

CANADIAN PHOENIX RESOURCES CORP.

Consolidated Financial Statements

For the years ended December 31, 2008 and 2007

April 30, 2009

Auditors' Report

To the Shareholders of Canadian Phoenix Resources Corp.

We have audited the consolidated balance sheets of Canadian Phoenix Resources Corp. as at December 31, 2008 and 2007 and the consolidated statements of operations, comprehensive loss and deficit 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, the consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2008 and 2007 and the results of its operations and cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

PricewaterhouseCoopers LLP

Chartered Accountants
Calgary, Alberta

CANADIAN PHOENIX RESOURCES CORP.
Consolidated Balance Sheet

	December 31, 2008 \$	December 31, 2007 \$
Assets		
Current assets		
Cash	10,402,670	1,285,235
Cash held in trust (note 4)	2,007,559	17,775,000
Accounts receivable (note 5)	6,733,166	1,561,834
Prepaid expenses	240,188	158,400
	19,383,583	20,780,469
Equity Investment (note 7)	43,129,618	—
Goodwill (notes 3a, 8)	—	—
Property, plant and equipment (note 6)	83,161,732	32,643,473
	145,674,933	53,423,942
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities (note 9)	25,254,427	3,604,400
Operating loan payable (note 11)	—	1,980,000
	25,254,427	5,584,400
Long term debt – debentures (note 12)	—	9,019,153
Future income tax liability (note 13)	4,827,942	1,947,086
Asset retirement obligation (note 10)	4,551,669	565,906
	34,634,038	17,116,545
Non-controlling interest (note 3a, 14)	26,777,183	—
Shareholders' Equity		
Share capital (note 15a, 15b)	118,977,580	40,496,130
Warrants (note 15d)	32,087,679	2,445,731
Contributed surplus (note 15c)	3,456,588	2,161,086
Deficit	(70,258,135)	(8,795,550)
	84,263,712	36,307,397
	145,674,933	53,423,942
Going concern (note 1)		
Commitments & contingencies (note 16)		
Subsequent events (note 20)		

See accompanying notes to the consolidated financial statements

On behalf of the Board of Directors:

“Robert J. Chenery”

Director

“D. Barry Lee”

Director

CANADIAN PHOENIX RESOURCES CORP.
Consolidated Statement of Operations, Comprehensive Loss and Deficit

	December 31 2008 \$	December 31 2007 \$
Revenue		
Oil and natural gas	9,185,496	5,446,928
Royalties	(2,358,480)	(1,311,176)
	6,827,016	4,135,752
Expenses		
Operating costs	3,086,837	1,521,503
Depletion, depreciation and accretion (note 6a)	7,805,758	3,473,770
Impairment of property, plant, & equipment (note 6b)	18,550,243	—
Impairment of goodwill (note 8)	7,587,513	—
Stock based compensation (note 14, 15c)	2,831,445	459,668
General and administrative	7,722,522	5,121,184
Financing fees (note 11)	5,092,427	—
Interest accretion – debentures (note 12)	1,575,284	3,085,917
Interest expense	1,653,712	380,149
Legal settlement (note 9, 20)	1,100,000	—
Other (income)	(728,286)	(1,241,991)
	56,277,455	12,800,200
Net loss before equity investment, non-controlling interest and tax	(49,450,439)	(8,664,448)
Net loss – equity investment (note 7)	(2,811,597)	—
Impairment of equity investment (note 7)	(19,000,000)	—
Net loss – non-controlling interest (note 14)	3,347,831	—
Net loss for the year before taxes	(67,914,205)	(8,664,448)
Current income tax recovery/(expense)	(8,356)	30,000
Future income tax recovery (note 13)	6,459,976	2,685,758
Net loss and comprehensive loss for the year	(61,462,585)	(5,948,690)
Deficit, beginning of year	(8,795,550)	(2,846,860)
Deficit, end of year	(70,258,135)	(8,795,550)
Net loss per share		
Basic and Diluted (note 15e)	(0.09)	(0.10)

See accompanying notes to the consolidated financial statements

CANADIAN PHOENIX RESOURCES CORP.
Consolidated Statement of Cash Flows

	December 31, 2008	December 31, 2007
Cash provided by (used in)		
Operating activities		
Net loss after tax for the year	(61,462,585)	(5,948,690)
Items not affecting cash		
Non-controlling interest	(3,347,831)	
Depletion, depreciation & accretion	7,805,758	3,473,770
Impairment – PP&E	18,550,243	—
Impairment – goodwill	7,587,513	—
Impairment – equity investment	19,000,000	—
Impairment – debtors	300,000	—
Equity investment loss	2,811,597	—
Stock-based compensation	2,831,445	459,668
Financing fees settled with shares	4,592,427	—
Interest accretion on debentures	1,575,284	3,085,917
Future tax recovery	(6,459,976)	(2,715,758)
Funds from operations	(6,216,125)	(1,645,093)
Change in non-cash working capital – operating activities	3,467,684	(4,367,922)
	(2,748,441)	(6,013,015)
Financing activities		
Decrease in bank loan	(1,980,000)	(2,925,000)
Financing fees paid	(500,000)	—
Issuance of common shares for cash, net of costs	44,601,425	22,036,312
Long term debenture issue	—	5,933,235
Change in non-cash working capital – financing activities	—	—
	42,121,425	25,044,547
Investing activities		
Business acquisition (net of cash acquired of \$6,851,754)	(12,311,158)	—
Equity investment	(11,553,088)	—
Acquisition of petroleum and natural gas properties	(25,997,569)	(793,688)
Proceeds from disposal of petroleum and natural gas properties	—	981,046
Movement in restricted cash/cash held in trust	15,767,441	(17,775,000)
Change in non-cash working capital – investing activities	3,838,825	(166,893)
	(30,255,549)	(17,754,535)
Increase in Cash	9,117,435	1,276,997
Cash, beginning of year	1,285,235	8,238
Cash, end of year	10,402,670	1,285,235
Taxes Paid	9,756	—
Interest paid	1,080,549	380,149

See accompanying notes to the consolidated financial statements

1. BASIS OF PREPARATION

Canadian Phoenix Resources Corp. (the “Corporation”) is engaged in the exploration, development and production of oil and natural gas in Western Canada. Effective January 3, 2008 pursuant to Section 173(3) of the Business Corporations Act (Alberta), the Corporation changed its name from Arapahoe Energy Corp. to Canadian Phoenix Resources Corp. The consolidated financial statements as at and for the year ending December 31, 2008 are comprised of the Corporation and its controlled entities (the “Group”).

The financial statements of the Group are stated in Canadian dollars and have been prepared in accordance with Canadian generally accepted accounting principles (“GAAP”).

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of revenues and expenses, assets and liabilities, and disclosure of contingent assets and liabilities. Key sources of judgment and estimation uncertainty are discussed in accounting policy Note 2(m).

Going concern

The financial statements have been prepared in accordance with GAAP on a going concern basis, which contemplates the realization of assets and the settlement of liabilities in the ordinary course of business. Should the Group be unable to continue as a going concern, it may be unable to realize the carrying value of its assets and meet its liabilities as they become due. The financial statements do not include any adjustments related to the recoverability and classification of recorded asset amounts and classification of liabilities that might be necessary should the Corporation or its subsidiary Serrano Energy Ltd. (“Serrano”) be unable to continue in existence. Such adjustments could be material.

The Group reported a loss of \$61.5 million and a net operating cash outflow of \$2.7 million for the year ended December 31, 2008, and at December 31, 2008 the Corporation had accumulated losses of \$70.3 million. At December 31, 2008 the Group had net assets of \$111.2 million, a working capital deficiency of \$5.9 million, no external long-term debt, and capital expenditure commitments of approximately \$8 million.

The Group’s ability to continue as a going concern is dependent on its ability to secure debt facilities or other external funding to meet its expected cash outflows for 2009, and more generally, on increased oil and natural gas prices to improve operating cashflows. It is also dependent on the ability of its subsidiary (Serrano) to renegotiate payment terms with its creditors. Subsequent to year end, Serrano has reached agreements with certain trade creditors to settle payables with share issuances, and has negotiated deferred payment plans with certain other creditors. As at April 2009, the Corporation and its subsidiary are also negotiating revolving credit facilities with expected limits of \$0.6 million (the Corporation) and \$6 million (Serrano).

It is the view of the directors that the Group should be able to finalize the credit facilities referred to above, and otherwise raise further debt or equity capital when needed to fund ongoing operations and exploration and development activities. However, given the current economic recession and weak oil and gas prices, access to either debt or equity financing is difficult and there is no assurance that management’s initiatives will be successful. Should a debt or equity financing not be obtained, the Group would be forced to curb exploration, development, general and

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administrative costs permanently or until such time as market conditions improve to allow a financing to proceed. In that scenario, there is significant doubt as to the ability of the Group to continue as a going concern, and the going concern basis of accounting may not be appropriate.

2. ACCOUNTING POLICIES

(a) Principles of Consolidation

The consolidated financial statements of the Group include the following controlled subsidiaries:

- Serrano – 47% (acquired August 20, 2008)
- CPH-Sarcee Corporation – 100% (incorporated November 6, 2008)

CPH – Sarcee Corp. had no assets or liabilities as at December 31, 2008.

The acquisition of Serrano was accounted for under the purchase method, whereby the Corporation recorded its acquired interest in Serrano's net identifiable assets at fair value, with the excess of consideration paid recorded as goodwill. The non-controlling interest was recorded at the book value of Serrano's net identifiable assets, in accordance with Canadian accounting standards.

Refer Note 3(a) for details of the Serrano acquisition and determination of control.

The non-controlling interest account in the consolidated financial statements is adjusted for post-acquisition movements in the book value of the net assets of Serrano, and post-acquisition movements in Serrano's warrants and option equity reserves. The net income or loss attributable to the non-controlling interest is shown in the consolidated income statement, and the non-controlling interest in the consolidated balance sheet is shown between non-current liabilities and shareholders' equity.

Post-acquisition decreases in the Corporation's ownership interest in its subsidiaries due to disposition of shares held or a share issuance by the subsidiary to outside interests are reflected as an increase to the non-controlling interest, with any difference between the proceeds received by the consolidated group and the reduction in the Corporation's interest recorded as an adjustment to property, plant and equipment in accordance with full-cost accounting guidelines.

Post-acquisition increases in the Corporation's ownership interest in its subsidiaries due to additional share purchases or share cancellations or redemptions by the subsidiary are accounted for as a reduction in the non-controlling interest, and otherwise in a similar manner to the initial acquisition of a controlling interest. Any excess of the consideration provided over the fair value of the Corporation's incrementally acquired interest is accounted for as goodwill. Any excess of fair value incrementally acquired over the consideration provided is accounted for as a reduction in the fair value of non-current assets acquired, with any remainder accounted for as a gain in the consolidated statement of operations.

Equity Accounted Investee

Effective September 19, 2008, the Corporation acquired a 56.51% interest in Marble Point Energy Limited ('Marble Point'). The acquisition was accounted for under the equity method, as under the terms of the Corporate Governance agreement between the Corporation and Marble Point, the Corporation does not control Marble Point despite owning greater than 50% of the voting shares.

Equity accounted investments are initially recorded at cost and the carrying value is adjusted thereafter to include the investor's pro-rata share of post-acquisition earnings of the investee, computed by the consolidation method. Equity earnings/(losses) are included in the determination of net income by the investor, with a corresponding increase/(decrease) in the carrying value of the investment. The investment account is also increased or decreased to reflect the investor's share of capital transactions and changes in accounting policies and correction of errors relating to prior period financial statements applicable to post-acquisition periods. Profit distributions received or receivable from an investee reduce the carrying value of the investment.

(b) Property, plant and equipment

(i) Petroleum and natural gas properties

The Group follows the full cost method of accounting for petroleum and natural gas properties, whereby all costs directly related to exploring for and developing petroleum and natural gas reserves are capitalized. Costs include land acquisition costs, geological and geophysical costs, carrying charges on non-producing properties, costs of drilling both producing and non-producing wells, and overheads directly related to acquisition, exploration and development activities.

The capitalized costs, less the costs of unproven properties, are depleted using the unit-of-production method based upon estimated proved petroleum and natural gas reserves (before royalties) as determined by independent engineers. Production and reserves of natural gas are converted to equivalent barrels of crude oil on the basis of six thousand cubic feet of gas to one barrel of oil.

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 rate.

At least annually, the Group's net capitalized costs of property, plant and equipment (PP&E) is subject to a two-part impairment (ceiling) test:

- a. If the carrying amount of PP&E exceeds the sum of the undiscounted future net cash flows (based on estimates of future prices and costs) expected to result from proved reserves, then an indicator of impairment is considered to exist, and a discounted cashflow test (b) is applied.
- b. Impairment is recognized if the carrying amount of PP&E exceeds its fair value, being the estimated net present value of future cash flows from proved plus probable reserves. Future cashflows are discounted at the risk-free rate, as risk factors are included in the estimates of future cashflows. In circumstances of impairment, the calculated impairment is charged to current operations as additional depletion.

The ceiling test is performed on a consolidated basis, whereby the carrying value of PP&E subject to the test, and the estimated reserves and future cashflows reflects the Corporation's interest. Regarding equity accounted investments, the carrying value of PP&E intrinsic in the equity investment is utilized in performing the ceiling test.

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The cost of unproved properties and major development projects are excluded from the ceiling test calculation and subject to a separate impairment assessment. This separate assessment results in an impairment when properties are likely to be abandoned, leases are not likely to be renewed, or the probability of yielding economically recoverable reserves is considered remote. Any impairment thus determined is included in the costs subject to depletion.

Office equipment and furniture is carried at cost and amortized using the declining balance method at rates between 20% and 50%.

(ii) Asset retirement obligations

The Group recognizes the fair value of the liability for asset retirement obligations in the period it is incurred with a corresponding increase to the carrying amount of property, plant and equipment. The fair value of the obligation is calculated as the present value of the expected future costs of the abandonment and reclamation activities, based on engineering reports, industry guidelines and management estimates. The interest rate used to discount future costs is a real rate, being the nominal rate reduced for the expected impact of inflation over the period to when the costs are expected to be incurred. The liability is increased each reporting period through the accretion of interest up to the future amount of the liability. The charge for accretion is classified with depletion and depreciation in the income statement. The additional asset included within property, plant and equipment is amortized on the same basis as PP&E. Actual costs incurred upon settlement of the retirement obligation are charged against the liability.

c) Goodwill

Goodwill represents the excess of purchase price over the fair value of net assets acquired in a business combination. Goodwill is not amortized, but assessed for impairment at least annually. The test for impairment is conducted by comparing the book value of the entity to which the goodwill relates to its fair value, and if the book value is greater, an impairment is deemed to have occurred. The impairment amount is measured by first allocating the fair value of the entity to its net assets, with any remainder allocated to goodwill. If the goodwill value so determined is less than its carrying value, the difference is recorded in the income statement as an impairment charge.

d) Revenue recognition

Revenue from the sale of crude oil, natural gas and natural gas liquids is recorded when title passes to a third party, which is normally upon receipt of the product at the processing plant. Operating and transportation costs, and production-based royalties related to the sale of the product are recognized in the same period in which the revenue is recorded.

Oil and gas receivables are initially recorded at fair value, and an impairment allowance is recorded for specific receivables on which collection is wholly or partially uncertain.

e) Joint ventures

A significant portion of the Group's activities are conducted within unincorporated joint ventures. The financial statements reflect the Group's proportionate interest in such activities.

f) Cash and cash equivalents

Cash and cash equivalents include cash, and money market instruments that carry terms less than 91 days at the date of investment. Cash that is restricted under indemnity or other agreements is classified separately in the balance sheet.

g) Flow-through shares

Tax deductions for income tax purposes related to exploratory and development activities funded by flow-through share arrangements are renounced to investors in accordance with income tax legislation. Share capital is reduced, with a corresponding increase to the future tax liability, by the estimated value of the tax deductions lost to the Group at the time the renouncement documents are filed with the appropriate government agency.

h) Future income taxes

Income taxes are calculated using the liability method of tax accounting. Temporary differences arising from the difference between the tax basis of an asset or liability and its carrying amount in the balance sheet are recognized as future income tax assets and liabilities, using tax rates anticipated to apply in the years that the temporary differences are expected to reverse. Future income taxes are recorded for all temporary differences, with the exception of goodwill recognized on a business combination.

Future income tax assets are also recognized in relation to tax losses. A valuation allowance is recorded in relation to future income tax assets which are not considered more likely than not of recovery.

The future income tax impact of transactions affecting equity is also recorded in equity.

i) Long-term debt

Debt instruments are recognized at fair value, net of transaction costs ('amortized cost'). The difference between the net proceeds received and the amortized cost (e.g. due to discounts or premiums in relation to the stated interest rate, conversion features, equity instruments) is amortized to interest expense over the life of the debt instrument under the effective interest method. The effective interest rate is the rate that exactly discounts all future principal and interest payments to the initial amortized cost of the debt.

j) Stock-based compensation plans

Stock options granted to directors, officers, employees and consultants in return for services provided to the Group are accounted for using the fair value method under which compensation expense is determined based on the estimated fair value of the options at the grant date using the Black-Scholes option pricing model. Compensation cost is recognized in the income statement over the vesting period with a corresponding increase in contributed surplus. The vesting period is the period over which the recipient becomes unconditionally entitled to the options.

Compensation cost is reversed for those options that do not vest due to failure to meet the service conditions of the options granted.

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When stock options are exercised, the cash proceeds along with the amount previously recorded as contributed surplus are recorded as share capital.

Warrants to acquire shares are similarly valued at fair value at the grant date using an asset pricing model such as Black-Scholes. Warrants which are issued as part of an equity or debt raising process are accounted for as a reduction in the cost assigned to the equity or debt instrument with a corresponding amount recorded in shareholders' equity.

k) Share issue costs

Costs related to raising equity capital, including both cash costs and equity-based costs (shares/warrants/options), are accounted for as a reduction in share capital.

l) Per share amounts

Basic per share amounts are calculated using the weighted average number of shares outstanding during the year. Diluted per share calculations reflect the exercise or conversion of potentially dilutive securities or contracts to common shares at the later of the date of the grant of such securities or the beginning of the year. The treasury stock method is used to determine the dilutive effect of stock options and warrants. The treasury stock method assumes that the proceeds received from the exercise of "in-the-money" stock options and warrants are used to purchase common shares of the Corporation at their average market price for the year.

m) Use of estimates and measurement uncertainty

The preparation of the financial statements in accordance with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts and presentation of assets, liabilities, revenues, expenses and disclosures of contingencies and commitments. Such estimates primarily relate to unsettled transactions and events at the balance sheet date which are based on information available to management at each financial statement date. Actual results could differ from those estimated. Key sources of estimation uncertainty and judgment are discussed below.

The amounts recorded for depletion and depreciation of property, plant and equipment, the provision for asset retirement obligations, and the amounts used for the impairment test calculations are based on estimates of reserves, future commodity prices, royalties, operating costs, development costs, abandonment costs, and the fair value of unproven properties, all of which are inherently uncertain. The Group's reserve estimates are evaluated annually by an independent engineering firm.

The determination of stock-based compensation expense requires a calculation of the fair value of the equity instrument at grant date, which involves a number of estimates, in particular the volatility of the Corporation's future share price.

The recognition of future income tax assets requires judgment as to the existence of future taxable income or reversal of temporary differences to which the tax assets can be applied and benefit realized.

By their nature, these estimates are subject to measurement uncertainty and the effect of changes in such estimates on the financial statements for current and future periods could be significant.

n) Changes in Accounting Policies

On January 1, 2008, the Group adopted prospectively the following accounting standards prescribed by the Canadian Institute of Chartered Accountants:

CICA Handbook Section 3862 “Financial Instruments-Disclosures”. This section describes the required disclosures to evaluate the significance of financial instruments for the entity’s financial position and performance as well as the nature and extent of risks arising from both recognized and unrecognized financial instruments to which the entity is exposed and how the entity manages those risks. Refer Note 18 for the required new disclosure.

Section 3863 “Financial Instruments-Presentation”. This section establishes standards for the presentation of financial instruments and non-financial derivative instruments. It details the presentation of the standards described in Section 3861 “Financial Instruments-Disclosure and Presentation”. All financial instruments must be classified into one of the following five categories: held for trading, held-to-maturity, loans and receivables, available-for-sale financial assets, or other financial liabilities. All the Group’s financial instruments are either loans and receivables or financial liabilities.

Section 1535 “Capital Disclosures”. This section establishes standards for disclosing information about an entity’s objectives, policies and processes for how it manages its capital. A company must also disclose qualitative data about what the entity regards as capital, whether the company has complied with any capital requirements and if not, the consequences of such non-compliance. Refer Note 19 for the required new disclosure.

The adoption of these standards had no effect on the Group’s net income or cashflows or on opening retained losses.

Future Changes in Accounting Standards – effective 2009

CICA Handbook Section 3064, “Goodwill and Intangible Assets” is effective for periods beginning on or after October 1, 2008. The Group will be required to adopt this standard in the 2009 fiscal year. The standard replaces CICA sections 3062 and 3450 and provides guidance relating to the recognition, measurement, presentation and disclosure of goodwill and intangible assets. The Corporation does not expect that the adoption of this standard will have a material effect on the consolidated financial statements.

Future Changes in Accounting Standards – IFRS adoption effective 2011

On February 13, 2008, the Canadian Accounting Standards Board confirmed that publicly accountable profit-oriented enterprises will be required to use International Financial Reporting Standards (“IFRS”) as issued by the International Accounting Standards Board (IASB) in interim and annual financial statements for fiscal years beginning on or after January 1, 2011. Over the next two years, Canadian GAAP will be modified to converge with International Financial Reporting Standards (“IFRS”). The initial year of reporting under IFRS will be December 31, 2011, with full comparatives.

The Corporation has commenced the process of assessing the impact of conversion to IFRS on the Group’s financial statements and internal and external financial reporting processes, as well as considering possible changes to information systems, staff training requirements, potential impacts on borrowing covenants, the terms of its corporate governance agreements with controlled and significantly influenced entities, and stock-based compensation and bonus arrangements.

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The IFRS assessment process is being lead by the Corporation's Financial Reporting manager, with oversight from the Chief Financial Officer and Audit Committee. Preliminary analysis of the impact of transitioning to IFRS has identified the following areas of significance:

- **Accounting for oil and gas exploration and development costs and property, plant and equipment** ('oil and gas assets') – transition from full-cost accounting. Accounting for these assets under IFRS will require a lower level of asset grouping for depletion/depreciation and impairment testing purposes. Assets will need to be divided into 'exploration and evaluation' and 'development/production' pools, ('cash generating units') and tested for impairment at the January 1, 2010 (the opening balance sheet for the first comparative reporting year under IFRS). Cash generating units are defined as the lowest asset grouping able to generate independent cash inflows, for example a group of wells in the same geographical area sharing common infrastructure and the same marketing function.

Ongoing impairment testing of development/production assets is required only when there is an impairment indicator. Impairment testing requires an estimate of recoverable amount, which is defined as the greater of 'value in use' and 'fair value less costs to sell'. Value in use will be based on a discounted cashflow assessment based on proved and probable reserves, and cannot include revenues and costs associated with future development.

Depreciation of development/production asset pools can be done utilizing proved and probable reserves – an accounting policy choice is available.

The Corporation will not be in a position to quantify the impact of re-stating oil and gas assets under IFRS until after January 1, 2010. The impact may be material.

- **Business Combinations** – revised CICA Handbook sections 1582 Business Combinations, 1601 Consolidated Financial Statements, and 1602 Non-controlling Interests have been issued and are effective January 1, 2011. Significant changes include:
 - Section 1582 - expensing of transaction costs, recognition of contingencies, up-front recognition of contingent consideration, and recognition of any non-controlling interest at fair value.
 - Section 1601/1602 – changes in parent's interest post-control are accounted for as equity transactions rather than against property, plant and equipment.

Future changes in IFRS are expected to be issued by the IASB in 2010 and 2011 which may impact on the Group. Until these standards are issued, and their application date to Canadian reporting issuers is established, the impact of these changes on the Group cannot be determined.

3. ACQUISITIONS AND INVESTMENTS IN SIGNIFICANTLY INFLUENCED ENTITIES

(a) Serrano

Effective August 20, 2008, pursuant to the executed term sheet with Serrano dated February 1, 2008 the Corporation completed the acquisition of 50.01% share ownership of Serrano. Serrano is a heavy oil producer and explorer operating in Alberta and Saskatchewan. The acquisition was effected through a series of arm's length transactions described as follows, for total consideration of \$29 million:

- (i) the Corporation sold the Freemont heavy oil property to Serrano, with an effective date of June 1, 2007, in exchange for 7.0 million shares of Serrano. The fair value of the Freemont property at August 20, 2008 was determined by an independent evaluator to be \$10,280,000. Under the terms of the sale, a purchase price adjustment of \$2,549,240 was paid to Serrano by the Corporation which comprised revenue and expenses associated with the Freemont property from the effective date of sale of June 1, 2007 to closing on August 20, 2008;
- (ii) the Corporation subscribed for 2.0 million shares of Serrano at a price of \$5.00 per share;
- (iii) in return for a further 2.0 million shares of Serrano, the Corporation agreed to farm-in on up to \$5.0 million of qualifying Canadian exploration expenses on certain Serrano properties and also provide Serrano with a right to purchase the working interest of the Corporation in such properties for \$1 on or before September 30, 2013. Serrano exercised this option subsequent to year-end - refer to Note 17 for details.

The transaction has been accounted for using the purchase method with the Corporation as the acquirer, and the results of Serrano's operations have been included in the consolidated financial statements since August 20, 2008. The Corporation is considered to control Serrano due primarily to the terms of the Corporate Governance Agreement (CGA) signed between the two parties concurrent with the purchase. Under the CGA, the Corporation holds the deciding vote on matters put to Serrano's board of directors. The Corporation's acquisition of just over 50% of the voting shares was not the primary factor in determining whether or not control was acquired.

The allocation of the purchase price based on management's best estimates of fair values is as follows. Note that the original allocation was adjusted at year end for a revised future income tax liability (up \$4.1 million) and asset retirement obligation (down \$0.2 million) resulting in an increased allocation to property and equipment (up \$1.9m) and goodwill (up \$1.6 million) and a decrease in the non-controlling interest (down \$0.3 million).

Net assets acquired	
Working capital	\$ (4,982,964)
Property and equipment	57,631,721
Asset retirement obligations	(2,815,795)
Future income tax liability	(5,933,736)
Goodwill	7,818,937
Non-controlling interest	(22,683,777)
	\$ 29,034,386

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Consideration	
Cash paid for Serrano common shares	\$ 10,000,000
Agreed farm-in expenditure value	5,000,000
Freemont property value	10,280,000
Interim purchase price adjustments	2,549,240
Transaction costs	1,205,146
	\$ 29,034,386

None of the goodwill is deductible for tax purposes.

From the date of acquisition to the end of the year, Serrano contributed an after-tax loss of \$6,320,457 to the Group's results.

Dilution of interest in Serrano – November 2008

In November 2008, Serrano issued 1.4 million common shares on a flow-through basis for gross proceeds of \$7.0 million. This transaction reduced the Corporation's interest in Serrano to 47.0%, however did not result in a loss of control. In accordance with full-cost accounting under Canadian GAAP, the \$1.78 million difference between the cash assets entering the Group (\$7.0 million) and the increase in value of the non-controlling interest (\$4.9 million), net of minor goodwill and PP&E adjustments (\$0.3 million) has been recorded as a reduction in the cost of PP&E.

Increase in interest in Serrano – subsequent to year end

In January 2009, the Corporation's interest in Serrano was increased to 56.8% following the finalization of an agreement between Serrano and one of its other shareholders. Under the agreement, Serrano cancelled 4 million shares held by the shareholder in return for a transfer of a part of a working interest in an oil sands project and a \$6.3 million future expenditure commitment (refer Note 20).

(b) Marble Point

Pursuant to the non-binding letter of intent as amended and executed April 16, 2008 with Marble Point Energy Limited, the Corporation completed the acquisition of 56.51% of Marble Point on September 19, 2008. Marble Point is an oil and natural gas producer and explorer with operations in Alberta, Saskatchewan and North-Eastern British Columbia.

The acquisition was effected through a series of arm's length transactions:

- (i) The Corporation subscribed for 90 million common shares of Marble Point at a price of \$0.65 per share for a total subscription amount of \$58.5 million. Including transaction fees the total purchase price was \$64.9 million. Payment for the common shares was by way of assignment of promissory notes to the Corporation by Marble Point (described in (ii) below) of \$49.5 million and cash consideration of \$9.0 million.

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- (ii) Prior to the subscription described in (i) above, Marble Point conducted a private placement of preferred shares at a price of \$0.65 per share for gross proceeds of \$49.5 million. Each preferred share was then redeemed by Marble Point via the issuance of a promissory note to each subscriber. The notes were assigned to the Corporation as part of the acquisition transaction.
- (iii) The Corporation issued 329.6 million subscription receipts at an agreed price of \$0.15 per receipt (total value \$49.5 million) to promissory note holders as settlement of the notes assigned to the Corporation in (ii) above. Each subscription receipt entitled the holder to receive one unit, which was comprised of one Canadian Phoenix common share and one Canadian Phoenix common share purchase warrant with an exercise price of \$0.20 and an expiry date of September 19, 2010. If the closing price of the Corporation's shares on the TSXV is at least \$0.30 for a minimum of at least 30 trading days, the Corporation may reduce the exercise period to that date which is 30 days following the date on which the holders of the warrants receive written notice of the shortened exercise period.

The investment in Marble Point is being accounted for on an equity basis and not on a consolidated basis as the Corporation is considered to have significant influence, but not control over Marble Point. Specifically, the Corporate Governance Agreement executed mutually by the Corporation and Marble Point does not transfer ongoing control of Marble Point to the Corporation despite it holding greater than a 50% voting interest. The determination of control was made in accordance with Canadian GAAP.

The equity investment cost of \$64.9 million includes goodwill of approximately \$1.1 million. The fair value of 56.51% of the net assets of Marble Point at the date of acquisition was approximately \$63.8 million, and the \$1.1 million excess paid reflects goodwill associated with the transaction.

The following table summarizes Marble Point's financial results between the acquisition date of September 19, 2008 and December 31, 2008, and reconciles the Corporation's equity share of that result.

Revenue	\$
Oil and gas	7,737,037
Royalties	(1,422,419)
	6,314,618
Expenses	
Operating costs	2,976,120
Depletion, depreciation and accretion	3,615,610
General and administrative	1,575,796
Stock-based compensation	1,166,738
Interest accretion- financing costs	94,819
Interest expense	560,567
Other – legal	660,633
	10,650,283
Net loss before taxes	(4,335,665)
Tax recovery on loss	-
Net loss after taxes	(4,335,665)
Proportional share of loss at 56.51%	(2,450,133)

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Consolidation adjustment – increased depreciation/depletion	(1,250,854)
Consolidation adjustment – deferred tax recovery on depletion	889,390
Total loss – Marble Point investment	(2,811,597)

At December 31, 2008, Marble Point had net assets of \$67.8 million (including PP&E of \$113 million) and a working capital deficit of \$41 million. Refer to Note 7 for details of the write-down in the Corporation's equity investment in Marble Point at December 31, 2008.

Financing transactions concurrent with the share purchase

In April 2008, concurrent with the negotiation of the share purchase agreements, Marble Point assigned the Corporation with a \$35 million debt obligation due to a third party lender. The Corporation loaned Marble Point an additional \$6.5 million and took back a \$41.5 million receivable. In October 2008 Marble Point repaid the \$41.5 million to the Corporation, which in turn extinguished the \$35 million debt obligation due to the third party lender. Fees associated with the \$35 million borrowing were paid by the Corporation via the issuance of 27.5 million shares, at a value of \$4 million (refer to Note 11). Fees were included in the amortized cost of the debt, and charged to income under the effective interest method. All unamortised fees were expensed at the date of extinguishment of the debt (October 2008). Interest on the facility during its term was shared equally between the Corporation and Marble Point.

(c) Purchase of oil and natural gas assets from Blue Parrot Energy Inc. (“Blue Parrot”)

On September 30, 2008, pursuant to the asset acquisition agreement with Blue Parrot, the Corporation purchased certain oil and natural gas assets in Alberta for a price of \$6.4 million. Consideration consisted of the issuance of 95 million units in the Corporation, consisting of one share and one-half of a purchase warrant entitling the holder to purchase one common share at an exercise price of \$0.20 per share, expiring September 30, 2010. The shares were valued at \$0.06 per share (total \$5.7 million), being the Corporation's average traded market price over several days before and after September 30, 2008. The warrants were valued at \$0.5 million using the Black Scholes pricing model – refer to Note 15(d).

If the closing price of the Corporation's shares on the TSXV is at least \$0.30 for a minimum of at least 30 trading days, the Corporation may reduce the exercise period to that date which is 30 days following the date on which the holders of the warrants receive written notice of the shortened exercise period.

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The acquisition of the assets from Blue Parrot was arm's length and has been accounted for based on the fair value of consideration provided as follows:

95,000,000 common shares	\$5,700,000
47,500,000 warrants	524,510
Cash transaction costs	158,526
Total purchase price	\$6,383,036
Allocation:	
Property and equipment	\$6,734,811
Asset retirement obligation	(351,775)
Net assets acquired	\$6,383,036

4. RESTRICTED CASH/CASH HELD IN TRUST

Total restricted cash at December 31, 2008 was \$2m. As part of the Marble Point transaction, the Corporation agreed to indemnify subscribers from possible withholding taxes payable on their preferred share dispositions. The Corporation thereby deposited into trust \$1.75 million. Certificates of Compliance were received from the Canada Revenue Agency, a condition of the trust agreement, evidencing withholding taxes were not applicable to the dispositions. Thereafter, the full balance of this cash held in trust with interest was released back to the Corporation in March 2009.

The remaining amount of restricted cash relates to amounts held on deposit to meet the future abandonment costs of certain oil and gas properties.

Cash held in trust as at December 31, 2007 related to December 2007 issuance of 102.2 million flow-through common shares for total proceeds of \$12.8 million and the issuance of 40 million warrant units for total proceeds of \$5.0 million. Due to the late closing of the transactions, the funds were held in trust by the Corporation's legal counsel until the first banking day in January 2008.

5. ACCOUNTS RECEIVABLE

Accounts receivable is net of a \$300,000 impairment allowance (2007: \$nil) which has been included within General and Administrative costs in the statement of operations.

In the prior year, the Corporation had advanced Serrano \$0.9 million as a contribution against the cumulative net operating revenue from the Freemont property (which had an effective date of sale of June 1, 2007 – refer Note 3). Upon closing in August 2008, the \$0.9 million was included as part of the \$2.6 million purchase price adjustment referred to in Note 3.

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6. PROPERTY, PLANT AND EQUIPMENT

a) Movement Schedule

	December 31, 2008			December 31, 2007		
	Cost	Accumulated depletion/depreciation	Net Book Value	Cost	Accumulated depletion/depreciation	Net Book Value
Petroleum and Natural Gas properties and equipment	119,532,639	36,640,574	82,892,064	37,811,903	5,334,553	32,477,350
Vehicles	-	-	-	25,000	14,587	10,413
Office Furniture/equipment/ leasehold improvements	477,470	207,802	269,668	281,337	125,627	155,710
Total PP&E	120,010,109	36,848,376	83,161,732	38,118,240	5,474,767	32,643,473

The impact of the Serrano and Blue Parrot acquisitions added approximately \$47 million and \$6.7 million respectively to consolidated PP&E. Other PP&E additions for the year related mainly to exploration and development projects in the Samson, Parkland, Pembina, and Sawdy areas of Alberta, the Klua area of north-eastern British Columbia, the Lloydminster area of Saskatchewan, and on the Blackrod oil sands project in north-eastern Alberta.

The Serrano transaction resulted in the disposition of the Fremont property in the Corporation's books, and the acquisition in Serrano's books for the same value (\$10.3 million), yielding no net change in respect of that asset. In accordance with Canadian GAAP, the \$10.3 million fair value of the property was removed from the Corporation's PP&E cost pool and no gain or loss was recorded as the disposition did not result in a change of greater than 20% in the Corporation's depletion rate. There were no other significant asset dispositions during the year.

Depletion and depreciation expense for the year was \$7.8 million. The depletion calculation was done on a consolidated basis, including the Corporation's 56.5% interest in Marble Point's PP&E and proved reserves. As a result, an additional \$1.25 million of depletion was recorded in the Marble Point equity investment account (refer Note 3b). The depletion calculation excluded unproven properties and major development projects of \$16.6 million (December 31, 2007 - \$7.2 million), including a proportionate \$12.3 million related to Marble Point. Future development costs of proved undeveloped reserves of \$10.2 million (Marble Point \$8 million) were included in the calculation (December 31, 2007 - \$nil). The Corporation has not capitalized any general and administrative expenses for the years ended December 31, 2008 or 2007.

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b) Impairment Assessment – Ceiling Test

PP&E impairment assessments utilized estimates of reserves data effective December 31, 2008, future operating and capital expenditure based on historical data and management's forecasts, and future price estimates from the independent reserves evaluator adjusted for heat content and basis differential.

Price Estimates Used for the Ceiling Test

	Exchange Rate (US\$/Cdn\$)	Nymex (\$U.S./Mcf)	AECO (\$Cdn/Mcf)	Edmonton Light (\$Cdn/Bbl)	Hardisty Heavy (\$Cdn/Bbl)
2009	0.825	7.00	7.58	68.61	43.10
2010	0.850	7.50	7.94	78.94	49.76
2011	0.875	8.00	8.34	83.54	54.35
2012	0.925	8.75	8.70	90.92	59.23
2013	0.950	9.20	8.95	95.91	62.54
>2013	0.950	2%	2%	2%	2%

The ceiling test was conducted on a consolidated basis in accordance with Canadian GAAP, whereby the PP&E of the Corporation plus the Corporation's interest in Serrano (47%) and Marble Point (56.5%)'s PP&E and was tested for impairment based on future cashflows accruing to the Corporation.

Total undiscounted cashflows based on proved reserves of \$122.4 million were less than the Group's carrying value of PP&E with proved reserves of \$158.0 million. This required a fair value assessment using discounted cashflows associated with proved and probable reserves. Future cashflows discounted at a rate of 5% were \$139.4 million, resulting in an impairment charge of \$18.6 million to the Group's PP&E.

The impairment charge is shown in the income statement as a separate line item due to its significance. No future income tax benefit was recognized as the benefit is not considered more likely than not of being realized.

The key factor driving the impairment charge was the reclassification of reserves at the Corporation's Sarcee properties from probable to contingent. Further evaluation of the Sarcee project is not planned at this time.

7. EQUITY INVESTMENT - NET LOSS AND IMPAIRMENT

As detailed in Note 3, the Corporation's investment in Marble Point contributed a loss of \$2.8 million from the September 19, 2008 date of purchase to December 31, 2008. At December 31, 2008, Marble Point had net assets of \$67.8 million (including PP&E of \$113 million) and a working capital deficit of \$41 million.

The significant drop in oil and natural gas prices subsequent to the investment in Marble Point, combined with the decline in Marble Point's net asset carrying value at year end, were indicators of impairment in the Corporation's investment, and therefore an impairment assessment was performed.

The fair value of the investment in Marble Point was assessed using Marble Point's proved and probable reserves, pricing assumptions and future costs as per the independent reserve evaluations from December 31, 2008 and a discount rate of 10%. The fair value was determined to be \$43.1 million and as such a write-down of \$19 million was recorded. The write-down includes \$1.1 million of goodwill implicit in the initial investment (refer Note 3). No tax benefit was recognized from the investment write-down.

8. GOODWILL AND IMPAIRMENT

Goodwill of \$7.8 million was recorded as part of the acquisition of Serrano, adjusted down to \$7.6 million as a result of the dilution of the Corporation's interest described in Note 3(a). The Corporation reassessed the fair value of goodwill in Serrano at year end, and based on that assessment the fair value was considered to be nil and a write-down of \$7.6 million was charged to income.

9. ACCOUNTS PAYABLE

Included in accounts payable at December 31, 2008 is an accrual of \$1.1 million for a legal settlement which was concluded subsequent to year end – refer Note 20 for additional detail.

10. ASSET RETIREMENT OBLIGATION

Asset retirement obligations were estimated by management based on the Group's working interest in its wells, estimated costs to remediate, reclaim and abandon the wells and estimated timing of the costs to be incurred in future periods. The net present value of the Group's estimated asset retirement obligation was \$4.5 million at December 31, 2008 (December 31, 2007 - \$0.6 million). These costs are expected to be incurred over the next 2 to 34 years. A credit-adjusted risk-free rate of 7.5% was used to calculate the net present value of the Group's asset retirement obligation.

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The following table provides a reconciliation of the carrying amount of the obligation associated with the retirement of oil and gas properties:

	Dec 31 2008	Dec 31 2007
Asset retirement obligation, beginning of year	\$565,906	\$ 556,300
Liabilities acquired/(disposed of) during the year	3,037,795	(74,922)
Liabilities incurred during the year	627,442	-
Adjustments to estimates	135,029	35,597
Accretion expense	185,497	48,931
Asset retirement obligation, end of year	\$4,551,669	\$ 565,906

11. OPERATING LOAN

Canadian Phoenix had a revolving line of credit with an arm's length lender which was suspended in April 2008 and \$nil was drawn at December 31, 2008. Prior to suspension, the facility bore an interest at the lender's prime rate plus 1 percent and was secured with a general security agreement over the property and assets of the Corporation. During the year ended December 31, 2008, the Corporation incurred \$7,234 of interest on this facility.

Marble Point facility

As described in Note 3, pursuant to the terms of the acquisition of Marble Point, Marble Point assigned a \$35 million credit facility due to an arm's length lender to the Corporation. The facility was entered into on April 30, 2008, bore interest at a rate of 12 percent per annum payable monthly, and was due March 31, 2009. In October 2008, the Corporation repaid the entire \$35 million balance outstanding under the credit facility.

From April 30, 2008 to October 2008, Marble Point and the Corporation each paid 50 percent of the interest costs. For the year ended December 31, 2008, the Corporation paid \$1.1 million of interest in cash and incurred \$4 million of fees related to the establishment of the loan, which were paid via common share issuances (refer Note 15(v)). A further \$1m (\$0.5m cash, \$0.5m shares) was paid to extend the loan until the closing of the Marble Point transaction - refer to Note 15(viii).

12. DEBENTURE FINANCING

During 2007, the Corporation issued 11.1 million debenture units for gross proceeds of \$11.1 million. Net of transaction and related fees proceeds were \$9.4 million. Each unit consisted of 1 debenture unit and 4 detachable warrants exercisable at \$0.125 per common share expiring in April and June 2009. Each debenture unit entitled the holder to convert 1 unit into 12 common shares of the corporation. As part of the transaction, broker warrants were issued at a rate of 10 percent of total shares issuable on conversion of the debentures into common shares of the Corporation.

In accordance with Canadian GAAP, the initial accounting for the debenture issuance resulted in an allocation (net of transaction costs) of \$0.7 million to the warrants, \$3.2 million to the conversion rights, and the remaining \$5.9 million to debt. The debt component was accreted thereafter at the effective interest rate to the amount owing at maturity and charged as interest expense.

On March 5, 2008, the debenture holders approved the transaction involving Serrano Energy Ltd. (described in Note 3) which constituted a Business Combination Transaction as defined in the trust indenture thereby obliging the conversion of each \$1.00 invested in the debenture into 12 common shares of the Corporation. On conversion, the debt component of the debentures was transferred to share capital. As a result 12.1 million warrants were issued with an exercise price of \$0.0833 per share. The warrants expired on April 11, 2009 without being exercised. Total interest expense incurred in 2008 on the debentures prior to conversion was \$1.58 million.

The following table summarizes the initial accounting for the debenture issue, the accounting for the conversion, and the relevant balances at December 31, 2008 and 2007.

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Debentures

	<u>Equity Component</u>		Debt Component
	Warrants	Conversion Rights	
Opening value, April 11, 2007	755,933	3,628,613	6,728,690
Less: Cash placement costs	(51,251)	(246,016)	(456,909)
Less: Broker warrants issuable	(37,974)	(182,284)	(338,545)
Adjusted opening carrying value, April 11, 2007	666,708	3,200,313	5,933,236
April 11 to December 31, 2007 interest accretion			3,085,917
Carrying value, December 31, 2007	666,708	3,200,313	9,019,153
Interest accretion prior to conversion - 2008			1,575,284
Debt component reclassified to share capital on conversion (April/May 2008)		10,594,437	(10,594,437)
Carrying value in equity, December 31, 2008 (refer to Note 15)	666,708	13,794,750	-

A future income tax liability was not required to be recorded under Canadian GAAP for the initial temporary difference on the debt component of the debenture issue.

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13. FUTURE INCOME TAX

Effective tax rate

Income tax expense (recovery) in the income statement is different from the amount computed by applying the combined statutory Canadian federal and provincial tax rates to the pre-tax loss for the year, reconciled as follows:

	2008	2007
Statutory combined federal and provincial income tax rates	30%	33.47%
Expected income tax recovery on pre-tax loss	\$20,374,261	\$ 2,864,312
Add (deduct) the income tax effect of:		
Impairment of goodwill	(2,276,254)	-
Valuation allowance	(14,555,410)	-
Debenture interest accretion	(464,709)	-
Stock-based compensation	(860,868)	(153,850)
Rate adjustments and other	4,242,956	15,509
Non-deductible expenses/other	(8,356)	(10,213)
Future/current income taxes recovery	\$ 6,451,620	\$ 2,715,758

Detail of future income tax liability

Future income taxes are the tax-effected difference between the accounting carrying values and tax bases of assets, liabilities and equity, and effectively represents the difference between when amounts are recognized for accounting purposes and when they are assessable or deductible for tax purposes. The net total represents a future tax benefit or future tax liability.

The components of the net future income tax liability as at December 31 are as follows:

	2008	2007
Tax rate applied	26%	26%
Future income tax assets:		
Asset retirement obligation	\$1,143,162	\$ 137,880
Share issue costs	1,077,344	374,958
Property, plant and equipment	3,053,826	-
Legal Accrual	286,000	-
Equity investment	6,539,695	-
Non-capital losses carried forward	5,204,622	2,415,315
	17,304,649	2,928,153
Valuation allowance	(14,555,410)	-
Future income tax liabilities:		
Property, plant and equipment	(7,577,181)	(4,875,239)
Net future tax liability	\$4,827,942	\$ 1,947,086

Separate future tax assets and liabilities have been recorded for PP&E, as the balances relate to separate legal entities. A valuation allowance of \$14.6 million has been recognized in the Corporation, reducing the otherwise overall future income tax asset position in the Corporation to \$nil.

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The valuation allowance will only be reversed, and a future income tax asset recognized, once management of the Corporation determines that taxable income is more likely than not to occur. Future tax benefits from deductible temporary differences and tax losses have been recognized to the extent of and on the same basis as the future tax liability stemming from the recovery of the PP&E assets.

The movement in the net future tax liability for the year includes several items that did not impact on the income statement, for example an increase in the future tax liability associated with flow-through share issuances (future tax liability recorded in equity), and the future tax liability recorded in Serrano in relation to the Freemont acquisition (recorded as an increase to PP&E). Hence, the movement in the net future tax liability does not correspond directly to the future tax recovery in the income statement.

The measurement of the Group's income tax liability and tax asset pools requires interpretation of complex laws and regulations. All tax filings and compliance with tax regulations are subject to audit and reassessment, potentially several years after the initial filing. Accordingly, actual income tax assets and liabilities may differ from the amounts initially estimated.

Recognized non-capital losses

As at December 31, 2008, the Group had approximately \$19.7 million (Corporation \$13.2 million, Serrano \$6.5 million) (2007: \$9.3 million) of non-capital losses available for deduction against future taxable income, as indicated below:

Year of Expiry	Total
2009	409,508
2010	826,785
2011	1,141,791
2012	1,266,700
2026	174,000
2027	5,100,221
2028	10,797,000
Total	19,716,005

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Flow-through Share Issuances

Under the terms of a flow-through share issue in November 2008, the Group is required to incur \$7.0 million of qualifying expenditure by December 31, 2009. As at December 31, 2008 \$1.3 million had been spent. As the tax deduction related to this expenditure had not been renounced to subscribers by year end, a future tax liability was not recorded in relation to this expenditure at December 31, 2008.

Under the terms of a flow-through share issue in December 2007, the Corporation was obligated to incur Canadian Exploration Expenditures in the amount of \$12.8 million prior to December 31, 2008. The full amount of \$12.8 million was renounced to the subscribers at December 31, 2007. As at December 31, 2008, the Corporation considers it has fulfilled all expenditure obligations related to this issue. As the issue of these shares results in the effective 'pass through' of the tax deduction related to the qualifying exploration expenditure from the Corporation to the underlying investors, a future income tax liability is created upon issuing the shares. This future income tax liability is recognized as a reduction in equity in accordance with Canadian accounting standards, effectively presenting the after tax proceeds of the flow-through equity raised.

Included in interest expense for the year is \$0.5 million of Part XII.6 tax due to Canada Revenue Agency in relation to flow-through expenditure incurred in 2008 subsequent to January 31, 2008. This tax levy was paid in full by the Corporation in March 2009.

14. NON CONTROLLING INTEREST ("NCI")

The following details the non-controlling interest balance in Serrano from the acquisition date to December 31, 2008:

	Dec 31, 2008
Non-controlling interest as at acquisition – (Note 3a)	\$ 22,683,777
NCI share of Serrano post-acquisition loss	(3,347,831)
Increase in non-controlling interest in relation to issued and outstanding options and warrants	2,559,180
Decrease in NCI – share issue costs in subsidiary	(52,163)
Increase in non-controlling interest in relation to shares issued by Serrano - November 2008	4,934,220
Balance, end of year	\$ 26,777,183

The non-controlling interest shown at the date of acquisition reflects the Corporation's proportionate holding of Serrano's net asset carrying value. The movement in the non-controlling interest reflects its share of Serrano's net loss since acquisition, with a further adjustment representing the movement in Serrano's option and warrant reserves (due to issuances or vesting) subsequent to acquisition.

Refer to Note 3 for a description of the accounting for the November 2008 dilution of the Corporation's interest in Serrano following the issuance of common shares by Serrano to outside interests, which increased the NCI by \$4.9 million.

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The following is a summary of Serrano's share capital:

The Corporation's holdings, December 31, 2008	11,050,000	47.0%
Non-controlling interest, December 31, 2008	12,444,733	53.0%
Balance - December 31, 2008	23,494,733	100%

The following is a summary of Serrano's options:

	Outstanding	Weighted Average	
		Remaining term	Exercise \$
At acquisition	783,249	3.1	\$ 0.50
Issued	1,307,445	4.7	\$ 2.41
Balance - December 31, 2008	2,090,694	3.7	\$ 1.97

Total stock-based compensation recorded in relation to options subsequent to acquisition was \$2.6 million, which has been recorded in the consolidated income statement, with a credit to the NCI.

The following is a summary of Serrano's warrants:

	Outstanding	Weighted Average	
		Remaining term	Exercise \$
At acquisition	850,000	3.6	\$ 3.60
Expired	(350,000)	—	—
Balance - December 31, 2008	500,000	3.6	\$ 3.60

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15. SHAREHOLDERS' EQUITY

a) Authorized

Unlimited number of common voting shares of no par value
Unlimited number of preferred shares of no par value

b) Issued and outstanding

	# Shares	\$ Value
Balance – December 31, 2006	55,305,432	21,892,645
Shares issued for debt settlement	1,500,000	189,475
Value of equity component – debenture conversion rights April 14, 14/2007- June 14/2007	—	3,200,313
Flow-through common shares issued (xiii)	102,200,000	12,775,000
Common share units issued in private placement (xiv)	40,000,000	3,779,779
Share issue costs (2007 Flow Through – net of tax)	—	(261,952)
Tax effect flow through renoucement (2006)	—	(1,079,130)
Balance – December 31, 2007	199,005,432	40,496,130
Tax effect flow through renoucement (2007)	—	(3,321,500)
Common shares issued on severance settlement (i)	3,500,000	260,000
Common shares issued in private placement (ii)	222,617,800	9,116,409
Common shares issued on exercise of warrants	124,000	21,700
Common shares issued on debenture conversion (iii)	91,317,408	7,714,492
Common shares issued on debenture conversion (iv)	41,989,680	2,879,945
Common shares issued to arm's length lender (v)	27,547,220	3,988,489
Common shares issued to Global Resource Investments (vi)	4,316,070	404,068
Common shares issued to Global Resource Investments (vii)	18,131,666	2,245,532
Common shares issued to arm's length lender (viii)	10,000,000	500,000
Common shares issued in private placement (ix)	82,011,167	7,677,819
Common shares issued on completion of Marble Point transaction (x)	329,666,661	40,827,829
Common shares issued- Blue Parrot asset purchase (xi)	95,000,000	5,700,000
Common shares issued – Marble Point transaction costs (xii)	6,666,667	466,667
Balance- December 31, 2008	1,131,893,771	118,977,580

- (i) On March 14, 2008, the Corporation settled a dispute with a former executive of the Corporation and issued 1,000,000 common shares as part of the settlement. In November 2008, a further 2,500,000 shares were issued to two former employees under a severance settlement.
- (ii) On March 17, 2008, the Corporation issued 202,398,000 units at a price of \$0.125 per unit for gross proceeds of \$25.3 million. Each unit consisted of one common share and one common share purchase warrant. Each warrant entitles the holder to purchase one common share during the period expiring on March 17, 2010 at an exercise price of \$0.15 per share. Total finder's fees in connection with the private placement amounted to an additional 20,219,800 units for a total of 222,617,800 units. Each finder's unit also had one attaching warrant with an exercise price of \$0.15 expiring

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March 17, 2010, for a total of 20,219,800 warrants. The value attributed to warrants was \$16,183,286 with the remainder being attributed to common shares at \$9,116,409.

- (iii) During the three months ended March 31, 2008, the Corporation issued 91,317,408 common shares in conversion of 8,236,784 of secured convertible debentures. The conversion resulted in a transfer of \$7,714,492 from long term debt to share capital (average value of \$0.084 per share).
- (iv) During the three months ended June 30, 2008, the Corporation issued 41,989,680 common shares in conversion of 2,872,140 of secured convertible debentures. The conversion resulted in a transfer of \$2,879,945 from long term debt to share capital (average value of \$0.068 per share).
- (v) On April 15, 2008, Marble Point as borrower, and Canadian Phoenix as guarantor, entered into a secured credit facility with an arm's length lender. Marble Point borrowed an initial amount of \$7.25 million from the lender to fund the payment of the deposits and fees for the purchase of oil and gas assets. Canadian Phoenix issued 4,381,753 common shares on April 15 to the lender in partial consideration of the initial advance under the facility. A further 23,165,467 common shares were issued to the lender on April 30, 2008 when the full amount of \$42 million was advanced to Marble Point under the Facility.
- (vi) On August 11, 2008, Global Resource Investments Ltd., ("Global") a party at arm's length to Marble Point and Canadian Phoenix, acted as finder in connection with a portion of the placement of the 82,011,167 subscription receipts which was completed on September 19, 2008 (refer to (ix) below). Global was paid a fee equal to 5.5% of the gross proceeds of a portion of the subscription receipt financing, payable with the issuance of 4,316,070 Canadian Phoenix units at a price of \$0.15 per unit. At the date of issue the fair value was \$647,412. Each unit consisted of one common share and one common share purchase warrant. Each warrant entitles the holder to purchase one common share during the period expiring on September 19, 2010 upon payment of the exercise price of \$0.20 per common share. However, in the event that the closing price of Canadian Phoenix shares on the TSX Venture Exchange is at least \$0.30 for a minimum of at least 30 trading days, Canadian Phoenix may reduce the exercise period to that date which is 30 days following the date on which the Warrant holder receives written notice of the shortened exercise period ("Warrant Terms"). The value attributed to warrants was \$243,344 with the remainder being attributed to common shares at \$404,068.
- (vii) Global also acted as finder on behalf of Marble Point in connection with Marble Point's private placement of preferred shares. In consideration of its services as finder, Global was paid a fee equal to 5.5% of the gross proceeds of such financing. Marble Point issued promissory notes in the total amount of \$2,719,750 to Global in payment of such finders fees. Marble Point assigned the notes to Canadian Phoenix, who subsequently issued 18,131,666 units to Global in satisfaction of the indebtedness under the notes. Each unit consisted of one common share and one common share purchase warrant. Each warrant carries the same terms as the previously defined Warrant Terms in note (vi) above. The value attributed to warrants was \$474,218 with the remainder being attributed to common shares at \$2,245,532.
- (viii) Canadian Phoenix issued 10,000,000 common shares at a price of \$0.05 per common share to an arm's length lender in connection with fees payable for extensions granted by the lender in order to close the transaction between Canadian Phoenix and Marble Point.
- (ix) On September 19, 2008, a non-brokered private placement of 82,011,167 units was completed at a price of \$0.15 per share for gross proceeds of \$12,301,675. Each unit consisted of one common share of Canadian Phoenix and one common share purchase warrant. Each warrant carries the same terms as the previously defined Warrant Terms in note (vi) above. The value attributed to warrants was \$4,623,856 with the remainder being attributed to common shares at \$7,677,819. An officer of the Corporation participated in the private placement for 1,666,667 units.
- (x) On September 19, 2008, concurrent with the completion of the Marble Point Transaction, Canadian Phoenix issued 329,666,661 units at a price of \$0.15 per unit. Each unit was comprised of one common share and one common share purchase warrant. Each warrant carries the same terms as the previously defined Warrant Terms in note (vi) above. The value attributed to warrants was \$8,622,170 with the remainder being attributed to common shares at \$40,827,829.

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- (xi) On September 30, 2008, Canadian Phoenix issued 95 million units as consideration for certain oil and natural gas properties from Blue Parrot. Each unit consisted of one common share of Canadian Phoenix and one-half common share purchase warrant. Each whole warrant carries the same terms as the previously defined Warrant Terms in note (vi) above. The shares were valued at the market price at closing of the transaction of \$0.06.
- (xii) Shares were issued at \$0.07 per share in October 2008 to a consultant for services related to the Marble Point transaction.

Prior year

- (xiii) On December 28, 2007, 102,200,000 flow-through common shares were issued at a price of \$0.125 per share for total proceeds of \$12,775,001, before fees and expenses. The terms of this issue require the Corporation to renounce to subscribers Canadian Exploration Expenditures in the amount of \$12,775,000 to be incurred before December 31, 2008.
- (xiv) On December 28, 2007, 40,000,000 units of the Corporation were issued at a price of \$0.125 per unit for total proceeds of \$5,000,000. Each unit consists of one common share and one common share purchase warrant. Each warrant entitles the holder to purchase one common share during the period expiring on December 31, 2008 at an exercise price of \$0.20 per share.

(c) Stock Option Plan

On August 15, 2008, the Corporation changed its stock option plan whereby the aggregate number of shares that may be reserved for issuance under the plan shall not exceed 10% (previously 20%) of the issued and outstanding Canadian Phoenix shares. The number of options and the exercise price thereof is set by the Board of Directors at the time of grant, provided that the exercise price shall not be less than the market price of the common shares on the stock exchange on which such shares are then traded. The options granted are exercisable over a period of 5 years with vesting conditions set by the Board of Directors at the time of grant. Vesting conditions normally include a minimum 18 month service period.

Below is a summary of the options issued under the Corporation's stock option plan as at December 31, 2008 and changes during the year ended December 31, 2008:

		2008
	# Shares	Weighted average exercise price (\$)
Outstanding – beginning of year	7,819,181	0.26
Granted during period	3,180,000	0.125
Expired during period	(155,834)	0.72
Forfeited during period	(4,657,347)	0.28
Outstanding - end of year	6,186,000	0.17

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On February 8, 2008, the Corporation granted certain officers and directors stock options to purchase 3.2 million common shares. All options have an exercise price of \$0.125, vest 25% immediately and 25% on each of the 6, 12 and 18 month anniversaries of the grant and expire on February 13, 2013.

The weighted-average fair value of the stock options granted in 2008 was \$0.108 per option, as determined at the date of grant using a Black-Scholes option pricing model with the following assumptions:

Volatility factor of expected market price	99.10%
Weighted average risk-free interest rate	4.01%
Weighted average expected life in years	5.0
Weighted average expected annual dividends per share	Nil

In July 2008, 4.7 million options were forfeited by personnel who ceased employment with the Corporation during the year. 1.4 million of the options had not vested at the time of forfeiture and therefore the stock-based compensation expense that had been recorded up to that point in time was reversed.

The following table summarizes information about stock options outstanding at December 31, 2008:

Exercise price	Outstanding Dec 31, 2008	Weighted average remaining contractual life in years	Weighted average exercise price	Number vested and exercisable	Weighted average exercise price – exercisable options
\$0.125 - \$0.68	3,006,000	3.1	\$0.210	2,404,500	\$0.210
\$0.125	3,180,000	4.1	\$0.125	2,385,000	\$0.125
	6,186,000	3.6	\$0.170	4,789,500	\$0.170

Compensation cost of \$0.3 million (2007: \$0.5 million) has been recognized by the Corporation in 2008 for stock options vesting in 2008. The charge to stock-based compensation expense results in a corresponding amount being credited to contributed surplus, as shown below.

Contributed Surplus		
	Year ended Dec 31, 2008	Year ended Dec. 31, 2007
Opening balance	\$2,161,086	\$1,701,419
Expiry of warrants	1,023,236	-
Stock Based Compensation	272,266	459,668
Closing balance	\$3,456,588	\$2,161,086

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d) Warrants

The following table is a summary of the Corporation's outstanding warrants as at December 31, 2008 and changes during the year ended December 31, 2008. Each warrant entitles the holder to purchase one common share in the Corporation at the relevant exercise price.

Date	Warrants	Weighted Average Exercise Price	Weighted Average Value per Warrant	Total \$ Value
Outstanding – start of year	97,134,236	\$ 0.154	\$0.025	2,445,731
Expired – reclass to c/surplus	(40,638,540)	\$ 0.195	(\$0.025)	(1,023,236)
Exercised	(124,000)	\$ 0.125	\$0.050	(6,200)
Issued:				
17-Mar-08 (Note 15b(ii))	222,617,800	\$ 0.150	\$0.073	16,183,286
11-Aug-08 (Note 15b (vi)(ix))	86,327,237	\$ 0.200	\$0.056	4,867,200
19-Sep-08 (Note 15b (x)(vii))	347,798,327	\$ 0.200	\$0.026	9,096,388
30-Sep-08 (Note 15b(xi))	47,500,000	\$ 0.200	\$0.011	524,510
Outstanding – end of year	760,615,060			32,087,679

The fair value of warrants granted during the year was estimated at the date of grant using a Black-Scholes option pricing model with the following assumptions:

Warrants issued	Issue date	Value	Volatility	Risk free rate	Life in years	Dividend /share
222,617,800	17-Mar-08	\$ 16,183,286	99.10%	4.00%	2	NIL
86,327,237	11-Aug-08	\$ 4,867,200	84.74%	4.00%	2	NIL
347,798,327	19-Sep-08	\$ 9,096,388	114.46%	4.00%	2	NIL
47,500,000	30-Sep-08	\$ 524,510	116.64%	4.00%	2	NIL

The following table is a summary of information about warrants outstanding at December 31, 2008:

Outstanding Dec 31, 2008	Weighted average remaining contractual life in years	Exercise price	Number exercisable
12,060,000	0.27	\$0.0833	12,060,000
44,311,696	0.27	\$0.125	44,311,696
222,617,800	1.21	\$0.15	222,617,800
481,625,564	1.63	\$0.20	481,625,564
760,615,060			760,615,060

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e) Per share amounts

For the year ended December 31, 2008 the weighted average number of shares outstanding was 665.6 million (2007 – 57.2 million), yielding a basic net loss per share of \$0.094. Diluted earnings per share assumes the exercise of options and warrants as if issued at the later of the date of grant or the beginning of the year. This calculation takes into account only the options and warrants that are considered in-the-money at December 31, 2008. Based on the share price at December 31, 2008, no options or warrants were considered to be dilutive and therefore the weighted average number of dilutive shares outstanding is the same as the weighted average number of shares outstanding.

16. COMMITMENTS & CONTINGENCIES

- a) Refer to Note 20 - Subsequent Events for discussion of a legal claim against the Corporation which was settled subsequent to year end.
- b) The Group has total capital expenditure commitments of \$8 million at December 31, 2008 including \$5.7 million of flow-through expenditure required by December 31, 2009.
- c) Claim statements totaling \$1.4 million have been filed against the Corporation's subsidiary by vendors looking to protect their interests. Serrano has filed a statement of defense with respect to certain of these claims. Serrano has also been served with approximately \$4.1 million of builders' liens on certain of its properties, which resulted in the suspension of the Group's credit facility as discussed in Note 18.
- d) Future minimum lease payments relating to operating leases for office space are as follows:

<u>Year</u>	<u>Payments</u>
2009	\$284,656
2010	\$115,936
2011	\$47,556
2012	\$47,556
2013	\$19,815

17. RELATED PARTY TRANSACTIONS

In 2008 the Corporation paid consulting fees to certain directors, in addition to directors' fees. D. Barry Lee was remunerated for \$106,750 and Robert Chenery was remunerated for \$65,000 related to general business and consulting services rendered during the year. The services are in the normal course of business and have been measured at the exchange amount which is also considered to be the fair value. Both Mr Chenery and Mr. Lee are members of the Audit Committee of the Corporation.

Included in administrative expenses, share issue costs and transaction fees are amounts totaling \$0.1 million which were charged to the Corporation by a legal firm in which a director, who was appointed on August 15, 2008, and the corporate secretary of the Corporation is a partner. These billings include only those amounts billed after appointment, and are in the normal course of business and are measured at the exchange amount which is also considered to be the fair value.

David Tuer, a director and executive of Marble Point, is also a director of Canadian Phoenix.

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As at December 31, 2008, the Corporation had a payable of \$1.5 million to its subsidiary Serrano. The Corporation has no further farm-in commitments to Serrano stemming from the August 20, 2008 purchase agreement.

Subsequent to year end, Serrano exercised its option available under the purchase agreement to re-acquire its 40% interest in a number of wells in the Sawdy region of Alberta, for consideration of \$1. The Corporation retained a 40% participating interest in a number of wells in the Pembina area of Alberta on which it had earned that interest under the Serrano purchase agreement. The result was that the Corporation paid Serrano and the operator of the wells at Baytex \$1.65 million (including expenditure incurred subsequent to year end) to satisfy all gross accounts payable between Serrano and the operator, and the Corporation and Serrano. There was no impact on consolidated financial statements as a result of the exercise of the option.

Marble Point, an equity accounted investee of the Corporation, paid total interest of \$0.4 million to the Corporation during the year in relation to the credit facility described in Note 11.

The Corporation has executed Corporate Governance Agreements with Marble Point and Serrano. These agreements detail certain rights and restrictions the Corporation has in its relationships with these parties.

2007

During the year ended December 31, 2007, the Corporation paid \$0.2 million to Kinghorn Resources Ltd, a corporation controlled by a director, in relation to the lease agreement (2006 - \$0.2 million). Effective December 31, 2007, the lease agreement with Kinghorn was terminated and the deposit in the amount of \$0.2 million was surrendered.

18. FINANCIAL INSTRUMENTS

The Group's financial instruments consist of cash, accounts receivable, accounts payable, and borrowings. The nature of these instruments and its operations expose the Group to market risk, credit risk and liquidity risks. The Corporation manages its exposure to these risks by operating in a manner that minimizes this exposure. While management monitors and administers these risks, the Board of Directors of the Corporation has the overall responsibility for the establishment and oversight of the Group's risk management framework.

Market risk

Market risks are those risks that are outside of the control of the Group, the key ones being unfavorable movements in commodity prices, interest rates, and foreign exchange rates. The objective of the Group is to mitigate exposure to these risks, while maximizing returns.

(a) Commodity price risk

Due to the volatility of commodity prices, the Group is exposed to adverse consequences such as declining revenue and asset recoverability risks in the event of declining oil and gas prices. The Group manages commodity price risk by updating and monitoring forecast cashflows and profitability and making appropriate actions as needed. To date the Group has not used hedging strategies, such as forward oil and natural gas sale contracts to lock in prices with respect to future deliveries, to counter commodity price risk. The Corporation may consider utilizing these types of derivative contracts in the future to protect its revenue cash flow.

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(b) Interest Rate risk

At December 31, 2008 the Group had minimal exposure to movements in interest rates. Movements in interest rates are monitored. The Group had no interest rate swaps or financial contracts to manage interest rate risk in place at year end, nor were any utilized during the year.

(c) Foreign exchange risk

Although the Group's product revenues are denominated in Canadian dollars, the underlying market prices are affected by the exchange rate between the Canadian and the United States dollar. The Group does not make any significant foreign currency denominated payments. Foreign exchange rates movements are monitored. As at December 31, 2008 the Group had no contracts in place to manage foreign exchange risk and no such contracts were utilized during the year.

Sensitivity Analysis – market risks

The impact of a change in commodity prices, foreign exchanges rates, or interest rate has no impact on the Group's financial instruments at December 31, 2008.

Credit Risk

Credit risk is the risk of default on payment by counterparties to financial assets held by the Group. A substantial portion (approximately 95%) of the Group's accounts receivables are concentrated with a limited number of customers and joint venture partners in the oil and gas industry. These receivables are subject to normal industry credit risk. Management considers this concentration of credit risk to be acceptable, as customers are major industry participants, and receivables from partners are protected by effective industry standard legal remedies. The Company requires cash calls from its partners on major field projects in advance of commencement.

Consolidated accounts receivable at December 31, 2008 were \$6.7 million. Receivables related to the sale of production are normally collected on the 25th day of the month following delivery. During 2008, there were no significant bad debt losses incurred. As at December 31, 2008 an impairment allowance of \$0.3m was recorded in relation to a portion of an amount due from a joint venture partner. No other receivables were considered impaired. At December 31, 2008 the Corporation's subsidiary had \$3.3 million in receivables outstanding for greater than 90 days, however the majority has been collected subsequent to year end, and with the exception of the \$0.3m balance noted above, no collection issues with the remaining balances are expected.

Liquidity risk

Liquidity risk is the risk that the Corporation or its controlled entities are not able to meet their financial obligations as they come due. As the oil and gas industry is very capital intensive, the majority of the Group's spending and hence liquidity risk is related to funding its capital programs. The Group's goal is to prudently make capital expenditures while maintaining a strong credit reputation amongst its suppliers.

At December 31, 2008, the Group's financial liabilities consist entirely of trade accounts payable, which are normally settled within 60 days. Refer to Note 1 'Going Concern' for discussion of the Group's plans to manage the settlement of its financial liabilities.

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From time to time the Group enters into agreements which require expenditure commitments, such as the raising of flow-through equity capital and farm-in agreements with joint venture partners in the oil and gas industry. As disclosed in Note 16, as at December 31, 2008 the Group had \$8 million of capital expenditure commitments.

The Group has established a standard of ensuring that it has enough available resources to meet its ongoing financial expenditure requirements. The Group also manages its available resources to ensure it can sustain a downturn in the oil and gas industry in which revenue streams contract and external financing may not be readily available.

Subsequent to year-end, the Corporation and Serrano established a borrowing facility with an arms length lender in the amount of \$6.5 million for each company, available to fund capital projects, acquisitions, and general working capital needs. This credit facility has been suspended and both the Corporation and Serrano are in discussions to establish independent facilities.

Serrano

The Corporation's subsidiary Serrano Energy Ltd carried a working capital deficiency of \$9.3 million (including \$22 million of accounts payable) at December 31, 2008 as a result of an intensive capital program during the year. It is the view of management of Serrano that a line of credit will be established in the near future which will allow it to settle a number of its accounts payable. Subsequent to year end the company has also negotiated settlement of certain trade payables via share issuances, and has proposed payment plans to other creditors.

It is expected that Serrano will continue to experience challenges to fund ongoing operations and its planned capital program. Serrano is pursuing additional financing, debt or equity, to continue under the current capital plan. In conjunction with the potential difficulty of obtaining additional financing, the current capital expenditure plan may need to be diminished.

Refer to Note 1 Going Concern.

Fair Values of Financial Assets and Liabilities

The fair values of the Group's financial instruments that are included in the consolidated balance sheet approximate their carrying amount due to the short-term maturity of those instruments.

19. CAPITAL MANAGEMENT

The Corporation considers the Group's capital structure to consist of shareholders' equity, bank debt and working capital. The Corporation will adjust its capital structure to manage its current and projected debt through issuing shares, increasing its bank line of credit, and/or adjusting its capital spending. Canadian Phoenix monitors its capital based on current and projected cash requirements. Objectives in managing capital structure are to:

- 1) create and maintain flexibility so that the Group can continue to meet its financial obligations; and
- 2) finance growth through internally generated projects, joint venture relationships or asset/corporate acquisitions.

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The Corporation's objective is to maintain a net debt to cash flow from operations ratio relevant to the environment, capital spending needs, and general circumstances such as commodity prices realized and projected. This ratio may fluctuate as a result of an acquisition; however the Corporation aims to maintain a disciplined approach to capital management over time. To facilitate the management of this ratio, the Corporation prepares an annual budget, which is updated each quarter for significant acquisitions, a change in economic circumstances outside the control of the Corporation, and success or failure of capital deployed. The annual budget is approved by the Board of Directors, with quarterly reviews throughout the year.

The Group has no externally imposed capital requirements. There were no changes in the Corporation's approach to capital management in 2008.

20. SUBSEQUENT EVENTS

Serrano-Pearl transaction

On January 28 2009, Serrano received all regulatory (Alberta Securities Commission) and shareholder approvals of a transaction with Pearl Exploration and Production Ltd. ("Pearl"):

- a. Serrano will transfer to Pearl E&P Canada Ltd., a wholly-owned subsidiary of Pearl ("Pearl E&P"), 3/7^{ths} of its interest (or a net 15% working interest) in its Blackrod oil sands leases located south of Fort McMurray, Alberta;
- b. The resulting working interests in the Blackrod project will be 20% for Serrano and 80% for Pearl (through its wholly-owned subsidiaries) and Serrano will transfer operatorship of the project to Pearl;
- c. Serrano will fund the next \$6.25 million of gross expenditures on the Blackrod project, which expenditures will qualify as Canadian Exploration Expense under the Income Tax Act (Canada); and
- d. Pearl will transfer to Serrano all of its 4,037,344 common shares in the capital of Serrano for cancellation and the Pearl nominee will resign from the board of directors of Serrano.

With the completion of this transaction with Pearl, Serrano had 19,457,389 common shares outstanding, resulting in an increase in the Corporation's interest from 47% to 56.8%.

New Debt Facility and Suspension

Subsequent to year-end, the Corporation and its subsidiary Serrano jointly entered into a revolving credit facility with an arms length lender. The facility provided a maximum loan of \$6.5 million to each party, repayable on demand and bearing interest at prime plus 1%. The loans are cross-guaranteed by each of the Corporation and Serrano with a \$25 million floating debenture and a general security agreement over the property and assets of both corporations.

This credit facility has been suspended due to a number of builders liens placed on Serrano's properties. Both the Corporation and Serrano are in discussions to establish independent facilities.

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Legal Settlement

On March 5, 2009 the Corporation settled a legal claim with an industry partner. The settlement required a cash payment of \$1.1 million by the Corporation, and receipt of a 50% working interest in the undeveloped Sarcee region of Alberta. The fair market value of the interest in the property received was assessed to be \$nil as the property has no proved and probable reserves. Included in accounts payable at December 31, 2008 is a liability in the amount of \$1.1 million, recognized as an expense in the income statement.

Sale of Bonnie-Glen Gross Overriding Royalty

On April 17th, 2009 the Corporation divested of a gross-overriding royalty that had been acquired in the Bonnie Glen Unit of central Alberta in the Blue Parrot transaction. The total proceeds of the sale were \$1 million. Consideration consisted of \$0.5 million cash at closing and a promissory note. The promissory note is secured with a debenture and general security agreement on the assets of Blue Parrot, subordinated to an arm's length lender with Blue Parrot. The promissory note will be repaid in two installments. The first installment of \$250,000 plus interest is due June 30, 2009 and the final payment of \$250,000 plus interest is due December 31, 2009. The purchaser has an option to repay the notes at any time without penalty.

Cash Held in Trust – Marble Point Indemnity

In March 2009, the escrow conditions were satisfied whereby the \$1.8 million that the Corporation posted in escrow in September 2008 in support of its agreement to indemnify Marble Point for any withholding taxes payable by non-resident former holders of Marble Point preferred shares on the redemption of such shares was released with interest and returned to the Corporation.

Resignation of Officer

On April 30th, 2009 Thomas Stan the Chief Executive Officer Corporation resigned. Robert Chenery who is the Co-chairman of the Corporation has assumed the interim position of Chief Executive Officer.