KENARTHA OIL AND GAS COMPANY LIMITED

FINANCIAL STATEMENTS

MARCH 31, 2005

Hilborn Ellis Grant LLP
Chartered Accountants
Toronto, Ontario

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Chartered Accountants

Auditors' Report

To the Shareholders of
Kenartha Oil and Gas Company Limited

We have audited the balance sheets of **Kenartha Oil and Gas Company Limited** as at March 31, 2005 and March 31, 2004 and the statements of income, retained earnings and cash flows for the years then ended. These financial statements are the responsibility of the company's management. 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 plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the company as at March 31, 2005 and March 31, 2004 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Hilborn Ellis Grant LLP

Toronto, Ontario
July 18, 2005

Chartered Accountants

Balance Sheet

March 31, 2005	**2005**	2004
	$	$
ASSETS		
Current Assets		
Cash	**16,785**	9,263
Accounts receivable	**15,701**	23,762
Deposits *(notes 7(d) and (e))*	**58,150**	11,150
Prepaid expenses	**4,645**	4,645
	95,281	48,820
Long-term Assets		
Equipment *(note 3)*	**62,482**	72,062
	157,763	120,882
LIABILITIES		
Current Liabilities		
Accounts payable and accrued liabilities *(notes 1 and 4)*	**125,489**	108,395
Note payable *(note 5)*	**140,500**	140,500
	265,989	248,895
SHAREHOLDERS' EQUITY (DEFICIENCY IN ASSETS)		
Capital stock *(note 6)*	**2,427,000**	2,427,000
Deficit	**(2,535,226)**	(2,555,013)
	(108,226)	(128,013)
	157,763	120,882

Approved on behalf of the Board:

(signed) Ernest W. Harrison, Director

(signed) Marty Martinello, Director

KENARTHA OIL AND GAS COMPANY LIMITED

Statement of Income

Year ended March 31, 2005	**2005**	**2004**
	$	**$**
Revenue		
Sales of natural gas	**204,126**	185,118
Expenses		
Production royalties *(note 4(a))*	**50,728**	52,450
Field supplies and maintenance *(note 4(b))*	**40,127**	38,903
Rent	**14,546**	15,600
Professional fees	**7,950**	5,000
Management fees *(note 4(b))*	**25,168**	-
General and administrative	**17,764**	19,439
Interest *(note 5)*	**6,476**	7,806
Amortization	**21,580**	19,827
	184,339	159,025
Income before income taxes	**19,787**	26,093
Income taxes	**11,369**	9,654
Recovery on application of prior years' losses	**(11,369)**	(9,654)
	-	-
Net income for year	**19,787**	26,093
Earnings per share	**.0025**	.0033

Statement of Retained Earnings

Year ended March 31, 2005	**2005**	**2004**
	$	**$**
Deficit, beginning of year	**(2,555,013)**	(2,581,106)
Net income for year	**19,787**	26,093
Deficit, end of year	**(2,535,226)**	(2,555,013)

Statement of Cash Flows

Year ended March 31, 2005	**2005** $	**2004** $
Cash flows from operating activities		
Net income for year	**19,787**	26,093
Item not requiring a current cash payment		
Amortization	**21,580**	19,827
	41,367	45,920
Changes in non-cash working capital		
Decrease in accounts receivable	**8,061**	29,059
Increase in deposits	**(47,000)**	-
Increase in prepaid expenses	**-**	(2,789)
Increase (decrease) in accounts payable	**17,094**	(23,202)
	19,522	48,988
Cash flows from investing activities		
Purchase of equipment	**(12,000)**	(51,075)
Increase (decrease) in cash during year	**7,522**	(2,087)
Cash, beginning of year	**9,263**	11,350
Cash, end of year	**16,785**	9,263

	2005 $	**2004** $
Supplementary Disclosure of Cash Flow Information		
Interest paid	6,476	7,806
Income taxes paid	-	-

March 31, 2005

1. **Basis of Presentation**

These financial statements have been prepared on a going concern basis, which contemplates that the company will be able to discharge its liabilities in the normal course of operations.

In order to continue in operation, the company requires extended payment terms on the amount due to a corporation, which is a member of the controlling group and the amount due under the note payable.

2. **Significant Accounting Policies and General**

a) **Amortization**

Amortization of equipment has been provided for on the declining balance method as follows:

Pipeline	- 20% per annum
Compressor	- 30% per annum
Equipment	- 20% per annum

b) **Financial instruments**

The company's financial instruments consist of cash, accounts receivable, deposits, accounts payable and accrued liabilities and note payable. The fair values of these financial instruments approximate their carrying values, unless otherwise noted.

c) **Management estimates**

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 disclosures of contingent liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

3. **Equipment**

	Cost $	Accumulated Amortization $	2005 Net $	2004 Net $
Pipeline	76,045	74,567	1,478	1,846
Compressor	195,445	134,472	60,973	70,173
Equipment	4,807	4,776	31	43
	276,297	213,815	62,482	72,062

March 31, 2005

4. **Related Party Transactions**

   a) Production royalty expense includes $25,513 (2004 - $23,140) charged by a corporation for which a director of the company is an officer. The corporation has been assigned a 12½% royalty on natural gas sales as an inducement with respect to financial assistance the corporation provided to Kenartha Oil and Gas Company Limited as detailed in note 5.

   b) A corporation, which is a member of the controlling group, provides management services to this company and makes certain payments on its behalf. Management fees of $25,168 (2004 - $nil) and field expenses of $8,729 (2004 - $nil) have been charged in this respect. Included in accounts payable are amounts due to the corporation totalling $24,203 (2004 - $nil).

5. **Note Payable**

   The promissory note due to a related corporation as described in note 4(a) is due on demand and bears interest at the Bank of Nova Scotia's prime lending rate, compounded monthly.

6. **Capital Stock**

   a) **Authorized**

2,000,000	voting, redeemable (at 1/10th of 1 cent each) non-participating preference shares
Unlimited	common shares

   b) **Issued**

500,000	preference shares	$ 500
7,895,790	common shares	2,426,500
		$2,427,000

   c) **Stock option plan**

   The company has a designated stock option plan ("DSOP") permitting the granting of options to officers, employees and consultants. On April 6, 2000, the directors reserved 131,496 common shares to the DSOP, at an option price of $0.20 per share, which must be allotted within five years. Pursuant to a stock dividend declared on May 10, 2002, the DSOP reserved common shares were increased to 788,976 shares. The option price of the additional 657,480 reserved common shares has yet to be fixed by the directors, but shall not be less than the fair market value of the outstanding common shares at the time the stock dividend was declared. The limit for the DSOP is 10% of the issued common shares and for a single participant, 5% of the issued common shares. No options have been allocated and granted under the DSOP. In 2003 the company passed a resolution to cancel the reservation of common shares under the DSOP.

7. **Commitments and Contingencies**

a) In common with other corporations in the gas industry, the company self-insures for any costs related to environmental matters. No events have occurred which might give rise to liability for site cleanup costs and no estimate can be made of future costs, if any, related to environmental matters.

b) The company is committed to make lease payments of $1,000 annually until 2005 for its revenue producing property. As at the financial statement reporting date, the company was in the process of negotiating a renewal of this lease.

c) On June 1, 2005, the company entered into a three-year premises lease requiring monthly payments of $1,168.

d) Deposits in the amount of $11,150 (2004 - $11,150) are held by the Ontario Ministry of Natural Resources for the company's three gas well leases. Under current legislation, an increase in deposits, to a maximum of $22,000, will be phased in over the next several years.

e) The company has entered into an agreement to purchase a 49% working interest in certain oil and gas wells to be drilled. To obtain the working interest the company is required to finance the drilling costs of each individual well. The number of wells in which the company acquires an interest is dependent on the amount of financing raised by the company.

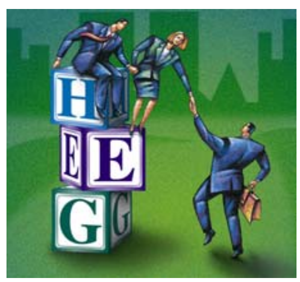
To finance the company's participation in the project described above the company issued a private placement offering memorandum dated March 17, 2005, which offers up to 400 units in the share capital of the company at $5,000 per unit; each unit consisting of 1,000 flow through common shares to be issued from the treasury of the company and one full warrant. The company will renounce its claim for Canadian Exploration Expenses to the holders of the flow through common shares. The warrants are exercisable at $2,500 each and will have the right to retain a net profit interest royalty of 24% in each of the above drilled wells that are purchased by capital raised under the offering memorandum, after the repayment from net profits of the expenditures paid by the company for drilling the wells. The company's net profit interest will accordingly be reduced to 25% for those wells financed by warrants. Included in deposits, is $47,000 advanced to begin drilling the first well in this project. No common shares have been issued for this project to the date of the Auditors' Report.

8. **Tax Losses Carried Forward**

a) The company has accumulated non-capital losses for income tax purposes of $42,086, which can be carried forward to be applied against taxable income. The right to use these losses expires in 2008.

In addition, the company has approximately $144,000 in amounts that have been deducted for accounting purposes that have not, as yet, been deducted for income tax purposes, relating to its equipment. The future income tax benefit related to this difference has not been recognized in the accounts.

b) The company has net capital losses of $250,607, which can be carried forward indefinitely to be applied against future taxable capital gains.



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Hilborn Ellis Grant LLP
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