yangarra resources ltd.

Yangarra Resources Ltd.

Interim Consolidated Financial Statements

March 31, 2010 and 2009

(Unaudited – Prepared by Management)

Notice of No Auditor Review of Interim Consolidated Financial Statements

In accordance with National Instrument 51-102 released by the Canadian Securities Administrators, the Company discloses that its auditors have not reviewed these unaudited interim consolidated financial statements as at and for the three months ended March 31, 2010 and 2009.

		March 31 2010		December 31 2009
Assets				
Current				
Accounts receivable	$	**607,202**	$	658,080
Prepaid expenses and deposits		**158,185**		152,853
		765,387		810,933
Property and equipment *(note 3)*		**41,618,103**		38,830,516
	$	**42,383,490**	$	39,641,449
Liabilities				
Current				
Bank debt *(note 4)*	$	**4,773,199**	$	8,195,069
Accounts payable and accrued liabilities		**1,490,751**		465,554
Commodity price risk contracts *(note 9)*		**–**		113,361
		6,263,950		8,773,984
Asset retirement obligation *(note 5)*		**2,229,560**		2,181,727
Preferred shares *(note 6(b))*		**1,012,329**		1,000,000
Future income tax liability		**737,558**		837,357
		10,243,397		12,793,068
Shareholders' Equity				
Share capital *(note 6)*		**46,917,278**		43,019,290
Warrants *(note 7)*		**2,283,216**		340,600
Contributed surplus *(note 8)*		**2,993,797**		2,972,097
Deficit		**(20,054,198)**		(19,483,606)
		32,140,093		26,848,381
	$	**42,383,490**	$	39,641,449

Nature of operations and basis of presentation *(note 1)*

Subsequent events *(note 17)*

Yangarra Resources Ltd.
Interim Consolidated Statements of Operations, Comprehensive Loss and Deficit
For the three months ended March 31
(unaudited)

	2010	2009
Revenue		
Petroleum and natural gas sales	$ **1,009,188**	$ 1,025,969
Royalties	**(40,588)**	(63,731)
Royalty recoveries *(note 10)*	**–**	175,636
	968,600	1,137,874
Commodity price risk contracts *(note 9)*	**186,861**	101,296
	1,155,461	1,239,170
Expenses and other items		
Production	**272,876**	302,517
Transportation	**48,893**	29,750
General and administrative	**223,379**	147,830
Interest and financing fees	**61,655**	251,780
Dividends *(note 6(b))*	**12,329**	–
Stock-based compensation *(note 6(c))*	**21,700**	–
Depletion and depreciation	**1,017,707**	1,045,374
Accretion	**42,385**	36,236
Other (income) expenses	**25,129**	(6,979)
	1,726,053	1,806,508
Loss before income taxes	**(570,592)**	(567,338)
Income taxes		
Future income tax recovery	**–**	162,288
Net loss and comprehensive loss for the period	**(570,592)**	(405,050)
Deficit, beginning of period	**(19,483,606)**	(12,215,586)
Deficit, end of period	$ **(20,054,198)**	$ (12,620,636)
Net loss per share – basic and diluted	$ **(0.00)**	$ (0.01)
Weighted average number of shares – basic and diluted	**199,384,474**	75,561,912

The accompanying notes are an integral part of these unaudited interim consolidated financial statements

		2010		2009
Operating				
Net loss for the period	$	**(570,592)**	$	(405,050)
Add back (deduct) non-cash items				
Unrealized gain on commodity price risk contracts		**(113,361)**		(101,296)
Interest and financing fees		**–**		26,676
Dividends		**12,239**		–
Stock-based compensation		**21,700**		–
Depletion and depreciation		**1,017,707**		1,045,374
Accretion		**42,385**		36,236
Unrealized gain on investment		**–**		(6,979)
Future income tax recovery		**–**		(162,288)
		410,168		432,673
Change in non-cash working capital *(note 11)*		**199,763**		(18,131)
		609,931		414,542
Financing				
Issue of equity instruments, net of issue costs		**5,740,805**		–
Bank debt (repayment) proceeds, net		**(3,499,755)**		225,676
Financing fees		**–**		(270,000)
		2,241,050		(44,324)
Investing				
Expenditures on property and equipment		**(3,799,846)**		(298,013)
Change in non-cash working capital *(note 11)*		**948,865**		(72,205)
		(2,850,981)		(370,218)
Change in cash during the period		**–**		–
Cash, beginning of period		**–**		–
Cash, end of period	$	**–**	$	–

Supplemental cash flow information				
Interest paid	$	**61,655**	$	233,515

The accompanying notes are an integral part of these unaudited interim consolidated financial statements

1. Nature of operations and basis of presentation

Yangarra Resources Ltd. (the "Company") is a publicly traded company involved in the production, exploration and development of resource properties in Western Canada. These unaudited interim consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries, Yangarra Resources Corp. ("YRC") and Athabaska Energy Ltd. ("Athabaska") after the elimination of intercompany transactions and balances.

These unaudited interim consolidated financial statements have been prepared on a going concern basis which contemplates the realization of assets and the payment of liabilities in the ordinary course of business. As at March 31, 2010, the Company had a working capital deficiency of $5,498,563 (December 31, 2009 – $7,963,051) and an accumulated deficit of $20,054,198 (December 31, 2009 – $19,483,606). Should the Company be unable to continue as a going concern, it may be unable to realize the carrying value of its assets and to meet its liabilities as they become due. The Company's ability to continue as a going concern is dependent upon its ability to attain profitable operations and generate funds therefrom and to continue to obtain capital financing from investors sufficient to meet current and future obligations.

2. Significant accounting policies

These unaudited interim consolidated financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles and on a basis consistent with the audited December 31, 2009 consolidated financial statements except certain disclosures have been condensed or omitted. Accordingly, these unaudited interim consolidated financial statements should be read in conjunction with the notes contained in the Company's audited December 31, 2009 consolidated financial statements. Because a precise determination of many assets and liabilities is dependent upon future events, the preparation of periodic financial statements necessarily involves the use of estimates and approximations. Accordingly, actual results could differ from those estimates.

3. Property and equipment

March 31, 2010	*Cost*	*Accumulated depletion and depreciation*	*Net book value*
Petroleum and natural gas properties	$ 73,932,413	$ 32,390,091	$ 41,542,322
Office equipment	286,925	211,144	75,781
	$ 74,219,338	$ 32,601,235	$ 41,618,103

December 31, 2009	*Cost*	*Accumulated depletion and depreciation*	*Net book value*
Petroleum and natural gas properties	$ 70,134,763	$ 31,380,391	$ 38,754,372
Office equipment	279,281	203,137	76,144
	$ 70,414,044	$ 31,583,528	$ 38,830,516

3. Property and equipment (continued)

At March 31, 2010, the Company excluded $1,064,824 (December 31, 2009 – $1,206,467) of resource properties relating to unproved properties from the depletion calculation. Unproved properties have been separately evaluated by management for impairment. In addition, $11,070,600 (December 31, 2009 – $11,055,300) of future development costs were included in the depletion calculation.

During the period ended March 31, 2010, the Company capitalized $5,488 (2009 – nil) related to the asset retirement obligation of property and equipment. The Company also capitalized $35,908 (2009 – $11,763) of general and administrative costs as well as related costs of the Company's working interest in operated capital expenditure programs on which operator's fees have been charged in accordance with standard industry operating agreements.

4. Bank debt

As at March 31, 2010, the maximum availability of the revolving operating demand loan is $8,195,000 (December 31, 2009 – $8,300,000) after monthly reductions based on the Company's excess cash flow (as defined in the loan agreement) which commenced on January 31, 2010. Interest on the revolving operating demand loan is at bank prime plus 1%.

As at March 31, 2010, the $4,773,199 (December 31, 2009 – $8,195,069) reported amount of bank debt was comprised of $4,700,000 (December 31, 2009 – $7,800,000) drawn on the revolving operating demand loan and $73,199 (December 31, 2009 – $395,069) of bank overdraft.

The Company is subject to a financial covenant with respect to working capital, which the Company was in compliance with at March 31, 2010. The annual renewal date of the bank debt is May 31, 2010.

5. Asset retirement obligation

The following table presents the reconciliation of the carrying amount of the obligation associated with the retirement of the Company's property and equipment:

Asset retirement obligation, December 31, 2009	$	2,181,727
Additions		5,448
Accretion		42,385
Asset retirement obligation, March 31, 2010	$	2,229,560

The following significant assumptions were used to estimate the asset retirement obligation:

Undiscounted cash flows	$	4,295,892
Discount rate		7% - 10%
Inflation rate		2%
Weighted average expected timing of cash flows		10.1 years

6. Share capital

a) Common shares issued

	Number of shares	*Amount*
Balance, December 31, 2009	186,940,030	$ 43,019,290
Unit private placement *(i)*	80,000,000	4,009,700
Exercise of warrants *(ii)*	1,400,000	187,684
Share issue costs, net of $99,799 of future income tax	–	(299,396)
Balance, March 31, 2010	268,340,030	$ 46,917,278

i) On March 17, 2010, the Company completed a private placement of 80,000,000 Units at $0.075 per Unit for gross proceeds of $6,000,000. Each Unit is comprised of one common share of the Company and one half of one common share purchase warrant, with each full warrant exercisable anytime up to March 15, 2012, at a price of $0.10 per share, subject to certain earlier termination provisions. Management and directors subscribed for 13,356,669 Units for gross proceeds of $1,001,750 or 16% of the financing. Finder's fees of $364,480 were paid in conjunction with the financing. The common shares and warrants issued and the common shares issuable on the exercise of the warrants are all subject to hold periods expiring on July 17, 2010.

At the time of issuance, the fair value of the warrants was estimated to be $1,990,300 ($0.05 per warrant) based on the Black-Scholes fair value pricing model (note 6(d)) and $4,009,700 was ascribed to common shares.

ii) In January 2010, the Company issued 1,400,000 common shares on the exercise of 1,400,000 warrants at $0.10 per share for cash proceeds of $140,000 plus a pro-rata allocation of the options' fair value in the amount of $47,684.

b) Preferred shares issued

As at March 31, 2010 and December 31, 2009, the Company had 1,000,000 preferred shares issued and outstanding with an annual dividend rate of 5% payable semi-annually in common shares of the Company. The preferred shares have an eighteen month term, at which time they are redeemable for $1,000,000 cash.

The $1,012,239 reported amount of preferred shares at March 31, 2010 is comprised of the $1,000,000 redemption value plus $12,139 of accrued dividends.

As the terms of the preferred shares provide for a mandatory redemption at a fixed amount, they are classified as a financial liability. The March 31, 2010 estimated fair value of preferred shares approximates their carrying value and redemption value.

c) Stock options

On January 7, 2010, the Company granted 500,000 stock options to a director. The options are exercisable at $0.10 per share, vest immediately and expire five years from the date of grant. The estimated fair value of the options was estimated at $21,700 ($0.04 per option) using the Black-Scholes pricing model (note 6(d)), all of which has been recognized as stock-based compensation in the period.

6. Share capital (continued)

c) Stock options (continued)

The following tables summarize information about stock options outstanding as at March 31, 2010:

	Number of Options	*Weighted – average exercise price*
Opening	17,711,275	$ 0.15
Granted	500,000	0.10
Expired	(318,250)	(0.74)
Forfeited	(175,000)	(0.28)
Closing	17,718,025	$ 0.14

Range of exercise price	*Number outstanding*	*Weighted-average remaining contractual life (years)*	*Weighted-average exercise price*	*Number exercisable*
$ 0.10 – $ 0.34	16,844,000	4.26	$ 0.12	16,844,000
$ 0.45 – $ 0.50	799,025	0.66	0.50	799,025
$ 0.71	75,000	0.84	0.71	75,000
	17,718,025	4.08	$ 0.14	17,718,025

d) Black-Scholes pricing model

The Black-Scholes pricing model calculations during the three months ended March 31, 2010 were based on the following significant assumptions:

Risk-free interest rate	1.59% to 2.75%
Expected volatility	146%
Expected life	2 to 5 years

7. Warrants

The following table summarizes information about warrants outstanding as at March 31, 2010:

	Number of warrants	*Weighted average exercise price*	*Fair value ascribed*
Balance – December 31, 2009	10,000,000	$ 0.10	$ 340,600
Issued *(note 6(a)(i))*	40,000,000	0.10	1,990,300
Exercised *(note 6(a)(ii))*	(1,400,000)	(0.10)	(47,684)
Balance – March 31, 2010	48,600,000	$0.10	$ 2,283,216

As at March 31, 2010, warrants had a weighted average remaining life of 2.73 years.

8. Contributed surplus

Balance, December 31, 2009	$	2,972,097
Stock-based compensation *(note 6(c))*		21,700
Balance, March 31, 2010	$	2,993,797

9. Commodity price risk contracts

As at January 1, 2010, the Company was committed to the following commodity price risk contracts for the sale of natural gas:

- 1,000 GJ per day from January 1 to January 31, 2010 at a fixed price of $5.51 per GJ;
- 1,000 GJ per day from February 1 to February 28, 2010 at a fixed price of $5.53 per GJ; and
- 500 GJ per day from January 1 to December 31, 2010 at a fixed price of $5.68 per GJ.

In addition the Company sold calls which provided a ceiling for the price it received for natural gas as follows:

- 500 GJ per day from January 1 to December 31, 2010 at the ceiling price of $6.25 per GJ;
- 500 GJ per day from March 1 to December 31, 2010 at the ceiling price of $6.50 per GJ; and
- 500 GJ per day from March 1 to December 31, 2010 at the ceiling price of $6.70 per GJ.

In March 2010, the Company settled all outstanding commodity price risk contracts for proceeds of $73,500 and reported an unrealized gain of $113,361 related to the reversal of the mark-to-market liability recognized at December 31, 2009.

Included in petroleum and natural gas revenue for the three months ended March 31, 2010 is $31,131 of realized gains (2009 – nil) on the fulfilled portion of the commodity contracts.

10. Royalty recoveries

During the three months ended March 31, 2009, the Company recognized a recovery in the amount of $175,636 of freehold and gross overriding royalties calculated and paid in previous years.

11. Change in non-cash working capital

Three months ended March 31		*2010*		*2009*
Accounts receivable	$	50,878	$	228,835
Prepaid expenses and deposits		(5,332)		(13,622)
Accounts payable and accrued liabilities		1,103,082		(305,549)
	$	1,148,628	$	(90,336)

The change in non-cash working capital has been allocated to the following activities:

Three months ended March 31		*2010*		*2009*
Operating	$	199,763	$	(18,131)
Investing		948,865		(72,205)
	$	1,148,628	$	(90,336)

12. Related party transactions

Except as disclosed elsewhere in these financial statements, the Company had the following related party transactions:

During the three months ended March 31, 2010 and 2009, the Company was charged or invoiced the following amounts by certain of its officers and directors and by companies controlled by certain of the Company's officers and directors:

		2010		*2009*
Administration and consulting fees	$	31,305	$	21,118
Production and capital expenditures	$	341,524	$	37,088

Included in accounts payable and accrued liabilities at March 31, 2010 is $7,554 (December 31, 2009 – $12,000) relating to the above transactions. These transactions were in the normal course of operations and were measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties.

13. Financial instruments and financial risk management

The Company's financial instruments include accounts receivable, investment, accounts payable and accrued liabilities, bank debt, credit facility and preferred shares (note 6(b)). The carrying values of accounts receivable, accounts payable and accrued liabilities, bank debt and credit facility approximate their fair values due to their relatively short periods to maturity.

The Company is required to classify fair value measurements using a hierarchy that reflects the significance of the inputs used in making the measurements. The fair value hierarchy is as follows:

- Level 1 - quoted prices in active markets for identical assets or liabilities;
- Level 2 - inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly; and
- Level 3 - inputs for the asset or liability that are not based on observable market data.

The Company's risk management policies are established to identify and analyze the risks faced by the Company, to set appropriate risk limits and controls, and to monitor risks and adherence to market conditions and the Company's activities. The Company has exposure to credit risk, liquidity risk and market risk as a result of its use of financial instruments. This note presents information about the Company's exposure to each of the above risks and the Company's objectives, policies and processes for measuring and managing these risks. Further quantitative disclosures are included throughout these financial statements.

The Board of Directors has overall responsibility for the establishment and oversight of the Company's risk management framework. The Board has implemented and monitors compliance with the risk management policies as set out herein:

13. Financial instruments and financial risk management (continued)

a) 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. A substantial portion of the Company's accounts receivable are with natural gas and liquids marketers and joint venture partners in the oil and gas industry and are subject to normal industry credit risks. Purchasers of the Company's natural gas and liquids are subject to credit review to minimize the risk of non-payment. As at March 31, 2010, the maximum credit exposure is the carrying amount of the accounts receivable and accruals of $607,202 (December 31, 2009 – $658,080). As at March 31, 2010, the Company's receivables consisted of $280,117 from joint venture partners and other trade receivables and $327,085 of revenue receivable from petroleum and natural gas marketers.

Receivables from petroleum and natural gas marketers are typically collected on the 25th day of the month following production. The Company's policy to mitigate credit risk associated with these balances is to establish marketing relationships with large purchasers. The Company historically has not experienced any significant collection issues with its petroleum and natural gas marketers. All of the revenue accruals and receivables from petroleum and natural gas marketers were received in April and May 2010.

Joint venture receivables are typically collected within one to three months of the joint venture bill being issued to the partner. The Company mitigates the risk from joint venture receivables by obtaining partner approval of capital expenditures prior to starting a project. However, the receivables are from participants in the petroleum and natural gas sector, and collection is dependent on typical industry factors such as commodity price fluctuations, escalating costs and the risk of unsuccessful drilling. Further risk exists with joint venture partners as disagreements occasionally arise which increases the potential for non-collection.

For properties that are operated by the Company, production can be withheld from joint venture partners who are in default of amounts owing. In addition, the Company often has offsetting amounts payable to joint venture partners from which it can net receivable balances.

The Company did not provide for any doubtful accounts nor was it required to write-off any receivables during the period ended March 31, 2010. The Company would only choose to write-off a receivable balance (as opposed to providing an allowance) after all reasonable avenues of collection had been exhausted.

As at March 31, 2010, the Company considers its receivables to be aged as follows:

Not past due	$	387,462
Past due by less than 90 days		17,008
Past due by more than 90 days		202,732
	$	607,202

b) Liquidity risk

Liquidity risk is the risk that the Company will incur difficulties meeting its financial obligations as they are due. The Company's approach to managing liquidity is to ensure, as far as possible, that it will have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions without incurring unacceptable losses or risking harm to the Company's reputation.

13. Financial instruments and financial risk management (continued)

b) Liquidity risk (continued)

The Company prepares annual capital expenditure budgets, which are regularly monitored and updated as considered necessary. The Company uses authorizations for expenditures on both operated and non-operated projects to further manage capital expenditures. To facilitate the capital expenditure program, the Company has a revolving reserve-based bank facility, as disclosed in note 4, which is regularly reviewed by the lender. The Company monitors its total debt position monthly. The Company also attempts to match its payment cycle with collection of petroleum and natural gas revenues on the 25th of each month. The Company anticipates it will have adequate liquidity to fund its financial liabilities through its future cash flows. The Company's financial liabilities are comprised of accounts payable and accrued liabilities, bank debt and the credit facility, which have expected maturities of less than one year resulting in their current classification on the balance sheet.

c) Market risk

Market risk consists of interest rate risk, currency risk and commodity price risk. The objective of market risk management is to manage and control market risk exposures within acceptable limits, while maximizing returns. The Company may use both financial derivatives and physical delivery sales contracts to manage market risks. All such transactions are conducted in accordance with a risk management policy as set out herein:

i) Interest rate risk
Interest rate risk is the risk that future cash flows will fluctuate as a result of changes in market interest rates. The Company is exposed to interest rate fluctuations on its bank debt which bears interest at a floating rate. For the three months ended March 31, 2010, if interest rates had been 1% lower with all other variables held constant, earnings for the period would have been $15,411 (2009 – $21,082) higher, respectively, due to lower interest expense. An equal and opposite impact would have occurred had interest rates been higher by the same amounts. The Company had no interest rate swap or financial contracts in place at March 31, 2010.

ii) Currency risk
Foreign currency exchange rate risk is the risk that the fair value or future cash flows will fluctuate as a result of changes in foreign exchange rates. All of the Company's petroleum and natural gas sales are denominated in Canadian dollars; however, the underlying market prices in Canada for petroleum and natural gas are impacted by changes in the exchange rate between the Canadian and United States dollar. The Company had no outstanding forward exchange rate contracts in place at March 31, 2010.

iii) Commodity price risk
Commodity price risk is the risk that the fair value or future cash flows will fluctuate as a result of changes in commodity prices. Commodity prices for petroleum and natural gas are impacted by world economic events that dictate the levels of supply and demand as well as the relationship between the Canadian and United States dollar, as outlined above. The Company's commodity price risk contracts are disclosed in note 9.

14. Capital management

The Company's objective when managing capital is to maintain a flexible capital structure which will allow it to execute its capital expenditure program, which includes expenditures in oil and gas activities which may or may not be successful. Therefore, the Company monitors the level of risk incurred in its capital expenditures to balance the proportion of debt and equity in its capital structure.

The Company considers its capital structure to include:

	March 31 2010	*December 31 2009*
Working capital deficiency	$ (5,498,563)	$ (7,963,051)
Shareholders' equity	32,015,093	26,848,381
	$ 26,516,530	$ 18,885,330

The Company monitors capital based on annual funds from operations and capital expenditure budgets, which are updated as necessary and are reviewed and periodically approved by the Company's Board of Directors.

The Company manages its capital structure and makes adjustments by continually monitoring its business conditions including the current economic conditions, the risk characteristics of the Company's petroleum and natural gas assets, the depth of its investment opportunities, current and forecasted net debt levels, current and forecasted commodity prices and other facts that influence commodity prices and funds from operations such as quality and basis differentials, royalties, operating costs and transportation costs.

In order to maintain or adjust the capital structure, the Company considers its forecasted funds from operations while attempting to finance an acceptable capital expenditure program including acquisition opportunities, the current level of bank credit available from the Company's lender, the level of bank credit that may be attainable from its lender as a result of petroleum and natural gas reserve growth, the availability of other sources of debt with different characteristics than existing debt, the sale of assets, limiting the size of the capital expenditure program and the issue of new equity if available on favorable terms.

At March 31, 2010, the Company's capital structure is subject to external restrictions as a result of the loan agreement with the Company's senior lender described in note 7 of the Company's audited December 31, 2009 consolidated financial statements. As a result, the Company's approach to capital management has changed to ensure compliance with the Loan Agreements. The Company's bank facility is determined by the senior lender and based on the lender's borrowing base model and the Company's petroleum and natural gas reserves.

The Company has not paid or declared any dividends on common shares since the date of incorporation, nor are any contemplated in the foreseeable future.

15. Contingency

In December 2009, the Company terminated the Standstill Agreement that it had with an industry partner regarding a joint producing property and served that industry partner with a Statement of Claim to the Court of Queen's Bench of Alberta, to which the Company claims breach of the agreements between the parties, gross negligence and default of operator. The Company seeks judgment for specified and such further damages to be determined by the court, as well as appointment as operator. The industry partner has indicated it plans to file a Statement of Defense and Counterclaim. The potential outcome of the lawsuit and claims are undetermined however they may be material. As the likely outcome of this litigation cannot be determined at this time, no provision has been made in these consolidated financial statements.

16. Commitment

During the period ended March 31, 2010, the Company incurred all of the $500,000 of qualifying flow-through expenditures required pursuant to flow-through shares issued in December 2009 that will be renounced effective December 31, 2010.

17. Subsequent events

a) On April 28, 2010, the Company received TSX-V Exchange approval for the consolidation of the common shares of the Company on a five old for one new (5:1) basis. Effective April 30, 2010, the Company's stock commenced trading under the new symbol "YGR" on a five old for one new consolidated basis.

b) On May 1, 2010, the Company and Athabaska were amalgamated and continue to carry on business under the name Yangarra Resources Ltd.

c) On May 21, 2010, the Company completed a private placement of 3,745,454 flow-through common shares at $0.55 per share for gross proceeds of $2,060,000. An 8% cash commission was paid on the sale of the associated funds raised.