

---

**WCSB Oil & Gas Royalty Income 2010-II  
Limited Partnership  
Condensed Interim Financial Statements**  
*September 30, 2011*

# WCSB OIL & GAS ROYALTY INCOME 2010-II LIMITED PARTNERSHIP

## Condensed Interim Statement of Financial Position

(unaudited)

(Canadian dollars)	Note	September 30, 2011	December 31, 2010
<b>ASSETS</b>			
<b>Current assets</b>			
Cash and cash equivalents		482,567	66,387
Short-term investment		-	5,000,000
Trade and other receivables		1,187,265	753,372
Prepaid expenses		7,500	18,268
		1,677,332	5,838,027
<b>Non-current assets</b>			
Royalty interests	6	13,788,922	11,350,233
<b>Total Assets</b>		15,466,254	17,188,260
<b>LIABILITIES</b>			
<b>Current liabilities</b>			
Trade and other payables		90,420	44,842
Due to related parties	10	-	13,040
Due to General Partner	10	227,770	47,908
		318,190	105,790
<b>Partners' equity</b>			
Partnership units	7	17,162,709	17,162,709
Deficit		(2,014,645)	(80,239)
		15,148,064	17,082,470
<b>Total Liabilities and Partners' Equity</b>		15,466,254	17,188,260

The accompanying notes are an integral part of these condensed interim financial statements. The condensed interim financial statements were approved by the Board on November 28, 2011 and were signed on its behalf.

Director (signed) "Shane Doyle" \_\_\_\_\_

Director (signed) "Hugh Cartwright" \_\_\_\_\_

**WCSB OIL & GAS ROYALTY INCOME 2010-II LIMITED PARTNERSHIP**  
**Condensed Interim Statement of Comprehensive Loss**  
(unaudited)

(Canadian dollars)	Note	Three months ended September 30, 2011	Nine months ended September 30, 2011	Period from Commencement of operations on May 31, 2010 to December 31, 2010
Royalty income		1,354,903	4,959,647	719,458
Interest		-	5,760	45,380
<b>Total revenue</b>		<b>1,354,903</b>	<b>4,965,407</b>	<b>764,838</b>
Depletion	6	(701,057)	(2,751,994)	(405,270)
Filing fees		(2,387)	(3,767)	(4,653)
General and administrative		(67,732)	(188,844)	(118,153)
Management fee		(95,881)	(287,643)	(191,894)
Professional fees		(25,588)	(30,724)	(43,682)
Registrar and transfer agent		-	(2,640)	(3,385)
Royalties		(135,491)	(495,965)	(71,950)
Software licensing		(6,089)	(18,268)	(6,090)
<b>Total comprehensive income (loss) for the period</b>		<b>320,678</b>	<b>1,185,562</b>	<b>(80,239)</b>
<b>Basic and fully diluted income (loss) per unit</b>		<b>1.67</b>	<b>6.18</b>	<b>(0.42)</b>
Basic and fully diluted units outstanding		191,762	191,762	164,200

The accompanying notes are an integral part of these condensed interim financial statements.

**WCSB OIL & GAS ROYALTY INCOME 2010-II LIMITED PARTNERSHIP**  
**Condensed Interim Statement of Changes in Equity**  
(unaudited)

(Canadian dollars)	Note	Limited Partnership Units \$	Deficit \$	Total Partners' Equity \$
<b>As at December 31, 2010</b>		17,162,709	(80,239)	17,082,470
Distributions			(1,447,803)	(1,447,803)
Total comprehensive income (loss) for the period			864,884	864,884
<b>As at June 30, 2011</b>		17,162,709	<b>(663,158)</b>	<b>16,499,551</b>
Distributions			(1,672,165)	(1,672,165)
Total comprehensive income (loss) for the period			320,678	320,678
<b>As at September 30, 2011</b>		17,162,709	<b>(2,014,645)</b>	<b>15,148,064</b>

The accompanying notes are an integral part of these condensed interim financial statements.

**WCSB OIL & GAS ROYALTY INCOME 2010-II LIMITED PARTNERSHIP**  
**Condensed Interim Statement of Cash flows**  
(unaudited)

(Canadian dollars)	Note	Three months ended September 30, 2011	Nine months ended September 30, 2011	Period from Commencement of operations on May 31, 2010 to December 31, 2010
<b>Cash provided by (used for) the following activities</b>				
<b>Operating activities</b>				
Total comprehensive income for the period		320,678	1,185,562	(80,239)
Add (deduct):				
Depletion	6	701,057	2,751,994	405,270
		<u>1,021,735</u>	<u>3,937,556</u>	<u>325,031</u>
Change in non-cash working capital				
Change in trade and other receivables		454,951	(433,893)	(753,372)
Change in prepaid expenses		(1,411)	10,768	(18,268)
Change in due to related parties		(35,796)	(13,040)	13,040
Change in due to General Partner		(17,472)	179,862	47,908
Change in trade and other payables		52,000	45,578	44,842
		<u>1,474,007</u>	<u>3,726,831</u>	<u>(340,819)</u>
<b>Investment activities</b>				
Short-term investment		-	5,000,000	(5,000,000)
Additions to royalty interests	6	54,057	(5,190,683)	(11,755,503)
<b>Cash from (used in) investing activities</b>		<u>54,057</u>	<u>(190,683)</u>	<u>(16,755,503)</u>
<b>Financing activities</b>				
General Partner contribution		-	-	10
Issue of initial Partnership unit		-	-	100
Redemption of Partnership unit		-	-	(100)
Proceeds from issue of Partnership units		-	-	19,176,200
Issue costs		-	-	(2,013,501)
Distributions		(1,672,165)	(3,119,968)	-
<b>Cash from (used in) financing activities</b>		<u>(1,672,165)</u>	<u>(3,119,968)</u>	<u>17,162,709</u>
Increase (decrease) in cash and cash equivalents		(144,101)	416,180	66,387
Cash and cash equivalents, beginning of period		626,668	66,387	-
<b>Cash and cash equivalents, end of period</b>		<u>482,567</u>	<u>482,567</u>	<u>66,387</u>

# WCSB OIL & GAS ROYALTY INCOME 2010-II LIMITED PARTNERSHIP

## Notes to the Condensed Interim Financial Statements (unaudited)

For the period ended September 30, 2011

All amounts disclosed are in Canadian dollars unless otherwise stated.

---

### 1. General information

WCSB Oil & Gas Royalty Income 2010-II Limited Partnership (the "Partnership") was formed on May 4, 2010 as a limited partnership under the laws of the Province of British Columbia and commenced operations on May 31, 2010. The principal purpose of the Partnership is to provide Limited Partners with a tax-assisted investment in the exploration and production of oil and natural gas by investing joint ventures with established oil and gas companies, the terms of which will provide the Partnership with royalty interests. The address of the registered office is 1200 Waterfront Centre, 200 Burrard St, Vancouver BC V7X 1T2.

The Partnership is managed by WCSB Oil & Gas Royalty Income 2010-II Management Corp. (the "General Partner"). Under the Limited Partnership Agreement between the General Partner and each of the limited partners (the "LPA"), 99.99% of net losses of the Partnership will be allocated to the limited partners and 0.01% of net losses of the Partnership will be allocated to the General Partner. According to the performance bonus entitlement in the LPA, until the limited partners have received 100% of their aggregate capital contribution, they will be allocated 100% of net income of the Partnership. Thereafter, the limited partners will be allocated 80% of net income of the Partnership and the General Partner will be allocated 20% of net income of the Partnership. Asset distributions will be allocated 100% to the limited partners until the limited partners have received 100% of their aggregate capital contribution. Thereafter, the limited partners will be allocated 80% of asset distributions and the General Partner will be allocated 20% of asset distributions.

The Limited Partnership operates in one business segment, the investing in oil and gas properties which provide royalties on oil and natural gas production in Western Canada.

### 2. Basis of preparation

#### Statement of compliance

These condensed interim financial statements have been prepared in accordance with International Accounting Standard 34, Interim Financial Reporting ("IAS 34") as issued by the International Accounting Standards Board ("IASB") and using the accounting policies the Partnership expects to adopt in its financial statements as at and for the year ending December 31, 2011.

These are the Partnership's third quarterly condensed interim financial statements prepared in accordance with International Financial Reporting Standards ("IFRS"), and the Partnership's date of transition was January 1, 2010 (the "Transition Date"). IFRS 1, First-time Adoption of International Financial Reporting Standards ("IFRS 1"), has been applied. An explanation of how the transition to IFRS has affected the financial statements is included in note 12.

The policies applied in these condensed interim financial statements are based on IFRS issued and outstanding as of November 28, 2011, the date the Board of Directors approved the condensed interim financial statements. Any subsequent changes to IFRS that are given effect in the Partnership's annual financial statements for the year ending December 31, 2011 could result in restatement of these condensed interim financial statements, including the transition adjustments recognized on change-over to IFRS.

These condensed interim financial statements should be read in conjunction with the Partnership's 2010 annual financial statements prepared in accordance with Canadian generally accepted accounting principles ("Canadian GAAP") and in consideration of the IFRS transition disclosures included in note 12.

#### Basis of measurement

These condensed interim financial statements are stated in Canadian dollars and were prepared on a going concern basis, under the historical cost convention except for derivative financial instruments which are measured at fair value.

# WCSB OIL & GAS ROYALTY INCOME 2010-II LIMITED PARTNERSHIP

## Notes to the Condensed Interim Financial Statements (unaudited)

For the period ended September 30, 2011

All amounts disclosed are in Canadian dollars unless otherwise stated.

---

### **Use of estimates and judgments**

The preparation of financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Although these estimates are based on management's best knowledge of the amount, event or actions, actual results ultimately may differ from those estimates. Areas where estimates are significant to the condensed interim financial statements are disclosed in Note 4.

### **Functional and presentation currency**

These condensed interim financial statements are presented in Canadian dollars, which is the Partnership's functional currency.

## **3. Summary of Significant Accounting Policies**

The principal accounting policies applied in the preparation of these condensed interim financial statements are set out below. These policies have been consistently applied to all the periods presented, unless otherwise stated.

### **A) Cash and cash equivalents**

Cash consists of cash and deposits with maturities of three months or less and is held with a Canadian chartered bank.

### **B) Revenue recognition**

Royalty revenue is recorded in accordance with the royalty rates as stated in the contract terms when the oil and natural gas is sold, title passes to the customer and collection is reasonably assured.

### **C) Exploration and evaluation expenditures**

General exploration and evaluation ("E&E") expenditures incurred prior to acquiring the legal right to explore are charged to the statement of loss as incurred.

E&E expenditures incurred subsequent to acquisition of the legal right to explore, including license and geological and geophysical expenditures are initially capitalized as E&E assets. E&E assets are not depleted and are moved into royalty interests when they are determined to meet certain technical feasibility and commercial viability thresholds as determined by management. Upon transfer to royalty interests, E&E assets are assessed for impairment in addition to regular impairment reviews to ensure they are not carried at amounts above their estimated recoverable values.

### **D) Royalty interests**

Expenditures on developed oil and gas properties such as drilling of development wells, tangible costs of facilities and infrastructure construction are capitalized to royalty interests when it is probable that a future economic benefit will flow to the Partnership as a result of the expenditure and the cost can be reliably measured. The initial cost of an asset comprises its purchase price or construction cost and any costs directly attributable to bringing the asset into operation.

#### Depreciation

Royalty interests are measured at cost less accumulated depletion and depreciation and accumulated impairment losses. Royalty interests are depleted using the unit-of-production method over their reserve life based on proved plus probable reserve volumes. Future development costs are included in costs subject to depletion. Reserves and estimated future development costs are determined annually by qualified independent reserve engineers. Changes in factors such as estimates of reserves that affect unit-of-production calculations are dealt with on a prospective basis.

# WCSB OIL & GAS ROYALTY INCOME 2010-II LIMITED PARTNERSHIP

## Notes to the Condensed Interim Financial Statements (unaudited)

For the period ended September 30, 2011

All amounts disclosed are in Canadian dollars unless otherwise stated.

---

### Disposals

Royalty interest assets are derecognized upon disposal or when no future economic benefits are expected to arise from the continued use of the asset. Any gain or loss on de-recognition of the asset, calculated as the difference between the proceeds on disposal, if any, and the carrying value of the asset, is recognized in the statement of comprehensive income in the period of de-recognition.

## **E) Non-derivative financial instruments**

Non-derivative financial instruments are recognized when the Partnership becomes a party to the contractual provisions of the instrument. Financial assets are derecognized when the rights to receive cash flows from the assets have expired or have been transferred and the Partnership has transferred substantially all risks and rewards of ownership. Non-derivative financial instruments are recognized initially at fair value plus, for instruments not at fair value through profit or loss, any directly attributable transaction costs.

At initial recognition, all financial instruments are classified in one of the following categories depending on the purpose for which the instruments were acquired:

### **Financial assets at fair value through profit or loss**

Financial assets at fair value through profit or loss ("FVTPL") are financial assets held for trading or financial assets designated as such by management on initial recognition. Such assets are held for trading if they are acquired principally for the purpose of selling in the short-term. These assets are initially recognized, and subsequently carried, at fair value, with changes recognized in the income statement. Transaction costs are expensed. Assets in this category include cash and cash equivalents and short-term investments.

### **Loans and receivables**

Loans and receivables are subsequently measured at amortized cost using the effective interest method, less any impairment losses, with interest expense recognized on an effective yield basis. Assets in this category include trade and other receivables.

### **Other financial liabilities**

Other financial liabilities are initially measured at fair value, net of transaction costs, and are subsequently measured at amortized cost using the effective interest method, with interest expense recognized on an effective yield basis. Liabilities in this category include trade and other payables, due to related parties and due to General Partner

## **F) Impairment**

### **Financial assets**

A financial asset is assessed at each reporting date to determine whether there is any objective evidence that it is impaired. Significant financial difficulties of a debtor, probability that the debtor will enter bankruptcy or financial reorganization, and default or delinquency in payments are considered indicators that the trade receivable is impaired. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account, and the amount of the loss is recognized in the statement of comprehensive income. When a trade receivable is uncollectible, it is written off against the allowance account for trade receivables.

### **Non-financial assets**

At the end of each reporting period, the Partnership reviews the carrying amounts of its long lived assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). Where it is not possible to estimate the recoverable amount of an individual asset, the Partnership estimates the recoverable amount of the cash-generating unit ("CGU") to which the asset belongs. Where a reasonable and consistent basis of allocation can be identified, corporate assets are also

# WCSB OIL & GAS ROYALTY INCOME 2010-II LIMITED PARTNERSHIP

## Notes to the Condensed Interim Financial Statements (unaudited)

For the period ended September 30, 2011

All amounts disclosed are in Canadian dollars unless otherwise stated.

---

allocated to individual CGU's, or otherwise they are allocated to the smallest group of CGU's for which a reasonable and consistent allocation basis can be identified.

Recoverable amount is the higher of fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the estimates of future cash flows have not been adjusted. If the recoverable amount of an asset or CGU is estimated to be less than its carrying amount, the carrying amount of the asset or CGU is reduced to its recoverable amount. An impairment loss is recognized immediately in comprehensive income.

Where an impairment loss subsequently reverses for assets with a finite useful life, the carrying amount of the asset or CGU is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognized for the asset or CGU in prior periods. A reversal of an impairment loss is recognized immediately in comprehensive income.

### G) Taxes

The Limited Partnership is not subject to income taxes. The income or loss for Canadian tax purposes is allocable to the Limited Partners, pro-rated by units held, and is included in the taxable income of the partners in accordance with the provisions of the *Income Tax Act* (Canada).

### H) Earnings per unit ("EPU")

Basic EPU is calculated by dividing profit or loss attributable to owners of the Partnership (the numerator) by the weighted average number of Partnership units outstanding (the denominator) during the period. The denominator (number of units) is calculated by adjusting the Partnership units outstanding at the beginning of the period by the number of units redeemed or issued during the period, multiplied by a time-weighting factor.

Diluted EPU is calculated by adjusting the earnings and number of Partnership units for the effects of potential dilutive units. The effects of anti-dilutive units are ignored in calculating diluted EPU. All options are considered anti-dilutive when the Partnership is in a loss position.

## 4. Critical judgments and accounting estimates

The preparation of the condensed interim financial statements in conformity with IFRS requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities and contingent liabilities at the date of the condensed interim financial statements and reported amounts of revenues and expenses during the reporting period. Estimates and judgments are continuously evaluated and are based on management's experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Actual outcomes can differ from these estimates.

The key sources of estimation uncertainty that have a significant risk of causing material adjustment to the amounts recognized in the condensed interim financial statements are:

#### Fair value of financial instruments

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

#### Impairment of non-financial assets

Impairment exists when the carrying value of an asset or cash generating unit exceeds its recoverable amount, which is the higher of its fair value less costs to sell and its value in use. The fair value less costs to sell calculation is based on available data from binding sales transactions in an arm's length transaction of similar assets or observable market prices less incremental costs for disposing of the asset. The value in use calculation is based on a discounted cash flow model. The cash flows are derived from the budget for

# WCSB OIL & GAS ROYALTY INCOME 2010-II LIMITED PARTNERSHIP

## Notes to the Condensed Interim Financial Statements (unaudited)

For the period ended September 30, 2011

All amounts disclosed are in Canadian dollars unless otherwise stated.

the next five years and do not include restructuring activities that the Partnership is not yet committed to or significant future investments that will enhance the asset's performance of the cash generating unit being tested. The recoverable amount is most sensitive to the discount rate used for the discounted cash flow model as well as the expected future cash inflows and the growth rate used for extrapolation purposes.

### Assessment of commercial reserves

Management is required to assess the level of the Partnership's commercial reserves together with the future expenditures to access those reserves, which are utilized in determining the depletion charge for the period, assessing whether any impairment charge is required against producing and developed, and the determination of the deferred tax liability. By their nature, these estimates of discovered and probable crude oil and natural gas reserves, including the estimates of future prices, costs, related future cash flows and the selection of a pre-tax risked discount rate relevant to the asset in question are subject to measurement uncertainty. The Partnership employs an independent reserves specialist who periodically assesses the Partnership's level of commercial reserves by reference to data sets including geological, geophysical and engineering data together with reports, presentation and financial information pertaining to the contractual and fiscal terms applicable to the Partnership's assets. Significant judgment is involved when determining whether there have been any significant changes in the Partnership's crude oil and natural gas reserves.

## 5. Recent accounting pronouncements

Certain new standards, interpretations, amendments and improvements to existing standards were issued by the IASB or International Financial Reporting Interpretations Committee ("IFRIC") that are mandatory for accounting periods beginning after January 1, 2010 or later periods. The standards impacted that are applicable to the Partnership are as follows:

- a) IFRS 9, 'Financial Instruments' was issued in November 2009 as the first step in its project to replace IAS 39 'Financial Instruments: Recognition and Measurement'. IFRS 9 introduces new requirements for classifying and measuring financial assets that must be applied starting January 1, 2013, with early adoption permitted. The IASB intends to expand IFRS 9 during the intervening period to add new requirements for classifying and measuring financial liabilities, de-recognition of financial instruments, impairment and hedge accounting. The Partnership is currently assessing the impact of this standard.
- b) IFRS 10, 'Financial Statements' was issued in May 2011 and will supersede the consolidation requirements in SIC-12 'Consolidation – Special Purpose Entities' and IAS 27 'and Separate Financial Statements' effective for annual periods beginning on or after January 1, 2013, with early application permitted. IFRS 10 builds on existing principles by identifying the concept of control as the determining factor in whether an entity should be included within the financial statements of the parent company. The standard also provides additional guidance to assist in the determination of control where this is difficult to assess. The Partnership is currently assessing the impact of this standard.
- c) IFRS 11, 'Joint Arrangements' was issued in May 2011 and will supersede existing IAS 31, 'Joint Ventures' effective for annual period beginning on or after January 1, 2013, with early application permitted. IFRS 11 provides for the accounting of joint arrangements by focusing on the rights and obligations of the arrangement, rather than its legal form (as is currently the case). The standard also eliminates the option to account for jointly controlled entities using the proportionate consolidation method. The Partnership is currently assessing the impact of this standard.
- d) IFRS 12, 'Disclosure of Interests in Other Entities' was issued in May 2011 and is a new and comprehensive standard on disclosure requirements for all forms of interests in other entities, including subsidiaries, joint arrangements, associates and unconsolidated structured entities. IFRS 12 is effective for annual periods beginning on or after January 1, 2013, with earlier application permitted. The Partnership is currently assessing the impact of this standard.
- e) IFRS 13, 'Fair Value Measurement' was issued in May 2011 and sets out in a single IFRS a framework for measuring fair value. IFRS 13 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. This definition of fair value emphasizes that fair value is a market-based measurement, not an entity-specific measurement. In addition, IFRS 13 also requires specific disclosures about fair value

# WCSB OIL & GAS ROYALTY INCOME 2010-II LIMITED PARTNERSHIP

## Notes to the Condensed Interim Financial Statements (unaudited)

For the period ended September 30, 2011

All amounts disclosed are in Canadian dollars unless otherwise stated.

measurement. IFRS 13 is effective for annual periods beginning on or after January 1, 2013, with earlier application permitted. The Partnership is currently assessing the impact of this standard.

### 6. Royalty interests

	\$
<b>Cost</b>	
At January 1, 2010	-
Additions	11,755,503
<b>At December 31, 2010</b>	<b>11,755,503</b>
Additions	5,190,683
<b>At September 30, 2011</b>	<b>16,946,186</b>
<b>Accumulated depletion and impairment</b>	
At January 1, 2010	-
Depletion	405,270
At December 31, 2010	405,270
Depreciation	2,751,994
<b>At September 30, 2011</b>	<b>3,157,264</b>
<b>Net book value</b>	
January 1, 2010	-
December 31, 2010	11,350,233
<b>September 30, 2011</b>	<b>13,788,922</b>

During the period ended September 30, 2011, the Partnership capitalized \$191,762 (December 31, 2010 - \$191,894) of geological, geo-physical, engineering and economic review expenses related to development activities. No impairment write-down was required as at September 30, 2011.

### 7. Partners' equity

#### A) Authorized

The Partnership is authorized to issue a maximum of 200,000 units.

All Limited Partnership units are of the same class with equal rights and privileges, including equal participation in any distribution made by the Partnership and the right to one vote at any meeting of the Limited Partners.

#### B) Issued and outstanding

	Number of units	\$
At December 31, 2010	191,762	19,176,210
Share issue costs	-	(2,013,501)
<b>At December 31, 2010 and September 30, 2011</b>	<b>191,762</b>	<b>17,162,709</b>

As at September 30, 2011, there were 191,762 (December 31, 2010 – 191,762) Limited Partnership units issued and outstanding and that were issued in 2010 for cash consideration of \$19,176,200.

Pursuant to the LPA, the General Partner contributed \$10 to the capital of the Partnership.

# WCSB OIL & GAS ROYALTY INCOME 2010-II LIMITED PARTNERSHIP

## Notes to the Condensed Interim Financial Statements (unaudited)

For the period ended September 30, 2011

All amounts disclosed are in Canadian dollars unless otherwise stated.

---

### 8. Capital management

The Partnership considers partners' equity as the component of capital to be managed. The Partnership's main objective when managing capital is to execute on its capital investment program to provide a reasonable return for Limited Partners while ensuring capital protection. The Partnership monitors expenditures as required to ensure capital is successfully deployed based on general industry conditions.

### 9. Financial instruments and risk management

The Partnership is engaged in the business of participating in the drilling, completing and managing oil and natural gas wells to earn royalties. The Partnership is exposed to a variety of financial risks, including commodity price risk, foreign exchange risk, credit risk and liquidity risk. The Board of Directors has overall responsibility for identifying the principal risks of the Partnership and ensuring policies and procedures are in place to appropriately manage these risks.

#### Fair values

Fair value represents the price at which a financial instrument could be exchanged in an orderly market, in an arm's length transaction between knowledgeable and willing parties who are under no compulsion to act. The Partnership classifies the fair value of the financial instruments according to the following hierarchy based on the amount of observable inputs used to value the instrument.

The following table provides an analysis of the financial instruments that are measured subsequent to initial recognition at fair value, grouped into Levels 1 to 3 based on the degree to which the fair value is observable.

- Level 1 fair value measurements are those derived from quoted prices (unadjusted) in the active market for identical assets or liabilities.
- Level 2 fair value measurements are those derived from inputs other than quoted prices that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (derived from prices)
- Level 3 fair value measurements are those derived from valuation techniques that include inputs for the asset or liability that are not based on observable market data (unobservable inputs).

# WCSB OIL & GAS ROYALTY INCOME 2010-II LIMITED PARTNERSHIP

## Notes to the Condensed Interim Financial Statements (unaudited)

For the period ended September 30, 2011

All amounts disclosed are in Canadian dollars unless otherwise stated.

Financial Instrument Classification	Note	September 30, 2011		December 31, 2010	
		Carrying Value \$	Fair value \$	Carrying Value \$	Fair Value \$
<b>FVTPL:</b>					
Cash and cash equivalents	(a)	482,567	482,567	5,066,387	5,066,387
<b>Loans and receivables:</b>					
Trade and other receivables	(b)	1,187,265	1,187,265	753,372	753,372
<b>Other financial liabilities:</b>					
Trade and other payables	(b)	90,420	90,420	44,842	44,842
Due to related parties	(b)	-	-	13,040	13,040
Due to General Partner	(b)	227,770	227,770	47,908	47,908

- (a) Fair values are determined from transaction values which reflect quoted active market prices. Fair values of these financial instruments are based on Level 1 measurements.
- (b) Carrying value is measured at amortized cost using the effective interest rate method. The carrying values approximate fair values due to the short term nature of the instrument. Fair values of these financial instruments are based on Level 3 measurements

### Financial risks

The Partnership's activities expose it to a variety of financial risks: credit risk, liquidity risk and market risk (currency fluctuations, interest rates and commodity prices). The Partnership's overall risk management program focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on the Partnership's financial performance.

### Credit Risk

Credit risk is the risk of financial loss to the Partnership if an investor or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from cash, and cash equivalents trade and other receivable. The maximum credit risk exposure is \$1,677,332 (December 31, 2010 - \$5,819,759). The receivables are due from a small number of oil & gas companies and were received subsequent to period end. The Partnership believes the credit risk associated with the cash and cash equivalents is limited due to the credit quality of the financial institution where the funds are held.

### Liquidity risk

Liquidity risk is the risk that the Partnership will not be able to meet its obligations as they are due. The Partnership prepares an annual budget and updates forecasts for operating, financing and investing activities on an ongoing basis to ensure it will have sufficient liquidity to meet its liabilities when due. The Partnership has sufficient cash to fund its obligations as they become due under normal operating conditions. All of the Partnership's financial liabilities are due within 12 months.

### Market risk

Market risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risk comprises three types of risk: currency risk, interest rate risk and other price risk. The Partnership is exposed to market risks resulting from fluctuations in foreign exchange rates, commodity prices and interest rates in the normal course of operations.

# WCSB OIL & GAS ROYALTY INCOME 2010-II LIMITED PARTNERSHIP

## Notes to the Condensed Interim Financial Statements (unaudited)

For the period ended September 30, 2011

All amounts disclosed are in Canadian dollars unless otherwise stated.

### Foreign exchange risk

Foreign currency exchange rate risk is the risk that the fair value of future cash flows will fluctuate as a result of changes in foreign exchange rates. While all of the Partnership's sales are denominated in Canadian dollars, the market prices in Canada for oil and natural gas are impacted by changes in the exchange rate between the Canadian and United States dollar. A strengthening Canadian dollar compared to the United States dollar negatively impacts the Partnership. The Partnership had no forward exchange contracts in place as at September 30, 2011.

### Commodity price risk

Commodity price risk is the risk that the fair value of future cash flows will fluctuate as a result of changes in commodity prices. Commodity prices for oil and natural gas are impacted not only by the relationship between the Canadian and United States dollar, as mentioned above, but also world economic events that dictate the levels of supply and demand. There were no financial instruments in place to manage commodity prices during the period ended September 30, 2011.

### Interest rate risk

Interest rate risk is the risk that the fair value of future cash flows will fluctuate as a result of changes in market interest rates. The Partnership is exposed to interest rate risk on its cash and cash equivalents that have a floating interest rate. The Partnership had no interest rate swaps or hedges as at September 30, 2011.

## 10. Related party transactions

Details of transactions between the Partnership and other related parties are disclosed below.

### Transactions with related parties

	September 30, 2011 \$	December 31, 2010 \$
Brickburn Asset Management Inc. Geological, geo-physical, engineering and economic review costs paid and capitalized in royalty interests costs.	191,762	191,894
Due to related party	-	12,840
CADO Bancorp Ltd. Due to related party	-	200
WCSB Oil & Gas Royalty Income 2010-II Management Corp		
Royalties	495,965	71,950
Administrative services paid, included in general and administrative expense	171,500	105,000
Management fee paid	287,643	191,894
Due to General Partner	227,770	47,908

# WCSB OIL & GAS ROYALTY INCOME 2010-II LIMITED PARTNERSHIP

## Notes to the Condensed Interim Financial Statements (unaudited)

For the period ended September 30, 2011

All amounts disclosed are in Canadian dollars unless otherwise stated.

The General Partner is entitled to an annual management fee of 2.0% of the gross proceeds of the initial public offering, calculated and payable monthly. The General Partner will also be entitled to a performance bonus of 20% of all distributions made by the Partnership once limited partners have received, in total, cumulative distributions equal to 100% of their aggregate capital contribution to the Partnership.

Pursuant to the LPA, the Partnership has granted the General Partner a General Partner's Share, which entitles the General Partner to a 10% share of the Partnership's gross over-riding royalty and also entitles the General Partner to 10% of the consideration received by the Partnership on divestiture of assets.

## 11. Earnings per unit

### Basic and diluted loss per unit

	Profit for the period \$	Weighted average number of units	Per unit amount \$
<b>As at September 30, 2011</b>			
Net comprehensive income – Basic and diluted	1,185,562	191,762	6.18

## 12. Explanation of transition to IFRS

The condensed interim financial statements for the period ended September 30, 2011 are the Partnership's third financial statements prepared under IFRS. For all accounting periods prior to this, the Partnership prepared its financial statements under Canadian GAAP. In accordance with IFRS 1 'First time adoption of IFRS', certain disclosures relating to the transition to IFRS are given in this note. These disclosures are prepared under IFRS as set out in the basis of preparation in Note 3.

IFRS 1 allows first time adopters to IFRS to take advantage of a number of voluntary exemptions from the general principal of retrospective restatement. The Partnership has taken the following exemptions:

### IFRS 6 - Exploration for and Evaluation of Mineral Resources

The Partnership has elected to apply the exemption from full retrospective application of IFRS 6. As such the Partnership has at January 1, 2010, measured the exploration and evaluation assets at the amount determined under Canadian GAAP and measured the development and production assets by allocating the amount determined under Canadian GAAP to the underlying assets on a pro rata basis using reserve values at that date. As a result of using the IFRS 1 optional exemption, the exploration and evaluation assets and the development and production assets have been subjected to an impairment test.

### A) Reconciliation of equity as at January 1, 2010

The Partnership commenced operations on January 22, 2010 and therefore, no reconciliation of equity as at January 1, 2010 is required.

# WCSB OIL & GAS ROYALTY INCOME 2010-II LIMITED PARTNERSHIP

## Notes to the Condensed Interim Financial Statements (unaudited)

For the period ended September 30, 2011

All amounts disclosed are in Canadian dollars unless otherwise stated.

### B) Reconciliations as at December 31, 2010

#### Reconciliation of equity as at December 31, 2010

	Canadian GAAP	Effect of transition to IFRS Depletion (Note 1)	IFRS
<b>ASSETS</b>			
<b>Current assets</b>			
Cash and cash equivalents	66,387	-	66,387
Short-term investment	5,000,000	-	5,000,000
Trade and other receivables	753,372	-	753,372
Prepaid expenses	18,268	-	18,268
	5,838,027	-	5,838,027
<b>Non-current assets</b>			
Royalty interests	11,322,365	127,868	11,350,233
<b>Total Assets</b>	17,060,392	127,868	17,188,260
<b>LIABILITIES</b>			
<b>Current liabilities</b>			
Trade and other payables	44,842	-	44,842
Due to related parties	13,040	-	13,040
Due to General Partner	47,908	-	47,908
	105,790	-	105,790
<b>PARTNERS' EQUITY</b>			
Partnership units	17,162,709	-	17,162,709
Deficit	(208,107)	127,868	(80,239)
	16,954,602	127,868	17,082,470
<b>Total Liabilities and Partners' Equity</b>	17,060,392	127,868	17,188,260

#### Reconciliation of the statement of comprehensive income for the year ended December 31, 2010:

	Canadian GAAP	Effect of transition to IFRS Depletion (Note 1)	IFRS
Royalty income	719,458	-	719,458
Interest	45,380	-	45,380
<b>Total revenue</b>	764,838	-	764,838
Depletion	(533,138)	127,868	(405,270)
General and administrative	(118,153)	-	(118,153)
Filing fees	(4,653)	-	(4,653)
Geological software licensing	(6,090)	-	(6,090)
Management fee	(191,894)	-	(191,894)
Professional fees	(43,682)	-	(43,682)
Registrar and transfer agent	(3,385)	-	(3,385)
Royalties	(71,950)	-	(71,950)
<b>Total comprehensive loss for the period</b>	(208,107)	127,868	(80,239)

# WCSB OIL & GAS ROYALTY INCOME 2010-II LIMITED PARTNERSHIP

## Notes to the Condensed Interim Financial Statements (unaudited)

For the period ended September 30, 2011

All amounts disclosed are in Canadian dollars unless otherwise stated.

---

### C) Notes to the reconciliation

The following explains the material adjustments as at December 31, 2010:

#### **Note 1 - Depletion**

The Partnership depletes its royalty assets using unit of production under both IFRS and Canadian GAAP. However, under IFRS, the depletion is based upon estimated proved plus probable reserves compared to proved reserves used under Canadian GAAP. This has resulted in reduction in the depletion charge for the period ended December 31, 2010 under IFRS.