

MANAGEMENT'S REPORT

To the Shareholders of Vero Energy Inc.

Management's Responsibility for Consolidated Financial Statements:

The accompanying consolidated 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.

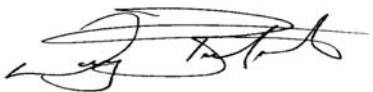
The consolidated financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles. When alternative accounting methods exist, management has chosen those methods it deems most appropriate in the circumstances. Financial statements are not precise 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's Assessment of Internal Controls over Financial Reporting

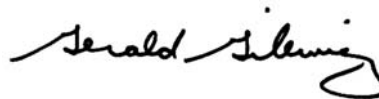
Management is also responsible for establishing and maintaining adequate internal control over the Company's financial reporting. Management has established systems of internal controls, which are designed to provide reasonable assurance the Company's assets are safeguarded from loss or unauthorized use and to produce reliable accounting records for the preparation of financial information. Internal control systems, no matter how well designed have inherent limitations. Therefore, even those systems that have been determined to be effective can only provide reasonable assurance with respect to financial statement preparation and presentation.

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 both management and the auditors. The results of this review have been reported to the Board of Directors, which in turn has approved the consolidated 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 8, 2010

VERO ENERGY INC.

Consolidated Statements of Operations, Comprehensive (Loss) Income and Retained Earnings

(in thousands of Canadian dollars, except per share data)

	2009	2008
REVENUE		
Production revenue	78,144	138,962
Realized (loss) gain on risk management activities	(2,938)	(1,107)
Unrealized loss on risk management activities	(1,245)	-
	73,961	137,855
Royalties	(11,127)	(35,601)
Interest and other	217	13
	63,051	102,267
EXPENSES		
Operating	23,254	16,704
Transportation	3,235	2,942
General and administrative	5,851	4,461
Stock based compensation (Note 9(e))	4,851	2,575
Interest and bank charges	4,406	2,559
Depletion, depreciation and accretion	47,961	40,917
	89,558	70,158
(LOSS) INCOME BEFORE INCOME TAXES	(26,507)	32,109
INCOME TAX (RECOVERY) EXPENSE (Note 8)		
Future	(6,451)	10,240
	(6,451)	10,240
NET (LOSS) EARNINGS AND COMPREHENSIVE (LOSS) INCOME	(20,056)	21,869
RETAINED EARNINGS, BEGINNING OF PERIOD	25,851	4,864
Repurchase of shares (Note 9(g))	(11)	(882)
RETAINED EARNINGS, END OF PERIOD	5,784	25,851
NET (LOSS) EARNINGS PER SHARE (Note 11)		
Basic	(0.50)	0.67
Diluted	(0.50)	0.67

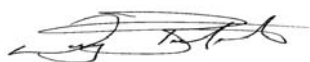
VERO ENERGY INC.**Consolidated Balance Sheets****As at December 31,***(in thousands of Canadian dollars)*

	<u>2009</u>	<u>2008</u>
ASSETS		
CURRENT		
Accounts receivable	29,541	29,218
Prepaid expenses and deposits	4,566	5,294
Loans receivable (Note 15(c))	2,289	350
	<u>36,396</u>	<u>34,862</u>
Property and equipment (Note 5)	287,645	297,697
Goodwill (Note 4)	19,913	19,913
	<u>343,954</u>	<u>352,472</u>
LIABILITIES		
CURRENT		
Accounts payable and accrued liabilities	47,588	63,354
Risk management contracts	1,132	-
Bank debt (Note 6)	77,719	75,419
	<u>126,439</u>	<u>138,773</u>
Risk management contracts	113	-
Asset retirement obligations (Note 7)	5,379	5,570
Future income taxes (Note 8)	15,286	17,416
	<u>147,217</u>	<u>161,759</u>
SHAREHOLDERS' EQUITY		
Share capital (Note 9)	181,343	160,103
Contributed surplus (Note 10)	9,610	4,759
Retained Earnings	5,784	25,851
	<u>196,737</u>	<u>190,713</u>
	<u>343,954</u>	<u>352,472</u>

Commitments (Note 12)

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

Paul R. Baay, Director

Douglas J. Bartole, Director

VERO ENERGY INC.

Consolidated Statements of Cash Flows

(in thousands of Canadian dollars)

	2009	2008
CASH FLOWS RELATED TO THE FOLLOWING ACTIVITIES:		
OPERATING		
Net (loss) earnings	(20,056)	21,869
Adjustments for:		
Unrealized loss on risk management contracts	1,245	-
Stock based compensation	4,851	2,575
Depletion, depreciation and accretion	47,961	40,917
Future income taxes	(6,451)	10,240
Asset retirement costs incurred	(571)	(222)
	26,979	75,379
Changes in non-cash working capital (Note 13(a))	(24,835)	659
	2,144	76,038
FINANCING		
Increase in bank debt	2,300	18,417
Proceeds from private placements, net of share issue costs (Note 9(a))	25,636	16,759
Repurchase of shares (Note 9(g))	(86)	(2,597)
Loans to officers/director (Note 15(c))	(1,939)	(350)
Proceeds from stock option exercises (note 9(d))	-	4,378
	25,911	36,607
INVESTING		
Corporate acquisitions (Note 4)	-	(2,816)
Additions to petroleum and natural gas properties	(53,507)	(106,308)
Purchase of petroleum and natural gas assets	(350)	(19,537)
Disposals of petroleum and natural gas assets	16,335	15
Additions to administrative assets	(7)	(39)
Changes in non-cash working capital (Note 13(a))	9,474	16,040
	(28,055)	(112,645)
NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS	-	-
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD	-	-
CASH AND CASH EQUIVALENTS, END OF PERIOD	-	-

Supplementary cash flow information (Note 13(b))

**Notes to the Consolidated Financial Statements
For the Years Ended December 31, 2009 and 2008**

(in thousands, except per share data)

1. NATURE OF OPERATIONS

Vero Energy Inc. (“Vero or “the Company”) is a resource based corporation engaged in the exploration for, and the development and production of natural gas, natural gas liquids and crude oil primarily in Alberta, Canada. The Company was incorporated on September 23, 2005 and 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”). Under the Arrangement Vero acquired certain producing and non-producing oil and gas assets.

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 accounts receivable, loans receivable, deposits, derivative financial instruments, accounts payable and accrued liabilities, and the bank credit facility. Financial instruments are measured at fair value on initial recognition of the instrument. Measurement in subsequent periods depends on whether the financial instrument has been classified as “held-for-trading”, “held-to-maturity”, “loans and receivables”, or “other financial liabilities” as defined by the accounting standard for financial instruments. Financial assets and liabilities “held-for-trading” are measured at fair value with changes in those values recognized in earnings. “Loans and receivables” and “other financial liabilities” are measured at cost.

Deposits and risk management liabilities are designated as “held-for-trading”. Accounts receivable and loans receivable are designated as “loans and receivables”. Accounts payable and accrued liabilities and Vero’s credit facility are designated as “other financial liabilities”.

**Notes to the Consolidated Financial Statements
For the Years Ended December 31, 2009 and 2008**

(in thousands, except per share data)

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

c) 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 unproved properties, are depleted using the unit-of-production method. This method uses 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 unproved properties are 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.

d) 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 net of drilling incentive credits 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 Consolidated Financial Statements
For the Years Ended December 31, 2009 and 2008***(in thousands, except per share data)*

2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)*e) 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 any 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. As at December 31, 2009 and 2008, there was no impairment of goodwill.

f) 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 and a reasonable estimate of fair value can be made. 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.

g) 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 accumulated future income tax assets and liabilities is recognized in income in the period that the change occurs.

Notes to the Consolidated Financial Statements
For the Years Ended December 31, 2009 and 2008
(in thousands, except per share data)

2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

h) 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.

i) Transportation costs

Costs paid by Vero for the transportation of natural gas, crude oil and natural gas liquids are recognized when the product is delivered and the services provided.

j) Equity based compensation

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 vesting period 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.

In 2009 the Company instituted a directors compensation plan which is described in Note 9(f). The intrinsic value of vested cash settled compensation awards is calculated at each reporting period and recorded as a liability. Compensation expense associated with the liability based compensation plan is recognized in income over the vesting period of the units granted based on their intrinsic value at each reporting period. Cash payments derived from the exercise of these units are recorded as a reduction in the liability at the exercise date.

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 cost of unproved properties. By their nature, these estimates are subject to measurement

Notes to the Consolidated Financial Statements
For the Years Ended December 31, 2009 and 2008
(in thousands, except per share data)

2. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

k) Measurement uncertainty (continued)

uncertainty and the effect on the financial statements of changes of estimates in future periods could be significant.

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. In addition, the measurement of Vero's income tax liability and tax pools requires interpretation of complex laws and regulations. All tax filings are subject to audit and reassessment, potentially several years after the initial filing. Accordingly, actual income tax assets and liabilities may differ significantly from the amounts initially estimated.

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 Consolidated Financial Statements
For the Years Ended December 31, 2009 and 2008**

(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.

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 subscription 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 for the shares. In recognition of the foregone tax benefits to the Company, the amount for which the shares are issued is reduced by the tax effect of the tax deductions renounced to subscribers at the time the renunciation documents are filed with the tax authorities.

p) Leases

All of the Company's leases are considered to be operating leases and are charged to expense on a straight-line basis.

q) Debt transaction costs and discounts

Debt transaction costs and discounts are capitalized within bank debt and are being amortized using the effective interest method.

3. CHANGES IN ACCOUNTING POLICIES

The following accounting pronouncements have been adopted for the current year.

a) Goodwill and intangible assets

Effective January 1, 2009, the Company adopted the new Canadian standard, Handbook Section 3064, Goodwill and Intangible Assets, which replaced Handbook Section 3062, Goodwill and Other Intangible assets. The new standard introduces guidance for the recognition, measurement and disclosure of goodwill and intangible assets, including internally generated intangible assets. The standard also harmonizes Canadian standards with IFRS and applies to interim and annual financial statements for fiscal years beginning on or after October 1, 2008. There was no material impact to the consolidated financial statements as a result of the implementation of the new standard.

**Notes to the Consolidated Financial Statements
For the Years Ended December 31, 2009 and 2008**

(in thousands, except per share data)

3. CHANGES IN ACCOUNTING POLICIES (CONTINUED)

b) Financial Instruments - Disclosures

In June, 2009 the CICA issued amendments to Handbook Section 3862, Financial Instruments – Disclosures. The amendments provide for enhanced disclosures on liquidity risk and require disclosures on fair value measurements of financial instruments. These requirements harmonize Canadian standards with IFRS and apply to annual financial statements for the fiscal years ending after September 30, 2009.

Recent accounting pronouncements issued and not yet adopted

International Financial Reporting Standards (IFRS)

The Accounting Standards Board (AcSB) has announced that Canadian publicly accountable enterprises will be required to adopt IFRS effective January 1, 2011. Although IFRS employs a conceptual framework that is similar to Canadian GAAP, there are significant differences in recognition, measurement, and disclosure. Vero has undertaken a project to assess the potential impacts of the transition to IFRS and has developed a plan to ensure compliance with the new standards.

The Corporation has completed its initial phase of the implementation which included diagnostic analysis of Vero's accounting data and a high-level assessment of key areas that may be impacted by the adoption of IFRS. This analysis resulted in prioritization of areas to be evaluated in the next phase, component evaluation. This phase, which is currently in progress, includes the analysis of accounting policy alternatives available under IFRS as well as the determination of changes required to existing information systems and business processes. As of the middle of 2009 the systems changes necessary to support the IFRS conversion had been implemented. Vero continues to assess the impact of the conversion on internal controls over financial reporting and disclosure controls and procedures and will continue to invest in training and resources throughout the transition period.

Vero will be required to adopt the following CICA Handbook sections as of January 1, 2011:

a) The CICA issued Handbook Section 1582 *Business Combinations*, which replaces Section 1581. This new standard aligns accounting for business combinations under Canadian GAAP with IFRS and is effective for business combinations entered into on or after January 1, 2011. The new standard requires assets and liabilities acquired in a business combination, contingent consideration and certain acquired contingencies to be measured at their fair values as of the acquisition date. The adoption of the revised standard is expected to impact Vero's financial statements only to the extent that business combinations are entered into after the effective date.

b) "Consolidated Financial Statements", Section 1601, which together with Section 1602 below, replace the former consolidated financial statements standard. Section 1601 establishes the requirements for the preparation of consolidated financial statements. It is not anticipated that the adoption of this standard will have a material impact on Vero's Consolidated Financial Statements.

**Notes to the Consolidated Financial Statements
For the Years Ended December 31, 2009 and 2008**

(in thousands, except per share data)

3. CHANGES IN ACCOUNTING POLICIES (CONTINUED)

c) "Non-controlling Interests", Section 1602. The standard establishes the accounting for a non-controlling interest in a subsidiary in consolidated financial statements subsequent to a business combination. This standard requires a non-controlling interest in a subsidiary to be classified as a separate component of equity. In addition, net earnings and components of other comprehensive income are attributed to both the parent and non-controlling interest. It is not anticipated that the adoption of this standard will have a material impact on Vero's Consolidated Financial Statements.

4. CORPORATE ACQUISITIONS

a) Acquisition of Dorian Energy Inc.

Effective April 15, 2008 Vero acquired all of the outstanding common shares of Dorian Energy Inc. ("Dorian"). Dorian shareholders received 0.294 of a Vero common share for each Dorian share held. A total of 1,835 Vero common shares were issued. The price ascribed to each common share of \$8.22 was based on the average trading price of Vero common shares on the five days prior, the day of, and the five days following the date the purchase was entered into. The operating results and corresponding cash flow and earnings related to the acquisition were included in the Company's consolidated financial statements effective April 16, 2008. The acquisition was accounted for using the purchase method and the purchase price was allocated based on fair values as follows:

Consideration paid:	
Issuance of 1,835 common shares (Note 9(b))	15,087
Transaction costs	165
	15,252
Allocation of purchase price:	
Current assets	3,594
Current liabilities	(2,763)
Risk management on acquired contract	(381)
Debt assumed	(2,200)
	(1,750)
Property, plant and equipment	13,380
Goodwill	4,879
Asset retirement obligations	(210)
Future income taxes	(1,047)
	15,252

Notes to the Consolidated Financial Statements
For the Years Ended December 31, 2009 and 2008

(in thousands, except per share data)

4. CORPORATE ACQUISITIONS (continued)

b) Acquisition of FX Energy Ltd.

Effective May 21, 2008 Vero acquired all of the outstanding common shares of FX Energy Ltd. ("FX"). FX shareholders received \$0.25043 per common share outstanding. The operating results and corresponding cash flow and earnings related to the acquisition were included in the Company's consolidated financial statements effective May 22, 2008. 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 FX shareholders	2,374
Transaction costs	67
	2,441
Allocation of purchase price:	
Current assets	366
Current liabilities	(107)
Debt assumed	(1,595)
	(1,336)
Property, plant and equipment	2,050
Asset retirement obligations	(41)
Future tax benefit	1,768
	2,441

c) Acquisition of Revolve Energy Inc.

Effective November 10, 2008 Vero acquired all of the outstanding common shares of Revolve Energy Inc. ("Revolve"). Revolve shareholders received 0.135 of a Vero common share for each Revolve share held. A total of 3,816 Vero common shares were issued. The price ascribed to each common share of \$6.20 was based on the average trading price of Vero common shares on the five days prior, the day of, and the five days following the date the purchase was entered into. The operating results and corresponding cash flow and earnings related to the acquisition were included in the Company's consolidated financial statements effective November 11, 2008. The acquisition was accounted for using the purchase method and the purchase price was allocated based on fair values as follows:

Consideration paid:	
Issuance of 3,816 common shares (Note 9(c))	23,659
Transaction costs	210
	23,869
Allocation of purchase price:	
Current assets	4,996
Current liabilities	(2,087)
Debt assumed	(7,194)
	(4,285)
Property, plant and equipment	23,599
Asset retirement obligations	(911)
Future tax benefit	5,466
	23,869

Notes to the Consolidated Financial Statements
For the Years Ended December 31, 2009 and 2008
(in thousands, except per share data)

5. PROPERTY AND EQUIPMENT

	December 31, 2009		
	Cost	Accumulated depletion, depreciation and accretion	Net Book Value
Petroleum and natural gas properties and facilities	434,235	(146,711)	287,524
Administrative assets	291	(170)	121
	434,526	(146,881)	287,645

	December 31, 2008		
	Cost	Accumulated depletion, depreciation and accretion	Net Book Value
Petroleum and natural gas properties and facilities	396,785	(99,246)	297,539
Administrative assets	284	(126)	158
	397,069	(99,372)	297,697

Undeveloped land costs and salvage values excluded from the depletion calculation as at December 31, 2009 were \$20,157 (December 31, 2008 - \$24,428). Future development costs on proved undeveloped reserves of \$42,169 (December 31, 2008 - \$59,931) were included in the depletion calculation. For the year ended December 31, 2009, the Company capitalized \$922 (December 31, 2008 - \$688) in salary and wages directly related to exploration and development activities.

Notes to the Consolidated Financial Statements
For the Years Ended December 31, 2009 and 2008

(in thousands, except per share data)

5. PROPERTY AND EQUIPMENT (continued)

The Company performed a ceiling test calculation as at December 31, 2009 to assess the recoverable value of petroleum and natural gas properties and equipment. The table below summarizes the benchmark prices for the next ten years used by the independent reserve evaluators in preparing the Company's reserve report. Based on the expected future commodity prices no write-down was required for the year ended December 31, 2009.

	WTI Cushing Oklahoma (\$US/bbl)	Edmonton Par 40 d API (\$Cdn/bbl)	Alberta AECO-C (\$Cdn/mmbtu)	Natural Gas Liquids (Pentane) (\$Cdn/bbl)
2010	82.28	77.50	6.20	81.17
2011	86.46	82.17	7.09	86.32
2012	88.53	85.60	7.40	90.02
2013	90.13	89.38	7.83	93.95
2014	92.01	93.62	8.17	98.34
2015	93.85	97.62	8.42	102.48
2016	95.72	101.17	8.65	106.19
2017	97.64	103.36	8.99	108.41
2018	99.59	105.54	9.32	110.66

The annual escalation rate used after 2018 is 2.0%.

6. BANK DEBT

The Company has a \$115,000 (December 31, 2008 - \$100,000), syndicated, credit facility and is comprised of a combination of: letters of credit, banker's acceptances and a revolving line of credit. The authorized limit is subject to both annual and semi-annual, borrowing base reviews by the syndicate. The facility is available to the Company at their discretion until March 31, 2010. At that date Vero may request a renewal of the facility for a period of up to 364 days. The facility is secured by a \$300,000 floating charge debenture over all the assets of the Company.

Advances under the facility are available by way of prime rate loans with interest rates of between 1.75 percent and 3.25 percent over the bank's prime lending rate. In addition to these advances, the Company has access to banker's acceptances and LIBOR loans, which are subject to stamping fees and margins ranging from 2.75 percent to 4.25 percent depending on the debt to cash flow ratio as calculated at the Company's immediately preceding quarters' end. Standby fees are charged on the undrawn facility at rates ranging from 0.6875 percent to 1.0625 percent depending on the debt to cash flow ratio at the Company's previous quarter end. For the year ended December 31, 2009 the effective interest rate of the Company was 4.1% (December 31, 2008 - 4.9%).

Debt discounts and transaction costs are capitalized within bank debt and are being amortized using the effective interest method. During 2009 \$4,018 (2008 - Nil) in transaction costs and discounts have been capitalized relating to the issuance of the revolving line of credit and bankers acceptances.

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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, 2009 to be \$12,721 (2008 - \$13,106), which will be incurred at various times between 2010 and 2024. The fair value of the asset retirement obligations incurred in the period ended December 31, 2009 was calculated using an average credit-adjusted risk free rate of 7.9% (2008 – 8.0%) and an average inflation factor of 1.8% (2008 – 1.7%). Settlement of the obligations will be funded from general corporate funds at the time of retirement or removal. As at December 31, 2009, no funds have been set aside to settle these obligations. Changes to asset retirement obligations during the period were as follows:

	2009	2008
Asset retirement obligations at beginning of period	5,570	2,641
Liabilities acquired on corporate acquisitions (Note 4)	-	1,162
Liabilities disposed of during the year	(140)	-
Liabilities incurred during the period	51	1,461
Liabilities settled during the period	(571)	(222)
Change in estimated future cash flows	17	220
Accretion	452	308
Asset retirement obligations at end of period	5,379	5,570

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8. INCOME TAXES

The provision for income tax reflects an effective rate which differs from the expected, statutory, federal and provincial tax rates. Differences for the years ended December 31, 2009 and 2008 are as follows:

	<u>2009</u>	<u>2008</u>
(Loss) income before income taxes	<u>(26,507)</u>	32,109
Expected income tax (benefit) expense at the statutory rate of 29.0% (2008 – 29.5%)	(7,687)	9,472
Tax effect of non-deductible and non-taxable amounts related to:		
Stock based compensation expense and other non-deductible amounts	1,420	784
Change in tax rates	(188)	-
Reconcile book to actual on filing tax returns	13	17
Other	(9)	(33)
Total income tax provision	(6,451)	10,240

The income tax provision is comprised of:

	<u>2009</u>	<u>2008</u>
Future income taxes	(6,451)	10,240

The future income tax liability is comprised of the following:

	<u>2009</u>	<u>2008</u>
Future income tax liabilities:		
Temporary differences relating to capital assets	18,520	20,643
Future income tax assets:		
Asset retirement obligations	(1,345)	(1,392)
Unrealized financial contract losses	(349)	-
Loss carryforwards	(545)	(970)
Financing costs and other	(972)	(861)
Other	(23)	(4)
	(3,234)	(3,227)
Net future income tax liability	15,286	17,416

As at December 31, 2009, Vero had \$222,944 (2008 - \$228,451) of tax pools available for deduction in future years. Included in this amount is \$2,227 (2008 – \$3,877) of non-capital losses, which expire at various times between 2014 and 2018.

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9. SHARE CAPITAL

	Shares (000's)	Amount
Authorized		
Unlimited number of voting common shares, no par value		
Unlimited number of first preferred shares, no par value		
Issued		
<i>Common shares</i>		
Total share capital at December 31, 2007	28,915	103,077
Private placement, net of share issue costs (a)	1,940	16,759
Issued on corporate acquisition (b)	1,835	15,087
Issued on corporate acquisition (c)	3,816	23,659
Exercise of stock options (d)	871	5,787
Normal course issuer bid (g)	(408)	(1,715)
Adjustment for tax benefits from share issue costs	-	356
Adjustment for tax cost of flow-through shares	-	(2,907)
Total share capital at December 31, 2008	36,969	160,103
Normal course issuer bid (g)	(17)	(75)
Adjustment for tax cost of flow-through shares (a)	-	(4,844)
Private placement, net of share issue costs (a)	4,000	13,916
Private placement, net of share issue costs (a)	2,231	11,720
Adjustment for tax benefits from share issue costs	-	523
Total share capital at December 31, 2009	43,183	181,343

a) Private Placements

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 net proceeds of issuance of \$16,759 were comprised of gross proceeds of \$17,945 less expenses of the issue of \$1,186. The tax effect of the tax benefits renounced to subscribers in respect of the Flow-Through shares was recognized in the current period which is when the renunciation documents were filed with the taxation authorities. This renunciation resulted in \$4,844 in future tax liability being offset to share capital. Using a combination of the regular, and the "look-back" provisions of the Income Tax Act, the Company was required to incur eligible expenditures in the amount of \$17,945 prior to December 31, 2009 (Note 12(e)).

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9. SHARE CAPITAL (continued)

On May 21, 2009 the Company closed a placement for the issuance of 4,000 common shares at a price of \$3.75 per share. The net proceeds of issuance of \$13,916 were comprised of gross proceeds of \$15,000 less expenses of the issue of \$1,084.

On November 3, 2009 the Company closed a private placement for the issuance of 2,231 Flow-Through common shares at a price of \$5.65 per share. The net proceeds of issuance of \$11,720 were comprised of gross proceeds of \$12,609 less expenses of the issue of \$889. The Company is required to incur eligible expenditures in the amount of \$12,609 prior to December 31, 2010 (Note 12(e)).

b) Acquisition of Dorian Energy Inc.

On April 15, 2008 Vero acquired all of the outstanding shares of a private company. Upon closing of the acquisition, 1,835 common shares were issued at a deemed value of \$15,087 (Note 4(a)).

c) Acquisition of Revolve Energy Inc.

On November 10, 2008 Vero acquired all of the outstanding shares of a private company. Upon closing of the acquisition, 3,816 common shares were issued at a deemed value of \$23,659 (Note 4(c)) or \$6.20 per share.

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, 2009 there were 4,318 (2008 – 3,697) 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.

No stock options were exercised in 2009. During the year ended December 31, 2008, 871 stock options were exercised. \$5,787 was credited to share capital, which was made up of \$4,378 in cash proceeds and \$1,409 for the reversal of amounts previously credited to contributed surplus (Note 10).

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9. SHARE CAPITAL (continued)

As at December 31, the following stock options were outstanding:

	2009		2008	
	Stock Options	Weighted Average Exercise Price \$	Stock Options	Weighted Average Exercise Price \$
Outstanding, beginning of year	3,085	6.69	2,434	5.18
Granted	1,840	3.83	1,528	8.16
Exercised	-	-	(871)	5.03
Surrendered for cancellation	(682)	7.90	-	-
Forfeited	(40)	5.39	(6)	5.90
Outstanding, end of year	4,203	5.26	3,085	6.69
Exercisable, end of year	1,690	5.62	719	5.31

Exercise Price	Options Outstanding					
	December 31, 2009			December 31, 2008		
	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
\$3.00 – 3.70	694	3.46	4.5	-	-	-
\$4.02 – 5.61	2,256	4.49	3.0	1,212	4.97	2.1
\$5.90 - 7.71	1,038	7.26	3.2	1,315	7.14	4.0
\$8.34 – 9.50	215	9.44	3.5	558	9.41	4.5
	4,203	5.26	3.3	3,085	6.69	3.4

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:

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9. SHARE CAPITAL (continued)

	2009	2008
Risk free rate (%)	2.2	3.2
Expected life (years)	5	5
Expected volatility (%)	48	70
Expected dividends	-	-

For the period ended December 31, 2009, 1,840 (2008 – 1,528) 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 \$1.69 (2008 - \$4.93) per share. \$4,851 (2008 - \$2,575) was recorded as stock compensation expense with respect to all options outstanding, with a corresponding credit to contributed surplus (Note 10).

In May of 2009, 682 non-officer, non-director, stock options, having exercise prices ranging from \$5.15 to \$10.80, were surrendered for cancellation. Included in the stock based compensation expense for the year was the remaining, unamortized stock based compensation costs associated with the cancelled options in the amount of \$1,116.

f) Directors Compensation Unit Plan

In November of 2009 Vero established a Directors Compensation Plan which includes compensation units granted only to directors of the Company. These units vest annually over a three year period and expire three years from the date of grant. Upon vesting, the holder is entitled to exercise the units for cash equal to the amount by which the exercise price (the fair value of a Vero common share on the date of exercise) exceeds the grant price (the fair value of a Vero common share on the date of grant). On November 9, 2009 225 units were issued to directors of Vero. Included in accounts payable and accrued liabilities is \$5 (2008 – nil) pertaining to these grants.

g) Normal Course Issuer Bid

In August of 2007, the Toronto Stock Exchange approved the Company's application to initiate a Normal Course Issuer Bid ("Bid"). The Bid is renewable on a yearly basis. In August of 2008 the Company renewed its Bid for an additional year. Under each Bid, Vero was entitled to purchase up to 5% of its outstanding common shares. During the year ended December 31, 2009, the Company purchased and subsequently cancelled 17 (2008 – 408) common shares pursuant to its Normal Course Issuer Bid. The aggregate cost of the purchases was \$86 (2008 – \$2,597) of which \$75 (2008 – \$1,715) was charged to share capital based on the average book value per share as of the date of repurchase, and the balance of \$11 (2008 – \$882) was charged to retained earnings. The average per share cost of the repurchase in 2009 was \$4.95 (2008 - \$6.36).

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10. CONTRIBUTED SURPLUS

The following table reconciles the Company's contributed surplus:

	2009	2008
Balance at January 1	4,759	3,593
Stock-based compensation expense	4,851	2,575
Exercise of stock options (Note 9(d))	-	(1,409)
Balance at December 31	9,610	4,759

11. PER SHARE AMOUNTS

The following table summarizes the shares used in calculating net (loss) earnings per share for the years ended December 31,:

Basic (loss) earnings per share computation	2009	2008
Net (loss) earnings	(20,056)	21,869
Weighted average shares outstanding - basic	39,762	32,623
Basic (loss) earnings per share	(0.50)	0.67

Diluted (loss) earnings per share computation	2009	2008
Net (loss) earnings	(20,056)	21,869
Weighted average shares outstanding - basic	39,762	32,623
Dilutive stock options outstanding	-	2,527
Shares notionally repurchased with proceeds from dilutive Stock options and returned to treasury	-	(2,360)
Weighted average shares outstanding - diluted	39,762	32,790
Basic (loss) earnings per share	(0.50)	0.67

At December 31, 2009, 4,203 (2008 – 660) of the issued stock options were excluded from the calculation of diluted weighted average shares outstanding as to include them would be anti-dilutive.

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12. 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:

	2009	2008
2009	-	387
2010	410	374
2011	406	370
2012	269	246
2013	14	13
Total minimum payments	1,099	1,390

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:

	2009	2008
2009	-	1,210
2010	1,045	1,045
2011	651	650
Total minimum payments	1,696	2,905

Included above is the commitment with respect to two leased premises. One is the head office of Vero and the other one is in respect of leased premises acquired pursuant to one the corporate acquisitions described in Note 4. The Company has sub-leased the premises related to the acquisition.

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. Currently, there are several statements of claim which have been filed against the Company. Management of the corporation does not believe that any of the lawsuits have merit and consequently have not made any provision in these financial statements for any loss. In addition, Management is not currently aware of any other claims or actions, actual or threatened, which would materially affect the Corporation's reported financial position or results from operations.

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12. COMMITMENTS (CONTINUED)

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 and other capital commitments

As at December 31, 2009 Vero had committed to drill and complete, or recomplete 5 (5.0 net) (2008 – 8 (6.7 net)) wells in Alberta with expected commencement dates that are all in 2010. The commitments are pursuant to farm-in agreements with industry partners. The Company expects to satisfy its net portion of the commitments at an estimated cost of \$10,100 (2008 – \$10,788).

e) Flow-Through shares

Pursuant to the Flow-Through share private placement entered into on November 3, 2009 (Note 9(a)) the Company was obligated to incur \$12,609 in eligible costs by December 31, 2010. As at December 31, 2009 the Company has \$11,725 remaining on this commitment.

Pursuant to the Flow-Through share private placement entered into on February 28, 2008 (Note 9(a)) the Company was obligated to incur \$17,945 in eligible costs by December 31, 2009. As at December 31, 2009 Vero had fulfilled this commitment.

13. SUPPLEMENTARY INFORMATION

a) Changes in non-cash working-capital

	2009	2008
Accounts receivable	(323)	(12,451)
Prepaid expenses and deposits	728	(1,771)
Accounts payable and accrued liabilities	(15,766)	27,303
Corporate acquisition of working capital (Note 4)	-	3,618
Change in non-cash working capital	(15,361)	16,699
Relating to:		
Investing activities	9,474	16,040
Operating activities	(24,835)	659
	(15,361)	16,699

b) Supplementary cash flow information

	2009	2008
Interest received	218	13
Interest paid	3,910	2,405

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14. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

The Company holds various forms of financial assets and liabilities. The fair values of financial assets and liabilities and a discussion of the risks associated with these assets and liabilities are presented as follows:

A) Fair Value of Financial Assets and Liabilities

The carrying value of financial instruments, which include accounts receivable, loans receivable, deposits, derivative financial instruments, accounts payable and accrued liabilities, and the bank credit facility approximates amounts at which these instruments could be exchanged in a transaction between knowledgeable and willing parties. The fair value of accounts receivable, loans receivable, deposits, accounts payable and accrued liabilities, and the bank credit facility approximates their carrying amounts due to their short term nature. The fair value of derivative financial instruments is determined by calculating the difference between the contracted price and published forward price curves as at the balance sheet date, and then multiplying this price differential by the contracted commodity volumes. Vero's bank debt bears interest at a floating market rate and accordingly the fair market value approximates the carrying value. The carrying and fair values of the Company's financial instruments as at December 31, 2009 were as follows:

	2009		2008	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
<u>Financial Assets</u>				
Held-for-trading:				
Deposits	4,159	4,159	4,707	4,707
Loans and receivables:				
Accounts receivable	29,541	29,541	29,218	29,218
Loans receivable	2,289	2,289	350	350
<u>Financial Liabilities</u>				
Held-for-trading:				
Risk management liabilities	1,245	1,245	-	-
Other financial liabilities				
Accounts payable and accrued liabilities	47,588	47,588	63,354	63,354
Credit facility	77,719	77,719	75,419	75,419

As at each reporting period the Company will assess whether a financial asset, other than those classified as held-for-trading is impaired. Any impairment loss will be included in earnings for the period.

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14. FINANCIAL INSTRUMENTS (Continued)

Commodity Price Sensitivities

The following table summarizes the sensitivities of the fair value of the Company's risk management positions to fluctuations in commodity price changes while holding all other variables constant. The Company believes that a ten percent change in commodity prices is a reasonable measure of volatility. Based on the crude oil financial instruments that were outstanding at December 31, 2009, fluctuations in commodity prices could have resulted in unrealized gains (losses) that would impact after-tax net earnings as at December 31, 2009 as follows:

	2009	
	Favourable 10% change	Unfavourable 10% change
Crude oil prices	1,464	(1,464)

B) Risks Associated with Financial Assets and Liabilities

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.

Market risk

Market risks are generally those risks that are outside of the control of the Company. These are: commodity prices, foreign exchange rates and interest rates. The objective of the Company is to mitigate exposure to these risks, while maximizing returns to the Company.

Commodity price risk

The resource industry, by its nature is subject to rapid and wide ranging fluctuations in its commodity prices. As a result, the Company is exposed to similar fluctuations in its net earnings. Due to the volatility of commodity prices the Company is exposed to adverse consequences of declining prices. The Company may enter into future related 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. The use of these risk management contracts is governed by a formal policy and is subject to maximum limits established by the Board of Directors. Throughout the year ended December 31, 2009, the Company entered into a variety of risk management contracts. As at December 31, 2009, the Company had the following contracts outstanding:

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14. FINANCIAL INSTRUMENTS (Continued)

Contract	Amount	Term	Price (CDN \$/bbl)	Type
Costless collar	500 bbl/day	April 1 – December 31, 2010	\$75.00 - \$100.00	Financial
Costless collar	1,000 bbl/day	January 1 – March 31, 2010	\$60.00 - \$80.30	Financial

Credit risk

Credit risk arises from the potential loss resulting from a counterparty failing to meet its obligations in accordance with the agreed terms. 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. Wherever possible, the Company requires cash calls from its partners on capital projects before they commence. Receivables related to the sale of the Company's petroleum and natural gas production are mainly from major marketing companies who have very good credit ratings and who have adequate asset backing that secure the revenues. These revenues are normally collected on the 25th day of the month following delivery.

The counter-party with which the Company maintains its risk management contracts (hedges) is a major Canadian chartered bank, which has an investment grade rating.

As at December 31, 2009, accounts receivable and their respective aging were comprised of the following:

	Less than 30 days	31 – 60 days	61 – 90 days	More than 90 days	Total
Sales and accrued revenue receivables	8,908	95	5	2,902	11,910
Joint interest billings with partners	5,023	2,487	833	2,761	11,104
Provincial government incentives	5,228	-	-	-	5,228
Other receivables	1,196	10	1	92	1,299
Total accounts receivable	20,355	2,592	839	5,755	29,541

As at December 31, 2008, accounts receivable and their respective aging were comprised of the following:

	Less than 30 days	31 – 60 days	61 – 90 days	More than 90 days	Total
Sales and accrued revenue receivables	11,213	158	212	1,406	12,989
Joint interest billings with partners	3,973	2,647	1,184	5,684	13,488
Provincial government incentives	-	-	-	590	590
Other receivables	336	1,724	5	86	2,151
Total accounts receivable	16,222	4,529	1,401	7,766	29,218

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14. FINANCIAL INSTRUMENTS (Continued)

The carrying amounts of accounts receivable plus the loans receivable represent the Company's maximum credit exposure. During the year ended December 31, 2009 the Company has not experienced any credit loss in the collection of its accounts or loans receivable. The Company did experience a credit loss of \$230 on one of its natural gas sales receivables during 2008. This loss was related to a counter-party that was inherited from one of the corporate acquisitions. Steps were immediately taken by the Company to terminate this contract upon its default and move the marketing to one of its mainstream marketers. While the loans receivable are secured only with the personal guarantees of the borrowers, they were repaid subsequent to the year-end (Note 15(c)). The Company does not have any allowance for doubtful accounts as at December 31, 2009.

Liquidity risk

Liquidity risk would occur if the Company is not able to meet its financial obligations as they come due. The Company has established a standard of ensuring that it has enough resources available to withstand any downturn in the industry. As our industry is very capital intensive, the majority of our spending is related to our capital programs. See Note 16 for disclosure related to the management of Vero's overall debt position. The Company's goal is to prudently spend its capital while maintaining its credit reputation amongst its suppliers. All of the financial liabilities of the Company are estimated to be settled within one year of the balance sheet date except for a portion of the interest rate swap. The banking credit facility is expected to be renewed by March 31, 2010 and the Company will manage its capital spending to stay within its expected and revised borrowing base limits for 2010.

As at December 31, 2009 the timing of cash outflows relating to financial liabilities are outlined in the table below:

	Less than 1 Year	1-3 Years	4-5 Years	There- after	Total
Accounts payable and accrued liabilities	47,588	-	-	-	47,588
Risk management liabilities	1,132	113	-	-	1,245
Credit facility	77,719	-	-	-	77,719

As at December 31, 2008 the timing of cash outflows relating to financial liabilities are outlined in the table below:

	Less than 1 Year	1-3 Years	4-5 Years	There- after	Total
Accounts payable and accrued liabilities	63,354	-	-	-	63,354
Credit facility	75,419	-	-	-	75,419

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14. FINANCIAL INSTRUMENTS (Continued)

Interest rate risk

Interest rate risk arises from changes in market interest rates that may affect the future cash flows from the Company's financial assets or liabilities. The Company's revolving demand loan facility is subject to floating rates and is therefore exposed to fluctuations in the market rates of interest. From time to time, the Company will enter into a variety of risk management contracts to mitigate its exposure to interest rate risk. The Company had the following interest rate swap in place at December 31, 2009 (2008 – Nil).

Contract	Notional Quantity	Term	Reference	Strike Price	Type
BA Rate	\$25,000/year	January 4, 2010 – January 3, 2012	CAD-BA - CDOR	2.05%	Swap

The contract in place resulted in an unrealized loss for the year ended December 31, 2009 of \$267 (2008 – \$Nil).

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. As a result, the Company is exposed to similar fluctuations in its net earnings. The Company's assessment of the sensitivity of net earnings to interest rate changes while holding all other variables constant and utilizing a one percent change in interest rates is a reasonable measure of volatility. At December 31, 2009 the increase or decrease in net earnings, on an after-tax basis, for a one percent change in interest rates on the floating rate debt amounts to \$566 (2008 - \$691).

Based on the interest rate financial instrument that was outstanding at December 31, 2009, fluctuations in commodity prices could have resulted in unrealized gains (losses) that would impact after-tax net earnings as at December 31, 2009 as follows:

	2009	
	Favourable 1% change	Unfavourable 1% change
Interest rate swap	375	(375)

Foreign currency exchange risk

Even though all of Vero's petroleum and natural gas sales are denominated in Canadian dollars, the underlying market prices for these commodities are impacted by the exchange rate between Canada and the United States. In addition, the fair value of our risk management contracts will fluctuate as a result of changes in foreign exchange rates as most derivative contracts are denominated in US dollars. As the effects of foreign exchange fluctuations are embedded in the Company's results from operations, the aggregate effect of foreign exchange rate fluctuations are not separately identifiable. As at December 31, 2009 the Company had no forward, foreign exchange contracts in place.

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15. RELATED PARTY TRANSACTIONS

During the years ended December 31, 2009 and 2008 the Corporation had the following related party transactions:

- a) Two officers and one director of the Company subscribed for an aggregate of 16 Flow-Through common shares at a price of \$9.25 per share in the February 28, 2008 private placement (note 9(a)). The prices at which the shares were issued were the same as those used in the subscription agreements entered into with non-related parties.
- b) One officer and one director of the Company subscribed for an aggregate of 14 Flow-Through common shares at a price of \$5.65 per share in the November 3, 2009 private placement (note 9(a)). The prices at which the shares were issued were the same as those used in the subscription agreements entered into with non-related parties.
- c) Three officers and one director of the corporation received demand loans from the Company in 2008. As at December 31, 2009 the aggregate amount of these loans outstanding was \$2,289 (2008 - \$350). The loans bear interest at the company's rate of borrowing from its chartered bank plus 25 basis points. Total interest paid during the year was \$164 (2008 - Nil). Included in the accounts receivable balances is \$1 (2008 - \$1) of interest receivable from these related parties. Subsequent to the end of the year all of the loans and accrued interest had been repaid.

16. CAPITAL DISCLOSURES

The Company considers its capital structure to include shareholders' equity, bank debt and working capital. The Company will adjust its capital structure to manage its current and projected debt through the issuance of shares, increasing its bank line of credit and/or adjusting its capital spending. Vero continually monitors its capital structure and makes adjustments to it primarily in light of a combination of, its drilling successes, the general economic conditions in the petroleum industry and global events that may affect commodity prices.

Vero's objectives in managing its capital structure are to:

- 1) create and maintain flexibility so that Vero can continue to meet its financial obligations; and
- 2) finance its growth either through internally generated projects, joint venture relationships or asset/corporate acquisitions.

The Board of Directors reviews and approves any material transactions out of the ordinary course of business, including acquisitions, financing arrangements, transactions with related parties, and the purchase of Vero shares for cancellation pursuant to its normal course issuer bids.

The Company monitors its capital structure primarily using the non-GAAP financial ratio of net debt to funds flow from operations. Vero's objective is to maintain a net debt to funds flow from operations ratio of one and one half times or less in a normalized commodity price and economic environment. This ratio may temporarily increase as a result of an acquisition; or as a result of declining commodity prices, however the Company aims to bring the ratio back to the desired level as soon as possible. Given the declines in commodity prices in 2009 which were mainly attributable to the slowdown in global economies, reduced industrial demand and the resulting increase in natural gas storage, this ratio was in excess of Vero's desired range.

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For the Years Ended December 31, 2009 and 2008

(in thousands, except per share data)

16. CAPITAL DISCLOSURES (CONTINUED)

Throughout the year, the Company monitors this ratio by looking at net debt to annualized quarterly funds flow from operations as the most recent quarter can sometimes be a better indicator due to a rapidly changing environment. Using annualized quarterly funds flow during 2009 the ratio fluctuated between 3.8 in the first quarter of 2009 to 6.6 times at the end of third quarter. Since the ratio was increasing well beyond the desired level, steps were taken to bring this ratio more in line with targets. Two significant steps were taken after the end of the third quarter to assist in this task. First, Vero completed a Flow-Through share private placement in November and second the Company disposed of certain non-core assets in December. The combination of these two initiatives, plus increasing funds flow for the fourth quarter assisted in bringing this ratio to 3.2 (2008 - 1.4) times at the end of the year. The goal for 2010 will be to achieve a ratio of between 1.5 to 2.0 times by the end of the year given the currently anticipated economic conditions and excluding extraordinary items such as an acquisition.

To facilitate the management of this ratio, the Company prepares an annual budget, which is updated monthly for internal, management purposes and takes into account any acquisitions or dispositions; changes in economic circumstances outside the control of the Company; and the success or failure of recently deployed capital. The budget is also updated quarterly for purposes of approving future capital expenditure levels at Board meetings. These budgets are approved by the Board of Directors and capital spending adjusted accordingly. Following is the calculation of net debt to funds flow for each of the years:

	2009	2008
Current assets	36,396	34,862
Accounts payable and accrued liabilities (excluding risk management contracts)	(47,588)	(63,354)
Bank debt	(77,719)	(75,419)
Net debt	(88,911)	(103,911)
	2009	2008
Net (loss) earnings	(20,056)	21,869
Add (deduct):		
Unrealized loss on financial derivatives	1,245	-
Stock-based compensation	4,851	2,575
Depletion, depreciation and accretion	47,961	40,917
Future income taxes	(6,451)	10,240
Funds flow from operations	27,550	75,601
Net debt to funds flow from operations (times)	3.2	1.4

The Company's capital is not subject to any external restrictions as to how it is deployed. The only financial covenant the Company has in respect of its credit facility is that aggregate corporate net debt does not exceed \$130,000. At no time during 2009 did the net debt exceed this level.

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(in thousands, except per share data)

17. SUBSEQUENT EVENT

On February 5, 2010 the Company entered a financial derivative, natural gas basis differential contract. The fixed price under this contract is \$0.35 per million British thermal units and is in respect of 7,500 million British thermal units per day for the period of April 1, 2010 through October 31, 2010.

Contract	Notional Quantity	Term	Reference	Strike Price (USD)	Type
Basis Spread	7,500 MMBTU/day	April 1, 2010 – October 31, 2010	CAD- NYMEX/AECO	\$0.35/MMBTU	Financial