PetroFrontier

# CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS AS AT AND FOR THE THREE AND SIX MONTHS ENDED JUNE 30, 2013

## *PetroFrontier Corp.*

## CONSOLIDATED STATEMENT OF FINANCIAL POSITION

*(Unaudited)*

*(Canadian Dollars)*

| *As at* | **June 30, 2013** | **December 31, 2012** |
|---|---|---|
| **ASSETS** | | |
| **Current** | | |
| Cash and cash equivalents (note 4) | 8,255,844 | 3,944,537 |
| Restricted cash (note 5) | 626,355 | 7,688,228 |
| Marketable securities | 1,172 | 3,777 |
| Accounts receivable (note 6) | 1,479,671 | 3,720,394 |
| Prepaid expenses and deposits (note 7) | 768,666 | 722,311 |
| | 11,131,708 | 16,079,247 |
| Corporate assets | 38,256 | 47,913 |
| Exploration and evaluation assets (note 10) | 46,004,875 | 112,614,425 |
| Goodwill (note 9) | - | 8,917,774 |
| | **57,174,839** | **137,659,359** |
| **LIABILITIES** | | |
| **Current** | | |
| Accounts payable and accrued liabilities | 1,508,856 | 3,787,574 |
| Decommissioning liabilities | 1,638,707 | 1,742,709 |
| Deferred tax liability | - | 16,210,131 |
| | 3,147,563 | 21,740,414 |
| **SHAREHOLDERS' EQUITY** | | |
| Share capital (note 11) | 125,916,046 | 125,916,046 |
| Warrants (note 11) | 1,220,886 | 1,220,886 |
| Contributed surplus | 9,240,479 | 9,027,112 |
| Accumulated other comprehensive income | (5,352,701) | 581,633 |
| Deficit | (76,997,434) | (20,826,732) |
| | 54,027,276 | 115,918,945 |
| | **57,174,839** | **137,659,359** |

See accompanying notes to the condensed consolidated financial statements

Commitments and contingencies (note 16)
Subsequent events (note 18)

## *PetroFrontier Corp.*

## CONSOLIDATED STATEMENT OF LOSS AND COMPREHENSIVE LOSS

*(Unaudited)*

*(Canadian Dollars)*

| | Three months ended June 30 | | Six months ended June 30 | |
|---|---|---|---|---|
| | **2013** | 2012 | **2013** | 2012 |
| **EXPENSES** | | | | |
| General and administrative | **970,875** | 1,852,541 | **2,223,175** | 2,830,731 |
| Loss on marketable securities | **3,995** | 12,494 | **2,605** | 29,003 |
| Foreign exchange loss | **3,388** | 277,700 | **16,892** | 155,231 |
| Financial instruments (note 14) | **-** | (132,553) | **-** | (150,631) |
| Share-based compensation (note 11) | **82,483** | 105,827 | **213,367** | 980,655 |
| Depreciation | **13,235** | 13,351 | **27,686** | 26,025 |
| Impairment (note 8) | **68,837,915** | - | **68,837,915** | - |
| **Results from operating activities** | **69,911,891** | 2,129,360 | **71,321,640** | 3,871,014 |
| Finance income | **47,606** | 94,589 | **87,059** | 187,077 |
| Finance costs | **(13,680)** | (15,871) | **(26,901)** | (23,001) |
| **Net finance income** | **33,926** | 78,718 | **60,158** | 164,076 |
| **NET LOSS BEFORE TAXES** | **(69,877,965)** | (2,050,642) | **(71,261,482)** | (3,706,938) |
| Deferred tax recovery | **15,090,780** | - | **15,090,780** | - |
| **NET LOSS** | **(54,787,185)** | (2,050,642) | **(56,170,702)** | (3,706,938) |
| **OTHER COMPREHENSIVE EARNINGS** | | | | |
| *Items that may be reclassified subsequently to net income (loss):* | | | | |
| Foreign exchange gain/(loss) on foreign operations | **(9,094,788)** | 946,386 | **(5,934,334)** | 612,112 |
| **COMPREHENSIVE LOSS** | **(63,881,973)** | (1,104,256) | **(62,105,036)** | (3,094,826) |
| **Net loss per share** | | | | |
| **Basic and diluted** (note 11) | **(0.69)** | (0.03) | **(0.71)** | (0.06) |

*See accompanying notes to the condensed consolidated financial statements*

# *PetroFrontier Corp.*

## CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

*(Unaudited)*

*(Canadian Dollars)*

| | Share Capital | Warrants | Contributed Surplus | Accumulated Other Comprehensive Income | Deficit | Total Equity |
|---|---|---|---|---|---|---|
| **Balance at January 1, 2013** | **125,916,046** | **1,220,886** | **9,027,112** | **581,633** | **(20,826,732)** | **115,918,945** |
| Net loss | | | | | (56,170,702) | (56,170,702) |
| Foreign exchange loss on translation of foreign operations | | | | (5,934,334) | | (5,934,334) |
| Share-based compensation | | | 213,367 | | | 213,367 |
| **Balance at June 30, 2013** | 125,916,046 | 1,220,886 | **9,240,479** | **(5,352,701)** | **(76,997,434)** | **54,027,276** |
| | | | | | | |
| Balance at January 1, 2012 | 117,189,874 | 1,073,250 | 6,528,103 | 743,128 | (14,150,245) | 111,384,110 |
| Net loss | | | | | (3,706,938) | (3,706,938) |
| Foreign exchange gain on translation of foreign operations | | | | 612,112 | | 612,112 |
| Issued on exercise of stock options | 27,360 | | (9,360) | | | 18,000 |
| Expiry of warrants | | (1,073,250) | 1,073,250 | | | - |
| Share-based compensation | | | 980,655 | | | 980,655 |
| Balance at June 30, 2012 | 117,217,234 | - | 8,572,648 | 1,355,240 | (17,857,183) | 109,287,939 |

*See accompanying notes to the condensed consolidated financial statements*

## *PetroFrontier Corp.*

## CONSOLIDATED STATEMENT OF CASH FLOWS

*(Unaudited)*

*(Canadian dollars)*

| | Three months ended June 30 | | Six months ended June 30 | |
|---|---|---|---|---|
| | **2013** | 2012 | **2013** | 2012 |
| **Cash provided by (used in)** | | | | |
| **OPERATING** | | | | |
| Net loss from continuing operations | **(54,787,185)** | (2,050,642) | **(56,170,702)** | (3,706,938) |
| Unrealized loss on marketable securities | **3,995** | 12,494 | **2,605** | 29,003 |
| Financial instruments | **-** | (95,675) | **-** | (55,478) |
| Depreciation | **13,235** | 13,351 | **27,686** | 26,025 |
| Share-based compensation | **82,483** | 105,827 | **213,367** | 980,655 |
| Net finance income | **(33,926)** | (78,718) | **(60,158)** | (164,076) |
| Deferred tax recovery | **(15,090,780)** | - | **(15,090,780)** | - |
| Impairment | **68,837,915** | - | **68,837,915** | - |
| | **(974,263)** | (2,093,363) | **(2,240,067)** | (2,890,809) |
| Change in non-cash working capital (Note 12) | **1,307,016** | 3,483,858 | **118,710** | (3,501,143) |
| Cash flow from (used in) operating activities | **332,753** | 1,390,495 | **(2,121,357)** | (6,391,952) |
| **FINANCING** | | | | |
| Issuance of common shares from exercise of stock options | **-** | 18,000 | **-** | 18,000 |
| Finance costs | **(3,666)** | (7,407) | **(5,840)** | (8,467) |
| Cash flow from (used in) financing activities | **(3,666)** | 10,593 | **(5,840)** | 9,533 |
| **INVESTING** | | | | |
| Exploration and evaluation expenditures | **(40,947)** | (5,328,924) | **(76,076)** | (6,137,854) |
| Corporate asset expenditures | **(3,516)** | (8,966) | **(18,029)** | (13,602) |
| Term deposits | **-** | - | **-** | 2,500,000 |
| Restricted cash | **682,674** | - | **7,061,873** | - |
| Interest received | **47,606** | 94,589 | **87,059** | 187,077 |
| Cash flow from (used in) investing activities | **685,817** | (5,243,301) | **7,054,827** | (3,464,379) |
| Effect of exchange rate changes on cash and cash equivalents held in foreign currency | **(774,455)** | 115,696 | **(616,323)** | 214,026 |
| Increase/(decrease) in cash and cash equivalents | **240,449** | (3,726,517) | **4,311,307** | (9,632,772) |
| Cash and cash equivalents, beginning of the period | **8,015,395** | 18,452,304 | **3,944,537** | 24,358,559 |
| **Cash and cash equivalents and term deposits, end of the period** | **8,255,844** | 14,725,787 | **8,255,844** | 14,725,787 |

*See accompanying notes to the condensed consolidated financial statements*

### 1. REPORTING ENTITY

PetroFrontier Corp. (the "Corporation") was incorporated in Alberta, Canada on February 6, 2009 under the name Australia Energy Corp. On December 31, 2010, the Corporation amalgamated with Pendulum Capital Corporation and filed articles of amalgamation to change its name to PetroFrontier Corp. The Corporation's registered office is 320, 715 – 5th Avenue S.W. Calgary, Alberta, Canada T2P 2X6. The Corporation is engaged in the business of international petroleum exploration in Northern Territory, Australia, through its two wholly owned subsidiaries, PetroFrontier (Australia) Pty Ltd ("PetroFrontier Australia") and Texalta (Australia) Pty Ltd ("Texalta Australia"). These condensed consolidated interim financial statements of the Corporation as at and for the three and six months ended June 30, 2013 comprises the Corporation, PetroFrontier Australia and Texalta Australia and unless otherwise indicated the term "Corporation" refers to both the Corporation and its wholly owned subsidiaries.

### 2. EXPLORATION STAGE CORPORATION

The Corporation is engaged primarily in the pursuit of petroleum and natural gas through exploration in the Northern Territory, Australia. Since inception, the efforts of the Corporation have been devoted to the pursuit of petroleum exploration licenses, land access agreements with aboriginal stakeholders, and initial stage seismic acquisition. To date, the Corporation has not earned revenue from these operations and is considered to be in the exploration stage. The recoverability of the costs incurred to date is uncertain and dependent upon achieving commercial production or sale, the ability of the Corporation to obtain sufficient financing to fulfill its obligations under the petroleum exploration licenses and upon future profitable operations.

On June 10, 2013, the Corporation entered into an agreement to amend the existing farm-in agreement with Statoil Australia Oil & Gas AS ("Statoil") (the "Amended Farm-in Agreement"). Pursuant to the Amended Farm-in Agreement and subsequent to quarter end, Statoil was transferred 80% of the Corporation's working interests in EP 103, EP 104, EP 127 and EP 128 and in EPA 213 and EPA 252 in exchange for exploration program related payments and carried costs of up to US$175.0 million over three phases to the end of 2016.

These condensed consolidated financial statements have been prepared by management in accordance with accounting principles applicable to a going concern, which assumes that the Corporation will continue in operation for the foreseeable future and will be able to realize its assets and discharge its liabilities in the normal course of operations. At June 30, 2013, the Corporation had working capital of $9,622,852, a deficit of $76,997,434 and a net loss from continuing operations for the three and six months ended June 30, 2013 of $54,787,185 and $56,170,702, respectively. The Corporation's petroleum licenses are in the exploration stage.

In September 2012, the Corporation closed a series of private placement offerings for gross proceeds of $10,000,000 through the issuance of 15,384,615 units (the "Units") at a price of $0.65 per Unit. Each Unit consists of one common share ("Share") and one common share purchase warrant ("Warrant"). Each Warrant entitles the holder thereof to acquire one additional Share at a price of $0.90 per Share. The Warrants will expire on September 8, 2014 (the "Warrant Expiry Date"), unless the volume weighted average trading price of the Shares on the TSX Venture Exchange Inc. during the 10 consecutive trading days immediately prior to the date for which such calculation is made is greater than $1.125 (the "Trigger Event"). If a Trigger Event occurs, the Warrant Expiry Date may, at the option of the Corporation, be accelerated to the later of: (i) 30 business days from the Trigger Event date; and (ii) one month following the expiry of the applicable hold period required under securities laws.

## 3. BASIS OF PRESENTATION, SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND CHANGES IN ACCOUNTING POLICIES

The Corporation prepares its financial statements in accordance with Canadian generally accepted accounting principles ("GAAP") as set out in section I of the Handbook of the Canadian Institute of Chartered Accountants ("CICA Handbook"); which requires publicly accountable enterprises to prepare their financial statements using International Financial Reporting Standards ("IFRS").

These condensed consolidated interim financial statements have been prepared in accordance with IFRS applicable to the preparation of interim financial statements, IAS 34 – *Interim financial reporting ("IAS 34").*

The policies applied in these condensed consolidated interim financial statements are based on IFRS issued and outstanding as of August 28, 2013, the date the condensed consolidated interim financial statements were approved by the Corporation's Audit Committee for issuance.

These condensed consolidated interim financial statements should be read in conjunction with the Corporation's 2012 annual consolidated financial statements.

As indicated in note 1 above, these condensed consolidated interim financial statements of the Corporation as at and for the three and six months ended June 30, 2013 comprise the Corporation, PetroFrontier Australia and Texalta Australia.

These condensed consolidated interim financial statements have been prepared on the historical cost basis except that the financial instruments held for trading are measured at fair value through profit or loss.

These condensed consolidated interim financial statements are presented in Canadian dollars, which is the Corporation's functional currency. The functional currency of PetroFrontier Australia and Texalta Australia is the Australian dollar.

On January 1, 2013, the Corporation adopted new standards with respect to consolidations (IFRS 10), joint arrangements (IFRS 11), disclosure of interests in other entities (IFRS 12), fair value measurements (IFRS 13) and amendments to financial instrument disclosures (IFRS 7). The adoption of these standards had no impact on the amounts recorded in the financial statements as at January 1, 2013 or on the comparative periods.

The Corporation has adopted the amendments to IAS 1, Presentation of Financial Statements which require the Corporation to group other comprehensive income items by those that will be reclassified subsequently to profit or loss and those that will not be reclassified. These changes did not result in any adjustments to other comprehensive income or comprehensive income.

**NOTES** *(continued)*

## 4. CASH AND CASH EQUIVALENTS

| | June 30, 2013 ($) | December 31, 2012 ($) |
|---|---|---|
| Cash at bank and on hand | 8,255,844 | 3,944,537 |
| Cash and cash equivalents | **8,255,844** | **3,944,537** |

## 5. RESTRICTED CASH

| | June 30, 2013 ($) | December 31, 2012 ($) |
|---|---|---|
| Operating and trust accounts (i) | 409,660 | 7,454,895 |
| Other (ii) | 216,695 | 233,333 |
| Restricted cash | **626,355** | **7,688,228** |

(i) The Corporation has established various operating and trust accounts to effectively manage and ensure the timely payment of capital expenditures for the joint ventures it operates. The amounts deposited into these various accounts are considered restricted to the operations of the joint ventures.

(ii) The Corporation had three term deposits outstanding as at June 30, 2013 that mature on August 31, 2013.

## 6. ACCOUNTS RECEIVABLE

| | June 30, 2013 | December 31, 2012 |
|---|---|---|
| Trade receivables | 358,046 | 1,814,930 |
| Joint venture receivables | 1,121,625 | 1,905,464 |
| Allowance for doubtful accounts | - | - |
| Accounts receivable | **1,479,671** | **3,720,394** |

**NOTES** *(continued)*

## 7. PREPAID EXPENSES AND DEPOSITS

| | June 30, 2013 ($) | December 31, 2012 ($) |
|---|---|---|
| Environmental and abandonment deposits | 655,569 | 631,687 |
| Rent, insurance and other | 113,097 | 90,624 |
| Prepaid expenses and deposits | **768,666** | **722,311** |

As at June 30, 2013, the Corporation had $682,600 (Australian dollars) on deposit with the Northern Territory government pertaining to various environmental and abandonment deposits.

## 8. IMPAIRMENT

| | Three and six months ended June 30, 2013 | Three and six months ended June 30, 2012 |
|---|---|---|
| Impairment of goodwill | 9,149,570 | - |
| Impairment of exploration and evaluation assets | 59,688,345 | - |
| | **68,837,915** | **-** |

The Corporation's goodwill at June 30, 2013 has been assessed for impairment. All of the Corporation's goodwill has been impaired. The execution of the Amended Farm-in Agreement with Statoil indicated that the aggregated carrying value of the goodwill exceeded the fair value less costs to sell. Accordingly, impairment of $9,149,570 was recorded for the three and six month ended June 30, 2013 (three and six months ended June 30, 2012 - nil). See note 9 for discussion regarding the Corporation's goodwill.

The Corporation's exploration and evaluation assets at June 30, 2013 have been assessed for impairment. The execution of the Amended Farm-in Agreement with Statoil indicated that the aggregated carrying value of the Corporation's exploration and evaluation assets exceeded the fair value less costs to sell. Accordingly, impairment of $59,688,345 was recorded for the three and six month ended June 30, 2013 (three and six months ended June 30, 2012 - nil). See note 10 for discussion regarding the Corporation's exploration and evaluation assets.

**NOTES** *(continued)*

## 9. GOODWILL

| | June 30, 2013 | December 31, 2012 |
|---|---|---|
| | **($)** | **($)** |
| **Cost:** | | |
| Balance, January 1 | 8,917,774 | 8,946,231 |
| Additions | - | - |
| Dispositions | - | - |
| Foreign currency translation | 231,796 | (28,457) |
| **Balance, period end** | **9,149,570** | **8,917,774** |
| | | |
| **Accumulated impairment losses:** | | |
| At January 1 | - | - |
| Impairment losses recognized in the year | (9,149,570) | - |
| **Balance, period end** | **(9,149,570)** | **-** |
| | | |
| **Net book value, period end** | **-** | **8,917,774** |

Goodwill was assessed for impairment as at June 30, 2013. The execution of the Amended Farm-in Agreement indicated that the aggregated carrying value of the goodwill exceeded the fair value less costs to sell. Accordingly, impairment of $9,149,570 was recorded.

## 10. EXPLORATION AND EVALUATION ASSETS

| | Exploration & Evaluation Assets ($) |
|---|---|
| **Cost:** | |
| At December 31, 2012 | 112,614,425 |
| Cumulative translation adjustments and additions | (6,921,505) |
| **At June 30, 2013** | **105,693,220** |
| | |
| **Accumulated impairment:** | |
| At December 31, 2012 | - |
| Impairment | (59,688,345) |
| **At June 30, 2013** | **(59,688,345)** |
| | |
| **Net Book Value:** | |
| At December 31, 2012 | 112,614,425 |
| **At June 30, 2013** | **46,004,875** |

The execution of the Amended Farm-in Agreement with Statoil indicated that the aggregated carrying value of the Corporation’s exploration and evaluation assets exceeded the fair value less costs to sell. Accordingly, impairment of $59,688,345 was recorded.

**NOTES** *(continued)*

## 11. SHARE CAPITAL

### A) Authorized

Unlimited number of common voting shares, no par value.
Unlimited number of preferred shares, no par value, issuable in series.

### B) Issued – common shares of PetroFrontier

| | Six Months Ended June 30, 2013 | | Year Ended December 31, 2012 | |
|---|---|---|---|---|
| | **Number of shares** | **Amount ($)** | **Number of shares** | **Amount ($)** |
| **Common Shares** | | | | |
| Balance, beginning of year | 79,400,768 | 125,916,046 | 63,998,153 | 117,189,874 |
| Private placement, net of share issue costs (i) | - | - | 15,384,615 | 8,698,812 |
| Exercise of stock options (ii) | - | - | 18,000 | 27,360 |
| **Balance, end of period** | **79,400,768** | **125,916,046** | **79,400,768** | **125,916,046** |
| **Warrants** | | | | |
| Balance, beginning of year | 15,384,615 | 1,220,886 | 675,000 | 1,073,250 |
| Private placement, net of share issue costs (i) | - | - | 15,384,615 | 1,220,886 |
| Expiry of warrants | - | - | (675,000) | (1,073,250) |
| **Balance, end of period** | **15,384,615** | **1,220,886** | **15,384,615** | **1,220,886** |

**Issue of Common Shares**

(i) In September 2012, the Corporation closed a series of private placement offerings for gross proceeds of $10,000,000 through the issuance of 15,384,615 units (the "Units") at a price of $0.65 per Unit. Each Unit consists of one common share ("Share") and one common share purchase warrant ("Warrant"). Each Warrant entitles the holder thereof to acquire one additional Share at a price of $0.90 per Share. The Warrants will expire on September 8, 2014 (the "Warrant Expiry Date"), unless the volume weighted average trading price of the Shares on the TSX Venture Exchange Inc. during the 10 consecutive trading days immediately prior to the date for which such calculation is made is greater than $1.125 (the "Trigger Event"). If a Trigger Event occurs, the Warrant Expiry Date may, at the option of the Corporation, be accelerated to the later of: (i) 30 business days from the Trigger Event date; and (ii) one month following the expiry of the applicable hold period required under securities laws.

The fair value of the Warrants issued in conjunction with the September 2012 private placement was estimated at $0.08 per Warrant.

(ii) For the year ended December 31, 2012, 18,000 stock options were exercised with an average exercise price of $1.00 per common share.

**NOTES** *(continued)*

### C) Stock options

Employees, officers, directors and consultants of the Corporation may be granted options to purchase common shares. Options granted have a term of five years to expiry and typically vest equally over a two year period on the basis of one-third on the date of grant, one-third on the first anniversary date of the grant, and one-third on the second anniversary date of the grant. The exercise price of each option equals the market price of the Corporation's common shares on the date of grant.

The following table summarizes the changes to the Corporation's option plan for the three months ended June 30, 2013:

| | Number of options | Weighted average price ($) |
|---|---|---|
| Balance, December 31, 2012 | 4,259,167 | 2.00 |
| Granted | - | - |
| Exercised | - | - |
| Forfeited | (93,333) | 1.98 |
| **Balance, June 30, 2013** | **4,165,834** | **2.00** |

The following table summarizes stock options outstanding and exercisable under the plan at June 30, 2013.

| | Options outstanding | | | Options exercisable | |
|---|---|---|---|---|---|
| **Exercise price** | **Number outstanding at period end** | **Weighted average remaining contractual life** | **Weighted average exercise price** | **Number exercisable at period end** | **Weighted average exercise price** |
| $0.25 | 200,000 | 0.7 | $0.25 | 200,000 | $0.25 |
| $1.00 | 811,667 | 1.7 | $1.00 | 811,667 | $1.00 |
| $1.20 | 105,000 | 0.7 | $1.20 | 105,000 | $1.20 |
| $1.99 | 500,000 | 3.6 | $1.99 | 375,000 | $1.99 |
| $2.00 | 1,396,667 | 2.5 | $2.00 | 1,396,667 | $2.00 |
| $3.05 | 1,017,500 | 2.9 | $3.05 | 1,017,500 | $3.05 |
| $3.09 | 35,000 | 2.7 | $3.09 | 35,000 | $3.09 |
| $3.60 | 100,000 | 2.6 | $3.60 | 100,000 | $3.60 |
| | **4,165,834** | **2.4** | **$2.00** | **4,040,834** | **$2.00** |

### D) Stock Based Compensation

The Corporation accounts for its stock based compensation plan using the fair value method. Under this method, a compensation cost is charged over the vesting period for stock options granted to employees, officers, directors and consultants of the Corporation, with a corresponding increase to contributed surplus.

**NOTES** *(continued)*

### E) Per common share amounts

The basic weighted average number of common shares outstanding for the six months ended June 30, 2013 and 2012 were 79,400,768 and 64,015,362, respectively. As the Corporation has recorded a loss for the three and months ended June 30, 2013 and 2012, no addition is made to the basic weighted average number of common shares when calculating diluted weighted average number of common shares as the diluted per common share amounts are anti-dilutive. For the three months ended June 30, 2013 and 2012, 200,000 and 1,188,334 options, respectively that could potentially dilute basic earnings per share in the future were not included in the calculation of diluted earnings per share because they are antidilutive.

### F) Management of capital structure

The Corporation's policy is to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain the future development of the business.

The Corporation manages its capital structure and makes adjustments to it in the light of changes in economic conditions and the risk characteristics of the underlying petroleum and natural gas assets. The Corporation considers its capital structure to include shareholders' equity, bank debt and working capital, however as at June 30, 2013, the Corporation has no bank debt.

As the Corporation is in the development phase and has not yet generated funds from operations, it is unable to monitor capital based on the ratio of net debt to annualized funds generated from operations. Therefore the Corporation monitors capital based on the projected rate of capital spending and available funds on hand. In order to adjust the capital structure, the Corporation may from time to time issue shares and/or adjust its capital spending levels.

With current working capital on hand and the completion of the Amended Farm-in Agreement with Statoil, the Corporation has adequate funding to provide for general operations and to meet the Corporation's minimum work requirements with the government of the Northern Territory of Australia for a period of at least 12 months.

## 12. Supplemental Cash Flow Information

Changes in non-cash working capital:

| | **Three month ended June 30** | | **Six month ended June 30** | |
|---|---|---|---|---|
| | **2013** | 2012 | **2013** | 2012 |
| | **$** | $ | **$** | $ |
| Accounts receivable | 1,816,569 | (5,645,652) | 2,240,723 | (4,705,733) |
| Prepaid expenses and deposits | 33,500 | 1,550,667 | (46,355) | (2,266,379) |
| Accounts payables and accrued liabilities | (592,804) | 7,515,955 | (2,278,718) | 3,626,851 |
| Other | 49,751 | 62,888 | 203,060 | (155,882) |
| **Change in non-cash working capital** | **1,307,016** | **3,483,858** | **118,710** | **(3,501,143)** |

## 13. DEFERRED INCOME TAXES

During the three and six months ended June 30, 2013, impairment of $66,855,189 was recorded by the Corporation as a result of the execution of the Amended Farm-in Agreement with Statoil. The reduction of the carrying value of the Corporation's goodwill and exploration and evaluation assets has resulted in a deferred tax recovery of $15,090,780 for the three and six months ended June 30, 2013 because the tax basis of the Corporation's assets now exceeds the accounting basis.

## 14. FINANCIAL INSTRUMENTS

### Fair value of financial instruments

The Corporation's financial instruments recognized in the statement of financial position consist of cash and cash equivalents, term deposits, accounts receivable, accounts payable, accrued liabilities and foreign exchange forward contracts. The fair value of these financial instruments, except for foreign exchange forward contracts, approximates their carrying amounts due to their short terms to maturity.

As the foreign exchange forward contracts are designated as held-for-trading they are carried at fair value. The Corporation classifies the fair value of the financial instruments according to the following hierarchy based on the amount of observable inputs used to value the instrument.

- Level 1 – Quoted prices are available in active markets for identical assets or liabilities as of the reporting date. Active markets are those in which transactions occur in sufficient frequency and volume to provide pricing information on an ongoing basis.
- Level 2 – Pricing inputs are other than quoted prices in active markets included in Level 1. Prices are either directly or indirectly observable as of the reporting date. Level 2 valuations are based on inputs, including quoted forward prices for commodities, time value and volatility factors, which can be substantially observed or corroborated in the marketplace.
- Level 3 – Valuations in this level are those with inputs for the asset or liability that are not based on observable market data.

Assessment of the significance of a particular input to the fair value measurement requires judgment and may affect the placement within the fair value hierarchy level.

Marketable securities are classified as level 1 within the fair value hierarchy and are recorded on the Corporation's statement of financial position at the fair value on the reporting date.

### Credit risk

As the Corporation is currently in the exploration phase, accounts receivable is limited to amounts largely pertaining to joint venture receivables and income tax credits on goods and services taxes in Australia and in Canada which are subject to normal credit risks.

### Currency risks

The Corporation is exposed to exchange rate fluctuations in relation to amounts due to services it must purchase in foreign currencies including the Australian and United States dollars. As at June 30, 2013, the Corporation's cash and cash equivalents included $7,539,317 denominated in Australian dollars. A decrease or increase of one percent to the Australia / Canada foreign exchange rate would have decreased or increased the other comprehensive loss by $75,393 for the six months ended June 30, 2013. Management continually monitors the Corporation's currency risk and believes this exposure is not material to its overall operations. The Corporation uses forward foreign currency exchange rate contracts in order to reduce its exposure to currency risks from fluctuations in the Canadian and Australian currencies.

### Interest rate risk

At June 30, 2013, the Corporation had no outstanding bank debt and is not exposed to interest rate risk at this time.

### Liquidity risk

Liquidity risk relates to the risk the Corporation will encounter difficulty in meeting obligations associated with financial liabilities. The financial liabilities on its statement of financial position are limited to accounts payable and accrued liabilities, all of which are current in nature. The Corporation anticipates it will continue to have adequate liquidity to fund its existing financial liabilities and ongoing operating and general administrative expenses through its existing working capital. The Corporation had no defaults or breaches on any of its financial liabilities. The Corporation expects to satisfy obligations under accounts payable in less than one year.

With current working capital on hand and the completion of the Amended Farm-in Agreement with Statoil, the Corporation expects to have adequate funding to provide for general operations and to meet the Corporation's minimum work requirements with the government of the Northern Territory of Australia for a period of at least 12 months.

### Market risk

Market risk is comprised of currency risk, interest rate risk and other price risks which consist primarily of fluctuations in petroleum and natural gas prices. With no bank debt as at June 30, 2013 there is no direct exposure to fluctuations in interest rates. As the Corporation is in the exploration stage, fluctuations in commodity prices bear no direct risk to the Corporation's revenue, however adverse fluctuations in interest rates, exchange rates and commodity prices may indirectly affect the Corporation's ability to obtain equity financing and future bank debt, if required, and on favorable terms.

## 15. RELATED PARTY TRANSACTIONS

In accordance with the terms of an Administrative Services Agreement ("ASA"), Rodinia Oil Corp. ("Rodinia") provides certain administrative services and office accommodations to the Corporation and vice versa on a cost recovery basis. ASA charges are recorded to general and administrative expenses in the Corporation's financial statements. For the three and six months ended June 30, 2013, the Corporation was charged $9,290 and $135,906 of ASA expense, respectively. As at June 30, 2013, $52,259 was receivable from Rodinia.

## 16. COMMITMENTS AND CONTINGENCIES

### EP 103 Minimum Work Plan Commitment

In accordance with the terms of the EP 103 agreement with the government of the Northern Territory of Australia, the Corporation has the following minimum work commitments and timelines:

| Year | Start | End | Minimum work requirements | Status as at June 30, 2013 |
|---|---|---|---|---|
| Year 5 | May 21, 2012 | May 20, 2014 | Drill one exploration well | Outstanding |

### EP 104 Minimum Work Plan Commitment

In accordance with the terms of the EP 104 agreement with the government of the Northern Territory of Australia, the Corporation has the following minimum work commitments and timelines:

| Year | Start | End | Minimum work requirements | Status as at June 30, 2013 |
|---|---|---|---|---|
| Year 5 | May 21, 2012 | May 20, 2014 | Drill one exploration well | Outstanding |

### EP 127 Minimum Work Plan Commitments

In accordance with the terms of the EP 127 agreement with the government of the Northern Territory, Australia, the Corporation has the following minimum work commitments and timelines:

| Year | Start | End | Minimum work requirements | Status as at June 30, 2013 |
|---|---|---|---|---|
| Year 4 | December 14, 2011 | December 13, 2014 | Acquire seismic data or drill a well | Outstanding |
| Year 5 | December 14, 2012 | December 13, 2015 | Drill an exploration well | Outstanding |

### EP 128 Minimum Work Plan Commitments

In accordance with the terms of the EP 128 agreement with the government of the Northern Territory, Australia, the Corporation has the following minimum work commitments and timelines:

| Year | Start | End | Minimum work requirements | Status as at June 30, 2013 |
|---|---|---|---|---|
| Year 3 | June 14, 2010 | December 13, 2013 | Acquire seismic data | Outstanding |
| Year 4 | December 14, 2011 | June 13, 2014 | Drill an exploration well | Outstanding |
| Year 5 | June 14, 2013 | June 13, 2015 | Drill an exploration well | Outstanding |

After satisfying the five year minimum work requirements for each of the exploration permits, the acreage is subject to relinquishment provisions. However, each of the exploration permits can enter into up to two additional five year work terms subject to the Corporation successfully renegotiating new minimum work requirements with the Northern Territory government.

**Statoil Farm-In Agreement**

On June 10, 2013, the Corporation entered into the Amended Farm-in Agreement with Statoil whereby Statoil committed to spend the next US$50 million throughout the remainder of 2013 and 2014. Pursuant to the Amended Farm-in Agreement, Statoil has been transferred 80% of the Corporation's working interests in EP 103, EP 104, EP 127 and EP 128 and in EPA 213 and EPA 252 in exchange for exploration program related payments and carried costs of up to US$175.0 million over three phases to the end of 2016.

Under the terms of the Amended Farm-in Agreement, up to the next US$160 million of exploration costs will be fully funded by Statoil as follows:

<u>Phase 1 & 2A (2013 and 2014):</u>

- Statoil will spend the next US$50 million on exploration (PetroFrontier – nil) and assume operatorship on September 1, 2013

- At the end of Phase 2A, Statoil will have the option to continue to Phase 2B; if Statoil elects not to continue, it must return to PetroFrontier 50% of its former working interest in the Permits, such that ownership will then be: Statoil (30%), PetroFrontier (70%)

<u>Phase 2B (2015):</u>

- Upon proceeding to Phase 2B, Statoil will spend the next US$30 million on exploration (PetroFrontier – nil)

- At the end of Phase 2B, Statoil will have the option to continue to Phase 3; if Statoil elects not to continue to Phase 3, then it must return to PetroFrontier 25% of its former working interest in the Permits, such that ownership will then be Statoil (55%), PetroFrontier (45%)

<u>Phase 3 (2016):</u>

- Upon proceeding to Phase 3, Statoil will spend the next US$80 million on exploration (PetroFrontier – nil)

- At the end of Phase 3, Statoil will own 80% and PetroFrontier will own 20% of PetroFrontier's former working interest in the Permits

At the end of Phase 3, Statoil will have completed its funding obligations under the Amended Farm-in Agreement and the sharing of future costs between Statoil and PetroFrontier will be based on their then respective ownership interests.

**NOTES** *(continued)*

As at June 30, 2013, the Corporation had the following material contracts and commitments:

| | Total | 2013 | 2014 | 2015 | 2016 | 2017 |
|---|---|---|---|---|---|---|
| EP 103 minimum commitments | **3,368,393** | - | 3,368,393 | - | - | - |
| EP 104 minimum commitments | **3,405,097** | - | 3,405,097 | - | - | - |
| EP 127 minimum commitments | **2,564,806** | 831,892 | - | 1,732,914 | - | - |
| EP 128 minimum commitments | **5,463,522** | 1,997,694 | 1,732,914 | 1,732,914 | - | - |
| Leases | **191,074** | 135,694 | 55,380 | - | - | - |
| | **14,992,892** | **2,965,280** | **8,561,784** | **3,465,828** | **-** | **-** |

The Corporation's minimum commitments under EP 103, EP 104, EP 127 and EP 128 are expected to be fully funded by Statoil in accordance with the Amended Farm-in Agreement.

During the three and six months ended June 30, 2013, the Corporation expensed $103,681 and $200,598 relating to operating leases it maintained throughout the year.

As at June 30, 2013, through the normal course of business the Corporation had an outstanding dispute with a third party service provider that in aggregate totaled $1,182,369. In management's opinion these charges are unsubstantiated and therefore have not been accrued.

**NOTES** *(continued)*

## 17. SEGMENTED INFORMATION

The Corporation has a foreign subsidiary and the following geographical segmented information is provided:

| | Three months ended June 30, 2013 | | Three months ended June 30, 2012 | |
|---|---|---|---|---|
| | Canada ($) | Australia ($) | Canada ($) | Australia ($) |
| **EXPENSES** | | | | |
| General and administrative | 400,679 | 570,196 | 571,507 | 1,281,034 |
| Loss on marketable securities | 3,995 | - | 12,494 | - |
| Foreign exchange loss | 242 | 3,146 | 277,700 | - |
| Financial derivative instruments (note 11) | - | - | (132,553) | - |
| Share-based compensation (note 8) | 82,483 | - | 105,827 | - |
| Depreciation | 173 | 13,062 | 281 | 13,070 |
| Impairment | - | 68,837,915 | - | - |
| Results from operating activities | 487,572 | 69,424,319 | 835,256 | 1,294,104 |
| Finance income | 2,175 | 45,431 | 36,768 | 57,821 |
| Finance costs | (248) | (13,432) | (3,506) | (12,365) |
| Net finance income | 1,927 | 31,999 | 33,262 | 45,456 |
| Net loss before taxes | (485,645) | (69,392,320) | (801,994) | (1,248,648) |
| Deferred tax recovery | - | 15,090,780 | - | - |
| **NET LOSS** | **(485,645)** | **(54,301,540)** | **(801,994)** | **(1,248,648)** |
| Exploration and evaluation assets (end of period) | - | 46,004,875 | - | 103,646,383 |
| Exploration and evaluation expenditures | - | 40,947 | - | 5,328,924 |
| Total assets (end of period) | 1,124,861 | 56,049,978 | 9,470,478 | 127,104,707 |
| Total liabilities (end of period) | 200,717 | 2,946,846 | 228,152 | 27,059,094 |

NOTES *(continued)*

| | Six months ended June 30, 2013 | | Six months ended June 30, 2012 | |
|---|---|---|---|---|
| | Canada ($) | Australia ($) | Canada ($) | Australia ($) |
| **EXPENSES** | | | | |
| General and administrative | 839,742 | 1,383,433 | 978,227 | 1,852,504 |
| Loss on marketable securities | 2,605 | - | 29,003 | - |
| Foreign exchange loss | 179 | 16,713 | 155,231 | - |
| Financial derivative instruments (note 11) | - | - | (150,631) | - |
| Share-based compensation (note 7) | 213,367 | - | 980,655 | - |
| Depreciation | 384 | 27,302 | 397 | 25,628 |
| Impairment | - | 68,837,915 | - | - |
| Results from operating activities | 1,056,277 | 70,265,363 | 1,992,882 | 1,878,132 |
| Finance income | 5,233 | 81,826 | 83,288 | 103,789 |
| Finance costs | (450) | (26,451) | (3,972) | (19,029) |
| Net finance income | 4,783 | 55,375 | 79,316 | 84,760 |
| Net loss before taxes | (1,051,494) | (70,209,988) | (1,913,566) | (1,793,372) |
| Deferred tax recovery | - | 15,090,780 | - | - |
| **NET LOSS** | **(1,051,494)** | **(55,119,208)** | **(1,913,566)** | **(1,793,372)** |
| Exploration and evaluation assets (end of period) | - | 46,004,875 | - | 103,646,383 |
| Exploration and evaluation expenditures | - | 76,076 | - | 6,137,854 |
| Total assets (end of period) | 1,124,861 | 56,049,978 | 9,470,478 | 127,104,707 |
| Total liabilities (end of period) | 200,717 | 2,946,846 | 228,152 | 27,059,094 |

## 18. SUBSEQUENT EVENTS

Subsequent to June 30, 2013, the Corporation was informed that the Foreign Investment Review Board of Australia ("FIRB") had no objection to, and the TSX Venture Exchange ("TSXV") had approved, the Amended Farm-in Agreement between Statoil and the Corporation and as such, the Corporation transferred 80% of its working interests in EP 103, EP 104, EP 127 and EP 128 and in EPA 213 and EPA 252 to Statoil.

**NOTES** *(continued)*

***Directors***
Robert J. Iverach
Chairman of the Board of Directors
Calgary, Alberta

Paul J. Bennett
Chief Executive Officer
PetroFrontier Corp.
Calgary, Alberta

Martin P. McGoldrick
Businessman
Calgary, Alberta

Kent Jespersen
Businessman
Calgary, Alberta

Dr. James W. Buckee
Businessman
Wiltshire, UK

Al Kroontje
Businessman
Calgary, Alberta

Donald Rae
Businessman
Calgary, Alberta

***Officers***
Paul J. Bennett
Chief Executive Officer

Shane J. Kozak
Vice President Finance and
Chief Financial Officer

Earl Scott
Chief Operating Officer

***Corporate Head Office***
320, 715 – 5th Avenue S.W.
Calgary, Alberta
T2P 2X6
Telephone: (403) 718-0366
Facsimile: (403) 718-3888
Website: www.petrofrontier.com
Email: info@petrofrontier.com

***Bankers***
HSBC
Corporate Banking
Canada Trust Tower
407, 8th Avenue S.W.
Calgary, Alberta
T2P 1E5

***Trustee and Transfer Agent***
Olympia Trust Company
Calgary, Alberta

***Solicitors***
Burstall Winger LLP
Suite 1600 - Dome Tower
333 – 7th Ave SW
Calgary, Alberta
T2P 2Z1

***Auditors***
PricewaterhouseCoopers LLP.
Suite 3100-111 5 Ave SW
Calgary, Alberta
T2P 5L3