

DALMAC ENERGY INC.
Consolidated Financial Statements
Year Ended April 30, 2006



AUDITORS' REPORT

To the Shareholders of **Dalmac Energy Inc.**

We have audited the consolidated balance sheet of **Dalmac Energy Inc.** as at April 30, 2006 and the consolidated statements of income, retained earnings and cash flows for the year then ended. These consolidated financial statements are the responsibility of the company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

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

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the company as at April 30, 2006 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

The consolidated financial statements as at April 30, 2005 and for the sixteen month period then ended, prior to adjustments for the accounting error as described in note 13, were audited by other auditors who expressed an opinion without reservation on those statements in their report dated July 27, 2005. We have audited the adjustments to the 2005 financial statements and in our opinion, such adjustments, in all material respects, are appropriate and have been properly applied.

Edmonton, Canada
July 20, 2006

Signed "Stout & Company LLP"
Chartered Accountants

DALMAC ENERGY INC.
Consolidated Balance Sheet
April 30, 2006

	2006	2005 <i>Restated</i>
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents <i>(Note 3)</i>	\$ 5,570,965	\$ -
Accounts receivable	3,180,717	2,197,000
Inventory	73,359	157,151
Prepaid expenses and deposits	514,824	282,130
Current portion of loan receivable <i>(Note 4)</i>	32,034	-
	9,371,899	2,636,281
RESTRICTED CASH <i>(Note 5)</i>	100,000	-
PROPERTY AND EQUIPMENT <i>(Note 6)</i>	5,180,299	5,495,939
GOODWILL <i>(Note 1)</i>	1,504,313	1,504,313
LOAN RECEIVABLE <i>(Note 4)</i>	102,974	-
	\$ 16,259,485	\$ 9,636,533
LIABILITIES		
CURRENT LIABILITIES		
Bank indebtedness <i>(Note 7)</i>	\$ 597,000	\$ 1,156,733
Accounts payable and accrued liabilities	1,784,858	1,056,702
Income taxes payable	52,776	146,515
Callable debt due within one year <i>(Note 8)</i>	106,212	95,388
Current portion of long term debt <i>(Note 9)</i>	1,224,957	1,201,449
	3,765,803	3,656,787
Callable debt <i>(Note 8)</i>	200,868	261,089
	3,966,671	3,917,876
LONG TERM DEBT <i>(Note 9)</i>	2,440,655	3,147,779
FUTURE INCOME TAXES <i>(Note 10)</i>	311,632	519,000
	6,718,958	7,584,655
SHAREHOLDERS' EQUITY		
SHARE CAPITAL <i>(Note 11)</i>	8,255,693	1,736,980
CONTRIBUTED SURPLUS <i>(Note 12)</i>	292,568	64,692
RETAINED EARNINGS	992,266	250,206
	9,540,527	2,051,878
	\$ 16,259,485	\$ 9,636,533

APPROVED ON BEHALF OF THE BOARD

Signed "John I. Babic" Director

Signed "Shawn T. Szydlowski" Director

See accompanying notes

DALMAC ENERGY INC.
Consolidated Statement of Income
Year Ended April 30, 2006

	2006 <i>(12 months)</i>	2005 <i>(16 months)</i> <i>Restated</i>
Revenue		
Service	\$ 13,073,990	\$ 6,637,667
Product sales	1,704,544	672,276
	14,778,534	7,309,943
Direct costs		
Service	9,230,219	4,153,739
Product sales	1,183,812	445,267
	10,414,031	4,599,006
	4,364,503	2,710,937
Expenses		
General and administrative	1,237,982	751,467
Wages and benefits	1,137,774	580,493
Amortization	737,959	388,846
Interest on long term debt	251,196	118,951
Interest on callable debt and other	67,206	23,665
	3,432,117	1,863,422
Income from operations	932,386	847,515
Other income (expense)		
Interest	34,869	8,944
Loss on disposal of property and equipment	(73,676)	(17,980)
	(38,807)	(9,036)
Income before income taxes	893,579	838,479
Income taxes <i>(Note 10)</i>		
Current	150,645	270,515
Future	874	300,602
	151,519	571,117
NET INCOME FOR THE YEAR	\$ 742,060	\$ 267,362
Net income per share		
Basic	\$ 0.10	\$ 0.08
Diluted	\$ 0.09	\$ 0.07
Weighted average number of shares		
Basic	7,678,768	4,154,757
Diluted	8,106,469	4,816,814

See accompanying notes

DALMAC ENERGY INC.
Consolidated Statement of Retained Earnings
Year Ended April 30, 2006

	2006 <i>(12 months)</i>	2005 <i>(16 months)</i> <i>Restated</i>
RETAINED EARNINGS (DEFICIT) AT BEGINNING OF YEAR		
As previously reported	\$ 310,395	\$ (16,981)
Prior period accounting error <i>(Note 13)</i>	<u>(60,189)</u>	-
As restated	250,206	(16,981)
Net income for the year	<u>742,060</u>	267,362
	992,266	250,381
Dividends	<u>-</u>	(175)
RETAINED EARNINGS AT END OF YEAR	\$ 992,266	\$ 250,206

See accompanying notes

DALMAC ENERGY INC.
Consolidated Statement of Cash Flows
Year Ended April 30, 2006

	2006 (12 months)	2005 (16 months) <i>Restated</i>
OPERATING ACTIVITIES		
Net income for the year	\$ 742,060	\$ 267,362
Items not affecting cash and cash equivalents:		
Amortization	737,959	388,846
Loss on disposal of property and equipment	73,676	17,980
Future income taxes	874	300,602
Stock-based compensation	-	64,692
	1,554,569	1,039,482
Changes in non-cash working capital	(498,205)	(1,176,077)
	1,056,364	(136,595)
INVESTING ACTIVITIES		
Purchase of property and equipment	(747,769)	(5,963,129)
Proceeds on disposal of property and equipment	251,776	78,344
Purchase of goodwill	-	(1,504,313)
Loan receivable	(160,206)	-
Payments received on loan receivable	25,198	-
Increase in restricted cash	(100,000)	-
	(731,001)	(7,389,098)
FINANCING ACTIVITIES		
Dividends paid	-	(175)
Proceeds from issuance of share capital	7,186,674	975,247
Share issuance costs	(648,327)	-
Proceeds from callable debt	70,609	364,426
Proceeds from long term debt	519,254	4,955,504
Repayment of callable debt	(120,006)	(7,949)
Repayment of long term debt	(1,202,869)	(606,276)
(Decrease) increase in bank indebtedness	(559,733)	1,156,733
	5,245,602	6,837,510
Increase (decrease) in cash and cash equivalents	5,570,965	(688,183)
Cash and cash equivalents at beginning of year	-	688,183
CASH AND CASH EQUIVALENTS AT END OF YEAR (Note 3)	\$ 5,570,965	\$ -

SUPPLEMENTARY INFORMATION (Note 14)

See accompanying notes

DALMAC ENERGY INC.
Notes to Consolidated Financial Statements
Year Ended April 30, 2006

1. DESCRIPTION OF OPERATIONS

Dalmac Energy Inc. (the "Company") was incorporated under the Canada Business Corporations Act and is listed on the TSX Venture Exchange. The company is a provider of hot oiler, hydro vac, vacuum, pressure and tanker truck services to the oil and gas industry in Alberta.

Effective November 8, 2004 the Company acquired for cash and common shares, all of the outstanding shares of McClelland Oil Services Inc. (McClelland). McClelland operates a fleet of service vehicles and equipment used in the oil and gas industry in Alberta.

McClelland acquisition

The purchase price was \$2,280,000, comprised of \$911,000 cash, \$509,000 of promissory notes, and 2,150,000 common shares valued at \$0.40 per share totaling \$860,000. The following table summarizes the estimated fair value of the assets acquired and liabilities assumed at the date of acquisition.

Current assets	\$ 2,164,204
Property and equipment	3,900,931
Goodwill	<u>1,222,713</u>
Total assets acquired	<u>7,287,848</u>
Current liabilities	3,047,722
Long-term debt	1,741,728
Other liabilities	<u>218,398</u>
Total liabilities assumed	<u>5,007,848</u>
Net assets acquired	<u>\$ 2,280,000</u>

Effective March 14, 2005, the Company acquired for cash and common shares the assets and business of S Young Oilfield Ltd. (S Young). S Young is engaged in hydro vac operations servicing the oil and gas industry in Alberta.

S Young acquisition

The purchase price was \$850,000, comprised of \$340,000 cash, \$386,000 of promissory notes, and 210,169 common shares valued at \$0.59 per share totaling \$124,000. The following table summarizes the estimated fair value of the assets acquired at the date of acquisition.

Property and equipment	\$ 568,400
Goodwill	<u>281,600</u>
Total assets acquired	<u>\$ 850,000</u>

The results of operations from these acquisitions are included in the accounts from the effective date of acquisition.

DALMAC ENERGY INC.
Notes to Consolidated Financial Statements
Year Ended April 30, 2006

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

(a) Basis of consolidation

The consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries 750761 Alberta Ltd. and McClelland Oil Services Inc.

(b) Cash and cash equivalents

The Company considers cash and short term investments as cash and cash equivalents.

(c) Inventory

Inventory is valued at the lower of cost and net realizable value with the cost being determined on a first-in, first-out basis.

(d) Property and equipment

Property and equipment are recorded at cost and amortized using the straight-line method over their estimated useful lives as follows:

Rental equipment	12 years
Service equipment	12 years
Plant equipment	10 years
Service vehicles	8 years
Trucks	8 years
Office equipment	4 years
Leasehold improvements	Term of lease

(e) Impairment of long-lived assets

In the event that facts and circumstances indicate that the carrying value of long-lived assets may be impaired, the Company performs a recoverability evaluation. If the evaluation indicates that the carrying value of the asset is not recoverable from undiscounted cash flows attributable to the asset, then an impairment loss is measured by comparing the carrying amount of the asset to its fair value.

(f) Goodwill

Goodwill comprises the excess of cost over fair values of the underlying net assets acquired arising from business combinations accounted for using the purchase method. Goodwill is not amortized.

The Company continually evaluates, on a two-step basis, whether an impairment of goodwill has occurred and whether an impairment loss should be recognized. The first test for impairment involves comparing the fair value of the Company with its carrying amount, including goodwill. The fair value of goodwill is determined by the excess of the fair value of the Company over the carrying amounts of its assets and liabilities. If the fair value of the Company exceeds its carrying amount, then goodwill is not considered to be impaired, and the second test is unnecessary. When the fair value of the Company does not exceed its carrying amount, the second test for impairment is performed, which involves comparing the fair value of goodwill with the carrying amount of goodwill. When the carrying amount of the goodwill exceeds the fair value of the goodwill, an impairment loss is recognized in an amount equal to the excess.

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2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES *(continued)*

(g) Income taxes

Income taxes are accounted for by the asset and liability method whereby future tax assets and liabilities are recognized for the future tax consequences attributable to the differences between the financial statement carrying amounts of existing assets and liabilities and their respective income tax bases.

(h) Revenue recognition

Service revenue is recognized when services are performed.

Product sales revenue is recognized when the products are shipped, at which time title passes to the customer.

(i) Use of estimates

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amount of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the period. The significant areas requiring the use of management estimates relate to the amortization of property and equipment, determining the impairment of goodwill and the assumptions used in determining stock based compensation. Actual results could differ from these estimates.

(j) Lease obligations

Leases are classified as capital or operating leases. A lease that transfers substantially all of the benefits and risks incidental to the ownership of property is classified as a capital lease. At the inception of a capital lease, an asset and an obligation are recorded at an amount equal to the lesser of the present value of the minimum lease payments and the property's fair value at the beginning of the lease. All other leases are accounted for as operating leases wherein payments are expensed as incurred.

(k) Asset retirement obligations

The fair value of a liability for an asset retirement obligation is recognized in the period in which it is incurred if a reasonable estimate of fair value can be made. The fair value is added to the carrying amount of the associated asset. The liability is accreted at the end of each period through charges to operating expenses.

(l) Stock-based compensation

Stock-based compensation of employees, directors, officers and consultants is recorded in accordance with the fair value based method.

(m) Net income per share

Basic net income per share is calculated based on the weighted average number of shares outstanding during the year. Diluted net income per share reflects the assumed conversion of all dilutive securities using the treasury stock method. Diluted net income per share figures are equal to those of basic net income per share if the effects of stock options and warrants have been excluded since they are anti-dilutive.

(n) Share issuance costs

Costs related to the issuance of shares (net of the related income effect) are charged against share capital.

DALMAC ENERGY INC.
Notes to Consolidated Financial Statements
Year Ended April 30, 2006

3. CASH AND CASH EQUIVALENTS

	<u>2006</u>	<u>2005</u>
Guaranteed investment certificate	\$ 5,032,274	\$ -
Cash	538,691	-
	<u>\$ 5,570,965</u>	<u>\$ -</u>

4. LOAN RECEIVABLE

Loan, receivable \$3,339 per month, principal and interest at prime plus 1%, due June, 2010. Automotive equipment of the borrower has been pledged as collateral. Approximate principal repayments to be received within the next five years are as follows:

2007	\$ 32,034
2008	33,940
2009	36,393
2010	30,107
2011	<u>2,534</u>
	<u>\$ 135,008</u>

5. RESTRICTED CASH

The Company has a \$100,000 deposit held in trust by legal counsel for a promissory note holder as security for the promissory note in the amount of \$245,402 (see note 9).

DALMAC ENERGY INC.
Notes to Consolidated Financial Statements
Year Ended April 30, 2006

6. PROPERTY AND EQUIPMENT

	Cost	Accumulated amortization	2006 Net book value
Land	\$ 32,657	\$ -	\$ 32,657
Rental equipment	74,573	30,129	44,444
Service equipment	4,449,225	1,497,012	2,952,213
Plant equipment	400,754	156,509	244,245
Service vehicles	3,403,509	1,611,890	1,791,619
Trucks	63,002	45,479	17,523
Office equipment	189,651	134,259	55,392
Leasehold improvements	107,100	64,894	42,206
	\$ 8,720,471	\$ 3,540,172	\$ 5,180,299

	Cost	Accumulated amortization	2005 Net book value
Land	\$ 32,657	\$ -	\$ 32,657
Rental equipment	67,318	24,066	43,252
Service equipment	4,160,383	1,249,377	2,911,006
Plant equipment	391,480	114,295	277,185
Service vehicles	3,463,265	1,394,265	2,069,000
Trucks	103,317	50,203	53,114
Office equipment	158,720	106,247	52,473
Leasehold improvements	103,458	46,206	57,252
	\$ 8,480,598	\$ 2,984,659	\$ 5,495,939

7. BANK INDEBTEDNESS

The Company's credit facility includes a demand revolving operating loan to a maximum of \$1,500,000 (marginated to accounts receivable), at an interest rate of prime plus 1%. At April 30, 2006, \$597,000 (2005 - \$730,000) had been drawn on this facility. In addition, the Company has a demand revolving term loan (see note 8) to a maximum of \$1,500,000 at an interest rate of prime plus 1.25%. At April 30, 2006, \$307,080 (2005 - \$356,477) has been drawn on this facility.

The following has been provided as collateral for bank indebtedness and callable debt (see note 8):

- i) general security agreement providing a first security interest in all present and after acquired property;
- ii) assignment and postponement of creditors claim from a director and former director; and
- iii) assignment of insurance coverage for full insurable values of all assets of the borrower.

As at April 30, 2006, certain debt covenants with respect to the Company's credit facility had not been met.

DALMAC ENERGY INC.
Notes to Consolidated Financial Statements
Year Ended April 30, 2006

8. CALLABLE DEBT

	2006		2005
Bank loan, payable \$657 per month principal, plus interest at prime plus 1.25%.	\$ 22,979	\$	30,863
Bank loan, payable \$7,292 per month principal, plus interest at prime plus 1.25%.	238,110		325,614
Bank loan, payable \$902 per month principal, plus interest at prime plus 1.25%.	45,991		-
	307,080		356,477
Less amount due within one year	(106,212)		(95,388)
	\$ 200,868	\$	261,089

As at April 30, 2006, certain debt covenants with respect to the Company's credit facility had not been met. Unless the bank loans are demanded the approximate principal repayments due within each of the next five years are as follows:

2007	\$	106,212
2008		106,212
2009		81,137
2010		10,824
2011		2,695
		206,880
	\$	307,080

Collateral has been provided for the callable debt (see note 7).

DALMAC ENERGY INC.
Notes to Consolidated Financial Statements
Year Ended April 30, 2006

9. LONG TERM DEBT

	2006	2005
Conditional sales contracts, with interest at rates ranging from 6.60% to 8.75% per annum, repayable in monthly principal and interest payments that vary over the term of each contract, maturing on various dates to April, 2011, secured by specific service vehicles and service equipment (carrying value \$3,913,243).	\$ 2,987,708	\$ 3,436,022
Conditional sales contracts, with interest rates of 8.76% per annum, repayable in monthly principal and interest payments that vary over the term of each contract, maturing on various dates to December, 2007, secured by specific trucks (carrying value \$44,217).	34,491	55,266
Promissory note, payable \$11,701 per month, principal and interest at 4.25%, due March, 2008, secured by a charge against the assets of the company, subrogated to any existing charges.	258,011	384,525
Promissory note due to a former director of the Company, payable \$8,373 per month, principal and interest at 4.25%, due November, 2008, secured by a general security agreement, shares of 750761 Alberta Ltd. sold by the promissory note holder to the Company and \$100,000 of monies in trust (see note 5).	245,402	333,415
Promissory note due to a director of the Company, repayable in equal monthly principal and interest payments of \$4,148 over thirty-six months with the first such payment commencing one month after the promissory note in the amount of \$245,402 (2005 - \$333,415) is paid in full, to bear interest commencing from that date at a rate of 4.25% per annum.	140,000	140,000
	3,665,612	4,349,228
Less current portion	(1,224,957)	(1,201,449)
	\$ 2,440,655	\$ 3,147,779

Approximate principal repayments due within each of the next five years are as follows:

2007	\$ 1,224,957
2008	1,110,088
2009	743,198
2010	409,784
2011 and subsequent	177,585
	\$ 3,665,612

DALMAC ENERGY INC.
Notes to Consolidated Financial Statements
Year Ended April 30, 2006

10. INCOME TAXES

(a) Non-capital losses

The Company has accumulated non-capital losses carried forward for income tax purposes of approximately \$373,600, the benefit of which has been reflected in these financial statements. These losses may be applied against future taxable income within the limitations prescribed by the Income Tax Act (Canada) and expire as follows:

2014		\$	29,700
2015			189,600
2016			154,300
			<hr style="border-top: 1px solid black;"/>
		\$	373,600
			<hr style="border-top: 3px double black;"/>

(b) Temporary differences

A future income tax liability reflects the net effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Significant components of the Company's future income tax liability are as follows:

	<u>2006</u>		<u>2005</u>
Income tax effect of taxable temporary differences:			
Net book value in excess of undepreciated capital cost for tax purposes	\$ 597,225	\$	494,000
Non capital losses carried forward	(119,678)		-
Share issuance costs deductible for tax purposes	(193,294)		-
Book value of goodwill in excess of tax value	27,379		25,000
			<hr style="border-top: 1px solid black;"/>
Recognized future income tax liability	\$ 311,632	\$	519,000
			<hr style="border-top: 3px double black;"/>

(c) Income tax reconciliation

The income tax provision recorded differs from the income tax obtained by applying the statutory income tax rate of 33.5% (2005 - 33.6%) to the income for the year and is reconciled as follows:

	<u>2006</u>		<u>2005</u>
			<i>Restated</i>
Expected income tax expense	\$ 299,349	\$	281,710
Tax effect of expenses deductible for income tax purposes in excess of accounting purposes	(207,172)		13,031
Tax effect of current year losses not recognized	51,683		-
Tax effect of changes in income tax rates	(56,280)		206,870
Tax effect of taxable temporary differences	63,939		69,506
			<hr style="border-top: 1px solid black;"/>
Effective income tax expense	\$ 151,519	\$	571,117
			<hr style="border-top: 3px double black;"/>

DALMAC ENERGY INC.
Notes to Consolidated Financial Statements
Year Ended April 30, 2006

11. SHARE CAPITAL

- (a) Authorized:
 Unlimited common voting shares
 Unlimited preferred shares, issuable in series
- (b) Common shares issued:

	2006		2005	
	Shares	Amount	Shares	Amount
Balance, beginning of year	5,795,964	\$ 1,736,980	3,350,983	\$ 761,733
Issued on exercise of options	292,143	133,719	84,812	25,444
Private placements	6,228,571	7,000,000	-	-
Issued on McClelland acquisition (<i>Note 1</i>)	-	-	2,150,000	860,000
Issued on S Young acquisition (<i>Note 1</i>)	-	-	210,169	124,000
Issued on exercise of warrants	62,300	52,955	-	-
Fair value of options on exercise (<i>Note 12</i>)	-	77,501	-	-
Share issuance costs	-	(745,462)	-	(34,197)
Balance, end of year	12,378,978	\$ 8,255,693	5,795,964	\$ 1,736,980

Subsequent to the year ended April 30, 2006 the company issued 39,595 shares for \$33,656 on exercise of warrants and 9,260 shares for \$6,482 on exercise of options.

In September 2005, pursuant to a private placement, the Company issued 1,428,571 units at \$0.70 per unit for aggregate proceeds of \$1,000,000. Each unit consisted of one common share and one-half common share purchase warrant. Each full warrant entitles the holder to purchase one common share at \$0.85 per share until September 27, 2007. The Company also issued options to the agent to acquire 142,857 units at an exercise price of \$0.70 per unit (see note 12). The options expire on September 27, 2007, and each unit is identical to those issued under the private placement.

In February 2006, pursuant to a private placement, the Company issued 4,800,000 units at \$1.25 per unit for aggregate proceeds of \$6,000,000. Each unit consisted of one common share and one-half common share purchase warrant. Each full warrant entitles the holder to purchase one common share at \$1.50 per share until February 28, 2008. The Company also issued options to the agent to acquire 480,000 units at an exercise price of \$1.25 per unit (see note 12). The options expire on February 28, 2008, and each unit is identical to those issued under the private placement.

During the period ended April 30, 2005 the company issued shares pursuant to business combinations described in note 1.

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11. SHARE CAPITAL *(continued)*

(c) Stock options

The Company has a stock option plan under which directors, officers and employees of the Company and its affiliates are eligible to receive stock options. The maximum number of shares issuable pursuant to the exercise of outstanding options granted under the plan shall be 10% of the issued shares of the Company at the time of granting the options. The maximum number of common shares optioned to any one optionee shall not exceed 5% of outstanding common shares of the Company and options granted under the plan may not exceed five years. The exercise price of each option shall be determined by the directors at the time of grant but shall not be less than the price permitted by the policy or policies of the stock exchange(s) on which the Company's common shares are then listed.

The Company accounts for options granted under this plan in accordance with the fair value based method of accounting for stock-based compensation. The application of the fair value based method requires the use of certain assumptions regarding the risk-free market interest rate, expected volatility of the underlying stock and life of the options.

During the year ended April 30, 2006, the Company granted 142,857 options on September 27, 2005 and 480,000 options on February 28, 2006 to agents of the Company as commissions. The fair value of the options granted on September 27, 2005 was calculated assuming the risk free interest rate was 3.3%, the expected life of the options was two years and the expected volatility was 57%. The market price of the Company's shares at the grant date exceeded the option exercise price. The fair value of the options granted on February 28, 2006 was calculated assuming the risk free interest rate was 3.91%, the expected life of the options was two years and the expected volatility was 55%. The market price of the Company's shares at the grant date exceeded the option exercise price. The options granted resulted in stock based compensation, which was recorded as a share issuance cost, and contributed surplus of \$305,377 during the year.

During the period ended April 30, 2005, the Company granted 150,000 options on March 21, 2005 to directors and senior officials of the company. The fair value of the options granted was calculated assuming the risk free interest rate was 2.5%, the expected life of the options was five years and the expected volatility was 4.5%. The market price of the Company's shares at the grant date exceeded the option exercise price. The options granted resulted in stock based compensation expense and contributed surplus of \$64,692 during the period.

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DALMAC ENERGY INC.
Notes to Consolidated Financial Statements
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11. SHARE CAPITAL *(continued)*

The following table summarizes activity related to stock options:

	Number	Weighted Average Exercise Price 2006	Number	Weighted Average Exercise Price 2005
Balance, beginning of year	662,051	\$ 0.33	596,863	\$ 0.30
Granted	622,857	1.12	150,000	0.45
Expired	(79,316)	0.30	-	-
Exercised	(292,143)	0.46	(84,812)	0.30
Outstanding, end of year	913,449	\$ 0.83	662,051	\$ 0.33
Exercisable, end of year	913,449	\$ 0.83	622,051	\$ 0.33

The following table summarizes stock options outstanding at April 30, 2006:

Expiry Date	Number outstanding	Exercise Price
September 27, 2007	27,667	0.70
February 28, 2008	480,000	1.25
December 22, 2008	255,782	0.30
March 21, 2010	150,000	0.45
	913,449	

(d) Warrants

The following table summarizes warrants outstanding at April 30, 2006:

	Expiry Date	Exercise Price	2006 Warrants Outstanding	2005 Warrants Outstanding
Issued pursuant to private placement in September, 2005	September 27, 2007	\$ 0.85	709,581	-
Issued pursuant to private placement in February, 2006	February 28, 2008	\$ 1.50	2,400,000	-
			3,109,581	-

The weighted average exercise price of the outstanding warrants is \$1.35.

DALMAC ENERGY INC.
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12. CONTRIBUTED SURPLUS

The following table summarizes the changes in contributed surplus:

	2006	2005
Balance, beginning of year	\$ 64,692	\$ -
Stock based compensation expense	-	64,692
Stock based compensation issued to agents on private placements <i>(Note 11(c))</i>	305,377	-
Fair value of options on exercise <i>(Note 11(b))</i>	(77,501)	-
Balance, end of year	\$ 292,568	\$ 64,692

13. PRIOR PERIOD ACCOUNTING ERROR

At April 30, 2005, consignment inventory in the amount of \$90,674 was inadvertently recorded in inventory. As a result of this accounting error the prior period's financial statements have been restated to:

- decrease inventory by \$90,674;
- increase cost of product sales by \$90,674;
- decrease income tax provision by \$30,485;
- decrease net income for the year by \$60,189;
- decrease income taxes payable by \$30,485; and
- decrease retained earnings by \$60,189.

14. CASH FLOW SUPPLEMENTARY INFORMATION

	2006	2005
Interest paid	\$ 318,402	\$ 142,616
Income taxes paid	\$ 244,384	\$ -
Stock based compensation relating to options (issued to agents) reflected as share issuance costs	\$ 305,377	\$ -
Future income tax effect of share issuance costs	\$ 208,242	\$ -

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15. FINANCIAL INSTRUMENTS

- a) The Company's financial instruments consist of cash and cash equivalents, accounts receivable, loan receivable, bank indebtedness, accounts payable and accrued liabilities, callable debt and long term debt. Unless otherwise noted, it is management's opinion that the Company is not exposed to significant interest, currency or credit risks arising from these financial instruments. The fair value of these financial instruments approximate their carrying values, unless otherwise noted.
- b) The Company is exposed, in its normal course of business, to credit risk from customers. A significant portion (29%) of the outstanding accounts receivable at April 30, 2006 is due from two customers. No other single party accounts for a significant balance of accounts receivable.

16. LEASE COMMITMENTS

The Company leases equipment and premises under long term operating leases. The leases for premises are exclusive of operating costs. Future minimum annual lease payments are as follows:

	2007	2008	2009	2010	2011
Equipment	\$ 651,177	\$ 597,913	\$ 569,425	\$ 380,475	\$ 38,949
Premises	215,494	215,494	66,505	-	-
	<u>\$ 866,671</u>	<u>\$ 813,407</u>	<u>\$ 635,930</u>	<u>\$ 380,475</u>	<u>\$ 38,949</u>

17. RELATED PARTY TRANSACTIONS

During the year the Company had the following transactions with related parties:

- (a) Leased premises from a company controlled by a director, for total consideration of \$81,600 (2005 - \$40,800)
- (b) Paid or accrued management and consulting fees to a company controlled by a director in the amount of \$160,380 (2005 - \$51,000). The Company pays consulting fees of \$9,350, increasing by 10% per year, pursuant to a contract agreement expiring on November 14, 2009. In addition, if the Company's net earnings before tax reach \$500,000, the contract agreement requires a bonus payment of 5% on the first \$500,000 of the Company's earnings before tax, 6% on amounts between \$500,001 and \$800,000, 7% on amounts between \$800,001 and \$1,000,000 and 7.5% on amounts over \$1,000,000.
- (c) The Company is indebted to a former director of the Company for an amount of \$245,402 (2005 - \$333,415) (see note 9). With respect to this loan, interest of \$12,463 (2005 - \$9,698) has been paid during the year.
- (d) The Company is indebted to a director of the Company for an amount of \$140,000 (2005 - \$140,000) (see note 9).
- (e) Effective November 8, 2004 the Company acquired all the outstanding shares of McClelland (see note 1). At date of acquisition a director of the Company was as shareholder of McClelland. Consideration received by the director was 850,000 common shares of the Company and a promissory note for \$140,000 (see note 9).

These transactions are in the normal course of operations and have been valued in these financial statements at the exchange amount which is the amount of consideration established and agreed to by the related parties.

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18. COMPARATIVE FIGURES

Certain comparative figures have been reclassified to conform with financial statement presentation adopted for the current year.
