



Audited Financial Statements
As at December 31, 2007 and 2006 and for the years then ended

Management's Report

The accompanying Financial Statements of MGM Energy Corp. (the "Company") are the responsibility of Management and have been approved by the Board of Directors. The Financial Statements have been prepared by Management in Canadian dollars in accordance with Canadian Generally Accepted Accounting Principles and include certain estimates that reflect Management's best judgments. When alternative accounting methods exist, Management has chosen those it considers most appropriate in the circumstances. These Financial Statements have been prepared on a carve-out basis from Paramount Resources Ltd. as described in Note 2 to the Financial Statements.

Management is also responsible for establishing and maintaining adequate internal control over the Company's financial reporting. The Company's internal control system was designed to provide reasonable assurance that all transactions are accurately recorded, that transactions are recorded as necessary to permit preparation of financial statements in accordance with Generally Accepted Accounting Principles, and that the Company's assets are safeguarded.

The Board of Directors is responsible for ensuring that Management fulfills its responsibilities for financial reporting and internal control. The Board of Directors exercises this responsibility through the Audit Committee. The Audit Committee meets regularly with Management and the independent auditors to ensure that Management's responsibilities are properly discharged and to review the Financial Statements. The Audit Committee reports its findings to the Board of Directors for consideration when approving the Financial Statements for issuance to the shareholders. The Audit Committee also considers, for review by the Board of Directors and approval by the shareholders, the engagement or re-appointment of the external auditors. The Audit Committee of the Board of Directors is comprised entirely of independent directors.

Ernst & Young LLP, independent auditors appointed by the shareholders of the Company, conducts an examination of the Financial Statements in accordance with Canadian generally accepted auditing standards. Ernst & Young LLP has full and free access to the Audit Committee and Management.

/s/ Clayton H. Riddell
Clayton H. Riddell
Chief Executive Officer

/s/ Richard N. Miller
Richard N. Miller
Chief Financial Officer

March 7, 2008

Auditors' Report

To the Shareholders of **MGM Energy Corp.**

We have audited the balance sheets of **MGM Energy Corp.** (the "Company") as at December 31, 2007 and 2006 and the statements of loss other comprehensive loss and deficit and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2007 and 2006 and the results of its operations and its cash flows for the years then ended in conformity with Canadian generally accepted accounting principles.

As discussed in note 2, prior to January 12, 2007, the Spinout Assets and Ancillary Asset were properties of Paramount Resources Limited and had no separate legal status.

Calgary, Canada
March 7, 2008

/s/ Ernst & Young LLP
Chartered Accountants

MGM Energy Corp.
Balance Sheets
(\$000s)

For periods prior to January 12, 2007, the financial statements of MGM Energy Corp., including the results of operations and cash flows, have been prepared on a carve-out basis from Paramount Resources Ltd. as is described in Note 2. These financial statements may not be indicative of the results that would have been attained if MGM Energy Corp. had operated as a stand-alone entity for these periods.

As at December 31	2007	2006 (Note 2)
ASSETS		
Current assets		
Cash and cash equivalents	\$ 111,301	\$ -
Accounts receivable	730	1,360
	112,031	1,360
Property, plant and equipment (Note 4)	237,320	70,268
Future income taxes (Note 9)	13,302	-
	\$ 362,653	\$ 71,628
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities		
Accounts payable and accrued liabilities	\$ 15,799	\$ 6,774
Due to related parties (Note 12)	81	-
	15,880	6,774
Asset retirement obligations (Note 6)	1,172	439
Future income taxes (Note 9)	-	3,895
	17,052	11,108
Contingencies and Commitments (Notes 7 & 13)		
Shareholders' Equity		
Share capital (Note 7)	404,275	-
Contributed surplus (Note 8)	2,307	-
Net investment by Paramount Resources Ltd. (Note 2)	-	60,520
Deficit	(60,981)	-
	345,601	60,520
	\$ 362,653	\$ 71,628

See the accompanying notes to the Financial Statements.

On behalf of the Board

/s/ H. W. Sykes
H. W. Sykes
Director

/s/ R. B. Hodgins
R. B. Hodgins
Director

MGM Energy Corp.
Statements of Loss, Other Comprehensive Loss and Deficit
(\$000s, except as noted)

For periods prior to January 12, 2007, the financial statements of MGM Energy Corp., including the results of operations and cash flows, have been prepared on a carve-out basis from Paramount Resources Ltd. as described in Note 2. These financial statements may not be indicative of the results that would have been attained if MGM Energy Corp. had operated as a stand-alone entity for these periods.

Years Ended December 31	2007 (Note 2)	2006 (Note 2)
Revenue		
Interest income	\$ 3,116	\$ -
Expenses		
General and administrative (Note 12)	6,281	638
Stock-based compensation (Note 8)	2,561	(123)
Pipeline regulatory and access	598	-
Exploration	11,191	399
Lease rental	1,051	198
Dry hole (Note 4)	66,423	3,355
Interest and financing charges	236	-
Accretion of asset retirement obligations (Note 6)	199	30
Depreciation	132	-
	88,672	4,497
Loss before income tax	(85,556)	(4,497)
Future income tax recovery (Note 9)	(23,225)	(1,720)
Net loss and other comprehensive loss	\$ (62,331)	\$ (2,777)
Net loss per Common Share (\$/share)		
Basic	(0.79)	
Diluted	(0.79)	
Weighted average Common Shares outstanding (000s) (Note 7)		
Basic	79,088	
Diluted	79,088	

Statements of Deficit
(\$000s)

Years Ended December 31	2007	2006
Deficit, beginning of year	\$ -	\$ -
Net loss	(62,331)	(2,777)
Allocation to net investment by Paramount Resources Ltd.	1,350	2,777
Deficit, end of year	\$ (60,981)	\$ -

See the accompanying notes to the Financial Statements.

MGM Energy Corp.
Statements of Cash Flows

(\$000s)

For periods prior to January 12, 2007, the financial statements of MGM Energy Corp., including the results of operations and cash flows, have been prepared on a carve-out basis from Paramount Resources Ltd. as is described in Note 2. These financial statements may not be indicative of the results that would have been attained if MGM Energy Corp. had operated as a stand-alone entity for these periods.

Years Ended December 31	2007	2006
	(Note 2)	(Note 2)
Operating activities		
Net loss and other comprehensive loss	\$ (62,331)	\$(2,777)
Add (deduct):		
Stock-based compensation – non cash portion	2,561	(385)
Exploration	11,191	399
Dry hole	66,423	3,355
Accretion of asset retirement obligations	199	30
Asset retirement obligation expenditures (Note 6)	(405)	-
Depreciation	132	-
Future income tax recovery	(23,225)	(1,720)
	(5,455)	(1,098)
Change in non-cash working capital (Note 11)	1,555	(621)
	(3,900)	(1,719)
Financing activities		
Repayment of note to Paramount Resources Ltd. resulting from spin-out transaction	(12,000)	-
Proceeds on settlement of note	163	-
Common shares issued, net of issuance costs	355,106	-
Net investment by Paramount Resources Ltd. for period prior to spin-out	3,195	5,901
	346,464	5,901
Investing activities		
Capital expenditures (Note 4)	(243,858)	(8,970)
Reorganization costs	(1,000)	-
Change in non-cash working capital (Note 11)	13,595	4,788
	(231,263)	(4,182)
Increase in cash and cash equivalents	111,301	-
Cash and cash equivalents, beginning of year	-	-
Cash and cash equivalents, end of year	\$ 111,301	\$ -
Supplemental cash flow information (Note 11)		

See the accompanying notes to the Financial Statements.

NOTES TO FINANCIAL STATEMENTS

(\$000s, except as noted)

1. Structure and Formation of the Company

MGM Energy Corp. (“MGM Energy” or the “Company”) is an independent Canadian public company, the principal business of which is to acquire, develop, optimize, exploit and produce oil and natural gas in Northern Canada. The Company was incorporated under the *Business Corporations Act* (Alberta) (the “ABCA”) on October 31, 2006 as 1278517 Alberta Ltd. On December 4, 2006, the Company’s articles were amended to change its name to “MGM Energy Corporation” and subsequently on January 9, 2007 the articles were further amended to change its name to “MGM Energy Corp.”

MGM Spinout

On January 12, 2007, Paramount Resources Ltd. (“Paramount”) completed a reorganization pursuant to a plan of arrangement under the ABCA involving Paramount, its shareholders and MGM Energy (the “MGM Spinout”).

Through the MGM Spinout:

- MGM Energy became the owner of (i) rights and obligations under a farm-in agreement (the “Farm-in Agreement”) respecting Mackenzie Delta, Northwest Territories Exploration Licence #394, Exploration Licence #427 and Inuvik Concession Blocks 1 and 2 (the “Farm-in Properties”); (ii) oil and gas properties in the Colville Lake / Sahtu area of the Central Mackenzie Valley, Northwest Territories (the “Colville Properties”); and (iii) an interest in one well in the Cameron Hills area of the southern portion of the Northwest Territories (the “Ancillary Asset”), all of such property formerly being owned by Paramount (collectively referred to as the “Spinout Assets”);
- MGM Energy issued Paramount a demand promissory note in the principal amount of \$12.0 million, bearing interest at 10 percent per annum, and 18.2 million voting Class A Preferred Shares, which note was subsequently repaid by MGM Energy and which shares were subsequently converted into voting common shares of MGM Energy (“Common Shares”) on a share-for-share basis; and
- MGM Energy issued Paramount’s shareholders an aggregate of approximately 2.8 million Common Shares and approximately 14.2 million warrant units, with each warrant unit consisting of one MGM Energy short term warrant (each, a “Short Term Warrant”) and one MGM Energy longer term warrant (each, a “Longer Term Warrant”).

Each warrant entitled the holder to purchase one Common Share or one flow-through Common Share as described in Note 7 (Share Capital). Each Longer Term Warrant was not exercisable, and was not separable from the corresponding Short Term Warrant included in the warrant unit, unless the corresponding Short Term Warrant was exercised.

Paramount has the option, subject to certain conditions, to reacquire the Ancillary Asset from MGM Energy for \$5 million, the same price that it sold such asset to MGM Energy through the MGM Spinout (the “Repurchase Option”). Because of the nature of the Repurchase Option, for accounting purposes the Ancillary Asset is deemed to be retained by Paramount and is not reflected in the balance sheet of MGM Energy.

The transfer of the Spinout Assets from Paramount to MGM Energy did not result in a substantive change in ownership of the Spinout Assets and therefore the transaction was accounted for using the carrying value of the property transferred, with the exception of the amount recorded in property, plant and equipment in respect of the

NOTES TO FINANCIAL STATEMENTS

(\$000s, except as noted)

Ancillary Asset, which was not recorded. The carrying values of assets and related liabilities transferred to MGM Energy on January 12, 2007 were as follows:

Property, plant and equipment	\$	71,859
Asset retirement obligations		(439)
Note receivable		163
Accounts payable		(1,000)
Future income taxes		(13,369)
Net carrying value	\$	57,214

The amounts recorded in MGM Energy's financial statements in respect of consideration for the Spinout Assets on January 12, 2007 were as follows:

Note payable	\$	12,000
Common Shares		3,508
Class A Preferred Shares		41,706
Total	\$	57,214

No amounts were attributed to the Short Term Warrants or the Longer Term Warrants.

MGM Energy shared 50 percent of the costs of the MGM Spinout with Paramount. Included in the net carrying value above, is \$1.0 million in respect of MGM Energy's share of such costs. The carrying value of Class A Preferred Shares was reduced by an equivalent amount.

2. Basis of Presentation

MGM Energy is considered to be a development stage enterprise, as it has yet to generate revenue from its planned principal operations. Similar to other development stage enterprises, the recoverability of amounts shown for property, plant and equipment are dependent upon the ability of the Company to obtain necessary financing for its planned exploration and development activities and to discover, develop, transport and market economically recoverable quantities of petroleum and natural gas. There can be no assurance, however, that the Company's efforts to obtain additional financing will ultimately be successful.

These Financial Statements are stated in Canadian dollars and have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP"). As described in Note 1, MGM Energy acquired the Spinout Assets from Paramount effective January 12, 2007 at which point the results of operations and cash flows accrue to the Company. These Financial Statements present the historic financial position, results of operations and cash flows of the Farm-in Properties and the Colville Properties and results of operations and cash flows of the Ancillary Asset on a carve-out basis from Paramount as if MGM Energy had operated as a stand-alone entity subject to Paramount's control prior to January 12, 2007. Because of the nature of the Repurchase Option, the Ancillary Asset is deemed to be retained by Paramount and has not been recorded by MGM Energy, but applicable asset retirement obligations, operating results and cash flows of the Ancillary Asset are reflected in these Financial Statements. The book value of the Ancillary Asset as at December 31, 2006 was \$1.6 million.

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(\$000s, except as noted)

Each of Paramount's core areas has distinct operating staff, capital budgets and targets. Paramount also has shared services such as drilling, facilities and construction, accounting, land administration and corporate compliance. Historically, Paramount has maintained accounting records necessary to support its consolidated financial statements and for other internal and tax reporting purposes. Certain expenses, assets and liabilities applicable to the Spinout Assets for periods prior to January 12, 2007 can be derived directly from the accounting records of Paramount, and it has been necessary to allocate certain items in the manner described below.

Accounts receivable, property, plant and equipment, accounts payable and accrued liabilities, and the liability for asset retirement obligations as at December 31, 2006 have been derived directly from the accounting records of Paramount.

For periods prior to January 12, 2007 the amounts for operating costs, geological and geophysical costs, dry hole costs, lease rental costs, accretion of asset retirement obligations and write-down of petroleum and natural gas properties have been derived directly from the accounting records of Paramount. As the Spinout Assets have never produced, except for limited periods of testing, there has been no revenue, royalties, transportation costs, or depletion and depreciation in respect of such properties. Similarly, no gains or losses associated with financial instruments related to revenue were allocated to the Spinout Assets because of their non-producing nature.

General and administrative costs incurred by Paramount for periods prior to January 12, 2007 have been allocated on a pro rata basis using the estimated percentage of time spent by individual employees on the Spinout Assets during the relevant period.

For periods prior to January 12, 2007, the income tax balances for the costs of acquiring, exploring for and developing the Spinout Assets, and the costs of associated tangible equipment, are blended with those of Paramount's other areas. The future income tax liability as at December 31, 2006 resulted from the utilization of specific tax pools for the purpose of satisfying certain flow-through share commitments.

For purposes of presentation of the statement of cash flows prior to January 12, 2007, cash receipts and disbursements were deemed to be transferred to and from Paramount's corporate account concurrent with the respective inflow or outflow of cash and are presented as "Net investment by Paramount Resources Ltd."

As a result of the basis of presentation described above, these financial statements may not be indicative of the results that would have been attained if MGM Energy had operated as a stand-alone entity prior to January 12, 2007.

3. Summary of Significant Accounting Policies

(a) *Joint Operations*

A portion of MGM Energy's activities are conducted jointly with others and accordingly, these Financial Statements reflect only the Company's proportionate share of any revenues, expenses, assets and liabilities.

(b) *Measurement Uncertainty and Use of Estimates*

The timely preparation of these Financial Statements in conformity with Canadian GAAP requires that management make estimates and assumptions and use judgment that affects: (i) the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements; and (ii) the reported amounts of

NOTES TO FINANCIAL STATEMENTS

(\$000s, except as noted)

expenses during the reported periods. Such estimates primarily relate to unsettled transactions and events as of the date of the Financial Statements. Actual results could differ materially from these estimates.

The amounts recorded for accretion and asset retirement obligations are based on estimates of future costs and other relevant assumptions. By their nature, these estimates are subject to measurement uncertainty and the impact of changes in these estimates and assumptions on the financial statements of future periods could be material.

(c) Cash and Cash Equivalents

Cash and cash equivalents consist of cash and short-term investments with original maturities of three months or less. The short-term investments are classified as held-to-maturity and measured at amortized cost using the effective interest method. As at December 31, 2007, cash equivalents included \$110 million (2006: nil) of investments in various short-term instruments with maturities of three months or less and which bore interest at rates between 4.47% and 4.71%.

(d) Property, Plant and Equipment

Property, plant and equipment are recorded at cost. MGM Energy follows the successful efforts method of accounting for petroleum and natural gas operations. Under this method, acquisition costs of oil and gas properties and costs of drilling and equipping development wells are capitalized. Costs of drilling exploratory wells are initially capitalized. If economically recoverable reserves are not found, such costs are charged to earnings as dry hole expense. Exploration wells are assessed annually, or more frequently as economic conditions dictate, for determination of reserves, and as such, success. Costs of drilling exploratory wells remain capitalized when a well has found a sufficient quantity of reserves to justify completion as a producing well and sufficient progress is being made to assess the reserves and the economic and operating viability of the well. All other exploration costs, including geological and geophysical costs and annual lease rentals are charged to earnings when incurred. Producing areas and significant unproved properties are assessed annually, or more frequently as economic events dictate, for potential impairment. Any impairment loss is the difference between the carrying value of the asset and its fair value.

(e) Depletion and Depreciation

Capitalized costs of proved oil and gas properties are depleted using the unit of production method. For purposes of these calculations, natural gas volumes are converted to barrels on an energy equivalent basis.

The costs of successful exploratory wells and development wells are depleted over proved developed reserves while acquired resource properties with proved reserves are depleted over proved reserves. Acquisition costs of probable reserves are not depleted or amortized while under active evaluation for commercial reserves. Costs become subject to depletion as proved reserves are recognized. Other property plant and equipment are depreciated over their estimated useful lives.

Costs associated with significant development projects are not depleted until commercial production commences.

(f) Asset Retirement Obligations

MGM Energy recognizes the fair value of an asset retirement obligation in the period in which it is incurred and when a reasonable estimate of the fair value can be made. The fair values of asset retirement obligations are capitalized as part of the cost of the related long-lived asset and depreciated on the same basis as the underlying asset. The accumulated asset retirement obligation is adjusted for the passage of time, which is recognized as

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(\$000s, except as noted)

accretion expense in the statements of loss, and for revisions in either the timing or the amount of the original estimated cash flows associated with the liability. Actual costs incurred upon settlement of the asset retirement obligation reduce the asset retirement obligation to the extent of the liability recorded. Differences between the actual costs incurred upon settlement of the asset retirement obligation and the liability recorded are recognized in the period in which the settlement occurs.

(g) Future Income Taxes

MGM Energy follows the liability method of accounting for income taxes. Under this method, future income taxes are recognized for the effect of any difference between the carrying amount of an asset or liability reported in the financial statements and its respective tax basis, using substantively enacted income tax rates. Accumulated future income tax balances are adjusted to reflect changes in substantively enacted income tax rates, with adjustments being recognized in the results of operations in the period in which the change occurs.

(h) Flow-Through Shares

MGM Energy has financed a portion of its exploration activities through the issue of flow-through shares. As permitted under the *Income Tax Act* (Canada), the tax attributes of eligible expenditures incurred with the proceeds of flow-through share issuances are renounced to subscribers. On the date that MGM Energy files the renouncement documents with the tax authorities, a future income tax liability is recognized and shareholders' equity is reduced, for the tax effect of expenditures renounced to subscribers.

(i) Stock-Based Compensation

MGM Energy has granted stock options to employees and directors, the details of which are described in Note 8 (Stock-based Compensation).

MGM Energy uses the fair value method to recognize compensation expense associated with the MGM Energy options and non-reciprocal awards of stock options previously made by Paramount to certain MGM Energy employees and officers. Fair values are determined using the Black-Scholes-Merton option-pricing model and relevant assumptions on the date options are granted. Compensation costs are recognized over the vesting period of the stock options.

(j) Other Comprehensive Income, Financial Instruments and Hedging

MGM Energy classifies all financial instruments into one of the following categories: loans and receivables, assets held-to-maturity, assets available-for-sale, other financial liabilities, and held-for-trading assets and liabilities.

Financial instruments that are classified as held-for-trading or available-for-sale are re-measured each reporting period at fair value with the resulting gain or loss recognized immediately in net income and other comprehensive income, respectively. All other financial instruments are initially accounted for at fair value and subsequently at amortized cost using the effective interest method with foreign exchange gains and losses recognized immediately in net income.

MGM Energy currently does not utilize hedges or other derivative financial instruments in its operations.

NOTES TO FINANCIAL STATEMENTS

(\$000s, except as noted)

(k) Recent Accounting Pronouncements

Capital Disclosures and Financial Instruments – Disclosure and Presentation

Beginning in 2008, MGM Energy will be required to adopt new accounting standards for *Capital Disclosures and Financial Instruments – Disclosure and Presentation*. The new standards require companies to disclose their objectives, policies and procedures for managing capital, as well as whether externally imposed capital requirements have been complied with and to provide enhanced disclosure of risks associated with financial instruments, including how these risks are managed.

International Financial Reporting Standards

In 2006, the Accounting Standards Board (AcSB) adopted a new strategic plan for financial reporting in Canada, “Accounting Standards in Canada: New Directions”. For publicly accountable enterprises (PAEs), the AcSB will converge Canadian GAAP with International Financial Reporting Standards (IFRS) over a period from 2006 to 2011. After this time period, Canadian GAAP will be replaced by IFRS and cease to exist as a separate, distinct basis of financial reporting for PAEs. Canada will continue to maintain its own standard-setting capability to carry out the strategic direction outlined above, although roles, structures, processes and resources may evolve.

(l) Comparative Figures

Certain comparative figures have been reclassified to conform to the current period’s financial statement presentation.

4. Property, Plant and Equipment

	December 31, 2007			December 31, 2006
	Cost	Accumulated Depletion and Depreciation	Net Book Value	Net Book Value
Petroleum and natural gas properties	\$ 236,719	\$ -	\$ 236,719	\$ 70,268
Other	733	132	601	-
	<u>\$ 237,452</u>	<u>\$ 132</u>	<u>\$ 237,320</u>	<u>\$ 70,268</u>

As the Company is in the development stage and has no production, all capitalized costs associated with non-producing petroleum and natural gas properties are currently not subject to depletion.

On May 30, 2007 MGM Energy closed an acquisition of petroleum and natural gas assets located primarily in the Mackenzie Delta and elsewhere in the Northwest Territories for an aggregate cost of \$173.1 million. MGM Energy assigned the entire amount of the purchase price to petroleum and natural gas properties and recognized a \$1.4 million asset retirement obligation related to those assets.

NOTES TO FINANCIAL STATEMENTS

(\$000s, except as noted)

Continuity of Suspended Exploratory Well Costs

	Year Ended December 31	
	2007	2006
Balance, beginning of year	\$ 70,268	\$ 65,001
Additions pending the determination of proved reserves	7,691	5,267
Well costs charged to dry hole expense	(25,181)	-
Balance, end of year	\$ 52,778	\$ 70,268

Aging of Capitalized Exploratory Well Costs

	Year Ended December 31	
	2007	2006
Exploratory well costs capitalized for a period of one year or less	\$ 7,691	\$ 5,267
Exploratory well costs capitalized for a period of greater than one year	45,087	65,001
Balance at end of year	\$ 52,778	\$ 70,268
Number of projects that have exploratory well costs that have been capitalized for a period greater than one year	6	9

At December 31, 2007, \$52.8 million of capitalized exploratory well costs relate to the Colville Lake Properties and the Farm-in Properties. The commerciality of the gas related to such properties is being evaluated in conjunction with the planned drilling program and anticipated timing for construction of the Mackenzie Valley Pipeline.

The dry hole expense of \$66.4 million for the year ended December 31, 2007 relate to two wells drilled in the 2006/07 winter program, two wells drilled in the 2007/08 winter program and three wells drilled in 2004 and 2005. The dry hole expense results from the determination by MGM Energy that there are no economically recoverable reserves related to these wells.

5. Demand Facility

In October, 2007, MGM Energy entered into a \$30 million senior secured revolving demand facility bearing interest at the lender's prime rate or banker's acceptance rate, at the discretion of MGM Energy, plus an applicable margin. MGM Energy is required to repay the facility or to have funds available in cash or short-term investments at least equal to the borrowings under the facility, excluding letters of credit, for a period of three consecutive business days each quarter. At December 31, 2007, there was no debt outstanding on the facility, however, there were undrawn letters of credit outstanding of \$26.6 million that reduce the amount available to MGM Energy under the facility.

NOTES TO FINANCIAL STATEMENTS

(\$000s, except as noted)

6. Asset Retirement Obligations

	Year Ended December 31	
	2007	2006
Asset retirement obligations, beginning of year	\$ 439	\$ 358
Liabilities incurred	926	-
Liabilities assumed on acquisition of properties	1,422	-
Revisions in estimated cost of abandonment	(1,409)	51
Liabilities settled	(405)	-
Accretion expense	199	30
Asset retirement obligations, end of year	\$ 1,172	\$ 439

The total future asset retirement obligations were estimated by management based on MGM Energy's net ownership in all wells, estimated work to reclaim and abandon the wells, and the estimated timing of the costs to be incurred in future periods. The undiscounted cash flows estimated to settle the asset retirement obligations associated with MGM Energy's oil and gas properties at December 31, 2007 are \$11.3 million (December 31, 2006 - \$2.0 million). The majority of these obligations are not expected to be settled for several years, or decades, and have been discounted using credit-adjusted risk-free rates between 7 7/8 percent and 10 percent, and assuming an inflation rate of 3 percent.

7. Share Capital

Authorized

MGM Energy's authorized capital is comprised of an unlimited number of Common Shares, 18.2 million voting Class A Preferred Shares convertible to Common Shares on a one-for-one basis without any further consideration and an unlimited number of preferred shares, issuable in series ("Preferred Shares"). All Class A Preferred Shares were converted into Common Shares on a one-for-one basis on February 16, 2007.

The Preferred Shares are issuable in one or more series. The Board of Directors of MGM Energy may determine the designation, rights, privileges, restrictions and conditions attached to each series of Preferred Shares before the issue of such series. The Preferred Shares will be entitled to a preference over Common Shares with respect to the payment of dividends and the distribution of assets of the Company in the event of the liquidation, dissolution or winding up of the Company.

NOTES TO FINANCIAL STATEMENTS

(\$000s, except as noted)

Issued and Outstanding

Common Shares	Shares	Amount
Balance December 31, 2005	-	-
Issued on incorporation of Company	1	-
Balance, December 31, 2006	1	\$ -
Issued on MGM Spinout	2,832,673	3,508
Cancelled on MGM Spinout	(1)	-
Issued on exercise of Short Term and Longer Term Warrants	13,824,021	76,504
Conversion of Class A Preferred Shares	18,200,000	41,706
Issued for cash	94,088,150	292,120
Share issuance costs, net of tax benefit	-	(9,563)
Balance, December 31, 2007	128,944,844	\$ 404,275

In February 2007, MGM Energy completed a private placement of 210,000 Common Shares at \$5.00 per share and 160,000 Common Shares issued on a flow-through basis at \$6.25 per share, with each Common Share accompanied by one Longer Term Warrant. The gross proceeds of this issue were \$2.1 million.

In May 2007, MGM Energy issued 42,726,193 Common Shares at \$3.10 per share and 11,991,957 Common Shares issued on a flow-through basis at \$3.85 per share, for gross proceeds of \$178.6 million.

In August 2007, MGM Energy issued 33,000,000 Common Shares at \$2.75 per share and 6,000,000 Common Shares issued on a flow-through basis at \$3.45 per share, for gross proceeds of \$111.5 million.

Class A Preferred Shares	Shares	Amount
Balance, December 31, 2006	-	\$ -
Issued on MGM Spinout	18,200,000	41,706
Converted to Common Shares	(18,200,000)	(41,706)
Balance, December 31, 2007	-	\$ -

On February 16, 2007 all of the issued and outstanding Class A Preferred Shares were converted into 18.2 million Common Shares.

Outstanding Warrants	Short Term Warrants	Longer Term Warrants
Balance, December 31, 2006	-	-
Issued on MGM Spinout	14,163,365	14,163,365
Issued on Private Placement	-	370,000
Exercised	(13,824,141)	(95)
Expired	(339,224)	(14,533,270)
Balance, December 31, 2007	-	-

Each Short Term Warrant entitled the holder thereof to acquire, at the holder's option, either (i) one Common Share at a price of \$5.00; or (ii) one flow-through Common Share at a price of \$6.25 and was exercisable until February

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(\$000s, except as noted)

16, 2007. A total of 7.9 million Short Term Warrants were exercised for Common Shares and 5.9 million Short Term Warrants were exercised for flow-through Common Shares for aggregate gross proceeds to MGM Energy of \$76.5 million.

As a result of the exercise of the Short Term Warrants, 13.8 million Longer Term Warrants were separated from the corresponding Short Term Warrants and became exercisable. Each Longer Term Warrant entitled the holder thereof to acquire, at the holder's option, either (i) one Common Share at a price of \$6.00; or (ii) one flow-through Common Share at a price of \$7.50. The Longer Term Warrants expired on September 30, 2007.

Flow-Through Shares

During 2007, MGM Energy has issued a total of \$104.8 million of Common Shares on a "flow-through" basis. As a result, the Company must incur an equivalent amount of qualifying resource expenditures. At December 31, 2007, MGM Energy estimates it has incurred approximately \$51 million of qualifying expenditures relative to the flow-through shares issued in 2007.

Per Share Information

Prior period share information is not presented as the results of operation have been presented on a carve-out basis.

8. Stock-Based Compensation

MGM Energy Options

MGM Energy has a stock option plan (the "Plan") that enables the Board of Directors or its Compensation Committee to grant to key MGM Energy employees and directors options to acquire Common Shares of the Company. The exercise price of an option is no lower than the closing market price of the Common Shares on the day preceding the date of grant. Upon exercise of options under the Plan, optionholders receive either (i) a share certificate for the Common Shares; or (ii) a cash payment in an amount equal to the positive difference, if any, between the market price and the exercise price of the number of Common Shares in respect of which the option is exercised (a "Cash Surrender"). MGM Energy, however, can refuse to accept a Cash Surrender and therefore require that the holder exercise their vested options for cash and acquire Common Shares.

MGM Energy Options

	Weighted Average Exercise Price	Options
	<i>(\$ / share)</i>	
Balance, December 31, 2006	\$ -	-
Granted on MGM Spinout	5.00	1,248,000
Granted since Spinout	2.52	1,898,000
Balance, December 31, 2007	\$ 3.50	3,146,000
Options exercisable, December 31, 2007	\$ 5.00	312,000

NOTES TO FINANCIAL STATEMENTS

(\$000s, except as noted)

Additional information about MGM Energy's stock options outstanding at December 31, 2007 is as follows:

Exercise Prices (\$ / share)	Outstanding		Exercisable
	Number	Weighted Average Contractual Life (years)	Number
\$2.42 – \$3.00	1,698,000	9.16	-
\$3.01 – \$4.00	100,000	3.84	-
\$4.01 - \$5.00	1,348,000	3.33	312,000
Total	3,146,000	6.49	312,000

Up to July 2007, options granted by MGM Energy had a term of approximately 4.5 years. The term of options granted subsequent to July 2007 was ten years.

The fair value of each option granted is estimated on the grant date using the Black-Scholes-Merton option-pricing model with weighted average assumptions for grants as follows:

For the twelve months ended December 31, 2007	
Weighted average fair value of options granted (\$/option)	\$ 1.72
Risk-free interest rate	4.22%
Expected lives (years)	5.63
Expected volatility	0.50
Annual dividend per share (\$/Common Share)	\$ -

Non-Reciprocal Awards to MGM Energy Employees

MGM Energy recognized compensation expense of \$0.1 million in 2007 in respect of non-reciprocal awards of stock options to MGM Energy employees previously made by Paramount. This amount was credited to contributed surplus.

Contributed Surplus

A reconciliation of Contributed Surplus is provided below.

	Year Ended December 31	
	2007	2006
Balance, beginning of year	\$ -	\$ -
Stock-based compensation expense	2,561	(123)
Portion of stock-based compensation related to period prior to Spin-out	(254)	123
Balance, end of year	\$ 2,307	\$ -

NOTES TO FINANCIAL STATEMENTS

(\$000s, except as noted)

9. Income Taxes

The following table reconciles income taxes calculated at the Canadian statutory rate to MGM Energy's recorded future tax recovery:

	Year Ended December 31, 2007	Year Ended December 31, 2006
Loss before tax	\$ (85,558)	\$ (4,497)
Effective Canadian statutory income tax rate	31.0%	35.7%
Expected tax recovery	\$ (26,523)	\$ (1,605)
Increase (decrease) resulting from:		
Statutory and other rate differences	2,499	(423)
Net investment by Paramount Resources Ltd.	68	-
Stock based compensation	715	(49)
Other	16	357
Future tax recovery	\$ (23,225)	\$ (1,720)

Components of Future Income Tax Asset:

	December 31, 2007	December 31, 2006
Property, plant & equipment—carrying value deficit (excess) over tax basis	2,111	\$ (4,012)
Asset retirement obligations	302	128
Loss carry forwards	7,744	-
Share issuance costs & other	3,145	(11)
Future income tax asset (liability)	\$ 13,302	\$ (3,895)

The future income tax asset at December 31, 2007 is anticipated to be reduced to nil by March 31, 2008 as a result of the renunciation of flow-through share expenditures in the first quarter of 2008.

10. Financial Instruments

Interest rate risk

MGM Energy is exposed to interest rate risk to the extent that changes in market interest rates impact MGM Energy's short term deposits that have floating interest rates and to the extent borrowings are made under the debt facility.

NOTES TO FINANCIAL STATEMENTS

(\$000s, except as noted)

11. Changes in Non-cash Working Capital

	Year Ended December 31	
	2007	2006
Accounts receivable	\$ (730)	\$ (485)
Accounts payable and accrued liabilities	15,799	4,652
Due to related parties	81	-
	\$ 15,150	\$ 4,167
Operating activities	\$ 1,555	\$ (621)
Investing activities	13,595	4,788
	\$ 15,150	\$ 4,167

Supplemental cash flow information

	Year Ended December 31	
	2007	2006
Interest paid	\$ 20	\$ -
Taxes paid	\$ -	\$ -

12. Related Party Transactions

Paramount Resources Ltd.

At December 31, 2007, Paramount held 21.5 million common shares of MGM Energy, representing 16.7 percent of the issued and outstanding common shares of MGM Energy at such time. In addition to the common shares of MGM Energy held by Paramount, MGM Energy and Paramount have certain common members of management and directors. The following provides a summary of the related party transactions between MGM Energy and Paramount:

- MGM Energy acquired the Spinout Assets from Paramount pursuant to the MGM Spinout, as is more fully described in Note 1 (Structure and Formation of the Company). The transaction was accounted for using the carrying value of the property transferred, with the exception of the Ancillary Asset. MGM Energy repaid the \$12.0 million principal amount demand promissory note and accrued interest during the first quarter. In addition, Paramount repaid a \$0.2 million principal amount demand promissory note due to MGM Energy.
- Paramount provided certain operational, administrative, and other services to MGM Energy and funded on MGM Energy's behalf, certain capital expenditures related to the Farm-in Agreement pursuant to a services agreement dated January 12, 2007 (the "Services Agreement"). Under the Services Agreement, MGM Energy pays Paramount its reasonable costs incurred in providing services to MGM Energy plus 10 percent of such costs. For the twelve months ended December 31, 2007, Paramount funded \$1.0 million of capital expenditures related to the Farm-in Agreement on MGM Energy's behalf. In addition, MGM Energy recorded costs billed by Paramount of \$1.7 million in respect of the costs of the MGM Spinout and other set-up costs benefiting MGM Energy. These transactions were recorded in these Financial Statements at their exchange amounts.

NOTES TO FINANCIAL STATEMENTS

(\$000s, except as noted)

- For the twelve months period ended December 31, 2007, other amounts billed by Paramount under the Services Agreement totaled \$1.1 million, including a 10 percent charge of approximately \$0.1 million.
- As a result of the MGM Spinout, certain employees and officers of MGM Energy held stock options previously issued by Paramount. The stock-based compensation expense relating to these options for 2007 totaled \$0.1 million and has been included in stock-based compensation expense. All of these options expired prior to December 31, 2007.
- Paramount Resources participated in the August 3, 2007 Common Share issuance, purchasing 3,270,000 Common Shares for gross proceeds of \$9.0 million.
- During 2007, MGM Energy received a rebate of lease payments of \$0.4 million related to its Colville Lake properties. MGM Energy and Paramount have not yet determined the entitlement to this rebate.

Other

During February 2007, MGM Energy completed a private placement to certain directors of MGM Energy of 160,000 flow-through Common Shares at a price of \$6.25 per share and 210,000 Common Shares at a price of \$5.00 per share, each accompanied by one Longer Term Warrant, for aggregate gross proceeds of \$2.1 million.

Certain directors and officers of MGM Energy participated in the May 30, 2007 Common Share issuance, purchasing 5,612,000 Common Shares and 2,364,935 Common Shares issued on a flow-through basis for aggregate gross proceeds to MGM Energy of \$26.5 million.

An officer and director of MGM Energy participated in the August 3, 2007 Common Share issuance, purchasing 1,740,000 Common Shares on a flow-through basis for gross proceeds of \$6.0 million.

During the year, MGM Energy purchased, at fair market value, office furniture and fixtures from Trilogy Energy Trust for \$0.4 million. Trilogy Energy Trust is a related party to MGM Energy due to Paramount's ownership interest in both parties.

13. Contingencies and Commitment

During 2006, Paramount entered into an area wide farm-in agreement respecting the Farm-in Properties. On January 12, 2007, Paramount assigned all of its rights and obligations under the Farm-in Agreement to MGM Energy through the MGM Spinout.

Under the Farm-in Agreement:

- MGM Energy can earn a staged 50 percent interest in the Farm-in Properties by drilling 11 wells within a four year period and making certain lease continuation payments. The aggregate of such lease continuation payments is expected to be \$11 million although it may range up to \$21 million (of which \$11 million has been paid to December 31, 2007 and the balance, if any, is to be paid in 2010);
- Approximately \$50 million of seismic must be acquired;

NOTES TO FINANCIAL STATEMENTS

(\$000s, except as noted)

- If all of the drilling commitments under the Farm-in Agreement are satisfied, MGM Energy will also earn a 50 percent interest in three discoveries previously made in the Mackenzie Delta by the counterparties to the Farm-in Agreement; and
- Of the 11 wells, MGM Energy must drill at least five test wells; two of which have been drilled during the 2006/2007 drilling season, and three wells are planned for the 2007/2008 winter drilling season. MGM Energy currently estimates that the cost of drilling the minimum three wells during the 2007/2008 winter drilling season will be approximately \$60 million. Once the five test wells have been drilled, MGM Energy may elect to stop further drilling and earn a reduced interest in the Farm-in Properties and no interest in the three discoveries. In that event, MGM Energy would remain responsible for the continuation payments and seismic commitment referenced above.

Paramount continued to be jointly and severally liable for the obligations of MGM Energy under the Farm-in Agreement to the extent that such obligations were not satisfied by MGM Energy so long as MGM Energy was an “affiliate” of Paramount as referred to in the Farm-in Agreement. As a result of equity issuances by MGM Energy during 2007, MGM Energy and Paramount are no longer “affiliates” as defined in the Farm-in Agreement.

At December 31, 2007, MGM Energy has the following commitments:

	2008	2009	2010	2011	2012	After 2012
Capital spending commitments	\$ 63,000	\$ 12,000	\$ 13,000	\$ 30,000	\$ 33,000	\$ -
Obligation under lease	\$ 656	\$ 780	\$ 906	\$ 906	\$ 906	\$ 1,358

MGM Energy is obligated under certain Northwest Territories Exploration Licenses to fulfill minimum work commitments totaling \$54 million over the next five years, which are included in the above table. As a condition of the Exploration Licenses, the Company was required to post security of 25 percent of these work commitments via letters of credit. The posted security is released in proportion to the actual work expenditures over the life of the Exploration License.

14. Subsequent Events

In January 2008, MGM Energy completed the drilling of the Atik P-19 well, which entitled MGM Energy to a full refund of a \$1,000,000 lease payment made in 2007. The refund was received in March 2008.

On February 28, 2008, MGM Energy announced that the Atik P-19 well was tested and did not encounter material amounts of hydrocarbons. On March 5, 2008, MGM Energy announced that the Aput C-43 well did not encounter commercial quantities of hydrocarbons. Expenditures of \$10.9 million related to these wells made in 2007 are included in dry hole expense for the year ended December 31, 2007.