



**X·TERRA**

**RESOURCES CORPORATION**

**X-TERRA RESOURCES CORPORATION**

**INTERIM CONSOLIDATED FINANCIAL STATEMENTS  
SIX-MONTHS PERIOD ENDED JUNE 30, 2008 AND 2007  
(unaudited)**

**FINANCIAL STATEMENTS**

Consolidated Balance Sheets

Consolidated Statements of Operations, Comprehensive loss and Deficit

Consolidated Cash Flows

Notes to Interim Consolidated Financial Statements

The interim consolidated financial statements which are included in this report have not been subject to a review by the Company's external auditors.

# X-TERRA RESOURCES CORPORATION

## CONSOLIDATED BALANCE SHEETS

As at June 30, 2008 and December 31, 2007

	JUNE 30 2008	DECEMBER 31 2007
	(unaudited) \$	(audited) \$
<b>Going concern assumption</b> (note 2)		
<b>Assets</b>		
<b>Current assets</b>		
Cash (note 4)	593,942	472,356
Restricted cash	500	500
Taxes receivable	14,991	15,628
Prepaid expenses	<u>9,091</u>	<u>-</u>
	618,524	488,484
<b>Equipment</b> (note 5)	7,679	-
<b>Mining properties</b> (note 6)	989,757	975,864
<b>Deferred exploration expenses</b> (note 7)	<u>69,029</u>	<u>47,430</u>
	<u>1,684,989</u>	<u>1,511,778</u>
<b>Liabilities</b>		
<b>Current liabilities</b>		
Accounts payable and accrued liabilities	<u>72,054</u>	<u>51,222</u>
<b>Shareholders' Equity (Deficiency)</b>		
<b>Capital stock</b> (note 8)	23,732,912	23,195,520
<b>Warrants</b>	376,520	511,185
<b>Contributed surplus</b> (note 9)	627,705	532,794
<b>Deficit</b>	<u>(23,124,202)</u>	<u>(22,778,943)</u>
	<u>1,612,935</u>	<u>1,460,556</u>
	<u>1,684,989</u>	<u>1,511,778</u>

ON BEHALF OF THE BOARD,

(s) Martin Dallaire, Director

(s) Sébastien Plouffe, Director

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

**X-TERRA RESOURCES CORPORATION****CONSOLIDATED STATEMENTS OF OPERATIONS, COMPREHENSIVE LOSS AND DEFICIT**

Three months period ended June 30 / Six months period ended June 30

	<b>2008</b>	<b>2007</b>	<b>2008</b>	<b>2007</b>
	\$	\$	\$	\$
<b>Going concern assumption</b> (note 2)				
<b>Administrative expenses</b>				
Insurance	3,575	16,000	5,958	16,000
Professional fees	41,847	114,982	44,459	115,754
General administrative expenses	103,948	38,459	139,673	42,412
Shareholder's communication	6,324	1,497	6,324	3,030
Transfer agent and regulatory fees	1,239	24,457	7,125	31,382
Stock-based compensation	129,455	35,970	147,440	35,970
Depreciation of equipment	<u>623</u>	<u>-</u>	<u>623</u>	<u>-</u>
	<u>287,011</u>	<u>231,365</u>	<u>351,602</u>	<u>244,548</u>
<b>Other expenses (Income)</b>				
Interest income	(2,681)	(719)	(6,343)	(719)
General exploration expenses	<u>-</u>	<u>-</u>	<u>-</u>	<u>910</u>
	<u>(2,681)</u>	<u>(719)</u>	<u>(6,343)</u>	<u>191</u>
<b>Net loss and comprehensive loss for the period</b>	<u>284,330</u>	<u>230,646</u>	<u>345,259</u>	<u>244,739</u>
<b>Deficit - Beginning of period</b>	<u>22,839,872</u>	<u>22,501,618</u>	<u>22,778,943</u>	<u>22,487,525</u>
<b>Deficit - End of period</b>	<u>23,124,202</u>	<u>22,732,264</u>	<u>23,124,202</u>	<u>22,732,264</u>
<b>Basic and diluted loss per share</b>	<u>0.04</u>	<u>0.06</u>	<u>0.05</u>	<u>0.06</u>

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

# X-TERRA RESOURCES CORPORATION

## CONSOLIDATED CASH FLOWS

	Three months period ended June 30 / Six months period ended June 30			
	2008	2007	2008	2007
			\$	\$
<b>Going concern assumption</b> (note 2)				
<b>Operating activities</b>				
Net loss for the period	(284,330)	(230,646)	(345,259)	(244,739)
Adjustment for				
Depreciation of equipment	623	-	623	-
Stock-based compensation	<u>129,455</u>	<u>35,970</u>	<u>147,440</u>	<u>35,970</u>
	(154,252)	(194,676)	(197,196)	(208,769)
Changes in non-cash operating working capital items	<u>(9,833)</u>	<u>24,858</u>	<u>12,378</u>	<u>26,938</u>
	<u>(164,085)</u>	<u>(169,818)</u>	<u>(184,818)</u>	<u>(181,831)</u>
<b>Financing activities</b>				
Cash inflow relating to capital stock and warrants	350,198	560,000	350,198	560,000
Due to related party	-	(17,565)	-	(11,782)
Share issuance expenses	<u>-</u>	<u>(34,150)</u>	<u>-</u>	<u>(34,150)</u>
	<u>350,198</u>	<u>508,285</u>	<u>350,198</u>	<u>514,068</u>
<b>Investing activities</b>				
Acquisition of equipment	(8,302)	-	(8,302)	-
Mining properties	(13,236)	-	(13,893)	-
Deferred exploration expenses	<u>(9,894)</u>	<u>-</u>	<u>(21,599)</u>	<u>-</u>
	<u>(31,432)</u>	<u>-</u>	<u>(43,794)</u>	<u>-</u>
<b>Increase in cash and cash equivalents during the period</b>	154,681	338,467	121,586	332,237
<b>Cash and cash equivalents - Beginning of period</b>	<u>439,261</u>	<u>7,757</u>	<u>472,356</u>	<u>13,987</u>
<b>Cash and cash equivalents - End of period</b>	<u><u>593,942</u></u>	<u><u>346,224</u></u>	<u><u>593,942</u></u>	<u><u>346,224</u></u>

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

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**NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS  
FOR THE SIX MONTHS ENDED JUNE 30, 2008 AND 2007**

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(unaudited)

**1 Nature of operations**

The Company is in the business of acquiring, exploring and developing mining and energy properties. As at June 30, 2008, the Company holds the Villedieu, Lindsay, Cool Lake, Rimouski, Rimouski North and Shawinigan properties.

As at June 30, 2008, the Company had cash of \$593,942 and working capital of \$546,470.

The interim consolidated financial statements of the Company have been prepared by management in accordance with Canadian generally accepted accounting principles, except that they do not contain all disclosures as required for annual financial statements. The interim consolidated financial statements have been prepared following the same accounting policies as for the consolidated financial statements for the year ended December 31, 2007 except as noted. Accordingly, they should be read in conjunction with the 2007 consolidated financial statements and the notes thereto.

In the opinion of management, all adjustments considered necessary for fair presentation of the results for the periods presented have been reflected in the interim consolidated financial statements.

**2 Going concern assumption**

These consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles on a going concern basis whereby it is assumed that the Company will realize its assets and assume its liabilities in the normal course of business.

The Company is in the process of exploring its mineral properties and has not yet determined whether these properties contain ore reserves. The recoverability of the amounts shown for mineral properties and related deferred expenditures is dependent upon the ability of the Company to obtain the necessary financing to complete exploration and development and upon future profitable production or proceeds from the disposition of properties. The Company will have to raise additional funds to complete the development phase of its programs and, while it has been successful in doing so in the past, there can be no assurance that it will be able to do so in the future. The application of generally accepted accounting principles on a going concern basis may be inappropriate, since there is a significant doubt as to the going concern assumption.

The financial statements do not reflect the adjustments to the carrying value of assets and liabilities, the reported amounts of revenues and expenses and the classification of balance sheet items if the going concern assumption were inappropriate, and these adjustments could be material. Management did not take these adjustments into account as it believes in the validity of the going concern assumption.

**3 New accounting standards**

On January 1, 2008, the Company adopted new accounting standards related to general standard of financial statement presentation, capital disclosure and financial instruments that were issued by the Canadian Institute of Chartered Accountants ("CICA"). The new CICA standards are as follows:

**Section 1400, *General Standard of Financial Statement Presentation***

This section specifies requirements to assess an entity's ability to continue as a going concern and disclose any material uncertainties that cast doubt on its ability to continue as a going concern. The Company disclosure reflects such assessment.

**Section 1535, *Capital Disclosures***

This section specifies the disclosure of information that enables users of an entity's financial statements to evaluate its objectives, policies and processes for managing capital such as qualitative information about its objectives, policies and processes for managing capital, summary quantitative data about what the entity manages as capital, whether it has complied with any capital requirements and, if it has not complied, the consequences of non-compliance. Disclosure requirements pertaining to this section are contained in note 8.

# X-TERRA RESOURCES CORPORATION

## NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS FOR THE SIX MONTHS ENDED JUNE 30, 2008 AND 2007

(unaudited)

### Section 3862, *Financial Instruments Disclosures*

### Section 3863, *Financial Instruments Presentation*

These sections replace Section 3861, *Financial Instruments Disclosure and Presentation*, revising and enhancing disclosure requirements while carrying forward its presentation requirements. These new sections place increased emphasis on disclosure about the nature and extent of risk arising from financial instruments and how the entity manages those risks. Disclosure requirements pertaining to this section are contained in note 13.

#### 4 Cash

As at June 30, 2008, cash includes an amount of \$251,571 (As at June 30, 2007 – nil) reserved for new exploration activities to be conducted in Canada before December 31, 2008 (note 11).

#### 5 Equipment

	Cost \$	Accumulated Depreciation \$	Net value as at June 30, 2008 \$	Net value as at June 30, 2007 \$
Computer equipment	<u>8,302</u>	<u>623</u>	<u>7 679</u>	<u>-</u>

#### 6 Mining properties

	Balance December 31, 2007 \$	Addition \$	Balance June 30, 2008 \$
Villedieu (100 %)	544,570	-	544,570
Lindsay (100%)	431,294	409	431,703
Cool Lake (100%)	-	2,172	2,172
Rimouski (100%) <sup>(1)</sup>	-	4,500	4,500
Rimouski North (100%) <sup>(1)</sup>	-	4,500	4,500
Shawinigan (100%) <sup>(1)</sup>	<u>-</u>	<u>2,312</u>	<u>2,312</u>
	<u>975,864</u>	<u>13,893</u>	<u>989,757</u>

(1) These properties are part of an assignment with Brownstone Ventures Inc., whereby Brownstone will acquire 50% interest (note 11).

#### 7 Deferred exploration expenses

	Balance December 31, 2007 \$	Addition \$	Balance June 30, 2008 \$
Villedieu (100 %)	600	-	600
Lindsay (100%)	46,830	12,705	59,535
Cool Lake (100%)	<u>-</u>	<u>8,894</u>	<u>8,894</u>
	<u>47,430</u>	<u>21,599</u>	<u>69,029</u>

# X-TERRA RESOURCES CORPORATION

## NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS FOR THE SIX MONTHS ENDED JUNE 30, 2008 AND 2007

(unaudited)

### 7 Deferred exploration expenses (continued)

	Three months period ended June 30 / Six months period ended June 30			
	2008	2007	2008	2007
	\$	\$	\$	\$
<b>Exploration costs</b>				
Accommodations	4,734	-	6,734	28
Maps, printing and drafting	350	-	350	13
Assay and geochemical analysis	-	-	4,825	-
Geology	-	-	1,300	-
Geophysics	4,810	-	7,540	-
Project management fees	-	-	850	67
Salaries and wages	-	-	-	802
	<u>9,894</u>	<u>-</u>	<u>21,599</u>	<u>910</u>
<b>General exploration expenses</b>	<u>-</u>	<u>-</u>	<u>-</u>	<u>(910)</u>
<b>Increase in deferred exploration expenses</b>	9,894	-	21,599	-
<b>Deferred exploration expenses - Beginning of period</b>	<u>59,135</u>	<u>-</u>	<u>47,430</u>	<u>-</u>
<b>Deferred exploration expenses - End of period</b>	<u>69,029</u>	<u>-</u>	<u>69,029</u>	<u>-</u>

### 8 Capital stock, warrants and options

Authorized: Unlimited common shares without par value, of which 7,245,069 common shares were issued as at June 30, 2008 (March 31, 2008: 6,776,671).

The Company defines its capital as the shareholder's equity and cash.

The Company's capital management objectives are to:

- have sufficient capital to be able to meet the Company's mining properties exploration and mining development plan in order to ensure the growth of the activities.
- have sufficient cash to fund the exploration expenses and investing activities and the working capital requirements.

**X-TERRA RESOURCES CORPORATION****NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS  
FOR THE SIX MONTHS ENDED JUNE 30, 2008 AND 2007**

(unaudited)

**8 Capital stock, warrants and options (continued)****Capital stock**

The following table details the changes in the Company's capital stock:

	<b>Number of shares</b>	<b>Amount \$</b>
Balance as at December 31, 2007	6,776,671	23,195,520
Options exercised	62,400	119,928
Warrants exercised	<u>405,998</u>	<u>417,464</u>
Balance as at June 30, 2008	<u>7,245,069</u>	<u>23,732,912</u>

**Warrants**

The following table details the changes in the Company's warrants:

	<b>Number of warrants</b>	<b>Amount \$</b>
Balance as at December 31, 2007	1,587,998	511,185
Exercised during the period	<u>(377,999)</u>	<u>(134,665)</u>
Balance as at June 30, 2008	<u>1,209,999</u>	<u>376,520</u>

Information relating to warrants outstanding as at June 30, 2008 is as follows:

<b>Expiry date</b>	<b>Number of warrants outstanding</b>	<b>Exercise price \$</b>
May 2009	650,000	0.70
October 2009	133,333	0.75
October 2009	<u>426,666</u>	1.00
	<u>1,209,999</u>	



# X-TERRA RESOURCES CORPORATION

## NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS FOR THE SIX MONTHS ENDED JUNE 30, 2008 AND 2007

(unaudited)

### 8 Capital stock, warrants and options (continued)

#### Stock options

In 2002, the Company adopted a stock option plan (the "Option Plan"), as amended, authorizing the granting of stock options to qualified optionees to purchase a total maximum of 10% of the number of outstanding issued common shares of the Company at any time. This is referred to as a "rolling plan". Under the Option Plan, the term of stock options granted may not exceed five years following the date of grant.

The Company applies the fair value method of accounting for stock options, and accordingly the fair value of the vested portion of stock options for the period for \$129,455 has been included in administrative expenses. The attributed amount of share purchase options granted to during the period was estimated using the Black Scholes pricing model with the following assumptions: life of 5 years for these options, risk-free interest rate of 3.24%, volatility of 97% and no expected dividends.

The following table summarizes the information relating to the share purchase options as at June 30, 2008.

	Number	Weighted average exercise price \$
Balance as at December 31, 2007	184,900	1.11
Expired	(7,500)	1.50
Exercised	(62,400)	1.08
Granted	<u>500,000</u>	1.90
Balance as at June 30, 2008	<u>615,000</u>	1.75

Expiry Date	Options outstanding	Exercise price \$
June 2012	115,000	1.10
June 2013	<u>500,000</u>	1.90
	<u>615,000</u>	

### 9 Contributed surplus

The following table details the changes in the Company's contributed surplus:

	2008 \$
Balance as at December 31, 2007	532,794
Stock-based compensation	147,440
Options exercised	<u>(52,529)</u>
Balance as at June 30, 2008	<u>627,705</u>

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**NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS  
FOR THE SIX MONTHS ENDED JUNE 30, 2008 AND 2007**

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(unaudited)

**10 Related party transactions**

The Company is engaged in a lease contract for an office in Rouyn-Noranda with a company controlled by a director and an officer of X-Terra Resources Corporation. During the period, the Company incurred \$6,000 for this leasing (comparable period of 2007: \$0). The Company incurred \$18,000 as management consultant fees from a company controlled by a director of X-Terra (comparable period of 2007: \$0). Also, the Company incurred \$16,050 in administrative services from a company controlled by an officer of X-Terra (comparable period of 2007: \$5,032). The Company incurred no amount as professional fees from a company controlled by a director of X-Terra (comparable period of 2007: \$4,657).

**11 Commitments**

The Company is committed to incurring Canadian exploration expenses of \$320,000 by December 31, 2008, with regard to the transfer of these expenditures to the subscribers of its flow-through share underwriting completed on October 3, 2007. As at June 30, 2008, \$68,429 has been incurred against this commitment.

X-Terra has entered into an assignment agreement with Brownstone Ventures Inc. (TSXV: BWN), whereby Brownstone will acquire a 50% interest in X-Terra's exploration licences for petroleum and natural gas on its shale gas properties (Rimouski, Rimouski North and Shawinigan properties) located in the St-Laurent Lowlands, Quebec (collectively, the "Licences"). In payment, Brownstone Ventures will issue 2,000,000 common shares and 2,000,000 common share purchase warrants to X-Terra. Each warrant will entitle X-Terra to purchase one common share of Brownstone at a price of \$2.00 for a period of two years. Brownstone will be the operator. The assignment agreement is subject to certain conditions, including confirmation of the granting of the Licences by the Ministère des Ressources Naturelles et de la Faune of the Province of Québec to X-Terra, and approval by the TSX Venture Exchange of the assignment of the 50% interest and the issuance by Brownstone to X-Terra of the 2,000,000 shares and warrants in payment.

**12 Subsequent events**

On July 11<sup>th</sup>, 2008 the Company has completed a private placement of 5,000,000 units at a price of \$1.00 per unit, for gross proceeds of \$5,000,000. Each of the units consists of one common share and one common share purchase warrant. Each warrant entitles its holder to purchase one additional common share of X-Terra at a price \$1.50 for two years. PowerOne Capital Markets Limited acted as agent for the private placement. In connection with the private placement, X-Terra paid a cash commission to PowerOne in an amount equal to 8% of the gross proceeds of the private placement, and issued compensation options to PowerOne, entitling it to purchase up to 400,000 units at a price of \$1.00 per unit for a period of two years after the closing of the private placement. Each of the units will be comprised of one common share and one common share purchase warrant. Each warrant will entitle its holder to purchase one additional common share of X-Terra at a price \$1.50 for two years from the closing of the private placement. The proceed will be used for exploration and working capital.

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**NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS  
FOR THE SIX MONTHS ENDED JUNE 30, 2008 AND 2007**

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(unaudited)

**13 Financial risk factors**

The Company's activities are exposed to financial risks: market risk (including currency risk and interest rate risk), credit risk and liquidity risk.

a) Market risks

i) Fair value

The carrying amount of all financial assets and liabilities, as reported on the consolidated balance sheet, approximate their fair value due to the relatively short-term maturities of these instruments.

Fair value estimates are made at the balance sheet date, based on relevant market information and other information about the financial instruments.

ii) Interest rate risk

Interest rate risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate due to changes in market interest rates. All current financial assets and liabilities are not exposed to interest rate risk because of their short-term nature and non-interest bearing.

iii) Currency risk

The Company is not exposed to currency fluctuations as all transactions occur in the functional and reporting currency.

b) Credit risk

Credit risk is the risk that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss. Financial instruments that potentially subject the Company to credit risk consist of cash and tax receivable. The Company has reduced its credit risk by investing its cash with a Schedule 1 Canadian chartered bank. Also, as the majority of its receivables are with the governments of Quebec and Canada in the form of sales tax receivables and government's incentives, the credit risk is minimal.

c) Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet the obligations associated with its financial liabilities. At the end of June 2008, the Company had enough funds available to meet its financial liabilities and future financial liabilities from its commitments for the current year.

**14 Stock-based compensation**

The attributed amount of share purchase options granted to the Directors during the period was estimated using the Black Scholes pricing model with the following assumptions: life of 5 years for these options, risk-free interest rate of 3.24%, volatility of 97% and no expected dividends.

**15 Comparative figures**

Certain comparative figures have been reclassified to conform to the presentation adopted for the period ended June 30, 2008.