

## MANAGEMENT'S REPORT

To the Shareholders of Vero Energy Inc.

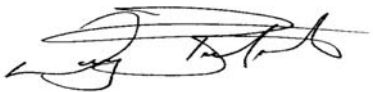
The accompanying financial statements of Vero Energy Inc. and all of the information in this Annual Report are the responsibility of management and have been approved by the Board of Directors.

The financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles. When alternative accounting methods exist, management has chosen those methods it deems most appropriate in the circumstances. Financial statements are not precise since they include certain amounts based on estimates and judgments. Management has determined such amounts on a reasonable basis in order to ensure that the financial statements are presented fairly, in all material respects. The financial information contained elsewhere in this report has been reviewed to ensure consistency with the financial statements.


Management has established systems of internal controls, which are designed to provide reasonable assurance the Company's assets are safeguarded from loss or unauthorized use and to produce reliable accounting records for the preparation of financial information.

The Board of Directors is responsible for ensuring that management fulfils its responsibilities for financial reporting and internal controls. It exercises its responsibilities primarily through the Audit Committee, which is comprised of independent, non-management directors. The Audit Committee has reviewed the financial statements with management and the auditors. This has been reported to the Board of Directors which has approved the financial statements.

The financial statements have been audited by PricewaterhouseCoopers LLP, the external auditors, in accordance with auditing standards generally accepted in Canada on behalf of the shareholders.



Douglas J. Bartole  
President and Chief Executive Officer



Gerald N. Gilewicz, C.M.A.  
Vice-President, Finance and  
Chief Financial Officer

Calgary, Canada  
March 7, 2008

# VERO ENERGY INC.

## Statement of Operations, Comprehensive Income and Retained Earnings

(in thousands, except per share data)

	2007	2006
<b>REVENUE</b>		
Production revenue	82,063	43,948
Realized gain on risk management activities	1,344	-
	83,407	43,948
Royalties	(23,003)	(10,749)
Interest and other	-	94
	60,404	33,293
<b>EXPENSES</b>		
Operating	11,189	5,564
Transportation	2,348	734
General and administrative	3,132	1,750
Stock-based compensation (Note 9(e))	1,449	2,056
Interest and bank charges	2,451	1,434
Depletion, depreciation and accretion	36,052	22,125
	56,621	33,663
<b>INCOME (LOSS) BEFORE INCOME TAXES</b>	3,783	(370)
<b>INCOME TAXES (RECOVERY) (Note 8)</b>		
Current	-	(292)
Future	619	(1,113)
	619	(1,405)
<b>NET EARNINGS AND COMPREHENSIVE INCOME</b>	3,164	1,035
<b>RETAINED EARNINGS, BEGINNING OF PERIOD</b>	1,700	665
<b>RETAINED EARNINGS, END OF PERIOD</b>	4,864	1,700
<b>NET EARNINGS PER SHARE AND COMPREHENSIVE INCOME PER SHARE (Note 12)</b>		
Basic	0.11	0.04
Diluted	0.11	0.04

---

**VERO ENERGY INC.****Balance Sheet****As at December 31,***(in thousands)*

	<u>2007</u>	<u>2006</u>
<b>ASSETS</b>		
<b>CURRENT</b>		
Accounts receivable	16,767	15,308
Prepaid expenses and deposits	3,523	1,089
	<u>20,290</u>	<u>16,397</u>
Property and equipment (Note 5)	171,727	135,427
Goodwill (Note 4)	15,034	15,034
	<u>207,051</u>	<u>166,858</u>
<b>LIABILITIES</b>		
<b>CURRENT</b>		
Accounts payable and accrued liabilities	36,051	30,286
Bank debt (Note 6)	46,013	35,651
	<u>82,064</u>	<u>65,937</u>
Asset retirement obligations (Note 7)	2,641	1,785
Future income taxes (Note 8)	10,812	10,567
	<u>95,517</u>	<u>78,289</u>
<b>SHAREHOLDERS' EQUITY</b>		
Share capital (Note 9)	103,077	84,710
Contributed surplus (Note 10)	3,593	2,159
Retained Earnings	4,864	1,700
	<u>111,534</u>	<u>88,569</u>
	<u>207,051</u>	<u>166,858</u>

Commitments (Note 13)

*See accompanying notes.***APPROVED BY THE BOARD**

Paul R. Baay, Director

Douglas J. Bartole, Director

---

# VERO ENERGY INC.

## Statement of Cash Flows

(in thousands)

	2007	2006
<b>CASH FLOWS RELATED TO THE FOLLOWING ACTIVITIES:</b>		
<b>OPERATING</b>		
Net earnings	3,164	1,035
Adjustments for:		
Depletion, depreciation and accretion	36,052	22,125
Stock-based compensation	1,449	2,056
Future income taxes	619	(1,113)
	41,284	24,103
Asset retirement costs incurred	(43)	-
Changes in non-cash working capital (Note 14(a))	(7,140)	(7,883)
	34,101	16,220
<b>FINANCING</b>		
Increase in bank debt	10,362	17,131
Proceeds from private placement, net of share issue costs	17,935	12,061
Proceeds from exercise of stock options	43	-
	28,340	29,192
<b>INVESTING</b>		
Corporate acquisition (Note 4)	-	(18,887)
Additions to petroleum and natural gas properties	(68,932)	(57,026)
Purchase of petroleum and natural gas assets	(2,478)	-
Disposals of petroleum and natural gas properties	-	300
Additions to administrative assets	(43)	(141)
Changes in non-cash working capital (Note 14(a))	9,012	17,819
	(62,441)	(57,935)
<b>NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS</b>	-	(12,523)
<b>CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD</b>	-	12,523
<b>CASH AND CASH EQUIVALENTS, END OF PERIOD</b>	-	-

Supplementary cash flow information (Note 14(b))

**Notes to the financial statements****For the Years Ended December 31, 2007 and 2006***(in thousands, except per share data)*

---

**1. NATURE OF OPERATIONS, ORGANIZATION AND BASIS OF PRESENTATION**

Vero Energy Inc. (“Vero” or the “Company”) was incorporated on September 23, 2005 under the laws of the Business Corporations Act (Alberta) and its primary business is the acquisition, exploration, development and production of natural gas, natural gas liquids and crude oil in Alberta. The Company commenced oil and gas operations on November 2, 2005 after the closing of a Plan of Arrangement between Vero, True Energy Inc. (“True”), and TKE Energy Trust (“TKE”). Vero is a public company and commenced trading on the Toronto Stock Exchange on November 7, 2005.

On February 24, 2006 the Company acquired all of the issued and outstanding shares of Ledge Resources Limited, a private Alberta oil and gas exploration and development company (Note 4).

The Company’s financial statements for the years ended December 31, 2007 and 2006 have been prepared on a going concern basis, which contemplates the realization of assets and the settlement of liabilities and commitments in the normal course of business.

These financial statements include the accounts of Vero Energy Inc. and its wholly-owned subsidiaries and are presented in accordance with Canadian generally accepted accounting principles. Effective January 1, 2007 Vero and its wholly-owned subsidiaries were amalgamated under the Alberta Business Corporations Act and continued under the name Vero Energy Inc.

**Notes to the financial statements**  
**For the Years Ended December 31, 2007 and 2006**  
*(in thousands, except per share data)*

---

**2. SIGNIFICANT ACCOUNTING POLICIES**

The financial statements of the Company have been prepared by management in accordance with Canadian generally accepted accounting principles. These financial statements have, in management's opinion, been properly prepared using careful judgement with reasonable limits of materiality and within the framework of the significant accounting policies summarized below:

*a) Financial instruments*

Financial instruments consist primarily of cash and cash equivalents, accounts receivable, accounts payable, accrued liabilities and bank indebtedness. It is management's opinion that the Company is not exposed to significant interest, currency or credit risks arising from these financial instruments. There are no significant differences between the carrying value of these financial instruments and their estimated fair value.

*b) Cash and cash equivalents*

The Company considers deposits in banks, certificates of deposit and short-term investments with original maturities of three months or less as cash and cash equivalents. Bank borrowings are considered to be financing activities.

*c) Petroleum and natural gas properties and facilities*

The Company follows the full cost method of accounting for petroleum and natural gas operations, whereby all costs relating to the exploration and development of petroleum and natural gas reserves are capitalized on a country-by-country cost centre basis. Such costs include land acquisition costs, costs of drilling both productive and non-productive wells, well equipment, flow-line and facility costs, geological and geophysical expenses, asset retirement costs, and overhead expenses directly related to exploration and development activities.

Proceeds from the sale of petroleum and natural gas properties are applied against capitalized costs, with no gain or loss recognized, unless such a sale would result in a greater than 20% change in the depletion and depreciation rate.

**Notes to the financial statements****For the Years Ended December 31, 2007 and 2006***(in thousands, except per share data)*

---

**2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)***d) Depletion and depreciation*

Petroleum and natural gas properties and facilities costs, together with estimated future capital costs associated with proved reserves, less estimated salvage values and costs related to unproven properties, are depleted using the unit-of-production method based on estimated proven reserves of petroleum and natural gas before the deduction of royalties as determined by independent petroleum engineers. For purposes of this calculation proven natural gas reserves and production are converted to equivalent volumes of crude petroleum based on the approximate energy equivalent ratio of six thousand cubic feet of natural gas to one barrel of crude oil. Costs of acquiring and evaluating unproved properties are initially excluded from the calculation and are periodically assessed for impairment. When proved reserves are assigned or the property is considered to be impaired, the cost of the property or the amount of the impairment is added to costs subject to depletion calculations.

Administrative assets are carried at cost and depreciated on a declining basis at an annual rate of 20% to 30% depending on the asset category.

*e) Ceiling Test*

The Company at least annually assesses the carrying value of its oil and gas properties to determine if impairment has occurred. The Company applies a two-stage ceiling test to capitalized costs to ensure that such costs do not exceed the undiscounted future cash flows from production of proved reserves. Undiscounted future cash flows are calculated based on an independent petroleum engineers estimate of forward indexed prices applied to estimated production of proved reserves plus the cost of undeveloped properties that were excluded from the depletion calculation, less estimated future operating costs, royalties net of applicable tax credits, future capital development costs and abandonment costs. When the carrying amount of a cost center is not recoverable the second stage of the process will determine the impairment whereby the cost center would be written down to its fair value. The second stage requires the calculation of discounted cash flows from proved plus probable reserves using a risk-free interest rate plus the cost of undeveloped land, net of any impairment. The fair value is estimated using generally accepted present value techniques, which incorporate risk and other uncertainties when determining expected cash flows.

**Notes to the financial statements**  
**For the Years Ended December 31, 2007 and 2006**  
*(in thousands, except per share data)*

---

**2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

*f) Goodwill*

Goodwill represents the excess of the purchase price of an acquired business over the fair value of the net identifiable assets received. Goodwill is stated at cost less impairment and is not amortized. Goodwill is assessed for impairment annually at year-end or more frequently if events or changes in circumstances indicate that the asset may be impaired. To assess impairment, the fair value of the reporting unit is determined and compared to the carrying value of the reporting unit. If the fair value is less than the carrying value, then a second test is performed to determine the amount of the impairment. The amount of the impairment is determined by deducting the fair value of the reporting unit's assets and liabilities from the fair value of the reporting unit to determine the implied fair value of goodwill and comparing that amount to the book value of the reporting unit's goodwill. Any excess of the book value of goodwill over the implied fair value of goodwill is the impaired amount. Impairment is charged to income in the period in which it occurs.

*g) Asset retirement obligations*

The fair value of obligations associated with the retirement, removal and site restoration of long-lived assets are recorded in the period in which the liability is incurred. The obligations recognized are estimates of statutory, contractual or legal obligations that the Company will reasonably be expected to incur and then discounted to their present value using the Company's credit adjusted risk-free interest rate. The corresponding amount increases the carrying amount of the related asset. The liability is accreted over time for changes in the fair value of the liability through charges to accretion expense. The provision will be revised for the effect of any changes to timing related to cash flow or undiscounted abandonment costs. The costs capitalized to the related assets are amortized to earnings in a manner consistent with the depreciation and depletion of the underlying asset. Actual costs incurred upon settlement of the retirement obligation are charged against the obligation to the extent of the liability recorded.

*h) Future income taxes*

The Company follows the liability method of accounting for income taxes. Under this method the Company records future income tax assets and liabilities based on "temporary differences" (differences between the accounting basis and the tax basis of the assets and liabilities) measured using the substantively enacted tax rates and laws expected to apply when these differences reverse. The effect of a change in substantively enacted income tax rates on future income tax assets and liabilities is recognized in income in the period that the change occurs.

**Notes to the financial statements**  
**For the Years Ended December 31, 2007 and 2006**  
*(in thousands, except per share data)*

---

**2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

*i) Revenue recognition*

Revenue from the sale of natural gas, natural gas liquids and crude oil is recognized based on volumes delivered at contractual delivery points when title passes from the Company to its customers. Costs associated with the operating of wells and facilities, delivery of the commodity, transportation and production-based royalty expenses, are recognized in the same period in which the related revenue is earned and recorded. Royalty tax credits are netted against oil, gas and liquids royalties. Transportation costs are recorded separately.

*j) Stock-based compensation plan*

The Company has a stock based compensation plan enabling officers, directors, employees and certain consultants to purchase common shares at exercise prices equal to the market price on the date the option is granted. Stock option awards are accounted for based on the fair value method of accounting (Note 9(e)). Under this method, stock-based compensation is recorded as an expense over the expected life of the option, with a corresponding increase in contributed surplus. Stock-based compensation expense is based on the estimated fair value of the related stock option at the time of the grant using the Black-Scholes option model. When stock options are exercised, the consideration paid to the Company, along with amounts previously credited to contributed surplus, is credited to share capital. Forfeitures are accounted for as they occur and result in a reduction of compensation expense if the options have not vested.

*k) Measurement uncertainty*

The preparation of the financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results may differ from these estimates.

Recorded amounts for depletion and depreciation of petroleum and natural gas properties and equipment are based on estimates. The ceiling test and impairment calculations are based on estimates of oil and gas reserves, future costs required to develop those reserves and the fair value of unproved properties. By their nature, these estimates are subject to measurement uncertainty and the effect on the financial statements of changes of estimates in future periods could be significant.

**Notes to the financial statements**  
**For the Years Ended December 31, 2007 and 2006**  
*(in thousands, except per share data)*

---

**2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)**

*k) Measurement uncertainty (continued)*

The value of the asset retirement obligations was based on Vero's net ownership interests in all wells and facilities and depends on estimates of current market interest rates and future restoration and reclamation expenditures. By their nature, these estimates are subject to measurement uncertainty and the effect on the financial statements of changes of estimates in future periods could be significant.

The calculation of future income tax is based on assumptions, which are subject to uncertainty as to timing as well as the tax rates at which temporary differences are expected to reverse.

The Black-Scholes option valuation model was developed for use in estimating the fair value of options, which were fully tradable with no vesting restrictions. This option valuation model requires the input of highly subjective assumptions including the expected stock price volatility. Because the Company's stock options have characteristics significantly different from those of traded options and because changes in the subjective input assumptions can materially affect the calculated fair value, such value is subject to measurement uncertainty.

*l) Joint venture activities*

A significant portion of the Company's exploration, development and production activities are conducted with joint venture partners. These financial statements reflect only the Company's proportionate interest in such activities.

*m) Per share amounts*

Basic per share amounts are calculated using the weighted average number of shares outstanding during the period. Diluted per share amounts reflect the exercise or conversion of potentially dilutive securities or other contracts to issue shares at the later of the grant of such securities or the beginning of the period. The Company computes diluted earnings per share based on the treasury-stock method to determine the dilutive effect of securities or other contracts. This method assumes that any proceeds obtained on the exercise of outstanding, in-the-money stock options, plus unrecognized stock compensation costs, would be used to purchase common shares of the Company at their average market price during the period.

**Notes to the financial statements****For the Years Ended December 31, 2007 and 2006***(in thousands, except per share data)*

---

**2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)***n) Hedging*

The Company may periodically enter into forward contracts to reduce its exposure to price fluctuations on a portion of its oil and natural gas production. The contracts are not used for speculative trading purposes. Payments or receipts on financial instruments that are designated and effective as hedges are recognized in income concurrently with the hedged transaction. Any financial instrument that does not constitute a hedge is recorded at fair value in the balance sheet with any gain or loss reflected in the statement of operations. Gains or losses on physical and qualifying hedge contracts are reported as adjustments to commodity revenues in the related production month. At December 31, 2007 the Company did not have any hedges outstanding.

*o) Flow through shares*

The Company finances a portion of its exploration program through the issuance of flow-through shares. Under the terms of the flow-through share agreements, and as provided for under the Income Tax Act, the tax attributes of qualifying exploration costs incurred by the Company are renounced to subscribers. To recognize the foregone tax benefits to the Company, the amount for which the shares are issued is reduced by the tax effect of the tax benefits renounced to subscribers at the time the renunciation documents are filed with the tax authorities.

**3. CHANGES IN ACCOUNTING POLICIES**

Effective January 1, 2007 the Company adopted the new recommendations from the Canadian Institute of Chartered Accountants (CICA) Handbook Section 3855, *Financial Instruments - Recognition and Measurement*; Section 1530, *Comprehensive Income*; Section 3861, *Financial Instruments - Disclosure and presentation*; Section 3251, *Equity* and Section 3865, *Hedges*. The adoption of these new financial instruments standards resulted in changes in the accounting for financial instruments as well as the recognition of certain transitional adjustments that have been recorded in opening accumulated other comprehensive income as described below. The components of equity and changes thereto have been disclosed. The standards are applied retroactively with prospective presentation except for adjustments relating to cumulative translation adjustments to account for foreign self-sustaining subsidiaries which are applied and presented retroactively. The principal changes in the accounting for financial instruments due to the adoption of these accounting standards are described below.

**Notes to the financial statements****For the Years Ended December 31, 2007 and 2006***(in thousands, except per share data)*

---

**3. CHANGES IN ACCOUNTING POLICIES (CONTINUED)***(a) CICA 1530 - Comprehensive Income and equity*

Section 1530 of the CICA Handbook introduced a new requirement effective for fiscal years beginning on or after October 1, 2006 to temporarily present gains and losses from changes in fair value outside net income. Comprehensive income is described as the change in a company's net assets that results from transactions, events and circumstances related to sources other than the company's shareholders. The CICA also made changes to section 3250 of the CICA Handbook, Surplus, and reissued it as section 3251, Equity. The section is also effective for fiscal years beginning on or after October 1, 2006. The Company has adopted this policy effective January 1, 2007, but the results of both comprehensive income and accumulated comprehensive income are not material to the financial statements and therefore no additional disclosure has been included.

*(b) CICA 3855 - Financial assets and financial liabilities*

Under Section 3855, financial assets and financial liabilities are initially recognized at fair value and are subsequently measured based on their classification as described below. The classification depends on the purpose for which the financial instruments were acquired and their characteristics. The classification generally cannot be changed subsequent to the designation at the initial recognition of the instruments.

Held for trading

Financial assets that are purchased and held with the intention of generating profits in the near term are classified as held for trading. These instruments are accounted for at fair value with the change in fair value recognized in net earnings during the period. Cash and cash equivalents were classified as held for trading, these instruments are highly liquid and are readily convertible to known amounts of cash and are so near maturity that there is no significant risk of changes in value due to rate changes.

Loans and receivables

Accounts receivable and accrued revenues are designated as "loans and receivables".

Other Liabilities

Accounts payable and long-term debt, are designated as "other liabilities".

Held-to-maturity

Securities that have a fixed maturity date and which the Company has positive intention and the ability to hold to maturity are classified as held-to-maturity and accounted for at amortized cost using the effective interest rate method. No investments were classified as held-to-maturity on January 1, 2007.

**Notes to the financial statements**  
**For the Years Ended December 31, 2007 and 2006**  
*(in thousands, except per share data)*

---

**3. CHANGES IN ACCOUNTING POLICIES (CONTINUED)**

*(b) CICA 3855 - Financial assets and financial liabilities (continued)*

Available-for-sale

Financial assets designated to be available-for-sale or not designated as one of the above categories are classified as available-for-sale. These assets are accounted for at fair value, with changes in fair value recognized in other comprehensive income. When a decline in fair value is determined to be other-than-temporary, the cumulative loss included in accumulated other comprehensive income is removed and recognized in net earnings. Gains and losses realized on disposal of available-for-sale securities are recognized in other income in net earnings. No investments were classified as available-for-sale on January 1, 2007.

*(c) CICA 3861 – Financial Instruments*

All derivative instruments, including embedded derivatives, are recorded on the balance sheet at fair value unless they qualify for the normal sale and purchase exception. All changes in fair value are included in earnings unless cash flow hedge or net investment accounting is used, in which case changes in fair value are recorded in other comprehensive income, to the extent the hedge is effective, and in earnings, to the extent it is ineffective.

Recent accounting pronouncements issued and not yet adopted

The following accounting standards will apply to fiscal periods commencing on or after October 1, 2007:

- Section 1535, “Capital Disclosures”. This section establishes standards for disclosing information about an entity’s objectives, policies and processes for how it manages its capital. A company must also disclose qualitative data about what the entity regards as capital; and whether the company has complied with any capital requirements and if not, the consequences of such non-compliance. The Company will adopt this new standard effective January 1, 2008.
- Section 3862, “Financial Instruments – Disclosures”. This section describes the required disclosures to evaluate the significance of financial instruments for the entity’s financial position and performance as well as the nature and extent of risks arising from both recognized and unrecognized financial instruments to which the entity is exposed and how the entity manages those risks. The Company will adopt this new standard effective January 1, 2008.
- Section 3863, “Financial Instruments – Presentation”. This section establishes standards for presentation of financial instruments and non-financial derivatives. It details the presentation of the standards described in Section 3861, “Financial Instruments – Disclosure and Presentation”. The Company will adopt this new standard effective January 1, 2008.

**Notes to the financial statements****For the Years Ended December 31, 2007 and 2006***(in thousands, except per share data)***3. CHANGES IN ACCOUNTING POLICIES (CONTINUED)**

- The CICA plans to converge Canadian GAAP with International Financial Reporting Standards (“IFRS”) over a transition period expected to end in 2011. The impact of the transition to IFRS on the Company’s financial statements is not yet determinable.

**4. ACQUISITION OF LEDGE RESOURCES LIMITED**

Effective February 24, 2006 Vero acquired all of the outstanding common shares of Ledge Resources Limited (“Ledge”). Ledge shareholders received \$1.90 and 0.49473 Vero common shares for each Ledge share held. A total of 4,754,945 Vero shares were issued. The price ascribed to the common shares of \$6.44 was based on the trading prices of Vero common shares on the five days prior, the day of, and the five days following the announcement of the purchase. The operating results and corresponding cash flow and earnings related to the acquisition were included in the Company’s financial statements effective February 25, 2006. The acquisition was accounted for using the purchase method and the purchase price was allocated based on fair values as follows:

**Consideration paid:**

Cash paid to Ledge shareholders	18,261
Issuance of 4,754,945 common shares (Note 9(a))	30,622
Transaction costs	626
	49,509

**Allocation of purchase price:**

Current assets	3,837
Current liabilities	(3,678)
Debt assumed	(18,520)
	(18,361)
Property, plant and equipment	65,738
Goodwill	15,034
Asset retirement obligations	(666)
Future income taxes	(12,236)
	49,509

**Notes to the financial statements**  
**For the Years Ended December 31, 2007 and 2006**  
*(in thousands, except per share data)*

**5. PROPERTY AND EQUIPMENT**

	<b>December 31, 2007</b>		
	Cost	Accumulated depletion, depreciation and accretion	Net Book Value
Petroleum and natural gas properties and facilities	230,277	(58,677)	171,600
Administrative assets	212	(85)	127
	<b>230,489</b>	<b>(58,762)</b>	<b>171,727</b>

	December 31, 2006		
	Cost	Accumulated depletion, depreciation and accretion	Net Book Value
Petroleum and natural gas properties and facilities	158,150	(22,846)	135,304
Administrative assets	169	(46)	123
	158,319	(22,892)	135,427

Costs of acquiring unproved properties and salvage values in the aggregate of \$14,135 were excluded from the depletion calculation as at December 31, 2007 (2006 - \$12,157). Management performed an impairment test and determined that the carrying values of unproved properties were not impaired as at December 31, 2007. Future development costs on proved undeveloped reserves of \$16,836 (2006 - \$4,846) are included in the depletion calculation.

During 2007, the Company capitalized \$524 (2006 - \$322) in salaries and wages directly related to exploration and development activities.

**Notes to the financial statements****For the Years Ended December 31, 2007 and 2006***(in thousands, except per share data)***5. PROPERTY AND EQUIPMENT (continued)**

The Company performed a ceiling test calculation as of December 31, 2007. The table below summarizes the benchmark prices for the next eleven years used by the external engineering firm in preparing the Company's reserve report. No write-down was required for the year ended December 31, 2007 based on the expected realized future commodity prices.

	WTI Cushing Oklahoma (\$US/bbl)	Edmonton Par 40 d API (\$Cdn/bbl)	Alberta AECO-C (\$Cdn/mmbtu)	Natural Gas Liquids (Butanes) (\$Cdn/bbl)
2008	89.15	88.48	6.74	67.25
2009	85.58	85.52	7.48	65.02
2010	83.25	83.88	7.69	63.83
2011	80.99	82.03	7.80	62.46
2012	80.18	81.16	7.84	61.81
2013	79.85	80.79	8.05	61.54
2014	81.03	82.00	8.26	62.45
2015	82.24	83.25	8.46	63.39
2016	83.47	84.49	8.64	64.30
2017	85.16	86.21	8.84	65.62

The annual escalation rate used after 2017 is 2.0%.

**6. BANK DEBT**

The Company has a \$70,000 (2006 - \$45,000) revolving credit facility with a Canadian Chartered Bank. The advances bear interest at bank prime. Any unutilized portion of the credit facility is subject to a standby fee. The authorized limit is subject to a mandatory annual, borrowing base review by the bank. The facility is available to the Company at their option until May 31, 2008. The facility may be renewed at the Company's request and subject to the review of the Company's reserves lending base by the bank. Interim reviews occur at the request of the Company with a view to make revisions to the borrowing base as new reserves are added. The facility is secured by a \$125,000 (2006 - \$75,000) floating charge debenture over the assets of the Company.

**Notes to the financial statements**  
**For the Years Ended December 31, 2007 and 2006**

*(in thousands, except per share data)*

**7. ASSET RETIREMENT OBLIGATIONS**

The Company's asset retirement obligations result from ownership interests in petroleum and natural gas assets, including well sites, gathering systems, batteries and processing facilities. The Company estimates the total undiscounted amount of cash flows required to settle its asset retirement obligations at December 31, 2007 to be \$6,455 (2006 - \$3,437), which will be incurred at various times between 2008 and 2022. The fair value of the asset retirement obligations incurred in the period ended December 31, 2007 was calculated using an average credit-adjusted risk free rate of 8.3% (2006 - 8.0%) and an average inflation factor of 2.1% (2006 - 2.0%). Settlement of the obligations will be funded from general corporate funds at the time of retirement or removal. As at December 31, 2007, no funds have been set aside to settle these obligations. Changes to asset retirement obligations during the period were as follows:

	2007	2006
Asset retirement obligations at beginning of period	<b>1,785</b>	380
Liabilities acquired on corporate acquisition (Note 4)	-	666
Liabilities incurred during the period	<b>755</b>	522
Liabilities settled during the period	<b>(43)</b>	(11)
Change in estimated future cash flows	<b>(39)</b>	125
Accretion	<b>183</b>	103
Asset retirement obligations at end of period	<b>2,641</b>	1,785

**Notes to the financial statements**  
**For the Years Ended December 31, 2007 and 2006**

*(in thousands, except per share data)*

**8. INCOME TAXES**

The provision for income tax differs from the amounts that would have resulted from the combined federal and provincial rate had it been applied for the periods ended December 31, 2007 and 2006 as follows:

	<u>2007</u>	<u>2006</u>
Income (loss) before income taxes	<u>3,783</u>	(370)
Expected income tax (benefit) expense at the statutory rate of 32.1% (2006 – 34.5%)	1,215	(128)
Tax effect of non-deductible and non-taxable amounts related to:		
Non-deductible crown payments	-	1,183
Resource allowance	-	(913)
Stock-based compensation expense and other non-deductible amounts	528	718
Alberta Royalty Tax Credit and Attributed Canadian Royalty Income	-	(376)
Change in tax rates	(1,630)	(1,600)
Reversal of prior year tax provision	-	(292)
Reconcile book to actual on filing tax returns	499	-
Other	7	3
Total income tax provision	<u>619</u>	<u>(1,405)</u>

The income tax provision is comprised of:

	<u>2007</u>	<u>2006</u>
Current income taxes	-	(292)
Future income taxes	619	(1,113)
	<u>619</u>	<u>(1,405)</u>

The future income tax liability is comprised of the following:

	<u>2007</u>	<u>2006</u>
<b>Future Income Tax Benefits</b>		
Asset retirement obligations	660	518
Financing costs and other	543	339
Attributed Canadian Royalty Income	370	388
	<u>1,573</u>	<u>1,245</u>
<b>Future Income Liabilities</b>		
Temporary differences relating to capital assets	(12,385)	(11,812)
	<u>(10,812)</u>	<u>(10,567)</u>

As at December 31, 2007, Vero had \$130,670 (2006 - \$100,707) of tax pools available for deduction in future years for Canadian income tax purposes.

**Notes to the financial statements**  
**For the Years Ended December 31, 2007 and 2006**  
*(in thousands, except per share data)*

**9. SHARE CAPITAL**

	<b>Shares (000's)</b>	<b>Amount</b>
Authorized		
Unlimited number of voting common shares		
Unlimited number of first preferred shares		
Issued		
<i>Common shares</i>		
<b>Balance December 31, 2005</b>	19,021	<b>41,703</b>
Issuance of shares on corporate acquisition (a)	4,755	<b>30,622</b>
Private placement, net of share issue costs (b)	2,131	<b>12,061</b>
Adjustment for tax benefits from share issue costs	-	<b>324</b>
<b>Balance December 31, 2006</b>	25,907	<b>84,710</b>
Private placement, net of share issue costs (c)	3,000	<b>17,935</b>
Exercise of stock options (d)	8	<b>58</b>
Adjustment for tax benefits from share issue costs	-	<b>374</b>
<b>Total share capital at December 31, 2007</b>	28,915	<b>103,077</b>

a) Acquisition of Ledge Resources Limited

On February 24, 2006 the Company acquired all of the outstanding shares of a private company. At closing, Vero issued 4,755 common shares at a deemed value of \$30,622 (see Note 4).

b) Private Placement – April 13, 2006

On April 13, 2006 the Company closed a private placement for the issuance of 2,131 common shares at a price of \$6.10 per share. The net proceeds of the issuance of \$12,061 are comprised of gross proceeds of \$13,000 less expenses of the issue of \$939.

**Notes to the financial statements**  
**For the Years Ended December 31, 2007 and 2006**  
*(in thousands, except per share data)*

---

**9. SHARE CAPITAL (continued)**

c) Private placement – April 5, 2007

On April 5, 2007 the Company closed a private placement for the issuance of 1,500 Common Shares at a price of \$5.55 per share and 1,500 Flow-Through Common Shares at a price of \$7.25 per share. The net proceeds of issuance of \$17,935 were comprised of gross proceeds of \$19,200 less expenses of the issue of \$1,265. The tax effect of the tax benefits renounced to subscribers in respect of the flow-through shares will be recognized in the period when the renouncement documents are filed with the taxation authorities. Using a combination of the regular, and the “look-back” flow-through Share provisions of the Income Tax Act, the Company is required to incur eligible expenditures in the amount of \$10,875 prior to December 31, 2008 (Note 13(e)).

d) Stock options

The Company has a stock option plan under which options to purchase common shares may be granted to officers, directors, employees and consultants. The Board has approved a policy of reserving up to 10% of the outstanding common shares for issuance to eligible participants. As at December 31, 2007 there were 2,891 (2006 – 2,591) shares reserved for issuance under the plan. All options awarded have a maximum term of five years and vest in equal one-third increments on each anniversary of the grant. As at December 31, the following stock options were outstanding:

	2007		2006	
Stock Options	Weighted Average Exercise Price	Share Options	Weighted Average Exercise Price	Share Options
	\$		\$	
Outstanding, beginning of year	2,321	1,600	5.14	4.87
Granted	140	721	5.81	5.74
Exercised	(8)	-	5.35	-
Cancelled	(19)	-	5.39	-
Outstanding, end of year	2,434	2,321	5.18	5.14
Exercisable, end of year	1,299	533		

**Notes to the financial statements****For the Years Ended December 31, 2007 and 2006***(in thousands, except per share data)***9. SHARE CAPITAL (continued)**

Exercise Price	Options Outstanding					
	December 31, 2007			December 31, 2006		
	Number of Options Outstanding	Weighted Average Exercise Price \$	Weighted Average Years to Expiry	Number of Options Outstanding	Weighted Average Exercise Price \$	Weighted Average Years to Expiry
\$4.87 - 5.35	<b>1,909</b>	<b>4.93</b>	<b>3.1</b>	1,856	4.91	4.0
\$6.00 - 6.31	<b>525</b>	<b>6.08</b>	<b>3.5</b>	465	6.08	4.4
	<b>2,434</b>	<b>5.18</b>	<b>3.2</b>	2,321	5.14	4.1

## e) Stock-based compensation

The Company accounts for its stock options granted to employees, officers, and directors using the fair value method. In accordance with the Company's incentive stock plan, these options have an exercise price equal to the fair value of the security at the date of grant. The fair value of each option granted is estimated on the date of grant using a modified Black-Scholes option-pricing model. The following assumptions have been used:

	2007	2006
Risk free rate (%)	<b>4.1</b>	4.2
Expected life (years)	<b>5</b>	5
Expected volatility (%)	<b>53</b>	39
Expected dividends	-	-

For the period ended December 31, 2007, 140 (2006 – 721) stock options were granted to employees, officers and directors. The option grants during the period had a weighted average fair value expense attributed to them of \$2.94 (2006 - \$2.32) per share. \$1,449 (2006 - \$2,056) was recorded as stock compensation expense with respect to all options outstanding, with a corresponding credit to contributed surplus (Note 10).

## f) Normal Course Issuer Bid

In August of 2007, the Toronto Stock Exchange approved the Company's application to initiate a Normal Course Issuer Bid. The Bid is for a period of one year and is renewable upon expiration. To date, no shares have been purchased for cancellation by the Company.

**Notes to the financial statements**  
**For the Years Ended December 31, 2007 and 2006**

*(in thousands, except per share data)*

**10. CONTRIBUTED SURPLUS**

The following table reconciles the Company's contributed surplus:

	2007	2006
Balance at January 1	2,159	103
Stock-based compensation expense	1,449	2,056
Exercise of stock options	(15)	-
Balance at December 31	<b>3,593</b>	2,159

**11. RELATED PARTY TRANSACTIONS**

Five officers of the Company subscribed for 26 common shares at a price of \$5.55 per share and 21 flow-through common shares at a price of \$7.25 per share in the April 5, 2007 private placement (note 9(c)). The prices at which the shares were issued were the same as those used in the subscription agreements entered into with non-related parties.

**12. PER SHARE AMOUNTS**

The following table summarizes the shares used in calculating net earnings per share as at December 31:

	2007	2006
Weighted average shares outstanding - basic	28,129	24,589
Dilutive stock options outstanding	2,299	1,856
Shares notionally repurchased with proceeds from dilutive stock options and returned to treasury	(2,110)	(1,856)
Weighted average shares outstanding - diluted	<b>28,318</b>	24,589

At December 31, 2007, 135 (2006 – 465) of the issued stock options were excluded from the calculation of diluted weighted average shares outstanding as to include them would be anti-dilutive.

**Notes to the financial statements**  
**For the Years Ended December 31, 2007 and 2006**  
*(in thousands, except per share data)*

---

### 13. COMMITMENTS

In addition to the commitments listed below, the Company has various indemnifications in place in the ordinary course of business, none of which, as assessed by management, are expected to have a significant impact on the Company's financial statements.

#### *a) Transportation costs*

The Company has committed to firm-service contracts for the transportation of its natural gas. The amounts below are the minimum cash obligations that the Company must pay under the terms of the contract. The combined minimum future costs as at December 31, were as follows:

	2007	2006
2007	-	23
2008	209	23
2009	209	23
2010	198	12
2011	194	7
2012	79	2
<b>Total minimum payments</b>	<b>889</b>	<b>90</b>

#### *b) Office lease costs*

The Company has committed to future minimum payments under operating leases that cover the rental of office space, a proportionate share of operating costs and office furnishings as follows:

	2007	2006
2007	-	758
2008	931	910
2009	928	910
2010	918	910
2011	531	531
<b>Total minimum payments</b>	<b>3,308</b>	<b>4,019</b>

**Notes to the financial statements**  
**For the Years Ended December 31, 2007 and 2006**

*(in thousands, except per share data)*

**13. COMMITMENTS (CONTINUED)**

*c) Indemnifications*

From time to time, the Company may become involved in litigation or have claims sought against it in the normal course of business operations. Management of the corporation is not currently aware of any claims or actions that would materially affect the Corporation's reported financial position or results from operations.

Under the terms of certain agreements and the Company's by-laws the Company indemnifies individuals who have acted at the Company's request to be a director and/or officer of the Company, to the extent permitted by law, against any and all damages, liabilities, costs, charges or expenses suffered by or incurred by the individuals as a result of their service. The Company has no outstanding claims having a potentially material adverse effect on the Company as a whole.

*d) Drilling commitments*

As at December 31, 2007 Vero was committed to drill one (0.8 net) well in Alberta. This well has a commencement date in 2008. The commitment is pursuant to a farm-in agreement with an industry partner. The Company expects to satisfy the net portion of this drilling commitment at an estimated cost of \$1,920.

*e) Flow-through shares*

Pursuant to the flow-through share private placement entered into on April 5, 2007, the Company was obligated to incur \$10,875 in eligible costs by December 31, 2008. As at December 31, 2007 Vero had \$959 remaining on this commitment.

**14. SUPPLEMENTARY INFORMATION**

*a) Changes in non-cash working-capital*

	<b>2007</b>	<b>2006</b>
Accounts receivable	<b>(1,459)</b>	(9,295)
Prepaid expenses and deposits	<b>(2,434)</b>	(934)
Accounts payable and accrued liabilities	<b>5,765</b>	20,298
Taxes payable	-	(292)
Corporate acquisition of working capital (Note 4)	-	159
Net change in non-cash working capital	<b>1,872</b>	9,936
Investing activities	<b>(9,012)</b>	(17,819)
Operating activities	<b>(7,140)</b>	(7,883)

**Notes to the financial statements**  
**For the Years Ended December 31, 2007 and 2006**  
*(in thousands, except per share data)*

---

**14. SUPPLEMENTARY INFORMATION (CONTINUED)**

*b) Supplementary cash flow information*

	2007	2006
Interest received	-	94
Interest paid	2,449	1,362

**15. FINANCIAL INSTRUMENTS**

As disclosed in Note 2(a), the Company holds various forms of financial instruments. The nature of these instruments and the Company's operations expose the Company to commodity price, credit and interest rate risks. The Company manages its exposure to these risks by operating in a manner that minimizes this exposure.

*Commodity price risk*

Due to the volatility of commodity prices the Company is exposed to adverse consequences of declining prices. The Company may enter into oil and natural gas contracts in order to protect its cash flow on future sales from the potential adverse impact of declining prices. The contracts reduce the fluctuation in sales revenue by locking in prices with respect to future deliveries of oil and natural gas. As at December 31, 2007, the Company did not have any of these contracts outstanding.

*Fair values of financial instruments*

The carrying value of financial instruments, which include short-term deposits, accounts receivable, deposits, accounts payable and accrued liabilities approximates amounts at which these instruments could be exchanged in a transaction between knowledgeable and willing parties.

*Credit risk*

Substantially all of the accounts receivable are with customers and joint venture partners in the oil and gas industry and are subject to normal industry credit risks. The Company generally extends unsecured credit to these customers and therefore, the collection of accounts receivable may be affected by changes in economic or other conditions. Management believes the risk is mitigated by entering into transactions with long-standing, reputable, counterparties and partners. The Company has not experienced any credit loss in the collection of its accounts receivable.

**Notes to the financial statements**  
**For the Years Ended December 31, 2007 and 2006**  
*(in thousands, except per share data)*

---

**15. FINANCIAL INSTRUMENTS (CONTINUED)**

*Interest rate risk*

The Company's revolving demand loan facility is subject to floating rates. The floating rate debt is subject to interest rate cash flow risk, as the required cash flows to service the debt will fluctuate as a result of changes in market rates.

*Foreign currency exchange risk*

The Company is exposed to foreign currency fluctuations as crude oil prices received are referenced to U.S. dollar denominated amounts.

**16. SUBSEQUENT EVENTS**

*a) Private Placement*

On February 28, 2008 the Company closed a private placement for the issuance of 1,940 flow-through common shares at a price of \$9.25 per share. The Company received gross proceeds of \$17,945.

*b) Hedging*

Effective February 13, 2008, the Company entered into a natural gas costless collar for 5,000 gigajoules per day at a floor of \$6.50 CDN per gigajoule and a ceiling of \$8.25 CDN per gigajoule. The contract term is from April 1, 2008 to October 31, 2008.

On February 14, 2008 the Company entered into a natural gas swap arrangement, which will fix the price realized by Vero at \$7.50 CDN per gigajoule on 5,000 gigajoules per day for the period of April 1, 2008 to October 31, 2008.

Effective February 22, 2008, the Company entered into a natural gas costless collar for 5,000 gigajoules per day at a floor of \$7.00 CDN per gigajoule and a ceiling of \$8.80 CDN per gigajoule. The contract term is from April 1, 2008 to October 31, 2008.

Effective February 25, 2008, the Company entered into a natural gas costless collar for 10,000 gigajoules per day at a floor of \$7.75 CDN per gigajoule and a ceiling of \$9.50 CDN per gigajoule. The contract term is from November 1, 2008 to December 31, 2008.