Condensed Consolidated Interim Financial Statements of
(Unaudited)

GASTEM INC.

Periods ended September 30, 2011 and 2010

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GASTEM INC.

Condensed Consolidated Interim Statements of Financial Position
(Unaudited)

September 30, 2011, December 31, 2010 and January 1, 2010

	September 30, 2011	December 31, 2010	January 1, 2010
Assets			
Current assets:			
Cash and cash equivalents	$ 22,573	$ 391,280	$ 1,217,033
Restricted cash	–	1,600,000	–
Funds reserved for exploration	3,095,985	5,631,653	6,343,005
Accounts receivable	845,466	1,178,800	2,948,404
Prepaid expenses and deposits	39,179	22,400	113,396
Total current assets	4,003,203	8,824,133	10,621,838
Non-current assets:			
Equipment	172,599	201,707	62,825
Gas properties (note 4)	5,763,711	5,709,163	5,674,526
Exploration and evaluation assets (note 5)	22,427,234	20,433,663	11,819,555
Long-term deposits	285,000	285,000	948,082
Total non-current assets	28,648,544	26,629,533	18,504,988
Total assets	$ 32,651,747	$ 35,453,666	$ 29,126,826
Liabilities			
Current liabilities:			
Accounts payable and accrued liabilities	$ 1,729,802	$ 2,192,479	$ 645,450
Total current liabilities	1,729,802	2,192,479	645,450
Equity			
Share capital and warrants (note 6)	46,628,221	46,628,221	37,951,898
Contributed surplus	2,702,271	2,658,732	2,611,830
Deficit	(18,408,547)	(16,025,766)	(12,082,352)
Total equity attributable to equity holders of the Company	30,921,945	33,261,187	28,481,376
Total liabilities and equity	$ 32,651,747	$ 35,453,666	$ 29,126,826

The notes on pages 5 to 37 are an integral part of these unaudited condensed consolidated interim financial statements.

GASTEM INC.

Condensed Consolidated Interim Statements of Comprehensive Income
(Unaudited)

Periods ended September 30, 2011 and 2010

	Three-month period ended September 30,		Nine-month period ended September 30,	
	2011	2010	2011	2010
Expenses:				
Salaries and benefits	$ 150,579	$ 119,223	$ 484,032	$ 411,153
Share-based payments (note 7)	30,366	12,378	43,539	34,378
Professional fees	126,304	197,278	551,943	420,533
Office, trustees and report to equity holders	104,960	113,130	322,360	449,577
Travel and promotion	22,680	39,553	92,101	105,542
Rent	21,673	25,391	78,844	70,788
Depreciation of equipment	10,433	11,463	30,258	17,734
	466,995	518,416	1,603,077	1,509,705
Impairment of exploration and evaluation assets	–	–	738,252	–
Site restoration expense	(200,000)	–	–	–
Loss before net finance income and income taxes	(266,995)	(518,416)	(2,341,329)	(1,509,705)
Net finance income (note 8):				
Finance income	10,959	22,763	45,972	71,683
Finance expense	(71,416)	(3,597)	(87,424)	(14,131)
Loss on disposal capital assets	–	(1,380)	–	(1,380)
	(60,457)	17,786	(41,452)	56,172
Loss before income taxes	(327,452)	(500,630)	(2,382,781)	(1,453,533)
Deferred income taxes (note 9)	–	(430,765)	–	(540,629)
Loss and comprehensive loss	(327,452)	(931,395)	(2,382,781)	(1,994,162)
Basic and diluted net loss per share	(0,004)	(0,012)	(0,027)	(0,027)
Weighted average number of outstanding shares, during the period	89,787,007	74,936,777	89,787,007	74,936,777

The notes on pages 5 to 37 are an integral part of these unaudited condensed consolidated interim financial statements.

GASTEM INC.

Condensed Consolidated Interim Statements of Cash Flows
(Unaudited)

Periods ended September 30, 2011 and 2010

	Three-month period ended September 30,		Nine-month period ended September 30,	
	2011	2010	2011	2010
Cash flows from operating activities:				
Net loss and comprehensive loss	$ (327,452)	$ (931,395)	$ (2,382,781)	$ (1,994,162)
Adjustment for:				
Depreciation of equipment	10,433	11,463	30,258	17,734
Deferred income taxes	–	430,765	–	540,629
Share-based payments	30,366	12,378	43,539	34,378
Interest income	(24,297)	(22,763)	(45,972)	(71,683)
Impairment of exploration and evaluation assets	–	(1,380)	738,252	(1,380)
Site restoration expense	(200,000)	–	–	–
Changes in non-cash working capital items:				
Accounts receivable	(244,215)	(21,188)	333,334	150,631
Prepaid expenses and deposits	(10,913)	(1,237,711)	(16,779)	(1,178,588)
Accounts payable and accrued liabilities	882,201	(188,638)	(462,677)	(424,377)
Interest received	24,297	22,763	45,972	71,683
	140,420	(1,925,706)	(1,716,854)	(2,855,135)
Cash flows from financing activities:				
Proceeds from share issuance	–	2,765,750	–	8,587,450
Share issuance costs	–	(321,597)	–	(798,242)
	–	2,444,153	–	7,789,208
Cash flows from investing activities:				
Decrease in restricted cash	–	–	1,600,000	–
Increase (decrease) in funds reserved for exploration	1,076,204	194,142	2,535,668	(2,462,727)
Additions to gas properties	25,436	(59,917)	(54,548)	(138,607)
Additions to exploration and evaluation assets	(1,322,817)	(1,943,927)	(2,731,823)	(2,960,798)
Additions to equipment	–	(98,308)	(1,150)	(164,313)
Deposits on long-term assets	–	2,555,512	–	326,056
Balance on sale of properties	–	–	–	550,000
Disposition of capital assets	–	400	–	400
Proceeds on disposal of gas property	–	(15,225)	–	–
	(221,177)	632,677	1,348,147	(4,849,989)
Decrease in cash and cash equivalents	(80,757)	1,151,124	(368,707)	84,084
Cash and cash equivalents, beginning of period	103,330	149,993	391,280	1,217,033
Cash and cash equivalents, end of period	22,573	1,301,117	22,573	1,301,117

The notes on pages 5 to 37 are an integral part of these unaudited condensed consolidated interim financial statements.

GASTEM

Condensed Consolidated Interim Statements of Changes in Equity
(Unaudited)

Periods ended September 30, 2011 and 2010

	Share capital and warrants	Contributed surplus	Deficit	Total
Balance, January 1, 2010	$ 37,951,898	$ 2,611,830	$ (12,082,352)	$ 28,481,376
Shares issued	8,515,750	–	–	8,515,750
Share issuance costs	–	–	(798,242)	(798,242)
Deferred taxes arising from share issuance costs	–	–	540,629	540,629
Share-based payments	–	34,378	–	34,378
Options exercised	160,573	(88,873)	–	71,700
Net loss	–	–	(1,994,162)	(1,994,162)
Balance, September 30, 2010	$ 46,628,221	$ 2,557,335	$ (14,334,127)	$ 34,851,429
Balance, January 1, 2010	$ 37,951,898	$ 2,611,830	$ (12,082,352)	$ 28,481,376
Shares issued	8,515,750	–	–	8,515,750
Share issuance costs	–	–	(813,447)	(813,447)
Deferred taxes arising from share issuance costs	–	–	751,622	751,622
Warrants exercised	–	(88,873)	–	(88,873)
Share-based payments	–	135,775	–	135,775
Options exercised	160,573	–	–	160,573
Net loss	–	–	(3,881,589)	(3,881,589)
Balance, December 31, 2010	46,628,221	2,658,732	(16,025,766)	33,261,187
Share-based payments	–	43,539	–	43,539
Net loss	–	–	(2,382,781)	(2,382,781)
Balance, September 30, 2011	$ 46,628,221	$ 2,702,271	$ (18,408,547)	$ 30,921,945

The notes on pages 5 to 37 are an integral part of these unaudited condensed consolidated interim financial statements.

Gastem inc. ("Gastem" or the "Company") is incorporated under the *Canada Business Corporations Act*. The address of the Company's registered office is 1155 University Street Montréal, Québec, Canada. The Company was set up to hold interests in gas properties, which are presently at the exploration stage and it has not yet been determined whether the properties contain reserves that are economically recoverable.

The condensed consolidated interim financial statements of the Company as at and for the period ended September 30, 2011 comprise the Company and its subsidiary (together referred to as the "Group" and individually as "Group entities").

1. Nature of operations and going concern:

The Company holds gas properties or interest in such properties and permits (''properties'') in the province of Québec and in the United States.

Although the Company has taken steps to verify title to gas properties in which it has an interest in accordance with industry standards for the current stage of exploration of such properties, these procedures do not guarantee the Company's title. Property title may be subject to unregistered prior agreements and non-compliance with regulatory requirements.

The condensed consolidated interim financial statements were prepared under the assumption of going concern, which presumes that the Company will continue its operations in the foreseeable future and will be able to realize its assets and discharge its liabilities in its normal course of operations.

The Company is in the process of exploring and evaluating its gas properties and projects and has not yet determined whether its properties and projects contain reserves that are economically recoverable. Operations activities have not generated yet any revenues. The ability of the Company to meet its commitments as they become payable, including the acquisitions of gas properties and the development of projects, is dependent on the ability of the Company to obtain necessary financing. The recoverability of amounts shown for gas properties is dependent upon the ability of the Company to obtain necessary financing to complete the acquisition, exploration and development thereof, and upon future profitable production or proceeds from the disposal of properties.

It should also be noted that the Minister of Sustainable Development, Environment and Parks has released a report to the Bureau d'audiences publiques sur l'environnement ("BAPE") filed on February 28, 2011 about the sustainable development of the shale gas industry in Quebec. In its report the commission of inquiry of the BAPE presents a number of findings and recommendations. Among others, all fracturing operations in the oil and gas industry in Quebec will now be subject to the Strategic Environmental Study ("SES"). Thus, all the fracturation activities will be authorized only for the purpose of developing scientific knowledge of environmental assessment, until the end of the SES.

1. Nature of operations and going concern (continued):

The Company's gas properties located in Quebec and the related deferred exploration costs, totalling $19,858,350 as at September 30, 2011, include fracture wells affected by these new procedures. In addition, as part of a farm-out contract, the operator of the St-Hyacinthe project and the Company are required to complete work on fracture wells of this property totalling approximately 6 million dollars by 2014, without which the society and its partner will lose their interest in the property. The amounts capitalized as gas properties and deferred exploration costs for this property totalled $5,660,337 as at September 30, 2011. To date, management is unable to determine when the exploration will continue on these properties.

Furthermore, similar environment-related concerns have been voiced in the Magdalen Islands and New York State, where the Company currently has properties and conducts operations. In particular, in New York State, the Draft Generic Environmental Impact Study by the Department of Conservation in New York State was presented on July 8, 2011. The DGEIS will report on hydraulic fracturing and make suggestions regarding this procedure.

These conditions indicate the existence of a significant uncertainty which may cast significant doubt on the ability of the Company to continue as a going concern.

These financial statements do not reflect adjustments that should be made to the book value of assets and liabilities, if the going concern assumption was inappropriate.

2. Basis of preparation:

Statement of compliance

The Company prepares its financial statements in accordance with Canadian generally accepted accounting principles as set out in the Handbook of the Canadian Institute of Chartered Accountants ("CICA Handbook"). In 2010, the CICA Handbook was revised to incorporate International Financial Reporting Standards ("IFRS"), which require publicly accountable enterprises to apply such standards effective for years beginning on or after January 1, 2011. Accordingly, the Company has commenced reporting on this basis in these condensed consolidated interim financial statements. In the financial statements the term "Canadian GAAP" refers to Canadian GAAP before the adoption of IFRS.

2. Basis of preparation (continued):

Statement of compliance (continued)

These condensed consolidated interim financial statements have been prepared in accordance with IFRS applicable to the preparation of interim financial statements as published by the International Accounting Standards Board ("IASB"), including IAS 34, *Interim Financial Reporting*, and IFRS 1, *First-time Adoption of International Financial Reporting Standards*. Subject to certain transition elections disclosed in note 12, the Company has consistently applied the same accounting policies in its opening IFRS statement of financial position at January 1, 2010 and throughout all periods presented, as if these policies had always been in effect. Note 12 discloses the impact of the transition to IFRS on the Company's reported financial position, financial performance and cash flows, including the nature and effect of significant changes in accounting policies, from those used in the Company's consolidated financial statements for the year ended December 31, 2010.

The accounting policies applied in these condensed consolidated interim financial statements are based on IFRS issued and outstanding as of September 27, 2011, the date on which the Board of Directors approved the condensed consolidated interim financial statements. Any subsequent changes to IFRS that are given effect in the Company's annual consolidated financial statements for the year ending December 31, 2011 could result in restatement of these condensed consolidated interim financial statements, including the transition adjustments recognized on transition to IFRS.

The condensed consolidated interim financial statements should be read in conjunction with the Company's Canadian GAAP annual financial statements for the year ended December 31, 2010. The notes disclose IFRS information for the year ended December 31, 2010, not already provided in the 2010 annual financial statements.

Basis of measurement

The condensed consolidated interim financial statements have been prepared on the historical cost basis.

Functional and presentation currency

These condensed consolidated interim financial statements are presented in Canadian dollar, which is the Company’s functional currency.

2. Basis of preparation (continued):

Use of estimates and judgements

The preparation of the condensed consolidated interim financial statements in conformity with IFRS requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected.

Information about critical judgements in applying accounting policies that have the most significant effect on the amounts recognized in the condensed consolidated interim financial statements is included in note 3 and consists in the determination of capitalizable costs as exploration and evaluation assets.

Information about assumptions and estimation uncertainties that have a significant risk of resulting in a material adjustment within the next financial year are included in the following notes:

- Notes 3, 4 and 5, recoverability of gas properties and exploration and evaluation assets;
- Note 3 - assessment of refundable tax credits related to resources;
- Notes 3 and 7 - estimation of fair value of share-based payment;
- Note 9 - recoverability of income tax assets;
- Note 3 - estimation of fair value of the liability related to flow-through shares.

3. Significant accounting policies:

The accounting policies set out below have been applied consistently to all periods presented in these condensed consolidated interim financial statements and in preparing the opening IFRS statement of financial position at January 1, 2010 for the purposes of the transition to IFRS, unless otherwise indicated.

The accounting policies have been applied consistently by Group entities.

3. Significant accounting policies (continued):

(a) Basis of consolidation:

Subsidiary

The condensed consolidated interim financial statements include the accounts of the Company and its wholly-owned subsidiary Gastem USA Inc.

A subsidiary is an entity controlled by the Group. The financial statements of a subsidiary are included in the consolidated financial statements from the date that control commences until the date that control ceases. The accounting policies of a subsidiary have been changed when necessary to align them with the policies adopted by the Group.

Jointly controlled assets

The Company holds interests in gas properties through joint operating agreements which constitute jointly controlled assets.

A jointly controlled asset involves joint control and offers joint ownership by the Group and other venturers of assets contributed to or acquired for the purpose of the joint venture, without the formation of a corporation, partnership or other entity. Where the Group's activities are conducted through jointly controlled assets, the Group recognizes its share of the jointly controlled assets, and liabilities it has incurred, its share of liabilities incurred jointly with other venturers, and exploration and evaluation costs in the financial statements.

Transactions eliminated on consolidation

Intra-group balances and transactions, and any unrealized income and expenses arising from intra-group transactions, are eliminated in preparing the consolidated financial statements.

(b) Foreign currency:

Transactions in foreign currencies are translated to the respective functional currencies of Group entities at exchange rates at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are retranslated to the functional currency at the exchange rate at that date. The foreign currency gain or loss on monetary items is the difference between amortized cost in the functional currency at the beginning of the period, adjusted for effective interest and payments during the period, and the amortized cost in foreign currency translated at the exchange rate at the end of the reporting period. Foreign currency differences arising on retranslation are recognized in profit or loss. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction.

3. Significant accounting policies (continued):

(c) Financial instruments:

Non-derivative financial assets and liabilities are initially recognized at fair value plus any directly attributable transaction costs.

Loans and receivables

Loans and receivables are financial assets with fixed or determinable payments that are not quoted in an active market. Subsequent to initial recognition, loans and receivables are measured at amortized cost using the effective interest method, less any impairment losses.

The Company classified its cash and cash equivalents, restricted cash, funds reserved for exploration and accounts receivables as loans and receivables.

Cash and cash equivalents, restricted cash and funds reserved for exploration include temporary investments with an original maturity date of three months or less.

The restricted cash corresponds to an amount extended as an irrevocable letter of credit to a supplier. This letter of credit has a short-term expiry.

The funds reserved for exploration represent proceeds from private placements of flow-through shares not yet expensed. The Company must use these funds for exploration of gas properties in accordance with restrictions imposed by these private placements.

Financial liabilities

The Company classified its accounts payable and accrued liabilities as financial liabilities at amortized cost. Subsequent to initial recognition, these financial liabilities are measured at amortized cost using the effective interest method.

(d) Gas properties and exploration and evaluation assets:

Gas properties correspond to acquired interests in gas exploration permits / claims which include the rights to explore for, extract and sell all minerals from such claims.

All pre-exploration costs, i.e. costs incurred prior to obtaining the legal right to undertake exploration and evaluation activities on an area of interest, are expensed as incurred.

Once the legal right to explore has been acquired, exploration and evaluation expenditure are capitalized in respect of each identifiable area of interest until the technical feasibility and commercial viability of extracting a gas resource are demonstrable.

Costs incurred include appropriate technical and administrative overheads.

Gas properties and exploration and evaluation assets are carried at historical cost less any impairment losses recognized.

3. Significant accounting policies (continued):

(d) Gas properties and exploration and evaluation assets (continued):

When technical feasibility and commercial viability of extracting a gas resource are demonstrable for an area of interest, the Group stops capitalizing gas properties and exploration and evaluation costs for that area, tests recognized exploration and evaluation assets for impairment and reclassifies any unimpaired exploration and evaluation assets either as tangible and intangible mine development assets according to the nature of the assets.

(e) Equipment:

Items of equipment are measured at cost less accumulated depreciation and accumulated impairment losses. Cost includes expenditures that are directly attributable to the acquisition of the asset. Purchased software that is integral to the functionality of the related equipment is capitalized as part of that equipment. The costs of the day-to-day servicing of equipment are recognized in profit or loss as incurred.

Depreciation is calculated over the depreciable amount, which is the cost of an asset, or other amount substituted for cost, less its residual value.

The estimated useful lives for the current and comparative periods are as follows:

- Furniture and equipment: 5 years
- Computer equipment: 5 years

Depreciation methods, useful lives and residual values are reviewed at each financial year-end and adjusted if appropriate.

(f) Impairment:

Financial assets

Financial assets are assessed at each reporting date to determine whether there is objective evidence that they are impaired. A financial asset is impaired if objective evidence indicates that a loss event has occurred after the initial recognition of the asset, and that the loss event had a negative effect on the estimated future cash flows of that asset that can be estimated reliably.

An impairment loss in respect of a financial asset measured at amortized cost is calculated as the difference between its carrying amount and the present value of the estimated future cash flows discounted at the asset's original effective interest rate. Losses are recognized in profit or loss and reflected in an allowance account against receivables. Interest on the impaired asset continues to be recognized through the unwinding of the discount. When a subsequent event causes the amount of impairment loss to decrease, the decrease in impairment loss is reversed through profit or loss.

3. Significant accounting policies (continued):

(f) Impairment (continued):

Non-financial assets

The carrying amounts of property, plant and equipment are reviewed at each reporting date to determine whether there is any indication of impairment.

The carrying amounts of gas properties and exploration and evaluation assets are assessed for impairment only when indicators of impairment exist, typically when one of the following circumstances apply:

- Exploration rights have or will expire in the near future;
- No future substantive exploration expenditures are budgeted;
- No commercially viable quantities are discovered and exploration and evaluation activities will be discontinued;
- Exploration and evaluation assets are unlikely to be fully recovered from successful development or sale.

If any such indication exists, then the asset's recoverable amount is estimated.

Gas properties and exploration and evaluation assets are also assessed for impairment upon the transfer of exploration and evaluation assets to development assets regardless of whether facts and circumstances indicate that the carrying amount of the exploration and evaluation assets is in excess of their recoverable amount.

The recoverable amount of an asset or cash-generating unit is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For the purpose of impairment testing, assets that cannot be tested individually are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups of assets (the "cash-generating unit, or CGU"). The level identified by the group for the purposes of testing exploration and evaluation assets for impairment corresponds to each gas property.

3. Significant accounting policies (continued):

(f) Impairment (continued):

Non-financial assets (continued)

An impairment loss is recognized if the carrying amount of an asset or its CGU exceeds its estimated recoverable amount. Impairment losses are recognized in profit or loss. Impairment losses recognized in respect of CGUs are allocated to the assets in the unit (group of units) on a pro rata basis.

Impairment losses recognized in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortization, if no impairment loss had been recognized.

(g) Provisions:

A provision is recognized if, as a result of a past event, the Company has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation.

(h) Share capital and warrants:

Common shares

Common shares are classified as equity. Incremental costs directly attributable to the issue of common shares and share options are recognized as an increase to deficit, net of any tax effects.

Flow-through shares

The Canadian tax legislation permits an entity to issue securities to investors whereby the deductions for tax purposes relating to resource expenditures may be claimed by the investors and not by the entity. These securities are referred to as flow-through shares. The Company finances a portion of its exploration programs with flow-through share issues.

At the time of share issuance, the Company allocates the proceeds between share capital and an obligation to deliver the tax deductions, which is recorded as a liability for flow-through shares obligation. The Company estimates the fair value of the obligation using the residual method, i.e. by comparing the price of the flow-through share to the quoted price of common share at the date of the financing announcement.

A company may renounce the deductions for tax purposes under either what is referred to as the "general" method or the "look-back" method.

3. Significant accounting policies (continued):

(h) Share capital and warrants (continued):

Flow-through shares (continued)

When tax deductions are to be renounced under the general method, and the Company has the expectation of renouncing and has capitalized the expenditures during the current year, then the entity records a deferred tax liability with the corresponding charge to income tax expense. The obligation is reduced to zero, with a corresponding income recorded.

When tax deductions are to be renounced under the look-back method, the Company records a deferred tax liability with a corresponding charge to income tax expense when expenditures are made and capitalized. At that time, the obligation would be reduced to zero, with a corresponding income recorded.

Warrants

Warrants are classified as equity as they are derivatives over the Company's own equity that will be settled only by the Company exchanging a fixed amount of cash for a fixed number of the Company's own equity instruments.

Share issuance costs

Share issuance costs are charged to deficit in the same period during which they are incurred.

(i) Share-based payments:

The grant date fair value of share-based payment awards granted to employees and directors is recognized as an expense, with a corresponding increase in contributed surplus, over the period that the employees unconditionally become entitled to the awards. The amount recognized as an expense is adjusted to reflect the number of awards for which the related service conditions are expected to be met, such that the amount ultimately recognized as an expense is based on the number of awards that do meet the related service conditions at the vesting date.

(j) Leases:

All leases are classified as operating leases and as such the leased assets are not recognized in the Company's statement of financial position.

Payments made under operating leases are recognized in profit or loss on a straight-line basis over the term of the lease.

(k) Finance income and finance costs:

Interests received and interests paid are classified under operating activities in the statement of cash flows.

3. Significant accounting policies (continued):

(l) Income tax:

Income tax expense comprises current and deferred tax. Current tax and deferred tax are recognized in profit or loss except to the extent that it relates to a business combination, or items recognized directly in equity or in other comprehensive income.

Current tax is the expected tax payable or receivable on the taxable income or loss for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax is recognized in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognized for the following temporary differences: the initial recognition of assets or liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable profit or loss, and differences relating to investments in subsidiaries to the extent that it is probable that they will not reverse in the foreseeable future.

Deferred taxes are recognized as income or expense in profit or loss except to the extent that tax arises from business combinations and transactions recognized in equity. Therefore, when deferred taxes relate to equity items, a backwards tracing is necessary to determine the adjustment to taxes (e.g. change in tax rates and change in valuation allowance) that should be recorded in equity. For this purpose, the accounting policy of the Company is to allocate changes in the recognition of deferred tax assets based on their expected maturity date.

Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date. Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax liabilities and assets, and they relate to income taxes levied by the same tax authority on the same taxable entity, or on different tax entities, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realized simultaneously.

A deferred tax asset is recognized for unused tax losses and deductible temporary differences, to the extent that it is probable that future taxable profits will be available against which they can be utilized. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realized.

3. Significant accounting policies (continued):

(m) Refundable tax credit related to resources:

The Company is eligible for a refundable tax credit related to resources in relation to eligible expenses incurred. The refundable tax credit related to resources represents up to 38.75% of the amount of eligible expenses incurred.

Credits related to resources are recognized against exploration and evaluation expenditures at fair value when there is reasonable assurance that they will be received and the Group will comply with the conditions associated with the credit. They are recognized in profit or loss on a systematic basis over the useful life of the related assets.

(n) Earnings per share:

The Company presents basic and diluted earnings per share ("EPS") data for its common shares. Basic EPS is calculated by dividing the profit or loss attributable to common shareholders of the Company by the weighted average number of common shares outstanding during the period, adjusted for own shares held. Diluted EPS is determined by adjusting the profit or loss attributable to common shareholders and the weighted average number of common shares outstanding, adjusted for own shares held, for the effects of all dilutive potential common shares, which comprise warrants and share options granted to employees.

(o) Segment reporting:

The Company determined that it had only one operating segment, i.e. the gas exploration.

(p) Adoption of new accounting standards:

Annual improvements to IFRS:

The improvements to IFRS 2010 are the result of the IASB's annual improvements project. This project has involved the IASB accumulating, throughout 2010, those improvements believed to be non-urgent, but necessary, and processing the amendments collectively. Effective dates, early application and transitional provisions are dealt with on a standard by standard basis with the majority of the amendments effective for periods beginning on or after January 1, 2011, with early adoption permitted. The Company has adopted and reflected applicable amendments in these condensed consolidated interim financial statements.

3. Significant accounting policies (continued):

(q) New standards and interpretations not yet adopted:

The following new standards have been issued but are not yet applicable to the Company:

(i) IFRS 9 Financial Instruments:

Effective for annual periods beginning on or after January 1, 2013, with earlier adoption permitted.

As part of the project to replace IAS 39, *Financial Instruments: Recognition and Measurement*, this standard retains but simplifies the mixed measurement model and establishes two primary measurement categories for financial assets. More specifically, the standard:

- deals with classification and measurement of financial assets;
- establishes two primary measurement categories for financial assets: amortized cost and fair value;
- prescribes that classification depends on entity's business model and the contractual cash flow characteristics of the financial asset;
- eliminates the existing categories: held to maturity, available for sale, and loans and receivables.

Certain changes were also made regarding the fair value option for financial liabilities and accounting for certain derivatives linked to unquoted equity instruments.

The extent of the impact of adoption of this new standard has not yet been determined.

(ii) IFRS 10 Consolidated Financial Statements:

In May 2011, the IASB issued IFRS 10 Consolidated Financial Statements, which is effective for annual periods beginning on or after January 1, 2013, with early adoption permitted. If an entity applies this standard earlier, it shall also apply IFRS 11, IFRS 12, IAS 27 (2011) and IAS 28 (2011) at the same time.

IFRS 10 replaces the guidance in IAS 27 Consolidated and Separate Financial Statements and SIC-12 Consolidation - Special Purpose Entities. IAS 27 (2008) survives as IAS 27 (2011) Separate Financial Statements, only to carry forward the existing accounting requirements for separate financial statements.

IFRS 10 provides a single model to be applied in the control analysis for all investees, including entities that currently are SPEs in the scope of SIC-12. In addition, the consolidation procedures are carried forward substantially unmodified from IAS 27 (2008).

3. Significant accounting policies (continued):

(q) New standards and interpretations not yet adopted (continued):

(ii) IFRS 10 Consolidated Financial Statements (continued):

The Company intends to adopt IFRS 10 in its financial statements for the annual period beginning on January 1, 2013. The Company does not expect IFRS 10 to have a material impact on the financial statements.

(iii) IFRS 11 Joint Arrangements:

In May 2011, the IASB issued IFRS 11 Joint Arrangements, which is effective for annual periods beginning on or after January 1, 2013, with early adoption permitted. If an entity applies this standard earlier, it shall also apply IFRS 10, IFRS 12, IAS 27 (2011) and IAS 28 (2011) at the same time.

IFRS 11 replaces the guidance in IAS 31 Interests in Joint Ventures.

Under IFRS 11, joint arrangements are classified as either joint operations or joint ventures. IFRS 11 essentially carves out of previous jointly controlled entities, those arrangements which although structured through a separate vehicle, such separation is ineffective and the parties to the arrangement have rights to the assets and obligations for the liabilities and are accounted for as joint operations in a fashion consistent with jointly controlled assets/operations under IAS 31. In addition, under IFRS 11 joint ventures are stripped of the free choice of equity accounting or proportionate consolidation; these entities must now use the equity method.

The Company intends to adopt IFRS 11 in its financial statements for the annual period beginning on January 1, 2013. The extent of the impact of adoption of IFRS 11 has not yet been determined.

(iv) IFRS 12 Disclosure of Interests in Other Entities:

In May 2011, the IASB issued IFRS 12 Disclosure of Interests in Other Entities, which is effective for annual periods beginning on or after January 1, 2013, with early adoption permitted. If an entity applies this standard earlier, it does not need to apply IFRS 10, IFRS 11, IAS 27 (2011) and IAS 28 (2011) at the same time.

IFRS 12 contains the disclosure requirements for entities that have interests in subsidiaries, joint arrangements (i.e. joint operations or joint ventures), associates and/or unconsolidated structured entities.

The Company intends to adopt IFRS 12 in its financial statements for the annual period beginning on January 1, 2013. The Company does not expect the amendments to have a material impact on the financial statements, because of the nature of the Company’s interests in other entities.

3. Significant accounting policies (continued):

(q) New standards and interpretations not yet adopted (continued):

(v) IFRS 13 Fair Value Measurement:

In May 2011, the IASB published IFRS 13 Fair Value Measurement, which is effective prospectively for annual periods beginning on or after January 1, 2013. The disclosure requirements of IFRS 13 need not be applied in comparative information for periods before initial application.

IFRS 13 replaces the fair value measurement guidance contained in individual IFRS with a single source of fair value measurement guidance. It defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, i.e. an exit price. The standard also establishes a framework for measuring fair value and sets out disclosure requirements for fair value measurements to provide information that enables financial statement users to assess the methods and inputs used to develop fair value measurements and, for recurring fair value measurements that use significant unobservable inputs (Level 3), the effect of the measurements on profit or loss or other comprehensive income.

IFRS 13 explains 'how' to measure fair value when it is required or permitted by other IFRS. IFRS 13 does not introduce new requirements to measure assets or liabilities at fair value, nor does it eliminate the practicability exceptions to fair value measurements that currently exist in certain standards.

The Company intends to adopt IFRS 13 prospectively in its financial statements for the annual period beginning on January 1, 2013. The Company does not expect IFRS 13 to have a material impact on the financial statements.

(vi) Amendments to IAS 28 Investments in Associates and Joint Ventures:

In May 2011, the IASB issued Amendments to IAS 28 Investments in Associates and Joint Ventures, which is effective for annual periods beginning on or after January 1, 2013, with early adoption permitted. If an entity applies this standard earlier, it shall also apply IFRS 10, IFRS 11, IFRS 12 and IAS 27 (2011) at the same time.

IAS 28 (2011) carries forward the requirements of IAS 28 (2008) with several limited amendments.

The Company intends to adopt the amendments in its financial statements for the annual period beginning on January 1, 2013. The extent of the impact of adoption of the amendments has not yet been determined.

4. Gas properties:

Gas properties can be detailed as follows:

			2011
Properties	January 1, 2011	Acquisition	September 30, 2011
Magdalen Islands	$ 5,420	$ 1,752	$ 7,172
St-Jean	86,560	16,475	103,035
Dundee	338,257	3,217	341,474
Matapédia	181,099	6,705	187,804
Yamaska	18,868	(1,964)	16,904
Miguasha	79,584	(107)	79,477
St-Hyacinthe	2,437,500	–	2,437,500
New York	2,561,875	28,470	2,590,345
	$ 5,709,163	$ 54,548	$ 5,763,711

					2010
Properties	January 1, 2010	Acquisition	Disposition	Impairment	December 31, 2010
Magdalen Islands	$ 3,669	$ 1,751	$ –	$ –	$ 5,420
St-Jean	85,661	899	–	–	86,560
Dundee	327,446	10,811	–	–	338,257
Matapédia	167,074	14,025	–	–	181,099
Yamaska	22,726	–	(3,858)	–	18,868
Miguasha	80,002	–	(418)	–	79,584
Shell Saint-Simon	100,000	–	–	(100,000)	–
St-Hyacinthe	2,437,500	–	–	–	2,437,500
New York	2,450,448	111,427	–	–	2,561,875
	$ 5,674,526	$ 138,913	$ (4,276)	$ (100,000)	$ 5,709,163

In 2004, the Company acquired an interest in 15 permits for the oil and natural gas properties of St-Jean, Dundee, Matapédia and Yamaska in consideration of the issue of 3,757,408 common shares to Ditem Exploration Inc. In addition, the Company obtained 117,000 hectares of exploration permits in the Gaspé Peninsula adjacent to the existing Matapédia blocks.

4. Gas properties (continued):

In 2005, the Company acquired an interest of 10% in the Shell Saint-Simon property by issuing 1,000,000 common shares and by assuming 10% of the future development costs. In 2011, the operator has decided to abandon this well.

In 2006, the Company acquired an interest of 10% in the Haldimand 1 (Petrolia 3) exploratory well by issuing 1,000,000 common shares and by assuming 10% of the future development costs. The interest was sold in 2009.

In 2007, the Company granted Forest Oil Corporation the right to earn up to a 60% working interest in the Yamaska property, which covers 45,381 hectares, by spending up to $10,000,000 in exploration. In 2008, Forest Oil notified the Company of its election to exercise its financial commitments option on the Yamaska property. The Yamaska property was subject to a 7.5% convertible gross overriding royalty ("GORR") with another partner, which was converted into a 20% working interest.

In 2007, the Company acquired an interest of 35% in the permit of Joly property. The Company maintained an option to drill a second well before September 1, 2010.

In 2008, the Company signed an agreement with Covalent Energy (now Utica Energy) for an option to acquire a working interest up to 65% on exploration permits covering 29,000 hectares in consideration of the cost of an exploration program (New York property). In September 2009, Gastem signed a final Amendment to the agreement. The Company paid an amount of US$35,000, issued 3,500,000 common shares to Utica and completed an exploratory vertical well and acquired an 80% interest in 34,150 acres. Utica retains a 2% overriding royalty interest ("ORRI") in existing permits and in new permits within the area of mutual interest in New York State. Utica also retains a participation right to a 20% working interest in new land acquisitions within the area of mutual interest.

In 2008, the Company signed, together with its partner Canbriam Energy, a farm-in agreement for a total of 85% working interest in the two St-Hyacinthe (formerly Mundiregina) permits (92,104 acres) situated in the St-Lawrence Lowlands. According to the terms of the Agreement, Gastem may earn a 17% interest and Canbriam, 68%, with the sellers maintaining a 15% carried interest. Under the terms of the Agreement, Gastem paid to the seller an upfront consideration of $2.5M and committed to pay 20% of a 6-well and seismic program to be carried out.

In the fourth quarter of 2010, the cost of the St-Simon property, as well as the deferred exploration costs incurred on this property in the total amount of $102,285, were written-off following the decision by the operator to abandon the well.

4. Gas properties (continued):

In 2008, Gastem acquired the petroleum and gas exploration permits to the Magdalen Islands known to be prospective for gas and situated in the Magdalen Basin from the Québec Natural Resources Department. The Magdalen permit is located in the central part of the Gulf of St-Lawrence.

In January 2009, the Company acquired permits in the Appalachian area in order to carry out exploration and development programs.

5. Exploration and evaluation assets:

Exploration and evaluation assets by nature can be detailed as follows:

	September 30, 2011	December 31, 2010
Balance, beginning of period	$ 20,433,663	$ 11,819,555
Increase (decrease):		
Drilling	354,520	4,945,471
Seismic work	19,934	727,964
Geological work	91,837	99,573
Site preparation, evaluation and others	2,323,424	2,991,580
Less contribution received from a partner	(57,892)	(147,730)
Less impairment of exploration and evaluation assets	(738,252)	(2,750)
	1,993,571	8,614,108
Balance, end of period	$ 22,427,234	$ 20,433,663

Following an issue of public opinion related to a low level gas leak on a vertical well on the St-Hyacinthe property, the operator decided to abandon the well. As a result, related exploration and evaluation assets were impaired resulting in an impairment loss of $738,252. In addition, a provision for site restoration of $200,000 was recorded in this respect.

5. Exploration and evaluation assets (continued):

Exploration and evaluation assets by property can be detailed as follows:

					2011
	January 1, 2011	Exploration costs	Contributions received from partners	Impairment	September 30, 2011
Magdalen Islands	$ 406,022	$ 237,367	$ –	$ –	$ 643,389
St-Jean	289,641	8,230	–	–	297,871
Dundee	716,391	371,309	(24,749)	–	1,062,951
Matapédia	985,816	579,430	(13,014)	–	1,552,232
Yamaska	4,578,339	204,868	–	–	4,783,207
Miguasha	2,900	1,223	–	–	4,123
St-Hyacinthe	3,121,739	857,751	(18,401)	(738,252)	3,222,837
Joly	4,917,865	200,509	–	–	5,118,374
New York	5,414,950	329,028	(1,728)	–	5,742,250
	$20,433,663	$ 2,789,715	$ (57,892)	$ (738,252)	$ 22,427,234

					2010
	January 1, 2010	Exploration costs	Contributions received from partners	Impairment	December 31, 2010
Magdalen Islands	$ 216,556	$ 189,466	$ –	$ –	$ 406,022
St-Jean	258,149	72,878	(41,386)	–	289,641
Dundee	411,491	292,070	12,830	–	716,391
Matapédia	420,337	526,218	39,261	–	985,816
Yamaska	3,964,194	394,044	220,101	–	4,578,339
Miguasha	2,900	–	–	–	2,900
Shell Saint-Simon	2,285	–	–	(2,285)	–
St-Hyacinthe	1,007,084	2,165,471	(50,816)	–	3,121,739
Joly	2,168,429	2,749,436	–	–	4,917,865
New York	3,368,130	2,374,541	(327,721)	–	5,414,950
	$11,819,555	$ 8,764,124	$ (147,731)	$ (2,285)	$20,433,663

6. Share capital and warrants:

Authorized:

An unlimited number of common shares, without par value

	September 30, 2011	December 31, 2010	January 1, 2010
Issued:			
89,787,007 common shares (December 31, 2010 - 89,787,007, January 1, 2010 - 74,302,300)	$ 46,628,221	$ 46,628,221	$ 37,951,898

	Nine-months ended September 30, 2011	Year ended December 31, 2010
Issuance during the period:		
For cash:		
15,274,707 common shares and warrants pursuant to private placements (i) (ii)	$ –	$ 8,515,750
210,000 common shares pursuant to the exercise of employee share options (including the cost of the options of $88,873)	–	160,573
	$ –	$ 8,676,323

(i) In March 2010, 6,764,707 flow-through shares were issued. Each share was issued for $0.85, for a total financing of $5,750,000. Each unit sold consisted of one flow-through share and one warrant. Each warrant entitles the holder to purchase one common share at a price of $1.05 for an 18-month period.

(ii) In August 2010, 8,510,000 common shares were issued at a price of $0.325 per share, for a total financing of $2,765,750. Each unit sold consists of one common share and one warrant. Each warrant entitles the holder to purchase one common share at a price of $0.45 for a 24-month period.

6. Share capital and warrants (continued):

Share purchase warrants:

The Company has granted share purchase warrants and could be required to issue shares upon the exercise of such warrants as follows:

Number of warrants	Exercise price	Expiring date
8,510,000	0.45	August 17, 2012

7. Share-based payments:

Under the share option plan for the benefit of the directors and officers of the Company, 5,822,612 common shares are available; the life of the options cannot exceed ten years and the options vest immediately or over a period of one, two or three years.

The number of outstanding share options changed as follows:

	Nine-month period ended September 30, 2011	Average exercisable price	Year ended December 31, 2010	Average exercisable price
Balance, beginning of period	3,357,394	$ 0.50	4,733,000	$ 0.55
Issued	420,000	0.18	100,000	0.41
Exercised	–	–	(210,000)	0.34
Cancelled	(929,667)	0.58	(1,265,606)	0.59
Balance, end of period	2,847,727	$ 0.47	3,357,394	$ 0.55
Exercisable options, end of period	2,697,727	$ 0.47	3,279,771	$ 0.55

7. Share-based payments (continued):

As at September 30, 2011, the following options were outstanding:

Number of options	Exercise price	Expiring date
275,000	$ 0.26	December 19, 2011
355,000	0.35	December 22, 2011
335,000	0.65	August 31, 2012
711,355	0.60	December 14, 2012
25,000	0.62	January 28, 2013
25,000	2.18	July 28, 2013
25,000	0.58	January 28, 2014
25,000	0.37	July 28, 2014
85,000	0.37	July 31, 2014
526,372	0.58	October 29, 2014
50,000	0.53	February 6, 2015
250,000	0.20	January 27, 2016
60,000	0.21	February 4, 2016
50,000	0.12	July 27, 2016
50,000	0.28	August 31, 2020

During the nine-month period ended September 30, 2011, the Company granted 420,000 share options at a price from $0.12 to $0.28 per share (50,000 during the nine-month period ended September 30, 2010 at a price of $0.53 per share). The fair value of each option granted was determined using the Black-Scholes option pricing model. At the date of the grant, the weighted average fair value of share options granted was $0.17 per option (2010 - $0.44). The following assumptions were used in these calculations:

	Nine-month period ended September 30,	
	2011	2010
Risk-free interest rate	3%	2%
Expected life	5 years	5 years
Expected volatility	119%	138 to 144%
Expected dividend yield	0%	0%

8. Net finance income:

Net finance income is detailed as follows:

	Nine-months ended September 30, 2011	Nine-months ended September 30, 2010
Interest income	$ 45,972	$ 71,683
Finance income	45,972	71,683
Bank charges	(19,129)	(5,439)
Net foreign exchange loss	(8,209)	(8,692)
Part XII.6 of taxes	(60,086)	–
Loss on disposal capital assets	–	(1,380)
Finance expense	(87,424)	(15,511)
(Loss) Net finance income recognized in the loss of the period	$ (41,452)	$ 56,172

9. Income taxes:

Income tax expense (recovery) differs from the amounts computed by applying the combined federal and provincial income tax rate of 28.4% (2010 - 29.9%) as a result of the following:

	Nine-months ended September 30, 2011	Nine-months ended September 30, 2010
Loss before income taxes	$ (2,382,781)	$ (1,453,533)
Computed "expected" tax recovery	$ (676,710)	$ (434,606)
Increase in income taxes resulting from:		
Non-deductible share-based payments	12,365	10,279
Income tax at future rate	25,569	35,115
Current year losses not recognized	(44,677)	389,212
Deferred tax arising from flow-through shares	646,817	540,629
Permanent difference arising from flow-through shares	36,636	–
Total income tax	$ –	$ 540,629

9. Income taxes (continued):

The income tax effect of temporary differences that give rise to deferred tax assets and liabilities is as follows:

	January 1, 2010	Recognized in profit or loss	Recognized, directly equity	December 31, 2010	Recognized in profit or loss	Recognized, directly equity	September 30, 2011
Deferred tax assets:							
Operating losses	$ 92,000	$ 797,736	$ 382,622	$ 1,272,358	$ 548,227	$ –	$ 1,820,585
Share issuance costs	–	–	369,000	369,000	(100,000)	–	269,000
Equipment	2,000	8,000	–	10,000	–	–	10,000
Other eligible capital expenditures	–	104,000	–	104,000	–	–	104,000
Provision for site restoration	–	–	–	–	–	–	–
Deferred tax liabilities:							
Exploration and evaluation assets	(94,000)	(1,661,358)	–	(1,755,358)	(448,227)	–	(2,203,585)
Net deferred tax liabilities	$ –	$ (751,622)	$ 751,622	$ –	$ –	$ –	$ –

Deferred tax assets have not been recognized in respect of the following items:

	September 30, 2011	December 31, 2010	January 1, 2010
Operating losses	$ 485,937	$ 530,614	$ 982,000
Share issuance costs	–	–	301,000
Total	$ 485,937	$ 530,614	$ 1,283,000

9. Income taxes (continued):

As at September 30, 2011, the Company has tax losses of approximately $7,955,022 at the federal and provincial levels and approximately $707,338 of tax losses for foreign jurisdiction available to apply against future taxable income as follows:

Expiry date	USA	Canada
2027	$ 14,000	$ –
2028	296,000	1,469,000
2029	88,000	2,039,000
2030	185,000	2,726,000
2031	124,338	1,721,022
	$ 707,338	$ 7,955,022

The Company also has Canadian exploration expenditures and other costs of approximately $11,307,000 which may be deducted from future income, with no defined period.

10. Related party transactions:

The Company has no ultimate parent.

Key management personnel compensation comprised:

	Nine-months ended September 30,		Year ended December 31,
	2011	2010	2010
Short-term employee benefits	$ 77,363	$ 60,541	$ 271,821
Share-based payments	43,539	34,378	26,125

Other related party transactions:

During the year, the Company paid its share of the cost of the lease and other office costs to a company controlled by a director of the Company in the amount of $78,844 (2010 - $69,958). These transactions were recorded at the exchange amount.

11. Subsequent event:

In late October, the company applied for a drilling permit in Chenango County, New York State, for a conventional well in the Oneida formation situated on a property near the town of Sidney.

In late November, the company has applied to the Quebec government for drilling permits for two conventional wells, the first on Gastem's Cyr Property in the town of Ristigouche Sud-Est and the second, on a property near the town of St-Léon.

The Company has negotiated an earn-in agreement on certain permits in the Matapedia Valley belonging to Marzcorp, subject to various meetings to be held in late November.

12. Explanation of transition to IFRS:

The accounting policies set out in note 3 have been applied in preparing the financial statements for the nine-month period ended September 30, 2011, the comparative information presented in these financial statements for the year ended December 31, 2010 and the nine-month period ended September 30, 2010 and in the preparation of an opening IFRS statement of financial position at January 1, 2010 (the Group's date of transition).

In preparing its opening IFRS statement of financial position, the Group has adjusted amounts reported previously in financial statements prepared in accordance with previous Canadian GAAP. An explanation of how the transition from previous Canadian GAAP to IFRS has affected the Group's financial position, financial performance and cash flows is set out in the following tables and the notes that accompany the tables.

12. Explanation of transition to IFRS (continued):

Reconciliation of equity:

	January 1, 2010			September 30, 2010			December 31, 2010		
	Previous Canadian GAAP	Effect of transition to IFRS	IFRS	Previous Canadian GAAP	Effect of transition to IFRS	IFRS	Previous Canadian GAAP	Effect of transition to IFRS	IFRS
Assets									
Current assets:									
Cash and cash equivalents	$ 1,217,033	$ –	$ 1,217,033	$ 1,301,117	$ –	$ 1,301,117	$ 391,280	$ –	$ 391,280
Restricted cash	–	–	–	–	–	–	1,600,000	–	1,600,000
Short-term investments	–	–	–	–	–	–	–	–	–
Funds reserved for exploration	6,343,005	–	6,343,005	8,805,732	–	8,805,732	5,631,653	–	5,631,653
Accounts receivable	2,948,404	–	2,948,404	2,247,773	–	2,247,773	1,178,800	–	1,178,800
Prepaid expenses and deposit	113,396	–	113,396	1,291,984	–	1,291984	22,400	–	22,400
Total current assets	10,621,838	–	10,621,838	13,646,606	–	13,646,606	8,824,133	–	8,824,133
Non-current assets :									
Equipment	62,825	–	62,825	210,384	–	210,384	201,707	–	201,707
Gas properties	5,674,526	–	5,674,526	5,813,133	–	5,813,133	5,709,163	–	5,709,163
Exploration and evaluation assets	11,819,555	–	11,819,555	14,780,353	–	14,780,353	20,433,663	–	20,433,663
Long-term deposits	948,082	–	948,082	622,026	–	622,026	285,000	–	285,000
Total non-current assets	18,504,988	–	18,504,988	21,425,896	–	21,425,896	26,629,533	–	26,629,533
Total assets	$ 29,126,826	$ –	$ 29,126,826	$ 35,072,502	$ –	$ 35,072,502	$ 35,453,666	$ –	$ 35,453,666

12. Explanation of transition to IFRS (continued):

Reconciliation of equity (continued):

	January 1, 2010			September 30, 2010			December 31, 2010		
	Previous Canadian GAAP	Effect of transition to IFRS	IFRS	Previous Canadian GAAP	Effect of transition to IFRS	IFRS	Previous Canadian GAAP	Effect of transition to IFRS	IFRS
Liabilities									
Current liabilities:									
Accounts payable and accrued liabilities	$ 645,450	$ –	$ 645,450	$ 221,073	$ –	$ 221,073	$ 2,192,479	$ –	$ 2,192,479
Total current liabilities	645,450	–	645,450	221,073	–	221,073	2,192,479	–	2,192,479
Deferred income taxes	–	–	–	948,000	(948,000)	–	–	–	–
Total non-current liabilities	–	–	–	948,000	(948,000)	–	–	–	–
Equity									
Share capital and warrants	37,951,898	–	37,951,898	46,628,221	–	46,628,221	46,628,221	–	46,628,221
Contributed surplus	2,611,830	–	2,611,830	2,557,335	–	2,557,335	2,658,732	–	2,658,732
Deficit	(12,082,352)	–	(12,082,352)	(15,282,127)	948,000	(14,334,127)	(16,025,766)	–	(16,025,766)
Total equity attributable to the equity holders of the Company	28,481,376	–	28,481,376	33,903,429	948,000	34,851,429	33,261,187	–	33,261,187
Total liabilities and equity	$ 29,126,826	$ –	$ 29,126,826	$ 35,072,502	$ –	$ 35,072,502	$ 35,453,666	$ –	$ 35,453,666

12. Explanation of transition to IFRS (continued):

Reconciliation of comprehensive income for the period of three month ended September 30, 2010

	Previous Canadian GAAP	Effect of transition to IFRS	IFRS
Expenses:			
Salaries and benefits	$ 119,223	$ –	$ 119,223
Share-based payments	12,378	–	12,378
Office, trustees and report to equity holders	113,130	–	113,130
Professional fees	197,278	–	197,278
Travel and promotion	39,553	–	39,553
Rent	25,391	–	25,391
Depreciation of equipment	11,463	–	11,463
(Loss) profit before net finance income and income taxes	(518,416)	–	(518,416)
Net finance income:			
Finance income	22,763	–	22,763
Finance expense	(3,597)	–	(3,597)
Loss on disposal capital assets	(1,380)	–	(1,380)
	17,786	–	17,786
(Loss) profit before income taxes	(500,630)	–	(500,630)
Deferred income taxes	–	(430,765)	(430,765)
Net comprehensive (loss) profit for the period	$ (500,630)	$ –	$ (931,395)
Basic and diluted net loss per share	$ (0.006)	$ (0,006)	$ (0.012)

12. Explanation of transition to IFRS (continued):

Reconciliation of comprehensive income for the period of nine month ended September 30, 2010

	Previous Canadian GAAP	Effect of transition to IFRS	IFRS
Expenses:			
Salaries and benefits	$ 411,153	$ –	$ 411,153
Share-based payments	34,378	–	34,378
Office, trustees and report to equity holders	449,577	–	449,577
Professional fees	420,533	–	420,533
Travel and promotion	105,542	–	105,542
Rent	70,788	–	70,788
Depreciation of equipment	17,734	–	17,734
(Loss) profit before net finance income and income taxes	(1,509,705)	–	(1,509,705)
Net finance income:			
Finance income	71,683	–	71,683
Finance expense	(14,131)	–	(14,131)
Loss on disposal capital assets	(1,380)	–	(1,380)
	56,172	–	56,172
(Loss) profit before income taxes	(1,453,533)	–	(1,453,533)
Deferred income taxes	625,000	(1,165,629)	(540,629)
Net comprehensive (loss) profit for the period	$ (828,533)	$ (1,165,629)	$ (1,994,162)
Basic and diluted net loss per share	$ (0.011)	$ (0.014)	$ (0.025)

12. Explanation of transition to IFRS (continued):

Reconciliation of comprehensive income for the year ended December 31, 2010

	Previous Canadian GAAP	Effect of transition to IFRS	IFRS
Expenses:			
Salaries and benefits	$ 538,690	$ –	$ 538,690
Share-based payments	135,775	–	135,775
Office, trustees and report to equity holders	708,786	–	708,786
Professional fees	800,958	–	800,958
Travel and promotion	166,528	–	166,528
Rent	93,884	–	93,884
Depreciation of equipment	30,523	–	30,523
Fees related to subscription to the Oslo Stock Exchange	547,692	–	547,692
Loss on disposal of properties	2,620	–	2,620
Impairment of gas properties	102,750	–	102,750
(Loss) profit before net finance income and income taxes	(3,128,206)	–	(3,128,206)
Net finance income:			
Finance income	93,456	–	93,456
Finance expense	(95,217)	–	(95,217)
	(1,761)	–	(1,761)
(Loss) profit before income taxes	(3,129,967)	–	(3,129,967)
Deferred income taxes	1,487,451	(2,239,073)	(751,622)
Net comprehensive (loss) profit for the period	$ (1,642,516)	$ (2,239,073)	$ (3,881,589)
Basic and diluted net loss per share	$ (0.02)	$ (0.03)	$ (0.05)

Material adjustments to the statement of cash flows for 2010

Interest received and interest paid have been presented separately in the body of the *Statement of Cash Flows*, within operating activities. There are no other material differences between the statement of cash flows presented under IFRS and the statement of cash flows presented under previous Canadian GAAP.

12. Explanation of transition to IFRS (continued):

Notes to the reconciliations

(a) Income taxes:

Flow-through shares

Under Canadian GAAP, common shares issued pursuant to flow-through share financing were recorded at their issue price and related income taxes were recorded under the liability method of accounting. According to this method, the temporary differences were recorded on the date that the Company renounced the deductions to investors together with a corresponding charge in the deficit.

The accounting treatment under IFRS, described in note 3 of the financial statements, differs from Canadian GAAP in several areas:

- Under IFRS, at the time of share issuance, the Company allocates the proceeds between share capital and an obligation to deliver the tax deductions, which is recorded as a liability related to flow-through shares obligation. However, the Company estimated that no such liability existed as at January 1, 2010, September 30, 2010 and December 31, 2010.
- The renunciation related to 2009 financing was made in the first quarter of 2010 using the look-back method, and exploration expenditures were incurred in 2010. Also, renunciation related to 2010 financing was made in the first quarter of 2011 using the look-back method and part of the related exploration expenditures were incurred in 2010. As such, under IFRS, deferred tax liabilities were calculated as expenditures were incurred, rather than at the date of renunciation under Canadian GAAP, with the counterpart as deferred income tax expense rather than deficit under Canadian GAAP.

Backward tracing

Under IFRS, deferred taxes are recognized in profit or loss except to the extent that tax arises from business combinations and transactions recognized in equity. Therefore, when deferred taxes relate to equity items, a backward tracing is necessary under IFRS to determine the amount of tax (e.g. due to a change in tax rates or a change in recognized deferred tax assets) that should be recorded in equity, while under Canadian GAAP they are charged in profit or loss.

12. Explanation of transition to IFRS (continued):

Notes to the reconciliations (continued)

(a) Income taxes (continued):

Backward tracing (continued)

The above differences resulted in the following impacts:

Debit/ (Credit)	September 30, 2010 Canadian GAAP	IFRS adjustment	IFRS	December 31, 2010 Canadian GAAP	IFRS adjustment	IFRS
Deferred tax liabilities	$ (948,000)	$ 948,000	$ –	$ –	$ –	$ –
Deferred tax (recovery) expense	(625,000)	1,165,629	540,629	(1,487,451)	2,239,073	751,622
Deficit - deferred taxes arising from related flow-through shares	1,701,000	(1,701,000)	–	1,706,268	(1,706,268)	–
Deficit - deferred taxes arising from related share issuance costs	(128,000)	(412,629)	(540,629)	(218,817)	(532,805)	(751,622)

(b) Reclassification within the statement of comprehensive income:

Interest income, bank charges, net foreign exchange losses and the Part XII.6 of taxes were reclassified within the finance income and expense line items under IFRS while they were presented under revenue, financial expense and foreign exchange loss under Canadian GAAP.

(c) Classification of other financial instruments:

Contrary to Canadian GAAP, cash, cash equivalents, restricted cash and funds reserved for exploration do not meet the criteria for the fair value through profit and loss designation under IFRS.

As a result, cash and cash equivalents, restricted cash and funds reserved for exploration are classified as loans and receivables under IFRS. This change in classification does not have a financial impact on the consolidated financial statements as the fair value of those instruments approximates their cost.