Regal Energy Ltd.

# 2008 First Quarter Report to the Shareholders of Regal Energy Ltd.

Regal Energy Ltd. ("Regal" or the "Corporation") announces its financial (unaudited) and operating results for the first quarter ended December 31, 2007.

| (unaudited) | Three Months ended December 31, 2007 | 2006 |
|---|---|---|
| **Financial** | | |
| Petroleum and natural gas sales | $ 691,631 | $ 456,790 |
| Funds flow from operations (non-GAAP) (1) | $ (61,680) | $ (68,461) |
| Cash flow from operations | $ 198,415 | $ (182,530) |
| Net earnings (loss) | $ (498,142) | $ (356,635) |
| Capital expenditures (2) | $ 1,389,589 | $ 3,743,911 |
| Working capital surplus (deficiency) | $ (3,836,298) | $ (2,826,938) |
| Total assets | $ 13,519,502 | $ 14,028,534 |
| Shareholders' equity | $ 7,910,239 | $ 9,177,528 |
| | | |
| Shares outstanding as of February 29, 2008 | 48,137,590 | |
| Shares issuable for warrants as of February 29, 2008 | 5,100,167 | |
| Stock options outstanding as of February 29, 2008 | 2,865,000 | |
| **Operations** | | |
| Production | | |
| Natural gas (Mcf) | 78,166 | 52,969 |
| Oil and NGLs (Bbls) | 3,528 | 2,554 |
| Total production (Boe) (3) | 16,556 | 11,382 |
| | | |
| Natural gas (Mcf/d) | 850 | 576 |
| Oil and NGLs (Bbl/d) | 38 | 28 |
| Total production (Boe/d) (3) | 180 | 124 |
| | | |
| Average selling price | | |
| Natural gas ($/Mcf) | $5.64 | $6.10 |
| Oil and NGLs ($/Bbl) | $71.14 | $52.36 |
| Total production ($/Boe) (3) | $41.78 | $40.13 |
| | | |
| Operating Netback ($/Boe) (3) (4) | $12.59 | $13.75 |

*Notes:*

*(1) Funds flow before net change in non-cash operating working capital balances does not conform to Generally Accepted Accounting Principles (GAAP). Refer to the "Non-GAAP Measurements" and "Net Earnings, Funds Flow and Cash Flow from Operations" sections of the Management's Discussion and Analysis.*

*(2) Amounts reported do not include non-cash capital recorded for asset retirement obligations and is net of dispositions.*

*(3) Natural gas is converted to oil equivalent at 6 Mcf = 1 Bbl. A Boe conversion ratio of 6 Mcf = 1 Bbl is based on an energy equivalency conversion method and does not represent a value equivalency at the wellhead; therefore Boe's may be misleading if used in isolation.*

*(4) Non-GAAP Measurement. Refer to the "Non-GAAP Measurements" section of th e Management's Discussion and Analysis.*

## 2008 First Quarter Report to the Shareholders of Regal Energy Ltd.

### Profile

**Regal Energy Ltd. ("Regal" or "the Corporation") is an emerging Canadian energy company engaged in the exploration, acquisition, development and production of crude oil and natural gas in Alberta and northeast British Columbia. Regal's common shares are listed and posted for trading on the TSX Venture Exchange under the symbol "REG".**

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### Abbreviations

| | |
|---|---|
| **$M** | **thousands of dollars** |
| **ARTC** | **Alberta Royalty Tax Credit** |
| **Bbls** | **barrels** |
| **Boe** | **barrels of oil equivalent (1)** |
| **Boe/d** | **barrels of oil equivalent per day** |
| **Bbl** | **barrels of oil & NGLs** |
| **Bbl/d** | **barrels of oil per day** |
| **MBbls** | **thousand barrels** |
| **MBoe** | **thousand barrels of oil equivalent (1)** |
| **Mcf** | **thousand cubic feet** |
| **Mcf/d** | **thousand cubic feet per day** |
| **MMBTU** | **million British Thermal Units** |
| **MMcf** | **million cubic feet** |
| **MStb** | **thousand stock tank barrels** |
| **NGLs** | **natural gas liquids** |

Note: (1) Natural gas is equated to oil on the basis
of 6 Mcf of natural gas = 1 barrel of oil equivalent (Boe)

## President's Report to Shareholders

During the first quarter of fiscal 2008, Regal drilled its first option location at Eight Mile, British Columbia to the south of the 7-8-81-17 W6M well (the "7-8 well"), with a view towards delineating the aerial extent of its new Doig gas pool discovery. The 14-5-81-17 W6M well (the "14-5 well") was drilled, cased and completed in the Doig zone during the month of December 2007. After fracture stimulation the final test rate was 250 Mcf/d gas, 38 Bbls/d of condensate and 69 Bbls/d of formation water. The information gathered from the 14-5 well will be incorporated into any potential future development drilling locations. As a result of drilling the 14-5 well, Regal earned an interest in two additional sections of land and each subsequent option well drilled will earn an interest in two sections of land.

The operator of the Eight Mile, BC area recently commenced work to construct a pipeline to tie-in the property to a compression and dehydration facility at 9-28-81-17 W6M with a projected production startup date of April 1, 2008. Further work is anticipated to be conducted within the area of mutual interest during 2008, including the acquisition of 3D seismic and exploratory and development drilling.

During the first quarter, Regal tied-in two natural gas wells (1.1 net) at Garrington and one natural gas well (0.34 net) at Pica. The Pica well averaged approximately 400 Mcf/d (136 Mcf/d net) over a 17 day period in December and then experienced water production problems and was subsequently shut-in. The well is not capable of further economic production.

Regal exited the first quarter of 2008 with higher than expected debt and working capital deficiency as a result of cost overruns on several capital projects, increased abandonment and reclamation costs, higher operating costs as a result of workovers conducted at its Veteran oil property and start-up costs for new production at Garrington and increased G&A costs. This debt and working capital deficiency level is expected to be reduced by the sale of certain minor property interests at Garrington, the sale of surplus production equipment at Atlee Buffalo, a reduction in discretionary capital expenditures and the sale of additional equity. Anticipated gas and NGLs production from the Eight Mile BC property combined with firmer forecasted spot prices for natural gas are expected to make a positive contribution to funds flow and provide Regal with increased financial flexibility.

I am pleased to announce that Greg Glenn has been promoted to the position of Vice President Land. Greg has over 30 years of continuous service in the industry and over the past several years has made a significant contribution towards developing and maintaining a strong land position for Regal in Alberta and northeast BC.

On behalf of the Board of Directors

**DOUGLAS O. McNICHOL**

President and Chief Executive Officer

February 29, 2008

## MANAGEMENT'S DISCUSSION AND ANALYSIS

*The following is management's discussion and analysis ("MD&A") of Regal Energy Ltd.'s ("Regal" or "the Corporation") unaudited operating and financial results for the three months ended December 31, 2007. This MD&A should be read in conjunction with Regal's unaudited interim financial statements and related notes for the three months ended December 31, 2007 and the Audited Financial Statements for the year ended September 30, 2007. This MD&A is current as at February 29, 2008. The accompanying financial statements of Regal have been prepared by Management and approved by the Corporation's Audit Committee and Board of Directors. The financial data presented herein has been prepared in accordance with Canadian generally accepted accounting principles ("GAAP"). Additional information relating to Regal is available on SEDAR at www.sedar.com and Regal's website (www.regalenergy.ca).*

## NON-GAAP FINANCIAL MEASUREMENTS

The Corporation has used certain measures of financial reporting that are commonly used benchmarks within the oil and natural gas industry in this MD&A that are considered to be non-GAAP measures. The measures discussed are widely accepted measures of performance and value within the industry, and are used by investors and analysts to compare and evaluate oil and gas exploration and producing entities. The non-GAAP measures used and referenced in this document include "operating netback" and "funds flow from operations". Operating netback is a benchmark used in the oil and gas industry to measure the contribution of crude oil and natural gas sales after deducting royalties and operating costs. Regal determines funds flow from operations to be the cash flow from operations before changes in non-cash working capital. Management believes that in addition to net earnings, funds flow from operations is a useful supplemental measure to assess the financial performance and ability of Regal to finance future spending. These measures are not defined under GAAP and should not be considered in isolation or as an alternative to conventional GAAP measures. These non-GAAP measures may not necessarily be comparable to similarly titled measures used by other entities and readers of this MD&A are cautioned in attempting to make such comparisons.

## OTHER MEASUREMENTS

The reporting and measurement currency of this MD&A is the Canadian dollar. For the purposes of calculating unit costs, natural gas has been converted to a barrel of oil equivalent (Boe) using 6,000 cubic feet (6 Mcf) of natural gas equal to one barrel of oil (6:1), unless otherwise stated. The Boe conversion ratio of 6 Mcf to 1 Bbl is based on an energy equivalency conversion method and does not represent a value equivalency; therefore Boe's may be misleading if used in isolation. (This conversion conforms to NI 51-101). References to natural gas liquids ("NGLs") in this MD&A include condensate, propane, butane and ethane and one barrel of NGLs is considered to be equivalent to one barrel of crude oil equivalent (Boe).

## ADVISORY REGARDING FORWARD LOOKING STATEMENTS

Certain information set forth in this MD&A, that are not historical facts, including Management's assessment of Regal's future plans and operations, contains "forward looking statements". All estimates and statements that describe the Corporation's objectives, goals, or future, including Management's assessment of future plans and operations, production estimates and expected production rates, timing of tie-ins and the effect of delays in tieing-in wells and the effects of third party compressor issues and other infrastructure issues, levels of decline rates and the effects thereof, expected royalty rates, expected general and administrative expenses and other expenses, effects of the results of successful wells, expected levels of capital expenditures and the method of funding them, the ability to incur qualifying expenditures renounceable to purchasers of flow-through shares and the expected levels of activities and results of operations of Regal may constitute forward looking information under securities laws and necessarily involve risks including, without limitation, risks associated with oil and gas exploration, development, exploitation, production, marketing and transportation, loss of markets, volatility of commodity prices, currency fluctuations, imprecision of reserve estimates, environmental risks, competition from other producers, inability to retain drilling rigs and other services, incorrect assessment of the value of acquisitions, failure to realize the anticipated benefits of acquisitions, delays resulting from or inability to obtain required regulatory approvals, the impact of general economic conditions and industry conditions, the lack of availability of qualified personnel or management, stock market volatility and the ability to access sufficient capital from internal and external sources. As a consequence Regal's actual results, performance or achievements could differ materially from those expressed in, or implied by, these forward looking statements and, accordingly no assurance can be given that any events anticipated by the forward looking statements will transpire or occur, or, if any of them do so, what benefits Regal will derive there from. Readers are cautioned that the foregoing list of factors is not exhaustive. Additional information on these and other factors that could affect Regal's operations and financial results are included in reports on file with Canadian securities regulatory authorities and may be accessed through the SEDAR website (www.sedar.com) and Regal's website (www.regalenergy.ca). Readers are cautioned that the assumptions used in the preparation of such information, although considered reasonable at the time of preparation, may prove to be imprecise and, as such, undue reliance should not be placed on forward looking statements. Furthermore, the forward looking statements contained in this MD&A are made as at the date of this MD&A and Regal does not undertake any obligation to update publicly or to revise any of the included forward looking statements, whether as a result of new information, future events or otherwise, except as may be required by applicable securities laws.

## THE CORPORATION

The Corporation was incorporated pursuant to the Canada Business Corporations Act on August 7, 1998 as "3519309 Canada Incorporated". On September 28, 2002, 3519309 Canada Incorporated amalgamated to form SiberCore Technologies Incorporated. The Corporation at that time was a semiconductor company developing high value-added standard chips for intelligent hardware based switching and routing platforms.

The shareholders of the Corporation approved a change of business direction on December 17, 2004 that resulted in the distribution of cash and technology assets to shareholders as a return of capital, the consolidation of the common shares of the Corporation on the basis of 1 for 30,000, conversion of the preferred shares of the Corporation on the basis of 0.012 common shares for each preferred share, and a change in the name of the Corporation from SiberCore Technologies Incorporated to Azeri Capital Inc. ("Azeri").

On December 30, 2004 the Corporation entered into a seismic joint venture agreement (the "Seismic JV") with Divestco Seismic Limited Partnership ("Divestco") and Spectrum Seismic Processors Ltd. The seismic underlying the Seismic JV is the majority of the proprietary seismic data of a senior Canadian integrated oil and gas company which consists of over 32,000 km of 2D data covering several areas throughout Alberta and Saskatchewan that was acquired by Divestco. Pursuant to the Joint Venture, the Corporation agreed to fund the estimated cost of reprocessing the seismic data of $1,375,000, and in exchange, the Corporation acquired for its own use a fully reprocessed copy of this seismic data as well as certain other geological and geophysical software usage, and a residual royalty on sales of the entire reprocessed database and individual line by line data sales. On November 9, 2006, this residual royalty was sold for $675,000.

On December 31, 2005, the Corporation acquired, by way of a Plan of Arrangement, all of the issued and outstanding shares of Regal Energy Corp., a public company listed on the TSX Venture Exchange, and changed the Corporation's name to Regal Energy Ltd. (the "Plan of Arrangement"). Pursuant to the Plan of Arrangement, the Corporation reorganized its share capital whereby the issued and issuable shares were split on a 7.37 for one basis. Shareholders of Regal Energy Corp. received one share of the Corporation for each five shares of Regal Energy Corp. previously held.

The Corporation was continued under the *Business Corporations Act.* (Alberta) on December 31, 2005.

The principal and head office of the Corporation is located at Suite 1520, Life Plaza 734 - 7th Avenue S.W., Calgary, Alberta T2P 3P8. The registered office of the Corporation is located at Suite 1600, Dome Tower, 333 - 7th Avenue S.W., Calgary, Alberta T2P 2Z1.

The Corporation has no subsidiaries.

Regal Energy Ltd.'s common shares are listed and posted for trading on the TSX Venture Exchange under the symbol REG.

## RESULTS OF OPERATIONS

### Highlights

During the first quarter of fiscal 2008, capital expenditures totaled $1.4 million, including $0.8 million for drilling and completions and $0.5 million for equipping and tie-in. During the quarter, there were three major operations underway: the drilling of our third well at Eight Mile in northeast British Columbia at 14-5-81-17 W6M (the "14-5 well"), the construction of a pipeline to tie in the 14-27-38-5 W5M well at Garrington and the tie in of the 13-6-84-5 W6M well at Pica.

The 14-5 well at Eight Mile was drilled, cased and completed in the Doig zone during the month of December 2007. After fracture stimulation the final test rate was 250 Mcf/d gas, 38 Bbls/d of condensate and 69 Bbls/d of formation water. The information gathered from the 14-5 well will be incorporated into any potential future development drilling locations. As a result of drilling the 14-5 well, Regal earned an interest in two additional sections of land and each subsequent option well drilled will earn an interest in two sections of land. Subsequent to the end of the quarter, the operator of Eight Mile commenced work to construct a pipeline to tie-in the property to a compression and dehydration facility at 9-28-81-17 W6M with a projected production startup date of April 1, 2008. Further work is anticipated to be conducted within the area of mutual interest during 2008, including the acquisition of 3D seismic and exploratory and development drilling.

At Garrington, during the quarter, a lease was constructed and a pipeline was installed to tie in the 14-27-38-5 W5 gas well. Difficulties were encountered during the construction of an adequate lease because the surface was located in a marsh- like area with the result being an over expenditure of approximately $200,000 from the original anticipated cost to construct the lease and tie in the well. The well is currently producing at 160 Mcf/d net to the Company. During the quarter, one additional gas well in which the Corporation owns a 5% working interest at Garrington was tied in and subsequent to the end of the quarter was placed on production at a rate of 25 Mcf/d net. Also subsequent to the end of the quarter, Regal agreed to sell its 5% interest in this well along with one additional gas well (0.75 net) and certain undeveloped Mannville rights to the operator of the well. During the first quarter of 2008 Regal farmed out its interest in a potential Edmonton gas location and retained an overriding royalty interest. Subsequent to the end of the quarter, a successful Edmonton gas well was drilled and completed under this agreement. On November 19, 2007 the option to drill further wells under the Corporation's main farm-in and option agreement at Garrington was terminated and as a result, Regal earned interests in 12 sections of land under this agreement.

At Pica, the operator completed the equipping and tie-in of the 13-6-84-5 W6M well at a net cost to Regal of approximately $150,000. Subsequent to the end of the quarter, the well has been shut in due to excessive water production. The well is not capable of further economic production.

At Hanna, during the month of October 2007, the operator of the Corporation's gas well at 7-22-34-11 W4M (43 percent working interest) shut-in the well pending evaluation for artificial lift. The operator has indicated it has plans to reactivate the well following spring breakup. For the three months ended September 30, 2007, the Corporation produced 6.3 MMcf of natural gas and 172 Bbls of light gravity crude oil at Hanna. As a result of poorer than expected results of the well, the Corporation relinquished its rights to further options to drill wells and earn additional lands under its farm-in agreement at Hanna.

Regal's average production rate during the first quarter was 180 Boe/d or 17 percent higher than the quarter ended September 30, 2007 and 45 percent higher than the comparable period in 2006. Overall, our blended commodity price strengthened somewhat over the previous quarter. The Corporation received an average selling price of $41.78 per Boe as compared to $37.69 for the final quarter of 2007 and $40.31 for the entire 2007 year. Spot natural gas prices are currently in the range of $7.50/GJ Canadian at the AECO C Hub which is approximately 30% higher than the average spot price of approximately $5.70/GJ during the quarter ended December 31, 2007.

## Producing properties of the Corporation

| Area | Working Interest (%) | Quarter Ended Dec.31, 2007 Average Production Rate Gas (Mcf/d) | Oil & NGLs (Bbl/d) | Total Oil Equivalent (Boe/d) | Quarter Ended Dec. 31, 2006 Average Production Rate Gas (Mcf/d) | Oil & NGLs (Bbl/d) | Total Oil Equivalent (Boe/d) |
|---|---|---|---|---|---|---|---|
| Garrington | 75-100 | 587 | 16 | 114 | 395 | 4 | 70 |
| Kaybob | 62 | 103 | 7 | 24 | 44 | 3 | 10 |
| Veteran | 30-50 | - | 12 | 12 | - | 18 | 18 |
| Viking Kinsella | 20 | 64 | - | 11 | 81 | - | 14 |
| Atlee Buffalo | 50-100 | 47 | - | 8 | 56 | 1 | 10 |
| Pica | 34.5 | 38 | - | 6 | - | - | - |
| Hanna | 42.5 | 10 | - | 2 | - | - | - |
| Judy Creek | 5 | 1 | 3 | 3 | - | 2 | 2 |
| Total | | 850 | 38 | 180 | 576 | 28 | 124 |

## OPERATING NETBACK

The following table reconciles the Company's operating netback which is considered to be a non-GAAP measure [(1)].

| **Netback Per Boe** | Three Months Ended Dec. 31, 2007 | Dec. 31, 2006 |
|---|---|---|
| Revenue | $41.78 | $40.13 |
| Royalties | (6.85) | (7.20) |
| Operating Costs | (22.34) | (19.18) |
| Operating Netback | $12.59 | $13.75 |

Note:

(1) Operating netback is a non-GAAP measure and is a benchmark used in the oil industry to measure the contribution of crude oil and natural gas sales, subsequent to the deduction of royalties and operating costs. This measure is not necessarily comparable to "Operating Netback" as reported by another entity.

The operating netback for the three months ended December 31, 2007 was $12.59 per Boe compared to $13.75 per Boe in the comparable period in 2006. Gross revenue increased by $1.65 per Boe and royalty expense decreased by $0.35 per Boe. These positives were offset by an increase in operating costs of $3.16 per Boe which caused an overall decline in the operating netback of $1.16 per Boe.

The average prices of the components of revenue for the quarter ended December 31, 2007 included $5.64 per Mcf for natural gas and $71.14 per Boe for crude oil and natural gas liquids. This compares to $6.10 per Mcf for natural gas and $52.36 per Boe for crude oil and natural gas liquids in the equivalent period of last year. As approximately 80% of Regal's production is from natural gas, the overall increase in gross revenue per Boe has been significantly tempered considering the substantial increase experienced in the prices received for crude oil and natural gas liquids. Subsequent to quarter-end, natural gas prices have continued to increase and the Company is hopeful this trend will continue.

Royalty expense for the current quarter on a per Boe basis decreased from $7.20 per Boe in the first quarter of 2007 to $6.85 per Boe in first fiscal quarter of 2008.

Total operating costs of $22.34 per Boe in the current fiscal quarter are $3.16 per Boe higher than the $19.18 per Boe experienced in the first fiscal quarter of 2007. During the current quarter extraordinary operating costs were incurred in the non-operated oil producing property at Veteran. During the quarter approximately $57,500 was spent on work over costs at Veteran in order to maintain production. These extraordinary costs increased overall operating costs by approximately $3.50 per Boe during the current quarter.

## FINANCIAL REVIEW

## NET EARNINGS , FUNDS FLOW AND CASH FLOW FROM OPERATIONS:

| | Three Months Ended | |
|---|---|---|
| | Dec. 31, 2007 | Dec. 31, 2006 |
| Weighted Average Shares Outstanding | 48,137,590 | 26,118,789 |
| Net Income (Loss) | $(498,142) | $(356,635) |
| Per Share Basic and Diluted | $(0.01) | $(0.01) |
| Funds Flow From Operations (1) | $(61,680) | $(68,461) |
| Per Share Basic and Diluted | $0.00 | $(0.00) |
| Cash Flow From Operations | $198,415 | $(182,530) |
| Per Share Basic and Diluted | $0.00 | $(0.01) |

Note:

(1) Funds flow from operations has been presented for information purposes only and should not be considered an alternative to, or more meaningful than, cash flow from operating activities as determined in accordance with GAAP. The Corporation considers funds flow from operations to be a key measure as it demonstrates the Corporation's ability to generate the cash necessary to repay debt and to fund future growth through capital investment. The determination of Regal's funds flow from operations may not be comparable to the same reported by other companies. The reconciliation of net earnings and funds flow from operations can be found in the statements of cash flow in the consolidated financial statements. Funds flow from operations per share was calculated using the same weighted average shares outstanding used in calculating net earnings per share.

## REVENUE

### Working Interest Sales

| | Three Months Ended | |
|---|---|---|
| **Sales Volumes** | Dec. 31, 2007 | Dec. 31, 2006 |
| Natural Gas (Mcf) | 78,166 | 52,969 |
| Crude Oil & NGLs (Bbls) | 3,528 | 2,554 |
| Total Oil Equivalent (Boe) | 16,556 | 11,382 |
| Total (Boe/d) | 180 | 124 |

| Sales Revenue | Three Months Ended Dec. 31, 2007 | Dec. 31, 2006 |
|---|---|---|
| Natural Gas | $440,633 | $323,071 |
| Crude Oil & NGLs | 250,998 | 133,719 |
| Total | $691,631 | $456,790 |

| Sales Price Per Unit | Three Months Ended Dec. 31, 2007 | Dec. 31, 2006 |
|---|---|---|
| Natural Gas ($/Mcf) | 5.64 | 6.10 |
| Crude Oil & NGLs ($/Bbl) | 71.14 | 52.36 |
| Total Blended ($/Boe) | 41.78 | 40.13 |

Total working interest revenue during the three months ended December 31, 2007 amounted to $691,631 (December 31, 2006 - $456,790) and was made up of natural gas sales in the amount of $440,633 (2006 - $323,071) and crude oil and natural gas liquids sales of $250,998 (2006 – $133,719). During the quarter, 78,166 Mcf or 850 Mcf/d (2006 – 52,969 Mcf or 576 Mcf/d) of natural gas was sold and 3,528 Boe or 38 Boepd (2006 – 2,554 Boe or 28 Boepd) of crude oil and natural gas liquids was sold for a total of 16,556 Boe or 180 Boe/d sold (2006 – 11,382 Boe or 124 Boe/d). Natural gas and NGLs production increased mainly as a result of the tie-in of additional wells at Garrington during the fourth quarter of 2007.

Sales volumes for the first quarter of 2008 increased by 56 Boepd or 45% from the comparable period of 2007.

## ROYALTIES

| | Three Months Ended Dec. 31, 2007 | Dec. 31, 2006 |
|---|---|---|
| Crown royalties | $63,414 | $56,362 |
| Freehold royalties | 8,267 | 8,295 |
| Overriding royalties | 41,803 | 31,331 |
| ARTC | - | (14,000) |
| Total | $113,484 | $81,988 |
| Total (per Boe) | $6.85 | $7.20 |

Royalties, which include crown, freehold and overriding royalties paid on oil, natural gas liquids and natural gas production amounted to $113,484 during the first quarter of 2008 compared to $81,988 during the first quarter of fiscal 2007. Average royalties during the first fiscal quarter of 2008 amounted to $6.85 per Boe or 16.4% of sales (2007 - $7.20 per Boe or 17.9%). This reduction on a per Boe basis and as a percentage of gross sales is primarily due to production at our Garrington area stabilizing at lower rates after initially coming on at "flush" production rates. As well, as the Alberta government natural gas royalty rates are sensitive to commodity prices, the reduction of average natural gas prices from $6.10 per Mcf during the first fiscal quarter of 2007 to $5.64 per Mcf in the current fiscal quarter has also contributed to the reduction in royalty costs on a per Boe and as a percentage of gross revenue basis.

On October 25, 2007 the Government of Alberta released its New Royalty Framework ("NRF") for the province which is proposed to take effect on January 1, 2009. Because the majority of the Corporation's production in Alberta is from low productivity wells, at current pricing levels, the NRF is expected to have a minimal impact on Regal's effective royalty rates.

## OPERATING EXPENSE

| | Three Months Ended | | | |
|---|---|---|---|---|
| Major Field | Dec. 31, 2007 | Per Boe | Dec. 31, 2006 | Per Boe |
| Atlee Buffalo | $26,724 | $36.76 | $31,962 | $35.85 |
| Garrington | 169,874 | 16.25 | 90,351 | 14.06 |
| Hanna | 19,835 | 94.55 | - | - |
| Judy Creek | 2,352 | 8.69 | 2,013 | 10.82 |
| Kaybob | 26,146 | 11.92 | 11,239 | 12.57 |
| Pica | 8,906 | 15.36 | - | - |
| Viking Kinsella | 2,173 | 2.21 | 12,336 | 9.96 |
| Veteran | 110,589 | 98.88 | 67,160 | 39.29 |
| Other | 3,209 | - | 3,201 | - |
| Total | $369,808 | $22.34 | $218,262 | $19.18 |

Total operating costs for the quarter ended December 31, 2007 amounted to $369,808 or $22.34 per Boe compared to $218,262 or $19.18 per Boe during the quarter ended December 31, 2006. During the current quarter, the operator of the Veteran property conducted workovers on two wells in order to restore production. The total cost of these workovers was approximately $57,500. Over the total production volume for the quarter, this amounts to almost $3.50 per Boe increase in operating expense. The Company does not expect any further extraordinary workover costs at Veteran during the remainder of the year. At Garrington, operating costs have increased by $2.19 per Boe as a result of the need to rent two wellsite compressors to maintain natural gas production from the wells. The compressors are trailer mounted and thus can be moved from location to location as the need arises.

## GENERAL AND ADMINISTRATIVE EXPENSE

| | Three Months Ended | |
|---|---|---|
| | Dec. 31, 2007 | Dec. 31, 2006 |
| Salaries & Benefits | $90,495 | $82,580 |
| Office Costs | 41,405 | 40,107 |
| Legal, Audit Engineering Fees | 97,065 | 65,825 |
| Other Consulting | 25,658 | 25,479 |
| Shareholder Services | 2,341 | 10,897 |
| Capital/Operating Recoveries | (14,743) | (45,321) |
| | $242,221 | $179,567 |
| G&A per Boe | $14.63 | $15.78 |

Total general and administrative expense during the first fiscal quarter of 2008 amounted to $242,221 or $14.63 per Boe compared to $179,567 or $15.78 per Boe during the equivalent period of fiscal 2007. The increase in salaries and benefits during the first fiscal quarter of 2008 relates primarily to salary increases that were granted to employees effective January 1, 2007. The increase in legal, audit and engineering fees is due to engaging an outside firm to assist the Corporation in responding to the CRA audit of transfer pricing on international transactions of a predecessor corporation – Sibercore Technologies Incorporated. The remaining major variance is the reduction of the amount of capital and operating recoveries in the first fiscal quarter of 2008 compared to the similar period in 2007. This reduction is entirely due to the level of capital expenditures in the related periods (2008 - $1.376 million versus 2007 - $3.744 million).

## INTEREST EXPENSE

Total interest expense for the first quarter ended December 31, 2007 amounted to $28,150 compared to $45,434 during the equivalent quarter ended December 31, 2006. Interest expense for the first quarter of 2008 is attributable to the increased level of the Corporation’s borrowings on its credit facilities while the interest expense during the first fiscal quarter of 2007 was primarily due to accrued interest payable to the Canada Revenue Agency relating to unexpended funds on the Corporation’s flow-through share issue.

## STOCK BASED COMPENSATION EXPENSE

The Corporation accounts for its stock-based compensation program using the fair-value method. Under this method, compensation expense related to this program is recorded in the statement of operations over the vesting terms of the options. During the first quarter of fiscal 2008, $22,895 of stock based compensation expense was recognized as compared to $27,038 as stock compensation expense during the first fiscal quarter of fiscal 2007. On February 12, 2007, 575,000 options were granted to directors of the Corporation and 1,125,000 options were granted to employees and consultants. Director's options vest immediately and employee's and consultant's options vest ½ on the date of grant and ½ on the first anniversary of the date of grant. In connection with this stock option grant $113,578 of stock compensation expense was recognized immediately while the expense on the unvested employee portion, stock compensation expense will be recognized over the vesting period.

## DEPLETION AND DEPRECIATION

| | Three Months Ended | |
|---|---|---|
| | Dec. 31, 2007 | Dec. 31, 2006 |
| Depletion | $373,782 | $224,542 |
| Depreciation | 5,714 | 4,562 |
| Total | $379,496 | $229,104 |
| Total (per Boe) | $22.92 | $20.13 |

Total depletion and depreciation expense for the quarter ended December 31, 2007 amounted to $379,496 or $22.92 per Boe compared to $229,104 or $20.13 per Boe for the quarter ended December 31, 2006. The depletion calculation is based on reserves as calculated by the Corporation's independent engineers as at September 30, 2007 and updated with internal Management estimates of reserve additions since that date and associated capital spent to place the added reserves on stream.

## AMORTIZATION INTANGIBLE ASSET

As a result of the acquisition of Regal Energy Corp. on December 31, 2005, an intangible asset was recognized on the balance sheet of $500,000 that represented the value placed on the Management team under contract and continuing with Regal Energy Ltd. as well as a value for the public listing of Regal Energy Corp. The costs of the intangible asset are excluded from the depletion calculation and are being amortized over a period of three years. Total amortization for the period ended December 31, 2007 was $24,993 compared to $24,994 for the same quarter one year earlier. The Corporation tests for impairment of this asset at each reporting period. At September 30, 2006 as a result of the resignation of two senior officers of the Corporation, an impairment of $149,960 was recorded against this asset. The remaining balance continues to be amortized over the original term of three years. At December 31, 2007 the remaining unamortized balance is $99,973 as compared to $199,947 on December 31, 2006.

## ACCRETION

Accretion expense represents the increase in the present value of the asset retirement obligation for the current period. During the quarter ended December 31, 2007 accretion expense amounted to $9,078 compared to $7,038 during the similar period in fiscal 2007. The increased expense on a year over year basis is due to additional wells drilled during the fiscal 2007 year and the resulting increase in the asset retirement obligation.

## INCOME TAXES

The Corporation estimates that it has approximately $63.3 million of tax pools available to shelter taxable income in future years. Due to the existence of these income tax pools, the Corporation does not expect to be taxable for the foreseeable future. A future tax benefit of $598,500 has been recognized in the financial statements as the criteria for recognition has been met. A valuation allowance of $12,949,475 has been applied against the remaining pools as the criteria for recognition has not been met.

Canada Revenue Agency ("CRA") has conducted an audit of transfer pricing on international transactions between SiberCore Technologies Incorporated and its United States subsidiary, SiberCore America Inc. for the years 2000, 2001 and 2002. SiberCore Technologies Incorporated was the predecessor company of Azeri and ultimately Regal Energy Ltd. The Corporation has received a proposed settlement letter from CRA that would result in a reduction of tax pools in the amount of $1,501,453. CRA has also proposed to charge a cash penalty of 10% of the adjustments. The

Corporation has responded to the proposed settlement letter and provided further information supporting Management's view that CRA's position has no merit. The outcome of this audit is uncertain at this time and as such no provisions have been made in these financial statements.

Subsequent to quarter-end, The Company has received reassessment notices on the audit of transfer pricing on international transactions between SiberCore Technologies Incorporated and its United States subsidiary, SiberCore America Inc. for 2001 and 2002 from CRA that result in a reduction of tax pools in the amount of $1,416,627. CRA has also assessed a cash penalty of $140,902. It is management's view that CRA's position has no merit and the Company plans to vigorously defend its position.

## CAPITAL EXPENDITURES

During the first fiscal quarter of 2008, the Corporation recorded $1,389,589 of capital expenditures compared to $3,743,911 during the first fiscal quarter of 2007. Amounts reported in the following tables do not include non-cash capital recorded for asset retirement obligation in the amount of $7,760 in the first quarter of 2008 or $66,110 in the first quarter of 2007. During the current quarter, capital expenditures were focused on the drilling and completion of the 14-5-81-17 W6M well at Eight Mile, British Columbia, the tie-in of a well at Garrington and the tie-in of a gas well at Pica.

| | Three Months Ended | |
|---|---|---|
| | Dec. 31, 2007 | Dec. 31, 2006 |
| Land Acquisition / Retention | $ 557 | $ - |
| Geological, Geophysical and Seismic | - | 278,048 |
| Drilling and Completions | 830,293 | 3,336,253 |
| Equipping and tie-ins | 539,939 | 259,331 |
| Property Acquisition / Disposition | 17,500 | 541,130 |
| Seismic Disposition | - | (675,000) |
| Furniture and Fixtures | 1,300 | 2,100 |
| Other Miscellaneous | - | 2,049 |
| | $1,389,589 | $3,743,911 |

## FINANCIAL RESOURCES AND LIQUIDITY

At December 31, 2007, the Corporation had a working capital deficiency of $3,836,298 compared to a working capital deficiency of $2,385,030 at September 30, 2007 and $2,826,938 at December 31, 2006. Components of the working capital deficiency are contained in the following table.

| | **Dec. 31, 2007** | **Sept. 30, 2007** | **Dec. 31, 2006** |
|---|---|---|---|
| Cash and cash equivalents | $ - | $ - | $ - |
| Accounts receivable | 1,284,028 | 486,313 | 1,614,863 |
| Deposits and prepaid expenses | 74,540 | 61,154 | 48,607 |
| Bank indebtedness | (2,256,912) | (1,078,357) | (565,962) |
| Accounts payable and accrued liabilities | (2,937,954) | (1,854,140) | (3,924,446) |
| Total Working Capital | $ (3,836,298) | $ (2,385,030) | $ (2,826,938) |

The Company considers all accounts receivables to be valued fairly and to be collectible.

At December 31, 2007, the Company was not in compliance with a covenant in our agreement with our lender regarding working capital. The Corporation has received a letter from the bank agreeing to waive this default. In order to rectify this non-compliance and allow the Company to proceed with the capital expenditure program necessary to increase our production and cash flow base, letters of intent for the sale of minor property interests at Garrington and the sale of miscellaneous surplus oilfield assets at Atlee Buffalo have been signed. The sale of minor property interests includes 2 gas wells (0.8 net) producing approximately 5 Boe/d net to Regal as well as associated Mannville petroleum rights and certain other undeveloped Mannville rights at Garrington. The primary portion of this sale is expected to be completed by mid-March, 2008.

The Corporation is investigating the possibility of divesting of further non-core assets that are currently producing minimal cash flow. To date however, no acceptable offers for these assets have been received and there can be no assurance that further non-core assets sales will be consummated.

The operator of the Corporation's Eight Mile property located in north east British Columbia has advised that it is proceeding with a pipeline that will tie-in the 7-8-81-17 W6M well in which the Corporation has a 40% working interest. In order to complete this operation, the Company has obtained bridge financing in the amount of $400,000 from parties that are related to the Corporation. Under the terms of this bridge financing, the Corporation will pay an initial fee of 3.0% of amounts advanced under the facility and the interest rate will be bank prime plus 3.0%. The maturity date will be 90 days from the advance of the funds. The board of directors of the Corporation has also agreed to complete an equity financing of up to $2.0 million in order to re-pay this bridge facility as well as provide working capital necessary to fund its ongoing capital requirements. There can be no guarantee however that this equity financing will be completed on terms that are acceptable to the Corporation.

The following projections are based on average wellhead prices of $68.89/Bbl for oil and NGLs for fiscal 2008 (10% higher than previous forecast), and $6.34/Mcf for natural gas for fiscal 2008 (5% higher than previous forecast). The revised forecast recognizes the current strength in commodity pricing. Current spot natural gas prices are approximately 30% higher than the average spot price during the quarter ended December 31, 2007. Management expects new production at Eight Mile will be placed on stream by April 1, 2008, which is expected to generate additional funds flow on a go-forward basis. The following projections make assumptions regarding the timing of tie-ins of wells and deliverabilities of wells that Management considers appropriate. The Corporation believes that with its current banking facilities, funds flow from operations, the sale of non-core assets and the issuance of additional equity, it will have the financial resources necessary to complete its $3 million capital budget. The following table shows Management's current estimate of fiscal 2008 results and outlines the Corporation's expected working capital position at September 30, 2008:

| | | |
|---|---|---|
| Working capital surplus (deficiency) December 31, 2007 | $ | (3,836,298) |
| Exercised of warrants (projected to occur May & August 2008) | | 250,033 |
| Issuance of further equity (net of costs) | | 1,873,000 |
| Expected funds flow January 1, 2008 - September 30, 2008 | | 820,931 |
| Projected net capital expenditures January 1, 2008 – September 30, 2008 | | (970,000) |
| Expected working capital (deficiency) September 30, 2008 (1) | $ | (1,862,334) |

Note:
(1) Total available banking facilities as at the date of this report - $3,250,000

## LENDING FACILITY

The Corporation has a revolving operating demand facility of $3,250,000 that bears interest at the bank prime rate plus 1/2 percent. Repayments of the facility are not required provided the amounts borrowed do not exceed $3,250,000 or an amount to be determined from time to time. The loan facility is subject to interim and annual reviews by the bank and is secured by a $5,000,000 floating charge demand debenture over all assets of the Corporation. At December 31, 2007, the Corporation was not in compliance with a banking covenant regarding working capital. The Corporation has received a letter from the bank agreeing to waive this default. At December 31, 2007 there was $2,250,000 drawn on the operating demand facility. In addition, there were net outstanding cheques of $6,912 to be drawn against this facility for total bank indebtedness of $2,256,912.

## EQUITY CAPITAL

At December 31, 2007 Regal had 48,137,590 common shares outstanding. In addition, there were 5,100,167 share purchase warrants outstanding of which 916,667 are exercisable until May 30, 2008 at a price of $0.20 per share, 333,500 are exercisable at a price of $0.20 per share until August 1, 2008 and 3,850,000 are exercisable at a price of $0.35 until July 16, 2009.

**Common Shares:**

| | **Shares** | **Amount** |
|---|---|---|
| Balance, September 30, 2006 | 22,709,179 | $70,172,113 |
| Private placement issued for cash – Nov. 30, 2006 | 5,000,000 | 972,816 |
| Private placement issued for cash on a flow through basis – Nov 30, 2006 | 4,583,333 | 1,077,345 |
| Rights offering– December 21, 2006 | 1,660,078 | 332,016 |
| Private placement issued for cash – Feb 1, 2007 | 3,335,000 | 626,740 |
| Private placement issued for cash on a flow through basis – June 28 and July 16, 2007 | 3,234,200 | 970,260 |
| Private placement issued for cash on a flow through basis – June 28 and July 16, 2007 | 3,765,800 | 1,129,740 |
| Private placement issued for cash – July 16, 2007 | 3,850,000 | 813,133 |

| | | |
|---|---|---|
| Tax impact of flow through share issue | - | (319,000) |
| Share issuance costs | - | (590,332) |
| Balance, September 30, 2007 and December 31, 2007 | 48,137,590 | $75,184,831 |

**Warrants:**

| | Number of Warrants | Number of Underlying Shares | Amount |
|---|---|---|---|
| Balance, September 30, 2006 | 1,723,566 | 1,723,566 | $ 406,300 |
| November 30, 2006 private placement | 916,667 | 916,667 | 49,838 |
| February 1, 2007 private placement | 333,500 | 333,500 | 40,260 |
| June 30, 2007 expiry of warrants | (817,923) | (817,923) | (188,000) |
| July 16, 2007 private placement | 3,850,000 | 3,850,000 | 187,867 |
| Balance, September 30, 2007 | 6,005,810 | 6,005,810 | $ 496,265 |
| December 31, 2007 expiry of warrants (1) | (905,643) | (905,643) | (218,300) |
| Balance December 31, 2007 | 5,100,167 | 5,100,167 | 277,965 |

(1) 905,643 warrants that were issued in connection with the acquisition of Regal Energy Corp. expired on December 31, 2007

**Options:**

The Corporation has a stock option plan under which directors, employees and consultants are eligible to receive grants. Options granted under the plan to outside independent directors vest immediately. Options granted to employees and consultants of the Corporation prior to December 31, 2006 vest one-third on the date of grant, and one third each on the first and second anniversaries of the date of grant. Options granted to employees and consultants subsequent to December 31, 2006 vest one half on the date of grant and one half on the first anniversary of the date of grant.

The following table summarizes the status of the Corporation's stock option plan and the activity from September 30, 2006 to December 31, 2007.

| | Number of Options | Weighted Average Exercise Price | Expiry Date |
|---|---|---|---|
| Balance September 30, 2006 | 1,626,000 | $0.96 | Various 2009-2011 |
| Options granted February 12, 2007 | 1,675,000 | 0.30 | February 12, 2012 |
| Options cancelled(1) | (350,000) | 0.95 | |
| Balance September 30, 2007 | 2,951,000 | $0.58 | |
| Options cancelled(1) | (86,000) | $1.00 | |
| Balance December 31, 2007 | 2,865,000 | $0.57 | |
| Exercisable at December 31, 2007 | 2,155,000 | $0.61 | |

(1) Options issued to former directors and officers of the Corporation

| Date of Grant | Number Outstanding | Exercise Price | Weighted Average Remaining Contractual Life (Years) | Date of Expiry | Number Exercisable at Dec. 31, 2007 |
|---|---|---|---|---|---|
| Dec. 31, 2005(2) | 80,000 | $1.00 | 1.08 | Jan. 30, 2009 | 80,000 |
| Dec. 31, 2005(2) | 50,000 | $0.90 | 1.63 | Aug. 17, 2009 | 50,000 |
| Dec. 31, 2005(2) | 55,000 | $1.00 | 2.28 | Apr. 13, 2010 | 55,000 |
| Jan. 1, 2006 | 1,005,000 | $0.95 | 3.01 | Jan. 1, 2011 | 845,000 |
| Feb. 12, 2007(1) | 1,675,000 | $0.30 | 4.12 | Feb. 12, 2012 | 1,125,000 |
| | 2,865,000 | $0.58 | | | 2,155,000 |

(1) On February 12, 2007, 575,000 options were granted to directors and 1,100,000 options were granted to officers, employees and consultants. Under the terms of the option agreements, options granted to directors vest immediately while those options granted to officers, employees and consultants vest one-half on the date of grant and one half on the first anniversary of the date of grant. The fair value of each option is estimated using the Black-Scholes option pricing model and assumes an expected volatility of 50%, a risk free rate of return of 5.0%, and a weighted average life of 5 years.

(2) Pursuant of the acquisition of Regal Energy Corp. replacement options were issued to directors and officers of Regal Energy Corp. These options vested upon the completion of the transaction as the change of control provision of the option plan was triggered.

As of the date of this MD&A, the Corporation has the following outstanding equity instruments:

| | |
|---|---|
| Shares outstanding | 48,137,590 |
| Shares issuable upon exercise of warrants | 5,100,167 |
| Stock options outstanding | 2,865,000 |
| Total equity instruments outstanding | 56,102,757 |

A total of 48,137,590 common shares are currently issued and outstanding. A further total of 7,965,167 shares are reserved for the exercise of options and warrants, bringing the total diluted number of shares to 56,102,757.

## COMMITMENTS

Pursuant to a flow-through financing completed on June 28, 2007 and July 16, 2007, the Company is committed to spend $2,100,000 on qualified exploration and development expenditures by December 31, 2008. As at December 31, 2007, the Company has expended approximately $1,350,000 relating to these commitments.

At December 31, 2007, the Company had commitments for a rental compressor totaling $29,200 in 2008.

## RELATED PARTY TRANSACTIONS

During the quarter ended December 31, 2007, there were no related party transactions.

## SUMMARY OF QUARTERLY RESULTS

| | Three months ended Dec. 31, 2007 | Three months ended Sep. 30, 2007 | Three months ended Jun. 30, 2007 | Three months ended Mar. 31, 2007 |
|---|---|---|---|---|
| Petroleum and natural gas sales $ | 691,631 | 532,854 | 542,243 | 477,805 |
| Net income (loss) $ | (498,142) | (3,126,430) | (429,510) | (474,420) |
| Per share – basic and diluted $ | (0.01) | (0.07) | (0.01) | (0.01) |
| Funds flow from operations (non-GAAP) $ | (61,680) | (3,267) | (29,834) | (97,481) |
| Per share – basic and diluted $ | 0.00 | 0.00 | 0.00 | 0.00 |
| Cash flow from operations $ | 198,415 | (170,620) | 165,025 | (143,082) |
| Per share – basic and diluted | 0.00 | 0.00 | 0.00 | 0.00 |
| Capital expenditures – net of dispositions $ | 1,389,589 | 1,219,051 | 717,567 | 870,581 |
| Average daily production (Boe/d) | 180 | 154 | 145 | 124 |
| Weighted average shares outstanding | 48,137,590 | 46,813,103 | 37,394,212 | 36,138,868 |

| | Three months ended Dec. 31, 2006 | Three months ended Sep. 30, 2006 | Three months ended Jun. 30, 2006 | Three months ended Mar. 31, 2006 |
|---|---|---|---|---|
| Petroleum and natural gas sales $ | 456,790 | 470,281 | 321,021 | 374,960 |
| Net income (loss) | (356,635) | (4,950,641) | (611,937) | (20,112) |
| Per share – basic and diluted | (0.01) | (0.22) | (0.03) | (0.00) |
| Funds flow from operations (non-GAAP) $ | (68,461) | (103,327) | (340,001) | (151,075) |
| Per share – basic and diluted | 0.00 | 0.00 | (0.01) | 0.00 |
| Cash flow from operations $ | (182,530) | 375,178 | (1,183,742) | (209,049) |
| Per share – basic and diluted | (0.01) | 0.02 | (0.05) | (0.03) |
| Capital expenditures – net of dispositions | 3,743,911 | 1,078,183 | 1,750,766 | 3,404,309 |
| Average daily production (Boe/d) | 124 | 116 | 67 | 100 |
| Weighted average shares outstanding | 26,118,789 | 22,709,179 | 22,709,179 | 22,709,179 |

## SUMMARY OF SHARE TRADING DURING THE FIRST THREE QUARTERS OF 2007 AND 2006

| | Price Range | | | | |
|---|---|---|---|---|---|
| **Period of Fiscal 2008** | **High ($)** | **Low ($)** | **Close ($)** | **Volume Traded** | **Value ($)** |
| Total First Quarter | 0.32 | 0.26 | 0.27 | 2,447,357 | 684,049 |

| | Price Range | | | | |
|---|---|---|---|---|---|
| **Period of Fiscal 2007** | **High ($)** | **Low ($)** | **Close ($)** | **Volume Traded** | **Value ($)** |
| First Quarter | 0.24 | 0.165 | 0.18 | 3,145,159 | 580,356 |
| Second Quarter | 0.39 | 0.18 | 0.26 | 2,448,675 | 593,969 |
| Third Quarter | 0.30 | 0.215 | 0.30 | 2,232,367 | 578,557 |
| Fourth Quarter | 0.36 | 0.26 | 0.28 | 2,484,691 | 713,043 |
| Total Year | 0.39 | 0.165 | 0.30 | 10,310,892 | 2,465,925 |

## DISCLOSURE CONTROLS AND PROCEDURES

Disclosure controls and procedures have been designed to ensure that information required to be disclosed by the Corporation is accumulated and communicated to our Management as appropriate to allow timely decisions regarding required disclosure. The Corporation's Chief Executive Officer and Chief Financial Officer have concluded, based on their evaluation as of December 31, 2007, that the Corporation's disclosure controls and procedures are effective to provide reasonable assurance that material information related to Regal, is made known to them by employees or third party consultants working for the Corporation. It should be noted that while the Corporation's Chief Executive Officer and Chief Financial Officer believe that our disclosure controls and procedures will provide a reasonable level of assurance and that they are effective, they do not expect that the disclosure controls and procedures will prevent all errors and fraud. A control system, no matter how well conceived or operated, can provide only reasonable, not absolute assurance that the objectives of the control system are met.

## CHANGES TO INTERNAL CONTROL OVER FINANCIAL REPORTING

There have been no changes to Regal's internal control over financial reporting since September 30, 2007, which have materially affected, or are reasonably likely to materially affect Regal's internal control over financial reporting.

## CRITICAL ACCOUNTING ESTIMATES

The preparation of financial statements in conformity with generally accepted accounting principals requires the Corporation to make assumptions, judgments and estimates that may have a significant impact on the financial statements. Estimates are reviewed periodically and as adjustments become necessary, they are reported in earnings in the period they become known. A summary of the Corporation's significant accounting policies can be found in Note 2 of the September 30, 2007 audited financial statements.

## ACCOUNTING CHANGES

Effective October 1, 2007, the Corporation adopted the CICA Handbook Section 1506 Accounting Changes that provides expanded disclosures for changes in accounting policies, accounting estimates and corrections of errors. Under the new standard, accounting changes should be applied retroactively unless otherwise permitted or where impracticable to determine. As well, voluntary changes in accounting policy are made only when required by a primary source of GAAP or the change results in more relevant and reliable information.

Effective October 1, 2007, the Corporation adopted two new CICA standards, Handbook Section 3862, Financial Instruments - Disclosures and Section 3863, Financial Instruments - Presentation replaced Section 3861, Financial Instruments - Disclosure and Presentation. The new disclosure standard increases the emphasis on the risks associated with both recognized and unrecognized financial instruments and how those risks are managed. The new presentation standard carries forward the former presentation requirements.

Effective October 1, 2007, the Corporation adopted the CICA Handbook Section 1535 - Capital Disclosures which requires companies to disclose their objectives, policies and processes for managing capital. In addition, disclosures are to include whether companies have complied with externally imposed capital requirements.

## CANADIAN ACCOUNTING PRONOUNCEMENTS

The CICA has amended Section 1400, "General Standards of Financial Statement Presentation", which is effective for interim periods beginning on or after October 1, 2008, to include requirements to assess and disclose the Company's ability to continue as a going concern. The adoption of this new section will not have an impact on the financial statements.

Effective October 1, 2008, the Company will be required to adopt CICA Handbook Section 3031 – Inventories. This new standard is not expected to have an impact on the Company's financial statements. In January 2006, the CICA Accounting Standards Board ("ASCB") adopted a strategic plan for the direction of accounting standards in Canada. As part of that plan, accounting standards in Canada for public companies are expected to converge with International Financial Reporting.

In 2006, Canada's Accounting Standards Board ratified a strategic plan that will result in Canadian GAAP, as used by public companies, being converged with International Financial Reporting Standards over a transitional period currently expected to be about five years. The precise timing of convergence will depend on an Accounting Standards Board progress review to be undertaken by early 2008. The impact of this transition on the Corporation's financial statements has not yet been determined; however, Management continues to monitor these regulatory developments.

## RISKS AND UNCERTAINTIES

The business of exploring for, developing and producing oil and gas reserves is inherently risky. There is a risk that the sale of the Corporation's reserves may be delayed indefinitely due to process constraints, lack of pipeline capacity or lack of markets. The price the Corporation receives for its crude oil and natural gas fluctuates continuously and for the most part is beyond its control. The Corporation is also subject to the risks associated with oil and gas properties, including exploration, development and production risks, and environmental risks such as the pollution of air, land and water. In all areas of the Corporation's business, it competes against entities that have greater technical and financial resources. The Corporation's growth is dependent upon external sources of financing which may not be available on acceptable terms. For a more detailed description regarding risks and uncertainties of the Corporation please see disclosures contained in the annual report filed on SEDAR or available on Regal's website.

## ADDITIONAL INFORMATION REGARDING REGAL ENERGY LTD.

Additional information regarding Regal Energy Ltd. is available on the internet at www.sedar.com and Regal's website (www.regalenergy.ca).

## NATIONAL INSTRUMENT 51-102

The Corporation's independent auditor has not performed an audit or review of the December 31, 2007 financial statements in accordance with the standards of the Canadian Institute of Chartered Accountants.

**Regal Energy Ltd.**
**Interim Financial Statements**
**December 31, 2007**

## Contents



**NOTICE:** **The interim financial statements and notes thereto for the three months ended December 31, 2007 have not been reviewed by the Company's external auditors.**

**These interim financial statements do not include all the note disclosuresrequired for annual financial statements and therefore they should be read in conjunction with the Company's audited financial statements for the year ended September 30, 2007 available on SEDAR at www.sedar.com or on the Company's website at www.regalenergy.ca.**

## Regal Energy Ltd.
## Balance Sheets

| As at | | Dec. 31, 2007 (unaudited) | | Sept. 30, 2007 (audited) |
|---|---|---|---|---|
| **ASSETS** | | | | |
| **Current Assets** | | | | |
| Cash and cash equivalents | **$** | **-** | $ | - |
| Accounts receivable | | **1,284,028** | | 486,313 |
| Deposits and prepaid expenses | | **74,540** | | 61,154 |
| | | **1,358,568** | | 547,467 |
| **Future tax asset** | | **598,500** | | 598,500 |
| **Property and equipment (Note 3)** | | **11,462,461** | | 10,444,607 |
| **Intangible assets** | | **99,973** | | 124,967 |
| | **$** | **13,519,502** | $ | 11,715,541 |
| **LIABILITIES AND SHAREHOLDER'S EQUITY** | | | | |
| **Current** | | | | |
| Bank indebtedness (Note 4) | **$** | **2,256,912** | **$** | 1,078,357 |
| Accounts payable and accrued liabilities | | **2,937,954** | | 1,854,140 |
| | | **5,194,866** | | 2,932,497 |
| **Asset retirement obligation (Note 7)** | | **414,397** | | 397,558 |
| **SHAREHOLDER'S EQUITY** | | | | |
| **Equity instruments (Note 5(b) and (c))** | | **75,462,796** | | 75,681,096 |
| **Contributed surplus (Note 5(e))** | | **1,457,415** | | 1,216,220 |
| **Deficit** | | **(69,009,972)** | | (68,511,830) |
| | | **7,910,239** | | 8,385,486 |
| | **$** | **13,519,502** | $ | 11,715,541 |
| **Commitments and contingencies (Note 10)** | | | | |
| **Subsequent events (Note 11)** | | | | |

See accompanying notes. Interim financial statements are prepared by management and have not been independently audited or reviewed by the Company's auditors

Approved on behalf of the Board:

*Signed: "Douglas O. McNichol"*

**Douglas O. McNichol – Director**

*Signed: "Richard M. Wlodarczak"*

**Richard M. Wlodarczak – Chairman of the Board**

## Regal Energy Ltd.
## Statements of Operations, Comprehensive Loss and Deficit

| | For the three month period ended Dec. 31, 2007 (unaudited) | For the three month period ended Dec. 31, 2006 (unaudited) |
|---|---|---|
| **REVENUE** | | |
| Production revenues | $ 691,631 | $ 456,790 |
| Royalties | (113,484) | (81,988) |
| Interest and other income | 352 | - |
| | 578,499 | 374,802 |
| **EXPENSES** | | |
| Operating | 369,808 | 218,262 |
| General and administrative | 242,221 | 179,567 |
| Interest | 28,150 | 45,434 |
| Stock-based compensation (Note 5(d)) | 22,895 | 27,038 |
| Depletion and depreciation | 379,496 | 229,104 |
| Amortization of intangible asset | 24,993 | 24,994 |
| Accretion | 9,078 | 7,038 |
| | 1,076,641 | 731,437 |
| **Net income (loss) for the period** | (498,142) | (356,635) |
| Other comprehensive income (loss) | - | - |
| **Net income (loss) for the period including comprehensive income (loss)** | (498,142) | (356,635) |
| **Deficit, beginning of period** | (68,511,830) | (64,124,835) |
| **Deficit, end of period** | $ (69,009,972) | $ (64,481,470) |
| **Net income (loss) per share - Basic and diluted** | $ (0.01) | $ (0.01) |
| **Weighted average shares outstanding - Basic** | 48,137,590 | 26,118,789 |

See accompanying notes. Interim financial statements are prepared by management and have not been independently audited or reviewed by the Company's auditors

# Regal Energy Ltd.
# Statements of Funds Flows

| | For the three month period ended Dec. 31, 2007 (unaudited) | For the three month period ended Dec. 31, 2006 (unaudited) |
|---|---|---|
| **FUNDS FLOW FROM OPERATING ACTIVITIES** | | |
| Net income (loss) for the period | $ (498,142) | $ (356,635) |
| Add non-cash items: | | |
| Stock-based compensation | 22,895 | 27,038 |
| Amortization of intangible asset | 24,993 | 24,994 |
| Depletion and depreciation | 379,496 | 229,104 |
| Accretion | 9,078 | 7,038 |
| Funds flow from operations | (61,680) | (68,461) |
| Net change in non-cash working capital balances | 260,095 | (114,069) |
| | 198,415 | (182,530) |
| **FUNDS FLOW FROM FINANCING ACTIVITIES** | | |
| Issue of common shares | - | 2,229,995 |
| Proceeds from bank loan | 1,178,556 | 206,926 |
| | 1,178,556 | 2,436,921 |
| **FUNDS FLOW FROM INVESTING ACTIVITIES** | | |
| Net change in non-cash working capital balances | 12,618 | 1,489,520 |
| Net cash paid on the acquisition of Regal Energy Corp. | | - |
| Capital expenditures | (1,389,589) | (3,743,911) |
| | (1,376,971) | (2,254,391) |
| **Increase in cash and cash equivalents** | - | - |
| **Cash and cash equivalents, beginning of period** | - | - |
| **Cash and cash equivalents, end of period** | $ - | $ - |

See accompanying notes. Interim financial statements are prepared by management and have not been independently audited or reviewed by the Company's auditors

## REGAL ENERGY LTD.
## NOTES TO THE INTERIM FINANCIAL STATEMENTS

### 1. Description of Business and Basis of Presentation

Regal Energy Ltd. ("Regal or the Company") is engaged in the exploration for and the development, production and acquisition of petroleum and natural gas reserves in Western Canada. Regal's financial year end is September 30.

The interim financial statements of the Company have been prepared by management, in accordance with Canadian generally accepted accounting principles and are unaudited. The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates. The interim financial statements have been prepared following the same accounting policies and methods of computation as the audited financial statements for the year ended September 30, 2007 except as discussed in Note 2. These interim financial statements do not include all the note disclosures required for annual financial statements and therefore they should be read in conjunction with the Company's audited financial statements for the year ended September 30, 2007.

The Company's financial statements as at and for the interim period ended December 31, 2007 have been prepared on a going concern basis, which contemplates the realization of assets and the settlement of liabilities and commitments in the normal course of business. The ability of the Company to continue as a going concern is dependent upon the Company's ability to generate future profitable operations and obtaining additional equity or debt financing.

### 2. Changes in Accounting Policies

The Canadian Institute of Chartered Accountants ("CICA") issued the following new Handbook Sections, which were effective for interim periods beginning on or after October 1, 2007.

a) Section 3862, "Financial Instruments – Disclosures", describes the required disclosure for the assessment of the significance of financial instruments for an entity's financial position and performance and of the nature and extent of risks arising from financial instruments to which the entity is exposed and how the entity manages those risks. This section and Section 3863, "Financial Instruments – Presentation" replaced Section 3861, "Financial Instruments – Disclosure and Presentation".
b) Section 3863, "Financial Instruments – Presentation", establishes standards for presentation of financial instruments and non-financial derivatives.
c) Section 1535, "Capital Disclosures", establishes standards for disclosing information about an entity's capital and how it is managed. It describes the disclosure requirements of the entity's objectives , policies and processes for managing capital, the quantitative data relating to what the entity regards as capital, whether the entity has complied with capital requirements, and, if it has not complied, the consequences of such non-compliance.

Future Accounting Changes

a) The CICA has amended Section 1400, "General Standards of Financial Statement Presentation", which is effective for interim periods beginning on or after October 1, 2008, to include requirements to assess and disclose the Company's ability to continue as a going concern. The adoption of this new section will not have an impact on the financial statements
b) Effective October 1, 2008, the Company will be required to adopt CICA Handbook Section 3031 – Inventories. This new standard is not expected to have an impact on the Company's financial statements.
c) In January 2006, the CICA Accounting Standards Board ("ASCB") adopted a strategic plan for the direction of accounting standards in Canada. As part of that plan, accounting standards in Canada for public companies are expected to converge with International Financial Reporting

Standards ("IFRS") by 2011. On February 13, 2008, The ASCB confirmed that the use of IFRS will be required in 2011 for publicly accountable profit-orientated enterprises. The Company continues to monitor and assess the impact of the convergence of Canadian GAAP and IFRS.

## 3. Property and Equipment

| December 31, 2007 | Cost | Accumulated depletion, depreciation and amortization | Net book value |
|---|---|---|---|
| Petroleum and natural gas properties and equipment | $20,467,051 | $9,913,348 | $10,553,703 |
| Seismic resources | 878,545 | - | 878,545 |
| Other assets | 68,729 | 38,516 | 30,213 |
| | $21,414,325 | $9,951,864 | $11,462,461 |

| September 30, 2007 | Cost | Accumulated depletion, depreciation and amortization | Net book value |
|---|---|---|---|
| Petroleum and natural gas properties and equipment | $19,071,001 | $9,539,566 | $9,531,435 |
| Seismic resources | 878,545 | - | 878,545 |
| Other assets | 67,429 | 32,802 | 34,627 |
| | $20,016,975 | $9,572,368 | $10,444,607 |

Costs of acquiring seismic resources referenced in the above tables in the amount of $878,545 at December 31, 2007 and $878,545 at September 30, 2007 were excluded from the depletable costs. Costs of unproven properties in the amount of $199,278 at December 31, 2007 and $198,278 at September 30, 2007 are also excluded from depletable costs.

## 4. Lending Facility

The Company has a revolving operating demand facility of $3,250,000 that bears interest at the bank prime rate plus 1/2 percent. Repayments of the facility are not required provided the amounts borrowed do not exceed $3,250,000 or an amount to be determined from time to time. At December 31, 2007 there was $2,250,000 drawn on the revolving operating demand facility. In addition, there were net outstanding cheques in the amount of $6,912 to be drawn against this facility for total bank indebtedness of $2,256,912 at December 31, 2007. The loan facilities are secured by a $5,000,000 floating charge demand debenture over all the assets of the Company. At December 31, 2007, the Company was not in compliance with a banking covenant regarding working capital. The Corporation has received a letter from the bank agreeing to waive this default.

At December 31, 2007, the bank prime rate was 6.0%. The loan facilities are subject to an interim review by the bank scheduled to occur by April 30, 2008.

As the Company's lending facilities bear interest at floating rates, the Company is exposed to interest rate risk on outstanding balances.

## 5. Equity Instruments

a) Authorized

Unlimited number of common shares

Unlimited number of non-voting preferred shares, issuable in series. The Board of Directors may fix from time to time the number of shares that comprise a series and the rights, privileges, restrictions and conditions for the series. Preferred shares of any series may be convertible into or exchangeable for common shares.

b) Common shares

| | Shares | Amount |
|---|---|---|
| Balance, September 30, 2006 | 22,709,179 | $70,172,113 |
| Private placement issued for cash(4) | 5,000,000 | 972,816 |
| Private placement issued for cash on a flow through basis (4) | 4,583,333 | 1,077,345 |
| Rights offering(5) | 1,660,078 | 332,016 |
| Private placement issued for cash(6) | 3,335,000 | 626,740 |
| Private placement issued for cash on a flow through basis (7) | 3,234,200 | 970,260 |
| Private placement issued for cash on a flow through basis (7) | 3,765,800 | 1,129,740 |
| Private placement issued for cash(8) | 3,850,000 | 813,133 |
| Tax impact of flow through share issue | - | (319,000) |
| Share issuance costs (1) | - | (590,332) |
| Balance, September 30, 2007 and December 31, 2007 | 48,137,590 | $75,184,831 |

| | Shares | Amount |
|---|---|---|
| Balance, September 30, 2005 | 7,466,576 | $59,640,080 |
| December 2005 private placements issued for cash | 737,000 | 650,000 |
| December 2005 private placements issued for cash on a flow-through basis | 8,217,506 | 8,028,000 |
| Tax impact of flow through share issue | - | (2,700,000) |
| Share issuance costs (1) | - | (804,912) |
| Shares issued on acquisition of Regal Energy Corp. | 6,147,469 | 5,225,349 |
| Shares issued as success fee on transaction | 140,628 | 133,596 |
| Balance, September 30, 2006 | 22,709,179 | $70,172,113 |

c) Warrants

| | Number of Warrants | Number of Underlying Shares | Amount |
|---|---|---|---|
| Balance, September 30, 2006 | 1,723,566 | 1,723,566 | $ 406,300 |
| November 30, 2006 private placement(4) | 916,667 | 916,667 | 49,838 |
| February 1, 2007 private placement(6) | 333,500 | 333,500 | 40,260 |
| June 30, 2007 expiry of warrants | (817,923) | (817,923) | (188,000) |
| July 16, 2007 private placement(8) | 3,850,000 | 3,850,000 | 187,867 |
| Balance, September 30, 2007 | 6,005,810 | 6,005,810 | $ 496,265 |
| December 31, 2007 expiry of warrants(3) | (905,643) | (905,643) | (218,300) |
| Balance December 31, 2007 | 5,100,167 | 5,100,167 | 277,965 |

| | Number of Warrants | Number of Underlying Shares | | Amount |
|---|---|---|---|---|
| Balance, September 30, 2005 | - | - | | - |
| December 15, 2005 private placement [2] | 817,923 | 817,923 | $ | 188,000 |
| Warrants issued as success fee on acquisition of Regal Energy Corp.[3] | 905,643 | 905,643 | | 218,300 |
| Balance, September 30, 2006 | 1,723,566 | 1,723,566 | $ | 406,300 |
| Total Common Shares and Warrants ("Equity Instruments") outstanding at December 31, 2007 | | | | $75,462,796 |

At December 31, 2007, there are 5,100,167 common shares reserved for issuance for outstanding warrants.

(1) No tax benefit has been recorded as the ultimate realization of such benefit is uncertain.

(2) In connection with the private placement of common and flow-through common shares on December 15, 2005, the Company issued 817,923 warrants that entitle the holder to purchase one common share of the Company for each warrant held at a price of $0.88 until June 30, 2007. The fair value of the warrants was determined using the Black-Scholes option pricing model and assumes an expected volatility of 50%, a risk-free rate of return of 3.5% and a weighted average life of 1.5 years.

(3) In connection with the acquisition of Regal Energy Corp. the Company issued 905,643 warrants as a success fee that entitles the holder to purchase one common share of the Company for each warrant held at a price of $0.95 per share until December 31, 2007. The fair value of the warrants was determined using the Black-Scholes option pricing model and assumes an expected volatility of 50%, a risk-free rate of return of 3.5% and a weighted average life of 2.0 years.

(4) On November 30, 2006, the Company completed a financing of 5,000,000 common shares at a price of $0.20 per common share and 4,583,333 flow-through common shares at a price of $0.24 per common share. Nova Bancorp Securities Ltd. acted as agent in the financing and is a related party to the Corporation as two directors of the Corporation are also directors, officers and shareholders of Nova Bancorp Securities Ltd. In connection with the financing the agent was granted 916,667 warrants that entitle the holder to purchase one common share of the Company for each warrant held at a price of $0.20 until May 30, 2008. The fair value of the warrants was determined to be $49,838 of which $22,655 is attributed to the flow-through portion of the financing using the Black-Scholes option pricing model and assumes an expected volatility of 58%, a risk free rate of return of 5.0% and a weighted average life of 1.5 years.

(5) On December 21, 2006, the Company, under a rights offering, issued 1,660,078 common shares at a price of $0.20.

(6) Under the agreement with Nova Bancorp Securities Ltd. on November 30, 2006, Nova Bancorp Securities Ltd. had the right to subscribe for any shares not subscribed for under the December 21, 2006 rights offering on the same basis as the rights offering. On February 1, 2007, Nova Bancorp Securities Ltd. exercised this right and 3,335,000 common shares were issued at a price of $0.20. Nova Bancorp Securities Ltd. acted as agent in the financing and is a related party to the Corporation as two directors of the Corporation are also directors, officers and shareholders of Nova Bancorp Securities Ltd. In connection with this financing, the agent was granted 333,500 warrants that entitle the holder to purchase one common share of the Company for each warrant held at a price of $0.20 until August 1, 2008. The fair value of the warrants was determined to be $40,260 using the Black-Scholes option pricing model and assumes an expected volatility of 57%, a risk free rate of return of 5% and a weighted average life of 1.5 years.

(7) On June 28 and July 16, 2007, the Company completed a financing of 7,000,000 flow-through common shares at a price of $0.30 per share. Nova Bancorp Securities Ltd. acted as co-agent in

the financing and is a related party, as two directors of the Corporation are also directors, officers and shareholders of Nova Bancorp Securities Ltd.

(8) On July 16, 2007, the Company completed a financing of 3,850,000 common shares at a price of $0.26 per share. In connection with the financing the agent was granted 3,850,000 warrants that entitle the holder to purchase one common share of the Company for each warrant held at a price of $0.35 until July 16, 2009. The fair value of the warrants was determined to be $187,867 using the Black-Scholes option pricing model and assumes an expected volatility of 31%, a risk free rate of return of 5.0% and a weighted average life of 2 years.

d) Stock options

The following table summarizes the status of the Company's stock option plan and the activity during the current quarter and the year ended September 30, 2007.

| | **Three months ended December 31, 2007** | | **Year ended September 30, 2007** | |
|---|---|---|---|---|
| | **Number of Options** | **Weighted Average Exercise Price** | **Number of Options** | **Weighted Average Exercise Price** |
| Balance, beginning of period | 2,951,000 | $0.96 | 1,626,000 | $0.96 |
| Granted | - | - | 1,675,000 | 0.30 |
| Cancelled | (86,000) | - | (350,000) | 0.95 |
| Balance, end of period | 2,865,000 | $0.57 | 2,951,000 | $0.58 |
| Exercisable, end of period | 2,155,000 | $0.61 | 2,241,000 | $0.63 |

During the quarter ended December 31, 2007, the Company recognized $22,895 of stock compensation expense for options granted under the Company's stock option plan.

e) Contributed surplus

The following table presents changes in contributed surplus:

| | **2007** | **2006** |
|---|---|---|
| Balance, September 30 | $1,216,220 | $823,552 |
| Replacement employee options | - | - |
| Stock based compensation - directors | - | - |
| Stock based compensation – employees and consultants | 22,895 | 27,038 |
| Expiry of warrants | 218,300 | |
| Balance, December 31 | $1,457,415 | $850,590 |

## 6. Capital Risk Management

The Company's objectives when managing capital is to safeguard the entity's ability to continue as a going concern, so that it can continue to provide returns for shareholders and benefits for other stakeholders. The Company sets the amount of capital in proportion to risk. The Company manages the capital structure and makes adjustments to it in light of changes in economic conditions and the risk characteristics of the underlying assets. The Company's objective is met by retaining adequate equity to provide for the possibility that cash flows from assets will not be sufficient to meet future cash flow requirements. The Board of Directors does not establish quantitative return on capital criteria for management; but rather promotes year over year sustainable profitable growth. The Company is not subject to any externally imposed capital requirements other than covenants on its operating demand facility with its lender to maintain its working capital ratio at a 1.0:1.0 level.

## 7. Asset Retirement Obligation

The following table presents the reconciliation of the beginning and ending aggregate carrying amount of the obligation associated with the retirement of oil and gas properties:

| | Dec. 31, 2007 | Dec. 31, 2006 |
|---|---|---|
| Asset retirement obligation, beginning of period | $397,558 | $287,450 |
| Liabilities incurred on drilling | 7,761 | 39,756 |
| Liabilities assumed on acquisition | | 26,104 |
| Accretion expense | 9,078 | 7,288 |
| Asset retirement obligation end of period | $414,397 | $360,598 |

The undiscounted amount of cash flows, required over the estimated reserve life of the underlying assets, to settle the obligation, adjusted for inflation is estimated to be $694,000. The obligation was calculated using a credit adjusted risk free discount rate of 9 percent and an inflation rate of 2 percent. It is expected that this obligation will be funded from general Company resources at the time the costs are incurred with the majority of costs expected to occur between 2010 and 2021.

## 8. Income Tax

Future income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts for income tax purposes. The components of the Company's future income tax assets and liabilities are as follows:

| | Dec. 31, 2007 | Sep. 30, 2007 |
|---|---|---|
| Property and equipment | $ (470,354) | $ (861,960) |
| Non-capital loss carry forwards | 8,850,486 | 9,587,672 |
| Scientific research and development pools | 4,913,887 | 5,386,377 |
| Share issue costs | 253,956 | 294,639 |
| | $ 13,547,975 | $ 14,406,728 |
| Valuation allowance | (12,949,475) | (13,808,228) |
| Net future tax asset | $ 598,500 | $ 598,500 |

The Company has scientific research and experimental development expenditures (SR&ED), non-refundable investment tax credits (Non-Refundable ITC's), non-capital loss carry forwards (Non-Capital Losses), and depreciable property and resource property tax pools (Other Tax Pools) available for income tax purposes which may be carried forward to reduce future years' taxable income. The approximate amounts and the related expiry dates of these tax pools are as follows:

| Expiry Date | SR&ED | Non-Refundable ITC's | Non-Capital Losses | Other Tax Pools | Total |
|---|---|---|---|---|---|
| 2008 | $ - | $ - | $10,018,000 | $ - | $10,018,000 |
| 2009 | - | 231,000 | 9,766,000 | - | 9,997,000 |
| 2010 | - | 340,000 | 5,720,000 | - | 6,060,000 |
| 2011 | - | 1,032,000 | - | - | 1,032,000 |
| 2012 | - | 876,000 | - | - | 876,000 |
| 2013 | - | 196,000 | - | - | 196,000 |
| 2014 | - | 45,000 | 4,672,000 | - | 4,717,000 |
| 2015 | - | - | 1,898,000 | - | 1,898,000 |
| 2016 | - | - | 1,263,000 | - | 1,263,000 |
| 2027 | - | - | 395,000 | - | 395,000 |
| 2028 | - | - | 399,000 | - | 399,000 |
| No expiry date | 18,899,500 | - | - | 7,576,000 | 26,475,500 |
| | $18,899,500 | $2,720,000 | $34,131,000 | $7,576,000 | $63,326,500 |

The future tax benefit of the non-capital losses or other tax pools being carried forward has not been recognized in these financial statements as the criteria for recognition has not been met. The research and development cost pool will be reduced by the amount of any investment tax credits utilized. The future tax benefit of $598,500 of the research and development pools has been recognized in these financial statements as the criteria for recognition has been met.

Canada Revenue Agency ("CRA") has conducted an audit of transfer pricing on international transactions between SiberCore Technologies Incorporated and its United States subsidiary, SiberCore America Inc. for the years 2000, 2001 and 2002. SiberCore Technologies Incorporated was the predecessor company of Azeri and ultimately Regal Energy Ltd. The Company has received a proposed settlement letter from CRA that would result in a reduction of tax pools in the amount of $1,501,453. CRA has also proposed to charge a cash penalty of 10% of the adjustments. The Company has responded to the proposed settlement letter and provided further information supporting management's view that CRA's position has no merit and intends to object to any notice of assessment that may be received. The outcome of this audit is uncertain at this time and as such no provisions have been made in these financial statements.

## 9. Supplemental Cash Flow Information

| December 31 | | 2007 | | 2006 |
|---|---|---|---|---|
| Changes in non-cash working capital balances related to: | | | | |
| Accounts receivable | $ | (797,715) | $ | (997,012) |
| Deposits and prepaid expenses | | (13,386) | | 9,251 |
| Accounts payable and accrued liabilities | | 1,083,814 | | 2,363,212 |
| | $ | 272,713 | $ | 1,375,451 |
| Changes in non-cash working capital balances related to: | | | | |
| Operating activities | $ | 260,095 | $ | (114,069) |
| Investing activities | | 12,618 | | 1,489,520 |
| | $ | 272,713 | $ | 1,375,451 |

| | | 2007 | | 2006 |
|---|---|---|---|---|
| Interest paid | $ | 28,150 | $ | 45,434 |
| Income taxes paid | $ | - | $ | - |

## 10. Commitments and Contingencies

Pursuant to a flow-through financing completed on June 28, 2007 and July 16, 2007, the Company is committed to spend $2,100,000 on qualified exploration and development expenditures by December 31, 2008. As at December 31, 2007, the Company has expended approximately $1,445,000 relating to these commitments.

At December 31, 2007, the Company had commitments for a rental compressor totaling $29,200 in 2008.

Other than the audit by the CRA on transfer pricing on international transactions from a predecessor company as detailed in Notes (8 and 11), the Company has no other contingencies that management is aware of.

## 11. Subsequent Events

a) On February 29, 2008, the Company entered into agreements with Companies controlled by three directors to provide bridge financing to provide necessary working capital to fund its short term needs.

Under the terms of the agreement, $400,000 will be advanced. A commitment fee of 3% will be paid at the time of the advance and amounts outstanding bear interest at bank prime rate plus 3%. The bridge facility has a maturity date of 90 days subsequent to the advance of funds under the facility and may be renewed for a further 90 days upon mutual consent of the parties. In the event a renewal of terms is agreed to, the Corporation has agreed to pay the lenders a renewal fee of 3% of the then outstanding funds of the bridge facility and the interest rate will be increased to bank prime rate plus 6%. The bridge facility has been secured by a general security agreement over the assets of the Corporation and the lenders were issued promissory notes for the amount of the bridge facility.

b) Subsequent to quarter end, The Company has received reassessment notices on the audit of transfer pricing on international transaction between SiberCore Technologies Incorporated and its United States subsidiary, SiberCore America Inc. for 2001 and 2002 from CRA that result in a reduction of tax pools in the amount of $1,416,627. CRA has also assessed a cash penalty of $140,902. It is management's view that CRA's position has no merit and the Company intends to file an objection to the notices of reassessment.

## CORPORATE INFORMATION

### CORPORATE HEADQUARTERS

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### DIRECTORS

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***Al J. Kroontje*** (1)(2) (3)
***Douglas O. McNichol*** (2)
***Robert M. Nicolay*** (1)(2)
***Richard M. Wlodarczak*** (1)(3)(4)

*(1) Audit Committee*
*(2) Reserves Committee*
*(3) Compensation & Governance Committee*
*(4) Chairman of the Board*

### OFFICERS & SENIOR MANGEMENT

***Douglas O. McNichol***
President & CEO

***Wayne R. Wilson***
Vice President Finance & CFO

***Greg C. Glenn***
Vice President Land

### AUDITORS

***Deloitte & Touche LLP***
Calgary, Alberta

### BANKER

***National Bank of Canada***
Calgary, Alberta

### EVALUATION ENGINEERS

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### LEGAL COUNSEL

***Burstall Winger LLP***
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### STOCK ECHANGE LISTING

***TSX Venture Exchange***
Trading Symbol: **REG**

# First Quarter 2008


**CORPORATE HEADQUARTERS**

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