

TWOCO PETROLEUMS LTD.

FINANCIAL STATEMENTS

JUNE 30, 2008

Notice to Reader

The accompanying unaudited interim financial statements of Twoco Petroleums Ltd. for the quarter ended June 30, 2008 have been prepared by management and approved by the Board of Directors of the Company. These statements have not been reviewed by Twoco Petroleums Ltd.'s external auditors.

Dated August 27, 2008.

On behalf of Twoco Petroleums Ltd.

(signed) "Wayne A. Malinowski"
Wayne A. Malinowski
President

(signed) "Tim Bashforth"
Tim Bashforth
Secretary and Treasurer

TWOCO PETROLEUMS LTD.

Balance Sheets

	June 30, 2008 <u>(unaudited)</u>	December 31, 2007 <u>(audited)</u>
Assets		
Current assets		
Accounts receivable	\$ 3,042,211	\$ 1,829,928
Prepaid expenses and deposits	<u>522,432</u>	<u>553,463</u>
	3,564,643	2,383,391
Property, plant and equipment	<u>49,737,186</u>	<u>50,350,663</u>
	<u>\$ 53,301,829</u>	<u>\$ 52,734,054</u>
Liabilities		
Current liabilities		
Bank indebtedness	\$ 3,942,691	\$ 6,209,859
Accounts payable and accrued liabilities	2,759,977	2,062,263
Current portion of capital lease obligations	227,988	220,670
Convertible debentures payable (note 3)	<u>11,904,405</u>	<u>-</u>
	18,835,061	8,492,792
Asset retirement obligations (note 4)	2,887,509	2,762,151
Future income taxes	5,068,000	4,636,350
Obligations under capital lease	423,678	539,505
Convertible debentures payable (note 3)	<u>-</u>	<u>11,840,675</u>
	<u>27,214,248</u>	<u>28,271,473</u>
Shareholders' Equity		
Share capital (note 5)	20,881,112	20,250,003
Equity portion of convertible debentures payable (note 3)	160,000	160,000
Contributed surplus (note 6)	914,615	1,128,929
Retained earnings	<u>4,131,854</u>	<u>2,923,649</u>
	<u>26,087,581</u>	<u>24,462,581</u>
	<u>\$ 53,301,829</u>	<u>\$ 52,734,054</u>

Approved by the Board:

(signed) "Wayne A. Malinowski", Director

(signed) "Larry C. Mah", Director

TWOCO PETROLEUMS LTD.

Statements of Operations, Comprehensive Income And Retained Earnings

(unaudited)

	Three Months Ended		Six Months Ended	
	June 30, 2008	June 30, 2007	June 30, 2008	June 30, 2007
Revenue				
Oil and gas sales	\$ 5,417,081	\$ 3,791,470	\$ 10,348,426	\$ 7,644,686
Less: Royalties	<u>(614,247)</u>	<u>(597,571)</u>	<u>(1,469,408)</u>	<u>(1,339,120)</u>
	4,802,834	3,193,899	8,879,018	6,305,566
Interest	<u>-</u>	<u>169</u>	<u>5</u>	<u>4,070</u>
	<u>4,802,834</u>	<u>3,194,068</u>	<u>8,879,023</u>	<u>6,309,636</u>
Expenses				
Operating costs	607,035	492,680	1,216,365	867,792
Transportation costs	159,409	137,622	346,616	274,232
General and administrative	199,827	180,457	478,246	287,763
Interest on bank debt	52,493	62,517	130,603	72,277
Interest on capital leases	10,556	13,759	21,931	28,288
Interest on debentures payable	237,716	237,717	472,967	472,968
Stock-based compensation	4,556	42,228	7,612	81,401
Amortization of convertible debentures financing charges	18,532	10,865	37,064	31,313
Depletion, amortization and accretion	<u>1,945,071</u>	<u>2,400,873</u>	<u>4,225,872</u>	<u>4,539,349</u>
	<u>3,235,195</u>	<u>3,578,718</u>	<u>6,937,276</u>	<u>6,655,383</u>
Income (loss) before income taxes	1,567,639	(384,650)	1,941,747	(345,747)
Income tax expense:				
- Current	-	13,844	-	13,844
- Future (recovery)	<u>444,000</u>	<u>(98,239)</u>	<u>431,650</u>	<u>(70,877)</u>
	<u>444,000</u>	<u>(84,395)</u>	<u>431,650</u>	<u>(57,033)</u>
Net income (loss) and comprehensive income (loss)	1,123,639	(300,255)	1,510,097	(288,714)
Retained earnings, beginning of period	3,188,921	4,118,510	2,923,649	4,106,969
Acquisition of shares in excess of carrying value (note 5[c])	<u>(180,706)</u>	<u>-</u>	<u>(301,892)</u>	<u>-</u>
Retained earnings, end of period	<u>\$ 4,131,854</u>	<u>\$ 3,818,255</u>	<u>\$ 4,131,854</u>	<u>\$ 3,818,255</u>
Net income (loss) and comprehensive Income (loss) per share:				
- Basic (note 5)	<u>\$ 0.07</u>	<u>\$ (0.02)</u>	<u>\$ 0.10</u>	<u>\$ (0.02)</u>
- Diluted	<u>\$ 0.07</u>	<u>\$ (0.02)</u>	<u>\$ 0.09</u>	<u>\$ (0.02)</u>

TWOOCO PETROLEUMS LTD.

Statements of Cash Flows

(unaudited)

	Three Months Ended		Six Months Ended	
	June 30, 2008	June 30, 2007	June 30, 2008	June 30, 2007
Cash provided by (used for):				
Operating activities				
Net income (loss)	\$ 1,123,639	\$ (300,255)	\$ 1,510,097	\$ (288,714)
Add items not affecting cash				
Stock-based compensation	4,556	42,228	7,612	81,401
Future income taxes	444,000	(98,239)	431,650	(70,877)
Convertible debentures accretion	13,333	13,333	26,666	26,666
Amortization of convertible				
debentures financing charges	18,532	10,865	37,064	31,313
Depletion, amortization and accretion	1,945,071	2,400,873	4,225,872	4,539,349
Settlement of asset retirement obligations	-	(45,135)	-	(45,135)
	<u>3,549,131</u>	<u>2,023,670</u>	<u>6,238,961</u>	<u>4,274,003</u>
Change in non-cash working capital (note 7[a])	<u>(1,220,950)</u>	<u>254,298</u>	<u>(1,345,199)</u>	<u>(79,149)</u>
	<u>2,328,181</u>	<u>2,277,968</u>	<u>4,893,762</u>	<u>4,194,854</u>
Financing activities				
Repayments of obligations under capital leases	(54,664)	(51,461)	(108,509)	(102,152)
Refund of financing charges on convertible debentures	-	23,000	-	23,000
Exercise of stock options	-	-	625,000	-
Share issuance costs	(557)	(500)	(557)	(500)
Repurchase of common shares	<u>(307,042)</u>	<u>-</u>	<u>(517,152)</u>	<u>-</u>
	<u>(362,263)</u>	<u>(28,961)</u>	<u>(1,218)</u>	<u>(79,652)</u>
Investing activities:				
Acquisition of property, plant and equipment	(2,169,789)	(3,385,337)	(3,487,038)	(10,962,230)
Change in non-cash working capital (note 7[a])	<u>741,770</u>	<u>(360,428)</u>	<u>861,662</u>	<u>(72,384)</u>
	<u>(1,428,019)</u>	<u>(3,745,765)</u>	<u>(2,625,376)</u>	<u>(11,034,614)</u>
Cash inflow (outflow)	537,899	(1,496,758)	2,267,168	(6,919,412)
Cash and cash equivalents, beginning of period	<u>(4,480,590)</u>	<u>(3,554,946)</u>	<u>(6,209,859)</u>	<u>1,867,708</u>
Cash and cash equivalents, end of period	<u>\$ (3,942,691)</u>	<u>\$ (5,051,704)</u>	<u>\$ (3,942,691)</u>	<u>\$ (5,051,704)</u>
Cash and cash equivalents is comprised of:				
Deposits with bank	\$ -	\$ 235,027	\$ -	\$ 235,027
Bank indebtedness	<u>(3,942,691)</u>	<u>(5,286,731)</u>	<u>(3,942,691)</u>	<u>(5,286,731)</u>
	<u>\$ (3,942,691)</u>	<u>\$ (5,051,704)</u>	<u>\$ (3,942,691)</u>	<u>\$ (5,051,704)</u>

Supplemental cash flow information (note 7)

TWOCO PETROLEUMS LTD.

Notes to Financial Statements

June 30, 2008
(unaudited)

1. Basis of Presentation

The interim financial statements of Twoco Petroleum Ltd. ("the Company") have been prepared by management in accordance with Canadian generally accepted accounting principles. The interim financial statements have been prepared following the same accounting policies and methods of computation as those utilized in the December 31, 2007 annual financial statements. The interim financial statements contain disclosures which are supplemental to the Company's annual financial statements. Certain disclosures which are normally required to be included in the notes to the annual financial statements have been condensed or omitted. The interim financial statements should be read in conjunction with the Company's audited financial statements and notes thereto for the year ended December 31, 2007.

2. Changes in Accounting Policies

Financial Instruments - Disclosures and Presentation

Effective January 1, 2008, the Company adopted two new Canadian Institute of Chartered Accountants ("CICA") standards. Handbook Section 3862, "Financial Instruments - Disclosures" and Handbook Section 3863, "Financial Instruments - Presentation". These Handbook Sections replaced existing Handbook Section 3861, "Financial Instruments - Presentation and Disclosure". The new disclosure standard increases the emphasis on the risks associated with both recognized and unrecognized financial instruments and how those risks are managed. Specifically, Section 3862 requires disclosure of the significance of financial instruments on the Company's financial position. In addition, the guidance outlines revised requirements for the disclosure of qualitative and quantitative information regarding exposure to risks arising from financial instruments. Refer to note 9, "Financial Instruments and Risk Management" for the additional disclosures under Section 3862. The new presentation standard carries forward the former presentation requirements.

Capital Disclosures

Effective January 1, 2008, the Company adopted CICA Handbook Section 1535 - "Capital Disclosures", which requires companies to disclose their objectives, policies and processes for managing capital, the nature of externally imposed capital requirements, how the requirements are incorporated into the Company's management of capital, whether the requirements have been complied with, or consequence of non-compliance and an explanation of how the Company is meeting its objectives for managing capital. In addition, quantitative disclosures regarding capital are required. Refer to note 8, "Capital Disclosures".

In addition, the Company has assessed new and revised accounting pronouncements that have been issued that are not yet effective and determined that the following may have a significant impact on the Company:

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2. Changes in Accounting Policies (continued)

Goodwill and Intangible Assets

As of January 1, 2009, the Company will be required to adopt CICA Section 3064, "Goodwill and Intangible Assets", which will replace CICA Section 3062. This new guidance reinforces a principles-based approach to the recognition of costs as assets in accordance with the definition of an asset and the criteria for asset recognition under CICA Section 1000, "Financial Statement Concepts". Section 3064 clarifies the application of the concept of matching revenues and expenses in Section 1000 to eliminate the current practice of recognizing as assets items that do not meet the definition and recognition criteria. Under this new guidance, fewer items meet the criteria for capitalization. The Company is currently determining the impact of this standard.

International Financial Reporting Standards

In January 2006, the CICA Accounting Standards Board adopted a strategic plan for the direction of accounting standards in Canada. As part of the plan, accounting standards in Canada for public companies will converge with International Financial Reporting Standards ("IFRS") on January 1, 2011. The Company continues to monitor and assess the impact of the convergence of Canadian GAAP and IFRS.

3. Convertible Debentures Payable

On March 31, 2006, the Company closed a private placement financing through the issuance of \$12 million of redeemable, convertible, unsecured debentures ("Convertible Debentures"). The Convertible Debentures bear interest at a rate of 7.5% per annum, payable commencing September 30, 2006 and quarterly thereafter and will mature on March 31, 2009 (the "Maturity Date"). Finder's fees and commissions previously recorded as deferred financing charges have been netted against convertible debentures payable. Amortization expense on convertible debentures financing charges of \$37,064 has been recognized for the six months ended June 30, 2008 (June 30, 2007 - \$31,313).

The Convertible Debentures will be convertible into common shares of the Company at the holder's option at any time prior to the Maturity Date at a conversion price of \$8.25 per share. The Company will have the ability to redeem the Convertible Debentures if the closing price of its common shares on the TSX Venture Exchange exceeds \$8.25 for 21 consecutive trading days or in certain circumstances where an offer is made to acquire common shares of the Company.

A market rate of interest for a non-convertible debt offering, representative of the Company's credit standing would be 8%. Therefore, the Company has received an interest benefit of 0.5% for the holder's conversion right, over the three year life of the debenture. The present value of this conversion benefit of \$160,000 was recorded on the financial statements as the equity portion of convertible debentures. The portion of convertible debentures classified as debt was initially determined to be \$11,840,000. The debt portion of the debentures will accrete up to the face value over the term to maturity. Accretion of \$26,666 has been recognized in interest expense for the six months ended June 30, 2008 (June 30, 2007 - \$26,666).

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4. Asset Retirement Obligations

The total future asset retirement obligation was estimated by management based on the Company's net ownership interest in all wells and facilities, estimated costs to reclaim and abandon said wells and facilities and the estimated timing of such abandonment.

The following table reconciles the Company's total asset retirement obligations:

	<u>June 30, 2008</u>	<u>December 31, 2007</u>
Balance, beginning of year	\$ 2,762,151	\$ 2,551,724
Accretion expense	82,867	139,480
Liabilities incurred	74,952	340,566
Liabilities incurred due to changes in estimate	(32,461)	(197,052)
Liabilities settled	<u>-</u>	<u>(72,567)</u>
Balance, end of year	<u>\$ 2,887,509</u>	<u>\$ 2,762,151</u>

Total estimated future retirement costs of \$3,973,975 (2007 - \$3,927,093) have been inflated at a weighted average estimated inflation rate of 2.00% (2007 - 1.95%) and discounted using a weighted average credit adjusted risk-free rate of 6.00% (2007 - 6.01%).

5. Share Capital

(a) Issued

	<u>Number</u>	<u>Stated Value</u>
Common Shares		
Balance, December 31, 2007	15,147,606	\$ 20,250,003
Pursuant to a normal course issuer bid	(159,900)	(215,817)
Exercise of stock options (note 5[b])	<u>500,000</u>	<u>846,926</u>
Balance, June 30, 2008	<u>15,487,706</u>	<u>\$ 20,881,112</u>

Per Share Amounts

The weighted average number of shares outstanding for the period ended June 30, 2008 was 15,659,146 (2007 - 15,259,806).

In computing diluted net income per share amounts, 568,723 (2007 - 633,602) shares were added to the weighted average number of common shares outstanding during the period ended June 30, 2008 for the dilutive effect of stock options.

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Notes to Financial Statements

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5. Share Capital (continued)

(a) Issued (continued)

The following reconciles the denominators for basic and diluted net earnings per share calculations:

	<u>Net Earnings (numerator)</u>	<u>Weighted Average Shares (denominator)</u>	<u>Per Share Amount</u>
Common Shares			
Basic net earnings per share	\$ 1,510,097	15,659,146	\$ 0.10
Dilutive securities:			
Options	-	568,723	
Diluted net earnings per share	\$ 1,510,097	16,227,869	\$ 0.09

(b) During the three months ended March 31, 2008, 500,000 stock options were exercised for gross cash proceeds of \$625,000. \$221,926 was reallocated from contributed surplus relating to those options.

(c) On October 16, 2007, the Company commenced a normal course issuer bid under which it can repurchase up to 750,000 of its common shares until October 16, 2008. All common shares purchased by the Company will be returned to treasury and cancelled. Although the Company has the intention to acquire common shares, it is not obliged to make any purchases pursuant to this 2007 issuer bid. For the period ended June 30, 2008, the Company acquired 159,900 (2007 - NIL) common shares at an average price of \$3.28. The excess cost of re-acquisition over stated value in the amount of \$301,892 (2007 - \$NIL) has been charged to retained earnings.

6. Contributed Surplus

The following table reconciles the Company's contributed surplus:

	<u>June 30, 2008</u>	<u>December 31, 2007</u>
Balance, beginning of year	\$ 1,128,929	\$ 985,181
Stock-based compensation expense	7,612	165,859
Exercise of stock options	(221,926)	(22,111)
Balance, end of year	\$ 914,615	\$ 1,128,929

TWOCO PETROLEUMS LTD.

Notes to Financial Statements

June 30, 2008
(unaudited)

7. Supplemental Cash Flow Information

(a) Changes in Non-cash Working Capital

	<u>June</u> <u>30, 2008</u>	<u>June</u> <u>30, 2007</u>
Accounts receivable	\$ (1,212,283)	(240,921)
Prepaid expenses and deposits	31,031	247,431
Accounts payable and accrued liabilities	<u>697,715</u>	<u>(158,043)</u>
	<u>\$ (483,537)</u>	<u>\$ (151,533)</u>
Change in non-cash working capital relating to:		
Investing activities	\$ 861,662	\$ (72,384)
Operating activities	<u>(1,345,199)</u>	<u>(79,149)</u>
	<u>\$ (483,537)</u>	<u>\$ (151,533)</u>

(b) The following non-cash transactions have been excluded from the statements of cash flows:

	<u>June</u> <u>30, 2008</u>	<u>June</u> <u>30, 2007</u>
Asset retirement liabilities incurred	<u>\$ 42,491</u>	<u>\$ 355,117</u>

(c) Interest and Taxes

	<u>3 Months</u> <u>Ended</u> <u>June</u> <u>30, 2008</u>	<u>3 Months</u> <u>Ended</u> <u>June</u> <u>30, 2007</u>	<u>6 Months</u> <u>Ended</u> <u>June</u> <u>30, 2008</u>	<u>6 Months</u> <u>Ended</u> <u>June</u> <u>30, 2007</u>
Interest paid	<u>\$ 287,471</u>	<u>\$ 302,441</u>	<u>\$ 598,874</u>	<u>\$ 548,648</u>
Income taxes paid	<u>\$ -</u>	<u>\$ 13,844</u>	<u>\$ -</u>	<u>\$ 13,844</u>

8. Capital Disclosures

The Company's objectives when managing capital are: (i) to maintain a flexible capital structure, which optimizes the cost of capital at acceptable risk; and (ii) to maintain investor, creditor and market confidence to sustain the future development of the business.

The Company manages its capital structure and makes adjustments to it in light of changes in economic conditions and the risk characteristics of our underlying assets. The Company considers its capital structure to include shareholders' equity, debt and working capital. To maintain or adjust the capital structure, the Company may from time to time, issue shares, raise debt and/or adjust its capital spending to manage its current and projected debt levels.

TWOCO PETROLEUMS LTD.

Notes to Financial Statements

June 30, 2008

(unaudited)

8. Capital Disclosures (continued)

The Company monitors capital based on the current and projected ratios of debt to cash flow and debt to capital employed. The Company's objective is to maintain a debt to cash flow from operations ratio of less than two times. The ratio may increase at certain times as a result of acquisitions. To facilitate the management of this ratio, the Company prepares annual budgets, which are updated depending on varying factors such as general market conditions and successful capital deployment. The annual budget is approved by the Board of Directors.

The Company's share capital is not subject to external restrictions.

There were no changes in the Company's approach to capital management from the previous year.

9. Financial Instruments and Risk Management

(a) Fair Values

The Company's financial instruments consist of bank indebtedness, accounts receivable, accounts payable and accrued liabilities, obligations under capital lease, convertible debentures payable and bank indebtedness. The fair value of these instruments approximate their carrying amounts due to their short terms to maturity or because they bear interest at market rates for similar instruments.

(b) Credit Risk

Virtually all of the Company's accounts receivable are due from joint venture partners in the oil and gas industry and from purchasers of the Company's petroleum and natural gas production and are subject to normal industry credit risks. The Company generally extends unsecured credit to these parties and therefore, the collection of accounts receivable may be affected by changes in economic or other conditions. Management believes the risk is mitigated by the size and reputation of the companies to which they extend credit.

Receivables from petroleum and natural gas marketers are normally collected on the twenty-fifth day of the month following production. Receivables related to the sale of the Company's petroleum and natural gas production are from major marketing companies with investment grade credit ratings. The Company historically has not experienced any collection issues with its petroleum and natural gas marketers.

Joint venture receivables are typically collected within one to three months of the joint venture bill being issued to the partner. The Company attempts to mitigate the risk from joint venture receivables by obtaining partner approval of significant capital expenditures prior to expenditure and issuing cash calls on large capital projects from its partners on capital projects before they commence. The Company reviews the financial status of joint venture partners before partner approval is obtained.

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(unaudited)

(c) Liquidity Risk

Liquidity risk relates to the risk the Company will encounter difficulty in meeting obligations associated with financial liabilities. The financial liabilities on its balance sheet consist of accounts payable and accrued liabilities, obligations under capital lease, convertible debentures payable and bank indebtedness. Management closely monitors cash flow requirements to ensure that it has sufficient cash on demand or borrowing capacity to meet operational and financial obligations.

(d) Market Risk

Market risk is the risk that changes in market prices, such as foreign exchange rates, commodity prices, and interest rates will affect the Company's net earnings or the value of financial instruments. These risks are generally outside the control of the Company. The objective of the Company is to mitigate market risk exposures within acceptable limits, while maximizing returns.

(e) Interest Rate Risk

The Company is exposed to interest rate cash flow risk on its outstanding bank indebtedness which has a floating interest rate and would impact the Company's future cash flows. The Company had no interest rate swaps or hedges at June 30, 2008.

In regards to interest rate risk, an increase or decrease of one percent to the effective interest rate for the Company would have impacted net earnings by \$19,659 for the period.

(f) Foreign Currency Risk

The Company is exposed to foreign currency fluctuations as crude oil and natural gas prices are referenced to U.S. dollar denominated prices. As at June 30, 2008, the Company had no forward foreign exchange contracts in place, nor any significant working capital items denominated in foreign currencies.

(g) Commodity Price Risk

The nature of the Company's operations results in exposure to fluctuations in commodity prices. As at June 30, 2008, the Company had no derivative natural gas contracts in place.

In regards to commodity prices, a \$0.25 change to the price per thousand cubic feet of natural gas would have impacted net earnings by approximately \$181,737 for the period, whereas a \$0.25 decrease to the price per thousand cubic feet of natural gas would have decreased net earnings by approximately \$231,256 for the period.

10. Subsequent Events

Subsequent to June 30, and pursuant to the Normal Course Issuer Bid dated October 16, 2007, the Company repurchased 117,600 common shares at prices ranging between \$3.00 to \$3.40 per share for gross consideration of \$390,585. This Normal Course Issuer Bid expires October 16, 2008.

Subsequent to June 30, 2008, 40,000 stock options were exercised for gross cash proceeds of \$50,000.