Management's Report

The management of Chinook Energy Inc. ("Chinook") is responsible for the preparation of the consolidated financial statements. The consolidated financial statements have been prepared by management in accordance with International Financial Reporting Standards and include certain estimates that reflect management's best estimates and judgments. Management has determined such amounts on a reasonable basis in order to ensure that the consolidated financial statements are presented fairly, in all material respects.

Management is responsible for the integrity of the consolidated financial statements. Internal control systems are designed and maintained to provide reasonable assurance that assets are safeguarded from loss or unauthorized use and to produce reliable accounting records for financial reporting purposes.

KPMG LLP (the "Auditor") was appointed by Chinook's shareholders to express an audit opinion on the consolidated financial statements. The Auditor's examination included such tests and procedures, as the Auditor considered necessary, to provide a reasonable assurance that the consolidated financial statements are presented fairly in accordance with International Financial Reporting Standards.

The Board of Directors is responsible for ensuring that management fulfills its responsibilities for financial reporting and internal controls. The Board of Directors exercises this responsibility through the Audit Committee, with the assistance from the Reserves Committee regarding the annual review of Chinook's petroleum and natural gas reserves. The Audit Committee, composed of independent non-management directors, meets regularly with management and the Auditor to ensure that management's responsibilities are properly discharged, to review the consolidated financial statements and recommend that the consolidated financial statements be presented to the Board of Directors for approval. The Audit Committee also considers the independence of KPMG LLP and reviews their fees. The Auditor has access to the Audit Committee without the presence of management.

Matthew Brister
President & Chief Executive Officer

Geoff Barlow
Vice President, Finance & Chief Financial Officer

Calgary, Alberta
March 22, 2012

Independent Auditors' Report

To the Shareholders of Chinook Energy Inc.

We have audited the accompanying consolidated financial statements of Chinook Energy Inc., which comprise the consolidated statements of financial position as at December 31, 2011, December 31, 2010 and January 1, 2010, the consolidated statements of operations and comprehensive loss, changes in shareholders' equity and cash flows for the years ended December 31, 2011 and December 31, 2010, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's responsibility for the consolidated financial statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained in our audits is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of Chinook Energy Inc. as at December 31, 2011, December 31, 2010 and January 1, 2010, and its consolidated financial performance and its consolidated cash flows for the years ended December 31, 2011 and December 31, 2010 in accordance with International Financial Reporting Standards.

KPMG LLP

Chartered Accountants
Calgary, Canada

March 22, 2012

Consolidated Statements of Financial Position

	December 31 2011	December 31 2010	January 1 2010
(in thousands of Canadian dollars)		*(note 24)*	*(note 24)*
Assets			
Current			
Cash	**$ 11,475**	$ 23,195	$ 8,027
Accounts receivable *(note 7)*	**48,539**	40,681	10,660
Derivative contracts *(note 17)*	**551**	3,516	–
Prepaids, deposits, inventory and other *(note 8)*	**6,626**	7,318	13,141
	67,191	74,710	31,828
Long-term derivative contracts *(note 17)*	**–**	1,764	–
Property held for sale	**–**	–	13,968
Development & production assets *(note 9)*	**647,512**	748,371	272,723
Exploration & evaluation assets *(note 9)*	**30,700**	52,172	73,127
	$ 745,403	$ 877,017	$ 391,646
Liabilities and Shareholders' Equity			
Current			
Accounts payable, accrued liabilities and other *(note 10)*	**$ 60,398**	$ 70,138	$ 10,130
Current portion of long-term debt *(note 11)*	**–**	–	8,170
Derivative contracts & swap option *(note 17)*	**3,580**	4,345	–
Deferred disposition proceeds on joint venture arrangement *(note 9)*	**3,051**	–	–
Taxes payable	**591**	2,902	133
	67,620	77,385	18,433
Long-term debt *(note 11)*	**137,500**	167,793	11,166
Decommissioning obligation *(note 12)*	**95,432**	125,653	6,107
Deferred income taxes *(note 13)*	**8,555**	13,763	29,552
Deferred lease obligation and other *(note 6)*	**1,585**	2,641	161
Shareholders' equity			
Share capital *(note 14(a))*	**778,070**	778,070	344,703
Contributed surplus	**17,240**	11,593	5,116
Deficit	**(360,672)**	(296,920)	(23,592)
Accumulated other comprehensive income (loss)	**73**	(2,961)	–
	434,711	489,782	326,227
	$ 745,403	$ 877,017	$ 391,646

See accompanying notes to the consolidated financial statements.

Approved on behalf of the Board

[signed] [signed]

Robert J. Herdman, Director

Stuart G. Clark, Director

Consolidated Statements of Operations and Comprehensive Loss

Year ended December 31	2011	2010
(in thousands of Canadian dollars, except per share amounts)		*(note 24)*
Revenue		
Petroleum, natural gas and other revenue	**$ 246,950**	$ 137,348
Royalties	**(35,719)**	(17,390)
Petroleum, natural gas and other revenue, net of royalties	**211,231**	119,958
Expense		
Production & operating	**99,576**	45,345
General & administrative	**19,704**	23,149
Exploration & evaluation	**11,686**	10,682
Derivative transactions and swap option loss (gain) *(note 17)*	**4,786**	(3,448)
Net financing expenses *(note 15)*	**11,259**	14,249
Depletion, depreciation & amortization *(note 9)*	**110,310**	65,775
Impairment of developed & producing assets *(note 9)*	**43,000**	–
Gain on disposition of properties *(note 9)*	**(22,914)**	(25,748)
Foreign exchange loss	**58**	1,675
Other recovery	**(770)**	–
	276,695	131,679
Income (loss) before income taxes and discontinued operations	**(65,464)**	(11,721)
Income taxes (recovery)		
Current income tax *(note 13)*	**3,496**	4,245
Deferred income tax recovery *(note 13)*	**(5,208)**	(2,642)
	(1,712)	1,603
Net loss from continuing operations	**(63,752)**	(13,324)
Discontinued operations, net of income taxes *(note 23)*	**–**	(13,540)
Net loss	**(63,752)**	(26,864)
Foreign currency translation gains (losses) on foreign operations	**3,034**	(24,140)
Available for sale assets fair value adjustment	**–**	(5)
Comprehensive loss	**(60,718)**	(51,009)
Net loss from continuing operations per share, basic and diluted *(note 14(d))*	**$ (0.30)**	$ (0.08)
Net loss per share, basic and diluted *(note 14(d))*	**$ (0.30)**	$ (0.17)

See accompanying notes to the consolidated financial statements.

Consolidated Statements of Changes in Shareholders' Equity

(in thousands of Canadian dollars)	Common Shares *(thousands)*	Share Capital	Contributed Surplus	Deficit	Accumulated Other Comprehensive Income (Loss)	Shareholders' Equity
Balance as at January 1, 2010 *(note 24)*	**75,225**	**$ 344,703**	**$ 5,116**	**$ (23,592)**	**$ –**	**$ 326,227**
Issued on exercise of options	744	2,194	(1,997)	–	–	197
Common shares issued on private placement	85,847	288,584	–	–	–	288,584
Issued on acquisition of Iteration *(note 6)*	52,147	141,841	–	–	–	141,841
Common shares issued to employees and directors	225	784	–	–	–	784
Share issue costs	–	(36)	–	–	–	(36)
Stock-based compensation *(note 14(c))*	–	–	5,862	–	–	5,862
Issuance of warrants *(note 14(b))*	–	–	2,612	–	–	2,612
Net loss for the period	–	–	–	(26,864)	–	(26,864)
Dilution adjustment *(note 23)*	–	–	–	(27,985)	–	(27,985)
"Return of equity" on Bridge Energy ASA distribution *(note 23)*	–	–	–	(218,479)	21,184	(197,295)
Other comprehensive loss for the period	–	–			(24,145)	(24,145)
Balance as at December 31, 2010 *(note 24)*	**214,188**	**$ 778,070**	**$ 11,593**	**$ (296,920)**	**$ (2,961)**	**$ 489,782**
Stock-based compensation *(note 14(c))*	–	–	5,647	–	–	5,647
Other comprehensive gain for the period	–	–	–	–	3,034	3,034
Net loss for the period	–	–	–	(63,752)	–	(63,752)
Balance as at December 31, 2011	**214,188**	**$ 778,070**	**$ 17,240**	**$ (360,672)**	**$ 73**	**$ 434,711**

See accompanying notes to the consolidated financial statements.

Consolidated Statements of Cash Flows

Year ended December 31	2011	2010
(in thousands of Canadian dollars)		
Operating Activities		
Net loss from continuing operations	**$ (63,752)**	$ (13,324)
Add (deduct):		
Accretion *(note 12)*	**3,269**	2,675
Depletion, depreciation and amortization *(note 9)*	**110,310**	65,775
Impairment of developed & producing assets *(note 9)*	**43,000**	–
Exploration & evaluation expenditures	**11,686**	10,682
Unrealized derivative transactions and swap option gain *(note 17)*	**3,965**	3,906
Gain on disposition of properties *(note 9)*	**(22,914)**	(25,748)
Foreign exchange loss	**57**	1,675
Shares issued *(note 14(b))*	**–**	784
Warrant expense *(note 14(b))*	**–**	2,612
Stock-based compensation *(note 14(c))*	**5,647**	5,862
Deferred income tax (recovery) *(note 13)*	**(5,208)**	(2,642)
Other non-cash charges	**(1,056)**	(528)
Decommissioning expenditures *(note 12)*	**(3,035)**	(3,417)
Change in other non-cash working capital *(note 21(b))*	**(11,169)**	5,256
Cash flow from continuing operating activities	**70,800**	53,568
Cash flow from discontinued operations before changes in non-cash working capital	**–**	3,672
Change in non-cash working capital from discontinued operations	**–**	1,047
Cash flow from discontinued operations before changes in non-cash working capital	**–**	4,719
Cash flow from operating activities	**70,800**	58,287
Financing Activities		
Issue of share capital	**–**	288,584
Long-term debt repayment	**(30,293)**	–
Long-term debt issue	**–**	142,793
Proceeds from exercise of stock options	**–**	197
Share issue costs	**–**	(36)
Change in non-cash working capital *(note 21(b)*	**(819)**	–
Cash flow from financing activities	**(31,112)**	431,538
Investing Activities		
Capital expenditures *(note 9)*	**(119,701)**	(235,373)
Business combinations *(note 6)*	**–**	(243,538)
Exploration and evaluation expense	**(11,686)**	(10,682)
Property dispositions *(note 9)*	**83,751**	
Change in non-cash working capital *(note 21(b))*	**(4,030)**	17,781
Investing activities from continuing operations	**(51,666)**	(471,812)
Investing activities from discontinued operations	**–**	(2,128)
Cash flow from investing activities	**(51,666)**	(473,940)
Change in cash and cash equivalents, during the period	**(11,978)**	15,885
Cash and cash equivalents, beginning of period	**23,195**	8,027
Cash and cash equivalents, foreign exchange	**258**	(717)
Cash and cash equivalents, end of period	**$ 11,475**	$ 23,195
Other supplementary cash flow information *(note 21(b))*		

See accompanying notes to the consolidated financial statements.

Notes to the Consolidated Financial Statements

As at December 31, 2011 and 2010
Tabular amounts in thousands of Canadian dollars, except as noted

1. Reporting Entity

Chinook Energy Inc., formerly Storm Ventures International Inc., was incorporated under the laws of the Province of Alberta, Canada, on August 28, 2003. On June 29, 2010, (date of the arrangement) through a plan of arrangement, Storm Ventures International Inc. (“SVI”) acquired all of the issued and outstanding securities of Iteration Energy Ltd. (“Iteration”) and formed Chinook Energy Inc. These consolidated financial statements are a continuation of SVI with the results of Iteration included in the accounts from the date of the arrangement.

These consolidated financial statements include the accounts of Chinook Energy Inc. and its directly and indirectly wholly-owned subsidiaries and foreign branches (collectively, “Chinook” or the “Company”), after the elimination of intercompany balances and transactions.

Chinook’s current operations are to explore, develop and produce natural gas, crude oil and natural gas liquids in Canada and Tunisia. Each country in which Chinook conducts business has been treated as an identifiable reporting segment, in addition to the corporate segment.

Chinook’s common shares are listed on the Toronto Stock Exchange under the symbol CKE. The head office and principal address of Chinook is Suite 700, 700 – 2nd Street SW, Calgary, Alberta, Canada T2P 2W1.

2. Basis of Presentation

Statement of Compliance

The consolidated financial statements represent the Company’s initial presentation of its results and financial position under International Financial Reporting Standards (“IFRS”) as issued by the International Accounting Standards Board and were prepared using accounting policies consistent with IFRS.

A summary of Chinook’s significant IFRS accounting policies are presented in Note 3. These policies have been retrospectively and consistently applied except where specific exemptions upon transition to IFRS permitted an alternative treatment in accordance with “First-time Adoption of International Reporting Standards” (“IFRS 1”) as disclosed in Note 24. An explanation of how the transition to IFRS has affected the reported statements of financial position and operations and comprehensive loss as at and for the year ended December 31, 2010, respectively is also disclosed in Note 24. The Company’s reported cash flows were not affected by the transition to IFRS.

These consolidated financial statements were approved and authorized for issuance by the Board of Directors on March 22, 2012.

Basis of Measurement

The consolidated financial statements have been prepared on the historical cost basis with the exception of derivative financial instruments which are measured at fair value. The method used to measure fair values is discussed in Note 17.

Functional and Presentation Currency

These consolidated financial statements are presented in Canadian dollars which is also the Company’s Canadian and Corporate segments’ functional currency. The Tunisian segment’s functional currency is the United States dollar.

Management Judgment and Estimation Uncertainty

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingencies at the date of the financial statements, and revenues and expenses during the reporting year. Actual results could differ from those estimated. The key sources of estimation uncertainty that have a significant risk of causing material adjustment to the carrying amounts of assets and liabilities are discussed below.

Recoverability of asset carrying values

The recoverability of development and production asset carrying values are assessed at the Cash Generating Units (“CGU”) level. Determination of what constitutes a CGU is subject to management judgments. The asset composition of a CGU can directly impact the recoverability of the assets included therein. In assessing the recoverability of petroleum and natural gas properties, each CGU’s carrying value is compared to its recoverable amount, defined as the greater of its fair value less cost to sell and value in use.

At December 31, 2011 the recoverable amounts of Chinook's CGUs were estimated as their fair value less cost to sell based on the following information:

a) The net present value, discounted at 10%, of the cash flows from oil and gas reserves of each CGU based on reserves estimated by Chinook's independent reserve evaluator; and

b) Consideration of acquisition metrics of recent transactions completed on similar assets to those contained within the relevant CGU.

Key input estimates used in the determination of cash flows from oil and gas reserves include the following:

a) Reserves – assumptions that are valid at the time of reserve estimation may change significantly when new information becomes available. Changes in forward price estimates, production costs or recovery rates may change the economic status of reserves and may ultimately result in reserves being restated.

b) Oil and natural gas prices – forward price estimates of the oil and natural gas prices are used in the cash flow model. Commodity prices have fluctuated widely in recent years due to global and regional factors including supply and demand fundamentals, inventory levels, exchange rates, weather, economic and geopolitical factors.

c) Discount rate – the discount rate used to calculate the net present value of cash flows is based on estimates of the Company's weighted average cost of capital. Changes in the general economic environment could result in significant changes to this estimate.

Impairment tests as carried out at December 31, 2011, were based on proved and probable reserves, using a discount rate of 10 percent and forward commodity price estimates. For the year ended December 31, 2011, the Company recorded an impairment of $43.0 million ($nil for the year ended December 31, 2010). A one percent increase in the assumed discount rate would result in an additional impairment of $4.0 million for the year ended December 31, 2011, while a five percent decrease in the forward commodity price estimate would result in an additional impairment of approximately $10.0 million.

Depletion of oil and gas assets

Depletion of oil and gas assets is determined based on total proved and probable reserve values as well as future development costs as estimated by Chinook's external reserve evaluators. Reserve assumptions that are valid at the time of reserve estimation may change significantly when new information becomes available. Changes in forward price estimates, production costs or recovery rates may change the economic status of reserves and may ultimately result in reserves being restated.

Decommissioning obligation

The provision for the decommissioning obligation is based on current legal and constructive requirements, technology, price levels and expected plans for remediation. Actual costs and cash outflows can differ from estimates because of changes in laws and regulations, public expectations, market conditions, discovery and analysis of site conditions and changes in technology.

Derivative instruments

The estimated fair value of derivative instruments resulting in financial assets and liabilities, by their very nature are subject to measurement uncertainty.

Stock-based compensation

The stock-based compensation expense recorded for Chinook's Share Option Plan is based on a Black-Scholes option valuation model. The inputs to this model rely on management judgment.

Deferred taxes

Tax interpretations, regulations and legislation are subject to change and as such income taxes are subject to measurement uncertainty. Deferred income tax assets are assessed by management at the end of the reporting period to determine the likelihood that they will be realized from future taxable earnings.

Foreign currency

The determination of the Company's Tunisian operation's functional currency requires assessing several factors, including the dominant currency used in transactions such as the settlement of revenues and operational and capital expenditures, and to a lesser extent financing of this operation. Management has determined that the US dollar is the functional currency of its Tunisian operations resulting in the revaluation of this segment's financial results and net assets into Chinook's Canadian dollar reporting currency with translation differences reported through other comprehensive income.

3. Summary of Accounting Policies

Basis of Consolidation

Subsidiaries:

Subsidiaries are entities controlled by Chinook. Control exists when Chinook has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, potential voting rights that currently are exercisable are taken into account. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

Jointly controlled assets:

Chinook conducts many of its petroleum and natural gas production activities through jointly controlled assets and the consolidated financial statements reflect only its proportionate interest in such activities.

Transactions eliminated on consolidation:

Intercompany balances and transactions, and any unrealized income and expenses arising from intercompany transactions, are eliminated in preparing the consolidated financial statement.

Business Combinations

The acquisition method of accounting is used to account for acquisitions of subsidiaries and assets that meet the definition of a business under IFRS. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed on the date of closing. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date. The excess of the cost of acquisition over the fair value of the identifiable assets, liabilities and contingent liabilities acquired is recorded as goodwill. If the cost of the acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognized immediately in the statement of operations and comprehensive income. Transaction costs that Chinook incurs in connection with a business combination are expensed as incurred.

Revenue Recognition

Revenue associated with the sale of crude oil, natural gas and natural gas liquids produced by Chinook is recognized when title is transferred from Chinook to its customers. Revenue is measured at the fair value of the consideration received or receivable. Revenue from the sale of crude oil, natural gas and natural gas liquids (which includes the deduction of transportation costs) is recognized when all of the following conditions have been satisfied:

- Chinook has transferred the significant risks and rewards of ownership of the production to the buyer;
- Chinook retains no continuing managerial involvement to the degree usually associated with ownership or effective control over the goods sold;
- The amount of revenue can be measured reliably;
- It is probable that the economic benefits associated with the transaction will flow to Chinook; and
- The costs incurred or to be incurred in respect of the transaction can be measured reliably.

Revenue is presented net of recognized transportation costs. Transportation of crude oil, natural gas and natural gas liquids from the wellhead to the point of title transfer are recognized when the transportation is provided.

Share-based Compensation

Chinook has established a share option plan for certain employees, officers, directors, consultants and other service providers that will settle through the issuance of equity. The fair value of share options granted to optionees is determined on their grant date using a valuation model and recorded as stock-based compensation expense, as included on the line item general & administrative expense as reported on the consolidated statements of operations and comprehensive loss, over the period that the share options vest, with a corresponding increase to contributed surplus, as reported on the consolidated statements of financial position. Forfeitures are estimated through the vesting period based on past experience and future expectations, and adjusted upon actual vesting. When share options are exercised, the proceeds, together with the amounts recorded in contributed surplus, are recorded in share capital.

Exploration & Evaluation Assets ("E&E Assets")

Exploration and evaluation expenditures are capitalized within E&E Assets until the technical feasibility and commercial viability of the project has been determined. Such E&E expenditures may include undeveloped land license acquisitions, certain technical services and studies and exploration drilling and testing. Expenditures incurred prior to obtaining the legal right to explore are expensed as incurred. If an E&E project is determined to be unsuccessful, all associated costs are charged through exploration and evaluation expense as reported on the statement of operations.

If commercial reserves are established for a project classified as an E&E Asset, the relevant cost is transferred from E&E Assets to development and producing assets as presented on the consolidated statement of financial position. The expenditures for an E&E project are reviewed for impairment prior to any such transfer.

Developed & Producing Assets ("D&P Assets")

D&P Assets, which include petroleum and natural gas development and production assets, in addition to administrative assets, are measured at cost less accumulated depletion, depreciation and amortization and accumulated impairment losses.

Gain and losses on disposal of an item of D&P Assets are partially determined by comparing the proceeds from disposal with the carrying amount of D&P Assets and are reported on the line item gains or losses on disposal of properties on the statement of operations. Exchanges of properties are measured at fair value, unless the transaction lacks commercial substance or fair value cannot be reasonably measured. Where the exchange is measured at fair value, a gain or loss is recognized in the statement of operations.

Overhead costs which are directly attributable to bringing an asset to the location and condition necessary for it to be capable of use in the manner intended by management are capitalized. These costs include directly attributable compensation costs paid to internal personnel.

Depletion, Depreciation & Amortization ("DD&A")

D&P Assets are componentized into groups of assets with similar useful lives for the purposes of performing depletion calculations. Depletion expense is calculated on the unit-of-production basis based on:

a) Total estimated proved and probable reserves calculated in accordance with National Instrument 51-101 – Standards of Disclosure for Oil and Gas Activities;

b) Total capitalized costs plus estimated future development costs of proved and probable reserves; and

c) Relative volumes of petroleum and natural gas reserves and production, before royalties, converted at the energy equivalent conversion ratio of six thousand cubic feet of natural gas to one barrel of crude oil.

E&E Assets as included in Chinook's Canadian Segment are amortized over the term of the license, which is generally over a period of five years, whereas E&E Assets in its Tunisian Segment are amortized over the specific exploration permit term.

Depreciation of corporate assets is calculated on a straight-line basis over the useful life of the related assets.

Impairment

D&P Assets

Chinook's D&P Assets are grouped into CGUs for the purpose of assessing impairment. A CGU is a grouping of assets that generate cash inflows independently of other assets held by the Company. Geological formation, product type, proximity to shared infrastructure and internal management are key factors considered when grouping Chinook's oil petroleum and natural gas assets into CGUs.

CGUs are reviewed at each reporting date for indicators of potential impairment. If such indicators exist, an impairment test is performed by comparing the CGU's carrying value to its recoverable amount, defined as the greater of a CGU's fair value less cost to sell and its current value in use. Any excess of carrying value over recoverable amount is recognized on the statement of operations and comprehensive loss as reported on the line item impairment expense.

If there is an indicator that a previously recognized impairment charge may no longer be valid, the recoverable amount of the relevant CGU is calculated and compared against the carrying amount. An impairment charge is reversed to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depletion, if no impairment loss had been recognized.

E&E Assets

E&E Assets are assessed for impairment at the operating segment level. Impairment tests are carried out when E&E Assets are transferred to D&P Assets following the declaration of commercial reserves, and any time that circumstances arise which could indicate a potential impairment.

Decommissioning Obligation

Chinook recognizes a decommissioning obligation in the period in which it has a present legal or constructive liability and a reasonable estimate of the amount can be made. On a periodic basis, management reviews these estimates, and changes, if any, are prospectively applied. The approximated fair value of the estimated decommissioning liability is recorded as a long-term liability, with a corresponding increase to the carrying amount of the related asset. The capitalized amount is depleted on a unit-of-production basis over the life of the associated proved plus probable reserves. The decommissioning liability is increased each reporting period with the passage of time and the associated accretion charge is recognized in the line item financing expenses as reported on the statement of operations and comprehensive loss. Periodic revisions to the liability specific discount rate, estimated timing of cash flows or to the original estimated undiscounted costs can also result in an increase or decrease to the decommissioning obligation. Actual costs incurred upon settlement of the obligation are recorded against the decommissioning liability to the extent of the liability recorded.

Deferred Taxes

Deferred tax is recognized by providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, based on the laws that have been substantively enacted by the period end date.

Deferred income tax expense is recognized in the statement of operations and comprehensive loss except to the extent that it relates to items recognized directly in equity, in which case it is recognized in equity.

Deferred tax assets and tax liabilities are offset to the extent there is a legal enforceable right to offset the recognized amounts and the intent is to either settle on a net basis or to simultaneously realize the asset and settle the liability.

Financial Instruments

Financial assets, financial liabilities and derivatives are measured at fair value on initial recognition. Measurement in subsequent periods depends on the financial instrument's classification, as described below:

a) Fair value through profit and loss

   Financial instruments designated as fair value through profit and loss are subsequently measured at fair value with changes in those fair values charged immediately to earnings. Chinook classifies its risk management contracts and swap option as fair value through profit and loss. Cash is also classified as fair value through profit and loss.

b) Held-to-maturity loans and receivables and other financial liabilities

   Held-to-maturity receivables and other financial liabilities are subsequently measured at amortized cost using the effective interest method. Chinook classifies accounts receivable to loans and receivables and accounts payable and accrued liabilities and long-term debt to other financial liabilities.

Foreign Currency Translation

Chinook's Tunisian segment's assets and liabilities, as denominated in the United States dollar, are translated into Canadian dollars, the Company's presentation currency, at the rate of exchange in effect on the date of the consolidated statement of financial position. The Tunisian Segment's foreign currency revenues and expenses are translated at the period average rates of exchange where translation gains and losses are reported through other comprehensive losses. The Company's Canadian segment's functional currency is Canadian dollars.

Earnings per Share

Basic earnings per share is calculated by dividing the net earnings or loss attributable to Chinook's common shareholders by the weighted average number of common shares outstanding during the period. Diluted earnings per share is determined by adjusting the net earnings attributable to Chinook's common shareholders and the weighted average number of common shares outstanding for the effects of dilutive instruments such as granted options.

4. New Accounting Policies

Current Year Accounting Changes

Chinook's first year reporting its financial statements under IFRS is 2011. Accounting standards issued to date effective for periods beginning on or after January 1, 2011 have been adopted as part of the transition to IFRS.

Future Accounting Changes

Chinook has reviewed new and revised accounting pronouncements that have been issued but are not yet effective and determined that the following may have an impact on the Company:

As of January 1, 2015, Chinook will be required to adopt IFRS 9 "Financial Instruments", which is the result of the first phase of the IASB project to replace IAS 39 "Financial Instruments: Recognition and Measurement". The new standard replaces the current multiple classification and measurement models and financial assets and liabilities with a single model that has only two classification categories: amortized cost and fair value. Portions of the standard remain in development and the full impact of the new standard on Chinook's consolidated financial statements will not be known until the project is complete.

In May 2011, the IASB released the following new standards: IFRS 10, "Consolidated financial statements", IFRS 11, "Joint Arrangements", IFRS 12, "Disclosures of interests in other entities" and IFRS 13, "Fair Value Measurement". Each of these standards is to be adopted for fiscal years beginning January 1, 2013 with earlier adoption permitted. Chinook is currently analyzing the expected impact, if any, that the adoption of the following standards will have on its consolidated financial statements:

- IFRS 10, "Consolidated financial statements" supersedes IAS 27 "Consolidation and Separate Financial Statements" and SIC-12 "Consolidation – Special Purpose Entities". This standard provides a single model to be applied in control analysis for all investees including special purpose entities.
- IFRS 11, "Joint Arrangements" divides joint arrangements into two types, joint operation and joint ventures, each with their own accounting model. All joint arrangements are required to be reassessed on transition to IFRS 11 to determine their type to apply the appropriate accounting.
- IFRS 13, "Fair Value Measurement" defines fair value, establishes a framework for measuring fair value and sets out disclosure requirements for fair value measurements. This standard defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

5. Determination of Fair Values

A number of Chinook's accounting policies and disclosures require the determination of fair value, for both financial and non-financial assets and liabilities. Fair values have been determined for measurement and/or disclosure purposes based on the following methods. When applicable, further information about the assumptions made in determining fair values is disclosed in the notes specific to that asset or liability.

Developed & Producing and Exploration & Evaluation Assets

The fair value of developed & producing & exploration and evaluation assets recognized in a business combination, is based on market values. The market value of developed & producing & exploration and evaluation assets is the estimated amount for which the assets could be exchanged on the acquisition date between a willing buyer and a willing seller in an arm's length transaction after proper marketing wherein the parties had each acted knowledgeably, prudently and without compulsion. The market value of oil and natural gas interests (included in developed & producing assets) and intangible exploration assets is estimated with reference to the discounted cash flows expected to be derived from oil and natural gas production based on externally prepared reserve reports. The risk-adjusted discount rate is specific to the asset with reference to general market conditions.

Accounts Receivable, Accounts Payable and Accrued Liabilities and Bank Debt

The fair value of accounts receivable, accounts payable and accrued liabilities and bank debt is estimated using amortized cost, which is the present value of future cash flows, discounted at the market rate of interest at the reporting date.

Derivatives and Swap Option

The fair value of forward contracts and swaps is determined by discounting the difference between the contracted prices and published forward price curves as at the reporting date, using the remaining contracted oil and natural gas volumes and a risk-free interest rate (based on published government rates). The fair value of options and costless collars is based on option models that use published information with respect to volatility, prices and interest rates.

Stock Options

The fair value of employee stock options is measured using a Black-Scholes option pricing model. Measurement inputs include the share price on the measurement date, exercise price of the instrument, expected volatility, weighted average expected life of the instruments and the risk-free interest rate.

6. Business Combinations

Iteration Energy Ltd. (“Iteration”)

On June 29, 2010, through a plan of arrangement, Chinook acquired all of the issued and outstanding securities of Iteration for $555.9 million, including Iteration’s bank debt and assumed its working capital deficiency. Iteration was a petroleum and natural gas company holding producing and undeveloped properties throughout the Western Canadian Sedimentary Basin (“WCSB”) and was a strategic fit with Chinook’s existing asset portfolio, also located throughout the WCSB. The plan of arrangement resulted in the newly amalgamated company, Chinook, being a publicly traded company listed on the Toronto Stock Exchange.

The plan of arrangement was an arm’s length transaction and has been accounted for as an acquisition of Iteration by Chinook using the acquisition method with Chinook being the acquirer. These consolidated financial statements are a continuance of Chinook with the results of operations of Iteration included in the accounts from the date of the arrangement. The allocation of the purchase price based on estimated fair values of Iteration on the acquisition date was as follows:

Net assets acquired:	
Property and equipment	$ 641,630
Unrealized gain on financial instruments	4,486
Asset retirement obligation	(77,661)
Future income tax liability	(12,515)
Assumption of bank debt	(175,000)
Working capital deficit	(9,874)
Deferred lease obligation	(4,225)
Total consideration transferred	$ 366,841

Consideration given:	
Cash	$ 225,000
Common shares issued (52,147,287)	141,841
Total purchase price	$ 366,841

In conjunction with this transaction, Chinook has recorded $5.2 million of applicable transaction costs to general & administrative expenses on the consolidated statement of operations. The net working capital deficiency acquired includes $21.4 million of trade accounts receivable and $34.7 million of accounts payable and accrued liabilities. Chinook also recorded a $4.2 million deferred lease obligation as the lease term it acquired through this business combination was favorable relative to terms it could have solely secured. The remaining deferred lease obligation of $2.6 million at December 31, 2011 (2010 – $3.7 million) is being amortized over the lease term.

Talisman Resources (Tunisia) Limited (“TRTL”)

On March 11, 2010, Chinook acquired all of the issued and outstanding shares of TRTL for $24.3 million. TRTL owns a 5% non-operated interest in the Adam Concession and a 10% non-operated interest in the Borj El Khadra Permit, both in Tunisia, North Africa. The consolidated financial statements incorporate the results of operations of the acquired TRTL properties from March 11, 2010. This acquisition gave the Company an operational entrance into Tunisia where it has subsequently expanded its production base through the acquisition and development of its Bir Ben Tartar Concession located within the Ghadames Basin in Southern Tunisia. The results of TRTL are included in the consolidated financial statements of the Company from the acquisition date.

The allocation of the purchase price based on the estimated fair value of TRTL on the acquisition date was as follows:

Net assets acquired:	
Cash	$ 11,240
Working capital	(1,691)
Property and equipment	18,809
Future income tax	(3,891)
Asset retirement obligation	(190)
Total consideration transferred	$ 24,277

Consideration given:	
Cash	$ 24,277

In conjunction with this transaction, Chinook has recorded $0.6 million of applicable transaction costs to general & administrative expenses on the consolidated statement of operations. The net working capital deficiency acquired includes $1.4 million of trade accounts receivable, $1.0 million of crude oil inventory, $3.9 million taxes payable and $0.2 million of accounts payable and accrued liabilities.

7. Accounts Receivable

The Company's accounts receivable is comprised of:

	December 31 2011	December 31 2010	January 1 2010
Trade accounts receivable	**$ 26,429**	$ 19,229	$ 3,446
Accrued trade accounts receivables	**17,526**	17,265	1,800
Other receivables	**6,278**	4,365	4,339
Cash call receivables	**1,229**	2,486	1,075
Allowance for doubtful accounts	**(2,923)**	(2,664)	–
	$ 48,539	$ 40,681	$ 10,660

The Company's accounts receivable balance is aged as follows:

	December 31 2011	December 31 2010	January 1 2010
Not past due	**$ 43,118**	$ 29,679	$ 8,884
Past due by more than 90 days, net of allowance	**5,421**	11,002	1,776
	$ 48,539	$ 40,681	$ 10,660

8. Prepaids, Deposits, Inventory and Other

Chinook's prepaids, deposits and other are comprised of:

	December 31 2011	December 31 2010	January 1 2010
Prepaids	**$ 2,432**	$ 2,192	$ 12,553
Deposits	**3,742**	5,075	524
Inventory	**452**	51	–
Other	**–**	–	64
	$ 6,626	$ 7,318	$ 13,141

9. Development & Production and Exploration & Evaluation Assets

The following table reconciles Chinook's D&P and E&E Assets:

	Development & Production Assets	Exploration & Evaluation Assets	Total
Cost of Assets			
Balance as at January 1, 2010	**$ 272,723**	**$ 73,127**	**$ 345,850**
Capital expenditures	227,986	7,387	235,373
ITX business combination *(note 6)*	588,630	53,000	641,630
TRTL business combination *(note 6)*	17,895	914	18,809
Cost of properties sold and distributed	(352,724)	(73,419)	(426,143)
Change in decommissioning asset additions	50,712	–	50,712
Foreign exchange adjustment	(1,338)	–	(1,338)
Balance as at December 31, 2010	**803,884**	**61,009**	**864,893**
Capital expenditures	118,238	1,463	119,701
Cost of properties sold	(81,061)	(537)	(81,598)
Transfer from E&E to D&P	3,710	(3,710)	0
Change in decommissioning asset additions	(18,366)	0	(18,366)
Foreign exchange adjustment	3,512	1	3,513
Balance as at December 31, 2011	**$ 829,917**	**$ 58,226**	**$ 888,143**
Accumulated Depletion, Depreciation & Amortization			
Balance as at January 1, 2010	**$ –**	**$ –**	**$ –**
Depletion, depreciation and amortization	(56,938)	(8,837)	(65,775)
Cost of properties sold and distributed	(258)	–	(258)
Foreign exchange adjustment	1,683	–	1,683
Balance as at December 31, 2010	**(55,513)**	**(8,837)**	**(64,350)**
Depletion, depreciation and amortization	(91,265)	(19,045)	(110,310)
Impairment	(43,000)	0	(43,000)
Inventoried depletion	(202)	0	(202)
Reversed on sale	8,431	211	8,642
Transfer from E&E to D&P	(145)	145	0
Foreign exchange adjustment	(711)	0	(711)
Balance as at December 31, 2011	**$ (182,405)**	**$ (27,526)**	**$ (209,931)**
Net Book Values			
Balance as at January 1, 2010 *(note 24)*	$ 272,723	$ 73,127	$ 345,850
Balance as at December 31, 2010 *(note 24)*	$ 748,371	$ 52,172	$ 800,543
Balance as at December 31, 2011	**$ 647,512**	**$ 30,700**	**$ 678,212**

For the year ended December 31, 2011, Chinook recognized an impairment charge of $43.0 million ($nil for the year ended December 31, 2010) as triggered through a reduction in Canadian natural gas prices. The impairment losses were recorded in a predominately natural gas weighted Canadian CGU as a result of a weakening of the forward price curve for natural gas at December 31, 2011, and capital expenditures in the Canadian area during 2011 without a corresponding increase in the Canadian area's proved and probable reserves. The impairment tests were carried out at December 31, 2011 and were based on proved and probable reserves, a discount rate of ten percent and the following forward commodity price estimates:

Year	WTI Crude Oil *(US$/bbl)* [1]	Brent Crude Oil *(US$/bbl)* [1]	AECO Gas *($/mmbtu)* [1]	US/Cdn Exchange *(US$/Cdn)* [1]
2012	$ 97.50	$ 107.50	$ 3.50	0.98
2013	$ 97.50	$ 102.60	$ 4.20	0.98
2014	$ 100.00	$ 102.60	$ 4.70	0.98
2015	$ 100.80	$ 103.50	$ 5.10	0.98
2016	$ 101.70	$ 104.40	$ 5.55	0.98
Thereafter	2%	2%	2%	0.98

[1] **Source: MacDaniels & Associates price forecast, effective January 1, 2012**

The Company capitalized $2.1 million (2010 – $2.5 million) of direct G&A costs as related to its exploration and development activity for the year ended December 31, 2011.

Joint Venture Arrangement

Chinook entered into an agreement with New Zealand Oil & Gas Ltd. ("NZOG") whereby NZOG has the option to participate in the development of Chinook's Cosmos Concession located offshore Tunisia, where Chinook holds an 80% working interest. Under the terms of the agreement, NZOG paid to Chinook initial cash consideration of US$3.0 million to secure the right to purchase a 40% working interest. NZOG's election is made at the point of Final Investment Decision ("FID") subject to regulatory approval, transfer of title and positive project economics. On a positive election, Chinook will retain a 40% working interest in the Cosmos Concession and in consideration NZOG shall pay the first US$19.0 million of Chinook's share of the costs and expenses in respect of the development plan. FID is anticipated to be considered by the partners mid 2012 with a recommendation for project sanction following shortly thereafter.

Property Dispositions

During the year ended December 31, 2011, Chinook has completed the sale of 15 non-core properties and various royalty interests for aggregate net proceeds of $83.7 million which proceeds were used to partially finance the repayment of a portion of the Revolving Term Credit Facility and the capital programs on Chinook's Canadian and Tunisian core properties. The carrying amount of the non-core properties, which is reduced by $12.1 million of associated decommissioning obligations (see Note 12), was less than the sales proceeds received resulting in a gain of $22.9 million for the year ended December 31, 2011 ($25.7 million for the year ended December 31, 2010).

10. Accounts Payable, Accrued Liabilities and Other

Chinook's accounts payable, accrued liabilities and other are comprised of:

	December 31 2011	December 31 2010	January 1 2010
Trade accounts payable	**$ 14,920**	$ 11,131	$ 4,617
Accrued liabilities	**30,108**	38,067	3,887
Joint operations accounts payable	**12,747**	17,902	1,623
Royalties payable	**1,567**	1,982	–
Deferred lease obligation *(note 6)*	**1,056**	1,056	–
	$ 60,398	$ 70,138	$ 10,130

11. Debt

On December 9, 2011, Chinook's 364 day revolving term credit facility was amended to $200.0 million (the "Revolving Term Credit Facility"). As a result of petroleum property sales, the Revolving Term Credit Facility was further reduced by $6.0 million to $194.0 million as at December 31, 2011. The current revolving period ends on June 25, 2012. In the event that the revolving period is not extended prior to this date, all amounts then outstanding under the Revolving Term Credit Facility must be repaid, at the option of Chinook, before June 25, 2013. The Revolving Term Credit Facility is subject to a semi-annual review and redetermination with the next review and redetermination to be calculated based on year end information prior to June 25, 2012. Changes in the availability of the Revolving Term Credit Facility are possible, from one renewal period to the next, with draws in excess of availability becoming immediately payable. At December 31, 2011, Chinook had drawn $137.5 million on the Revolving Term Credit Facility (December 31, 2010 - $167.8 million) resulting in available credit on this facility of $56.5 million (December 31, 2010 - $62.2 million). Debt as at January 1, 2010 of $19.3 million was secured by Chinook's UK North Sea business (see Note 23).

The Revolving Term Credit Facility is collateralized by floating charges and security interests over all present and future properties and assets of the Company. Interest payable on amounts drawn on this facility vary based on Canadian prime, U.S. Base rate, U.S. LIBOR or Bankers' Acceptance depending on the borrowing option selected by the Company. The effective interest rate on the Revolving Credit Term Facility for the year ended December 31, 2011, was 4.3% (2010 – 4.9%). The Revolving Credit Term Facility contains a covenant whereby the ratio of Chinook's debt to earnings before interest, taxes, depreciation and amortization cannot be greater than 4:1 as determined on a rolling four quarter basis for the most current fiscal quarter. At December 31, 2011, Chinook was in compliance with this covenant.

12. Decommissioning Obligation

The total future decommissioning obligations were estimated by management based on Chinook's net ownership interest in all wells and facilities, estimated costs to reclaim and abandon the wells and facilities and the estimated timing of the costs to be incurred in future periods. Chinook has estimated the net present value of its total decommissioning obligation based on a total future undiscounted liability of $106.3 million ($150.0 million at December 31, 2010). At December 31, 2011 management estimates that these payments are expected to be made over the next 54 years. A risk free rate of 2% to 3% in 2011 (3% to 4% in 2010) and an inflation rate of 2% to 3% in 2011 (2% in 2010) were used to calculate the present value of the decommissioning obligations.

Year ended December 31	2011	2010
Balance, beginning of period	**$ 125,653**	$ 6,106
Increase in liabilities relating to corporate acquisitions	**–**	77,851
Increase in liabilities relating to development activities	**4,527**	50,712
Decrease in liabilities relating to change in estimates	**(22,893)**	–
Settlement of reclamation liabilities during the period	**(3,035)**	(3,417)
Decrease in liabilities relating to dispositions and dilution	**(12,119)**	(6,216)
Accretion expense	**3,269**	2,675
Foreign exchange adjustment	**30**	(2,058)
Balance, end of period	**$ 95,432**	$ 125,653

13. Income Taxes

The major components of income tax expense for the years ended December 31 were as follows:

	2011	2010
Current tax		
Current income tax charge	**$ 4,063**	$ 4,208
Adjustments in respect of current income tax of previous years	**(567)**	37
	$ 3,496	$ 4,245
Deferred income tax		
Relating to origination and reversal of temporary differences	**(6,634)**	(2,642)
Adjustments in respect of defered income tax of previous year	**1,426**	–
Total income tax expense	**$ (5,208)**	$ (2,642)

Current taxes arise from the Tunisia business segment.

The provision for income taxes reflects an effective tax rate which differs from the expected statutory rate. Differences were accounted for as follows:

	2011	2010
Income (loss) before tax	**$ (65,464)**	$ (11,721)
Expected tax rate	**26.5%**	28.0%
Expected income tax expense (recovery)	**$ (17,348)**	$ (3,282)
Effect on income tax resulting from:		
Difference between current and future tax rates	**1,291**	(1,265)
Stock-based compensation	**1,496**	1,641
Change in unrecognized tax asset	**9,652**	(1,185)
Difference between foreign tax rates and Canadian tax rates	**1,790**	2,911
Other non-deductible expenses	**1,407**	2,783
Total income tax expense	**$ (1,712)**	$ 1,603

The statutory tax rate consists of the combined federal and provincial tax rates applicable for the Company and its subsidiaries. The combined statutory rate decreased from 28% for the year ended December 31, 2010 to 26.5% for the year ended December 31, 2011 due to a reduction in the 2011 Canadian corporate tax rates as part of a series of corporate tax rate reductions previously enacted by the Canadian Federal Government in 2007.

Unrecognized deferred tax assets:

At December 31, 2011 the Company had $30.6 million (December 31, 2010 – $9.9 million) of non-capital losses that will expire in the years 2025 to 2031. At December 31, 2011, the Company also had other available tax deductions amounting to $36.6 million. The Company has not recorded deferred tax assets in respect of these items because it is not probable that future taxable profit will be available against which the Company can utilize the benefits.

Recognized deferred tax assets and liabilities:

Deferred tax assets and liabilities are attributable to the following:

	2011	2010
Deferred tax liabilities:		
Development and production / Exploration and evaluation assets	**$ 47,620**	$ 51,936
Derivative contracts	**138**	157
	47,758	52,093
Less deferred tax assets:		
Non-capital losses	**(12,800)**	(2,133)
Derivative contracts	**(895)**	–
Provisions	**(25,508)**	(36,197)
Net deferred tax liability	**$ 8,555**	$ 13,763

Movement in deferred taxes related to temporary differences during the year ended December 31, 2011:

	Balance at December 31, 2010	Recognized in statement of loss	Acquired in business combinations	Balance at December 31, 2011
Development and production / Exploration and evaluation assets	$ 51,936	$ (4,316)	$ –	**$ 47,620**
Derivative contracts	157	(19)	–	**138**
Non-capital tax losses	(2,133)	(10,667)	–	**(12,800)**
Derivative contracts	–	(895)	–	**(895)**
Provisions	(36,197)	10,689	–	**(25,508)**
	$ 13,763	$ (5,208)	$ –	**$ 8,555**

Movement in deferred taxes related to temporary differences during the year ended December 31, 2010:

	Balance at January 1, 2010	Recognized in statement of loss	Disposed on discontinued operations	Acquired in business combinations	Balance at December 31, 2010
Development and production / Exploration and evaluation assets	$ 111,005	$ (1,424)	$ (111,005)	$ 53,360	$ 51,936
Derivative contracts	–	(1,369)	–	1,526	157
Non-capital tax losses	(81,453)	9,497	81,452	(11,629)	(2,133)
Provisions	–	(9,346)	–	(26,851)	(36,197)
	$ 29,552	$ (2,642)	$ (29,553)	$ 16,406	$ 13,763

14. Share Capital

a) Authorized:

An unlimited number of no par value common shares and first preferred shares in addition to 1,279,000 share purchase warrants.

b) Issued and Outstanding:

Common Shares

All common shares are fully paid. The holders of common shares are entitled to share equally in dividends, returns of capital and to vote at shareholders' meetings.

First Preferred Shares

No first preferred shares have been issued.

Warrants

The Company issued 1,279,000 share purchase warrants ("Warrants") on May 27, 2010, in connection with a financing. As at December 31, 2011 and December 31, 2010, all of the Warrants were outstanding. Each Warrant is exercisable to acquire one common share of the Company at a price of $3.25 per common share on or before June 30, 2013. For the year ended December 31, 2010, the Company recognized $2.6 million as the fair value for these warrants in the line item financing expenses on the consolidated statement of operations.

c) Stock-Based Compensation Plan

The Company has a share option plan pursuant to which options to purchase common shares of the Company may be granted to employees, directors, officers, and other service providers of the Company. The maximum number of common shares issuable on exercise of options granted pursuant to the share option plan may not exceed 10% of the issued and outstanding common shares of the Company. The outstanding options of the Company vest over a period of three years and expire five years after the date granted.

A summary of options outstanding is as follows:

	Number of Options *(thousands)*
Balance as at January 1, 2010	**4,090**
Granted	10,390
Exercised	(744)
Forfeited	(1,600)
Balance as at December 31, 2010	**12,136**
Granted	4,743
Exercised	–
Forfeited	(1,424)
Balance as at December 31, 2011	**15,455**

The table below summarizes outstanding stock options and the weighted average exercise prices remaining life in years, the number of exercisable options and their respective weighted average exercise prices and remaining life.

	Outstanding Options			Options Exercisable		
Range of Exercise Prices *($/option)*	Options Outstanding *(thousands)*	Weighted Average Exercise Prices *($/option)*	Weighted Average Remaining Life *(years)*	Options Outstanding *(thousands)*	Weighted Average Exercise Prices *($/option)*	Weighted Average Remaining Life *(years)*
$ 1.42 – 1.74	3,395	$ 1.44	4.9	–	$ –	–
$ 1.75 – 1.85	1,559	1.81	4.2	286	1.83	3.9
$ 1.86 – 2.20	6,648	2.11	3.4	2,829	2.07	3.1
$ 2.21 – $2.72	3,853	2.58	3.3	1,287	2.58	3.3
	15,455	$ 2.05	3.8	4,402	$ 2.21	3.2

Total stock-based compensation, as included in the line item general and administrative expense as reported in the consolidated statements of operations, for the year ended December 31, 2011, was $5.6 million, (2010 – $5.9 million). The following factors were used in the Black-Scholes pricing model for the determination of the fair value for options granted during the year ended December 31, 2011 and 2010:

Year ended December 31	**2011**	2010
Expected average life *(years)*	**1 to 5**	1 to 5
Risk-free interest rate *(%)*	**0.86 to 2.84**	1.74 to 2.77
Estimated forfeiture rate per annum *(%)*	**0 to 30**	0 to 30
Volatility factor *(%)*	**44 to 59**	59 to 100

The weighted average fair value determined for options granted during the year ended December 31, 2011, was $0.52 per option (2010 – $1.02 per option).

d) Per Share Amounts

The per share amounts for the year ended December 31, 2011 and 2010, were calculated as per the following table. Diluted income per share assumes the exercise of options and Warrants as if issued at the later of the date of grant or the beginning of the period. This calculation takes into account only the options and Warrants that are considered to be "in-the-money" at December 31, 2011. Based on the Company's share price at December 31, 2011, per the treasury method, there were no additional shares that would have been added to the weighted average diluted shares outstanding for the years ended December 31, 2011 and 2010.

Year ended December 31	**2011**	2010
Net loss – continuing operations	**$ (63,752)**	$ (13,324)
Per share – basic and diluted *($/share)*	**$ (0.30)**	$ (0.08)
Net loss – discontinued operations	**$ –**	$ (13,540)
Per share – basic and diluted *($/share)*	**$ –**	$ (0.08)
Net loss	**$ (63,752)**	$ (26,864)
Per share – basic and diluted *($/share)*	**$ (0.30)**	$ (0.17)
Weighted average shares outstanding – basic and diluted *(thousands)*	**214,188**	162,003

15. Net Financing Expenses

Year ended December 31	2011	2010
Interest on bank debt	**$ 7,158**	$ 4,891
Interest earned on bank deposits	**(87)**	(89)
Finance charges and fees	**919**	6,772
Accretion of decommissioning obligation	**3,269**	2,675
Net financing expenses	**$ 11,259**	$ 14,249

16. Related Party Transactions

Chinook has determined that the key management personnel consists of its officers and directors. In addition to the salaries and directors fees paid to the officers and directors respectively, the officers and directors participate in the Company's share option plan. The officers salary and directors fees paid, in addition to stock-based compensation and other benefits, as included in general and administrative expenses relating to key management personnel for 2011 was $1.9 million and $2.7 million, respectively (2010 - $1.5 million and $3.1 million, respectively).

Chinook utilizes the services of a law firm in which the Corporate Secretary and a director of the Company are partners. During the year ended December 31, 2011, Chinook expensed $0.6 million (2010 - $1.6 million) on legal services obtained from the firm. At December 31, 2011, $0.1 million remained in accounts payable.

AIMCo is a major shareholder to which Chinook provides certain services to nominees of AIMCo pursuant to an administrative services and cost sharing agreement and manages the working interests of nominees of AIMCo in a limited partnership. The calculated reimbursement during the year ended December 31, 2011 is $3.0 million (year ended December 31, 2010 - $2.3 million), of which $0.3 million as at December 31, 2011, was included in accounts receivable (December 31, 2010 - $2.3 million). At December 31, 2011, a net payable of $0.1 million remained related to the ongoing operations of jointly-held producing and non-producing oil and natural gas properties (at December 31, 2010, a net payable of $6.1 million).

All related party transactions are in the normal course of business and have been valued at normal commercial terms.

17. Financial Instruments and Market Risk Management

Financial Instrument Classification and Measurement

Chinook's financial instruments carried on the consolidated statement of financial position are carried at amortized cost with the exception of cash, risk management contracts and a swap option, which are carried at fair value. There are no significant differences between the carrying value of financial instruments and their estimated fair values as at December 31, 2011.

Chinook's cash and risk management contracts are transacted in active markets whereas the swap option is not transacted in an active market. Chinook classifies the fair value of these transactions according to the following hierarchy based on the amount of observable inputs used to value the instrument:

- Level 1 – Quoted prices are available in active markets for identical assets or liabilities as of the reporting date. Active markets are those in which transactions occur in sufficient frequency and volume to provide pricing information on an ongoing basis.
- Level 2 – Pricing inputs are other than quoted prices in active markets included in Level 1. Prices in Level 2 are either directly or indirectly observable as of the reporting date. Level 2 valuations are based on inputs, including quoted forward prices for commodities, time value and volatility factors, which can be substantially observed or corroborated in the marketplace.
- Level 3 – Valuations in this level are those with inputs for the asset or liability that are not based on observable market data.

Chinook's cash, risk management contracts and swap option have been assessed on the fair value hierarchy described above. Chinook's cash is classified as Level 1 and risk management contracts and the swap option as Level 2. Assessment of the significance of a particular input to the fair value measurement requires judgment and may affect the placement within the fair value hierarchy level.

Market Risk Management

Chinook is exposed to a number of market risks that are part of its normal course of business. Management has primary responsibility for monitoring and managing financial instrument risks under direction from the Board of Directors, which has overall responsibility for establishing the Company's risk management framework. In the sections below, Chinook has prepared sensitivity analyses in an attempt to demonstrate the effect of changes in these market risk factors on its statement of operations.

Commodity Price Risk

Chinook's operational results and financial condition are largely dependent on the commodity prices received for its crude oil and natural gas production. Commodity prices have fluctuated widely during recent years due to global and regional factors including supply and demand fundamentals, inventory levels, weather, economic and geopolitical factors. Movement in commodity prices could have a significant positive or negative impact on Chinook's net loss. The use of such instruments is subject to limits established and approved by the Board of Directors. The Company's policy precludes the use of derivative financial instruments for speculative purposes.

Chinook is constantly exposed to the risk of changing commodity prices. Commodity prices for petroleum and natural gas are impacted by not only the relationship between the Canadian and United States dollar, but also global economic events that dictate the levels of supply and demand. To partially mitigate exposure to commodity price risk, Chinook has entered into various financial derivative instruments (see Risk Management Contracts). The following table illustrates the effects of movement in commodity prices on the net loss due to changes in the fair value of risk management contracts in place at December 31, 2011. The sensitivity is based on a 10% increase and decrease in the price of WTI, Brent and AECO natural gas. The commodity price assumptions are based on management's assessment of reasonably possible changes in oil and natural gas prices that could occur between December 31, 2011 and Chinook's next reporting date.

	Increase in Commodity Price		Decrease in Commodity Price	
	Crude Oil	Natural Gas	Crude Oil	Natural Gas
Net income increase (decrease)	$ (5,681)	$ (54)	$ 4,970	$ 54

As noted above, the sensitivities are hypothetical and based on management's assessment of reasonably possible changes in commodity prices between the statement of financial position and Chinook's next reporting date. The results of the sensitivity should not be considered to be predictive of future performance. Changes in the fair value of risk management contracts cannot generally be extrapolated because the relationship of change in certain variables to a change in fair value may not be linear.

Interest Rate Risk

Changes in interest rates would result in a change in the amount Chinook pays to service variable interest rate debt. If interest rates applicable to Chinook's variable rate debt were to increase by 100 bps it is estimated that Chinook's net income would decrease by $1.4 million, all of which is the result of increased interest expense as Chinook has no risk management contracts that would be affected by interest rates in place at December 31, 2011.

Foreign Exchange Risk

North American crude oil and natural gas prices are based, directly or indirectly, upon US dollar denominated commodity prices. As a result, the price received by Chinook is affected by the Canadian/US dollar exchange rate that may fluctuate over time.

All of the Company's Tunisian production revenues are received in US dollars whereas a significant portion of this segment's operational and capital expenditures are paid in United States dollars. Chinook translates the financial results and net assets of its Tunisian segment from US dollars to Canadian dollars using the average rate for the period and spot rate in effect on the date of the statement of financial position, respectively. Translation gains or losses are reported on the line item foreign currency translation gains (losses) of foreign operations as included within the statement of comprehensive loss. The following table illustrates the effects on Chinook's Tunisian segments net book value at December 31, 2011 of a 10 percent increase or decrease in the US dollar relative to the Canadian dollar:

	Decrease in USD/CAD	Increase in USD/CAD
Other comprehensive income increase (decrease) due to revaluation of USD to CAD	$ 8,330	$ (6,830)

As at December 31, 2011, the Company had no risk management contracts in place to reduce foreign exchange risk.

Risk Management Contracts

Chinook uses commodity price risk management contracts to reduce its exposure to fluctuations in commodity prices. The following price risk management contracts are in place as at December 31, 2011:

Natural Gas Indexed Price	Notional Volumes	Company's Received Price	Remaining period
AECO – C	3,800 GJ/d	$5.00/GJ to $7.70/GJ	January 1, 2012 to March 1, 2012

Crude Oil Indexed Price	Notional Volumes	Company's Received Price	Remaining period
WTI [1]	1,000 bbl/d	$98.75 US/bbl	January 1, 2012 to December 31, 2012
Brent	500 bbl/d	$100.00 US/bbl to $107.00 US/bbl	January 1, 2012 to December 31, 2012
Brent	500 bbl/d	$100.00 US/bbl to $133.00 US/bbl	January 1, 2012 to December 31, 2012

[1] West Texas Intermediate

The swap commodity price contracts are reported at their fair value as determined through the difference in the referenced market forward prices of the respective commodity over the remaining period of the contract as compared to Chinook's received price multiplied by the notional volumes during the remaining period. The swap option is reported at fair value as determined by a Black-Scholes model which includes the inputs of a forward WTI price and expected WTI price volatility over the remaining term of the swap option.

On or before December 31, 2012, the counterparty to the $98.75 *USD/bbl* swap crude oil price contract has the option, but not the obligation, to extend the commodity contract over the period January 1, 2013 to December 31, 2013, at the same strike price, indexed market and notional volume as the original swap crude oil contract. As at December 31, 2011, Chinook's fair value liability estimate of the swap option was $3.6 million.

The impact on Chinook's net loss from commodity price risk management contracts and the swap option contract for the years ending December 31, 2011 and 2010 were as follows:

Year ended December 31	2011	2010
Realized loss (gain) on swap commodity price contracts	$ 821	$ (7,354)
Unrealized loss (gain) on swap commodity price contracts and swap option	3,965	3,906
	$ 4,786	$ (3,448)

18. Financial Assets and Credit Risk

Credit risk is the risk of financial loss to Chinook if a partner or counterparty to a product sales contract or financial instrument fails to meet its contractual obligations. Chinook is exposed to credit risk with respect to is accounts receivable and risk management contracts. Most of Chinook's accounts receivable relate to oil and natural gas sales and are subject to typical industry credit risk. The majority of the credit exposure on accounts receivable at December 31, 2011 pertains to accrued revenue for December 2011 production volumes. Chinook transacts with a number of commodity end users ("purchasers"). Purchasers typically remit amounts to Chinook prior to end of the month following production. Joint interest receivables are typically collected within one to three months following production. At December 31, 2011, no one counterparty accounted for more than 25 percent of the total accounts receivable balance.

Chinook's allowance for doubtful accounts was $2.9 million and $2.7 million as at December 31, 2011 and 2010, respectively. Chinook recognized an additional provision of $0.3 million and $2.7 million for non-collectable accounts receivable during the years ended December 31, 2011 and 2010, respectively. When determining whether amounts that are past due are collectable, management assesses the credit worthiness and past payment history of the counterparty, as well as the nature of the past due amount. Chinook considers all amounts greater than 90 days after the due date to be past due. As at December 31, 2011, $8.3 million of accounts receivable are past due, all of which but $2.9 million are considered to be collectible.

Maximum credit risk is calculated as the total recorded value of cash, accounts receivable and risk management contract assets at the statement of financial position date.

19. Financial Liabilities and Liquidity Risk

Liquidity difficulties would emerge if Chinook was unable to meet its financial obligations as they fell due within normal credit terms. The Company prepares annual budgets, which are monitored and updated as required. Generally the Company will, over a reasonable period of time, limit its capital programs to available funds. The Company frequently evaluates the options available, with respect to sources of short and long-term capital. Management believes that future cash flows generated from these sources will be adequate to settle Chinook's financial liabilities.

The following table details Chinook's financial liabilities as at December 31, 2011:

	Within 1 year	1 to 2 years
Accounts payable and accrued liabilities	$ 60,398	$ –
Risk management contracts	20	–
Swap option contract	3,560	–
Long-term debt	–	137,500
Total financial liabilities	$ 63,978	$ 137,500

Chinook actively maintains credit and working capital facilities to ensure that it has sufficient available funds to meets its financial requirements at a reasonable cost. Refer to Note 11 for further details on available amounts under the existing banking arrangement.

20. Commitments and Contingencies

At December 31, 2011, the Company had commitments that require the following minimum future payments:

Year ended December 31	2012	2013	2014	2015	Total
Long-term debt and interest	$ 5,775	$ 140,388	$ –	$ –	$ 146,163
Operating leases	3,171	1,995	916	99	6,181
	$ 8,946	$ 142,383	$ 916	$ 99	$ 152,344

Certain office space has been sublet resulting in a partial recovery of costs for varying terms extending through to July 31, 2012. As a result of the sublet leases, which are not included in the above table, the Company recovers lease payments of approximately $1.3 million and $0.2 million for the years ended December 31, 2012 and 2013, respectively.

Chinook is involved in litigation and claims arising in the normal course of operations. Such claims are not expected to have a material impact on Chinook's results of operations or cash flows.

21. Supplemental Disclosures

a) Consolidated statement of operations presentation

Chinooks statement of operations is prepared primarily by nature of expense, with the exception of employee compensation costs which are included in both the operating and general and administrative expense line items.

The following table details the amount of total employee compensation costs included in the operating and general and administrative expense line items in the statement of operations.

Year ended December 31	2011	2010
Operating	**$ 18,806**	$ 7,630
General and administrative	**9,098**	11,642
Total employee compensation cost	**$ 27,904**	$ 19,272

b) Consolidated statement of cash flows

Changes in non-cash working capital

Year ended December 31	2011	2010
Accounts receivable	**$ (7,778)**	$ (7,127)
Accounts payable and accrued liabilities	**(6,823)**	22,265
Prepaids, deposits, inventory and other	**894**	10,135
Taxes payable	**(2,311)**	(1,189)
	$ (16,018)	24,084
Operating activities	**$ (11,169)**	$ 5,256
Investing activities	**(4,030)**	17,781
Financing activities	**(819)**	–
Discontinued operations	**–**	1,047
	$ (16,018)	$ 24,084

Other supplemental cash flow information:

Year ended December 31	2011	2010
Cash taxes paid	**$ 5,896**	$ 4,686
Cash interest paid	**$ 7,190**	$ 4,264

22. Segmented Information

Chinook's continuing operating and reportable segments are as follows:

- **Canada –** includes the Company's Western Canadian Sedimentary Basin's producing properties and undeveloped land predominately located in the Peace River and Grande Prairie areas located along the northern portion of the border between the Provinces of British Columbia and Alberta and extending down to West Central Alberta.
- **Tunisia –** includes eight blocks totaling over three million gross acres: offshore in the Gulf of Hammamet within the Pelagian Basin (Cosmos, Yasmin and Hammamett) with onshore properties located in Sud Remada, Bir Ben Tartar, Jenein, Adam and Borj El Khadra Blocks, all within the Ghadames Basin.
- **Corporate –** includes general and administrative costs and assets held corporately.

Selected Segment Information

	Canada		Tunisia		Corporate		Consolidated	
Year ended December 31	2011	2010	2011	2010	2011	2010	2011	2010
Capital expenditures	**$ 88,351**	$ 220,200	**$ 30,913**	$ 12,281	**$ 437**	$ 2,892	**$ 119,701**	$ 235,373
Development & production and exploration & evaluation assets	**$ 579,690**	$ 730,404	**$ 95,395**	$ 67,385	**$ 3,127**	$ 2,754	**$ 678,212**	$ 800,543
Total assets	**$ 631,048**	$ 789,477	**$ 103,614**	$ 79,229	**$ 10,741**	$ 8,311	**$ 745,403**	$ 877,017

Results by Segment [1]

	Canada		Tunisia		Corporate		Consolidated	
Year ended December 31	2011	2010	2011	2010	2011	2010	2011	2010
Revenue								
Petroleum, natural gas and other revenue, net of royalties	**$ 171,717**	$ 103,296	**$ 39,514**	$ 16,660	**$ –**	$ 2	**$ 211,231**	$ 119,958
Expenses								
Production and operating	**92,093**	42,018	**7,483**	3,327	**–**	–	**99,576**	45,345
General and administrative	**–**	–	**1,118**	739	**18,586**	22,410	**19,704**	23,149
Exploration and evaluation expenditures	**5,096**	2,993	**6,590**	7,689	**–**	–	**11,686**	10,682
Derivative transactions and swap option gain	**–**	–	**–**	–	**4,786**	(3,448)	**4,786**	(3,448)
Financing expenses	**11,161**	13,962	**93**	275	**5**	12	**11,259**	14,249
Depletion, depreciation and amortization	**101,286**	63,724	**8,984**	2,030	**40**	21	**110,310**	65,775
Impairment of developed and producing assets	**43,000**	–	**–**			–	**43,000**	–
Gain on disposition of properties	**(22,914)**	(25,748)	**–**	(0)	**–**	–	**(22,914)**	(25,748)
Foreign exchange loss (gain)	**–**	–	**59**	613	**(1)**	1,062	**58**	1,675
Other	**–**	–	**115**	–	**(885)**	–	**(770)**	–
	229,722	96,949	**24,442**	14,673	**22,531**	20,057	**276,695**	131,679
Income (loss) before income taxes and discontinued operations	**(58,005)**	6,347	**15,072**	1,987	**(22,531)**	(20,054)	**(65,464)**	(11,721)
Income Taxes								
Current income tax	**7**	37	**3,489**	4,208	**–**	–	**3,496**	4,245
Deferred income tax (recovery)	**(7,181)**	(4,456)	**1,973**	1,814	**–**	–	**(5,208)**	(2,642)
	(7,174)	(4,419)	**5,462**	6,022	**–**	–	**(1,712)**	1,603
Net income (loss) before discontinued operations	**(50,831)**	10,766	**9,610**	(4,035)	**(22,531)**	(20,055)	**(63,752)**	(13,324)
Discontinued operations net of income taxes	**–**	–	**–**	–	**–**	(13,540)	**–**	(13,540)
Net income (loss)	**(50,831)**	10,766	**9,610**	(4,035)	**(22,531)**	(33,595)	**(63,752)**	(26,864)

[1] United Kingdom segment was sold in May 2010 and shown as discontinued operations in the Corporate segment during the year ended December 31, 2010.

23. Discontinued Operation

On March 30, 2010, Chinook's indirect wholly-owned subsidiary, Silverstone Energy Limited ("Silverstone"), completed a business combination transaction with Bridge Energy Norge AS whereby each of the companies became subsidiaries of a holding company, Bridge Energy ASA ("Bridge Energy"). Storm Ventures International (BVI) Limited formerly owned all of the shares of Silverstone which contained Chinook's United Kingdom – North Sea business. Pursuant to the transaction, Storm Ventures International (BVI) Limited received 28.8 million common shares of Bridge Energy, which represented approximately 80% of the Bridge Energy shares, which were outstanding immediately following the business combination. On March 30, 2010, Bridge Energy also issued 16.2 million shares to subscribers in a private placement at NOK 20 per share (or approximately USD $3.33 per share), for gross proceeds of NOK 324.5 million (or approximately USD $54.1 million). Following the private placement, Chinook's ownership in Bridge Energy was reduced to 55.1%. The dilution loss of $28.2 million associated with Chinook's change in ownership was accounted for as a reduction to retained earnings at March 31, 2010.

On May 10, 2010, the Company distributed all of the shares of Bridge Energy, held by Storm Ventures International (BVI) Limited, to its shareholders of record as of April 20, 2010, such that the Company no longer has ownership in any assets or holdings in the North Sea. Operating results related to these assets have been included in net loss from discontinued operations on the consolidated statement of operations and comprehensive loss for the year ended December 31, 2010, which incorporated the effect of the discontinued operation on the following line items:

Year ended December 31	2010
Revenue	
Production revenue	$ 6,510
Royalties	(493)
	6,017
Processing and other income	15
	6,032
Expenses	
Production expenses	772
General and administration	1,330
Derivatives gain	(930)
Foreign exchange gain (loss)	4
Depletion, depreciation and accretion	31,672
Release of decommissioning provision	–
Interest expense	258
	33,106
Net loss before tax	(27,074)
Future taxes (recovery)	(13,534)
Net income (loss) from discontinued operations	$ (13,540)

The distribution has been accounted for as a distribution of equity and resulted in a charge to retained earnings in the amount of $218.5 million and recovery of accumulated other comprehensive losses of $21.2 million. As at January 1, 2010, immediately prior to adoption of IFRS, Chinook had an accumulated comprehensive loss of $13.9 million related to this discontinued operation.

24. International Financial Reporting Standards Adoption

Chinook adopted IFRS on January 1, 2011, with a transition date of January 1, 2010, (the "Transition Date"). Prior to adopting IFRS, Chinook prepared its consolidated financial statements in accordance with the previous Canadian generally accepted accounting principles ("GAAP"). While the adoption of IFRS has not changed Chinook's cash flows, the adoption has resulted in changes to its reported financial position and results of operations.

IFRS 1 sets forth guidance for the initial adoption of IFRS. Under IFRS 1 the standards are applied retrospectively at the Transition Date with all adjustments to assets and liabilities recognized in retained earnings unless certain exemptions are applied.

IFRS employs a conceptual framework that is similar to Canadian GAAP. However, significant differences exist in matters of recognition, measurement and disclosure of specific items. While adoption of IFRS has not changed Chinook's actual cash flows, it has resulted in changes to Chinook's reported financial position and results of operations. Chinook's statements of financial position at January 1, 2010 and December 31, 2010 as prepared under Canadian GAAP and statement of operations and comprehensive loss for the year ended December 31, 2010, as prepared under Canadian GAAP, have been reconciled to IFRS, with the resulting adjustments explained in the following notes:

Consolidated Statement of Financial Position

As at January 1, 2010

	GAAP	IFRS 1 *(note 24(a))*	IFRS 1 *(note 24(b))*	IFRS 1 *(note 24(c))*	IFRS 1 *(note 24(d))*	Total	Reclass	IFRS
Assets								
Current								
Cash	$ 8,027	$ –	$ –	$ –	$ –	$ –	$ –	$ 8,027
Accounts receivable	10,660	–	–	–	–	–	–	10,660
Prepaids, deposits, inventory and other	13,141	–	–	–	–	–	–	13,141
	31,828	–	–	–	–	–	–	31,828
Property held for sale	–	–	–	–	–	–	13,968	13,968
Development and production assets	362,372	(2,554)	(87,095)	–	–	(89,649)		272,723
Exploration and evaluation assets	–		87,095	–	–	87,095	(13,968)	73,127
	$ 394,200	$ (2,554)	$ –	$ –	$ –	$ (2,554)	$ –	$ 391,646
Liabilities and Shareholders' Equity								
Current								
Accounts payable, accrued liabilities and other	$ 10,130	$ –	$ –	$ –	$ –	$ –	$ –	$ 10,130
Current portion of long-term debt	8,170	–	–	–	–	–	–	8,170
Taxes payable	133	–	–	–	–	–	–	133
	18,433	–	–	–	–	–	–	18,433
Long-term debt	11,166	–	–	–	–	–	–	11,166
Decommissioning obligation	6,032	–	–	75	–	75	–	6,107
Deferred income taxes	29,552	–	–	–	–	–	–	29,552
Other liabilities	161	–	–	–	–	–	–	161
Shareholders' equity								
Share capital	344,703	–	–	–	–	–	–	344,703
Contributed surplus	4,137	–	–	–	979	979	–	5,116
Deficit	(6,298)	(16,240)	–	(75)	(979)	(17,294)	–	(23,592)
Accumulated other comprehensive income (loss)	(13,686)	13,686	–	–	–	13,686	–	–
	328,856	(2,554)	–	(75)	–	(2,629)	–	326,227
	$ 394,200	$ (2,554)	$ –	$ –	$ –	$ (2,554)	$ –	$ 391,646

(a) Cumulative translation differences

The Company elected to set the cumulative translation account, which is included in accumulated other comprehensive loss, to nil at the Transition Date. As a result of IAS 21, The Effects of Changes in Foreign Exchange Rates (see Note 24(j)), the Company recognized $2.6 million of cumulative currency exchange losses as at the Transition Date related to its Tunisian segment. The Company elected as at the Transition Date to remove the Tunisian segment's cumulative currency exchange losses that would have been reportable as accumulated other comprehensive losses and, accordingly, increase the deficit.

(b) Deemed cost exemption for development and production and exploration and evaluation assets

The Company has elected to report these assets on the Transition Date at the deemed Canadian GAAP net carrying value versus retroactive application of IFRS. Crude oil and natural gas assets that were part of the full cost pool and determined to be developed or production assets under Canadian GAAP were allocated to CGUs pro rata using reserve values, subject to an impairment test on the Transition Date to IFRS.

(c) Decommissioning liability

In accounting for changes in obligations to dismantle, remove and restore items of development and production assets, the guidance under IFRS requires changes in such obligations to be added to or deducted from the cost of the asset to which it relates. The adjusted depreciable amount of the asset is then depreciated prospectively over its remaining useful life. Rather than recalculating the effect of all such changes throughout the life of the obligation, the Company has elected to measure the liability and the related accretion effects at the Transition Date which had the effect of increasing the decommissioning liability by $0.1 million, with an offsetting increase to the deficit.

(d) Share-based compensation

The Company has elected not to apply IFRS 2 "Share-Based Payments" to options which vested before the Transition Date. As such, a $1.0 million increase in the deficit was made for options that were granted before the Transition Date but had not vested, with an offsetting increase in contributed surplus.

(e) Business combinations

The Company applied the exemption to not retrospectively report IFRS 3 Business Combinations for any business combinations prior to the Transition Date.

In October 2009, Chinook entered into an agreement with British Petroleum Ltd. to acquire their 25% working interest in certain North Sea, UK fields in exchange for Chinook's interest in the Vanquish, North Sea UK field. The deal closed in 2010. Under IFRS, upon review of this transaction the conditions to disclose the Vanquish field asset as held for sale were judged to have been met whereas under Canadian GAAP such conditions were judged not to have been met. As a result, Chinook has reclassified $14.0 million from exploration & evaluation assets to property held for sale.

In addition to the IFRS 1 exemptions applied above, all applicable mandatory exceptions prescribed in IFRS 1 have been applied at the date of transition. No effect of hindsight was used in calculating transitional amounts.

Consolidated Statement of Financial Position

As at December 31, 2010

		Adjustments									
	GAAP	IFRS 1	IAS 12 *(note 24(f))*	IAS 16 *(note 24(g))*	IFRS 2 *(note 24(h))*	IAS 37 *(note 24(i))*	IAS 21 *(note 24(j))*	IFRS 6 *(note 24(k))*	Total	Reclass *(note 24(l))*	IFRS
Assets											
Current											
Cash	$ 23,195	$ –	$ –	$ –	$ –	$ –	$ –	$ –	$ –	$ –	$ 23,195
Accounts receivable	40,681	–	–	–	–	–	–	–	–	–	40,681
Derivative contracts	3,516	–	–	–	–	–	–	–	–	–	3,516
Prepaids, deposits, inventory and other	7,318	–	–	–	–	–	–	–	–	–	7,318
	74,710	–	–	–	–	–	–	–	–	–	74,710
Long-term derivative contracts	1,764	–	–	–	–	–	–	–	–	–	1,764
Development and production assets	729,258	(89,649)	–	38,516	–	58,074	(3,232)	–	3,709	15,404	748,371
Exploration and evaluation assets	–	87,095	–	–	–	–	–	(19,519)	67,576	(15,404)	52,172
	$ 805,732	$ (2,554)	$ –	$ 38,516	$ –	$ 58,074	$ (3,232)	$ (19,519)	$ 71,285	$ –	$ 877,017
Liabilities and Shareholders' Equity											
Current											
Accounts payable, accrued liabilities and other	$ 70,138	$ –	$ –	$ –	$ –	$ –	$ –	$ –	$ –	$ –	$ 70,138
Derivative contracts	4,345	–	–	–	–	–	–	–	–	–	4,345
Taxes payable	2,902	–	–	–	–	–	–	–	–	–	2,902
Current portion of deferred income taxes	1,114	–	(1,114)	–	–	–	–	–	(1,114)	–	–
	78,499	–	(1,114)	–	–	–	–	–	(1,114)	–	77,385
Long-term debt	167,793	–	–	–	–	–	–	–	–	–	167,793
Decommissioning obligation	74,705	75	–	–	–	50,873	–	–	50,948	–	125,653
Deferred income taxes	4,978	–	8,785	–	–	–	–	–	8,785	–	13,763
Other liabilities	2,641	–	–	–	–	–	–	–	–	–	2,641
Shareholders' equity											
Share capital	778,070	–	–	–	–	–	–	–	–	–	778,070
Contributed surplus	10,985	979	–	–	(371)	–	–	–	608	–	11,593
Deficit	(311,939)	(17,294)	(7,671)	38,516	371	7,201	(271)	(19,519)	1,333	13,686	(296,920)
Accumulated other comprehensive income (loss)	–	13,686	–	–	–	–	(2,961)	–	10,725	(13,686)	(2,961)
	477,116	(2,629)	(7,671)	38,516	–	7,201	(3,232)	(19,519)	12,666	–	489,782
	$ 805,732	$ (2,554)	$ –	$ 38,516	$ –	$ 58,074	$ (3,232)	$ (19,519)	$ 71,285	$ –	$ 877,017

Consolidated Statement of Operations and Comprehensive Loss

Year ended December 31, 2010

		Adjustments						
	GAAP	IAS 16 *(note 24(g))*	IFRS 2 *(note 24(h))*	IAS 37 *(note 24(i))*	IAS 21 *(note 24(j))*	IFRS 6 *(note 24(k))*	Total	IFRS
Revenue								
Petroleum, natural gas and other revenue, net of royalties	$ 119,958	$ –	$ –	$ –	$ –	$ –	$ –	$ 119,958
Expenses								
Production and operating	45,345	–	–	–	–	–	–	45,345
General and Administrative	23,520	–	(371)	–	–	–	(371)	23,149
Exploration and evaluation	–	–	–	–	–	10,682	10,682	10,682
Derivative transaction gain	(3,448)	–	–	–	–	–	–	(3,448)
Financing expenses	11,574	–	–	2,675	–	–	2,675	14,249
Depletion, depreciation and amortization	79,583	(18,984)	–	(3,661)	–	8,837	(13,808)	65,775
Gain on disposition of properties	–	(19,532)	–	(6,216)	–	–	(25,748)	(25,748)
Foreign exchange loss (gain)	1,404	–	–	–	271	–	271	1,675
	157,978	(38,516)	(371)	(7,202)	271	19,519	(26,299)	131,679
Income (loss) before income taxes and discontinued operations	(38,020)	38,516	371	7,202	(271)	(19,519)	26,299	(11,721)
Income taxes								
Current income tax	4,245	–	–	–	–	–	–	4,245
Deferred income tax expense (recovery)	(10,313)	11,235	108	2,101	(79)	(5,693)	7,671	(2,642)
	(6,068)	11,235	108	2,101	(79)	(5,693)	7,671	1,603
Net income (loss) from continuing operations	(31,952)	27,281	263	5,101	(192)	(13,826)	18,628	(13,324)
Discontinued operations, net of income taxes	(13,540)	–	–	–	–	–	–	(13,540)
Net income (loss)	$ (45,492)	$ 27,281	$ 263	$ 5,101	$ (192)	$ (13,826)	$ 18,628	$ (26,864)
Net income (loss) per share, basic and diluted, continuing operations	$ (0.20)	$ 0.17	$ 0.00	$ 0.03	$ (0.00)	$ (0.09)	$ 0.11	$ (0.08)
Net income (loss) per share, basic and diluted (income)	$ (0.28)	$ 0.17	$ 0.00	$ 0.03	$ (0.00)	$ (0.09)	$ 0.11	$ (0.17)
Consolidated statement of comprehensive income (loss)								
Net income (loss)	$ (45,492)	$ 27,281	$ 263	$ 5,101	$ (192)	$ (13,826)	$ 18,628	$ (26,864)
Foreign currency translation loss on foreign operations	(21,179)	–	–	–	(2,961)		(2,961)	(24,140)
Available for sale assets fair value adjustment	(5)	–	–	–	–	–	–	(5)
Comprehensive income (loss)	$ (66,676)	$ 27,281	$ 263	$ 5,101	$ (3,153)	$ (13,826)	$ 15,667	$ (51,009)

(f) IAS 12 Adjustments – Income Taxes

Under IFRS, in comparison to Canadian GAAP, deferred income taxes are not to be classified as current liabilities. As such, Chinook reclassified the current deferred income taxes as reported under Canadian GAAP at December 31, 2011, to long-term deferred income taxes as reported under IFRS.

The Company has recognized an additional $7.7 million of deferred income tax expense for the year ended December 31, 2010 resulting from changes in its accounting bases due to the following IFRS adjustments.

(g) IAS 16 Adjustments – Property and Equipment

Under Canadian GAAP, a gain or loss on disposition of properties is reported when the subsequent full cost depletion rate changes by 20% or more, otherwise the proceeds of the property sale reduce the full cost pool. Under IFRS, any differences from proceeds of the property sale relative to its net book value are reported as either gains or losses. For the year ended December 31, 2010, the Company sold properties which did not change its full cost depletion rate by at least 20% under previous Canadian GAAP but resulted in IFRS reportable gains of $19.5 million.

Upon transition to IFRS, the Company adopted a policy of depleting crude oil and natural gas assets on a unit-of-production basis over proved plus probable reserves. The depletion policy under Canadian GAAP was based on units-of-production over proved reserves. In addition, IFRS requires depletion to be calculated at a component level where such components have similar economic lives whereas under Canadian GAAP depletion was calculated on the Company's petroleum and natural gas assets at a geographic level. As a result of these differences between IFRS and Canadian GAAP, the Company recognized a $19.0 million decrease in its depletion expense, as reported within the line item depletion, depreciation and amortization, for the year ended December 31, 2010.

(h) IFRS 2 Adjustments – Share-Based Payments

For the year ended December 31, 2010, under IFRS the Company recognized a decrease in stock-based compensation of $0.4 million. Share-based compensation for the year ended December 31, 2010, decreased under IFRS mostly due to the inclusion of forfeiture estimates, as based on historical forfeitures, in the redetermination of the fair value of granted options during this period in addition to the unvested outstanding options at the Transition Date relative to Canadian GAAP where forfeitures of awards were recognized as they occurred.

(i) IAS 37 Adjustments – Provisions, Contingent Liabilities and Contingent Assets

Under Canadian GAAP, accretion expense was included in the line item depletion, depreciation and accretion whereas under IFRS, accretion expense related to the decommissioning liability is included in the line item financing expenses resulting in the reclassification of $3.7 million for the year ended December 31, 2010. Further, under Canadian GAAP decommissioning liabilities were discounted at the Company's credit adjusted risk free rate of 8.5% whereas under IFRS the estimated cash flow to abandon and remediate wells and facilities has been risk adjusted resulting in the use of a risk free discount rate. The lower discount rate applied to the decommissioning liability under IFRS relative to Canadian GAAP resulted in lower accretion expense of $1.0 million for the year ended December 31, 2010 respectively as reported in the line item financing expenses, of $2.7 million. The affect of the lower discount rate as applied under IFRS relative to Canadian GAAP, resulted in the Company recognizing a $58.1 million increase in its decommissioning obligation, with a corresponding increase in developed & producing assets, as partially offset by $6.2 million through the disposal of decommissioning obligations through the sale of producing properties.

(j) IAS 21 Adjustments – The Effects of Changes in Foreign Exchange Rates

Under IFRS, the functional currency of a subsidiary or branch is determined by focusing on the primary economic environment in which it operates with less emphasis placed on factors such as the financing from and operational involvement of the consolidated reporting entity. This resulted in the Company's Tunisian operations being assessed as having a U.S. dollar functional currency versus the Company's Canadian dollar reporting currency. As such, the foreign exchange gains or losses that arise between the translation of the Tunisian operational results and statements of financial position into the Company's reporting currency are recognized in other comprehensive income. Previously, under Canadian GAAP, the Company considered its Tunisian operations as integrated whereby only exchange differences between the monetary net assets and operational results were reported as foreign exchange gains or losses.

The application of IAS 21 resulted in adjustments to the following accounts:

Other Comprehensive Loss and Accumulated Other Comprehensive Income (Loss)

For the year ended December 31, 2010, under IFRS, the Company reported a $3.0 million foreign currency translation adjustment as other comprehensive loss, upon the revaluation of its Tunisian operational results and statement of financial position.

Foreign Exchange Gain (Loss)

The Company, under Canadian GAAP, recognized a foreign exchange gain of $0.3 million for the year ended December 31, 2010 on the revaluation from US dollar denominated monetary net assets to Canadian dollars. The Company reversed these Canadian GAAP foreign exchange adjustments for the year ended December 31, 2010 as under IFRS foreign exchange adjustments between the revaluation of the Tunisian net assets and operational results are reported through other comprehensive income (loss).

(k) IFRS 6 Adjustments – Exploration and Evaluation Assets

Under IFRS, the Company has selected an accounting policy whereby exploratory lands will be amortized over the life of the lease term (generally a term of five years in Canada) in addition to other exploration costs concomitant to such lands. Under IFRS, the Company has also selected the accounting policy to expense all exploratory dry holes and geological and geophysical expenditures as incurred. Under Canadian GAAP, the Company followed the full cost method of accounting for its petroleum and natural gas interests whereby all exploration costs were capitalized and accumulated within geographic cost centres.

For the year ended December 31, 2010, under the Company's IFRS 6 accounting policies, the Company expensed $10.7 million of prospecting and exploration expense most of which pertained to the unsuccessful drilling of exploratory wells on the Company's Tunisian exploration lands as previously capitalized to property, plant and equipment under Canadian GAAP, in addition to amortizing $8.8 million of expenditures mostly associated with its Canadian undeveloped lands.

(l) Reclassification

Exploration & Evaluation Assets to Developed & Producing Assets

As at January 1, 2010, the majority of Chinook's developed & producing and exploration & evaluation assets were comprised by its UK North Sea operations, which were subsequently disposed during 2010 (see Note 23) and gave effect to reduce the aforementioned balances. In addition, Chinook adjusted its 2010 capital expenditures as reported under Canadian GAAP from developed & producing to exploration & evaluation assets. The net effect of these movements gave rise to a reclassification from exploration & evaluation assets to developed & producing assets.

Accumulated Other Comprehensive Income to Deficit

Under Canadian GAAP, during May 2010, Chinook distributed its holdings in Bridge Energy ASA ("Bridge Energy"), to Chinook's shareholders which resulted in a charge to its retained earnings of $232.2 million. Bridge Energy partially held Chinook's United Kingdom – North Sea operations on which it had reported $13.7 million in accumulated other comprehensive losses immediately prior to the Transition Date. As Chinook elected on the Transition Date to apply the IFRS 1 exemption whereby all cumulative foreign exchange losses are moved to its deficit account, the Company also made an adjustment to the distribution of its holdings in Bridge Energy to its shareholders by decreasing the loss by $13.7 million as offset in accumulated other comprehensive losses.