

Alberta Oilsands Inc.

CONSOLIDATED FINANCIAL STATEMENTS

DECEMBER 31, 2007 AND 2006

AUDITORS' REPORT TO THE SHAREHOLDERS

We have audited the consolidated balance sheets of Alberta Oilsands Inc. as at December 31, 2007 and 2006 and the consolidated statements of operations and deficit and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2007 and 2006 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

“signed KPMG LLP”

Chartered Accountants

Calgary, Canada

April 10, 2008

Alberta Oilsands Inc.
Consolidated Balance Sheets
December 31

Assets	<u>2007</u>	<u>2006</u>
Current		
Cash and cash equivalents (<i>note 4</i>)	\$ 11,445,658	\$ 4,868
Accounts receivable	634,043	796,327
Prepaid expenses	323,293	158,297
Commodity contract (<i>note 5</i>)	–	48,030
Deferred financing fees (<i>note 8</i>)	–	19,643
	<u>12,402,994</u>	<u>1,027,165</u>
Property and equipment (<i>notes 6 and 13</i>)	<u>24,680,605</u>	<u>11,396,512</u>
	<u>\$ 37,083,599</u>	<u>\$ 12,423,677</u>
 Liabilities		
Current		
Accounts payable and accrued liabilities	\$ 4,738,332	\$ 1,243,214
Bank debt (<i>note 7</i>)	–	2,100,000
Bridge facility (<i>note 8</i>)	–	1,000,000
	<u>4,738,332</u>	<u>4,343,214</u>
Asset retirement obligation (<i>note 9</i>)	838,186	967,497
Future income taxes (<i>note 14</i>)	425,858	281,297
	<u>6,002,376</u>	<u>5,592,008</u>
 Shareholders' Equity		
Share capital (<i>note 10</i>)	32,793,456	8,567,290
Contributed surplus (<i>note 12</i>)	3,173,984	395,841
Deficit	<u>(4,886,217)</u>	<u>(2,131,462)</u>
	<u>31,081,223</u>	<u>6,831,669</u>
	<u>\$ 37,083,599</u>	<u>\$ 12,423,677</u>

Basis of presentation (*note 1*)

Commitments (*note 18*)

Subsequent events (*note 20*)

On behalf of the Board

Signed "Shabir Premji"

Director

Signed "Michael Lee"

Director

See accompanying notes to the consolidated financial statements.

Alberta Oilsands Inc.
Consolidated Statements of Operations and Deficit
For the years ended December 31

	<u>2007</u>	<u>2006</u>
Revenue		
Petroleum and natural gas sales	\$ 2,980,974	\$ 5,766,744
Commodity contract (note 5)	(48,030)	48,030
Royalties	(488,752)	(667,800)
	<u>2,444,192</u>	<u>5,146,974</u>
Interest income	295,904	719
	<u>2,740,096</u>	<u>5,147,693</u>
Expenses		
Production	924,167	1,118,633
Transportation	101,397	337,370
General and administrative	2,083,049	1,212,252
Business development (note 15)	227,737	641,930
Stock-based compensation (note 10)	2,380,158	205,389
Financing fees (note 8)	194,643	–
Interest	155,450	137,023
Accretion	60,941	67,613
Depletion and depreciation	1,730,103	3,502,086
	<u>7,857,645</u>	<u>7,222,296</u>
Loss before the undernoted	(5,117,549)	(2,074,603)
Gain on disposal of property and equipment (note 13)	2,244,439	–
Loss before income taxes	(2,873,110)	(2,074,603)
Future income tax reduction (note 14)	118,355	654,194
	<u>(2,754,755)</u>	<u>(1,420,409)</u>
Net loss for the year	(2,754,755)	(1,420,409)
Deficit, beginning of year	(2,131,462)	(711,053)
Deficit, end of year	\$ (4,886,217)	\$ (2,131,462)
Net loss per share		
Basic and diluted (note 10)	\$ (0.06)	\$ (0.05)

See accompanying notes to the consolidated financial statements.

Alberta Oilsands Inc.
Consolidated Statements of Cash Flows
For the years ended December 31

	<u>2007</u>	<u>2006</u>
Operating		
Net loss for the year	\$ (2,754,755)	\$ (1,420,409)
Non-cash items:		
Commodity contract	48,030	(48,030)
Bridge facility fee (<i>note 8</i>)	150,000	27,500
Stock-based compensation	2,380,158	205,389
Accretion	60,941	67,613
Depletion and depreciation	1,730,103	3,502,086
Future income tax reduction	(118,355)	(654,194)
Gain on disposal of property and equipment	(2,244,439)	–
Abandonment expenditures	–	(6,284)
	<u>(748,317)</u>	<u>1,673,671</u>
Change in non-cash working capital (<i>note 16</i>)	<u>166,554</u>	<u>146,495</u>
	<u>(581,763)</u>	<u>1,820,166</u>
Financing		
Issuance of shares, net of costs	24,060,634	2,978,923
Bank debt proceeds (repayment)	(2,100,000)	1,507,557
Bridge facility proceeds (repayment)	(1,000,000)	1,000,000
Change in non-cash working capital (<i>note 16</i>)	15,382	11,487
	<u>20,976,016</u>	<u>5,497,967</u>
Investing		
Expenditures on property and equipment	(20,221,545)	(4,534,398)
Proceeds from disposal of property and equipment	7,937,969	–
Change in non-cash working capital (<i>note 16</i>)	3,330,113	(2,779,367)
	<u>(8,953,463)</u>	<u>(7,313,765)</u>
Increase in cash and cash equivalents	11,440,790	4,368
Cash and cash equivalents, beginning of year	<u>4,868</u>	<u>500</u>
Cash and cash equivalents, end of year	\$ 11,445,658	\$ 4,868
Supplemental cash flow information:		
Interest paid	<u>\$ 82,211</u>	<u>\$ 133,393</u>

See accompanying notes to the consolidated financial statements.

Alberta Oilsands Inc.

Notes to Consolidated Financial Statements

December 31, 2007 and 2006

1. Basis of presentation and future operations

Alberta Oilsands Inc. ("the Company") is incorporated under the Business Corporations Act (Alberta) and is listed on the TSX Venture Exchange. The Company is involved in the production, exploration and development of resource properties. The Company operated as Platform Resources Inc. prior to May 29, 2007, when shareholders approved a resolution to change the name of the Company to Alberta Oilsands Inc. These consolidated financial statements include the accounts of the Company and its wholly owned subsidiary, Platform Resources Inc.

These 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. Property and equipment is recognized in these financial statements in accordance with the accounting policies outlined in note 2. Accordingly, their carrying amounts represent costs incurred to date, net of abandonments and write-downs, and do not necessarily reflect present or future values. In addition, the Company has incurred operating losses over the past two years. The ability of the Company to continue as a going concern and recover amounts shown for the properties is dependent upon the existence of economically recoverable reserves. The Company's ability to continue as a going concern is dependent upon its ability to obtain additional financing to continue the development of the Company's properties and generate funds therefrom and to meet current and future obligations. Should the going concern assumption not be appropriate, certain asset and liability amounts would require adjustment and reclassification.

2. Significant accounting policies

a) Property and equipment

i) Capitalized costs

The Company follows the full cost method of accounting for its petroleum and natural gas operations. Under this method all costs related to the exploration for and development of petroleum and natural gas reserves are capitalized on a country-by-country basis. Costs include lease acquisition costs, geological and geophysical expenses and costs of drilling both productive and non-productive wells. Proceeds from the sale of properties are applied against capitalized costs, without any gain or loss being realized, unless such sale would alter the rate of depletion and depreciation by more than 20%.

ii) Depletion and depreciation

Depletion of petroleum and natural gas properties and depreciation of production equipment, net of estimated salvage or residual value, is provided using the unit-of-production method based upon estimated gross proved petroleum and natural gas reserves as determined by independent engineers. The costs of significant unevaluated properties are excluded from costs subject to depletion. For depletion and depreciation purposes, relative volumes of petroleum and natural gas production and reserves are converted at the energy equivalent conversion rate of six thousand cubic feet of natural gas to one barrel of crude oil.

Office equipment is depreciated on a declining balance basis over its estimated useful life at rates varying from 20% to 45%.

Alberta Oilsands Inc.

Notes to Consolidated Financial Statements

December 31, 2007 and 2006

2. Significant accounting policies (continued)

a) Property and equipment (continued)

iii) Impairment test

Under the full cost method of accounting, a "ceiling test" is performed to recognize and measure impairment, if any, of the carrying amount of petroleum and natural gas properties. Impairment is recognized if the carrying amount of the petroleum and natural gas properties, less the cost of undeveloped properties, net of impairment, exceeds the estimated undiscounted future cash flows from the Company's proved reserves. The future cash flows are based on a forecast of prices and costs, as provided by an independent third party. The magnitude of the impairment, if any, is then measured by comparing the carrying amount of petroleum and natural gas properties less the cost of undeveloped properties, net of impairment, to the estimated discounted future cash flows from the Company's proved and probable reserves. The future cash flows are discounted at the Company's risk-free interest rate, using forecasted prices and costs.

Any impairment recognized is recorded as additional depletion and depreciation expense.

b) Asset retirement obligation

The Company recognizes the fair value of a liability for an asset retirement obligation in the period in which it is incurred and records a corresponding increase in the carrying amount of the related long-lived asset. The fair value is determined through a review of engineering studies, industry guidelines, and management's estimate on a site-by-site basis. The liability is subsequently adjusted for the passage of time, and is recognized as an accretion expense in the consolidated statement of operations and deficit. The liability is also adjusted due to revisions in either the timing or the amount of the original estimated cash flows associated with the liability. The increase in the carrying amount of the asset is amortized using the unit of production method based on estimated gross proved reserves as determined by independent engineers. Actual costs incurred upon settlement of the asset retirement obligations are charged against the asset retirement obligation to the extent of the liability recorded.

c) Flow-through shares

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

d) Future income taxes

The Company follows the asset and liability method of accounting for income taxes. Under this method future tax assets and liabilities are determined based on differences between financial reporting and income tax bases of assets and liabilities, and are measured using substantively enacted tax rates and laws that will be in effect when the differences are expected to reverse. The effect on future tax assets and liabilities of a change in tax rates is recognized in net income (loss) in the period in which the change is substantively enacted. A valuation allowance is recorded against a future income tax asset if it is more likely than not that the asset will not be realized.

e) Joint operations

Substantially all of the exploration, development and production activities of the Company are conducted jointly with others and these financial statements reflect only the Company's proportionate interest in such activities.

Alberta Oilsands Inc.

Notes to Consolidated Financial Statements

December 31, 2007 and 2006

2. Significant accounting policies (continued)

f) Revenue recognition

Petroleum and natural gas sales are recognized as revenue when commodities are delivered to purchasers.

g) Per share amounts

Basic per share amounts are computed by dividing net loss by the weighted average number of common shares outstanding during the year. The Company utilizes the treasury stock method in the determination of diluted per share amounts. Under this method, the diluted weighted average number of shares is calculated assuming that proceeds arising from the exercise of options and other dilutive instruments where the market price exceeds option price are used to purchase, for cancellation, common shares of the Company at their average market price for the period.

h) Stock options

Under the Company's stock option plan described in note 10, options to purchase common shares are granted to directors, employees and consultants at current market prices. Stock-based compensation is recorded over the vesting period of the options with a corresponding amount recorded as contributed surplus. Stock-based compensation for options granted to directors and employees is based on the estimated fair value at the time of the grant. Stock-based compensation for options granted to consultants is based on the estimated fair value at each balance sheet date until the related options are fully vested. Upon the exercise of the stock options, consideration paid together with the amount previously recognized in contributed surplus is recorded as an increase in share capital. In the event that vested options expire unexercised, previously recognized compensation expense associated with such stock options is not reversed. In the event that unvested options are cancelled, previously recognized compensation expense associated with such stock options is reversed.

i) Commodity contracts

Commodity contracts are recorded on the consolidated balance sheet at fair value and changes in fair value are recognized in income in the period in which the change occurs.

j) Deferred financing fees

Fees paid to secure bridge facility financing are deferred and amortized to general and administrative expenses on the consolidated statement of operations and deficit over the term of the related bridge facility.

k) Cash and cash equivalents

Cash and cash equivalents consist of bank balances and term deposits with maturities of three months or less.

l) Measurement uncertainty

The amounts recorded for depletion and depreciation of property and equipment and the ceiling test are based on estimates of gross proved reserves, production rates, oil and gas prices, royalties, future costs and other relevant assumptions. By their nature, these estimates are subject to measurement uncertainty and the impact on the financial statements of changes in such estimates in future periods could be material.

Inherent in the fair value calculation of asset retirement obligations are numerous assumptions and judgments including the ultimate settlement amounts, inflation factors, credit adjusted discount rates, timing of settlement, and changes in the legal and regulatory environments. To the extent future revisions to these assumptions impact the fair value of the existing asset retirement obligation liability, a corresponding adjustment is made to the property and equipment balance.

Alberta Oilsands Inc.

Notes to Consolidated Financial Statements

December 31, 2007 and 2006

3. Changes in accounting policies

On January 1, 2007, the Company adopted the new or revised Canadian accounting standards for accounting changes, financial instruments – recognition and measurement, financial instruments – presentation and disclosures and comprehensive income. The adoption of these standards had no impact on these financial statements.

a) Financial instruments—recognition and measurement

This new standard requires all financial instruments within its scope, including all derivatives, to be recognized on the balance sheet initially at fair value. Subsequent measurement of all financial assets and liabilities except those held-for-trading and available for sale are measured at amortized cost determined using the effective interest rate method. Held-for-trading financial assets are measured at fair value with changes in fair value recognized in earnings. Available-for-sale financial assets are measured at fair value with changes in fair value recognized in comprehensive income and reclassified to earnings when derecognized or impaired.

<u>Held-for-trading</u>	<u>Loans and receivables</u>	<u>Other liabilities</u>
Cash and cash equivalents	Accounts receivable	Accounts payable and accrued liabilities

Derivative instruments, including embedded derivatives, are recorded on the balance sheet at fair value. Changes in the fair values of derivative instruments are recognized in net loss with the exception of derivatives designated as cash flow hedges. The Company did not identify any derivatives which require separate recognition and measurement.

b) Hedges

This new standard specifies the circumstances under which hedge accounting is permissible and how hedge accounting may be performed. On adoption of these standards, the Company did not have any agreements or contracts which are following hedge accounting.

c) Comprehensive income

Comprehensive income is the change in shareholders' equity during a period from transactions and other events and circumstances from non-owner sources and includes unrealized gains and losses on financial assets classified as held available-for-sale. When related amounts are recorded in accordance with this new standard, the Company will report a statement of comprehensive income combined with the statement of operations and a new category, accumulated other comprehensive income, in the shareholders' equity section of the balance sheet.

d) Accounting changes

Voluntary changes in accounting policies are permitted only if they result in financial statements which provide more reliable and relevant information. Accounting policy changes are applied retrospectively unless it is impracticable to determine the period or cumulative impact of the change. Corrections of prior period errors are applied retrospectively and change in accounting estimates are applied prospectively by including the effect of the change in earnings.

Alberta Oilsands Inc.

Notes to Consolidated Financial Statements

December 31, 2007 and 2006

3. Changes in accounting policies *(continued)*

e) Pending accounting pronouncements:

The Company is currently assessing the impact of these following new standards on its consolidated financial statements:

(i) Capital Disclosures and Financial Instruments – Disclosures and Presentation

On December 1, 2006 three new accounting standards were issued by the CICA. These were Capital Disclosures, Financial Instruments – Disclosure and Financial Instruments – Presentation. These new standards will be effective on January 1, 2008.

Capital disclosures specifies the disclosure of (i) an entity's objectives, policies, and processes for managing capital, (ii) quantitative data about what the entity regards as capital, (iii) whether the entity has complied with any capital requirements, and (iv) if it has not complied, the consequences of such non-compliance.

Financial Instruments – Disclosure and Presentation, have revised and enhanced its disclosure requirements, and carrying forward unchanged its presentation requirements. These new sections place increased emphasis on disclosures about the nature and extent of risks arising from financial instruments and how the entity manages those risks.

(ii) International Financial Reporting Standards ("IFRS")

In 2005, the Accounting Standards Board of Canada ("AcSB") announced that accounting standards in Canada are to converge with IFRS. The AcSB has indicated that Canadian entities will need to begin reporting under IFRS by the first quarter of 2011 with appropriate comparative data from the prior year. Under IFRS, the primary audience is capital markets and as a result, there is significantly more disclosure required, specifically for quarterly reporting. Further, while IFRS uses a conceptual framework similar to Canadian GAAP, there are significant differences in accounting policy which must be addressed.

(iii) Inventories

In March 2007, Inventories was adopted which aligns Canadian GAAP with IFRS. This standard will be effective on January 1, 2008.

(iv) Goodwill and Intangible Assets

In January 2008, Goodwill and Intangible Assets was issued to replace Goodwill and Other Intangible Assets and Research and Development Costs. This standard aligns Canadian GAAP with IFRS and will be effective on October 1, 2008.

4. Cash and cash equivalents

	December 31, 2007	December 31, 2006
Cash in bank	\$ 2,106,177	\$ 4,868
Term deposit	9,339,481	–
	<u>\$ 11,445,658</u>	<u>\$ 4,868</u>

The term deposit outstanding as at December 31, 2007 earned interest at a rate of 4.65% and matured in January 2008 at which time it was reinvested at similar terms.

Alberta Oilsands Inc.

Notes to Consolidated Financial Statements

December 31, 2007 and 2006

5. Commodity contract

During 2006, the Company entered into a financial commodity collar for the sale of 100 barrels of oil per day from October 1, 2006 to December 31, 2007 at a ceiling strike price of U.S. \$77.20 per barrel and a floor strike price of U.S. \$60.00 per barrel. In March 2007, the Company had a partial termination of this contract whereby it amended the quantity to 50 barrels of oil per day at the same ceiling and floor strike prices. As at December 31, 2007, the contract was fulfilled and the realized loss of \$18,097 from the contract is included in petroleum and natural gas sales.

6. Property and equipment

	December 31, 2007		
	Cost	Accumulated depletion and depreciation	Net
Petroleum and natural gas properties			
Oil sands properties	\$ 19,129,410	\$ -	\$ 19,129,410
Conventional properties	11,672,612	6,223,500	5,449,112
Office equipment	167,364	65,281	102,083
	<u>\$ 30,969,386</u>	<u>\$ 6,288,781</u>	<u>\$ 24,680,605</u>
	December 31, 2006		
	Cost	Accumulated depletion and depreciation	Net
Petroleum and natural gas properties	\$	\$	\$
Conventional properties	15,861,470	4,524,300	11,337,170
Office equipment	93,720	34,378	59,342
	<u>\$ 15,955,190</u>	<u>\$ 4,558,678</u>	<u>\$ 11,396,512</u>

During 2007 the Company capitalized \$117,083 of general and administrative costs and \$524,367 of stock based compensation and \$152,066 of related future incomes taxes (2006 – \$nil).

At December 31, 2007, the Company excluded \$19,900,230 (2006 - \$489,800) of petroleum and natural gas property costs relating to unproved properties from the depletion and ceiling test calculations. In addition, \$299,400 (2006 - \$213,000) of future development costs have been included in the depletion calculation.

The Company applied the ceiling test to its capitalized assets at December 31, 2007 and determined that there was no impairment. As at September 30, 2007, there was an impairment in the amount of \$211,900 which is included in the depletion expense.

For the purposes of the December 31, 2007 impairment test, the following benchmark prices were used:

	Edmonton Light Cdn\$/bbl	AECO Spot \$/MMbtu
2008	90.00	6.75
2009	87.00	7.25
2010	84.00	7.50
2011	81.00	7.75
2012	81.00	7.75

Alberta Oilsands Inc.
Notes to Consolidated Financial Statements
December 31, 2007 and 2006

7. Bank debt

Upon the disposition of certain properties in March 2007 (note 13), the Company repaid the bank debt in full and the credit facility was cancelled.

8. Bridge facility

Upon the disposition of certain properties in March 2007 (note 13), the Company repaid the bridge facility in full and expensed the remaining unamortized portion of deferred financing fees of \$19,643. The bridge facility was then cancelled.

In October 2007, the Company entered into a new bridge facility with the same lender for a maximum amount of \$5.0 million, maturing on June 30, 2008. The facility bears interest at 9% per annum with a deferred fee of 4% on any amounts repaid under the facility. A commitment fee in the amount of \$175,000 was satisfied by a cash payment of \$25,000 and the issuance of 116,279 common shares of the Company (2006 – 88,710 common shares for a value of \$27,500). The Company had not borrowed any amounts under this facility as at December 31, 2007.

9. Asset retirement obligation

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

	<u>2007</u>	<u>2006</u>
Balance, beginning of year	\$ 967,497	\$ 760,418
Liabilities incurred	30,327	145,435
Dispositions (<i>note 13</i>)	(193,266)	-
Revisions	(27,313)	315
Accretion	60,941	67,613
Liabilities settled	-	(6,284)
Balance, end of year	<u>\$ 838,186</u>	<u>\$ 967,497</u>

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

	<u>2007</u>	<u>2006</u>
Undiscounted abandonment costs	\$ 1,194,100	\$ 1,450,200
Credit adjusted risk-free rate	8%	8%
Inflation rate	2%	2%
Weighted average expected timing of cash flows	3 years	5.6 years

Alberta Oilsands Inc.

Notes to Consolidated Financial Statements

December 31, 2007 and 2006

10. Share capital

a) Authorized

Unlimited number of common shares without nominal or par value

b) Common shares issued

	Number of Shares		Amount
Balance, December 31, 2005	21,059,387	\$	6,193,801
Exercise of warrants (i)	2,904,047		1,426,367
Flow-through private placement (ii)	4,765,000		2,001,300
Financing fee (note 8)	88,710		27,500
Tax effect of flow-through shares	–		(927,912)
Share issue costs (net of tax of \$79,838)	–		(153,766)
Balance, December 31, 2006	28,817,144	\$	8,567,290
Issue of flow-through common shares ((iii) and (iv))	14,848,500		13,000,025
Issue of common shares (iv)	8,888,900		12,000,015
Issue of common shares (v)	232,307		302,000
Exercise of options (vi)	638,968		336,490
Financing fee (note 8)	116,279		150,000
Tax effect of flow-through shares (ii)	–		(587,382)
Share issue costs (net of tax of \$476,532)	–		(974,982)
Balance, December 31, 2007	<u>53,542,098</u>	\$	<u>32,793,456</u>

- (i) In January and February 2006, 2,904,047 shares were issued on the exercise of the same number of warrants at exercise prices of \$0.30 to \$0.45 per common share for gross cash proceeds of \$1,211,227 plus the related fair value previously recorded to contributed surplus in the amount of \$215,140.
- (ii) In June 2006, a private placement was completed for 4,765,000 flow-through common shares at \$0.42 per share for gross proceeds of \$2,001,300. The tax effect of the qualifying expenditures was recognized in 2007 when the renouncement documents were filed with the tax authorities.
- (iii) In May 2007, a private placement was completed for 10,000,000 flow-through common shares at \$0.50 per share for gross proceeds of \$5,000,000. In conjunction with the private placement the Company paid \$50,000 of commissions. Directors and officers subscribed for 1,090,000 flow-through common shares. The Company is required to incur \$5,000,000 in qualifying expenditures by December 31, 2008, of which \$1,323,700 had been incurred at December 31, 2007.
- (iv) In June 2007, a private placement financing was completed for the issuance of 8,888,900 common shares at a price of \$1.35 per share and 4,848,500 flow-through common shares at a price of \$1.65 per share for total gross proceeds of \$20,000,040. In connection with the private placement, the Company paid a commission to the underwriters of approximately \$1.2 million. The Company is required to spend \$8,000,025 in qualifying expenditures by December 31, 2008, none of which had been incurred at December 31, 2007.
- (v) In December 2007, pursuant to a non-brokered private placement, 232,307 common shares at a price of \$1.30 per share were issued for gross proceeds of \$302,000.

Alberta Oilsands Inc.

Notes to Consolidated Financial Statements

December 31, 2007 and 2006

10. Share capital (continued)

(vi) During the year ended December 31, 2007, a total of 638,968 stock options were exercised at exercise prices ranging from \$0.29 to \$0.38 per common share, for total cash proceeds of \$210,108. In addition to the cash proceeds, a pro-rata allocation of the options' fair value in the amount of \$126,382 has been reclassified from contributed surplus to share capital.

(vii) Pursuant to the bridge facility (*note 8*), a total of 116,279 common shares valued at \$1.29 per share were issued.

c) Stock options

The Company has established a stock option plan for its directors, officers, employees and consultants. Pursuant to this plan, the Company is authorized to reserve for issuance up to 10% of its common shares outstanding from time to time. Options expire five years from the date of grant and vest over periods as determined by the board of Directors at the time of grant.

During the year ended December 31, 2007, the Company granted a total of 3,474,373 stock options all of which vested one-third upon grant date and one-third on the first and second anniversaries of the grant date and expire five years from grant date. The total fair value of the options granted was estimated to be \$5,285,329.

The Black-Scholes pricing model was used to estimate the fair value of options granted using a forfeiture rate of 0%, a dividend yield of nil and based on the following significant assumptions:

Weighted average risk-free interest rate	4.38%
Weighted average volatility	151%
Expected life	5 years

The following is a continuity of stock options as at December 31, 2007:

	December 31, 2007		December 31, 2006	
	Options	Weighted average exercise price	Options	Weighted average exercise price
Opening	2,604,000	\$ 0.34	1,221,000	\$ 0.30
Granted	3,474,373	1.84	1,566,000	0.37
Exercised	(638,968)	(0.33)	-	-
Forfeited	(313,000)	(0.34)	(183,000)	(0.32)
Closing	5,126,405	\$ 1.25	2,604,000	\$ 0.34

The following summarizes information about stock options outstanding as at December 31, 2007:

Range of exercise prices	Number outstanding	Weighted average remaining contractual life (years)	Number exercisable	Weighted average exercise price
\$ 0.29 – 0.30	742,000	2.41	642,000	\$ 0.30
0.37 – 0.40	1,129,032	3.67	687,000	0.37
0.45 – 0.67	331,000	4.31	112,333	0.62
0.89 – 1.30	530,000	4.75	176,667	1.26
1.47 – 1.91	1,166,373	4.40	388,791	1.86
1.92 – 2.21	1,228,000	4.60	409,333	2.21
	5,126,405	4.03	2,416,124	\$ 1.25

Alberta Oilsands Inc.
Notes to Consolidated Financial Statements
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10. Share capital (continued)

c) Stock options (continued)

The Company recognized stock-based compensation expense in the year ended December 31, 2007 for the following option grants:

Year of option grant	Weighted average value per share	Year ended December 31, 2007
2005	\$0.31	\$ 7,425
2006	\$0.47	206,566
2007	\$1.52	2,690,534
		<u>2,904,525</u>
Capitalized to property and equipment (<i>note 6</i>)		(524,367)
Expense		<u>\$ 2,380,158</u>

d) Per share amounts

Basic per share amounts are calculated using the weighted average number of shares outstanding of 42,765,794 for the year ended December 31, 2007 (year ended December 31, 2006 – 25,964,131). In computing diluted per share amounts for the years ended December 31, 2007 and 2006 all of the Company's outstanding options were excluded as they were considered to be anti-dilutive.

11. Warrants

	Number of Warrants	Amount
Balance, December 31, 2005	3,637,518	\$ 262,437
Exercise of warrants (<i>note 10(b)i</i>)	(2,904,047)	(215,140)
Expiry of warrants	(733,471)	(47,297)
Balance, December 31, 2006 and 2007	<u>–</u>	<u>\$ –</u>

12. Contributed surplus

Balance, December 31, 2005	\$ 143,155
Stock-based compensation expense	205,389
Expiry of warrants (<i>note 10</i>)	<u>47,297</u>
Balance, December 31, 2006	\$ 395,841
Stock-based compensation expense (<i>note 10 (c)</i>)	2,380,158
Capitalized stock-based compensation (<i>note 10 (c)</i>)	524,367
Options exercised (<i>note 10 (b)</i>)	<u>(126,382)</u>
Balance, December 31, 2007	<u>\$ 3,173,984</u>

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13. Gain on disposal of property and equipment

The Company disposed of certain properties in March 2007 for net proceeds of \$7.8 million. The gain recorded for the disposal has been estimated at \$2.2 million. In addition, the Company disposed of \$193,266 of its asset retirement obligations pursuant to the disposition.

14. Income taxes

The Company's computation of income taxes is as follows:

	<u>2007</u>	<u>2006</u>
Expected income tax reduction at 32.83% (2006 – 34.25%)	\$ (943,242)	\$ (710,552)
Crown payments	–	34,214
Resource allowance	–	(66,384)
Stock-based compensation expense	790,936	70,346
Changes in enacted tax rates and other	<u>33,951</u>	<u>18,182</u>
Future income reduction	<u>\$ (118,355)</u>	<u>\$ (654,194)</u>

The components of the net future income tax liability at December 31, 2007 are as follows:

	<u>2007</u>	<u>2006</u>
Non-capital loss carryforwards	\$ 477,220	\$ 121,400
Asset retirement obligation	246,008	314,146
Share issue costs	421,839	134,872
Property and equipment	<u>(1,570,925)</u>	<u>(851,715)</u>
Future income tax liability	<u>\$ (425,858)</u>	<u>\$ (281,297)</u>

As at December 31, 2007 the Company has approximately \$17.8 million in tax pools and \$1.6 million in non-capital losses available for deduction against future taxable income. Non-capital losses expire between 2008 and 2014.

15. Business development expenses

During the year ended December 31, 2007 the Company incurred \$227,737 (2006 – \$641,930) of business development expenses related to the pursuit of projects outside of the conventional Canadian oil and gas exploration and development business. These expenses include consulting and related costs as well as costs associated with the on-going pursuit of additional financing to support any potential transactions.

16. Change in non-cash working capital

	<u>2007</u>	<u>2006</u>
Accounts receivable	\$ 162,284	\$ 429,847
Prepaid expenses	(164,996)	(108,051)
Deferred financing fees	19,643	(19,643)
Accounts payable and accrued liabilities	<u>3,495,118</u>	<u>(2,923,538)</u>
	<u>\$ 3,512,049</u>	<u>\$ (2,621,385)</u>

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16. Change in non-cash working capital (continued)

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

	2007	2006
Operating	\$ 166,554	\$ 146,495
Financing	15,382	11,487
Investing	3,330,113	(2,779,367)
	<u>\$ 3,512,049</u>	<u>\$ (2,621,385)</u>

17. Related parties

Except as disclosed elsewhere in the financial statements the Company had the following related party transactions for which the expenses are included in general and administrative expenses, business development expenses and share issue costs:

- a) During the year ended December 31, 2007, the Company was charged \$304,716 (2006 – \$79,401) in legal fees by legal firms in which directors and officers of the Company are partners. Included in accounts payable at December 31, 2007 is \$83,911 (2006 – \$53,496) due to the legal firms.
- b) During the year ended December 31, 2007, the Company paid \$383,400 (2006 - \$79,900) to an individual prior to him becoming an employee and officer of the Company. Included in accounts receivable at December 31, 2007 is \$6,342 due from this employee for which payment was received subsequent to December 31, 2007.
- c) During the year ended December 31, 2007, the Company paid \$139,050 (2006 - \$112,600) consulting fees to an individual prior to him becoming an employee and officer of the Company. In addition, the Company was charged \$25,373 (2006 - \$450) for geological expenses from a corporation controlled by this individual.
- d) During the year ended December 31, 2007 the Company loaned an employee and officer a total of \$65,000 on a non-interest bearing note. This note was repaid prior to December 31, 2007.

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

18. Commitments

- a) The Company is committed to an agreement for office premises on a monthly basis at a rate of \$12,500 per month.
- b) The Company has granted a two percent gross overriding royalty on specific properties to a consultant who subsequently became an employee. The carrying amount of the respective lands is \$3.2 million. In addition, the individual has also been allocated an amount equal to 10% of all future stock options which become capable of being granted by the Company as a result of an increase in the number of issued and outstanding common shares resulting from future equity financings.
- c) Pursuant to flow-through private placements, the Company is required to incur approximately \$11.7 million on qualifying expenditures by December 31, 2008.

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19. Financial instruments

a) Fair values of financial assets and liabilities

Financial instruments consist of cash and cash equivalents, accounts receivable, commodity contract and accounts payable and accrued liabilities. At December 31, 2007 there were no significant differences between the carrying amounts reported on the balance sheet and estimated fair values.

b) Credit risk

The majority of the Company's accounts receivable are in respect of oil and natural gas operations. Management believes the risk is mitigated by the size and reputation of the companies to which they extend credit.

c) Interest rate risk

Interest rate risk is the risk that the value of a financial instrument might be adversely affected by a change in the interest rates. In seeking to minimize the risks from interest rate fluctuations, the Company manages exposure through its normal operating and financing activities. The Company is exposed to interest rate risk primarily through its variable interest rate on its cash and cash equivalents.

d) Commodity price risk

The Company's operations are exposed to commodity price fluctuations. The Company does not have any commodity contracts as at December 31, 2007.

20. Subsequent events

a) In January 2008, pursuant to a non-brokered private placement, the Company issued 8,709,677 common shares at a price of \$0.93 per share for gross proceeds of \$8.1 million.

b) In February 2008, the Company signed an agreement with another corporation whereby they will participate equally in the capital program of certain of the Company's properties. The Company expects to receive approximately \$2.5 million cash payment from expenditures incurred to December 31, 2007.