Terra Nova Energy Ltd.

[Formerly "Terra Nova Minerals Inc."]

Financial Statements

Year ended July 31, 2012

(Expressed in Canadian Dollars)

MANAGEMENT'S REPORT

The management of Terra Nova Energy Ltd. (formerly "Terra Nova Minerals Inc.") is responsible for the preparation of all information included in these consolidated financial statements and Management's Discussion & Analysis ("MD&A"). The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB") and adopted in Canada. Financial information that is presented in the MD&A is consistent with the consolidated financial statements.

In preparation of the consolidated financial statements, estimates are sometimes necessary because a precise determination of certain assets and liabilities is dependent on future events. Management believes such estimates have been based on careful judgments and have been presented fairly in all material respects.

Management maintains appropriate systems of internal control that provide reasonable assurance that transactions are appropriately authorized, assets are safeguarded from loss or unauthorized use and financial records provide reliable and accurate information for the presentation of consolidated financial statements.

KPMG LLP, an independent firm of chartered accountants, was appointed by the board of directors to audit the consolidated financial statements of Terra Nova Energy Ltd. and provide an independent professional opinion. Their report is presented with the consolidated financial statements below.

The Board of Directors, through its Audit Committee, has reviewed the consolidated financial statements including notes thereto with management and KPMG LLP. The Audit Committee is composed of independent directors. The Directors of Terra Nova Energy Ltd. approved the information contained in the consolidated financial statements based on the recommendation of the Audit Committee.

[signed] *"Norman J. Mackenzie"*

Norman J, Mackenzie
Chairman and CEO

[signed] *"Andrew R. Williams"*

Andrew R. Williams
CFO

November 27, 2012

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INDEPENDENT AUDITORS' REPORT

To the Shareholders of Terra Nova Energy Ltd. (formerly "Terra Nova Minerals Inc.")

We have audited the accompanying consolidated financial statements of Terra Nova Energy Ltd. (formerly "Terra Nova Minerals Inc."), which comprise the consolidated statements of financial position as at July 31, 2012, July 31, 2011 and August 1, 2010, the consolidated statements of loss and comprehensive loss, changes in equity (deficiency) attributable to shareholders and cash flows for the years ended July 31, 2012 and July 31, 2011, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits 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 consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation and fair presentation of the consolidated 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 entity'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 consolidated financial statements.

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

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated statements financial position of Terra Nova Energy Ltd. as at July 31, 2012, July 31, 2011 and August 1, 2010, and its consolidated financial performance and its consolidated cash flows for the years ended July 31, 2012 and July 31, 2011 in accordance with International Financial Reporting Standards.

KPMG LLP is a Canadian limited liability partnership and a member firm of the KPMG network of independent member firms affiliated with KPMG International Cooperative ("KPMG International"), a Swiss entity.
KPMG Canada provides services to KPMG LLP.

Emphasis of Matter

Without modifying our opinion, we draw attention to Note 2(d) in the consolidated financial statements which indicates that Terra Nova Energy Ltd. has substantial commitments of which Terra Nova Energy Ltd. currently does not have the resources to meet. These conditions, along with other matters as set forth in Note 2(d) in the consolidated financial statements, indicate the existence of a material uncertainty that may cast significant doubt about Terra Nova Energy Ltd's ability to continue as a going concern.

KPMG LLP

Chartered Accountants

Calgary, Canada
November 27, 2012

Terra Nova Energy Ltd.

Consolidated Statement of Financial Position

[Expressed in Canadian Dollars]

	July 31 2012	July 31 2011	August 1 2010
	$	$	$ (note13)
Assets			
Current			
Cash	**4,181,307**	428,200	3,377
Cash held-in-trust - notes 5 and 9	**4,629,037**	-	-
GST/HST recoverable	**71,677**	7,590	23,988
Recoverable withholding taxes paid on interest earned	**13,795**	-	-
Funds deposited on account - notes 5 and 9	**263,400**	-	-
Pre-paid expenses	**2,677**	-	-
	9,161,893	435,790	27,365
Exploration and evaluation interests - notes 5 and 8	**1,129,332**	-	-
Mineral property interest - note 6	**-**	48,401	-
	10,291,225	484,191	27,365
Liabilities			
Current			
Accounts payable and accruals - note 8	**354,378**	29,519	949,002
Equity (Deficiency) Attributable to Shareholders			
Share capital - note 7	**23,013,555**	17,682,546	16,211,526
Contibuted surplus	**5,789,878**	1,220,289	890,446
Accumulated other comprehensive income	**280,800**	-	-
Deficit	**(19,147,386)**	(18,448,163)	(18,023,609)
	9,936,847	454,672	(921,637)
	10,291,225	484,191	27,365

Nature of operations - note 1
Basis of presentation and going concern - note 2
Commitments and contingencies - notes 1, 2, 5, 7, 8 and 10
Subsequent events - notes 1, 5, 7, 8 and 11

Approved on behalf of the Board of Directors on November 27, 2012

"Norman J. Mackenzie", Director

"Peter Miles", Director

The accompanying notes are an integral part of these financial statements.

Terra Nova Energy Ltd.

Consolidated Statement of Loss and Comprehensive Loss
Year ended July 31
[Expressed in Canadian Dollars]

	2012	2011
	$	$
Expenses		
Administration	**-**	(14,000)
Audit and accounting - note 8	**(72,269)**	(37,361)
Filing and transfer agent	**(23,582)**	(22,248)
Legal	**(82,793)**	(30,912)
Management - note 8	**(108,534)**	(23,500)
Office and miscellaneous	**(73,413)**	(527)
Shareholder communications	**(36,400)**	(3,563)
Stock-based compensation - notes 7 and 8	**(265,918)**	(278,618)
Travel and related	**(4,477)**	(1,810)
	(667,386)	(412,539)
Other income (expense)		
Gain on debt forgiveness	**5,250**	1,867
Gain realized on foreign currency transactions	**-**	(13,395)
Interest	**29,183**	(487)
Write-off of mineral property interests - note 6	**(66,270)**	-
Net loss	**(699,223)**	(424,554)
Other comprehensive income		
Exchange gain on translation of foreign accounts	**280,800**	-
Net loss and comprehensive loss	**(418,423)**	(424,554)
Loss per share - basic and diluted	**(0.03)**	(0.05)
Weighted average number of shares outstanding - basic and diluted	**23,730,789**	9,421,046

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The accompanying notes are an integral part of these financial statements.

Terra Nova Energy Ltd.

Consolidated Statement of Cash Flows
Year ended July 31
[Expressed in Canadian Dollars]

	2012	2011
	$	$
Cash Provided From (Used in):		
Operating Activities		
Net loss for the year	**(699,223)**	(424,554)
Items not affecting cash:		
Gain on debt forgiveness	**(5,250)**	(1,867)
Stock-based compensation	**265,918**	278,618
Write-off of mineral property interests	**66,270**	-
	(372,285)	(147,803)
Net change in non-cash working capital items		
GST/HST recoverable	**(62,423)**	16,398
Recoverable withholding taxes paid on interest earned	**(13,093)**	-
Pre-paid expenses	**(2,677)**	-
Accounts payable and accruals	**158,467**	(917,616)
	(292,011)	(1,049,021)
Financing Activities		
Proceeds from securities issued, net of issuance cost	**10,652,075**	1,522,245
Share issuance costs	**(1,267,395)**	
Receipt of loan	**-**	40,000
Repayment of loan	**-**	(40,000)
	9,384,680	1,522,245
Investing Activities		
Funds deposited on account	**(250,000)**	-
Exploration and evaluation interests	**(707,656)**	-
Mineral property interest	**(17,869)**	(48,401)
	(975,525)	(48,401)
Foreign exchange gain on cash held in foreign currencies	**265,000**	-
Increase in cash	**8,382,144**	424,823
Cash - beginning of year	**428,200**	3,377
Cash and cash held-in-trust - end of year	**8,810,344**	428,200

Supplemental cash flow information - note 12

The accompanying notes are an integral part of these financial statements.

Terra Nova Energy Ltd.

Consolidated Statement of Changes in Equity (Deficiency) Attributable to Shareholders
Year ended July 31
[Expressed in Canadian Dollars]

	Number of common shares	Share Capital	Contributed Surplus	Deficit	Accumulated other comprehensive income	Total Equity
		$	$	$	$	$
Balance - August 1, 2010	2,865,897	16,211,526	890,446	(18,023,609)	-	(921,637)
Shares issued in consideration for						
Cash, pursuant to private placement	10,245,000	1,485,525	51,225	-	-	1,536,750
Payment of finder's fees	988,000	143,260	4,940	-	-	148,200
Share issue costs paid in consideration for:					-	-
Cash	-	(14,505)	-	-	-	(14,505)
Finder's fees	-	(143,260)	(4,940)	-	-	(148,200)
Stock-based compensation	-	-	278,618	-	-	278,618
Net loss for the year	-	-	-	(424,554)	-	(424,554)
Balance - July 31, 2011	14,098,897	17,682,546	1,220,289	(18,448,163)	-	454,672
Shares issued in consideration for:						
PNG Interests	1,000,000	250,000	-	-	-	250,000
Cash	42,608,300	6,932,116	3,719,959	-	-	10,652,075
Less share issuance costs paid in consideration for:						
Cash	-	(1,267,395)	-	-	-	(1,267,395)
Agent options	-	(583,712)	583,712	-	-	-
Stock-based compensation	-	-	265,918	-	-	265,918
Other comprehensive income	-	-	-	-	280,800	280,800
Net loss for the year	-	-	-	(699,223)	-	(699,223)
Balance - July 31, 2012	**57,707,197**	**23,013,555**	**5,789,878**	**(19,147,386)**	**280,800**	**9,936,847**

The accompanying notes are an integral part of these financial statements.

1. Nature of operations

Terra Nova Energy Ltd. (formerly "Terra Nova Minerals Inc.") is a public company (the "Company" or "Terra Nova"). At a special meeting of shareholders held on August 13, 2012, shareholders voted in favour of a continuation of the Company from the federal jurisdiction into Alberta (the "Continuance") and approved a name change to Terra Nova Energy Ltd. The Continuance did not result in any change in the business of the Company.

The Company's shares are listed on the TSX Venture Exchange (the "TSX V") on which the Company has been classified as an "oil and gas company" since May 11, 2012 and the Frankfurt Stock Exchange. Prior to May 11 2012, the Company was classified on the TSX V as a "mineral resource company". The Company's principal business is the acquisition and exploration of petroleum and natural gas properties.

On October 19, 2012, Terra Nova announced a proposed non-brokered private placement financing to raise up to $2,000,000 from the sale of 10 million units to subscribers outside Canada and the United States (the "October 2012 Financing"). Proceeds from the October 2012 Financing were combined with funds on hand and used primarily to fund a drilling commitment that was due on November 1, 2012.

On May 11, 2012, in conjunction with the completion of a $10,652,075 brokered private placement Financing (the "May 2012 Financing"), through a wholly-owned subsidiary company, Terra Nova Resources Inc. ("Alberta Co."), the Company executed an oil and gas farm-in agreement to secure the right to earn up to a 55% working interest in petroleum and natural gas rights on certain on-shore Australian Petroleum Exploration Licenses ("PEL's"), known as PEL's 112 and 444 (the "Exploration and Evaluation Interests" or "E&E Interests") in Australia (the "Farm-in Agreement"). The temporarily held in the name of Alberta Co. pending transfer to a wholly-owned Australian subsidiary with effect from June 4, 2012, the date on which the Company incorporated Terra Nova Holdings (Australia) Pty. Ltd. ("TN Holdings Australia") and its wholly-owned subsidiary, Terra Nova Energy (Australia) Pty. Ltd ("TN Energy Australia") to hold the Farm-in rights.

On executing the Farm-in Agreement, the Company ceased to operate as a mineral resource entity and incurred a $66,270 write-off of all of its mineral property interests (note 6).

In December 2010, the Company completed a reactivation that entailed obtaining regulatory approval for completion of the following transactions: secured a 50% interest in a mineral property; a consolidation of its common shares on the basis of 1 new share for every 13.5 old shares (the "Share Consolidation"); and, completed a private placement of 11,233,000 units to result in gross proceeds of $1,536,750 (the "December 2010 Reactivation Financing").

On completion of the Share Consolidation, on December 30, 2010, a total of 38,689,868 old shares outstanding were cancelled in exchange for 2,865,897 new shares. For purposes of discussion in these financial statements, regardless of the share consolidation date, all references to share quantities expressed herein are expressed in terms of new shares unless otherwise expressly disclosed.

2. Basis of preparation and going-concern

a) Statement of compliance

These consolidated financial statements present Terra Nova's first annual audited consolidated financial statements to be issued under IFRS as at and for the years ended July 31, 2012 and 2011. These consolidated financial statements have been prepared in accordance with IFRS accounting policies and methods of computation as set forth in note 3 below. Previously, the Company prepared its financial statements in accordance with Canadian Generally Accepted Accounting Principles ("Canadian GAAP").

These financial and all statements were approved by the board of directors on November 27, 2012.

The preparation of these consolidated financial statements resulted in selected changes to the Company's accounting policies as compared to those disclosed in Terra Nova's annual audited consolidated financial statements for the year ended July 31, 2011 issued under Canadian GAAP. Accordingly, the IFRS accounting policies have been retrospectively and consistently applied in the accordance with IFRS 1 - First-time Adoption of IFRS. An explanation of how the transition to IFRS has affected the reported financial position, financial performance and cash flows of the Company is provided in note 12. As disclosed in note 12, the application of IFRS did not result in any changes to the financial statements as previously prepared under Canadian GAAP to those under IFRS, for the comparative periods as at August 1, 2010 and as at and for the year ended July 31, 2011.

The accounting policies that relate to the E&E Interests as disclosed in note 3 below were adopted in compliance with IFRS in the year ended July 31, 2012 and consequently, the adoption of these policies had no effect on operations prior to August 1, 2011.

b) Basis of measurement

These consolidated financial statements have been prepared on the historical cost basis except for certain financial and non-financial assets and liabilities, which have been measured at fair value. The methods used to measure fair value are discussed in note 4.

The Company's consolidated financial statements include the accounts of Terra Nova and its subsidiaries and are expressed in Canadian Dollars, unless otherwise stated.

c) Functional and presentation currency

These consolidated financial statements are presented in Canadian Dollars ("C$") which is Terra Nova's reporting currency. Terra Nova's foreign subsidiaries transact in currencies other than C$ and have a functional currency of Australian Dollars ("A$"). The functional currency of the Australian subsidiaries is the currency of the primary economic environment in which the subsidiaries operate. Transactions denominated in a currency other than the functional currency are translated at the prevailing rates on the date of the transaction. Any monetary items held in a currency which is not the functional currency of the subsidiary are translated to the functional currency at the prevailing rate as at the date of the balance sheet. All exchange differences arising as a result of the translation to the functional currency of the subsidiary are recorded in each respective subsidiary's net earnings.

Translation of all assets and liabilities from the respective functional currencies to the reporting currency are performed using the rates prevailing at the balance sheet date. The differences arising upon translation from the functional currency to the reporting currency are recorded as currency translation adjustments in other comprehensive income ("OCI") and are held within accumulated other comprehensive income ("AOCI") until a disposal or partial disposal of a subsidiary. A disposal or partial disposal will then give rise to a realized foreign exchange gain or loss which is recorded in net earnings.

d) Going concern

Since inception, operations of the Company have primarily been funded by the issuance of common shares. In addition to assessing the merits of the E&E Interests currently held by the Company, it is likely the Company will seek additional E&E opportunities, which will require additional financing.

These financial statements have been prepared in accordance with International Financial Reporting Standards ('IFRS") on a going concern basis, which presume the realization of assets and discharge of liabilities in the normal course of business for the foreseeable future. The Company's ability to continue as a going concern is dependent upon achieving profitable operations and upon obtaining additional financing. While the Company is expending its best efforts in this regard, the outcome of these matters cannot be predicted at this time. Accordingly, these financial statements do not give effect to adjustments that would be necessary should the Company be unable to continue as a going

concern and therefore be required to realize its assets and liquidate its liabilities, contingent obligations and commitments in other than the normal course of business and at amounts different from those reported in these consolidated financial statements.

There is significant doubt about the Company's ability to continue as a going concern. Currently defined plans over the period through November 2013 contemplate completion of a proposed seismic program on PEL 444, for which in addition to approximately A$1,600,000 that is supposed to be funded by third-party joint working-interest partners with the remaining A$2,000,000 to be funded by the Company. In addition, although the Company funded the A$4,500,000 earn-in drilling deposit as required by November 1, 2012 to fund dry-hole costs associated with an initial 3-well drilling program (note 7), the Company is liable for any related cost overruns plus 50% of the related completion costs, if any. In addition, if the foregoing drilling activity results in a significant discovery and the Company elects to earn into the Farm-in Agreement to the extent of its 55% working-interest maximum, the Company will be required to pay a secondary A$4,500,000 drilling deposit as well as to fund any related dry-hole cost overruns as well as the related completion costs, if any.

During the year ended July 31, 2012, the Company incurred a net loss of $699,223 (2011 - $424,554) and as at July 31, 2012 had accumulated losses of $19,147,386 and can be expected to incur losses for the foreseeable future. As at July 31, 2012, the Company had working capital available for future operations amounting to $8,807,515 which management estimates is insufficient to meet operating and property requirements over the next twelve months. Accordingly, in order to meet its operating obligations as currently contemplated and any incremental exploration expenditures, the Company will require additional financing.

There can be no assurance that any additional financing can be secured.

e) Use of estimates and judgments

The preparation of financial statements in conformity with IFRS requires management to make judgments, 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 year in which the estimates are revised and in any future years affected. Significant estimates and judgments made by management in the preparation of these consolidated financial statements are outlined below.

Critical judgments in applying accounting policies and key sources of estimation uncertainty:

Critical judgments that management has made in the process of applying the Company's accounting policies and the related key sources of estimation uncertainty that could have the most significant effect on the amounts recognized in these audited consolidated financial statements are as follows:

(i) Reserves

As at July 31, 2012, the Company did not have any petroleum and natural gas reserves. However, the estimation of reported recoverable quantities of proved and probable reserves include judgmental assumptions regarding production profile, commodity prices, exchange rates, remediation costs, timing and amount of future development costs, and production, transportation and marketing costs for future cash flows. It also requires interpretation of geological and geophysical models in anticipated recoveries. The economic, geological and technical factors used to estimate reserves may change from period to period. Changes in reported reserves can impact the carrying values of the Company's petroleum and natural gas properties and equipment, the calculation of depletion and depreciation, the provision for decommissioning obligations, and the recognition of deferred tax assets and liabilities due to changes in expected future cash flows. The recoverable quantities of reserves and estimated cash flows from any

future Terra Nova petroleum and natural gas interests will be independently evaluated by reserve engineers annually.

Any calculations of petroleum and natural gas reserves represent estimated quantities of petroleum, natural gas and natural gas liquids which geological, geophysical and engineering data demonstrate with a specified degree of certainty to be economically recoverable in future years from known reservoirs and which are considered commercially producible. Such reserves may be considered commercially producible if management has the intention of developing and producing them and such intention is based upon a reasonable assessment of the future economics of such production, a reasonable expectation that there is a market for all or substantially all the expected petroleum and natural gas production, and evidence that the necessary production, transmission and transportation facilities are available or can be made available. Reserves may only be considered proven and probable if the ability to produce is supported by either production or conclusive formation tests. Terra Nova's petroleum and gas reserves will be determined pursuant to National Instrument 51-101, Standard of Disclosures for Oil and Gas Activities.

(ii) Identification of cash-generating units

Terra Nova's assets are aggregated into cash-generating units ("CGU" or "CGUs"), for the purpose of calculating impairment, based on their ability to generate largely independent cash flows. By their nature, these estimates and assumptions are subject to measurement uncertainty and may impact the carrying value of the Company's assets in future periods.

(iii) Share-based payments

All equity-settled, share-based awards issued by the Company are recorded at fair value using the Black-Scholes option-pricing model. In assessing the fair value of equity-based compensation, estimates have to be made regarding the expected volatility in share price, option life, dividend yield, risk-free rate and estimated forfeitures at the initial grant date.

(iv) Decommissioning obligations

The Company estimates future remediation costs of production facilities, wells and pipelines at different stages of development and construction of assets or facilities. In most instances, removal of assets occurs many years into the future. This requires judgment regarding abandonment date, future environmental and regulatory legislation, the extent of reclamation activities, the engineering methodology for estimating cost, future removal technologies in determining the removal cost and liability-specific discount rates to determine the present value of these cash flows. As at July 31, 2012, the Company was not liable for any decommissioning liabilities.

(v) Impairment of petroleum and natural gas assets and exploration and evaluation interests

For the purposes of determining whether any impairment of petroleum and natural gas assets has occurred, and the extent of any impairment or its reversal, the key assumptions the Company uses in estimating future cash flows are future petroleum and natural gas prices, expected production volumes and anticipated recoverable quantities of proved and probable reserves. These assumptions are subject to change as new information becomes available. Changes in economic conditions can also affect the rate used to discount future cash flow estimates. Changes in the aforementioned assumptions could affect the carrying amounts of assets, and impairment charges and reversal will affect profit or loss. As at July 31, 2012, the Company determined that no impairment of its E&E interests was required.

(vi) Income taxes

Tax provisions are based on enacted or substantively enacted laws. Changes in those laws could affect amounts recognized in profit or loss both in the period of change, which would include any impact on cumulative provisions, and in future periods. Deferred tax assets (if any) are recognized only to the extent it is considered probable that those assets will be recoverable. This involves an assessment of when those deferred tax assets are likely to reverse and a judgment as to whether or not there will be sufficient taxable profits available to offset the tax assets when they do reverse. This requires assumptions regarding future profitability and is therefore inherently uncertain. To the extent assumptions regarding future profitability change, there can be an increase or decrease in the amounts recognized in respect of deferred tax assets as well as the amounts recognized in profit or loss in the period in which the change occurs.

3. Significant accounting policies

The accounting policies set out below have been applied consistently to all years presented in these consolidated financial statements, except where specific exemptions permitted an alternative treatment on transition to IFRS in accordance with IFRS-1, and have been applied consistently by the Company and its subsidiaries.

a) Basis of consolidation

(i) Subsidiaries:

Subsidiaries are entities controlled by the Company. Control exists when the Company has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, potential voting rights that currently are exercisable are taken into account. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

The acquisition method of accounting is used to account for acquisitions of subsidiaries and assets that meet the definition of a business under IFRS. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date. The excess of the cost of acquisition over the fair value of the identifiable assets, liabilities and contingent liabilities acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognized immediately in the statement of loss as a gain.

(ii) Jointly controlled operations and jointly controlled assets:

Many of the Company's oil and natural gas activities involve jointly controlled assets. The consolidated financial statements include the Company's share of these jointly controlled assets and a proportionate share of the relevant revenue and related costs.

(iii) Transactions eliminated on consolidation:

Intercompany balances and transactions, and any unrealized income and expenses arising from intercompany transactions, are eliminated in preparing the consolidated financial statements.

b) Financial instruments

(i) Non-derivative financial instruments:

Non-derivative financial instruments comprise accounts receivable, cash and cash equivalents, and accounts payable. Non-derivative financial instruments are recognized initially at fair value plus, for instruments not at fair value through profit or loss, any directly attributable transaction

costs. Subsequent to initial recognition non-derivative financial instruments are measured as described below.

Cash and cash equivalents comprise cash on hand, term deposits held with banks, other short-term highly liquid investments with original maturities of three months or less. Other non-derivative financial instruments, such as accounts receivable and accounts payable, are measured at amortized cost using the effective interest method, less any impairment losses.

c) Share capital*:*

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

d) Property, plant and equipment and exploration and evaluation assets

(i) Recognition and measurement:

Exploration and evaluation ("E&E") expenditures:

Pre-license costs are recognized in the statement of loss as incurred. Exploration and evaluation costs, including the costs of acquiring licenses and directly attributable general and administrative costs, are capitalized initially as exploration and evaluation assets. The costs are accumulated in cost centers by well, field or exploration area pending the determination of technical feasibility and commercial viability.

Exploration and evaluation assets are assessed for impairment if sufficient data exists to determine technical feasibility and commercial viability, and facts and circumstances suggest that the carrying amount exceeds the recoverable amount. For purposes of impairment testing, exploration and evaluation assets are allocated to cash-generating units. The technical feasibility and commercial viability of extracting a mineral resource is generally considered to be determinable when proven and/or probable reserves are determined to exist. A review of each exploration license or field is carried out, at least annually, to ascertain whether proven and/or probable reserves have been discovered. Upon determination of proven and/or probable reserves, intangible exploration and evaluation assets attributable to those reserves are first tested for impairment and then reclassified from exploration and evaluation assets to property, plant and equipment.

Development and production costs:

Items of property, plant and equipment ("PP&E"), which include oil and gas development and production assets, are measured at cost less accumulated depletion and depreciation and accumulated impairment losses. Development and production assets are grouped into CGU for impairment testing. When significant parts of an item of PP&E, including oil and natural gas interests, have different useful lives, they are accounted for as separate items (components).

Gains and losses on disposal of an item of property, plant and equipment, including oil and natural gas interests, are determined by comparing the proceeds from disposal with the carrying amount of PP&E and are recognized in profit or loss.

(ii) Subsequent costs:

Costs incurred subsequent to the determination of technical feasibility and commercial viability and the costs of replacing parts of PP&E are recognized as oil and natural gas interests only when they increase the future economic benefits embodied in the specific asset to which they relate. All other expenditures are recognized in profit or loss as incurred. Such capitalized oil and natural gas interests generally represent costs incurred in developing proved and/or probable reserves and bringing in or enhancing production from such reserves, and are accumulated on a

field or geotechnical area basis. The carrying amount of any replaced or sold component is derecognized. The costs of the day-to-day servicing of property, plant and equipment are recognized in profit or loss as incurred.

(iii) Depletion and depreciation:

The net carrying value of development or production assets is depleted using the unit of production method by reference to the ratio of production in the year to the related proved plus probable reserves, taking into account estimated future development costs necessary to bring those reserves into production. Future development costs are estimated taking into account the level of development required to produce the reserves. These estimates are reviewed by independent reserve engineers at least annually.

Other corporate assets are recorded at cost on acquisition and amortized on a declining-balance basis at rates of 20 percent to 50 percent per year.

(iv) Exploration and evaluation expense:

Upon determination that an exploration and evaluation asset is impaired, the Company will transfer costs associated with the applicable asset to exploration and evaluation expense in the period.

e) Impairment

(i) Financial assets:

A financial asset is assessed at each reporting date to determine whether there is any objective evidence that it is impaired. A financial asset is considered to be impaired if objective evidence indicates that one or more events have had a negative effect on the estimated future cash flows of that asset. 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 original effective interest rate. Individually significant financial assets are tested for impairment on an individual basis. The remaining financial assets are assessed collectively in groups that share similar credit risk characteristics. All impairment losses are recognized in profit or loss. An impairment loss is reversed if the reversal can be related objectively to an event occurring after the impairment loss was recognized. For financial assets measured at amortized cost the reversal is recognized in profit or loss.

(ii) Non-financial assets:

The carrying amounts of the Company's non-financial assets, other than E&E assets and deferred tax assets, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated. For goodwill, an impairment test is completed each year.

E&E assets are assessed for impairment when they are reclassified to property, plant and equipment, and also if facts and circumstances suggest that the carrying amount exceeds the recoverable amount. For the purpose of impairment testing, assets are grouped together into CGUs being 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 CGU. The recoverable amount of an asset or a CGU 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. Value-in-use is generally computed by reference to the present value of the future cash flows expected to be derived from production of proved plus probable reserves. Any goodwill acquired in an acquisition, for the purpose of impairment testing,

is allocated to the CGUs that are expected to benefit from the synergies of the combination. E&E assets are allocated to related CGUs when they are assessed for impairment, both at the time of any triggering facts and circumstances as well as upon their eventual reclassification to PP&E.

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 first to reduce the carrying amount of any goodwill allocated to the units and then to reduce the carrying amounts of the other assets in the unit (group of units) on a pro-rata basis.

An impairment loss in respect of PP&E and E&E assets, recognized in prior years, is 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 depletion and depreciation or amortization, if no impairment loss had been recognized. An impairment loss in respect of goodwill is not reversed.

f) Share based payments

The grant date fair value of options granted to employees is recognized as compensation expense, with a corresponding increase in contributed surplus over the vesting period. A forfeiture rate is estimated on the grant date and is adjusted to reflect the actual number of options that vest. Share-based payments to non-employees are measured at the fair value of the goods or services received, unless the fair value cannot be estimated reliably.

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. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the liability. Provisions are not recognized for future operating losses.

h) Decommissioning obligations:

The Company's activities give rise to dismantling, decommissioning and site disturbance re-mediation activities. Provision is made for the estimated cost of site restoration and capitalized in the relevant asset category. Decommissioning obligations are measured at the present value of management's best estimate of expenditure required to settle the present obligation at the balance sheet date. Subsequent to the initial measurement, the obligation is adjusted at the end of each period to reflect the passage of time and changes in the estimated future cash flows underlying the obligation. The increase in the provision due to the passage of time is recognized as finance costs whereas increases/decreases due to changes in the estimated future cash flows are capitalized. Actual costs incurred upon settlement of the decommissioning obligations are charged against the provision to the extent the provision was established.

i) Revenue

Presently, the Company has no revenues. However, it proposes to record any future revenues from the sale of oil and natural gas when the significant risks and rewards of ownership of the product is transferred to the buyer which is usually when legal title passes to the external party.

Royalty income, if any will be recognized as it accrues in accordance with the terms of the overriding royalty agreements.

j) Finance income and expenses

Finance expense comprises interest expense on borrowings, accretion of the discount on provisions and impairment losses recognized on financial assets.

Borrowing costs incurred, except those that pertain to Exploration and Evaluation assets, for the construction of qualifying assets are capitalized during the period of time that is required to complete and prepare the assets for their intended use or sale. All other borrowing costs are recognized in profit or loss using the effective interest method. The capitalization rate used to determine the amount of borrowing costs to be capitalized is the weighted average interest rate applicable to the Company's outstanding borrowings during the period.

Interest income is recognized as it accrues in profit or loss, using the effective interest method.

k) Income tax

Income tax expense comprises current and deferred tax. Income tax expense is recognized in profit or loss except to the extent that it relates to items recognized directly in equity, in which case it is recognized in equity.

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

Deferred tax is recognized using the balance sheet method, providing for 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 on the initial recognition of assets or liabilities in a transaction that is not a business combination. In addition, deferred tax is not recognized for taxable temporary differences arising on the initial recognition of goodwill.

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, 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 to the extent that it is probable that future taxable profits will be available against which the temporary difference 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.

l) Earnings per share

Basic earnings per share 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. Diluted earnings per share is determined by adjusting the profit or loss attributable to common shareholders and the weighted average number of common shares outstanding for the effects of dilutive instruments such as options granted to employees.

m) Mineral property interests

All costs related to the acquisition, exploration and development of mineral property interests were capitalized by property. If economically recoverable ore reserves were developed, capitalized costs of the related property were reclassified as mining assets and amortized using the units of production method. When a property was abandoned, all related costs were written off to operations. When a

property was placed into commercial production, deferred costs were depleted using the units of production method.

n) Recent accounting standards and interpretations issued but not yet effective

Unless otherwise stated, the following pronouncements from the IASB will become effective for financial reporting periods beginning on or after January 1, 2013. All of these new or revised standards permit early adoption with transitional arrangements depending upon the date of initial application.

IFRS-9 - *Financial Instruments* issued in November 2009 and amended in October 2010 introduces new requirements for the classification and measurement of financial assets and financial liabilities and for de-recognition. IFRS-9 is expected to be published in three parts. The first part, Phase 1 – classification and measurement of financial instruments sets out the requirements for recognizing and measuring financial assets, financial liabilities and some contracts to buy or sell non-financial items. Phase 1 simplifies the measurement of financial assets by classifying all financial assets as those being recorded at amortized cost or being recorded at fair value. Phase 1 is effective for periods beginning on or after January 1, 2015, although earlier adoption is allowed. Except for certain additional disclosures, the adoption of this standard is not expected to have an impact on the Company's financial statements.

In 2011, the International Accounting Standards Board ("IASB") issued the following new and revised IFRSs effective for annual periods beginning on or after January 1, 2013. Earlier application is permitted providing that IFRS-10, IFRS-11, IFRS-12, IAS-27 and IAS-28 are adopted together, except that IFRS-12 may be adopted earlier. The Company is currently assessing the impact of adopting these pronouncements. The Company is assessing the impact of these new standards will have on its consolidated financial statements.

IFRS-10 - *Consolidated Financial Statements* builds on existing principles by identifying the concept of control as the determining factor in whether an entity should be included within the consolidated financial statements of the parent company. The standard provides additional guidance to assist in the determination of control where this is difficult to assess. IFRS-10 replaces those parts of IAS-27 Consolidated and Separate Financial Statements (revised 2011) that address when and how an entity should prepare consolidated financial statements and replaces SIC-12 Consolidation – Special Purpose Entities in its entirety. IAS-27 retains the current guidance for separate financial statements.

IFRS-11 - *Joint Arrangements* provides for a more substance based reflection of joint arrangements by focusing on the rights and obligations of the arrangement, rather than its legal form (as is currently the case). The standard addresses inconsistencies in the reporting of joint arrangements by requiring a single method to account for interests in jointly controlled entities. IFRS-11 supersedes IAS-31 Interests in Joint Ventures and SIC-13 Jointly Controlled Entities – Non-Monetary Contributions by Ventures. IAS-28 Investments in Associates and Joint Ventures (revised 2011) has been amended to conform to changes based on the issuance of IFRS-10 and IFRS-11.

IFRS-12 - *Disclosure of Interests in Other Entities* requires extensive disclosures relating to an entity's interests in subsidiaries, joint arrangements, associates and unconsolidated structured entities. An entity is required to disclose information that helps users of its financial statements evaluate the nature of and risks associated with its interests in other entities and the effects of those interests on its financial statements. The effective date of IFRS-12 is January 1, 2013 but entities are permitted to incorporate any of the new disclosures in their financial statements before that date.

IFRS-13 - *Fair Value Measurement* establishes a single framework for measuring fair values. This standard applies to all transactions and balances (whether financial or non-financial) for which IFRS requires or permits fair value measurements, with the exception of share-based payment transactions

accounted for under IFRS-2 Share-based Payment and leasing transactions within the scope of IAS-17 Leases. IFRS-13 defines fair value, provides guidance on its determination and introduces consistent requirements for disclosures on fair value measurements.

4. Determination of fair values

A number of the Company's accounting policies and disclosures require the determination of fair value, for both financial and non-financial assets and liabilities. Fair values have been determined for measurement and/or disclosure purposes based on the methods described below. When applicable, further information about the assumptions made in determining fair values is disclosed in the notes specific to that asset or liability.

a) Property, plant and equipment ("PP&E") and intangible exploration and evaluation ("E&E") assets:

The fair value of PP&E recognized in an acquisition is based on market values. The market value of PP&E is the estimated amount for which property, plant & equipment could be exchanged on the acquisition date between a willing buyer and a willing seller in an arm's length transaction after proper marketing wherein the parties had each acted knowledgeably, prudently and without compulsion. The market value of oil and natural gas interests (included in PP&E) is estimated with reference to the discounted cash flows expected to be derived from oil and natural gas production based on externally prepared reserve reports. The risk-adjusted discount rate is specific to the asset with reference to general market conditions. The market value of exploration and evaluation assets is estimated based on either internally or externally prepared evaluations of these assets.

b) Cash and cash equivalents, accounts receivable and accounts payable.

The fair value of cash and cash equivalents, accounts receivable and accounts payable are estimated as the present value of future cash flows, discounted at the market rate of interest at the reporting date. At July 31, 2012 and July 31, 2011, the fair value of these balances approximated their carrying values due to their short term to maturity.

c) Stock options:

The fair value of employee stock options is measured using a Black Scholes option pricing model. Measurement inputs include share price on measurement date, exercise price of the instrument, expected volatility (based on weighted average historic volatility adjusted for changes expected due to publicly available information), weighted average expected life of the instruments (based on historical experience and general option holder behavior), expected dividends, and the risk-free interest rate (based on government bonds).

5. Exploration and evaluation interests

Exploration and evaluation interests consist of two components as follows:

	July 31 2012	July 31 2011
	$	$
Holloman Farm-in Agreement acquisition costs	**941,616**	-
Deferred Seismic Earn-in Obligation expenditures	**132,980**	-
Effects of translation of foreign accounts	**54,736**	
	1,129,332	-

a) Farm-in Agreement

The purchase price paid for the E&E rights totaled $996,352 included cash payments that totaled $351,165 (US$350,000), 1,000,000 common shares having a market value of $250,000, an

A$100,000 (approximately C$105,000) contingency for Australian stamp duties (note 5(d) below), transaction costs including directly attributable due diligence and legal fees of $235,448.

The salient terms of the Farm-in Agreement require staged payments into trust against earn-in obligations as follows:

Earn-in Obligation stage	Due date	Trust account payment	Working interest earned on completion
		A$	
Seismic	May 11, 2012	4,700,000	20%
Initial 3 - Well Program	November 1, 2012	4,500,000	5.8333% per well
Option 3 - Well Program	later of March 1, 2013 or 45 days after completion of initial well program	4,500,000	5.8333% per well
Total		**13,700,000**	**up to 55%**

The above referenced working interests cover interests earned in both PEL 112 and 444. The A$4,500,000 Payment on the Initial 3 - Well Program Earn-in Obligation was made on November 1, 2012.

The above referenced trust account payments with respect to each of the Initial and Option Well Programs are to cover estimated total dry-hole costs for each Program. The Company is liable for any dry hole cost overruns incurred pursuant to the Initial 3 - Well Program and up to a maximum of the first A$4,500,000 and 55% thereafter in dry-hole costs incurred pursuant to the Option 3 - Well Program. Completion, equipping and costs to tie into a hydrocarbon gathering system (if available) shall be borne Terra Nova as to 50% and by the Farmors as to 50%. Under the terms of the Farm-in Agreement, Terra Nova shall be entitled to 80% of the revenues earned from each of the wells drilled under the Initial Well Program and the Option Well Program until such time as it shall have recovered 100% associated with the drilling and testing of each respective well.

Any trust funds remaining on account at the end of each of the above three phases shall be applied first as to the funding of any succeeding trust obligation and in the event that Terra Nova elects not to proceed with any of the succeeding phases, any unspent trust funds shall be for the account of the Company. Notwithstanding anything in the joint operating agreement, Terra Nova shall act as operator of the PEL's and shall have the exclusive right to propose to carry out all exploration and development work on these properties, including without limitation seismic work area clearance, Seismic Earn-in Obligation, the Initial Well Program, the Option Well Program and the completion and subsequent operation of any wells.

The Farm in Agreement also contains various provisions in clauses for such matters as site restoration and non-participation that are typical in the oil and gas exploration industry.

b) Seismic projects

On May 11, 2012 Terra Nova paid the initial A$4,700,000 into trust to cover costs to complete a seismic program sufficient to meet the minimum seismic acquisition requirements for each of PEL 112 and 444 and the interpretation of the acquired data. Any amounts incurred pursuant to the Seismic Earn-in Obligation in excess of A$4,700,000 shall be borne by Terra Nova as to 55% and by

the Farmors as to 45%. As at July 31, 2012, the balance in the trust account amounted to A$4,393,543 (approximately C$4,629,037).

Immediately upon execution of the Farm-in Agreement on May 11 2012, the Company, as operator, implemented a plan of action to complete the seismic work required with respect to Seismic Earn-in Obligation. As at July 31, 2012, in addition to a A$250,000 (approximately C$263,400) deposit on account with a seismic contractor, the Company had made seismic expenditures totaling $132,980.

c) Initial 3 - Well Program Earn-in Obligation

As at November 1, 2012, the Company had made the A$4,500,000 due pursuant to the Initial 3 - Well Program Earn-in Obligation.

d) Contingencies and commitments

Although the Company believes that it has title to its E&E interests, and has taken reasonable precautions appropriate in the circumstances, it cannot control or completely protect itself against the risk of title disputes or challenges. In addition, under South Australian State law, the transfer of E&E interests are subject to assessment of a 5.5% stamp duty. As at November 27, the Company had not yet secured such assessment on the transfer of its interests on execution of the Farm-in Agreement. However, as at July 31, 2012, the Company has taken a provision of $105,000 (A$100,000) which has been included in accounts payable and accruals.

As at July 31, 2012, the Company had advanced A$250,000 (approximately $263,400) on account against a seismic contractual commitment that commenced during August 2012. The funds were subsequently applied on account in consideration for services provided.

Further, in order to earn all of the 55% working interests contemplated under the Farm in Agreement, the Company is required to incur minimum Earn-in Obligation expenditures in the order of A$13,700,000 ($4.5 million of which is remains to be paid at November 27, 2012) and possibly more in seismic, and dry-hole cost overruns before any provision for its share of the related costs to test, complete, and bring wells to production where merited.

6. Mineral property interest

In the period since the Reactivation, the Company incurred total expenditures of $66,270 in order to retain an option on an undivided 50% interest in a gold prospect known as the El Capitan Property ("El Capitan"). Prior to the end of May 2012, in conjunction with its announced intention to become an oil and gas exploration issuer, the Company exercised its right to terminate the El Capitan Option Agreement by giving 30 days written notice of such termination to AMC. Upon abandonment of this interest, the Company wrote off a total of $66,270 it had incurred on El Capitan.

7. Share capital

a) Authorized:

An unlimited number of common shares without par value.

b) October 2012 Financing

On October 19, 2012, the Company announced the October 2012 Financing pursuant to the terms of a non-brokered private placement under which the Company proposed to offer up to 10,000,000 units at a price of $0.20 per unit to result in gross proceeds of up to $2,000,000. Each unit consists of one common share and one non-transferable share purchase warrant entitling the holder thereof to purchase one additional common share at a price of $0.30 each for a period of 24 months from closing (a "November 2014 Unit Warrant'). A Finder's fee consisting of a 5% cash payment and a 5% Finder's warrant (the "November 2014 Finder's Warrants") is payable on sale of certain of the units

offered. The November 2014 Finder's Warrants are exercisable on the same basis as the November 2014 Unit Warrants.

On October 31, 2012, the Company completed a partial closing of the October 2012 Financing upon the sale of 3,500,000 units resulting in the receipt of gross proceeds of $700,000. As of November 27, 2012, the Company had closed on the sale of a total of an additional 2,550,000 units resulting in additional gross proceeds of $510,000 for combined gross receipts pursuant to the October 2012 Financing $1,210,000 on the sale of 6,050,000 units.

As at November 27,2012, under the terms of the October 2012 Financing, the Company was committed to pay $60,500 in finder's fees and issue 302,500 November 2014 Finder's Warrants.

Proceeds from the October 31, 2012 closing amounting to approximately $700,000 were combined with funds on hand to fund the A$4,500,000 Initial 3 - Well Program Earn-in Obligation that was due on November 1, 2012 and for general working capital purposes. Proceeds from closings subsequent to October 31, 2012 totaling $510,000 were used for general working capital purposes and to repay $300,000 in promissory demand notes extended on October 31, 2012 from two directors (note 11).

c) May 2012 Financing

On May 11, 2012, pursuant to the terms of an agency agreement, the Company completed the May 2012 Financing that resulted in gross proceeds of $10,652,075 on the issuance of 42,608,300 units at a price of $0.25 each (the "Agency Agreement"). Each unit consists of one common share and one non-transferable share purchase warrant entitling the holder thereof to purchase one additional common share at a price of $0.30 each at any time up until May 11, 2014 (a "May 2014 Unit Warrant"). Under the terms of the Agency Agreement, the agent was entitled to a cash commission equal to 8% of gross proceeds ($852,166) plus an option to purchase 3,408,664 common shares at a price of $0.25 at any time up until and including May 11, 2014, being 8% of the total number of units sold (the "May 2014 Agent Option"). In addition to the 8% cash commission, the Company has incurred cash issue costs amounting to another $452,229 to cover the Company's related legal, printing, filing, and audit expenses as well as out-of-pocket costs incurred by the Agent amounting to $76,948 to result in net proceeds to the Company of $9,384,680.The fair market value of the May 2014 Agent Options totaled $583,712

The allocation of unit proceeds from the May 2012 Financing was made using the relative residual fair value method under which the estimated fair market value of the warrants is determined using the Black Scholes option pricing model (the "Black Scholes Unit Warrant Value"). The Black Scholes Unit Warrant Value is then added to the quoted market value of the shares and taken as a ratio of the total and applied to the unit offering price to arrive at the Relative Value of the Unit Warrants. The Relative Value of the Unit Warrants is then deducted from the unit offering price to yield the Residual Value of the financing proceeds attributable to the shares. On this basis, $3,719,959 of the gross proceeds from the May 2012 Financing have been allocated as warrant proceeds with the residual balance of $6,932,117 credited to share capital.

The assumptions used in applying the Black-Scholes option pricing model included the prevailing market value of $0.30 per share, volatility of 100%, expected life of 2 years, a risk-free interest rate of 1.5% and a strike price of $0.30 per share and an expected dividend rate of nil.

d) December 2010 Reactivation Financing

On December 30, 2010, immediately following the Share Consolidation, the Company completed a non-brokered private placement of 10,245,000 units at a price of $0.15 per unit, for aggregate gross proceeds of $1,536,750. Each unit consisted of one common share and one share purchase warrant entitling the holder thereof to acquire one additional share at a price of $0.30 each at any time up until and including December 30, 2012 (the "December 2012 Unit Warrants"). The proceeds from each unit were allocated as to $0.145 cents per share and as to $0.005 per share purchase warrant.

As of November 23, 2012, the TSX V had approved the Company's application to extend the expiry date on 10,245,000 December 2012 Unit Warrants exercisable at a price of $.30 each from December 30, 2012 to June 30, 2013. All other terms of the warrants, including the exercise price of $0.30 each will remain the same.

A finder's fee consisting of 988,000 units was paid ("December 2010 Finder's Units") for a gross consideration of $148,200. In addition, the Company incurred related issuance costs totaling $14,505 that was paid in cash.

The finder's fee consideration was determined on the basis of $0.145 for each of the shares attached to the Finder's Units and the value of each warrant attached to the Finder's Units was $0.005 ("December 2010 Finder's Warrants").

e) Per share amounts

Per share amounts have been calculated using the weighted average number of common shares outstanding. The weighted average number of common shares outstanding for the year ended July 31, 2012 is 23,730,789 (July 31, 2011 - 9,421,046). The average number of common shares outstanding was not increased for outstanding stock options and warrants as the effect would be anti-dilutive.

f) Warrants and Agent Options outstanding

Changes in the balance of warrants and Agent Options outstanding during the year ended July 31, 2012 were as follows:

	Weighted average exercise price per share	Remaining life	Number issuable
	$	(years)	(shares)
Total warrants and agent options outstanding, July 31, 2011	0.30	1.42	11,233,000
Exercised during the year	-	-	-
Issued during the year	0.30	1.78	46,016,964
Total warrants and agent options outstanding, July 31, 2012	0.30	1.51	57,249,964

As at July 31, 2012, the balance of warrants and Agent Options outstanding was as follows:

	Expiry date	Weighted average exercise price per share	Remaining life	Number issuable
		$	(years)	(shares)
December 2012 Unit Warrants	as extended from December 30, 2012 to June 30, 2013	0.30	0.92	10,245,000
December 2012 Finder's Unit Warrants	December 30, 2012	0.30	0.42	988,000
May 2014 Unit Warrants	May 11, 2014	0.30	1.78	42,608,300
May 2014 Agent Options	May 11, 2014	0.25	1.78	3,408,664
		0.30	1.60	57,249,964

In the event that the common shares trade at a price of $0.70 each for 20 consecutive trading days on the TSX-V, the expiry date of the May 2014 Unit Warrants can be accelerated upon 30 days notice from the Company to subscribers.

In addition to the above, as at November 27, 2012, under the provisions of the October 2012 Financing, the Company had issued 6,050,000 November 2014 Unit Warrants exercisable at a price of $0.30 each and 302,500 November 2014 Finder's Warrants exercisable at a price of $0.30 each for a period of 24 months from the date of issue.

g) Incentive Stock Options

On completion of the Reactivation, Company shareholders approved a revised incentive stock option plan (the "Incentive Stock Option Plan"). Incentive Under the Stock Option Plan, the Company may grant options to directors, officers, employees, independent contractors or consultants. The number of options outstanding at any time may not be more than 10% of the issued and outstanding shares of the Company. The exercise price associated with each option granted is determined by the Company and is subject to the policies of the TSX Venture Exchange. The maximum term of each option's life is 10 years. Any options granted are vested at the discretion of the board of directors, or in the case of options granted to consultants performing investor relations activities (as defined), options will vest over a minimum of 12 months with no more than one quarter of such options vesting in any three-month period.

On May 16, 2012, the Company granted 10-year stock options to officers and directors and independent consultants to purchase 2,750,000 options exercisable at a price of $0.30 each of which half vest immediately and the remainder have an 18 month vesting period (the "May 2022 Stock Options). Subject to vesting the May 2022 Stock Options can be exercised at any time up until and including May 16, 2022. In consideration for the May 2022 Stock Options, the Company recorded stock-based compensation expenses totaling $265,918. The estimated fair value of these options was determined using the Black-Scholes option pricing model using the following assumptions: a prevailing market price of $0.25; a risk-free interest rate 2.0%; an expected life of 4 years; an expected volatility of 100%, and an expected dividend rate of nil.

On February 1, 2011, stock options to purchase up to 760,000 shares of the Company at a price of $0.53 each for a period of 10 years were granted under the provisions of the Incentive Stock Option Plan in consideration for which the Company recorded stock-based compensation expenses totalling $278,618 (the "February 2021 Stock Options"). The estimated fair value of these options was

determined to be $0.173 each using the Black-Scholes option pricing model under the following assumptions: a prevailing market price of $0.53 per share; a risk-free interest rate of 1.43%; an expected life of 4.0 years; expected volatility of 100%; and an expected dividend rate of nil.

In conjunction with the completion of the May 2012, holders of the February 2021 Stock Options agreed to forfeit 760,000 stock options.

As at July 31, 2012, the balance of Incentive stock Options outstanding was as follows:

	Expiry date	Weighted average exercise price per share	Remaining life	Number issuable
		$	(years)	(shares)
May 2022 Incentive Stock Options	May 16, 2022	0.30	9.80	2,750,000

Changes in the balance of Incentive Stock Options outstanding during the year ended July 31, 2012 were as follows:

	Weighted average exercise price per share	Remaining life	Number issuable
	$	(years)	(shares)
Total incentive options outstanding, July 31, 2011	0.53	(111.66)	760,000
Exercised during the year	-	-	-
Forfeited during the year	0.53	-	(760,000)
Granted May 16, 2012	0.30	9.80	2,750,000
Total incentive options outstanding, July 31, 2012	0.30	9.80	2,750,000

Vesting privileges on the May 2022 Incentive Stock Options are: immediately when granted as to 50%; and on November 16, 2013 as to 50%.

8. Key management compensation

The retention of certain key management personnel is subject to management agreements that expire on April 30, 2015 unless terminated earlier in accordance with the terms of each respective contract. Upon resignation at the Company's request or in the event of a change of control, these agreements provide for termination benefits that can include up to 12 month's basic remuneration plus provisions for payments in lieu of any benefits and otherwise forfeited on early termination.

Some key management personnel, or their related parties, may hold positions in other entities whose services are retained by the Company. In such instances, these appointments result in the Company's key management personnel representing those related parties in which they hold control or significant influence over the financial or operating policies of these entities. Details of transactions with these related parties can be found in note 11.

Key management includes current and former senior officers and directors (executive and non-executive) of the Company. The Company incurred the following expenditures for services and short term benefits provided to the Company by key management as follows:

	2012	2011
	$	$
Non-audit accounting fees	**28,621**	11,715
Management fees	**100,000**	23,500
Exploration and evaluation interests	**148,042**	-
Share Issuance costs	**53,780**	14,505
Share-based compensation	**212,734**	278,618
	543,177	328,338

The amounts charged were the exchange amounts, which was the amount of consideration established and agreed upon by the parties.

Included in accounts payable and accrued liabilities as at July 31, 2012 is $92,548 (July 31, 2011 - $150; August 1, 2010 - $696,566) due to the related parties. The amounts owing were unsecured, non-interest bearing and due on demand.

9. Financial risk management

The Company's activities expose it to a variety of financial risks that arise as a result of its exploration, development, production, and financing activities such as:

- Credit risk
- Market risk
- Liquidity risk

The following discussion presents information about the Company's exposure to each of the above risks, the Company's objectives, policies and processes for measuring and managing risk, and the Company's management of capital. Further quantitative disclosures are included throughout these financial statements.

The Board of Directors oversees managements' establishment and execution of the Company's risk management framework. Management has implemented and monitors compliance with risk management policies. The Company's risk management policies are established to identify and analyze the risks encountered by the Company, to set appropriate risk limits and controls, and to monitor risks and adherence to market conditions and the Company's activities.

Credit risk

Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Company's receivables from joint venture partners and oil and natural gas marketers. The maximum exposure to credit risk at year-end is as follows:

	July 31 2012	July 31 2011
	$	$
Funds deposited on account	**263,400**	-

- Funds deposited on account / trade and other receivables:

At July 31, 2012, the Company's credit risk related to funds deposited on account with a service provider pursuant to a contractual commitment and Cash held-in-trust with an Australian bank to fund teh Company's seismic program.

Receivables from participants in the petroleum and natural gas sector, and collection of the outstanding balances can be impacted by industry factors such as commodity price fluctuations, limited capital availability and unsuccessful drilling programs. As operator, the Company will not typically obtain collateral from petroleum and natural gas marketers or joint venture partners; however the Company will generally cash call on major projects and does have the ability, in most cases, to withhold production from joint venture partners in the event of non-payment, or withhold accounts payable remittances.

The total carrying amount of accounts receivable and funds deposited on account as at July 31, 2012 totalled A$250,000 (approximately C$263,400) (July 31, 2011 - nil) represented the maximum credit exposure. As at July 31, 2012 and July 31, 2011, the Company did not have any receivables and consequently the Company does not consider any receivables to be past due.

Market risk

Market risk is the risk that changes in market conditions, such as commodity prices, foreign exchange rates and interest rates will affect the Company's income or the value of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while maximizing the Company's return.

- Foreign currency exchange rate risk:

Foreign currency exchange rate risk is the risk that the fair value of future cash flows will fluctuate as a result of changes in foreign exchange rates. As at July 31, 2012, cash held-in-trust totalling A$4,393,543 (approximately C$4,629,037 related to the Seismic Earn-in expenditure obligation. Going forward, future petroleum and natural gas sales and production operations, if any, will be conducted primarily in Australia and denominated in Australian dollars. As such, the Company is exposed to any fluctuations in the Australian dollar to Canadian dollar exchange rate.

- Interest rate risk:

Interest rate risk is the risk that future cash flows will fluctuate as a result of changes in market interest rates. Except to the extent that the balance of cash held-in trust as at July 31, 2012 totalling A$4,393,543 (approximately C$4,629,037) is earning interest at the rate of approximately 4%, the Company has no financial instruments that could otherwise be exposed to interest rate risk.

- Commodity price risk:

Commodity price risk is the risk that future cash flows will fluctuate as a result of changes in commodity prices. Commodity prices for petroleum and natural gas are impacted by the relationship between the Canadian dollar and Australian dollar, the Canadian dollar and United States dollar, and global economic events that dictate the levels of supply and demand.

Liquidity risk:

Liquidity risk is the risk that the Company will encounter difficulty in meeting obligations associated with its financial liabilities. The Company's financial liabilities consist of accounts payable and accruals. Accounts payable consists of invoices payable to trade suppliers for office, State of South Australia stamp transfer taxes, field operating activities and capital expenditures. The Company processes invoices within a normal payment period. Accounts payable have contractual maturities of less than one year. The Company maintains and monitors a certain level of cash flow which is used to finance all operating and capital expenditures.

Capital management:

The Company's objective when managing capital is to maintain a flexible capital structure which allows it to execute its growth strategy through strategic acquisitions and expenditures on exploration and development activities while maintaining a strong financial position. The Company's capital structure includes working capital and shareholders' equity. Currently, total capital resources available include

working capital which as at July 31, 2012 included cash held-in trust pursuant to the terms of the Farm-in Agreement.

In addition to the possibility of securing additional joint working interest partners, that would result in a dilution of the Company's E&E interests, the Company is largely reliant on junior resource venture capital markets for additional financing requirements. There can be no assurance that funding from this source can be secured at any given time; or, if available, in quantities and under terms that meet Company requirements or that are acceptable to the Company.

The Company's capital expenditure includes expenditures in oil and gas activities which may or may not be successful. The Company makes adjustments to the capital structure in light of changes in economic conditions, and in the immediate term, the results of seismic data collected over the course of completing the Seismic Earn-in Obligation and the related proposed Post Earn-in Seismic Obligation as well as the risk characteristics of the underlying petroleum and natural gas assets. In order to maintain or adjust the capital structure, the Company may, from time to time, issue shares, adjust its capital spending or issue debt instruments. The Company is not subject to any externally imposed capital requirements other than covenants pursuant to the Farm-in Agreement.

Terra Nova has not utilized bank loans or debt capital to finance capital expenditures to date, nor can the Company be expected to be in a position to secure a loan / credit facility against production and cash flow in Australia at least until such time as the Company has demonstrable reserves and commercially viable production, if ever.

10. Income taxes

The Company's effective tax rate differs from the amount obtained by applying statutory rates to the reported losses due to the following:

	2012	2011
Statutory tax rate	**25.63%**	27.33%
	$	$
Income tax recovery at statutory rates	**179,000**	116,000
Tax rate adjustments and foreign exchange differences	**(4,000)**	-
Non deductible items and other	**69,000**	(70,000)
Unrecognized benefit of tax attributes	**(244,000)**	(46,000)
	-	-

The decrease in statutory income tax rates from 2011 to 2012 was due to a rate reduction in the 2012 Canadian corporate tax rates as a result of changes in tax legislation previously enacted by the Canadian federal government.

Deductible temporary differences for which no deferred income tax assets have been recognized as at July 31, 2012 and 2011 are as follows:

	2012	**2011**
	$	$
Mineral property interests	**8,865,000**	8,972,000
Share issue costs	**1,576,000**	12,000
Non capital loss carryforwards	**3,313,000**	2,484,000
Other	**558,000**	-
	14,312,000	11,468,000

Deferred income tax assets have not been recognized in respect of the above temporary differences because it is not probable that future taxable profits will be available against which the Company can utilize the benefit. The unrecognized deferred tax asset relates to Canada. The Company continues to earn tax deductions in Australia.

The Company has non capital losses in Canada of approximately $3.3 million which may be available to offset future income for income tax purposes which expire in various years from 2014 to 2032.

11. Related parties

Following execution of the Farm-in Agreement, the chairman of the corporation that acts as the principal representative for the farmor group was appointed as a Company director. Since that time, Terra Nova has not entered into any transactions or commitments with that corporation other than as they pertain to transactions incurred pursuant to the terms of the Farm-in Agreement.

On October 31, 2012, pursuant to the terms of 3% demand promissory notes with two Company directors, the Company received a total of $300,000. Proceeds from the notes were used primarily to fund the A$4,500,000 Earn-in Obligation that was due and paid on November 1, 2012 to fund dry hole costs associated with the Initial 3-Well Program Earn-in Obligation. As of November 27, 2012, the Company had repaid the 3% demand promissory notes in full.

Since April 30, 2012, Terra Nova's Chief Operating Officer who is retained on a management consulting fee as included in the disclosure under "Key management compensation" - note 8 is also the chief operating decision-maker for the Company's primary geological consulting firm, Apex Energy Consultants Inc. ("Apex") who the Company has retained as a consultant pursuant to the terms of a formal agreement As at July 31, 2012, under the terms of the this agreement the Company had paid a total of $198,401 to Apex that included a total of $98,401 for services and out-of-pocket expenses charged to the Company other than amounts charged with respect to a monthly retainer entitlement. All payments to Apex other than out-of-pocket expenses have been included in the disclosure presented under key management compensation in note 8.

In addition, the Company's wholly-owned subsidiaries are considered to be related parties. Upon consolidation of its accounts, the Company eliminates the effect of any intercompany transactions with these companies. The Company has no other subsidiary interests, the accounts of which have been excluded from these consolidated financial statements.

12. Supplemental cash flow information

	2012	2011
	$	$
Non-cash financing (investing) transactions:		
Accounts payable and accruals used to fund E&E Interest expenditures	**164,911**	-
Shares issued to fund E&E Interest acquisition costs	**250,000**	-
Estimated maket value attributed to Agent Options included in issue costs	**583,712**	-
Increase in contributed surplus recognized on Agent Option value	**(583,712)**	-
Non-cash consideration paid for E&E Interests	(414,911)	-
	-	**-**
Cash payments information:		
Interest	**-**	-
Income taxes	**-**	-

13. First-time adoption of IFRS

The Company's financial statements for the year ending July 31, 2012 are its first annual financial statements prepared in accordance with IFRS. The Company adopted IFRS on August 1, 2011 with transition date of August 1, 2010 (the "Transition Date") under the provisions of IFRS 1 - *'First-time Adoption of International Financial Reporting Standards'*, whereby IFRS is applied retrospectively at the Transition Date with all adjustments to assets and liabilities as stated under Canadian GAAP taken to deficit unless certain exemptions are applied. The Company has elected to apply the following exemptions to:

- not restate business combinations that occurred prior to the Transition Date and the accounting thereof;
- not restate the accounting for any compound financial instruments issued and settled by the Company prior to the Transition Date; and
- apply IFRS 2 - *'Share-based Payments'*, to liabilities arising from share-based payment transactions that were settled before the Transition Date.

After applying the above exemptions, the Company did not recognize any adjustments on transition to IFRS as at August 1, 2010 as follows:

	Balance on Transition to IFRS **August 1 2010**	Adjustments on transition to IFRS August 1 2010	As reported under CGAAP July 31 2010
	$	$	$
Total assets	**27,365**	-	27,365
Total liabilities	**949,002**	-	949,002
Shareholder deficiency	**(921,637)**	-	(921,637)

14. Segmented information

Management has presented segmented information on a geographical basis as this is the basis upon which the chief executive officer makes operating decisions.

	July 31 2012	July 31 2011	August 31 2010
	$	$	$
Total assets:			
Canada	**4,222,952**	484,191	27,365
Australia	**6,068,273**	-	-
	10,291,225	484,191	27,365
Net (loss) income:			
Canada	**(703,543)**	(424,554)	
Australia	**4,320**	-	
	(699,223)	(424,554)	
Capital expenditures:			
Canada	**17,869**	48,401	
Australia	**707,656**	-	
	725,525	48,401	