of the reserve life

**PanTerra Resources Corp.**  
**NOTES TO THE FINANCIAL STATEMENTS**  
December 31, 2010 and 2009

**Note 6 FUTURE INCOME TAXES**

The provision for income taxes recorded in the financial statements differs from the amount that would be obtained by applying the statutory income tax rate of 28.0% (2009 – 29.0%) to the loss before tax for year ended December 31 as follows:

	2010	2009
Loss before income taxes	\$ (1,999,328)	\$ (1,508,693)
Anticipated income tax recovery	(559,812)	(437,521)
Increase (decrease) resulting from		
Stock-based compensation	76,812	126,387
Meals and entertainment	699	435
Impact of tax rate differences	53,878	(12,862)
Changes in prior year tax estimates	-	1,543
Expiration of non-capital loss carry forward	32,756	54,849
Share issue costs	(96,426)	(186)
Other	21,097	-
Change in valuation allowance	470,996	(167,674)
Future income tax recovery	\$ -	\$ (435,029)

The components of the Company's net future income tax asset (liability) are as follows:

	2010	2009
Future tax assets (liabilities)		
Property and equipment	\$ (1,616,820)	\$ (1,747,411)
Asset retirement obligation	304,459	293,331
Non capital losses carried forward	1,663,316	1,388,081
Share issue costs	126,656	120,348
Eligible capital expenditures	2,925	2,925
Other capital assets	-	-
	480,536	57,274
Valuation allowance	(480,536)	(57,274)
	\$ -	\$ -

The Company has the following losses available to deduct from future taxable income:

	Loss	Year of expiry
	\$ 133,552	2011
	855,280	2012
	829,297	2016
	1,045,987	2027
	1,259,667	2028
	1,083,967	2029
	1,189,621	2030
	\$ 6,397,371	

**PanTerra Resources Corp.**  
**NOTES TO THE FINANCIAL STATEMENTS**  
December 31, 2010 and 2009

**Note 7 ASSET RETIREMENT OBLIGATION**

The following table presents the reconciliation of the beginning and ending aggregate carrying amount of the obligation associated with the retirement of oil and natural gas properties:

	December, 2010	December, 2009
Asset retirement obligation, beginning of period	\$ 1,128,179	\$ 320,175
Liabilities acquired	-	748,938
Liabilities settled	(78,783)	-
Accretion expense	121,601	59,066
Asset retirement obligation, end of period	\$ 1,170,997	\$ 1,128,179

The undiscounted amount of cash flows to settle the obligation is \$360,000 for the Saskatchewan properties and \$1,183,200 for the Alberta properties. The obligation was calculated using a credit-adjusted risk free discount rate of approximately 7.50 percent per annum respectively and an inflation rate of 2.00 and 1.50 percent per annum respectively over various periods of time depending on the estimated dates of abandonment. It is expected that this obligation will be funded from Company resources at the time the costs are incurred.

**Note 8 COMMITMENTS**

The Company has a lease for office premises which expires June 30, 2011. The future minimum payments on the lease amount to \$19,032 plus operating costs and taxes.

There are no lease commitments after 2011.

Of the \$17,784,462 investment in petroleum and natural gas property and equipment, \$8,242,593 was expended on the Saskatchewan permits. All of the expenditures have now been approved enabling PanTerra to retain up to 25% of the land over these permits. The Company is in the process of applying to continue selected land as leases pursuant to applicable law.

**PanTerra Resources Corp.**  
**NOTES TO THE FINANCIAL STATEMENTS**  
December 31, 2010 and 2009

**Note 9 SHARE CAPITAL**

**a) Shares**

i) Authorized

Unlimited number of common shares

Unlimited number of preferred shares

ii) Issued common shares

	Year Ended December 31, 2010		Year Ended December 31, 2009	
	Shares	Amount	Shares	Amount
Balance, beginning of year	12,870,983	\$24,843,300	8,580,629	\$22,061,282
Private placement proceeds	12,710,608	2,387,946		
Issued in exchange for producing properties	-	-	4,290,354	3,217,765
Effect of tax renunciation on flow-through shares	-	-	-	(435,029)
Share issue costs	-	(281,182)	-	(718)
	<u>25,581,591</u>	<u>26,950,064</u>	<u>12,870,983</u>	<u>24,843,300</u>

**b) Warrants**

Balance, beginning of year	-	-	710,974	888,120
Issued with private placement	2,856,415	309,620	-	-
Issued to agents	360,000	-	-	-
Less warrants expired	-	-	(710,974)	(888,120)
Share issue costs	-	(104,520)	-	-
	<u>3,216,415</u>	<u>205,100</u>	<u>-</u>	<u>-</u>
Balance shares and warrants, end of year		<u>\$27,155,164</u>		<u>\$24,843,300</u>

On December 29, 2010 the Company closed a private placement financing of 2,777,778 common shares at a price of \$0.18 per share for gross proceeds of \$500,000.

On July 30, 2010 the Company closed a private placement financing comprised of 4,220,000 common flow-through shares of the Company at a price of \$0.25 per share and 5,712,830 units of the Company at a price of \$0.20 per unit. Each unit consists of one common share and one half of one common share purchase warrant. Each whole common share purchase warrant may be exercised into one common share of the Company at a price of \$0.40 per share for a period of two years following the date of closing. Proceeds realized by the Company from the offering totaled \$2,197,566, of which \$2,113,498 was received in cash. Commissions paid on the private placements totaled \$385,702, of which \$165,661 was paid via cash, \$39,022 was settled through issuance of agent warrants, \$96,951 was settled through agent options and \$84,066 was settled through issuance of common shares.

Effective October 13, 2009, PanTerra shares were consolidated on a one for ten basis. The 2009 comparative number of shares and per share amounts reflect this consolidation.

On September 1, 2009, the Company issued 4,290,354 shares (post consolidation) in exchange for producing properties in the Carrot Creek and Tomahawk areas of Alberta priced at \$0.75 per share.

**PanTerra Resources Corp.**  
**NOTES TO THE FINANCIAL STATEMENTS**  
December 31, 2010 and 2009

**Note 9 SHARE CAPITAL (continued)**

**c) Options**

The Company has a Stock Option Plan whereby the Board of Directors is authorized to approve incentive stock option agreements with directors, officers, consultants and employees, up to a maximum of 10% of the issued and outstanding shares as at the date of grant. The price is determined on the date of the grant by taking the closing price of the previous day on the TSX Venture Exchange. The options are non-transferable and expire ninety days after the optionee ceases to be an "eligible person", or one year after the death or disability of the optionee. At December 31, 2010, there were no shares authorized or reserved for stock option grants other than for the options outstanding at that date as disclosed in the table below.

As at December 31, 2010 and December 31, 2009 the Company had the following stock options outstanding:

	2010			2009		
	Number of Options	Weighted Average Remaining Life	Weighted average exercise price	Number of Options	Weighted Average Remaining Life	Weighted average exercise price
Outstanding, beginning of year	1,108,000		\$ 1.26	611,000		\$ 2.60
Granted	1,170,000		0.26	920,500		0.59
Agents options	720,000		0.20	-		-
Expired or cancelled	(713,000)		1.84	(423,500)		2.70
Outstanding, end of year	<u>2,285,000</u>	<u>3.48</u>	<u>0.23</u>	<u>1,108,000</u>	<u>4.12</u>	<u>1.26</u>
Exercisable, at end of year	<u>1,406,655</u>		<u>\$ 0.22</u>	<u>534,996</u>		<u>\$ 1.71</u>

During the year 1,170,000 options were granted to employees, directors and consultants, and 713,000 expired or were cancelled. The expired options had already vested and therefore no adjustment to stock based compensation expense was required. The options granted vest over a two year period.

The Company recorded stock-based compensation for the year ended December 31, 2010 in the amount of \$274,328 (2009 – \$435,818) for stock options granted or vested during the year. A fair value of \$309,620 was attributed to the warrants issued on the private placements. The fair value of stock options and warrants granted, averaging \$0.143 (2009 - \$0.392) per award, was estimated using the Black-Scholes option pricing model with the following assumptions:

	2010	2009
Risk-free rate	2.30%	2.26%
Expected life	2 to 5	5
Expected volatility	129%	153%
Expected dividend yield	0%	0%

**PanTerra Resources Corp.**  
**NOTES TO THE FINANCIAL STATEMENTS**  
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**Note 9 SHARE CAPITAL (continued)**

**d) Warrants**

As at December 31, 2010 and 2009 the Company had the following warrants outstanding:

	Year ended December 31, 2010	
	Number of Warrants	Weighted Average Exercise Price
Outstanding, beginning of period	-	-
Issued with private placement	2,856,415	\$ 0.40
Issued agents w arrants	360,000	\$ 0.40
Outstanding, end of period	3,216,415	\$ 0.40

The following table summarizes information about the warrants outstanding at December 31, 2010:

	Exercise Price Range	Warrants Outstanding	Weighted Average Remaining Life	Weighted Average Exercise Price	Number of Warrants Currently Exercisable
Share purchase w arrants	\$ 0.40	2,856,415	1.53	\$ 0.40	2,856,415
Agents w arrants	\$ 0.40	360,000	1.53	\$ 0.40	360,000
	\$ 0.40	3,216,415	1.53	\$ 0.40	3,216,415

**e) Contributed surplus**

The following table reconciles the Company's contributed surplus:

	December 31 2010	December 31 2009
Balance, beginning of year	\$ 3,323,005	\$ 1,975,728
Stock- based compensation expense	274,328	435,818
Stock- based compensation capitalized	-	23,339
Transfer of expired w arrants	-	888,120
Fair value transfer re agents options	96,951	-
Fair value of w arrants issued to agents	39,022	-
Balance, end of year	\$ 3,733,306	\$ 3,323,005

**PanTerra Resources Corp.**  
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**Note 9 SHARE CAPITAL (continued)**

**f) Loss per share**

For the year ended December 31, 2010, the basic and diluted weighted average number of shares is 17,190,472 (2009 - 10,014,683).

As a result of the net loss for the year ended December 31, 2010, 2,285,000 options (2009 - 1,108,000) and 3,216,415 warrants (2009 - nil) outstanding have not been included in the calculation of diluted loss per share because to do so would have been anti-dilutive.

**Note 10 FINANCIAL INSTRUMENTS, RISK MANAGEMENT**

The Company, as part of its operations, carries a number of financial instruments. Management does not believe the Company is exposed to significant credit, currency or interest rate risks.

**(a) Fair values of financial assets and liabilities**

The fair values of the Company's cash and cash equivalents, accounts receivable and accounts payable are estimated to approximate their carrying values due primarily to the immediate or short-term maturity of these financial instruments.

PanTerra classifies the fair value of the financial instruments according to the following hierarchy based on the amount of observable inputs used to value the instrument.

Level 1 – inputs to the valuation methodology are quoted prices for identical assets or liabilities in active markets.

Level 2 – inputs to the valuation methodology included quoted prices for identical assets or liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument. Level 2 valuations are based on inputs, including quoted forward prices for commodities, time value and volatility factors, which can be substantially observed or corroborated in the marketplace.

Level 3 – inputs to the valuation methodology are not based on observable market data.

Level 1 assumptions are used to value cash.

**(b) Financial risk factors**

**Credit risk**

Credit risk is the risk of financial loss to a company if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Company's receivables from petroleum and natural gas marketers. Receivables from petroleum marketers are normally collected on the 25<sup>th</sup> day of the month following production. The Company historically has not experienced collection issues with its petroleum and natural gas marketers. The Company does not obtain collateral from petroleum and natural gas marketers. In addition the Company has financial instruments including cash and term deposits in Canadian chartered banks, interest receivable from the same banks and GST receivable from the federal government. The Company considers the risk of default from these parties to be low.

**Liquidity risk**

Liquidity risk relates to the risk that the Company will encounter difficulty in meeting its obligations associated with financial liabilities. The financial liabilities on the balance sheet consist of accounts payable and accrued liabilities. The Company anticipates it will have adequate liquidity to fund its financial liabilities through issuing share capital and operations.

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**Note 10 FINANCIAL INSTRUMENTS, RISK MANAGEMENT (continued)**

**Market risk**

Market risk is the risk that changes in market prices, such as currency exchange rate risk, commodity price risk and interest rate risk will affect the Company's net earnings, future cash flows, the value of financial instruments, or the fair value of its assets and liabilities.

Currency exchange rate risk

The Company does purchase services from the United States and as such is exposed to currency fluctuations from the time a liability is incurred until payment is made.

Commodity price risk

Commodity price risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate as a result of changes in commodity prices. Commodity prices for petroleum and natural gas are impacted by the relationship between the Canadian and US dollar as well as world economic events dictating the levels of supply and demand. The Company did not have any financial instruments in place to manage commodity prices during the year ended December 31, 2010

Interest rate risk

The Company has no debt and generally receives a fixed interest on term deposits and as such has very limited exposure to interest risk.

**Note 11 CAPITAL MANAGEMENT**

The Company's policy is to maintain a strong and stable capital base for the objectives of maintaining financial flexibility, to sustain the development of the Company's current capital projects and for future development of the Company. The Company monitors its working capital and expected capital spending and issues share capital to manage its development plans. The Company has no externally imposed capital requirements.

The Company considers its capital structure to include shareholders' equity and working capital.

**Note 12 RELATED PARTY TRANSACTIONS**

Included in general and administrative expenses for the year ended December 31, 2010, are consulting fees of \$364,090 (2009 - \$289,944) paid to companies controlled by officers of the Company. In addition legal fees of \$91,665 (2009 - \$18,511) were paid to a law firm of which the Company's corporate secretary is a partner. Of these related party amounts, \$12,039 (2009 - \$1,739) were payable as of December 31, 2010.

During the 2010 year \$120,000 in severance was paid to a company controlled by a former officer of the company.

**Note 13 COMPARATIVE FIGURES**

Certain comparative figures have been reclassified to conform to the current year's presentation.

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**Note 14 SUBSEQUENT EVENT**

On January 26, 2011 the Company closed a private placement financing comprised of 1,250,000 common shares at a price of 0.20 per share for gross proceeds of \$250,000.

Effective January 11, 2011 the Company granted to certain officers, directors and employees share options for the purchase of 990,000 shares for a period of five years at \$0.21 per share.