



(A Development Stage Company)

**FINANCIAL STATEMENTS**

**DECEMBER 31, 2010**



## INDEPENDENT AUDITOR'S REPORT

To the Shareholders of  
**Rallyemont Energy Inc.**

We have audited the accompanying financial statements of Rallyemont Energy Inc., which comprise the balance sheet as at December 31, 2010 and 2009, and the statements of loss and deficit and cash flows for the periods then ended, and a summary of significant accounting policies and other explanatory information.

### *Management's Responsibility for the Financial Statements*

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Canadian generally accepted accounting principles, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

### *Auditor's Responsibility*

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the company's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the company's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### *Opinion*

In our opinion, the financial statements present fairly, in all material respects, the financial position of Rallyemont Energy Inc. as at December 31, 2010 and 2009, and the results of its operations and its cash flows for the periods then ended in accordance with Canadian generally accepted accounting principles.

SASKATOON, SASKATCHEWAN

March 16, 2011

Chartered Accountants

**RALLYEMONT ENERGY INC.**  
(A Development Stage Company)

**BALANCE SHEET**

**DECEMBER 31**

	<u>2010</u>	<u>2009</u>
<b><u>ASSETS</u></b>		
<b>Current assets</b>		
Cash and cash equivalents	\$ 11,993,413	\$ 1,142,948
GST receivable	83,445	15,008
Prepays	<u>6,121</u>	<u>106,897</u>
	<b>12,082,979</b>	<b>1,264,853</b>
Future income taxes (Note 3)	397,700	82,975
Property, plant and equipment (Note 4)	16,248	-
Petroleum and natural gas properties (Note 5)	<u>7,872,578</u>	<u>1,970,682</u>
	<b><u>\$ 20,369,505</u></b>	<b><u>\$ 3,318,510</u></b>
<b><u>LIABILITIES</u></b>		
<b>Current liability</b>		
Accounts payable and accrued liabilities	\$ 859,018	\$ 252,911
Asset retirement obligation (Note 6)	<u>26,514</u>	<u>-</u>
	<b><u>885,532</u></b>	<b><u>252,911</u></b>
<b><u>SHAREHOLDERS' EQUITY</u></b>		
Share capital (Note 7)	19,893,554	3,114,373
Contributed surplus (Note 7)	166,931	22,984
Deficit	<u>(576,512)</u>	<u>(71,758)</u>
	<b><u>19,483,973</u></b>	<b><u>3,065,599</u></b>
	<b><u>\$ 20,369,505</u></b>	<b><u>\$ 3,318,510</u></b>

Approved by the Board

"Stephen P. Halabura" Director

"Corey J. Giasson" Director

**RALLYEMONT ENERGY INC.**  
(A Development Stage Company)

**STATEMENT OF LOSS AND DEFICIT**

**PERIODS ENDED DECEMBER 31**

	(12 months) <u>2010</u>	(5 months) <u>2009</u>
<b>Income</b>		
Interest	<b><u>\$ 13,138</u></b>	<b><u>\$ 330</u></b>
<b>Expenses</b>		
Amortization	2,585	-
Consulting fees	395,915	36,516
Insurance	12,544	902
Office and other	64,250	13,653
Professional fees	74,901	26,775
Salaries and benefits	16,867	-
Stock based compensation	68,984	15,355
Travel	<u>40,583</u>	<u>16,011</u>
	<b><u>676,629</u></b>	<b><u>109,212</u></b>
<b>Loss before income taxes</b>	<b>(663,491)</b>	<b>(108,882)</b>
Future income tax recovery	<u>158,737</u>	<u>37,124</u>
<b>Net loss</b>	<b>(504,754)</b>	<b>(71,758)</b>
Deficit, beginning of period	<u>(71,758)</u>	<u>-</u>
<b>Deficit, end of period</b>	<b><u>\$ (576,512)</u></b>	<b><u>\$ (71,758)</u></b>
<b>Basic and diluted loss per share</b>	<b><u>\$ (0.02)</u></b>	<b><u>\$ (0.01)</u></b>
<b>Average weighted number of common shares</b>	<b><u>30,473,626</u></b>	<b><u>5,627,235</u></b>

**RALLYEMONT ENERGY INC.**  
(A Development Stage Company)

**STATEMENT OF CASH FLOWS**

**PERIODS ENDED DECEMBER 31**

	<u>(12 months)</u>	<u>(5 months)</u>
	<u>2010</u>	<u>2009</u>
<b>Cash flows from operating activities</b>		
Net loss	\$ (504,754)	\$ (71,758)
Items not affecting cash		
Amortization	2,585	-
Future income taxes (recovery)	(158,737)	(37,124)
Stock based compensation	68,984	15,355
Net change in non-cash working capital items:		
GST receivable	(68,437)	(15,008)
Prepays	(1,611)	(4,510)
Accounts payable and accrued liabilities	<u>10,613</u>	<u>73,388</u>
	<u>(651,357)</u>	<u>(39,657)</u>
<b>Cash flows from investing activities</b>		
Prepaid expenses	102,387	(102,387)
Accounts payable relating to properties	135,584	179,524
Purchases of property, plant and equipment	(18,833)	-
Petroleum and natural gas property expenditures	<u>(5,875,382)</u>	<u>(1,970,682)</u>
	<u>(5,656,244)</u>	<u>(1,893,545)</u>
<b>Cash flows from financing activities</b>		
Proceeds from issuance of shares	18,346,150	3,288,415
Share issue costs	(1,647,994)	(212,265)
Share issue costs payable	<u>459,910</u>	<u>-</u>
	<u>17,158,066</u>	<u>3,076,150</u>
<b>Net increase in cash during the period (Note 8)</b>	10,850,465	1,142,948
<b>Cash and cash equivalents, beginning of period</b>	<u>1,142,948</u>	<u>-</u>
<b>Cash and cash equivalents, end of period</b>	<b><u>\$ 11,993,413</u></b>	<b><u>\$ 1,142,948</u></b>

**RALLYEMONT ENERGY INC.**  
(A Development Stage Company)

**NOTES TO THE FINANCIAL STATEMENTS**

**DECEMBER 31, 2010**

**1. Nature of operations**

Rallyemont Energy Inc. (“Rallyemont” or the “Company”) was incorporated under the Business Corporations Act (Saskatchewan) on July 29, 2009. On March 4, 2010 the Company acquired all of the issued and outstanding shares of 101154728 Saskatchewan Ltd. in exchange for 4,323,280 shares (Note 8). The two companies amalgamated immediately thereafter.

The Company seeks to acquire heavy oil resource properties, delineate the resource and introduce enhanced oil recovery technologies to access petroleum reserves. The Company is in the development stage and its ability to continue as a going concern is dependent upon the discovery of economically recoverable reserves, the ability of the Company to obtain necessary financing to complete exploration and development, and future production or proceeds from the disposition thereof.

**2. Significant accounting policies**

These financial statements have been prepared in accordance with Canadian generally accepted accounting principles (“GAAP”) and reflect the following significant accounting policies:

**Cash and cash equivalents**

Cash and cash equivalents consist of cash on hand and short-term investments in guaranteed investment certificates.

**Property, plant and equipment**

Property, plant and equipment consist of leasehold improvements and are stated at cost less accumulated amortization. Amortization is calculated using the straight-line method over the term of the lease.

**Petroleum and natural gas properties**

**Capitalized costs**

The Company follows the full cost method of accounting for exploration development expenditure, wherein all costs related to the acquisition, exploration and development of petroleum and natural gas reserves are capitalized in a Canadian cost centre. Such costs include lease acquisition costs, geological and geophysical expenditures, lease rentals on non-productive properties, cost of drilling both productive and non-productive wells and related production equipment costs, and that portion of general and administrative expenses directly attributable to exploration and development activities. Proceeds from the disposition of petroleum and natural gas properties are applied to reduce the capitalized costs and no gain or loss is recognized on the disposal of petroleum and natural gas properties unless such disposition would alter the depletion and amortization rate by 20% or more.

**RALLYMONT ENERGY INC.**  
(A Development Stage Company)

**NOTES TO THE FINANCIAL STATEMENTS**

**DECEMBER 31, 2010**

**2. Significant accounting policies (continued)**  
**Petroleum and natural gas properties (continued)**

**Depletion/Depreciation**

Capitalized costs, together with estimated future capital costs associated with proved undeveloped reserves and amounts related to asset retirement obligations, will be depleted and depreciated using the unit-of-production method based on total estimated proven petroleum and natural gas reserves, before royalties, as determined by independent engineers. The relative volumes of petroleum and natural gas reserves and production are converted to equivalent units of oil based on relative energy content of six thousand cubic feet of natural gas to one barrel of oil. Costs of undeveloped and unproved properties are initially excluded from depletion calculations. 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 capitalized costs subject to depletion.

**Impairment**

Property costs are reviewed at least annually to consider whether there are conditions that may indicate impairment. The carrying values of petroleum and natural gas properties are compared to their net recoverable amount as estimated by quantifiable evidence of the market value of similar assets or geological resources. If the carrying value is found to exceed the estimated net recoverable amount, a write down will be recorded.

**Income taxes**

The Company uses the asset and liability method of accounting for income taxes. Under this method, future tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases (temporary differences), and losses carried forward. Future tax assets and liabilities are measured using substantively enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. A valuation allowance is recorded against any future tax asset if it is more likely than not that the asset will not be realized. The effect on future tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the date of substantive enactment.

**Non-monetary transactions**

Non-monetary transactions are measured at the more reliably measurable amount of either the fair value of the asset given up or fair value of the asset received.

**Revenue recognition**

Interest income is recognized when it is earned.

**Income per share**

Basic per share amounts are calculated using the weighted average number of shares outstanding during the period. Diluted per share amounts are calculated based on the treasury-stock method, which assumes that any proceeds received on exercise of warrants would be used to purchase common shares at the average market price during the period. The weighted average number of shares outstanding is then adjusted by the net change.

**RALLYEMONT ENERGY INC.**

(A Development Stage Company)

**NOTES TO THE FINANCIAL STATEMENTS**

**DECEMBER 31, 2010**

**2. Significant accounting policies (continued)**

**Stock-based compensation**

Options and warrants granted are accounted for using the fair value method. Under this method, the fair value of stock options and warrants granted are measured at estimated fair value at the grant date and recognized over the vesting period. Consideration received on the exercise of stock options is recorded as share capital and the related contributed surplus on options granted is transferred to share capital.

The Company uses the Black-Scholes option-pricing model to determine the fair value of these incentives.

**Measurement uncertainty**

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period.

Significant areas requiring the use of management estimates include fair value of related party transactions, stock-based compensation expenses, useful lives for amortization of capital assets, and contingencies reported in the notes to the financial statements. Financial results as determined by actual events could differ from those estimates.

By nature, estimates are subjective and do not necessarily result in precise determinations. Should underlying assumptions change, the estimated values could change by a material amount.

**Asset retirement obligations**

The Company recognizes the fair value of liabilities for asset retirement obligations in the period in which they occur and/or in which a reasonable estimate of such costs can be made. The asset retirement obligation is recorded as a liability with a corresponding increase to the carrying amount of the related long-lived asset. Subsequently, the asset retirement cost is allocated to expenses using a systematic and rational method and is also adjusted to reflect period to period changes in the liability resulting from passage of time and revisions to either timing or the amount of the original estimate of the undiscounted cash flow.

**Flow-through shares**

A portion of the Company's exploration activities is financed through proceeds received from the issue of flow-through shares. Under the terms of the flow-through issues, the tax attributes of the related expenditures are renounced to the subscribers. To recognize the foregone tax benefits to the Company, the carrying amount of the shares issued is reduced by the tax effect of the benefits renounced to subscribers. The tax effect of the renouncement is recorded when the renouncement documents are filed with the tax authorities.

**RALLYEMONT ENERGY INC.**  
(A Development Stage Company)

**NOTES TO THE FINANCIAL STATEMENTS**

**DECEMBER 31, 2010**

**2. Significant accounting policies (continued)**

**Financial instruments presentation and disclosure**

The Company has designated its cash and cash equivalents as held for trading, which are measured at fair value, and its accounts payable as other financial liabilities, which are measured at amortized cost.

**Future accounting pronouncements**

On January 1, 2011, the Company will adopt one of two new forms of GAAP. The first is International Financial Reporting Standards ("IFRS") which the Canadian Institute of Chartered Accountants ("CICA") will adopt as Canadian GAAP for publically accountable enterprises with non-publically accountable enterprises having the option to adopt as well. The second is Accounting Standards for Private Enterprises ("ASPE") which will be applicable for private enterprises in Canada.

The Company expects to adopt IFRS and is currently assessing the impact of the IFRS convergence on the Company's financial statements.

**3. Future income taxes**

Future income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Significant components of the Company's future assets and liabilities are as follows:

	<u>2010</u>	<u>2009</u>
Non-capital loss carry-forwards	\$ 317,027	\$ 37,126
Deferred share issue costs	399,133	45,849
Petroleum and natural gas properties	(318,735)	-
Property, plant and equipment	<u>275</u>	<u>-</u>
	<b><u>\$ 397,700</u></b>	<b><u>\$ 82,975</u></b>

At December 31, 2010, the Company had non-capital losses for tax purposes of \$1,174,174 (2009 - \$135,085), which may be carried forward to reduce income for tax purposes in future periods. The non-capital losses will begin to expire in 2029.

**RALLYEMONT ENERGY INC.**  
(A Development Stage Company)

**NOTES TO THE FINANCIAL STATEMENTS**

**DECEMBER 31, 2010**

**4. Property, plant and equipment**

		<u>2010</u>		<u>2009</u>
<u>Cost</u>	<u>Accumulated Amortization</u>	<u>Net Book Value</u>	<u>Net Book Value</u>	
Leasehold improvements	<b><u>\$ 18,833</u></b>	<b><u>\$ 2,585</u></b>	<b><u>\$ 16,248</u></b>	<b><u>\$ -</u></b>

**5. Petroleum and natural gas properties**

		<u>2010</u>		<u>2009</u>
<b>Balance, beginning of period</b>		\$ 1,970,682	\$	-
Land and mineral rights		1,895,673		1,953,910
Geological and exploration drilling		3,946,324		16,772
Facility development		33,385		-
Asset retirement obligation		<u>26,514</u>		<u>-</u>
<b>Balance, end of period</b>		<b><u>\$ 7,872,578</u></b>	<b><u>\$</u></b>	<b><u>1,970,682</u></b>

The Company has acquired a 100% interest in the mineral rights relating to approximately 50 sections of land in Saskatchewan for the purpose of exploration and development of heavy oil resources. All costs to date have been excluded from the depletion calculations because they relate to unproven properties.

The Company has provided a letter of credit in the amount of \$22,200 in favour of the Saskatchewan Ministry of Energy and Resources to secure future well abandonment costs.

**6. Asset retirement obligation**

Future asset retirement obligations are estimated based on the Company's net ownership interest in all wells and facilities, the estimated costs to reclaim and abandon the wells and facilities and the estimated timing of the costs to be incurred in future periods. Management of the Company has estimated the total undiscounted cash flows required to settle the obligations will be \$100,000. The obligations have been discounted using a credit adjusted risk free rate of 8% and an inflation rate of 2% per year. Most of these obligations are not expected to be paid until approximately 20 years in the future and will be funded from general Company funds at that time.

**RALLYEMONT ENERGY INC.**  
(A Development Stage Company)

**NOTES TO THE FINANCIAL STATEMENTS**

**DECEMBER 31, 2010**

**7. Share capital**

Authorized an unlimited number of  
Class A, Class B and Class C common shares without par value.

**Class A common shares issued**

	<u>Common Shares</u>	<u>Share Capital</u>
<b>Balance, July 29, 2009</b>	-	\$ -
Non flow-through private placement	12,154,389	2,177,510
Flow-through private placement	3,688,490	1,110,905
Share issue costs	-	<u>(174,042)</u>
<b>Balance, December 31, 2009</b>	<b><u>15,842,879</u></b>	<b><u>\$ 3,114,373</u></b>
Non flow-through private placement	16,069,080	7,718,422
Flow-through private placement	12,400,690	9,114,392
Issued to acquire 101154728 Saskatchewan Ltd.	4,323,820	1,513,337
Flow-through renunciation	-	(299,946)
Share issue costs	-	<u>(1,267,024)</u>
<b>Balance, December 31, 2010</b>	<b><u>48,636,469</u></b>	<b><u>\$ 19,893,554</u></b>

In September 2009, the Company completed an offering of Class A shares, issuing 6,210,100 shares at \$0.10 per share, for gross proceeds of \$621,010.

In October 2009, the Company completed an offering of Class A shares, issuing 2,375,000 shares at \$0.20 per share, for gross proceeds of \$475,000.

In December 2009, the Company completed a brokered offering of 3,601,333 Class A shares on a flow-through basis at \$0.30 per share, for gross proceeds of \$1,080,400. As part of the same offering, the Company issued 3,355,004 Units at \$0.30 per Unit, for gross proceeds of \$1,006,500. Each Unit was comprised of one Class A share and one-half of one warrant to purchase one Class A share at \$0.75 per share for a period of 24 months following issuance.

Also in December 2009, the Company completed an additional brokered offering of 44,300 Class A shares on a flow-through basis at \$0.35, for gross proceeds of \$15,505. As part of the same offering, the Company issued 214,285 Units at \$0.35 per Unit, for gross proceeds of \$75,000. Each Unit was comprised of one Class A share and one-half of one warrant to purchase one Class A share at \$0.75 for a period of 24 months following issuance.

**RALLYEMONT ENERGY INC.**  
(A Development Stage Company)

**NOTES TO THE FINANCIAL STATEMENTS**

**DECEMBER 31, 2010**

**7. Share capital (continued)**

Also in December 2009, the Company issued 42,857 Class A shares on a flow-through basis at \$0.35, for gross proceeds of \$15,000.

In February 2010, the Company completed an offering of Class A shares, issuing 8,357,812 shares at \$0.35 per share, for gross proceeds of \$2,925,234.

On March 4, 2010, the Company acquired all of the outstanding shares of 101154728 Saskatchewan Ltd. in exchange for 4,323,820 Class A shares. Immediately thereafter the two companies were amalgamated.

In May 2010, the Company issued 190,000 Class A shares at \$0.35, for gross proceeds of \$66,500.

In July 2010, the Company completed a brokered offering of 4,030,800 Class A shares on a flow-through basis at \$0.60 per share, and 2,691,000 Class A shares on a non-flow through basis at \$0.50 per share for gross proceeds of \$3,763,980.

In December 2010, the Company completed a brokered offering of 2,972,750 Class A shares on a flow-through basis at \$0.80 per share, and 2,406,838 Class A shares on a non-flow through basis at \$0.70 per share for gross proceeds of \$4,062,987.

Also in December 2010, the Company issued 5,397,140 Class A shares on a flow-through basis at \$0.80 per share, and 2,423,430 Class A shares on a non-flow through basis at \$0.70 per share for gross proceeds of \$6,014,113.

**Stock options**

Options granted are non-transferable, vest 25% upon grant and 25% per year for the next three years, and will expire the earlier of ten years after issuance, the 90th day after holder ceases to be a director, officer or consultant of the Company, or one year after death of the holder. The maximum number of shares issuable under the plan shall not exceed 10% of the total shares issued and outstanding from time to time.

During the year, the Company modified the term of stock options issued in 2009 from 5 years to 10 years to agree with the terms of the new issuances. In accordance with CICA 3870, modifications to the terms of an award are treated as an exchange of the original award for a new award.

**RALLYEMONT ENERGY INC.**  
(A Development Stage Company)

**NOTES TO THE FINANCIAL STATEMENTS**

**DECEMBER 31, 2010**

**7. Share capital (continued)**

**Stock options (continued)**

A summary of the status of the Company's stock option plan and changes during the period ended December 31, 2010 is presented below.

For options outstanding at December 31, 2010, weighted average exercise prices are as follows:

<u>Expiry Date</u>	<u>Exercise Price</u>	<u>Balance December 31, 2009</u>	<u>Issued</u>	<u>Exercised and Expired</u>	<u>Balance December 31, 2010</u>
October 7, 2019	\$ 0.10	574,425	-	-	574,425
November 13, 2019	0.20	205,812	-	-	205,812
December 14, 2019	0.30	657,344	-	-	657,344
April 12, 2020	0.35	-	950,000	-	950,000
May 1, 2020	0.35	-	300,000	-	300,000
June 14, 2020	0.50	-	50,000	-	50,000
July 15, 2020	0.50	-	680,000	-	680,000
October 1, 2020	0.50	-	40,000	-	40,000
		<b><u>1,437,581</u></b>	<b><u>2,020,000</u></b>	<b><u>-</u></b>	<b><u>3,457,581</u></b>

  

<u>Options Price Per Share</u>	<u>Number Outstanding</u>	<u>Weighted Average Remaining Life</u>
\$ 0.10	574,425	8.77
0.20	205,812	8.87
0.30	657,344	8.96
0.35	1,250,000	9.29
0.50	770,000	9.54
	<b><u>3,457,581</u></b>	<b><u>9.17</u></b>

The fair value of stock options issued in 2010 was estimated using the Black-Scholes option-pricing model, with the following assumptions: risk free rate of 2.79% - 3.66%, volatility of nil, dividend yield of nil and expected term of ten years. During 2010, the Company granted a total of 2,020,000 stock options. All options have a term of ten years and strike prices ranging from \$0.35 - \$0.50. The value of the options that vested during the period, using the Black-Scholes option-pricing model, was \$68,984, which was allocated to stock-based compensation expense with a corresponding increase in contributed surplus.

**RALLYEMONT ENERGY INC.**  
(A Development Stage Company)

**NOTES TO THE FINANCIAL STATEMENTS**

**DECEMBER 31, 2010**

**7. Share capital (continued)**

**Share purchase warrants and broker warrants**

On certain issues of common shares, the Company grants broker warrants as partial consideration to the agent for services associated with the share issuance. Each broker warrant entitles the agent to acquire one common share of the Company at a price of \$0.30 - \$0.70 a share for a period of two to three years from closing. The broker warrants issued in 2010 were determined to have a fair value of \$74,963. The fair value of the warrants was determined using the Black-Scholes option-pricing model with the following assumptions: volatility of nil, risk free rate of return of 3.16% - 3.36% expected dividend of nil and expected term of two to three years.

A continuity schedule for share purchase warrants and broker warrants for the period ended December 31, 2010 is as follows:

<u>Expiry Date</u>	<u>Exercise Price</u>	<u>Balance December 31, 2009</u>	<u>Issued</u>	<u>Exercised and Expired</u>	<u>Balance December 31, 2010</u>
December 2011	\$ 0.75	1,784,647	-	-	1,784,647
December 2012	0.30	356,507	-	-	356,507
December 2012	0.35	20,686	-	-	20,686
February 2013	0.35	-	507,482	-	507,482
June 2013	0.50	-	394,131	-	394,131
July 2013	0.50	-	61,760	-	61,760
December 2014	0.70	-	878,080	-	878,080
		<u><b>2,161,840</b></u>	<u><b>1,841,453</b></u>	<u><b>-</b></u>	<u><b>4,003,293</b></u>

**Performance warrants**

During 2009, the Company approved the grant of 1,555,212 performance warrants to certain officers and consultants of the Company. One-third of these warrants are exercisable at \$0.10 and vested immediately. One-third of these warrants are exercisable at \$0.30 and vested on January 2, 2010. One-third of these warrants are exercisable at \$0.50 and will vest on January 2, 2011.

The performance warrants issued in 2009 were determined to have a fair value of \$6,376. The fair value of the warrants was determined using the Black-Scholes option-pricing model with the following assumptions: volatility of nil, risk free rate of return of 2.63% expected dividend of nil, and expected term of five years.

**RALLYEMONT ENERGY INC.**  
(A Development Stage Company)

**NOTES TO THE FINANCIAL STATEMENTS**

**DECEMBER 31, 2010**

**7. Share capital (continued)**

**Contributed surplus**

The fair values of stock options and warrants have been valued using the Black-Scholes option-pricing model. Upon grant, the fair value of these securities is added to contributed surplus. Upon exercise, the corresponding amount of contributed surplus related to the security is removed from contributed surplus and added to share capital. A summary of the contributed surplus activity is as follows:

	2010	2009
<b>Balance, beginning of period</b>	\$ 22,984	\$ -
Fair value of options granted	68,984	8,979
Fair value of performance warrants granted	-	6,376
Fair value of broker warrants granted	74,963	7,629
<b>Balance, end of period</b>	<b><u>\$ 166,931</u></b>	<b><u>\$ 22,984</u></b>

**8. Amalgamation of 101154728 Saskatchewan Ltd.**

On March 4, 2010 the Company acquired all of the issued and outstanding shares of 101154728 Saskatchewan Ltd. ("101154728") pursuant to an amalgamation.

The purchase price paid by Rallyemont for all of 101154728's shares, pursuant to the amalgamation, was \$1,513,337, which was satisfied by the issuance of 4,323,820 shares.

The following table summarizes the fair value of the assets acquired and liabilities assumed at the date of amalgamation.

**Net assets acquired**

Cash and accounts receivable	\$ 1,516,388	
Other assets		11,947
		<b>1,528,335</b>
Liabilities		14,998
		<b><u>\$ 1,513,337</u></b>
 <b><u>Consideration</u></b>		
Common shares		<b><u>\$ 1,513,337</u></b>

**RALLYEMONT ENERGY INC.**  
(A Development Stage Company)

**NOTES TO THE FINANCIAL STATEMENTS**

**DECEMBER 31, 2010**

**9. Related party transactions**

In 2009 the Company had accrued or paid \$225,174 in petroleum and natural gas property costs to North Rim Exploration Ltd., an entity which was influenced by a member of the Company's Board of Directors.

The Company has accrued or paid \$395,915 (2009 - \$36,516) in consulting fees to entities controlled by officers of the Company.

These transactions are in the normal course of operations and are measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties.

**10. Capital disclosure**

The Company's objectives when managing capital are to safeguard the Company's ability to continue as a going concern, so that it can provide returns for shareholders and benefits for other stakeholders. The Company considers the items included in shareholder's equity as capital. The Company manages the capital structure and makes adjustments to it in response to changes in economic conditions and the risk characteristics of the underlying assets. In order to maintain or adjust the capital structure, the Company may issue new shares, or acquire or dispose of assets.

In order to facilitate the management of its capital requirements, the Company will prepare annual expenditure budgets that are updated as necessary. The annual budgets will be approved by the Board of Directors.

In order to maximize ongoing exploration efforts, the Company does not pay out dividends. The Company's investment policy is to invest its cash in highly-rated, liquid short-term interest-bearing investments, with an initial term to maturity of 12 months or less.

The Company is not subject to externally-imposed capital requirements, except as disclosed.

**11. Financial instruments**

**Fair value of financial instruments**

The carrying amounts of cash, accounts receivable, accounts payable and accrued liabilities approximate their fair values due to the short-term maturity of those instruments.

**Commodity price risk**

Price risk is the risk that the value of petroleum and natural gas properties will fluctuate due to changes in market prices of the underlying commodities. A change in the price may have a direct effect on the value of the underlying petroleum and natural gas properties.