Aquila
Resources Inc.

# AQUILA RESOURCES INC.

**(an exploration stage enterprise)**
**CONSOLIDATED FINANCIAL STATEMENTS (PREPARED BY MANAGEMENT)**
**For the three month period ended**
**MARCH 31, 2008**
**(Unaudited)**

## Responsibility for Financial Statements

The accompanying financial statements for Aquila Resources Inc. have been prepared by management in accordance with Canadian generally accepted accounting principles consistently applied. The most significant of these policies have been set out in the March 31, 2007 audited financial statements. These statements are presented on an accrual basis of accounting. Accordingly, a precise determination of many assets and liabilities is dependent upon future events. Therefore, estimates and approximations have been made using careful judgment.
Recognizing that the Company is responsible for both the integrity and objectivity of the financial statements, management is satisfied that these financial statements have been fairly stated.

## Disclosure Required Under National Instrument 51-102 - Continuous Disclosure Obligations - Part 4.3(3)(a)

The auditor of Aquila Resources Inc. has not performed a review of the unaudited comparative financial statements for the three month period ended March 31, 2008.

## INDEX

**Aquila Resources Inc.**
**(an exploration stage enterprise)**
**CONSOLIDATED BALANCE SHEETS (PREPARED BY MANAGEMENT)**
**AS AT MARCH 31, 2008**
(Unaudited)

| | March 31, 2008 (unaudited) | March 31, 2007 (unaudited) | December 31, 2007 (audited) |
|---|---|---|---|
| **ASSETS** | | | |
| **Current** | | | |
| Cash and cash equivalents | $ 10,869,877 | $ 23,355,034 | $ 13,416,459 |
| Accounts receivable | 27,478 | 117,764 | 78,280 |
| Funds held in trust | - | 300,000 | - |
| Prepaid expenses and deposits | 67,795 | 30,408 | 49,604 |
| | 10,965,150 | 23,803,206 | 13,544,343 |
| **Deposits** | 116,540 | 116,540 | 116,540 |
| **Mineral property costs**, (Note 2) | 21,200,991 | 10,173,443 | 18,136,287 |
| Capital assets | 1,002,709 | 781,100 | 776,005 |
| | $ 33,285,390 | $ 34,874,289 | 32,573,175 |
| **Liabilities** | | | |
| **Current** | | | |
| Accounts payable and accrued liabilities | $ 1,618,030 | $ 416,743 | $ 919,386 |
| Current portion of mortgages payable | - | 25,858 | - |
| | 1,618,030 | 442,601 | 919,386 |
| Long term portion of mortgages payable | - | 359,734 | - |
| **Shareholders' Equity** | | | |
| Share capital, (Note 3) | 36,461,711 | 36,025,032 | 36,461,711 |
| Contributed surplus, (Note 4) | 4,134,973 | 4,009,925 | 3,826,573 |
| Deficit | (8,929,324) | (5,963,003) | 8,634,495 |
| | 31,667,360 | 34,071,954 | 31,653,789 |
| | $ 33,285,390 | $ 34,874,289 | 32,573,175 |

**Approved on behalf of the board:**

"*Edward J. Munden*" Director
"*Robin Dunbar*" Director

See accompanying notes to the financial statements

**Aquila Resources Inc.**
**(an exploration stage enterprise)**
**CONSOLIDATED STATEMENT OF LOSS (PREPARED BY MANAGEMENT)**
**FOR THE THREE MONTH PERIOD ENDED MARCH 31, 2008**
(Unaudited)

| | Three Months March 31, 2008 | Three Months March 31, 2007 | Cumulative from the Date of Commencement of Development Stage January 16, 2004 |
|---|---|---|---|
| **Expenses** | | | |
| Consulting fees | $ 14,400 | $ 20,850 | $ 180,470 |
| Directors' fees | 21,000 | - | 106,250 |
| Licenses, taxes and fees | - | - | 85,000 |
| Write-down of mineral property costs | - | - | 768,774 |
| Rent | 5,588 | 5,596 | 38,468 |
| Foreign exchange loss | (157,505) | 104,022 | 1,221,303 |
| Management fees | 18,750 | 18,750 | 549,066 |
| Professional fees | 1,663 | 33,281 | 337,911 |
| Office, general and administration | 13,771 | 15,270 | 181,059 |
| Interest and bank charges | 603 | 142 | 92,304 |
| Filing and regulatory fees | 22,096 | 26,035 | 262,221 |
| Amortization | 925 | 63 | 22,049 |
| Stock-based compensation | 308,400 | 2,139,402 | 4,892,927 |
| Travel and promotion | 89,997 | 19,509 | 513,842 |
| Salaries and wages | 64,565 | 37,863 | 772,922 |
| | 404,253 | 2,420,783 | 10,024,566 |
| Interest and other income | (109,424) | (252,235) | 4,892,927 |
| **Loss for the three month period** | 294,829 | 2,168,548 | $ 10,024,566 |
| Deficit, beginning of period | 8,634,495 | 3,794,455 | |
| Deficit, ended of period | $ 8,929,324 | $ 5,963,003 | |
| **Loss per share** | | | |
| Basic and fully diluted | $ (0.00) | $ (0.03) | |
| Weighted average number of shares | 70,109,478 | 69,521,453 | |

See accompanying notes to the financial statements

**Aquila Resources Inc.**
**(an exploration stage enterprise)**
**CONSOLIDATED STATEMENT OF CASH FLOWS (PREPARED BY MANAGEMENT)**
**FOR THE THREE MONTH PERIOD ENDED MARCH 31, 2008**
(Unaudited)

| | Three Months March 31, 2008 | Three Months March 31, 2007 | Cumulative from the Date of Commencement of Development Stage January 16, 2004 |
|---|---|---|---|
| **Cash flows from operating activities** | | | |
| Loss for the three month period | $ (294,829) | $ (2,168,548) | $ (8,983,709) |
| Amortization | 925 | 63 | 22,049 |
| Financing fee | - | - | 20,424 |
| Stock-based compensation | 308,400 | 2,139,402 | 4,892,927 |
| Writedown of mineral resource properties | - | - | 768,774 |
| Interest accrual | - | - | 1,913 |
| | 14,496 | (29,083) | (3,277,622) |
| Changes in non-cash working capital balances, (Note 10) | 731,255 | (166,727) | 1,398,408 |
| Cash flows provided from operating activities | 745,751 | (195,810) | (1,879,214) |
| **Cash flows from investing activities** | | | |
| Purchase of capital assets | (227,629) | - | (339,966) |
| Mineral properties - acquisition costs | (271,500) | (48,697) | (4,359,763) |
| Mineral properties - exploration costs | (2,793,204) | (843,529) | (14,142,020) |
| Deposits | - | - | (116,540) |
| | (3,292,333) | (892,226) | (18,958,289) |
| **Cash flows from financing activities** | | | |
| Issuance of common shares | - | 418,100 | 34,165,883 |
| Issue costs | - | - | (2,188,236) |
| Notes payable | - | - | 117,110 |
| Increase in common shares | - | - | (461,548) |
| Loans payable | - | - | 74,171 |
| Repayment of mortgage payable | - | (9,631) | - |
| | - | 408,469 | 31,707,380 |
| Net (decrease) increase in cash | (2,546,582) | (679,567) | 10,869,877 |
| Cash , beginning of period | 13,416,459 | 24,034,601 | - |
| **Cash, ended of three month period** | $ 10,869,877 | $ 23,355,034 | $ 10,869,877 |

See accompanying notes to the financial statements

## Nature and continuance of operations:

The Company is involved in the mineral exploration business and controls mineral and surface rights at the Back Forty Project located in Menominee County, Michigan. In addition, the Company has entered into an agreement to acquire the Cedros property in Honduras; however, at the current time the Company has not yet secured title and has fully written down the property.

The Company is in the business of exploring for and developing mineral properties. Substantially all of the efforts of the Company are devoted to these business activities. To date the Company has not earned significant revenue and is considered for accounting purposes to be in the exploration stage. The ability of the Company to carry out its business plan rests with its ability to secure equity and other financing.

The Company uses the same methods and policies as were used in the December 31, 2007 audited financial statements.

## 1. Change in Accounting Policies:

### Financial Instruments

Effective January 1, 2008, Aquila Resources Inc. prospectively adopted the new CICA Handbook Sections 3862, Financial Instruments – Disclosures and 3863, Financial Instruments – Presentation. The purpose of these sections is to enhance the financial statement users' ability to evaluate:

- the significance of financial instruments over an entity's financial position, performance and cash flows;
- the nature and extent of risks arising from financial instruments to which the entity if exposed during the period and at the balance sheet date; and
- how the entity manages those risks.

The new standards required additional disclosure with no effect on the financial statements.

### Capital Management

Effective January 1, 2008, Aquila Resources Inc. adopted the new CICA Handbook Section 1535, Capital Disclosures for disclosure of a company's objectives, policies and processes for managing capital.

### Effect of Future Changes in Accounting Policies

The CICA Accounting Standards Board has adopted the following new or amended Handbook Sections:

In February 2008, the CICA issued Section 3064, Goodwill and intangible assets, ("Section 3064") replacing Section 3062, Goodwill and other intangible assets ("Sections 3062") and Section 3450, Research and development costs. Various changes have been made to other standards to be consistent with the new Section 3064. Section 3064 will be applicable to financial statements relating to fiscal years beginning on or after October 1, 2008. Accordingly, Aquila Resources Inc. will adopt the new standards for its fiscal year beginning January 1, 2009. Section 3064 establishes standards for the recognition, measurement, presentation and disclosure of goodwill and of intangible assets. Standards concerning goodwill are unchanged from the standards included in the previous Section 3062. Aquila Resources Inc. is currently evaluating the impact of the adoption of this new Section on its consolidated financial statements; however, we do not expect that the adoption of this new Section will have a material impact on its consolidated financial statements.

In January 2006, the Accounting Standards Board adopted a strategic plan for the direction of accounting standards in Canada. Public companies in Canada are required to adopt International Financial Reporting Standards effective January 1, 2011.

## 2. Mineral property costs and commitments:

**Michigan, USA**

*Back Forty Project*

The Back Forty Project consists of approximately 9,700 acres of surface and mineral rights owned or held under lease or option by a 100% owned U.S. subsidiary. Some lands are subject to net smelter royalties varying from 1% to 3.5%, with certain lands subject to a 2% - 7% state royalty, which under state law can be renegotiated. Annual option and property acquisition costs for 2007 were $2,117,244 (2006-$1,971,019). The entire project is subject to a 7% net distributable earnings royalty ("Net Profits after Payback") payable to a former joint venture partner.

| **2008** | Balance beginning of period | Acquisition | Exploration | Recoveries | Write-down | Balance end of period |
|---|---|---|---|---|---|---|
| **Michigan, USA** | | | | | | |
| Back Forty Project | $ 18,136,287 | $ 271,500 | $ 2,793,204 | $ - | $ - | $ 21,200,991 |
| | $ 18,136,287 | $ 271,500 | $ 2,793,204 | $ - | $ - | $ 21,200,991 |

| **2007** | Balance beginning of year | Acquisition | Exploration | Recoveries | Write-down | Balance end of year |
|---|---|---|---|---|---|---|
| **Michigan, USA** | | | | | | |
| Back Forty Project | $ 8,512,443 | $ 2,117,244 | $ 7,506,600 | $ - | $ - | $ 18,136,287 |
| **Honduras** | | | | | | |
| Cedros Property | 768,774 | - | - | - | (768,774) | - |
| | $ 9,281,217 | $ 2,117,244 | $ 7,506,600 | $ - | $ (768,774) | $ 18,136,287 |

**Michigan, USA**

*Back Forty Project*

a) On August 3, 2006, the Company entered into an option agreement to acquire a 100% interest in approximately 50 acres of surface and mineral rights in Lake Township, Menominee County, Michigan (the "MRT property"). The aggregate price payable due in annual installments on the anniversary date and, over a nine year option period, is as follows: A total cash payment of US $11,700,000 payable: US $1,333,333 which was paid August 3, 2006, US $1,333,333 on each of the 1st and 2nd anniversaries, US $250,000 on each of the 3rd and 4th anniversaries, and US $1,440,000 on each of the 5th through 9th anniversaries. During 2007 the Company made a cash payment of US $1,333,333 to maintain its interest in the property.

The Company maintains a cash deposit in the amount of $116,540 (US$100,000), pursuant to an escrow agreement. The amount is being held as security for the fulfillment of obligations in accordance with the above noted option agreement.

b) The Company purchased a property, held under option by a geological consulting company of which the President, CEO and another Director are major shareholders for $586,421, including costs. The Company had made a $50,000 option payment on this property in 2006.

c) On October 7, 2006, the Company entered into an option agreement to acquire a 100% interest in 181 acres of surface and mineral rights in Lake Township, Menominee County, Michigan. In order to earn a 100% interest in the project area from the option, the Company entered into a three-year option agreement, for an aggregate price payable of US $2,300,000 payable: US $300,000 in year one, of which US $50,000 has been paid, US $1,000,000 in year two, and US $1,000,000 in year three.

The Company renegotiated the option payment to US$12,000 for 2007 for a short term extension. During the quarter the Company elected to terminate the option. No further commitments or encumbrances remain.

## 3. Share Capital:

a) Authorized
Unlimited number of common shares

b) Issued
Common shares

| | Number of Common Shares | $ |
|---|---|---|
| Issued at December 31, 2006 | 69,313,311 | 35,582,542 |
| Issued for cash / on exercise of options | 796,167 | 452,600 |
| Fair value of options exercised | - | 428,647 |
| Issue costs | - | (2,078) |
| Issued at March 31, 2008 and December 31, 2007 | 70,109,478 | $ 36,461,711 |

c) Stock-option plan:

The Company maintains a Stock Option Plan (the "Plan") for the benefit of directors, officers, employees, consultants and other service providers of the Company and its subsidiaries in order to assist the Company in attracting, retaining, and motivating such persons by providing them with the opportunity, through stock options to acquire an increased proprietary interest in the Company. Under the Plan, options are non-assignable and may be granted for a term not exceeding five years. The number of common shares that may be reserved for issuance to any one person must not exceed 5% of the outstanding common shares. The exercise price of an option may not be lower than the closing price of the common shares on the TSX, subject to applicable discounts, on the business day immediately proceeding the date the option is granted. The options are non-transferable.

The fair value of each option was estimated on the date of grant. Under Black-Scholes the options issued during the three month period ended March 31, 2008 have been valued at $514,000, and of that amount $308,4000 has been vested and expensed to loss, using the following assumptions at the measurement date:

| | 2008 | 2007 |
|---|---|---|
| Risk-free interest rate | 3.26% | 4.12% |
| Expected life | 5 years | 4.3 years |
| Price volatility | 115% | 115% |
| Dividend yield | Nil | Nil |

A summary of the status of the Company's stock option plan as of March 31, 2008 and December 31, 2007 and changes during the period are presented below:

| | March 2008 | | December 2007 | |
|---|---|---|---|---|
| | Shares | Weighted average exercise price | Shares | Weighted average exercise price |
| Outstanding at beginning of the period | 4,550,000 | 1.17 | 3,646,167 | $ 0.35 |
| Exercised | - | - | (796,167) | 0.37 |
| Expired | - | - | - | - |
| Granted | 700,000 | 0.90 | 1,700,000 | 2.04 |
| Outstanding at end of the period | 5,250,000 | 1.13 | 4,550,000 | $ 1.17 |

## 4. Contributed Surplus:

| | March 2008 | December 2007 |
|---|---|---|
| Balance, beginning of the period | $ 3,826,573 | $ 1,894,913 |
| Stock-based compensation cost | 308,400 | 2,360,307 |
| Fair value of stock options exercised | - | (428,647) |
| Balance, end of the period | $ 4,134,973 | $ 3,826,573 |

## 5. Capital Management:

Aquila Resources Inc.'s objectives when managing capital are:

a) To safeguard Aquila Resources Inc.'s financial capacity and liquidity for future earning in order to continue to provide an appropriate return to shareholders and other stakeholders;

b) To maintain a flexible capital structure which optimizes the cost of capital at an acceptable risk; and

c) To enable Aquila Resources Inc. to maximize growth by meeting its capital expenditure budget and to expend its budget to accelerate projects, and take advantage of acquisition opportunities.

Aquila Resources Inc.'s capital structure includes shareholders' equity, cash and cash equivalent.

| | March 2008 | December 2007 |
|---|---|---|
| Shareholders' equity | 31,667,360 | 31,653,789 |
| Cash and cash equivalents | 10,869,877 | 13,416,459 |
| **Capital** | 42,537,237 | 45,070,248 |

Aquila Resources Inc. regularly monitors and reviews the amount of capital in proportion to risk and future development and exploration opportunities. Aquila Resources Inc. manages the capital structure and makes adjustments to it in the light of changes in economic conditions and the risk characteristics of the underlying assets. In order to maintain or adjust the capital structure, Aquila Resources Inc. may issue new debts or equity or similar instruments, reduce debt levels from or make adjustments to its capital expenditure program.

Aquila Resources Inc.'s objectives with regard to capital management remain unchanged from 2007.

## 6. Financial Instruments:

Aquila Resources Inc. manages its exposure to a number of different financial risks arising from its operations as well as its use of financial instruments including market risks (commodity prices, foreign currency exchange rate and interest rate), credit risk and liquidity risk through its risk management strategy. The objective of the strategy is to support the delivery of Aquila Resources Inc. financial targets while protecting its future financial security and flexibility.

Financial risks are primarily managed and monitored through operating and financing activities and, if required, through the use of derivative financial instruments. Aquila Resources Inc. does not use derivative financial instruments for purposes other than risk management. The financial risks are evaluated regularly with due consideration to changes in the key economic indicators and up-to-date market information.

Aquila Resources Inc.'s risk exposure and risk management policies and procedures have not changed from 2007.

### Market risk

Market risk the risk or uncertainty arising from possible market price movements and their impact on the future performance of the business. Aquila Resources Inc. may use derivative financial instruments such as foreign exchange contracts and interest rate swaps to manage certain exposures. These market risks are evaluated by monitoring changes in key economic indicators and market information on an on-going basis.

The maximum exposure to credit risk is equal to the carrying amount of financial instruments classified as receivables.

## Liquidity risk

Liquidity risk encompasses the risk that a company cannot meet its financial obligations in full. Aquila Resources Inc.'s main sources of liquidity are its common stock issuances. These funds are primarily used to finance working capital, operating expanses, capital expenditures, dividends and acquisitions.

Aquila Resources Inc. manages its liquidity risk by regularly monitoring its cash flows from operating activities, holding adequate amounts of cash and cash equivalents. The current year's budget will be funded by cash and cash equivalents.

Accounts payable and accrued liabilities are current financial instruments expected to be settled in the normal course of operations.

## Fair value

The carrying value and fair value of these financial instruments at March 31, 2008 is disclosed below by financial instrument category as well as any related interest expense for the three month period ended March 31, 2008:

| | Period ended March 31, 2008 | | | Year ended December 31, 2007 | |
|---|---|---|---|---|---|
| **Financial Instrument** | **Carrying Value** | **Fair Value** | **Int./Carrying Expense** | **Value** | **Fair Value** |
| **Financial Assets** | | | | | |
| *Held for trading* | | | | | |
| Cash and cash equivalents | 10,869,877 | 10,869,877 | - | 13,416,459 | 13,416,459 |
| *Loan and receivable* | | | | | |
| Accounts receivable | 27,478 | 27,478 | - | 78,280 | 78,280 |
| **Financial Liabilities** | | | | | |
| Other liabilities | | | | | |
| Accounts payable and accrued liabilities | 1,618,030 | 1,618,030 | - | 919,386 | 919,386 |

There has been no change to the classification of financial instruments since inception on January 1, 2007.

The fair values of financial instruments were calculated on the basis of market information available on the balance sheet date using the methods and premises presented below.

a) Cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities

Due to the short term nature of these financial instruments, fair value approximates carrying value.

## 7. Related party transactions:

For the three month period ended March 31, 2008 management fees amounting to $18,750 (2007 - $18,750) were charged by a company controlled by the CFO and a director of the Company.

During the three month period ended March 31, 2008, the President and CEO received salary of $57,413. The spouse of the President and CEO of the Company is the Assistant Corporate Secretary who received salary of $18,644.

A total of US $456,027 (2007 US $688,081) was charged in the operations at the Back Forty Project by a geological consulting company of which the President and CEO and another director are major shareholders.

During the three month period ended March 31, 2008 the Company was charged Directors' fees totaling $21,000 (2007 - $NIL) by non-executive directors.

During the three month period ended March 31, 2008, the Company was charged legal fees totaling $1,663 (2007-$21,190) by a law firm whose partner is a director of the Company.

Rental expenditures in the amount of $5,588 (2007-$5,596) were charged by a Company with common directors.

Management believes these transactions are in the normal course of business and are measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties.

## 8. Income taxes:

The Company has non-capital losses of approximately $3,679,859 which expire through 2028. The benefit of these losses has not been recognized for financial statement purposes.

For the three month period ended March 31, 2008, the Company's provision for income taxes differ from the amounts computed by applying the basic current rates to loss for the year before taxes, as shown in the following table:

| | | |
|---|---|---|
| Statutory rate applied to loss for the year before income taxes | $ | (106,138) |
| Increase in taxes resulting from: | | |
| Non-deductible stock based compensation | | 111,024 |
| Non-deductible items | | - |
| Write down of mineral property | | - |
| Share issue costs | | - |
| Tax benefit not recognized on current year's losses | | (4,886) |
| | $ | - |

The company has provided a full valuation allowance against future tax assets as at March 31, 2008 due to uncertainties in the Company's ability to utilize its net operating losses.

## 9. Comparative figures:

Certain comparative figures have been reclassified to conform to the current period's presentation. These reclassifications did not affect the prior year's net losses.

## 10. Changes in non-cash operating working capital:

| | March 31 2008 | December 31 2007 |
|---|---|---|
| Accounts receivable | $ 50,802 | $ (67,242) |
| Funds held in trust | - | (300,000) |
| Prepaid expenses | (18,191) | (41,982) |
| Accounts payable and accrued liabilities | 698,644 | 361,698 |
| | $ 731,255 | $ (47,526) |

## 11. Supplemental cash flow information:

Non-cash activities were as follows:

| | March 2008 | December 2007 |
|---|---|---|
| Amortization capitalized to resource properties | 2,584 | 10,249 |