Clear direction. Global growth.

Arsenal Energy Inc.

LETTER TO SHAREHOLDERS

The second quarter of 2006 was extremely rewarding to Arsenal. The Tower Creek well successfully reached a total depth of 5100 meters late in the quarter ahead of schedule and under budget. This well was completed and flow tested in early August and initial results indicate that the well has encountered a significant reservoir which we expect to put onto production late in the fourth quarter of 2006 or early in the first quarter of 2007 at a rate of approximately 20 million cubic feet of gas per day ("mmcf/d").

The same factors that delayed the testing of this significant discovery caused some of our production to be shut-in for a portion of the quarter, resulting in actual production of 1,717 barrels of oil equivalent lagging our original forecasts.

In July we continued to strengthen our senior management team with the hiring of Mr. Tony VanWinkoop, a Geologist with more than 25 years experience in the Western Canadian sedimentary basin, the Williston Basin of North Dakota and Eastern Canada's Offshore Rift Basin. Tony's addition to the team has already added immediate value in our efforts to expand, explore and exploit our existing lands at Evi, Lubicon and Worsley, and will enhance exploitation at Galahad, Princess/Alderson, Wildmere, Maidstone and North Dakota. This experience will also assist us in our efforts to explore the Nuqra Rift Basin in Egypt as well as evaluate and access additional international opportunities.

At the end of June we were able to secure drilling rigs, and throughout July had as many as four rigs drilling at one time. This drilling program consisted of 2 additional wells being drilled at Worsley, 2 wells drilled at Lubicon, 1 well drilled at Evi and 3 wells drilled at Wildmere. Arsenal is pleased to announce that all of these wells were cased. We will continue to move as quickly as drilling and completion services allow to continue to evaluate and bring the successful wells into production as soon as possible.

In April we completed the processing of the 800 kilometers of newly acquired seismic data in Egypt and in July we completed the interpretation of the total 4000 kilometers of seismic data which allowed us to select the top prospects to be drilled. We are finalizing the selection of the initial 2 locations, have identified an available rig and are negotiating the drilling rig contract. We will release additional information when these locations are finalized and the rig contract is signed.

ARSENAL ENERGY INC.

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SECOND QUARTER CORPORATE HIGHLIGHTS

- Record cashflow $2.12 million for the three months ended June 30th.
- Successful drilling, completion and testing of a deep gas well at Tower Creek.
- Completion of processing of 800 kilometers of new seismic data over the Nuqra concession in Egypt, included the new data into the interpretation of the total 4000 kilometers of data and high graded the locations to position us to finalize the first two wells slated to be drilled in the fourth quarter of 2006 or early in 2007.
- Drilled and cased 8 gross wells in June and July of 2006 at Worsley, Evi, Lubicon, Alderson and Wildmere.

OPERATIONS IN REVIEW

Production averaged a record 1,717 barrels of oil equivalent per day, exiting the quarter at approximately 2,000 barrels of oil equivalent per day, with approximately 250 barrels of oil equivalent per day behind pipe and an additional 250 barrels of oil equivalent shut-in awaiting service rigs and optimization. We were unable to secure rigs due to weather and activity levels until June. We had as many as four rigs drilling throughout July at Worsley, Evi, Lubicon, Alderson and Wildmere. Several wells at Lloydminster were shut in awaiting a service rig for several weeks during the quarter. These factors resulted in our production lagging our forecast.

TOWER CREEK

The Tower Creek well was drilled and cased on time and under budget during the second quarter. A short production test was completed in early August, and indicate hydrocarbon accumulations of significant levels. The well was flowed for a total of 36 hours at several flow rates with a total of 21 mmscf of gas produced during the test period. A final stabilized rate of 14.7 mmscf/d at a flowing tubing pressure of 26,000 kPa (3,770 psi) was maintained. The final flow rate was restricted to comply with EUB flare permit limitations.

Arsenal and its partners have estimated that the well will initially produce 20.0 mmcf/d. We expect to have an independent initial reserve analysis completed in the near future. The level of CO_2 and sulphur in this well came in below our projections leaving room for additional reserves as a result. Arsenal and its partners have identified competing facilities within a 40 kilometer radius with sufficient capacity and we are presently trying to finalize a deal which will bring this well into production at the end of 2006, or early 2007 subject to pipeline crew availability.

EGYPT

An 800 km 2-D seismic acquisition program commenced in early January 2006 was completed during April. This new data was processed by the end of the second quarter. Arsenal and partners have now combined the newly acquired data and the original 3,200 kilometers of data into a combined interpretation and are preparing for a two well exploration drilling program to commence in late 2006, or early 2007. Production casing, wellheads and other long lead time item have been ordered with deliveries scheduled for early in the third quarter. An available drilling rig has been identified and we are presently finalizing a contract for this drilling rig.

NORTH DAKOTA

Production has remained stable throughout the second quarter and we are continuing to evaluate with the intent of conducting further operations to enhance production.

LLOYDMINISTER

We have initiated a three well drilling program at Wildmere which was completed in early August. The first well was brought into production at encouraging rates and we expect the other two to be on production by the end of the third quarter.

WORSLEY

We were successful in adding to our land base here through crown land sales in the second quarter. We drilled and cased our first well at the end of the first quarter. This well was completed during the second quarter and it is expected to be on production in the third quarter. We have drilled and cased an additional two wells by the end of July which are in the process of being evaluated. This is an area which has multi-zone potential and several other operators have drilled extremely prolific wells on acreage in the vicinity during the past six months. We are optimistic about our prospects in this area and we will continue to add to our land position as opportunities are identified.

COMMODITY PRICING

Crude oil continues to test historical highs with increasing tension in the Middle East, stagnant global production and periodic supply interruptions. It is anticipated in the market that West Texas Intermediate crude could remain around $70 US for the remainder of the year.

Natural gas prices have been significantly depressed during the first half of the year, however recent heat waves in the northeastern United States have resulted in considerable storage draws, and prices have strengthened throughout July and August. Natural gas futures for winter 2006 and 2007 deliveries are presently above $10 US on the NYMEX exchange.

The winter of 2005 and 2006 witnessed record heavy oil differentials in Canada, which had a significant impact on our corporate cashflow. The differential in the second quarter tightened considerably, reflecting historical seasonality, and currently is less than $20 per barrel.

The acquisition of Tiverton and drilling gas plays like Tower Creek demonstrate Arsenal's commitment to a reduction in exposure to wide heavy oil differentials. Historically, natural gas prices have increased in the winter and trended lower during the summer, which is the reciprocal of the heavy oil price trend and we expect this to continue. Increasing our exposure to natural gas will act as a natural hedge to our existing heavy oil production and we will continue to seek out opportunities to grow in this direction.

OUTLOOK

In the third quarter, we will put new wells drilled at Worsley, Evi, Lubicon, Alderson and Wildmere into production as quickly as possible while continuing to drill in these areas. We will continue to pursue acquisition opportunities we believe will help us to build shareholder value at Arsenal. We will be finalizing locations for the first wells on the Nuqra concession in Egypt which are slated to be drilled during the fourth quarter of 2006 or early 2007. We will continue to pursue additional international opportunities that match our stringent guidelines. We would like to thank our shareholders for their support and look forward to continuing the growth in share value which we have demonstrated and which you continue to expect from Arsenal Energy Inc.

On behalf of the Board of Directors,

Errol Stewart
President and Chief Executive Officer

SELECTED FINANCIAL AND OPERATIONAL INFORMATION

	Three Months Ended June 30		Six Months Ended June 30	
FINANCIAL	**2006**	2005	**2006**	2005
Financial				
Funds from operations[1]	**2,167,425**	871,288	**3,124,643**	1,357,861
Per unit - basic	**0.04**	0.03	**0.06**	0.06
Per unit - diluted	**0.04**	0.03	**0.05**	0.05
Bank debt	**18,748,615**	7,601,583	**18,748,615**	7,601,583
Operating costs per boe	**15.56**	16.39	**14.36**	11.36
Operating netbacks per boe	**22.98**	14.31	**19.43**	15.62
Market				
Shares outstanding				
End of period	**65,636,501**	28,015,244	**65,636,501**	28,015,244
Weighted average - basic	**65,205,504**	26,601,305	**56,088,944**	23,531,894
Weighted average - diluted	**66,165,023**	27,817,126	**57,048,463**	24,747,715
Shares trading				
High	**1.88**	1.69	**1.88**	1.92
Low	**1.05**	1.00	**1.38**	0.88
Close	**1.30**	1.40	**1.41**	1.48
Average daily volume	**163,000**	51,600	**137,000**	51,100
OPERATIONS				
Daily production (average)				
Crude oil (bbl)	**1,239**	1,022	**1,284**	758
NGLs (bbl)	**56**	43	**48**	31
Natural gas (mcf)	**2,530**	597	**1,417**	231
Total (boe)[2]	**1,717**	1,165	**1,568**	828
Realized commodity prices ($Cdn.)				
Total crude oil (bbl)	**60.29**	41.19	**51.15**	38.67
NGLs (bbl)	**45.22**	40.78	**44.49**	38.53
Natural gas (mcf)	**5.35**	7.19	**6.44**	7.46
Average (boe)[2]	**52.88**	41.35	**49.06**	38.59
Reference pricing				
WTI (U.S.$/bbl)	**70.74**	53.17	**67.11**	49.84
AECO gas ($Cdn./mcf)	**6.04**	6.99	**7.41**	6.63
Foreign Exchange ($U.S./$Cdn.)	**1.12**	1.24	**1.14**	1.23

[1] Funds from operations before change in non-cash working capital is not a recognized measure under Canadian generally accepted accounting principles. Management uses funds from operations before change in non-cash working capital to analyze performance and considers it a key measure as it demonstrates the Company's ability to generate the cash necessary to fund future capital investments and to repay debt. Funds from operations before change in non-cash working capital has been defined by the Company as net earnings (loss) plus the add back of non-cash items (depletion, depreciation and accretion, stock-based compensation, future income taxes, convertible debenture accretion and unrealized foreign exchange) and excludes the change in non-cash working capital related to operating activities. Arsenal's determination of funds from operations before change in non-cash working capital may not be comparable to that reported by other companies. Arsenal also presents funds from operations before change in non-cash working capital per share whereby amounts per share are calculated using weighted average shares outstanding consistent with the calculation of earnings per share.

[2] The term barrels of oil equivalent ("boe") may be misleading, particularly if used in isolation. A boe conversion ratio of six thousand cubic feet per barrel (6mcf/bbl) of natural gas to barrels of oil equivalence is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead. All boe conversions in the report are derived from converting gas to oil in the ratio mix of six thousand cubic feet of gas to one barrel of oil.

MANAGEMENT'S DISCUSSION AND ANALYSIS

This Management's Discussion and Analysis ("MD&A") for Arsenal Energy Inc. ("Arsenal" or the "Company") should be read in conjunction with the unaudited interim consolidated financial statements for the three and six months ended June 30, 2006 and 2005 and with the audited consolidated financial statements and MD&A for the year ended December 31, 2005. The consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles ("Canadian GAAP") and are presented in Canadian currency except where indicated as being in another currency. Arsenal is an oil and gas issuer and disclosures pertaining to oil and gas activities are presented in accordance with National Instrument 51-101 ("NI 51-101"). For additional disclosures as required under NI 51-101 please refer to www.sedar.com. This MD&A is dated August 2, 2006.

Funds from operations before change in non-cash working capital is not a recognized measure under Canadian generally accepted accounting principles. Management uses funds from operations before change in non-cash working capital to analyze performance and considers it a key measure as it demonstrates the Company's ability to generate the cash necessary to fund future capital investments and to repay debt. Funds from operations before change in non-cash working capital has been defined by the Company as net earnings (loss) plus the addback of non-cash items (depletion, depreciation and accretion, stock-based compensation, convertible debenture accretion, future income taxes and unrealized foreign exchange) and excludes the change in non-cash working capital related to operating activities. Arsenal's determination of funds from operations before change in non-cash working capital may not be comparable to that reported by other companies. Arsenal also presents funds from operations before change in non-cash working capital per share whereby amounts per share are calculated using weighted average shares outstanding consistent with the calculation of earnings per share.

RESULTS OF OPERATIONS

PRODUCTION AND MARKETING

Production volumes for the three and six month periods ended June 30, 2006 increased 47% and 57% respectively over comparable periods in 2005. The increase in volume is attributable to the integration of corporate and property acquisitions and new wells drilled during the year.

With the completion of the Tiverton Petroleums Inc. ("Tiverton") acquisition on March 14, 2006, Arsenal is currently producing approximately 2,000 boe/d. Arsenal is committed to decreasing its exposure to heavy oil, the Tiverton production was gas weighted, reflecting the significant increase in gas as a portion of the Company's production portfolio.

	Three Months Ended June 30			Six Months Ended June 30		
	2006	2005	% Change	**2006**	2005	% Change
Crude Oil (bbl/d)	**1,239**	1,022	21	**1,284**	890	44
NGL (bbl/d)	**56**	43	30	**48**	37	30
Natural gas (mcf/d)	**2,530**	597	324	**1,417**	414	242
Total (boe/d)	**1,717**	1,165	47	**1,568**	996	57
Production split						
Oil & NGLs	**75%**	91%	(18)	**85%**	93%	(9)
Natural Gas	**25%**	9%	187	**15%**	7%	117

COMMODITY PRICES

Commodity price realizations during the three and six month periods ended June 30, 2006 increased 28% and 27% respectively, over comparable periods in 2005. The impact of favourable crude oil prices was partly offset by an 8% decline in the value of the US dollar relative to the Canadian dollar during the year, as well as the impact of the forward contract which expires September 2006.

The increase in commodity price realizations is reflective of the asset portfolio of Arsenal at June 30, 2006, with approximately 60% of its oil production comprised of lower gravity heavy crude oil, compared to more than 75% of corporate production in comparable periods. The heavy oil differential traditionally widens over winter, as demand for heavy crude is highest in the summer. The differential exceeded $25 per barrel for much of the first quarter, and has decreased starting in April reflecting historical seasonality. Arsenal expects the differential to return to the historical average of approximately 75% of WTI for the remainder of summer, and widening to less than 70% of WTI in winter. Arsenal will continue its plan to reduce the effects of this wide heavy oil differential on its cash flows.

The tensions in the Middle East, supply interruptions and increases in world wide demand have resulted in the WTI price reaching record highs. Arsenal anticipates continued high commodity prices particularly in crude oil while inventory issues may continue to partially impact natural gas. It is anticipated that a colder than normal winter in North America could dramatically impact the North American gas price.

($Cdn.)	Three Months Ended June 30			Six Months Ended June 30		
Prices - Before Derivatives	**2006**	2005	% Change	**2006**	2005	% Change
Total crude oil (bbl)	**60.29**	41.19	46	**51.15**	38.67	32
NGLs (bbl)	**45.22**	40.78	11	**44.49**	38.53	15
Natural gas (mcf)	**5.35**	7.19	(26)	**6.44**	7.46	(14)
Total (boe)	**52.88**	41.35	28	**49.06**	38.59	27
Reference Pricing						
WTI ($U.S./bbl)	**70.74**	53.17	33	**67.11**	51.51	30
AECO gas ($Cdn./mcf)	**6.04**	6.99	(14)	**7.41**	6.67	11
NYMEX gas ($U.S./mmbtu)	**6.83**	6.85	(0)	**7.95**	6.58	21
Foreign exchange ($Cdn./$U.S.)	**1.12**	1.24	(10)	**1.14**	1.24	(8)

OIL AND GAS REVENUE

Net oil and gas revenue for the three and six month periods ended June 30, 2006 were 91% and 94% higher respectively, than comparable periods in 2005, reflecting increased petroleum and natural gas production and commodity prices. Revenue per boe for the three and six month periods ended June 30, 2006 increased 30% and 24% respectively, over comparable periods in 2005, as the impact of the hedged production was offset by higher commodity prices.

($Cdn.)	Three Months Ended June 30			Six Months Ended June 30		
	2006	2005	% Change	**2006**	2005	% Change
Crude oil sales	**6.797,251**	3,768,420	80	**11,730,089**	6,295,479	86
NGL sales	**230,447**	158,829	45	**410,021**	314,566	30
Natural gas sales	**1.232,818**	384,448	221	**1,744,068**	493,113	254
Other	**53,818**	93,951	(43)	**115,618**	187,564	(38)
Loss on forward contracts	**(474,525)**	(311,725)	52	**(878,659)**	(542,941)	62
Net oil and gas revenue	**7,839,809**	4,093,923	91	**13,121,137**	6,747,781	94
Per boe	**49.64**	38.21	30	**43.58**	35.29	24

ROYALTIES

Royalties as a percentage of gross oil and gas revenue were consistent with comparable periods in 2005 at 22%. Royalties per boe increased 48% and 26% respectively over comparable periods in 2005, reflecting the changed asset portfolio of the Company, with a greater portion of corporate production coming from higher burden natural gas as a result of the Tiverton acquisition. Arsenal expects the corporate royalty rate to remain at 22% of gross oil and gas revenues for the remainder of the year.

($Cdn.)	Three Months Ended June 30			Six Months Ended June 30		
	2006	2005	% Change	**2006**	2005	% Change
Royalties	**1,752,513**	803,083	118	**2,946,180**	1,402,759	110
% of gross oil and gas revenue	**22**	20	12	**22**	21	7
Per boe	**11.10**	7.49	48	**9.79**	7.78	26

OPERATING COSTS

Operating expenses per boe for the three and six month periods ended June 30, 2006 decreased 5% and 1% respectively over the same periods in 2005. Costs have trended lower from the fourth quarter of 2005, when they averaged $17.54/boe. Operating costs for the second quarter were higher than the first quarter, owing to workovers completed at Galahad and Maidstone. The Tiverton production acquired by Arsenal has historically been less expensive than Arsenal's existing production, reflecting the natural gas weighting of the assets. As the full impact of the Tiverton production is realized, Arsenal expects operating costs per boe to trend lower.

($Cdn.)	Three Months Ended June 30			Six Months Ended June 30		
	2006	2005	% Change	**2006**	2005	% Change
Operating expense	**2,458,159**	1,757,315	40	**4,323,444**	2,622,212	65
Per boe	**15.56**	16.39	(5)	**14.36**	14.55	(1)

PRODUCT NETBACKS[1]

Netbacks for the three and six month periods ended June 30, 2006 increased 61% and 29% respectively, over the comparative periods in 2005. Higher commodity prices were partially offset by increased royalties experienced during 2006.

($Cdn. per boe)	Three Months Ended June 30			Six Months Ended June 30		
	2006	2005	% Change	**2006**	2005	% Change
Net revenue after derivatives	**49.64**	38.19	30	**43.58**	37.43	16
Royalties	**(11.10)**	(7.49)	48	**(9.79)**	(7.78)	26
Operating expenses	**(15.56)**	(16.39)	(5)	**(15.36)**	(14.55)	(1)
Operating netback	**22.98**	14.31	61	**19.43**	15.10	29

GENERAL AND ADMINISTRATIVE EXPENSES

General and administrative costs per boe for the three month period ended June 30, 2006 decreased by 25% over the comparative period in 2005. Included in general and administrative costs for the first quarter is $275,000 relating to employee annual bonuses for 2005, which resulted in general and administrative costs for the six month period ended June 30, 2006 which were 14% greater than the comparable period in 2005. Arsenal anticipates general and administrative costs to increase in absolute terms but decrease on a per barrel basis as the Company continues to grow production.

($Cdn.)	Three Months Ended June 30			Six Months Ended June 30		
	2006	2005	% Change	**2006**	2005	% Change
General and administrative	**1,085,309**	514,955	111	**2,135,932**	1,122,758	90
Per boe	**3.60**	4.80	(25)	**7.09**	6.23	14

FINANCE CHARGES

Finance charges for the three month and six month periods ended June 30, 2006 increased 60% and 25% respectively over the comparative periods in 2005, as the Company drew on its credit facility to fund both drilling and acquisition activities during 2006. Included in finance charges for the second quarter of 2006 is $138,056 in interest relating to interest accrued and paid to the holders of the convertible debentures acquired through the acquisition of Tiverton.

($Cdn.)	Three Months Ended June 30			Six Months Ended June 30		
	2006	2005	% Change	**2006**	2005	% Change
Bank line interest	**300,591**	127,455	136	**378,877**	192,185	97
Convertible debenture interest	**138,056**	–	100	**138,056**	–	100
	438,647	127,455	244	**516,933**	192,185	169
Per boe	**1.90**	1.19	60	**1.26**	1.00	25

DEPLETION, DEPRECIATION, AND ACCRETION

Depletion, depreciation and accretion per boe increased 249% for the three month period ended June 30, 2006 and 166% for the six month period ended June 30, 2006 compared to the same periods in 2005. The increase is attributable to the higher production rates, significantly higher asset base in 2006 compared to 2005, and additional accretion incurred on the asset retirement obligation and convertible debentures.

($Cdn.)	Three Months Ended June 30			Six Months Ended June 30		
	2006	2005	% Change	**2006**	2005	% Change
Depletion, depreciation and accretion	**3,325,793**	647,364	414	**5,148,761**	1,160,987	343
Per boe	**21.06**	6.04	249	**17.10**	6.44	166

TAXES

During second quarter of 2006 Arsenal recovered current income taxes totalling $13,000 compared to $nil during the same period in 2005. Current taxes relate to Canada Large Corporations Tax ("LCT") and Saskatchewan Capital Tax. The recovery is attributable to changes to LCT which will no longer be applicable after January 1, 2007. During the first and second quarters of 2006 Arsenal recovered future income taxes totalling $2,539,997, compared to an expense of $80,905 during the same period in 2005. Of this amount, $1.8 million is attributable to the reduction in the substantially enacted corporate income tax rates for oil and gas producers. A future income tax balance of $14.1 million is recorded as a liability as at June 30, 2006 (June 30, 2005 – $5,676,686).

($Cdn.)	Three Months Ended June 30			Six Months Ended June 30		
	2006	2005	% Change	**2006**	2005	% Change
Current income taxes	**13,000**	–	100	**–**	–	100
Future income taxes (reduction)	**2,300,138**	(44,291)	(5,293)	**2,539,997**	(80,905)	(3,239)
	2,313,138	(44,291)	(5,323)	**2,539,997**	(80,905)	(3,239)
Per boe	**14.65**	(0.41)	(3,643)	**8.44**	(0.42)	(2,094)

SUMMARY OF QUARTERLY RESULTS

The following table highlights the Company's performance for the most recent eight quarters that comprise first and second quarters of 2006, four quarters of 2005, and the last two quarters of 2004. Total revenue is primarily impacted by commodity prices and production volumes. Net income and net income per share are primarily impacted by royalties, operating costs, general and administrative costs, depletion, depreciation and accretion, and future income taxes.

Per share values for the first and second quarters of 2006 and fourth quarter of 2005 are also impacted by the significant increase in shares outstanding, reflecting the Tiverton acquisition and equity issues during the periods.

($Cdn.)	2006		2005				2004	
	Q2	Q1	Q4	Q3	Q2	Q1	Q4	Q3
Total net revenue	**7,839,810**	5,281,327	4,568,443	4,479,544	3,290,840	2,054,182	1,802,339	716,186
Net income (loss)	**787,985**	(848,458)	(611,180)	(200,436)	(157,408)	(156,261)	45,846	(50,832)
Per share - basic	**0.01**	(0.02)	(0.04)	(0.01)	(0.01)	(0.01)	0.00	(0.01)
Per share - diluted	**0.01**	(0.02)	(0.04)	(0.01)	(0.01)	(0.01)	0.00	(0.01)
Funds from operations	**2,167,425**	957,218	1,122,820	1,835,348	871,288	486,573	92,492	119,608
Per share - basic	**0.04**	0.02	0.03	0.06	0.03	0.02	0.01	0.01
Per share - diluted	**0.04**	0.02	0.03	0.06	0.03	0.02	0.01	0.01
Total assets	**118,007,389**	112,189,351	54,157,383	48,955,973	38,308,547	30,978,254	16,690,703	9,777,944
Total bank debt	**18,748,615**	11,128,145	2,496,195	12,443,478	12,668,469	7,601,583	3,743,852	3,700,000
Shares outstanding	**65,636,501**	65,528,875	42,231,244	33,400,567	28,015,244	26,407,303	18,989,706	13,588,667

LIQUIDITY

($Cdn.)	Six Months ended June 30, 2006
Sources	
Funds from operations	3,124,643
Exercise of warrants	59,122
Exercise of options	59,000
Change in non-cash working capital - operating items	(2,994,499)
Change in non-cash working capital - investing items	(452,874)
Total sources of cash	(204,607)
Uses	
Plant, property and equipment additions	(5,818,650)
Share issue costs	(556,546)
Total uses of cash	(6,375,196)
Increase in bank debt	**(6,579,803)**

Bank Debt plus Working Capital Deficit

At June 30, 2006, the Company had $18.7 million outstanding on its credit facility and a working capital surplus, excluding debt of $1.5 million, for total debt plus working capital deficit of $17.2 million, compared to total debt plus working capital deficit of $12.8 million at June 30, 2005. The Company's anticipated funds from operations before change in non-cash working capital is expected to be sufficient to meet the current working capital deficit. The capital intensive nature of the industry will generally result in the Company having a working capital deficit, however, the Company will maintain total debt plus working capital deficit below the Company's credit facility. At June 30, 2006, the Company had a credit facility of $23.0 million.

Convertible Debenture

Arsenal completed the corporate acquisition of Tiverton effective March 14, 2006. A portion of Tiverton's capital structure was comprised of unsecured convertible debentures totalling $3,480,000. Interest accrues on the debentures at 8% on the debentures, payable semi-annually on June 30th and December 31st of each year. The debentures will mature on February 15, 2009 unless called for redemption earlier by Arsenal. After giving effect to the plan of arrangement, the debentures are convertible by the holders at any timer prior to maturity into 1,539,170 shares of the Company, representing a conversion price of $2.26 per Arsenal share.

The Company can elect to prepay the debenture providing the Company's shares trade above $2.60 per share for 22 consecutive days. The convertible debentures are a debt security with an embedded conversion option and were segregated into their debt and equity components based on their respective fair values at the date of acquisition. The $370,000 equity component represents the holder's conversion right and is included in Shareholders' Equity, the remaining balance of $3,110,000 has been classified as debt. If the holder exercises the conversion right, they will receive accrued and unpaid interest up to and including the conversion date.

During the second quarter, Arsenal incurred $60,000 in accretion expense relating to the amortization of the discount of the debenture. In addition, Arsenal accrued and paid $138,056 in interest charges to the debenture holders relating to interest for the first six months of 2006.

Share Capital

The following table outlines the common share issues, warrant and option exercises during the year:

	Common shares
Opening	**42,231,244**
Issued to acquire Tiverton	**23,237,671**
Issued on exercise of warrants	**67,586**
Issued on exercise of options	**100,000**
Shares issued	**65,636,501**
Shares held in escrow	**(325,000)**
Closing	**65,311,501**

CAPITAL RESOURCES

Revolving demand loan

At June 30, 2006, Arsenal has a revolving demand loan for $23.0 million (June 30, 2005 – $12.8 million) with a Canadian financial institution. The facility may be drawn down or repaid at any time and there are no scheduled repayment terms. The facility can be utilized in either Canadian or US dollars, bears interest on Canadian or US bank prime plus 0.25%, increasing to Canadian or US bank prime plus 0.40% if Net Debt to Annualized Cashflow exceeds 1.25:1. The facility is secured by a fixed and floating charge debenture providing a fixed charge over certain petroleum and natural gas interests and a floating charge over all Canadian and U.S. assets.

CAPITAL EXPENDITURES

Capital expenditures for the six month period ended June 30, 2006 totalled $53.5 million. $41.2 million was spent for the acquisition of Tiverton which closed March 14, 2006. Land costs relate to undeveloped lands acquired in northwestern Alberta. Drilling and facility costs were incurred at Armada, Worsley, Evi, Lubicon and Tower Creek.

($ Cdn.)	Total
Corporate, property and land acquisition	**45,441,649**
Seismic	**958,159**
Drilling and completions	**5,810,567**
Production facilities	**1,085,978**
Other	**226,646**
Total capital expenditures	**53,522,999**

COMMITMENTS AND CONTINGENCIES

Arsenal has contractual obligations in the normal course of operations including purchase of assets and services, operating agreements, transportation commitments and sales commitments. These obligations are of a recurring and consistent nature and impact cash flow in an ongoing manner.

Letter of Credit

During the second quarter, Arsenal provided a letter of credit to the Egyptian government for USD $1.6 million. The letter of credit is to be held until April 10, 2010, or until certain performance measures are achieved by Arsenal and its partners. Arsenal has obtained a Performance Security Guarantee ("PSG") from the Canadian government which guarantees Arsenal against the call of the bond by the Egyptian government. There is no impact to the existing credit facility of Arsenal from providing the letter of credit due to the PSG, however the company incurred approximately $50,000 in stamping fees to obtain the PSG.

Flow Through Shares

At June 30, 2006, the Company has approximately $3.0 million of qualifying expenditures pursuant to flow through share financings completed in 2005.

RISK MANAGEMENT

Business risks affecting Arsenal are unchanged from those disclosed in the MD&A dated March 21, 2006 prepared in conjunction with the December 31, 2005 and 2004 financial statements.

SIGNIFICANT ACCOUNTING POLICIES AND ESTIMATES

The interim consolidated financial statements dated June 30, 2006 have been prepared following the same accounting policies and methods of computation as the consolidated financial statements for the fiscal year ended December 31, 2005.

FINANCIAL REPORTING UPDATE

COMPREHENSIVE INCOME

The CICA has issued Section 1530 "Comprehensive Income" which establishes standards for reporting and display of comprehensive income. This Section is effective for annual and interim periods beginning on or after October 1, 2006 with early adoption permitted for fiscal year ending on or after December 31, 2004. Arsenal has assessed that this guideline is unlikely to have a material effect on the financial statements and does not anticipate adopting the standard until October 2006.

OUTLOOK

STRATEGY

Arsenal's domestic production and cashflow has increased significantly over the past two years. The Company anticipates continued growth domestically both through the drill-bit and accretive acquisitions. The addition of a new Vice President of Exploration has already begun to provide results for shareholders.

The Company remains committed to utilizing a portion of cashflows earned domestically to fund high impact international opportunities like the Nuqra concession in Egypt. The Company continues to search for other international opportunities with the following profile:

- Stable Government and Operating Environment
- Significant upside relative to capital exposure
- Experienced and established international operator
- Considerable land acreage
- Pre-existing seismic or geological data establishing existence of source and reservoir rock.

Egypt

The 800 km seismic acquisition and processing was completed in Second quarter 2006. This data was included in the interpretation resulting from the reprocessing of the 3,200 km of seismic previously acquired over the concession. This combination of processed and interpreted data has confirmed several locations which we have high graded to allow us to select the first two drilling locations. We have identified an available rig and are in the process of negotiating a drilling contract. These first two wells are scheduled to be drilled in the fourth quarter of 2006, or first quarter of 2007.

North America

Arsenal emphasises a full-cycle approach to its business and plans to continue with internal development opportunities as a means to enhancing its production base and creating value for shareholders. Consistent with its full-cycle approach, Arsenal actively added to its undeveloped land position through crown land sales during 2005 and 2006 in order to establish high-quality drilling prospects. The Company also commenced an active evaluation of the seismic obtained in the Tiverton acquisition and has already identified several drilling opportunities on its existing land base and on open crown lands.

The Company will continue to pursue acquisitions that will be accretive on a per share basis to cash flow, production, reserves and net asset value. One of the key components of the Tiverton acquisition is the existence of a high quality drilling inventory which Arsenal intends to quickly develop during this year. Arsenal believes that over the long term, outlook for both crude oil and natural gas pricing remains strong.

SENSITIVITIES

The following table provides estimates for 2006 of the sensitivity of the Company's 2006 net income and cash flow to changes in commodity prices and the U.S./Cdn. Dollar exchange rate:

Variable	Change	Cash Flow
Crude oil price	$U.S. 1/bbl	$ 350,000
Natural gas price	$Cdn. 0.10/mcf	$ 50,000
$U.S./$Cdn. exchange rate	0.01	$ 50,000
Interest rate	1.00%	$ 60,000
Crude oil production	100 bbl/d	$ 750,000
Natural gas production	100 mcf/d	$ 125,000

[1] Funds from operations before change in non-cash working capital is not a recognized measure under Canadian generally accepted accounting principles. Management uses funds from operations before change in non-cash working capital to analyze performance and considers it a key measure as it demonstrates the Company's ability to generate the cash necessary to fund future capital investments and to repay debt. Funds from operations before change in non-cash working capital has been defined by the Company as net earnings (loss) plus the add back of non-cash items (depletion, depreciation and accretion, stock-based compensation, future income taxes, convertible debenture accretion and unrealized foreign exchange) and excludes the change in non-cash working capital related to operating activities. Arsenal's determination of funds from operations before change in non-cash working capital may not be comparable to that reported by other companies. Arsenal also presents funds from operations before change in non-cash working capital per share whereby amounts per share are calculated using weighted average shares outstanding consistent with the calculation of earnings per share.

INTERIM CONSOLIDATED BALANCE SHEETS
(UNAUDITED)

As at	**June 30, 2006**	December 31, 2005
ASSETS		
Current assets		
Accounts receivable	**7,705,165**	4,583,927
Reclamation bonds	**195,026**	203,291
Property, plant and equipment	**91,743,207**	44,578,604
Goodwill	**18,363,990**	4,791,561
	118,007,389	54,157,383
LIABILITIES		
Current liabilities		
Accounts payable and accrued liabilities	**6,039,443**	6,365,577
Revolving demand loan (note 3)	**18,748,615**	2,496,195
Deferred revenue	**28,680**	287,533
	24,816,738	9,149,305
Convertible debentures (note 8)	**3,242,473**	–
Future income tax (note 12)	**14,088,847**	7,509,044
Asset retirement obligations (note 4)	**2,434,092**	1,295,500
	44,582,150	17,953,849
SHAREHOLDERS' EQUITY		
Common shares (note 5)	**72,878,630**	36,514,809
Warrants (note 6)	**303,731**	303,731
Contributed surplus (note 7)	**1,718,800**	1,170,444
Common share conversion rights (note 8)	**370,000**	–
Deficit	**(1,845,922)**	(1,785,450)
	73,425,239	36,203,534
	118,007,389	54,157,383

Segmented information (note 10)
Commitments (note 11)

See accompanying notes to the interim financial statements.

INTERIM CONSOLIDATED STATEMENTS OF OPERTIONS AND DEFICIT
(UNAUDITED)

	Three Months Ended June 30		Six Months Ended June 30	
	2006	2005	**2006**	2005
REVENUE				
Oil and gas	**7,839,810**	4,093,923	**13,121,137**	6,767,781
Royalties	**(1,752,513)**	(803,083)	**(2,946,180)**	(1,402,759)
	6,087,297	3,290,840	**10,174,957**	5,345,022
EXPENSES				
Operating	**2,458,159**	1,757,315	**4,323,444**	2,622,212
General and administrative	**1,085,309**	549,868	**2,135,932**	1,195,206
Finance charges	**438,647**	127,455	**516,933**	192,185
Convertible debenture accretion	**60,000**	–	**60,000**	–
Depletion, depreciation and accretion	**3,325,793**	647,364	**5,148,761**	1,160,987
Stock-based compensation (note 7)	**244,541**	321,955	**590,356**	407,196
	7,612,450	3,403,957	**12,775,426**	5,577,786
Loss before income taxes	**(1,525,153)**	(113,117)	**(2,600,469)**	(232,764)
Income taxes				
Current tax (expense) reduction	**13,000**	–	**–**	–
Future income tax (expense) reduction (note 12)	**2,300,138**	(44,291)	**2,539,997**	(80,905)
	2,313,138	(44,291)	**2,539,997**	(80,905)
Net income (loss)	**787,985**	(157,408)	**(60,472)**	(313,669)
Deficit - beginning of period	**(2,633,908)**	(841,287)	**(1,785,450)**	(685,026)
Deficit - end of period	**(1,845,922)**	(998,695)	**(1,845,922)**	(998,695)
Income (loss) per share - basic and diluted	**$ 0.01**	$ (0.01)	**$ (0.00)**	$ (0.02)

Segmented information (note 10)

INTERIM CONSOLIDATED STATEMENT OF CASH FLOWS
(UNAUDITED)

	Three Months Ended June 30		Six Months Ended June 30	
	2006	2005	**2006**	2005
Cash flows from operating activities				
Net income (loss)	**787,985**	(157,408)	**(60,472)**	(313,669)
Items not affecting cash				
Depletion, depreciation and accretion	**3,325,793**	647,364	**5,148,761**	1,160,987
Convertible debenture accretion	**60,000**	–	**60,000**	–
Future income taxes (reduction)	**(2,300,138)**	44,291)	**(2,539,997)**	80,905
Stock-based compensation expense (note 7)	**244,541**	321,955	**590,356**	407,196
Deferred revnue	**(135,604)**	(19,827)	**(258,853)**	(50,006)
Unrealized foreign exchange loss	**184,848**	34,913	**184,848**	72,448
	2,167,425	871,288	**3,124,643**	1,357,861
Net change in non-cash working capital (note 9)	**(932,489)**	(1,363,332)	**(2,994,499)**	(1,849,129)
Net cash provided by (used in) operating activities	**1,234,937**	(492,044)	**130,145**	(491,268)
Cash flows from investing activities				
Corporate and property acquisitions (note 2)	**–**	(5,500,000)	**–**	(5,500,000)
Additions to property, plant and equipment	**(3,537,385)**	(1,709,391)	**(5,818,650)**	(8,755,924)
Changes in non-cash working capital (note 9)	**504,989**	25,908	**(452,874)**	68,482
Net cash provided by (used in) investing activities	**(3,032,396)**	(7,183,483)	**(6,271,524)**	(14,187,442)
Cash flows from financing activities				
Issues of shares for cash	**–**	1,672,510	**–**	1,672,510
Issue of shares upon exercise of warrants	**–**	946,418	**59,122**	3,855,750
Issue of shares for cash upon exercise of stock options	**59,000**	–	**59,000**	193,784
Share issue costs	**90,606**	(10,287)	**(566,546)**	(185,014)
Revolving demand loan	**1,647,853**	5,066,886	**6,579,803**	8,924,617
Net cash provided by (used in) financing activities	**1,797,459**	7,675,527	**6,141,379**	14,461,647
Change in cash during the period	**–**	–	**–**	(217,063)
Cash - Beginning of period	**–**	–	**–**	217,063
Cash - End of period	**–**	–	**–**	–

Supplemental information (note 9)

NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

1. SIGNIFICANT ACCOUNTING POLICIES

The interim consolidated financial statements of Arsenal Energy Inc. ("Arsenal" or the "Company") have been prepared by management in accordance with accounting principles generally accepted in Canada. The interim consolidated financial statements have been prepared following the same accounting policies and methods of computation as the consolidated financial statements for the fiscal year ended December 31, 2005. The disclosures provided below are incremental to those included with the annual consolidated financial statements. The interim consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto in Arsenal's annual report for the year ended December 31, 2005.

2. BUSINESS ACQUISITION

On March 14, 2006 Arsenal acquired all of the issued and outstanding securities of Tiverton Petroleums Ltd. ("Tiverton"). On March 31, 2005 Arsenal acquired all of the issued and outstanding of IC Energy Inc. ("IC Energy"). The purchase method of accounting was used for both business combinations and the allocation of the purchase price and consideration for each acquisition is as follows:

	Tiverton 2006	IC Energy 2006
Net assets acquired at assigned values:		
Working capital deficiency	**(2,085,000)**	–
Property, plant and equipment	**42,740,000**	10,243,000
Goodwill	**13,572,428**	2,665,198
Bank debt	**(3,700,000)**	–
Convertible debentures	**(3,182,473)**	–
Asset retirement obligation	**(1,095,000)**	(123,713)
Future income taxes	**(6,937,798)**	(2,784,485)
Common share conversion rights	**(370,000)**	–
Net assets acquired	**38,942,157**	10,000,000
Financed by:		
Shares issued	**38,342,157**	4,500,000
Cash	**–**	5,500,000
Acquisition costs	**600,000**	–
Purchase price	**38,942,157**	10,000,000

The above amounts are estimates made by management based on currently available information. Amendments may be made to the purchase allocations as the cost estimates and tax balances are finalized.

3. REVOLVING DEMAND LOAN

At June 30, 2006, the Company has available a demand operating loan in the amount of $23.0 million (December 31, 2005 - $14.2 million). The facility can be utilized in either Canadian or US dollars, bears interest on Canadian or US bank prime plus 0.25%, increasing to Canadian or US bank prime plus 0.40% if Net Debt to Annualized Cashflow exceeds 1.25:1. The facility is secured by a fixed and floating charge debenture providing a fixed charge over certain petroleum and natural gas interests and a floating charge over all Canadian and U.S. assets.

4. ASSET RETIREMENT OBLIGATIONS

The following table presents the beginning and ending aggregate asset retirement obligations associated with the retirement of oil and gas properties:

	Six Months Ended June 30, 2006	Year Ended December 31, 2005
Asset retirement obligations - beginning of period	**1,295,500**	780,889
Liabilities acquired (note 2)	**1,095,000**	334,119
Liabilities incurred	**40,500**	114,808
Change in estimate	**(50,908)**	(14,022)
Accretion expense	**54,000**	79,706
Asset retirement obligations - end of period	**2,434,092**	1,295,000

5. COMMON SHARES

	Six Months Ended June 30, 2006		Year Ended December 31, 005	
	Shares	**Amount ($)**	Shares	Amount ($)
Balance - beginning of period	**42,231,244**	**36,514,809**	18,989,706	7,458,134
Issued to acquire Tiverton	**23,237,671**	**38,942,157**	–	–
Issued to acquire IC Energy	–	–	3,000,000	4,500,000
Issued to acquire Quadra	–	–	4,088,292	5,483,014
Issued for cash	–	–	8,760,496	13,573,157
Cost of shares issued	–	**(556,546)**	–	(723,785)
Tax effect of flow-through shares	–	**(2,369,913)**	–	(1,445,169)
Tax effect of share issue costs	–	**188,000**	–	247,000
Issued on exercise of options	**100,000**	**59,000**	972,025	207,334
Issued on exercise of warrants	**67,586**	**59,122**	6,745,725	6,133,159
Allocated from contributed surplus	–	**42,000**	–	93,205
Allocated from warrants	–	–	–	988,760
Shares issued	**65,636,501**	**72,878,630**	42,556,244	36,514,809
Shares held in escrow	**(325,000)**	–	(325,000)	–
Balance - end of period	**65,311,501**	**72,878,630**	42,231,244	36,514,809

The per share calculations for the six month period ended June 30, 2006 were based on weighted average shares outstanding of 56,088,944 (June 30, 2005 – 23,531,894). The per share calculations for the three month period ended June 30, 2006 were based on weighted average shares outstanding of 65,205,504 (June 30, 2005 – 26,601,305). In computing net loss per share – diluted, 959,519 shares (June 30, 2005 – 1,215,821) were added to the weighted average number of shares outstanding for the three month period, reflecting the dilutive effect of stock options and share purchase warrants.

6. WARRANTS

When share purchase warrants are exercised, the consideration paid is recorded to the shareholders' equity account along with an allocation for the deemed value of the warrants previously recognized in the warrants account. The following table details the changes in the warrant account balance:

	Six Months Ended June 30, 2006		Year Ended December 31, 005	
	Warrants	Amount ($)	Warrants	Amount ($)
Balance - beginning of period	**2,031,100**	**303,731**	6,588,664	988,760
Private placement	–	–	2,031,100	303,731
Agents' warrants (1)	**67,586**	–	157,061	–
Allocated to common equity upon exercise of warrants	**(67,586)**	–	(6,745,725)	(988,760)
Balance - end of period	**2,031,100**	**303,731**	2,031,100	303,731

(1) During 2006 the Company's underwriters and agents exercised their right to an additional 67,586 warrants pursuant to their respective agency agreements relating to equity offerings completed in 2004 and 2005.

7. STOCK OPTIONS

A summary of the changes in the options outstanding under the Option Plan is as follows:

	Six Months Ended June 30, 2006		Year Ended December 31, 2005	
	Options	Weighted Average Price ($)	Options	Weighted Average Price ($)
Balance - beginning of period	**3,592,252**	**0.99**	2,505,000	0.40
Granted	**760,000**	**1.14**	2,495,000	1.24
Exercised	**(100,000)**	**0.59**	(972,025)	0.23
Cancelled	**(125,000)**	**1.23**	(435,723)	0.59
Balance - end of period	**4,127,252**	**1.02**	3,592,252	0.99
Exercisable - end of period	**2,627,252**	**0.93**	1,977,259	0.90

The Company incurred non-cash compensation expense of $590,356 for the six month period ended June 30, 2006 (2005 – $407,196) related to vested options issued under the Option Plan with a corresponding increase to contributed surplus. When options are exercised by employees, contractors and directors of the Company, the consideration paid is recorded to the shareholders' equity account along with related non-cash compensation expense previously recognized in contributed surplus. The following table reconciles the movement in the contributed surplus balance:

	Six Months Ended June 30, 2006	Year Ended December 31, 2005
Balance - beginning of period	**1,170,444**	144,183
Issuance of stock options	**590,356**	1,119,466
Reclassification to common shares on exercise of options	**(42,000)**	(93,205)
Balance - end of period	**1,718,800**	1,170,444

8. CONVERTIBLE DEBENTURE

As outlined in Note 2, Arsenal completed the corporate acquisition of Tiverton effective March 14, 2006. A portion of Tiverton's capital structure was comprised of unsecured convertible debentures totalling $3,480,000. Interest accrues on the debentures at 8% on the debentures, payable semi-annually on June 30th and December 31st of each year. The debentures will mature on February 15, 2009 unless called for redemption earlier by Arsenal. After giving effect to the plan of arrangement, the debentures are convertible by the holders at any time prior to maturity into 1,539,170 shares of the Company, representing a conversion price of $2.26 per Arsenal share.

The Company can elect to prepay the debenture providing the Company's shares trade above $2.60 per share for 22 consecutive days. Interest is payable semi-annually on June 30th and December 31st of each year. The convertible debentures are a debt security with an embedded conversion option and were segregated into their debt and equity components based on their respective fair values at the date of acquisition. The $370,000 equity component represents the holderís conversion right and is included in Shareholders' Equity, the remaining balance of $3,242,473 has been classified as debt. If the holder exercises the conversion right, they will receive accrued and unpaid interest up to and including the conversion date.

9. SUPPLEMENTAL CASH FLOW INFORMATION

	Three Months Ended June 30, 2006	Three Months Ended June 30, 2005	**Six Months Ended June 30, 2006**	Six Months Ended June 30, 2005
Change in non-cash working capital items				
Operating accounts receivable	**(1,476,926)**	(693,020)	**(3,121,239)**	(1,312,964)
Operating accounts payable	**544,438**	(670,312)	**126,740**	(536,165)
Amounts relating to operating activities	**(932,488)**	(1,363,332)	**(2,994,499)**	(1,849,129)
Amounts relating to investing activities	**504,989**	25,908	**(452,874)**	68,482
	(427,499)	(1,337,424)	**(3,447,373)**	(1,780,647)
Taxes paid	**–**	–	**213,985**	–
Interest paid	**372,107**	105,476	**450,393**	170,026

10. SEGMENTED INFORMATION

A significant portion of the Company's assets and revenues are earned in the United States and Egypt and are monitored as identifiable reporting segments by management. The remaining assets and associated revenues are earned in Canada by Arsenal Energy Inc. The following table outlines key operating results by entity:

		2006		
($ Cdn.)	**Canada**	**U.S.**	**Egypt**	**Total**
Oil and gas revenue	**9,239,452**	**3,881,685**	**–**	**13,121,137**
Net income (loss) before income taxes	**(2,532,537)**	**52,304**	**(120,236)**	**(2,600,469)**
Property, plant and equipment	**82,080,509**	**4,302,464**	**5,360,234**	**91,743,207**
Capital expenditures (including acquisitions)	**5,720,497**	**98,153**	**–**	**5,818,650**

		2005		
($ Cdn.)	Canada	U.S.	Egypt	Total
Oil and gas revenue	3,312,548	3,535,233	–	6,847,781
Net income (loss) before income taxes	(944,631)	630,962	–	(313,669)
Property, plant and equipment	1,243,003	1,479,807	–	2,722,810
Capital expenditures (including acquisition)	14,264,174	–	–	14,264,174

11. COMMITMENTS

Letter of Credit

During the second quarter, Arsenal provided a letter of credit to the Egyptian government for USD $1.6 million. The letter of credit is to be held until April 10, 2010, or until certain performance measures are achieved by Arsenal and its partners. Arsenal has obtained a Performance Security Guarantee (“PSG”) from the Canadian government which guarantees Arsenal against the call of the bond by the Egyptian government. There is no impact to the existing credit facility of Arsenal from providing the letter of credit due to the PSG, however the Company incurred approximately $50,000 in stamping fees to obtain the PSG.

Flow Through Shares

At June 30, 2006, the Company has approximately $3.0 million of qualifying expenditures pursuant to flow through share financings completed in 2005.

12. FUTURE INCOME TAXES

During the second quarter, the Company reduced its future income tax liability by $2.3 million. Of this amount, approximately $1.8 million of the reduction related to a change in the substantially enacted corporate tax rates for Canadian oil and gas producers.

NOTES

Corporate Information

Officers and Management

Errol Stewart
President and Chief Executive Officer

Jesse Meidl CA (4)
Chief Financial Officer

Bernie Dumanowski P. Eng.
Vice President Operations

Tony VanWinkoop
Vice President Exploration

Exchange Listings
Toronto Stock Exchange: AEI
Frankfurt Stock Exchange: A1E

Legal Counsel
Borden Ladner Gervais LLP

Auditors
KPMG LLP

Bankers
ATB Financial

Evaluation Engineers
AJM Petroleum Consultants

Registrar and Transfer Agent
Computer Share Trust
Company of Canada

Privacy Officer
Jesse Meidl CA
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Board of Directors

Michael Vandale

William Hews (1) (3)

Errol Stewart (2) (4)

Greg Belzberg (1)

R. Neil MacKay (2) (4)

Alain Gaucher (1) (4)

Curtis Stewart (2) (3)

Donald Edwards (4)
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Committees of the Board of Directors
(1) Audit Committee member
(2) Reserves Committee member
(3) Compensation Committee member
(4) Disclosure Committee member

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