

Consolidated Financial Statements of

## **PetroKamchatka Plc**

(formerly PetroKamchatka Resources Ltd. – note 1)

As at May 31, 2010 and 2009  
and for the years ended May 31, 2010 and 2009  
(United States Dollars)

## AUDITORS' REPORT

### To the Shareholders of PetroKamchatka Plc

We have audited the consolidated balance sheets of PetroKamchatka Plc (formerly PetroKamchatka Resources Ltd.) as at May 31, 2010 and 2009 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 Corporation's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

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

**KPMG LLP**

Chartered Accountants

Calgary, Canada

September 28, 2010

# PetroKamchatka Plc

(formerly PetroKamchatka Resources Ltd. (note 1))  
Consolidated Balance Sheets

As at May 31, 2010 and 2009  
(United States Dollars)

	2010	2009
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 7,915,415	\$ 2,108,822
Accounts receivable (note 5)	2,758,064	1,514,742
Prepaid expenses	27,958	146,527
	<u>10,701,437</u>	<u>3,770,091</u>
Property and equipment (note 6)	27,375,366	53,857,598
	<u>\$ 38,076,803</u>	<u>\$ 57,627,689</u>
<b>Liabilities and Shareholders' Equity</b>		
Current liabilities:		
Accounts payable and accrued liabilities	\$ 3,249,580	\$ 6,562,053
Shareholder loans (note 8)	–	395,051
	<u>3,249,580</u>	<u>6,957,104</u>
Shareholders' equity:		
Share capital (note 9(b))	91,755,940	69,731,912
Share purchase warrants (note 9(c))	7,038,779	6,960,263
Contributed surplus (note 9(e))	3,903,396	3,224,396
Currency translation adjustment	1,018,864	1,018,864
Deficit	(68,889,756)	(30,264,850)
	<u>34,827,223</u>	<u>50,670,585</u>
Going concern (note 2)		
Commitments and contingencies (notes 6 and 13)		
Subsequent events (note 14)		
	<u>\$ 38,076,803</u>	<u>\$ 57,627,689</u>

*See accompanying notes to financial statements*

(signed) "Robert McClinton"  
Director

(signed) "Graeme Phipps"  
Director

# PetroKamchatka Plc

(formerly PetroKamchatka Resources Ltd. (note 1))

Consolidated Statements of Operations, Comprehensive Loss and Deficit

Years ended May 31, 2010 and 2009

(United States Dollars, unless otherwise stated)

	2010	2009
Interest income	\$ 88,364	\$ 37,980
Expenses:		
General and administration	4,525,263	3,606,204
Reorganization and listing costs (note 1)	1,173,750	—
Financing and other costs	(425,303)	271,486
Foreign exchange (gain) loss	(94,071)	870,978
Stock-based compensation (note 9(e))	679,000	574,630
Depreciation	734,972	44,824
Write down of property and equipment (note 6)	31,948,499	2,482,417
	38,542,110	7,850,539
Loss before income taxes	(38,453,746)	(7,812,559)
Income taxes (note 10)	—	—
Net loss and comprehensive loss for the year	(38,453,746)	(7,812,559)
Deficit, beginning of year	(30,264,850)	(22,452,291)
Transaction costs (note 1)	(171,160)	—
Deficit, end of year	\$(68,889,756)	\$(30,264,850)
Net loss per share	\$ (0.09)	\$ (0.05)
Weighted average number of common shares outstanding:		
Basic and diluted	430,392,239	154,969,626

*See accompanying notes to financial statements*

# PetroKamchatka Plc

(formerly PetroKamchatka Resources Ltd. (note 1))  
Consolidated Statements of Changes in Cash Flows

Years ended May 31, 2010 and 2009  
(United States Dollars, unless otherwise stated)

	2010	2009
Cash provided by (used in):		
Operations:		
Net loss and comprehensive loss for the year	\$(38,453,746)	\$ (7,812,559)
Items not involving cash:		
Write down of property and equipment	31,948,499	2,482,417
Depreciation	734,972	44,824
Stock-based compensation (note 9(e))	679,000	574,630
Shares issued for services (note 9(b))	174,773	141,523
Shares issued for bonuses and other (notes 9(b)(vii) and 9(b)(viii))	543,334	–
Shares issued for settlement of claim (note 9(b))	–	350,000
Unrealized foreign exchange (gain) loss	(169,463)	10,172
	<u>(4,542,631)</u>	<u>(4,208,993)</u>
Change in non-cash working capital (note 12)	(78,188)	(274,091)
	<u>(4,620,819)</u>	<u>(4,483,084)</u>
Investing:		
Property and equipment expenditures (note 6)	(5,657,906)	(16,261,027)
Short-term investments	–	9,425,204
Rig loan	–	(4,108,758)
Change in non-cash working capital (note 12)	(3,156,896)	(6,596,544)
	<u>(8,814,802)</u>	<u>(17,541,125)</u>
Financing:		
Issue of share capital and warrants for cash, net (note 9)	19,812,264	11,762,651
Shareholders loan (repayment) (note 8)	(395,051)	395,051
Change in non-cash working capital (note 12)	–	6,615,000
	<u>19,417,213</u>	<u>18,772,702</u>
Foreign exchange gain (loss) on cash held in foreign currencies	(174,999)	65,009
Increase (decrease) in cash and cash equivalents	5,806,593	(3,186,498)
Cash and cash equivalents, beginning of year	2,108,822	5,295,320
Cash and cash equivalents, end of year	<u>\$ 7,915,415</u>	<u>\$ 2,108,822</u>

*See accompanying notes to financial statements*

# PetroKamchatka Plc

(formerly PetroKamchatka Resources Ltd. (note 1))  
Notes to the Consolidated financial Statements

Years ended May 31, 2010 and 2009  
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## 1. General:

- (a) PetroKamchatka Plc (the "Corporation" or "PKP") was incorporated on December 23, 2008 under the Companies (Jersey) Law 1991 by directors and officers of PetroKamchatka Resources Ltd. with the intent to have it acquire all of the shares of PetroKamchatka Resources Ltd. ("PKR"). PKR was incorporated on November 23, 1998 under the Business Corporations Act (Yukon, Canada) and was re-domiciled to Cyprus on August 25, 2009. PKR is principally engaged in the exploration and development of petroleum and natural gas resources in the Kamchatka Peninsula of Russia pursuant to exploration licenses (note 6). To date, the Corporation has received no revenue from these operations.
- (b) In October 2009, PKP issued a Take-Over Bid Circular to the shareholders of PKR, to acquire all of the issued and outstanding Class A Common Shares of PKR including any that would become outstanding upon the conversion of warrants of PKR or exercise of options of PKR and to acquire all of the issued and outstanding warrants of PKR (the "Offer"). The shareholders of PKR received one share of PKP for each PKR share held. The warrant holders of PKR received one warrant of PKP for each warrant of PKR held. The PKP warrants and options were issued on substantially similar terms and conditions as the PKR warrants and options (note 9). Under this Offer, PKP acquired PKR effective November 23, 2009 (note 9).
- (c) The Corporation followed the continuity of interest basis of accounting whereby the Corporation is considered a continuation of PKR. These consolidated financial statements reflect the assets, liabilities and results of operations of PKR for periods prior to the acquisition by PKP. PKR is consolidated as a 100% owned subsidiary of PKP. As PKP had no significant assets, liabilities, capital, income or expense prior to the acquisition, the transaction had no significant impact on the consolidated financial statements, except for transaction costs, which were included in expense as part of reorganization and listing costs.

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## 1. General (continued):

(d) On October 2, 2009, the Corporation entered into an Arrangement Agreement to complete a business combination with Bluerock Acquisition Corp. ("Bluerock") a capital pool corporation listed on the TSX Venture Exchange. The arrangement was approved at a special meeting of the Bluerock shareholders and by the Court of Queen's Bench of Alberta, Canada on November 25, 2009 resulting in the Corporation issuing 6,626,501 common shares, on the basis of 0.46837 of a common share for each Bluerock common share outstanding and 187,348 warrants. The warrants expired unexercised (note 9(c)). Bluerock had no operating assets and limited working capital. As a result, the transaction has not been recorded as a business combination, but rather as a capital transaction (note 9).

Details of the acquisition were as follows:

	Number of shares	Amount
Working capital (including cash of \$171,160)	–	\$ 98,840
Common shares issued to Bluerock shareholders (note 9(b))	6,626,501	\$ 98,840

Transaction costs of \$171,160, incurred by Bluerock relating to the acquisition, were recorded as a charge to deficit to the extent of cash available in Bluerock. Additional costs related to the Bluerock transaction, the PKP acquisition of PKR and the listing of the common shares of PKP for trading on the TSX Venture Exchange have been expensed as reorganization and listing costs.

## 2. Going concern:

These consolidated financial statements have been prepared on the basis of accounting principles applicable to a going concern, which assumes that the Corporation will realize its assets and discharge its liabilities in the normal course of operations. If the going concern assumption was not appropriate for these consolidated financial statements, then adjustments would be necessary to adjust the carrying value of assets and liabilities, reported expenses and to revise the balance sheet classifications used.

The Corporation presently does not have sufficient funds to meet all of its exploration and drilling commitments on its licenses in Kamchatka, Russia (note 6). The drilling of two dry holes has negatively impacted the ability of the Corporation to raise additional capital.

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## 2. Going concern (continued):

During the year ended May 31, 2010, the Corporation raised net cash proceeds of \$19,812,264 through two private placements and became a listed public Corporation (notes 1 and 9(b)). At May 31, 2010, the Corporation's working capital was \$7,451,857. If the Corporation is unable to raise additional funds as needed, the Corporation may be in breach of its funding obligations under its agreements with KNOC Kamchatka Petroleum Limited ("KKPL") and may not be able to meet all of its license commitments on its remaining licenses in Kamchatka. It could therefore lose all or part of its interests in the remaining Russian properties. Management believes the going concern assumption to be appropriate for these consolidated financial statements.

## 3. Significant accounting policies:

The consolidated financial statements of the Corporation have been prepared by management in accordance with Canadian generally accepted accounting principles ("GAAP").

### (a) Basis of presentation:

All consolidated financial statement amounts are stated in United States currency.

The consolidated financial statements include the accounts of the Corporation and its subsidiaries and the Corporation's proportionate share of the accounts of its joint interest corporations. The Corporation conducts certain of its oil and gas exploration activities on a joint interest basis (note 7).

### (b) Petroleum and natural gas properties:

At present, all activities of the Corporation are in the exploration stage. The Corporation follows the full cost method of accounting for oil and gas properties whereby all costs of exploring for and developing oil and natural gas resources or reserves are capitalized in cost centers, on a country-by-country basis. Such costs include exploration license acquisition costs and geological, geophysical and drilling costs. All general and administrative costs are expensed as incurred. Carrying costs directly attributable to property and equipment under construction are capitalized.

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### 3. Significant accounting policies (continued):

#### (b) Petroleum and natural gas properties (continued):

Upon the commencement of commercial production, capitalized costs net of impairments, less the carrying value of unevaluated properties, will be depleted within each cost centre using the unit-of-production method based upon estimated proven reserves before royalties, as determined by independent reservoir engineers. For the purposes of this calculation, natural gas will be converted to oil on an energy equivalent basis. The cost of acquiring and evaluating unproven properties are initially excluded from the depletion calculation. These properties are assessed periodically for impairment. When proved reserves are assigned or the property is considered to be impaired, the cost of the property or the amount of the impairment is added to the costs subject to depletion. Proceeds from the sale of petroleum and natural gas properties will be accounted for as an adjustment to capitalized costs, with no gain or loss recognized, unless such adjustment would alter the rate of depletion and depreciation by more than 20%.

In applying the full cost method, the Corporation will complete a ceiling test calculation whereby the carrying amount of property and equipment is compared to the sum of the undiscounted cash flows expected to result from the future production of proved reserves and the sale of unproved properties. Cash flows are based on third party quoted forward prices, adjusted for transportation and quality differentials. Should the ceiling test result in an excess of the carrying amount, the Corporation would then measure the amount of impairment by comparing the carrying amounts of property and equipment to an amount equal to the estimated net present value of future cash flows from proved plus probable reserves and the sale of unproved properties. The Corporation's risk-free interest rate will be used to arrive at the net present value of the future cash flows. Any excess carrying amount would be recorded as impairment and included in depletion and depreciation.

#### (c) Asset retirement obligations:

The Corporation recognizes the fair value of an asset retirement obligation in the period in which it is incurred when a reasonable estimate of the fair value can be made. The fair value of the estimated obligation is recorded as a liability, with a corresponding increase in the carrying amount of the related asset. The capitalized amount is depleted on the unit-of-production method based on proved reserves. The liability amount is increased each reporting period due to the passage of time and the amount of accretion is expensed to income in the period. Actual costs incurred upon the settlement of the obligation are charged against the liability.

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### 3. Significant accounting policies (continued):

(d) Drilling rig and related equipment - Russia:

Depreciation of the drilling rig and related equipment is calculated using the straight-line method over the estimated useful life of the assets of seven years. The cost of normal maintenance and repairs is charged to expense as incurred. Material expenditures that increase the life of an asset are capitalized and depreciated over the estimated remaining useful life of the asset. The cost of equipment sold, or otherwise disposed of, and the related accumulated depreciation is removed from the accounts and any gain or loss is reflected in current operations. The Corporation began using and depreciating the drilling rig and related equipment in October 2009.

(e) Office furniture and equipment:

Office furniture and equipment is recorded at cost upon acquisition. Depreciation is calculated on a declining basis with rates ranging from 30% to 100% per annum. Additions during the period are depreciated at 50% of the assigned rate.

(f) Stock-based compensation:

The Corporation uses the fair value method for accounting for all stock and other stock-based payments, which requires the use of the fair value method of valuing all stock options granted and other stock-based payments whether they be to employees, directors or non-employees. The fair value is recognized in earnings over the vesting period of the options as stock-based compensation expense with a corresponding increase to contributed surplus. Stock-based compensation for options granted to directors and employees is based on the estimated fair value at the time of the grant. Stock-based compensation for options granted to consultants is based on the estimated fair value at each balance sheet date until the related options are fully vested. Upon the exercise of the stock options, consideration paid together with the amount previously recognized as contributed surplus is recorded as an increase to share capital.

(g) Foreign currency translation:

The Corporation determined, effective June 1, 2006, that its functional currency is the United States dollars. Foreign currency amounts are expressed in United States dollars using the temporal method. Under this method, monetary assets and liabilities are translated at the rates of exchange at the balance sheet date; non-monetary assets and related depreciation, amortization and write downs are translated at historic rates; revenues and expenses are translated at rates in effect as they have occurred. Foreign exchange gains and losses are recognized in earnings.

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### 3. Significant accounting policies (continued):

(h) Cash and cash equivalents:

Cash and cash equivalents are comprised of cash and highly liquid investments with original maturities of three months or less.

(i) Future income taxes:

The Corporation uses the asset and liability method of accounting for income taxes. Under this method, income tax liabilities and assets are recognized for the estimated tax consequences attributable to differences between the amounts reported in the consolidated financial statements and their respective tax basis, using income tax rates substantively enacted at the balance sheet date. The effect of a change in rates on future income tax liabilities and assets is recognized in the period in which the change occurs. A valuation allowance is recorded against any future income tax assets if it is more likely than not that the asset will not be realized.

(j) Revenue recognition:

Revenues associated with the sale of crude oil, natural gas and natural gas liquids will be recorded when title passes to the customer. Revenues from properties in which the Corporation has an interest with other producers will be recognized on the basis of the Corporation's net working interest.

(k) Per share data:

Basic per share amounts are computed by dividing the net loss by the weighted average number of common shares outstanding during the year. Diluted per share amounts reflect the potential dilution that would occur if securities or other contracts to issue common shares were exercised or converted to common shares. The treasury stock method is used to determine the dilutive effect of stock options and other dilutive instruments.

(l) Measurement uncertainty:

The preparation of financial statements in accordance with Canadian generally accepted accounting principles requires management to make assumptions and estimates that affect the reported amounts of assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from and affect the results reported in these consolidated financial statements. The most significant estimates relate to the valuation of the Russian petroleum and natural gas properties and equipment and the HighKelly drilling rig (note 6).

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### 3. Significant accounting policies (continued):

(m) Financial instruments:

Cash and short-term investments are held-for-trading investments and the fair values approximate their carrying value due to their short-term nature. Accounts receivable are classified as receivables and accounts payable and accrued liabilities are classified as other financial liabilities. The fair values of accounts receivable and accounts payable and accrued liabilities approximate their carrying values due to the short-term nature of these instruments. The Company has not designated any financial instruments as available for-sale or held-to-maturity.

### 4. Changes in accounting policies:

Effective June 1, 2008, the Corporation adopted the following new accounting standards issued by the Canadian Institute of Chartered Accountants ("CICA"):

- Section 1535 "Capital Disclosures";
- Section 3862 "Financial Instruments – Disclosures"; and
- Section 3863 "Financial Instruments – Presentation".

The new sections enhance disclosure requirements for financial instruments but leave the presentation requirements unchanged.

Section 1535 specifies the disclosure of information about an entity's objectives, policies and processes for managing capital; quantitative data about what the entity regards as capital; whether the entity has complied with any externally imposed capital requirements; and if the entity has not complied, the consequences of non-compliance. Adoption of this standard has resulted in additional note disclosures in the Corporation's consolidated financial statements (note 11).

Section 3862 and Section 3863 specify the standards of presentation and enhanced disclosures on financial statements, particularly with respect to the nature and extent of risks arising from financial instruments and how the entity manages those risks. The standards have resulted in increased disclosures provided in the Corporation's consolidated financial statements (note 11).

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(formerly PetroKamchatka Resources Ltd. (note 1))  
Notes to the Consolidated financial Statements

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## 4. Changes in accounting policies (continued):

Effective June 1, 2008, the Corporation adopted the new accounting standard, Section 3064 “Goodwill and Intangible Assets”, issued by the CICA, replacing Section 3062 “Goodwill and Other Intangible Assets” and Section 3450 “Research and Development Costs”. Section 3064 establishes standards for the recognition, measurement, presentation and disclosure of goodwill and intangible assets subsequent to its initial recognition. Standards concerning goodwill are unchanged from the standards included in the previous Section 3062. Adoption of these standards had no impact on the Corporation’s consolidated financial statements for the years ended May 31, 2010 and 2009.

In January 2009, the CICA Accounting Standards Board (“AcSB”) issued CICA Handbook Section 1582, “Business Combinations”, which replaces former guidance on business combinations. Section 1582 establishes principles and requirements of the acquisition method for business combinations and related disclosures. Section 1582 applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after January 1, 2011 with earlier application permitted. The adoption of section 1582 will affect the accounting for business combinations by the Corporation on or after June 1, 2011.

In January 2009, the AcSB issued CICA Handbook Sections 1601, “Consolidated Financial Statements”, and Section 1602, “Non-controlling Interests”, which replace existing guidance. Section 1601 establishes standards for the preparation of consolidated financial statements. Section 1602 provides guidance on accounting for a non-controlling interest in a subsidiary in consolidated financial statements subsequent to a business combination. These standards are effective on or after the beginning of the first annual reporting period beginning on or after January 1, 2011. Early adoption is permitted provided the new standards are adopted simultaneously with Section 1582 “Business Combinations”. Section 1582 requires equity instruments issued as part of the purchase consideration to be measured at the fair value of the shares at the acquisition date. In addition, guidance generally requires all acquisition costs to be expensed whereas such amounts could be capitalized as part of the purchase price under the previous standard. The adoption of these recommendations may have a material impact on any future business combinations or future investments reported in the Corporation’s consolidated financial statements. The Corporation is currently assessing the impact that the adoption of these Sections may have on its results of operations or financial position.

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#### **4. Changes in accounting policies (continued):**

Effective for fiscal years beginning on or after January 1, 2011, the Corporation will be required to report under IFRS, which will replace Canadian generally accepted accounting principles. The Corporation has developed a changeover plan to complete the transition to IFRS by June 1, 2011. The first unaudited interim consolidated financial statements reported under IFRS will be for the quarter ending August 31, 2011, with comparative figures for the respective period in the year ending May 31, 2011. The Corporation continues to monitor, assess and plan its conversion from Canadian GAAP to IFRS.

#### **5. Accounts receivable:**

Accounts receivable include \$1,338,504 (May 31, 2009 - \$1,492,380) being the Corporation's net proportionate share of refunds of Russian Value Added Taxes ("VAT").

# PetroKamchatka Plc

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Years ended May 31, 2010 and 2009  
(United States Dollars, unless otherwise stated)

## 6. Property and equipment:

May 31, 2010	Cost	Accumulated depreciation	Accumulated impairment	Net book value
Petroleum and natural gas properties:				
Russia	\$ 46,054,358	\$ -	\$ (29,759,649)	\$ 16,294,709
Canada	5,184,840	-	(5,184,840)	-
	51,239,198	-	(34,944,489)	16,294,709
Drilling rig and equipment - Russian	7,498,228	(644,942)	-	6,853,286
Joint interest in drilling rig	8,567,260	-	(4,430,000)	4,137,260
Office furniture and equipment	376,613	(286,502)	-	90,111
	\$ 67,681,299	\$ (931,444)	\$ (39,374,489)	\$ 27,375,366

May 31, 2009	Cost	Accumulated depreciation	Accumulated impairment	Net book value
Petroleum and natural gas properties:				
Russia	\$ 40,190,403	\$ -	\$ -	\$ 40,190,403
Canada	5,018,990	-	(5,018,990)	-
	45,209,393	-	(5,018,990)	40,190,403
Drilling rig and equipment - Russia	7,498,228	-	-	7,498,228
Drilling rig and equipment – Russia	8,368,964	-	(2,407,000)	5,961,964
Office furniture and equipment	403,475	(196,472)	-	207,003
	\$ 61,480,060	\$ (196,472)	\$ (7,425,990)	\$ 53,857,598

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## 6. Property and equipment (continued):

The ultimate recovery of property and equipment costs is dependent upon the existence and commercial exploitation of petroleum and natural gas reserves or a sale of properties to a third party. The Corporation presently does not have sufficient cash to fund all expenditure commitments embedded in the terms of its Russian exploration licenses (note 2). Uncertainties regarding the political, legal, tax or regulatory environment, including the potential for adverse and retroactive changes with respect to the Corporation's operations in Russia could significantly affect the Corporation and the ultimate cost recovery of its assets.

Exploration licenses in Russia are issued by the federal Ministry of Natural Resources ("MNRF") and grant the holder of the license the right to explore for oil and natural gas reserves within the area specified in the license. In the event of a commercial discovery, the Corporation has the right to convert parts of the exploration license into a production license. Exploration licenses have an associated license agreement, which specifies a required geological and geophysical work program to be completed.

At May 31, 2010, the Corporation held interests in exploration licenses in the following areas of Kamchatka, Russia comprising 3,690,900 gross hectares: Tigil, Icha, Urginskaya, Ichaskaya, Palanskaya, Pustaretskaya, and Vorovskaya (note 14(i)).

The following is a summary of the impairments of property and equipment recorded in the years ended May 31, 2010 and 2009:

	May 31, 2010	May 31, 2009
Russian full cost pool		
Tigil – (note 6(a)(i) and note 7)	\$ 29,469,147	\$ -
Urginskaya – (note 6(a)(iii))	237,873	-
Palanskaya – (note 6(a)(iii))	34,617	-
Pustaretskaya – (note 6(a)(iii))	18,012	-
	29,759,649	-
Canadian full cost pool – (note 6(c))	165,850	75,417
Joint interest in drilling rig – (note 6(b))	2,023,000	2,407,000
Total impairments in the year	\$ 31,948,499	\$ 2,482,417

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## 6. Property and equipment (continued):

### (a) Russia:

#### (i) Tigil:

The Corporation is the operator and owns a 45.0% indirect interest (being 90% of 50%) in the Tigil and Icha exploration licenses. On August 11, 2009, the Corporation's indirect interest increased from 42.5% to 45.0% when it acquired an additional 5% equity ownership in its Russian subsidiary from a minority shareholder.

The Tigil license (327,400 gross hectares) was granted to the Corporation on December 29, 2005. The license is valid until December 31, 2010. The Tigil exploration license specifies that the license holder must shoot 400 kilometers of seismic data during 2006 and 2007 and drill two wells during 2007 and 2008. The Corporation previously completed its requirements with respect to the seismic program. The Corporation also obtained an extension of its commitment to drill its wells whereby one well was required to be drilled by December 31, 2009, and the remaining well by December 31, 2010. The Corporation completed drilling of the first well in January 2010 and the second well in May 2010, thereby fulfilling its license obligations.

As both exploration wells were unsuccessful, the Corporation determined that the carrying value of its petroleum and natural gas properties in Russia was impaired resulting in a write down of Tigil carrying costs of \$29,469,147.

#### (ii) Icha:

The Icha exploration license (377,700 gross hectares) was acquired on December 29, 2006. The work program requirements for seismic data were completed in April 2007. The license also requires the drilling and completion of one well before the license expiry on December 30, 2011.

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## 6. Property and equipment (continued):

### (a) Russia (continued):

#### (iii) Urginskaya:

On January 29, 2008, the Corporation obtained a 90% indirect interest in the Urginskaya exploration license in the Kamchatka Peninsula. The Urginskaya exploration license (213,400 gross hectares), valid until February 15, 2013, specified that the license holder must complete a minimum of 200 kilometers of seismic by February 1, 2010; and drill and complete one well within the first three years of the license term. The Corporation did not meet these requirements. Subsequent to May 31, 2010, the Corporation surrendered the Urginskaya exploration license back to the MNFR (note 14(i)). The impairment of the Russian full cost pool of petroleum and natural gas properties includes amounts previously capitalized relating to Urginskaya of \$237,873.

#### (iv) Other:

In September 2009, the Corporation acquired 100% interests in the Pustaretskaya, Palanskaya, Ichinskaya and Vorovksaya exploration licenses. The licenses, valid until September 2014, each required minimum seismic, drilling and completion programs in the first two to three years of the license term. Subsequent to fiscal year end, the Corporation surrendered the Pustaretskaya (553,700 gross hectares) and the Palanskaya (1,251,600 gross hectares) exploration licenses back to the MNFR (note 14(i)). The impairment of the full cost pool of petroleum and natural gas properties includes the amounts previously capitalized relating to Pustaretskaya of \$18,012 and Palanskaya of \$34,617.

### (b) Joint interest in a drilling rig:

The aggregate amount of \$8,567,260 (May 31, 2009 - \$8,368,964) represents the Corporation's 46.25% share of the original purchase price for a new drilling rig (the "HighKelly rig") of \$17,533,000 plus the Corporation's share of other costs. The Corporation and KKPL determined that this rig is not suited for the Russian drilling program and purchased a separate mobile rig and other ancillary equipment to drill in Russia.

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## 6. Property and equipment (continued):

### (b) Joint interest in a drilling rig (continued):

The estimated fair market values of the drilling rig as at August 1, 2010, as indicated by an independent appraisal, was \$9,223,200 gross. On this basis, the carrying value of the Corporation's 46.25% interest was written down in the current fiscal year by \$2,023,000 (May 31, 2009 - \$2,407,000) to \$4,137,260, which amount is net of estimated selling costs.

The Corporation is informed that KKPL has not yet obtained all of the information that it requires to be assured that the rig meets the contracted specifications such that it would be in a position to formally accept the rig. On August 18, 2009, KKPL initiated an arbitration proceeding in The International Court of Arbitration against the manufacturer of the rig in respect of the claim by KKPL that the manufacturer failed to comply with its contractual obligations to manufacture and deliver a customized rig to KKPL in compliance with specific contracted requirements. Pursuant to KKPL's request for arbitration, KKPL is seeking to reject the rig and recover the amounts paid or, alternatively, damages for the alleged breach. Upon resolution of this dispute, the Corporation and KKPL have undertaken to sell the rig.

### (c) Canada:

The Corporation is not active in Canada and its properties in British Columbia have been fully written down.

## 7. Joint ventures:

Effective December 7, 2005, the Corporation effectively sold 50% of its interests in its Tigil and Icha exploration licenses to KNOC Kamchatka Petroleum Limited ("KKPL"), a partially owned subsidiary of Korea National Oil Corporation ("KNOC"). Under shareholder agreements, concluded on February 22, 2006, and initial share purchase agreements, KKPL agreed to fund initial expenditures incurred by the Corporation as follows: 50% of certain equipment previously acquired for use in the projects; 80% of the first \$10,000,000 of exploratory expenditures with respect to the Icha and Tigil licenses; 53.75% of the next \$20,000,000; and for costs in excess of \$30,000,000, KKPL agreed to pay between 50% and 52.5% (formerly 53.75%).

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## 7. Joint ventures (continued):

On October 5, 2007, the Corporation and KKPL, together with KNOC, signed a Settlement Agreement, which, among other things called for certain payments to be made by the Corporation. The obligations of the Corporation under the Settlement Agreement were secured by a pledge of 51% of the Corporation's shares in the Tigil and Icha project companies, which entities own the Russian assets. The terms and conditions of the Settlement Agreement called for a release of the pledge upon satisfaction of payments required under these contracts and satisfactory performance under the project agreements or provision of other acceptable security. Management considers that the Corporation's obligations under the Settlement Agreement have been met. KKPL released the pledge against the shares in July 2010 which release was then accepted for filing by the Russian Registrar (note 14(ii)).

The Corporation's net interests in Tigil and Icha are accounted for on a proportionate consolidation basis.

For the year ended May 31, 2010, the Corporation's net share of amounts contributed to the joint ventures was as follows:

	Tigil	Icha	Total
<b>Balance Sheet:</b>			
Cash	1,500,332	349,206	1,849,538
Accounts receivable	1,428,262	—	1,428,262
Property and equipment, cost (note 6)	29,469,147	16,267,828	45,736,975
Accumulated impairment (note 6)	(29,469,147)	—	(29,469,147)
Drilling rig and related equipment	6,196,956	—	6,196,956
Accounts payable	(186,039)	(5,778)	(191,817)
Net contribution to joint venture	8,939,511	16,611,256	25,550,767
<b>Income Statement:</b>			
Revenues	—	—	—
Expenses (recovery)	29,994,918	(1,779)	29,993,139
Proportionate share of net income (loss)	(29,994,918)	1,779	(29,993,139)
<b>Cash flows:</b>			
Operating activities	77,229	850	78,079
Financing activities	4,570,096	(1,326,307)	3,243,789
Investing activities	(3,803,826)	1,671,048	(2,132,778)
Proportionate share of increase in cash	843,499	345,591	1,189,090

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## 7. Joint ventures (continued):

For the year ended May 31, 2009, the Corporation's net share of amounts contributed to the joint ventures was as follows:

	Tigil	Icha	Total
<b>Balance Sheet:</b>			
Cash	656,833	3,615	660,448
Accounts receivable	99,236	1,709,091	1,808,327
Property and equipment, cost (note 6)	23,618,662	16,297,516	39,916,178
Drilling rig and related equipment (note 6)	6,140,931	—	6,140,931
Accounts payable	(208,746)	(929,841)	(1,138,587)
Net contribution to joint venture	30,306,916	17,080,381	47,387,297
<b>Income Statement:</b>			
Revenues	—	—	—
Expenses (recovery)	(87,290)	13,496	(73,794)
Proportionate share of net income (loss)	87,290	(13,496)	73,794
<b>Cash flows:</b>			
Operating activities	(75,393)	8,065	(67,328)
Financing activities	17,913,247	(3,103,571)	14,809,676
Investing activities	(19,580,839)	1,625,484	(17,955,355)
Proportionate share of (decrease) in cash	(1,742,985)	(1,470,022)	(3,213,007)

## 8. Related party transactions and balances:

At May 31, 2010 and 2009, there were no amounts receivable from directors or officers. The Corporation's aggregate liabilities owing to directors and officers for services performed and expenses incurred in the normal course of operations as at May 31, 2010 amounted to \$67,500 (May 31, 2009 - \$216,590).

At May 31, 2009, the Corporation owed a person who is a shareholder, officer and director of the Corporation the aggregate amount of \$390,000 plus interest for two loans made to the Corporation in the fiscal year ended May 31, 2009. The first loan was an unsecured demand loan of \$90,000, bearing interest at a fixed rate of 12% per annum. The second loan was a demand loan bearing interest at LIBOR plus 3% per annum and was secured by a first priority assignment of the assets of the Corporation. The loans together with interest of \$5,051 were repaid in full in the fiscal year ended May 31, 2010.

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## 9. Share capital:

### (a) Authorized:

An unlimited number of common shares and an unlimited number of preferred shares.

### (b) Common shares issued and outstanding – (note 1 and note 9(b)(i) to 9(b)(xii)):

	May 31, 2010		May 31, 2009	
	Number issued	Amount	Number issued	Amount
Share capital, beginning of year	158,119,627	\$ 69,731,912	131,107,734	\$ 57,799,682
Issued for cash (note 9(b)(v) and (i))	228,505,044	11,477,980	24,960,000	12,480,000
Less share issue costs (note 9(b)(v))	–	(89,401)	–	(717,349)
Less portion representing warrant value	–	–	–	(321,944)
Issued for delay in public listing	–	–	17,562	–
Issued for settlement of claim (note 9(b)(iii))	–	–	1,750,000	350,000
Issued for services (note 9(b)(iv), (ix) and (xii))	2,417,184	174,773	284,331	141,523
Issued for bonus (note 9 (b)(viii))	8,766,666	876,667	–	–
Issued for settlement of liabilities (note 9(b)(vi))	17,600,000	880,000	–	–
Issued for shares of subsidiary (note 9(b)(vii))	5,200,000	260,000	–	–
Issued for cash (note 9(b)(xi))	61,828,486	9,274,273	–	–
Less share issue costs (note 9(b)(xi))	–	(850,591)	–	–
Less portion representing warrant value (note 9(b)(xi))	–	(78,516)	–	–
Issued to acquire Bluerock (note 1 and 9(b)(x))	6,626,501	98,840	–	–
PKP shares upon incorporation (note 9(b)(ii))	2	3	–	–
	489,063,510	\$ 91,755,940	158,119,627	\$ 69,731,912

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## 9. Share capital (continued):

### (b) Common shares issued and outstanding:

- (i) In May 2008, the Corporation issued 43,270,000 common shares pursuant to a private placement for consideration of \$0.50 per share, before the agents' 5.5% commission and other costs. At May 31, 2008, \$6,615,000 in subscriptions related to this placement remained unpaid. In addition, 2,343,000 agent warrants were issued representing 5.5% of the number of shares sold by the agent. The agent warrants provide for the purchase of common shares at \$0.50 each for a period of two years following the date on which the Corporation becomes listed on a recognized stock exchange. In July 2008, the second tranche of the private placement was completed with an additional 24,960,000 common shares being issued at \$0.50 per share and 1,347,500 agent warrants.
- (ii) On December 23, 2008, upon incorporation of the Corporation under the Companies (Jersey) Law 1991, two directors of PKR (note 1) subscribed for two common shares of the Corporation for \$3.
- (iii) On February 13, 2009, the Corporation issued 1,750,000 common shares at \$0.20 per share as a \$350,000 partial and final settlement of a total claim of \$750,000.
- (iv) During the year ended May 31, 2009, the Corporation issued 135,581 common shares to directors, former directors, officers and contractors for services rendered in the amount of \$67,148. In addition, the Corporation issued 148,750 common shares to non-executive directors for services during the year in the amount of \$74,375.
- (v) From June 2009 through August 2009, the Corporation issued, through an offering to shareholders and others closely associated with the Corporation, 217,959,590 common shares at \$0.05 per share and the right to acquire 10,545,454 common shares at \$0.055 per share. The Corporation acquired the obligation to the rightsholders and converted these to common shares of the Corporation when it completed its reorganization and financing transactions in November 2009. This offering generated gross proceeds of \$10,897,980 and \$580,000 respectively, before costs related to the issues of \$89,401.
- (vi) On June 22, 2009, the Corporation issued 17,600,000 common shares at \$0.05 per share to one of the Corporation's vendors to settle aggregate outstanding invoices of approximately \$880,000.

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## 9. Share capital (continued):

### (b) Common shares issued and outstanding (continued):

- (vii) On August 11, 2009, the Corporation issued 5,200,000 common and paid additional costs to acquire an additional 5% equity ownership of its Russian subsidiary from a minority shareholder. After this acquisition, PetroKamchatka owns 90% of its Russian subsidiary. This increased the Corporation's beneficial ownership of the Tigil and Icha licenses to 45%.
- (viii) On October 1, 2009, the Corporation declared a bonus of \$1,155,000 payable to officers, employees and contractors, comprised of \$278,333 in cash and indicated that the remaining portion of \$876,667 would be in the form of 8,766,666 common shares at a price of \$0.10 per share when issuable. The shares were issued in November 2009, upon the completion of its reorganization and financing transactions.
- (ix) In November, 2009, upon the completion of its reorganization and financing transactions, the Corporation issued 1,851,715 common shares to directors, officers and contractors for services rendered in the amount of \$111,023.
- (x) On November 26, 2009, the Corporation issued 6,621,501 common shares and 187,348 warrants to acquire common shares of the Corporation pursuant to an Arrangement Agreement dated October 2, 2009 to complete a business combination with Bluerock (note 1(d)). The warrants expired unexercised on May 14, 2010 (note 9(c)).
- (xi) On November 26, 2009, the Corporation issued 61,828,486 common shares to convert subscription receipts, which were issued by a wholly-owned subsidiary pursuant to a brokered private placement financing at a price of \$0.15 per subscription receipt, into common shares, which financing generated gross proceeds of \$9,274,273, before costs related to the issue of \$850,591. Under the financing, 1,365,834 warrants were issued to brokers to purchase the same number of common shares of the Corporation for \$0.15 per share until November 19, 2011. The warrants were ascribed a fair value of \$78,516 using the Black-Scholes pricing model, assuming a risk-free interest rate of 2.28%; life of 2 years; dividend yield of nil; and expected volatility rates of 69%.
- (xii) On May 31, 2010, the Corporation issued 565,469 common shares to directors at a price of CAD \$0.115 per share for services rendered for the three months ended March 31, 2010 in the amount of \$63,750, representing one-half of the fees owed (see also note 14(iii)).

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## 9. Share capital (continued):

### (c) Warrants:

The following is a continuity of warrants issued to investors and brokers:

	May 31, 2010		May 31, 2009	
	Number issued	Amount	Number issued	Amount
Balance, beginning of year	19,516,940	\$ 6,960,263	21,866,217	\$ 8,021,512
Adjustment	-	-	250,001	-
Issued to brokers	1,365,834	78,516	1,347,500	321,944
Issued to investors (note 1(d))	187,348	-	-	-
Expired	(187,348)	-	(3,946,778)	(1,383,193)
Balance, end of year	20,882,774	\$ 7,038,779	19,516,940	\$ 6,960,263

The following summarizes information on warrants issued to investors to purchase common shares that were outstanding as at May 31, 2010:

Exercise Price		Outstanding and exercisable	Contractual life
\$	£		
	£0.525	5,760,809	December 10, 2011
CAD 1.25		7,590,000	December 10, 2011
Balance, end of year		13,350,809	

On March 15, 2010, the Corporation received approval from investor warrant holders of the £0.525 and CAD \$1.25 warrants to amend the existing term of the warrants. The warrants were exchanged for warrants with substantially similar terms and conditions except that the contractual life was amended to expire on December 10, 2011, two years after the Corporation's listing on the TSX Venture Exchange. The original warrants expired fifteen days following the listing of the Corporation on a recognized public stock exchange and the TSXV was not considered to be a recognized exchange under the original warrant agreement.

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## 9. Share capital (continued):

### (c) Warrants (continued):

The following summarizes information about warrants issued to brokers to purchase common shares that were outstanding as at May 31, 2010:

Exercise price		Outstanding and	Contractual life
\$	£	exercisable	
CAD 0.50		28,800	December 10, 2011
	0.42	614,105	December 10, 2011
CAD 1.00		607,200	December 10, 2011
USD 0.50		4,916,026	December 10, 2011
USD 0.15		1,365,834	November 19, 2011
Balance, end of year		7,531,965	

### (d) Stock options:

The Corporation has a stock option plan for employees, consultants, officers and directors. On October 16, 2009, the Board of Directors of the Corporation adopted a new stock option plan. Under the terms of the option plan, the Corporation may grant options up to 10% of the aggregate number of common shares outstanding, with no one optionee permitted to hold more than 5% of the total options outstanding in any 12 month period. The options granted may not be for a term exceeding five years and vest one-third each year from the date of grant. The exercise price of options is approved by the Board and cannot be less than the market price of its common shares on the day the option is granted.

The following options have been granted:

	May 31, 2010	May 31, 2009
Outstanding, beginning of year	6,225,000	5,400,000
Granted	15,400,000	825,000
	21,625,000	6,225,000
Exercisable, end of year	3,941,667	1,933,333

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## 9. Share capital (continued):

### (d) Stock options (continued):

The fair value of stock options granted and warrants issued during the year ended May 31, 2010 was estimated on the date of grant using the Black-Scholes option-pricing model with the following assumptions:

	Warrants	Options
Fair value of stock options granted in the year ended May 31, 2009 (per option)	–	\$ 0.30
Fair value of stock options granted in the year ended May 31, 2010 (per option)		\$ 0.06
Fair value of warrants granted in the year ended May 31, 2009 (per warrant)	\$ 0.24	–
Fair value of warrants granted in the period ended May 31, 2010 (per warrant)	\$ 0.06	–
Expected volatility	84%	69%
Risk free rate of return	3.2% to 4.3%	2.9% to 4%
Expected option life	2 to 5 years	5 years
Forfeiture rate	nil%	nil%
Dividend yield	nil%	nil%

The following table summarizes stock options outstanding and exercisable at May 31, 2010:

Exercise price	Stock options outstanding			Stock options exercisable	
	Number outstanding	Weighted-average remaining contractual life	Weighted-average exercise price	Number exercisable	Weighted average exercise price
\$ 1.25 CAD	200,000	0.71	\$ 1.25 CAD	200,000	\$ 1.25 CAD
\$ 0.50	6,025,000	2.92	\$ 0.50	3,741,667	\$ 0.50
\$ 0.10	15,100,000	4.59	\$ 0.10	–	\$ 0.10
\$ 0.11	300,000	4.59	\$ 0.11	–	\$ 0.11
	21,625,000	4.08		3,941,667	

Based on the vesting terms of the options, the Corporation recognized stock-based compensation expense for the fiscal year ended May 31, 2010 of \$679,000 (May 31, 2009 - \$574,630) with an equal and offsetting amount recognized as contributed surplus.

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## 9. Share capital (continued):

### (e) Contributed surplus:

Changes in contributed surplus are as follows:

	May 31, 2010	May 31, 2009
Beginning of year	\$ 3,224,396	\$ 1,266,573
Stock-based compensation	679,000	574,630
Expired warrants	–	1,383,193
	<u>\$ 3,903,396</u>	<u>\$ 3,224,396</u>

## 10. Income taxes:

On August 25, 2009, PKR continued out of Canada into Cyprus. Based upon a preliminary valuation, the Corporation believes its estimated value is below its tax basis. PKR is considered to have disposed of all its assets at fair value on the date of re-domiciliation (note 1) and the Canadian tax pools were utilized or expired as part of the re-domiciliation process.

The income tax provision differs from the amount that would be obtained by applying the PKR income tax rate of 0% (May 31, 2009 - 29.9% the Canadian based federal and provincial income tax rate) to earnings (loss) before taxes. The main differences between expected and actual tax provisions are as follows:

	May 31, 2010	May 31, 2009
Net loss	\$(38,453,746)	\$(7,812,559)
Tax rate	<u>0%</u>	<u>29.29%</u>
Computed income tax recovery	-	(2,288,429)
Re-domiciled from Canada to Cyprus	6,911,174	-
Change in tax rate due to operating jurisdiction	(197,880)	165,838
Change in valuation allowance	(6,713,294)	1,582,841
Stock-based compensation	-	168,319
Non-deductible costs	-	99,381
Change in estimates and effective tax rates	-	272,050
	<u>\$ -</u>	<u>\$ -</u>

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## 10. Income taxes (continued):

The components of future income taxes are approximately as follows:

	May 31, 2010	May 31, 2009
Future income tax assets:		
Non-capital loss carries forward	\$ 884,000	\$ 4,895,000
Property and equipment	102,000	2,079,000
Share issue costs	-	725,000
	<u>986,000</u>	<u>7,699,000</u>
Less valuation allowance	(986,000)	(7,699,000)
	<u>\$ -</u>	<u>\$ -</u>

## 11. Financial instruments and risk management:

### (a) Capital management:

As an exploration company, the Corporation's operations are financed principally through shareholders' equity. The Corporation's objectives when managing capital are to: finance planned exploration activities; continue as a going concern; maximize returns for shareholders; provide benefits for other stakeholders; and provide resources to facilitate growth.

The Corporation manages the capital structure and responds to changes in economic conditions and planned requirements. It will continue to use cash from equity offerings to fund operations and invest in its capital expenditure program. Future capital strategies may include debt financing and obtaining strategic partners to fund a portion of its projects.

Current economic conditions continue to affect capital markets and the allocation of capital. This situation, together with the impact of unsuccessful drilling results from its first two wells in Tigil during the fiscal year ended May 31, 2010, stress the need for greater conservation of capital and careful monitoring of the Corporation's rate of spending on capital projects in Russia and to fund general and administrative costs, especially given the absence of adequate financing at May 31, 2010 (note 2).

There are no external restrictions on the Corporation's capital.

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## 11. Financial instruments and risk management (continued):

### (b) Fair values:

The fair value of the Corporation's financial instruments, including cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities approximated their carrying values as at May 31, 2010 and May 31, 2009.

### (c) Financial instrument risk exposure and management:

The Corporation is exposed to various risks associated with its financial instruments. These risks are categorized as market risk, credit risk and liquidity risk.

#### Market risk:

Market risk is the risk that changes in market conditions, such as commodity prices, exchange rates and interest rates, will affect the Corporation's net earnings or the value of its financial instruments. The objective of market risk management is to manage and control exposures within acceptable limits, while maximizing returns.

#### Commodity risk:

Commodity price risk is the risk that the fair value of future cash flows will fluctuate as a result of changes in commodity prices. Significant changes in commodity prices can also reduce the Corporation's ability to raise capital. Commodity prices for crude oil are impacted by world economic events that dictate the levels of supply and demand. In the future, the Corporation may attempt to mitigate commodity price risk through the use of financial derivatives. The Corporation does not have any oil or gas production and did not have any risk management contracts in place as at or during the years ended May 31, 2009 and 2010, or thereafter.

#### Foreign currency risk:

The Corporation is exposed to foreign currency fluctuations as it holds cash and incurs expenditures in property and equipment in foreign currencies. The Corporation incurs expenditures in Russian rubles, Pound sterling, Euros and Canadian dollars and is exposed to fluctuations in exchange rates in these currencies. There are no exchange rate contracts in place as at or during the years ended May 31, 2009 or 2010, or thereafter.

A 1% change in foreign exchange rates between the Russian ruble and the U.S. dollar would have resulted in approximate \$40,000 change in net loss for year ended May 31, 2010.

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## 11. Financial instruments and risk management (continued):

### (c) Financial instrument risk exposure and management (continued):

#### Credit Risk:

Financial instruments that potentially subject the Corporation to concentration of credit risk consist of accounts receivable. There is low credit risk on accounts receivable. Accounts receivable consists of Russian value added taxes (note 5) and accounts receivable from the Corporation's joint ventures. At May 31, 2010 the Corporation's receivables were current.

#### Liquidity Risk:

Liquidity risk is the risk that the Corporation will not be able to meet its financial obligations as they become due. The Corporation's financial liabilities consist of accounts payable and accrued liabilities. Accounts payable consists primarily of invoices payable to trade suppliers or professionals for capital expenditures and services rendered.

The Corporation prepares budgets for its corporate operations and capital expenditure programs which are regularly monitored and updated as considered necessary.

## 12. Supplemental cash flow disclosures:

### Change in non-cash working capital:

	Years ended May 31,	
	2010	2009
Share subscriptions receivable	\$ –	\$ 6,615,000
Accounts receivable	(1,243,322)	(1,426,079)
Prepaid expenses	118,569	(102,999)
Accounts payable and accrued liabilities	(3,312,473)	(5,341,557)
	(4,437,226)	(255,635)
Unrealized foreign exchange loss on working capital	345,496	–
Less non-cash working capital acquired from Bluerock (note 1)	(72,320)	–
Add shares issued for accounts payable	928,966	–
	(3,235,084)	(255,635)
Less changes in non-cash working capital related to investing	3,156,896	6,596,544
Less changes in non-cash working capital related to financing	–	(6,615,000)
Changes in non-cash working capital related to operations	\$ (78,188)	\$ (274,091)

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## 12. Supplemental cash flow disclosures (continued):

Cash interest of \$5,051 (note 8) was paid during the year ended May 31, 2010 (2009 - \$182,489).

## 13. Commitments and contingencies:

Under the terms and conditions of its Russian exploration licenses, the Corporation is committed to completion of seismic work programs and the drilling of exploration wells by certain dates in order to retain its rights under the licenses (note 6).

The Corporation is committed to making payments with respect to its office leases in Canada which expire on June 30, 2013 and October 31, 2013.

Future net minimum lease payments for these leases by fiscal year are as follows:

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2011	\$ 264,000
2012	264,000
2013	264,000
2014	55,000
	<hr/> \$ 847,000

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## 14. Subsequent events:

Subsequent to May 31, 2010, the Corporation:

- (i) Surrendered the Urginskaya (213,400 gross hectares), the Palanskaya (1,251,600 gross hectares) and the Pustaretskaya (553,700 gross hectares) exploration licenses back to the MNRF without further commitments or obligations beyond the payment of current lease rentals (note 6);
- (ii) Received from KKPL the signed Order to release the pledge against the Corporation's share holdings in CJSC Tigil Exploration and CJSC Icha Exploration, formerly issued in favor of KKPL pursuant to the terms of the Settlement Agreement. These releases were recorded in the Russian Registry (note 7);
- (iii) Issued 676,130 common shares to directors at a price of CAD \$0.05 per share for services rendered for the three months to June 30, 2010 in the amount of \$31,875, representing one-half of the fees owed.