XTERRA

RESOURCES CORPORATION

ANNUAL REPORT 2007

X-TERRA RESOURCES CORPORATION
(formerly Canadian Empire Exploration Corp.)
(the "Company")

MANAGEMENT DISCUSSION AND ANALYSIS
("MD&A")
(FORM 51-102F1)

FOR THE YEAR ENDED DECEMBER 31, 2007
(the "Period")

The Company prepares its financial statements in accordance with accounting principles generally accepted in Canada. This MD&A should be read in conjunction with the audited consolidated financial statements of the Company for the years ended December 31, 2007 and 2006 and the related notes thereto. It was prepared in accordance with Regulation 51-102A1 and was approved by our Company's Board of Directors. Unless otherwise indicated, all amounts in this MD&A are in Canadian dollars. The Company capitalizes property acquisition and exploration expenditures relating to mineral properties in which it has an active interest. In the event that such properties become inactive or prove uneconomic, they are written-off. Any reference in this document to "properties" means any mineral resources properties in which the Company has earned or in the future may earn an interest. Management is responsible for the preparation of the consolidated financial statements and other financial information relating to the Company included in this report.

The Board of Directors is responsible for ensuring that management fulfills its responsabilities for financial reporting. In furtherance of the foregoing, the Board has appointed an Audit Committee composed of three directors, who are independent and not members of management. The Committee meets with management and the auditors in order to discuss results of operations and the financial condition of the Company prior to making recommendations and submitting the financial statements to the Board of Directors for its consideration and approval for issuance to shareholders. On the recommendation of the Audit Committee, the Board of Directors has approved the Company's financial statements.

DATE

This MD&A is prepared as of April 28, 2008.

OVERALL PERFORMANCE

Description of Business

X-Terra is a mineral resource company focused on acquiring and exploring gold and uranium properties in Canada. X-Terra has active uranium exploration projects and is looking actively for a gold project in province of Quebec, Canada. Priority targets for uranium are high-grade, shallow uranium deposits that are amenable to low-cost open-pit mining techniques. Priority targets for gold are large grass root land project.

Recognizing the global need for clean energy through nuclear power, X-Terra is aggressively expanding and exploring existing properties and will continue to acquire additional prospective projects. At X-Terra we are committed to discovering new sources of uranium - the clean fuel of today and tomorrow.

Increasing the current cash position in X-Terra is actually a priority for the new team in place.

As at December 31, 2007, the Company has 100% interest in two mineral properties in exploration stage only. The Villedieu property was acquired in May and the Lindsay property in August 2007. On February 23, 2007, the Company changed its name from Canadian Empire Exploration Corp. to X-Terra Resources Corporation, and consolidated its share capital as to 10 old shares in the capital of Canadian Empire Exploration Corp. for one new share in the capital of X-Terra Resources Corporation (TSX-V:XT). The Company is a reporting issuer in British Columbia, Alberta, Manitoba and Ontario and is traded on the TSX Venture Exchange ("TSX-V"), under the symbol XT. It also trades on the Frankfort and Berlin Exchanges in Europe under the symbol DFUA.

In May 2007 the Company closed a non-brokered private placement of one million units at a price of $0.56 per unit for gross proceeds of $560,000. The Company intends to use the proceeds of the private placement for general working capital, and to finance the proposed exploration and development work in the Villedieu township. In June 2007, X-Terra proposed a non-brokered private placement of up to three million units at a price of $0.75 per unit. This financing was cancelled due to market conditions at that time. However, the Company closed a $400,000 private placement in October 2007 which will be used for general working capital, and to finance the proposed exploration and development work on the Villedieu and Lindsay properties. At the annual general meeting of shareholders held June 14, 2007, the Company elected new management team and new Board of Directors as follows: Laurent Hallé, Sébastien Plouffe and Xin Zhao were elected to the Board of Directors of the Company as Class III directors for a three-year term. John Brock and Wayne Roberts did not stand for re-election and R.E. Gordon Davis voluntarily tendered his resignation following the meeting to accommodate the Board's restructuring. Class I director Lawrence Page remains on the Board.

In June 2007, the Company changed its head office and moved to 1100 – 1199 West Hastings St., Vancouver, and leases an office in Rouyn-Noranda for its administrative and exploration activities (see Contractual Obligations). Finally, during the first quarter of 2008, X-Terra appointed Martin Dallaire to the Company's Board of Directors. Mr.Dallaire is the President and a director of Fieldex Exploration Inc. and Visible Gold Mines Inc. Also, Sylvain Champagne was appointed as the new chief financial officer of the Company. Mr.Champagne is the chief financial officer and a director of Fieldex Exploration Inc. and Visible Gold Mines Inc. Mr.Sébastien Plouffe resigned as the chief financial officer and will remain as Vice-President and Secretary of the Company.

PROPERTIES

Villedieu and Lindsay Properties

The Villedieu and Lindsay properties are contiguous properties. The Villedieu/Lindsay uranium project is located approximately 125 kilometres south of Rouyn-Noranda, Quebec and 70 kilometres east-northeast of North Bay, Ontario, along the provincial border, halfway between the Elliot Lake uranium camp and the Abitibi gold belt, within the Grenville front. The project consists of 26 unpatented mining claims (1,534 hectares) in Villedieu township. The Villedieu/Lindsay project is an early stage exploration project with historical uranium and rare-element occurrences and economic potential for these commodities.

The property is underlaid by gneiss derived from a mature sequence of detrital and chemical metasedimentary rocks called the Kipawa formation that has been metamorphosed to upper amphibolite facies (Rive 1973b). The Kipawa alkaline intrusive complex is situated immediately north of the property and this plutonic mass could extend to the south of the property. The composition and texture of the complex is heterogeneous. Three principal internal units are present: a syenitic-monzonite facies; a banded mafic gneiss facies; and a peralkaline granite facies. The discovery of uranium and gold mineralization at Hunter's Point in 1957 increased uranium exploration in the Kipawa region. Since then, several mining companies have sporadically undertaken exploration work in the region. The increased price of uranium over the last several years (currently at $68US/pound; http:www.uxc.com/review/uxc_prices.aspx) has reinvigorated interest in uranium exploration in this region. Many companies are currently active in this sector. More recently, many mining companies have undertaken major exploration work in the region. Aurizon Mines Ltd. has carried out a magnetic, electromagnetic and airborne radiometric survey, covering a vast territory of this sector. In addition, a till sampling survey was conducted by Aurizon Mines in the regions considered most favourable for gold mineralization. This survey has defined four trends of gold dispersion utilizing the analysis of heavy mineral concentrates. The northeast dispersion trend of gold in heavy mineral concentrate is located immediately to the northwest of the property and is evident along the length of a major geological structure in a northwest direction that covers the property at its centre. The heavy mineral concentrates have yielded analyses of more than 0.1 g/T of gold in 27% of samples, including analyses of 1.3 g/T and 2.0 g/T of gold.

The 2007 exploration program consisted of 76 till samples on a 1,000-metre-by-500-metre grid, conducted on a portion of the area covered by the government airborne survey. The objective of the till sampling was to delineate isolated heavy mineral concentrate gold anomalies.

Gold:

- One sample returned 1.22 grams per tonne (g/t);
- Four samples over 0.2 g/t or 200 parts per billion;
- One sample between 100 to 200 ppb;
- Eighteen samples between 21 to 50 ppb.

A radiometric survey for uranium is also planned on the northern portion of the property. A further airborne magnetic and electromagnetic survey on 100-metre spacing combined with a diamond drill program to test gold and uranium targets will be executed in 2008. To view a location map of the 1,490-hectare claim blocks, please visit the Company's website.

The Villedieu property was approved for filing by the TSX Venture Exchange on May 10, 2007 and 550,000 shares were

issued at a deemed total value of $544,500.
The Lindsay property was approved for filing by the TSX-V on August 24, 2007 and 700,000 common shares were issued at a deemed total value of $406,000 and a cash payment of $25,000 was made.

Liquidity and Capital Resources
The Company changed its name from Canadian Empire Exploration Corp. to X-Terra Resources Corporation and consolidated its capital stock as to 10 old shares of Canadian Empire Exploration Corp. for one new share of X-Terra Resources Corporation. All the opening figures related to the number of common shares, warrants and options outstanding have been modified to reflect this consolidation.

As at December 31, 2007, the Company had stock options outstanding allowing for the purchase of up to 7,500 common shares at $1.50 per share until January 2008, 12,400 common shares at $1.00 per share until September 2009 and 165,000 common shares at $1.10 per share until June 2012. As at December 31, 2007, the Company had a working capital of $437,262 (2006: ($213,544)), which included cash of $472,356 (2006: $13,987). However, the Company has reserved an amount of $273,170 for its exploration activities to be conducted in Canada before December 31, 2008 with regards to the transfer of exploration expenditures to the subscribers of its flow-through shares underwriting completed on October 3, 2007.

In May 2007, the Company closed a debt settlement of $183,534 with the issuance of 327,739 common shares at a deemed price of $0.56 per share. Also, in May 2007, the Company closed a non-brokered private placement of one million units at a price of $0.56 per unit for gross proceeds of $560,000. Each unit consists of one common share of the Company and one non-transferable share purchase warrant, with each warrant entitling the holder to acquire one additional common share of the Company at a price of $0.70 per share until May 2009.

In October 2007, the Company closed a private placement with the MineralFields Group for gross proceeds of $400,000. In total, the Company issued 426,666 flow-through units at a price of $0.75 per unit, with each unit consisting of one flow-through common share and one non-flow-through common share purchase warrant. Each purchase warrant entitles the holder thereof to purchase one non-flow-through common share of the Company until October 2, 2009 at an exercise price of $1.00 per share. The Company also issued 133,333 non-flow-through units at a price of $0.60 per unit, with each unit consisting of one common share and one common share purchase warrant. Each warrant entitles the holder thereof to purchase one common share of the Company until October 2, 2009 at an exercise price of $0.75 per share. Limited Market Dealer Inc. received a cash finder's fee of 5% of the gross proceeds and non-transferable finder's fee units entitling it to purchase up to 27,999 non-flow-through units at a price of $0.60 per unit, with each unit consisting of one common share and one common share purchase warrant. Each purchase warrant entitles the holder thereof to purchase one common share of the Company until October 2, 2009 at an exercise price of $0.75 per share.

The Company has limited financial resources at the moment and its ability to continue operating is dependent on management's ability to secure additional financing. Failure to obtain additional financing could result in limited exploration work. The Company is dependent on raising funds by the issuance of shares or disposing of interests in its mineral properties (by option, joint ventures or sales) in order to finance further acquisitions, undertake exploration and development of other mineral properties, and meet general and administrative expenses in the immediate and long term. There can be no assurance that the Company will be successful in raising the required financing. The new management team is actively pursuing such additional sources of financing, and while it has been successful in doing so in the past, there can be no assurance it will be able to do so in the future. Because of this uncertainty, there is substantial doubt about the ability of the Company to continue as a going concern. The audited financial statements do not include the adjustments that would be necessary should the Company be unable to continue as a going concern and these adjustments could be material.

Financing	**Date**	**Purpose**	**Commercial objectives**
Private financing $560,000	May 2007	Exploration work and working capital	This financing consolidates the Company's working capital.
Private financing $399,999	October 2007	Exploration work and working capital	The Company has initiated an exploration program on its two properties acquired in 2007.

During the last fiscal year, the Company has received $959,999 in private investments for its financing activities.

RESULTS OF OPERATIONS

Comparative figures

Certain comparative figures have been reclassified to conform to the presentation adopted for the year ended December 31, 2007.

Mineral Projects

For the year ended December 31, 2007, the Company expended $48,340 in general exploration and capitalized $47,430 from this amount in deferred exploration expenses.

Corporate

Selected administrative expenses:

	12 MONTHS ENDED DECEMBER 31, 2007 ($)	12 MONTHS ENDED DECEMBER 31, 2006 ($)	3 MONTHS ENDED DECEMBER 31, 2007 ($)	3 MONTHS ENDED DECEMBER 31, 2006 ($)
Insurance	16,000	1,700	-	-
Consulting	-	3,100	-	-
Professional fees	137,709	42,062	25,659	24,678
General administrative expenses	114,909	3,358	8,654	6,458
Shareholder's communication	4,363	5,408	1,032	1,822
Transfer agent and regulatory fees	39,580	28,298	6,423	(4,791)
Interest on promessory notes	-	8,534	-	8,534
Stock-based compensation	71,940	22,263	-	-
Total administrative expenses	384,501	114,723	41,768	36,701

During the period, the Company incurred administrative expenses of $384,501 (2006: $114,723). The amount is higher compared with the year 2006 and shows new activities in the Company to implement financing and the acquisition of properties. This explains the increase in professional fees which include audit and legal fees. Management and administrative services and office operations and facilities were provided by Badger & Co. Management Corp. (see "Related Party Transactions") until June 14, 2007 and since then by Terrax Management, and are established on the basis of the time expended on management of the Company.

Stock-based compensation is a non-cash item, resulting from the application of the Black-Scholes option pricing model using assumptions for expected dividend yield, average risk-free interest rates, expected life of the options and expected volatility. The $71,940 (2006: $22,263,) represents the fair value of the vested portion of options for the period.

Properties	**Deferred expenses as at December 31, 2006**	**Expenditures for 2007**	**Future goals**
Villedieu	-	$600	Identify trends for gold dispersion and uranium prospection.
Lindsay	-	$46,830	Identify trends for gold dispersion and uranium prospection.

SUMMARY OF QUARTERLY AND ANNUAL INFORMATION

Summary of Quarterly Results

The following table sets forth a comparison of selected quarterly financial information for the previous eight quarters:

Years	2007				2006			
Period	Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1
Current assets	488,484	238,055	357,382	8,385	14,097	11,542	14,162	35,048
Mining properties	975,864	975,500	544,500	-	-	-	-	-
Current liabilities	51,222	37,354	70,311	236,022	227,641	289,427	283,186	352,644
Shareholders' Equity (Deficiency)								
Capital stock	23,195,520	23,117,511	22,712,011	21,813,127	21,813,127	21,813,128	21,813,128	21,811,753
Contributed surplus/warrants	1,043,979	532,794	496,824	460,854	460,854	460,853	460,853	460,853
Deficit	(22,778,943)	(22,827,604)	(22,732,264)	(22,501,618)	(22,487,525)	(22,551,866)	(22,543,005)	(22,578,903)
Gain (loss) for the period	48,661	(95,340)	(230,646)	(14,093)	64,342	(8,861)	35,897	(37,046)
Working capital (deficit)	437,262	200,701	287,071	(227,637)	(213,544)	(277,885)	(269,024)	(317,597)
Basic and diluted income (loss) per share	0.01	(0.02)	(0.06)	(0.00)	0.02	(0.00)	0.01	(0.01)

Selected Annual Information

The following table sets forth a comparison of revenues and earnings (audited) for the previous three most recently completed financial years:

	December 31, 2007 ($)	December 31, 2006 ($)	December 31, 2005 ($)
Revenue	-	-	-
Income (loss)	(291,418)	54,332	(1,465,324)
Income (loss) per share	(0.06)	0.01	(0.40)
Total assets	1,511,778	14,097	32,080
Total long-term financial liabilities	-	-	-
Cash dividends declared	-	-	-

Variations in annual and quarterly loss and loss per share are affected by administration costs and by the write-down or write-off of mineral property carrying costs in 2005. These losses vary from period to period and from year to year depending on the Company's level of activity, and the amount of write-off relating to the project(s) abandoned during the year. Resource asset balances are dependent on the costs spent to date to earn an interest in projects held at period-end. In accordance with its policies, management reviews the carrying value of the deferred mineral property acquisition and exploration expenditures to assess whether there has been any impairment in value. In the event that mineral deposits are determined to be insufficient to recover the carrying value of any property, the carrying value is written-down or written-off, as appropriate.

No cash dividends have been declared or paid since the date of incorporation and the Company has no intention presently of paying dividends on its common shares. The Company anticipates that all available funds will be used to finance the growth of its business.

CONTRACTUAL OBLIGATIONS

On June 15, 2007, the Company entered an agreement to lease an office in Rouyn-Noranda for its administrative and exploration activities at a base rate of $2,000 per month. The term of the lease is a periodic tenancy commencing on June 15, 2007 and continuing on a year-to-year basis (June 30, 2008) until the landlord or the tenant terminates the tenancy. On 30 day's notice for the landlord and 15 day's notice for the tenant, each party may terminate this lease without cause or reason.

The Company is committed to incurring Canadian exploration expenses of $320,000 by December 31, 2008, with regard to the transfer of these expenditures to the subscribers of its flow-through share underwriting completed on October 3, 2007. As at December 31, 2007, $46,830 has been incurred against this commitment.

RELATED PARTY TRANSACTIONS

Related party transactions occurred in the normal course of business and were recorded at the exchange values which is the consideration determined and agreed to by the related parties. Until June 14, 2007, the Company was party to management agreements with Badger & Co. Management Corp., a private company owned by certain individuals who were directors and/or senior officers of the Company until that date. Pursuant to these agreements, the Company paid $15,010 during the period January 1 to June 14, 2007.

During the period from January 1 to December 31, 2007, the Company paid $4,947 for the provision of administrative services to a company controlled by a director and $22,202 for legal services provided by a law corporation controlled by a director.

On May 16, 2007, the Company closed a debt settlement for the loans made by John S. Brock and Wayne J. Roberts through their private companies on February 2, 2006 and October 26, 2006 in the aggregate principal amount of $175,000 with interest at 6% per annum as evidenced by promissory notes, for a total of $183,534, with the issuance of 327,739 common shares at a deemed price of $0.56 per share.

GENERAL ADMINISTRATIVE EXPENSES AND PROFESSIONAL FEES

This is the detail for general administrative expenses for the year ended December 31, 2007 :

	$
Bank charges	1,795
Advertising and promotion	2,226
Travel expenses and representation	16,455
Office operations and facilities	24,119
Management and administrative services	70,314
	114,909

This is the detail for professional fees for the year ended December 31, 2007 :

	$
Audit and related services	28,554
Legal	109,155
	137,709

USE OF ESTIMATES

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Significant areas where management judgment is applied are the useful life of assets for amortization purposes, the valuation of mineral properties and deferred expenditures, future income tax and valuation of stock-based compensation and warrants. Actual results could differ from those estimates.

NEW ACCOUNTING STANDARDS

Accounting standards newly adopted

On January 1, 2007, the Company adopted four new accounting standards related to accounting changes, financial instruments, comprehensive income and hedges that were issued by the Canadian Institute of Chartered Accountants ("CICA"). The new CICA standards are as follows.

i) Section 1506, "Accounting Changes"

This Section establishes criteria for changes in accounting policies, accounting treatment and disclosure regarding changes in accounting policies, estimates and corrections of errors. In particular, this Section allows for voluntary changes in accounting policy only when they result in the financial statements providing reliable and more relevant information. Furthermore, this Section requires disclosure of when an entity has not applied a new source of Canadian generally accepted accounting principles ("GAAP") that has been issued but is not yet effective. Such disclosures are provided below. The adoption of this Section had no further effect on the consolidated financial statements for the year ended December 31, 2007.

ii) Section 3855, "Financial Instruments – Recognition and Measurement"

This Section establishes standards for recognizing and measuring financial assets and financial liabilities and non-financial derivatives. All financial instruments are required to be measured at fair value on initial recognition, except for certain related party transactions. Measurement in subsequent periods depends on whether the financial instrument has been classified as held for trading, available for sale, held to maturity, loans and receivables, or other liabilities.

Financial assets and financial liabilities classified as held for trading are required to be measured at fair value, with gains and losses recognized in net income.

Financial assets classified as held to maturity, loans and receivables, and financial liabilities (other than those held for trading) are required to be measured at amortized cost using the effective interest method.

Available-for-sale financial assets are required to be measured at fair value, with unrealized gains and losses recognized in other comprehensive income. Investments in equity instruments classified as available for sale that do not have a quoted market price in an active market should be measured at cost.

The Company has implemented the following classifications:

- Cash is classified as held for trading.
- The Company's accounts receivable are classified as loans and receivables.
- Accounts payable and accrued liabilities are classified as other liabilities.

iii) Section 1530, "Comprehensive Income"

This Section establishes standards for reporting and presenting comprehensive income which is defined as the change in equity from transactions and other events from non-owner sources. Other comprehensive income refers to items recognized in comprehensive income that are excluded from net income.

The classification of the Company's financial instruments as at January 1, 2007 and their subsequent changes as at December 31, 2007 have resulted in no gains or losses that require separate presentation in other comprehensive income. There was no effect on opening equity as of January 1, 2007 or on subsequent measurements as a result of applying this new standard.

iv) Section 3865, "Hedges"

This Section establishes the standard of how hedge accounting may be applied. The Company currently does not have any hedges in place, and therefore this standard has no impact on its consolidated financial statements.

New accounting standards not yet adopted

i) Section 1400, "General Standards of Financial Statement Presentation"

In June 2007, the CICA amended Section 1400 to include requirements to assess an entity's ability to continue as a going concern and disclose any material uncertainties that cast doubt on its ability to continue as a going concern. This new requirement will be effective January 1, 2008. The Company has already performed such assessment and provided adequate disclosure.

ii) Section 1535, "Capital Disclosures"

On December 1, 2006, the CICA issued this new accounting standard which will be effective January 1, 2008. Section 1535 specifies the disclosure of information that enables users of an entity's financial statements to evaluate qualitative information about its objectives, policies and processes for managing capital, summary quantitative data about what the entity manages as capital, whether it has complied with any capital requirements and, if it has not complied, the consequence of non-compliance.

iii) Section 3862, "Financial Instruments – Disclosures", and Section 3863, "Financial Instruments – Presentation"

These sections will replace Section 3861, "Financial Instruments – Disclosure and Presentation", revising and enhancing disclosure requirements while carrying forward its presentation requirements. These new sections will place increased emphasis on disclosure about the nature and extent of risk arising from financial instruments and how the entity manages those risks. The mandatory effective date is for annual and interim periods in fiscal years beginning on or after October 1, 2007. The Company will begin application of these sections effective January 1, 2008.

It is not anticipated that the adoption of Sections 1535, 3862 and 3863 will impact the amounts reported in the Company's consolidated financial statements as they relate primarily to disclosure.

FINANCIAL INSTRUMENTS

The Company invests its cash only in bank term deposits.

OTHER MD&A REQUIREMENTS

Share data

As at April 28, 2008, the Company had the following:

Issued and outstanding- 6,776,671 shares

Warrants outstanding:

Expiry date	Number of warrants outstanding	Exercise price ($)
May 28 2009	1,000,000	0.70
October 2009 *	161,332	0.75
October 2009	426,666	1.00
	1,587,998	

* These include 27,999 finder options which expire in October 2009. Each finder option entitles the holder to subscribe for an equal number of units in consideration of $0.60, composed of one share and one warrant at a price of $0.75.

Stock options outstanding:

Expiry date	Number of options outstanding	Number of options exercisable	Exercise price ($)
September 2009	12,400	12,400	1.00
June 2012	165,000	82,500	1.10
	177,400	94,900	

Risk and Uncertainties

The securities of the Company are highly speculative. In evaluating the Company, it is important to consider that it is a resources exploration enterprise in the exploratory stage of its operations. To date, the Company has had no revenues and there is no immediate expectation of revenues. A prospective investor or other person reviewing the Company should not consider an investment in it unless the investor is capable of sustaining an economic loss of the entire investment. All costs have been funded through equity. Certain risks are associated with the Company's business including:

Mineral Exploration and Development

The Company's properties are in the exploration stage and are without a known body of commercial ore. Development of any of its properties will only follow after obtaining satisfactory exploration results. Mineral exploration and development involve a high degree of risk and few properties which are explored are ultimately developed into producing mines. There is no assurance that the Company's mineral exploration and development activities will result in the discovery of a body of commercial ore on any of its properties. Several years may pass between the discovery and development of commercial mineable mineralized deposits. Most exploration projects do not result in the discovery of commercially mineralized deposits.

Trends

The Company's financial success is dependent on the discovery of properties which could be economically viable to develop. Such development could take years to complete and the resulting income, if any, is difficult to determine. The sales value of any mineralization discovered by the Company is largely dependent on factors beyond the Company's control, such as market value of the products produced. Other than as disclosed herein, the Company is not aware of any trends, uncertainties, demands, commitments or events which are reasonably likely to have a material effect on its results or financial position.

Operating Hazards and Risks

Mineral exploration involves many risks. The operations in which the Company has a direct or indirect interest will be subject to all the hazards and risks normally incidental to exploration, development and production of resources, any of which could result in work stoppages and damage to persons or property or the environment and possible legal liability for any and all damage. Fires, power outages, labour disruptions, flooding, explosions, cave-ins, landslides and the inability to obtain suitable or adequate machinery, equipment or labour are some of the risks involved in the operation of a mine and the conduct of exploration programs. Although the Company will, when appropriate, secure liability insurance in an amount which it considers adequate, the nature of these risks is such that liabilities might exceed policy limits, the liability and hazards might not be insurable, or the Company might elect not to insure itself against such liabilities due to high premium costs or other reasons, in which event the Company could incur significant costs that could have a material adverse effect on its financial condition.

Economics of Developing Mineral Properties
Substantial expenditures are required to establish ore reserves through drilling, to develop metallurgical processes to extract metal from ore and to develop the mining and processing facilities and infrastructure at any site chosen for mining. No assurance can be given that minerals will be discovered in sufficient quantities to justify commercial operation or that the funds required for development can be obtained on a timely basis.

The marketability of any minerals acquired or discovered may be affected by numerous factors which are beyond the Company's control and which cannot be predicted, such as market fluctuations, the proximity and capacity of milling facilities, mineral markets and processing equipment, and such other factors as government regulations, including regulations relating to royalties, allowable production, importing and exporting of minerals, and environmental protection. Depending on the price of minerals produced, the Company may determine that it is impractical to commence or continue commercial production.

Environmental Factors
The Company proposes to conduct exploration activities in various parts of Canada. Such activities are subject to laws, rules and regulations governing the protection of the environment, including, in some cases, posting of reclamation bonds. In Canada, extensive environmental legislation has been enacted by federal, provincial and territorial governments. All phases of the Company's operations are subject to environmental regulation in the jurisdictions in which it operates. Environmental legislation is evolving in a manner which requires stricter standards and enforcement, increased fines and penalties for non-compliance, more stringent environmental assessments of proposed properties and a heightened degree of responsibility for companies and their officers, directors and employees. There is no assurance that future changes in environmental regulations, if any, will not adversely affect the Company's operations. The cost of compliance with changes in governmental regulations has the potential to reduce the profitability of operations or to preclude entirely the economic development of a property. Environmental hazards may exist on the Company's properties, which hazards are unknown to the Company at present, which may have been caused by previous or existing owners or operators of the properties. The Company is not aware of any environmental hazards on any of the properties held by the Company.

The approval of new mines on federal lands in Canada is subject to detailed review through a clearly established public hearing process, pursuant to the Canadian Environmental Assessment Act. In addition, lands under federal jurisdiction are subject to the preparation of a costly environmental impact assessment report prior to commencement of any mining operations. These reports entail a detailed and scientific assessment as well as a prediction of the impact on the environmental and proposed development. Further, under such review process, there is no assurance that regulatory and environmental approvals will be obtained on a timely basis or at all. Failure to comply with the legislation may have serious consequences. Orders may be issued requiring operations to cease or be curtailed or requiring installation of additional facilities or equipment. Violators may be required to compensate those suffering loss or damage by reason of their mining activities and may be fined if convicted of an offense under such legislation.

Canadian provincial mining legislation establishes requirements for the decommissioning, reclamation and rehabilitation of mining properties in a state of temporary or permanent closure. Such closure requirements relate to the protection and restoration of the environment and the protection of public safety. Some former mining properties must be managed for long periods of time following closure in order to fulfill closure requirements. The costs of closure of mining properties, and, in particular, the cost of long-term management of mining properties can be substantial. The Company intends to progressively rehabilitate its mining properties during their period of operation should any properties become operational so as to reduce the cost of fulfilling closure requirements after the termination or suspension of production.

The Company has adopted environmental practices designed to ensure that it continues to comply with or exceed all environmental regulations currently applicable to it. All of the Company's activities are in compliance in all material respects with applicable environmental legislation. The Company is currently engaged in exploration with nil to minimal environmental impact.

Uncertainty of Ownership Rights and Boundaries of Resource Properties
There is no assurance that the rights of ownership and other rights in concessions held by the Company are not subject to loss or dispute particularly because such rights may be subject to prior unregistered agreements or transfers or other land claims and may be affected by defects and adverse laws and regulations which have not been identified by the Company. Notwithstanding that the exploration and operating concessions in respect of which the Company may hold various interests have been surveyed, the precise boundary locations thereof may be in dispute. Although the Company has exercised the usual due diligence with respect to title to properties in which it has a material interest, there is no guarantee

that title to the properties will not be challenged or impugned. The Company's mineral property interest may be subject to prior unregistered agreements or transfers or native land claims and title may be affected by undetected defects. In addition, certain of the mining claims in which the Company has an interest are not recorded in its name and cannot be recorded until certain steps are taken by other parties. Before a number of claims under option can be recorded in the Company's name, the underlying title holder has to assign title to the Company once the Company satisfies its option agreement obligations. There are no assurances that the underlying title holder will assign title.

Potential Conflicts of Interest
The directors of the Company serve as directors of other public and private companies and devote a portion of their time to manage other business interests. This may result in certain conflicts of interest. To the extent that such other companies may participate in ventures in which the Company is also participating, such directors and officers of the Company may have a conflict of interest in negotiating and reaching an agreement with respect to the extent of each company's participation. The laws of British Columbia require the directors and officers to act honestly, in good faith, and in the best interests of the company and its shareholders. However, in conflict of interest situations, directors of the Company may owe the same duty to another company and will need to balance the competing obligations and liabilities of their actions. There is no assurance that the needs of the Company will receive priority in all cases. From time to time, several companies may participate together in the acquisition, exploration and development of natural resource properties, thereby allowing these companies to: (i) participate in larger programs; (ii) acquire an interest in a greater number of programs; and (iii) reduce their financial exposure with respect to any one program. A particular company may assign, at its cost, all or a portion of its interests in a particular program to another affiliated company due to the financial position of the company making the assignment. In determining whether or not the Company will participate in a particular program and the interest therein to be acquired by it, it is expected that the directors of the Company will primarily consider the degree of risk to which the Company may be exposed and its financial position at the time.

Indemnity and Protection of Directors, Officers and Employees
Article 19.1 of the Registrant's Articles states:

> "Subject to the provisions of the Company Act [the British Columbia Company Act], the directors shall cause the company to indemnify a director or former director of the company and the directors may cause the company to indemnify a director or former director of a corporation of which the company is or was a shareholder and the heirs and personal representatives of any such person against all costs, charges and expenses including any amount paid to settle an action or satisfy a judgment, actually and reasonably incurred by him or them including an amount paid to settle an action or satisfy a judgment in a civil, criminal or administrative action or proceeding to which he is or they are made a party by reason of his or their being or having been a director of the company or a director of such corporation, including any action brought by the company or any such corporation. Each director of the company, on being elected or appointed, shall be deemed to have contracted with the company on the terms of the foregoing indemnity."

The Article also provides similar protection for officers and employees for liabilities incurred arising out of the performance of their duties or by reason of their position with the Registrant. Thus, the Company may be required to pay amounts to settle any such claims that may arise, if any. The impact of any such possible future indemnity protection cannot be determined at this time. Insofar as indemnification for liabilities arising under the U.S. Securities Act of 1933 (the "1933 Act") may be permitted to directors, officers or persons controlling the Company pursuant to the foregoing provisions, the Company has been informed that, in the opinion of the Securities and Exchange Commission, such indemnification is against public policy as expressed in the 1933 Act and is therefore unenforceable.

Canadian Aboriginal Land Claims
Canadian aboriginal rights may be claimed on Crown properties or other types of tenure with respect to which mining rights have been conferred. The Company is aware of the mutual benefits afforded by cooperative relationships with indigenous people in conducting exploration activity and is generally supportive of measures established to achieve such cooperation. While there is, to the Company's knowledge, no existing claim in respect of any of its properties, the advent of any future aboriginal land claims and the outcome of any aboriginal land claims negotiations cannot be predicted.

Competition
The mineral industry is intensely competitive in all its phases. The Company competes with many companies possessing greater financial resources and technical facilities than it for the acquisition of mineral concessions, claims, leases and other mineral interests as well as for the recruitment and retention of qualified employees. Many of the mining companies with which the Company competes have operations and financial strengths many times that of the Company. Nevertheless, the market for the Company's possible future production of minerals tends to be commodity rather than enterprise oriented

since mineral products tend to be fungible. As a result, the competitive factors are principally impacted by overall market issues rather than by corporate presence and strength. Accordingly, the Company expects to compete by keeping its production costs low (as yet, the Company does not have any property in the development or production stage) through judicious selection of the property to be developed and by keeping overhead and other charges within industry standards.

Governmental Regulation

Operations, development and exploration on the Company's properties are affected to varying degrees by: (i) government regulations relating to such matters as environmental protection, health, safety and labour; (ii) mining law reform; (iii) restrictions on production, price controls, and tax increases; (iv) maintenance of claims; (v) tenure; and (vi) expropriation of property. There is no assurance that future changes in such regulation, if any, will not adversely affect the Company's operations. Changes in such regulation could result in additional expenses and capital expenditures, availability of capital, competition, reserve uncertainty, potential conflicts of interest, title risks, dilution, and restrictions and delays in operations, the extent of which cannot by predicted.

The Company is at the exploration stage on all of its properties. Exploration on the Company's properties requires responsible best exploration practices to comply with Company policy, government regulations, and maintenance of claims and tenure. The Company is required to be registered to do business and have a valid prospecting license (required to prospect or explore for minerals on crown Mineral land or to stake a claim) in any Canadian province in which it is carrying out work. Mineral exploration primarily falls under provincial jurisdiction. However, the Company is also required to follow the regulations pertaining to the mineral exploration industry that fall under federal jurisdiction, such as the Fish and Wildlife Act.

If any of the Company's projects are advanced to the development stage, those operations will also be subject to various laws and regulations concerning development, production, taxes, labour standards, environmental protection, mine safety and other matters. In addition, new laws or regulations governing operations and activities of mining companies could have a material adverse impact on any project in the mine development stage that the Company may possess.

Uncertainty of Markets for Metals

The global market price for metals is influenced by numerous factors beyond the Company's control. Such factors include supply and demand, inflation, imposition of export controls, government regulated ad valorem taxes and royalties that may be imposed on metal production, refining costs and penalties, labour problems experienced by large producers and market price fluctuations resulting from speculative and production hedging activity. The exact effect of these factors cannot be accurately predicted and the combination of these factors may result in the Company not receiving an adequate return on invested capital.

Need for Additional Financing

Currently, exploration programs and feasibility studies are pursued by the Company with the objective of establishing mineralization of commercial quantities. The Company may fund the proposed programs and feasibility studies through equity financing and the possible exercise of outstanding options. Such funding would be dilutive to current shareholders. Should sources of equity financing not be available to the Company, the Company would seek a joint venture relationship in which the funding source could become entitled to a shared, negotiated interest in the property or the projects. If exploration programs carried out by the Company are successful in establishing ore of commercial quantities and/or grade, additional funds will be required to develop the properties and reach commercial production. In that event, the Company may seek capital through further equity funding, debt instruments, by offering an interest in the property being explored and allowing the party or parties carrying out further exploration or development thereof to earn an interest, or through a combination of funding arrangements. There can be no assurance of such funding sources. Furthermore, if the Company is not able to obtain the capital resources necessary to meet property payments or exploration or development obligations which now apply or which would apply in joint ventures with others, its potential as a "going concern" could be seriously affected.

Management and Directors

The Company is dependent on a relatively small number of key directors and officers: Laurent Hallé and Sébastien Plouffe. Loss of any one of these persons could have an adverse affect on the Company. The Company does not maintain "key-man" insurance in respect of any of its management.

Price Fluctuations: Share Price Volatility
In recent years, the international securities markets have experienced high levels of price and volume volatility, and the market price of securities of many mineral exploration companies have experienced wide fluctuations in price which have not necessarily been related to the operating performance, underlying asset values or prospects of such companies. There can be no assurance that the continual fluctuations in price will not occur.

Uninsurable Risks
In the course of exploration and development of, and production from, mineral resource properties, certain risks and, in particular, unexpected or unusual geological formations and engineering operating conditions may occur and may expose the Company to liabilities. Should such liabilities arise, the payment of such liabilities may have a material adverse effect on the Company's financial position. It is not always possible to fully insure against such risks or the Company may elect not to cover such risks because of the high cost of such insurance. The Company may become subject to liability for pollution or hazards. Payment of liabilities for claims for such occurrences could reduce or eliminate any future profitability and could result in increasing costs and a decline in the value of the securities of the Company. Currently, the Company is a named insured with respect to commercial general liability and excess liability in a gross amount limited to $10 million (Cdn.) for each occurrence.

Variations in Operating Results
The Company was incorporated on February 24, 1987 and since incorporation, has not realized net income nor paid dividends. Variations in annual and quarterly loss and loss per shares are affected by administration costs and the write-down or write-off of mineral property carrying costs. There is no assurance that these trends in operating results will change.

Plan of Operations and Financial Sources and Liquidity
See Liquidity and Capital Resources, Results of Operations, and Share Data contained within this document.

To date, the Company's mineral exploration activities have been funded through sales of common shares. The Company's ability to continue operations is dependent on management's ability to secure additional financing. Management is actively pursuing such additional sources of financing, and while it has been successful in doing so in the past, there can be no assurance it will be able to do so in the future. Because of this uncertainty, there is substantial doubt about the ability of the Company to continue as a going concern. The consolidated financial statements do not include the adjustments that would be necessary should the Company be unable to continue as a going concern.

INTERNAL CONTROL OVER FINANCIAL REPORTING
Management has designed internal control over financial reporting to provide reasonable assurance regarding the reliability of financial reporting and preparation of the financial statements for external purposes in accordance with Canadian generally accepted accounting principles. As at December 31, 2007, the Chief Executive Officer and Chief Financial Officer evaluated the design of the company's internal control over financial reporting. Based on that evaluation, the Chief Executive Officer and the Chief Financial Officer concluded that design of internal control over financial reporting was effective as at December 31, 2007 to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with Canadian GAAP.

There have been no changes in the Company's internal control over financial reporting that occurred during the most recent interim period ended September 30, 2007 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

NATIONAL INSTRUMENT 52-109 - CERTIFICATES OF ANNUAL FILING
The Chief Executive Officer and Chief Financial Officer have signed certificates that, among things, report on the design and effectiveness of disclosure controls and procedures and the design of internal controls over financial reporting.

The Company's management has a process to evaluate the effectiveness and the design of the aforementioned controls and procedures, and is satisfied, as at December 31, 2007, that these are adequate for ensuring that complete and reliable financial information is produced.

OTHER INFORMATION
The Company's web address is www.xterraresources.com. Other information relating to the Company may be found on the SEDAR website (www.sedar.com).

DISCLOSURE CONTROLS AND PROCEDURES

Current securities policies in Canada require that management of the Company certifies that it has assessed the effectiveness of the Company's disclosure controls and procedures as at December 31, 2007. Management has concluded that the disclosure controls as at December 31, 2007 were effective in ensuring that all material information required to be filed had been provided to it in a timely manner, and that the information was recorded, processed and reported within the time period necessary to prepare the filings.

FORWARD-LOOKING STATEMENTS

This discussion includes certain statements that may be deemed "forward-looking statements". Other than statements of historical facts, statements in this discussion include, but are not limited to, the Company's expectations as to, future production, reserve potential, exploration drilling, exploration activities and events or developments, commodities market prices, timetables, costs, capital expenditures, work programs, and budgets. Although the Company believes the expectations expressed in such forward-looking statements are based on reasonable assumptions, the risks, hazards, uncertainties. Factors that could cause actual results to differ materially from those in forward-looking statements include, but are not limited to, operating, exploration and geological successes, continued availability of capital and financing, and general economic, environmental, industry, market or business conditions, volatility and sensitivity to market metal prices. Such statements are not guarantees of future performance and actual results or developments may differ materially from those in the forward-looking statements. Investors are cautioned that any such statements are not guarantees of future performance, that the Company expressly disclaims any responsibility for revising or expanding the forward-looking statements to reflect actual results or developments, and that actual results or developments may differ materially from those projected in the forward-looking statements.

X-Terra Resources Corporation

(formerly Canadian Empire Exploration Corp.)
(an exploration stage company)

Consolidated Financial Statements
December 31, 2007 and 2006

PRICEWATERHOUSECOOPERS

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April 28, 2008

Auditors' Report

To the Shareholders of
X-Terra Resources Corporation

We have audited the consolidated balance sheets of **X-Terra Resources Corporation** as at December 31, 2007 and 2006 and the consolidated statements of operations, 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.

In our opinion, these consolidated 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, comprehensive loss and deficit and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

PricewaterhouseCoopers LLP

Chartered Accountants

X-Terra Resources Corporation

(formerly Canadian Empire Exploration Corp.)
(an exploration stage company)
Consolidated Balance Sheets
As at December 31, 2007 and 2006

	2007 $	2006 $
Going concern assumption (note 2)		
Assets		
Current assets		
Cash (note 5)	472,356	13,987
Restricted cash	500	-
Accounts receivable	15,628	110
	488,484	14,097
Mining properties (note 6)	975,864	-
Deferred exploration expenses (note 7)	47,430	-
	1,511,778	14,097
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities	51,222	32,325
Due to directors and officers	-	11,782
Promissory notes due to directors and officers	-	183,534
	51,222	227,641
Shareholders' Equity (Deficiency)		
Capital stock (note 8)	23,195,520	21,813,127
Warrants (note 8)	511,185	-
Contributed surplus (note 9)	532,794	460,854
Deficit	(22,778,943)	(22,487,525)
	1,460,556	(213,544)
	1,511,778	14,097

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

Approved by the Board of Directors

Laurent Hallé (signed) Director
Laurent Hallé

Sébastien Plouffe (signed) Director
Sébastien Plouffe

X-Terra Resources Corporation

(formerly Canadian Empire Exploration Corp.)
(an exploration stage company)
Consolidated Statements of Operations, Comprehensive Loss and Deficit
For the years ended December 31, 2007 and 2006

	2007 $	2006 $
Going concern assumption (note 2)		
Administrative expenses		
Insurance	16,000	1,700
Consulting	-	3,100
Professional fees	137,709	36,586
General administrative expenses	114,909	8,834
Shareholder's communication	4,363	5,408
Transfer agent and regulatory fees	39,580	28,298
Interest on promissory notes	-	8,534
Stock-based compensation (note 8)	71,940	22,263
	384,501	114,723
Other expenses (income)		
Interest income	(7,993)	(1)
Reclamation bond recovered	-	(4,398)
Forgiveness of due to directors and officers	-	(70,154)
Writeoff of accrued liability	-	(96,644)
Writeoff of exploration expenses	-	219
Writeoff of mining property cost	-	954
General exploration expenses	910	969
	(7,083)	(169,055)
Loss (income) and comprehensive loss for the year before income taxes	377,418	(54,332)
Future income tax recovery (note 12)	(86,000)	-
Net loss (income) and comprehensive loss for the year	291,418	(54,332)
Deficit – Beginning of year	22,487,525	22,541,857
Deficit – End of year	22,778,943	22,487,525
Basic and diluted net loss (income) per share (note 8)	0.06	(0.01)
Weighted average number of shares outstanding (basic and diluted) (note 8)	5,178,930	3,638,103

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

X-Terra Resources Corporation

(formerly Canadian Empire Exploration Corp.)
(an exploration stage company)
Consolidated Statements of Cash Flows
For the years ended December 31, 2007 and 2006

	2007 $	2006 $
Going concern assumption (note 2)		
Cash flows from		
Operating activities		
Net income (loss) for the year	(291,418)	54,332
Adjustments for		
Forgiveness of due to directors and officers	-	(70,154)
Writeoff of accrued liability	-	(96,644)
Stock-based compensation	71,940	22,263
Writeoff of exploration expenses	-	219
Writeoff of mining property cost	-	954
Future income tax recovery (note 12)	(86,000)	-
Other	-	(4,398)
	(305,478)	(93,428)
Changes in non-cash operating working capital items (note 10)	2,879	(100,935)
	(302,599)	(194,363)
Investing activities		
Mining properties	(25,364)	(954)
Reclamation bond returned	-	15,698
Deferred exploration expenses	(47,430)	(219)
	(72,794)	14,525
Financing activities		
Issue of common shares and warrants	959,999	1,375
Due to directors and officers	(11,782)	175,000
Share issue expenses	(114,455)	-
	833,762	176,375
Increase (decrease) in cash and cash equivalents during the year	458,369	(3,463)
Cash and cash equivalents – Beginning of year	13,987	17,450
Cash and cash equivalents – End of year	472,356	13,987
Supplementary information		
Interest paid	-	8,534

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

1 Nature of operations

The Company is in the business of acquiring, exploring and developing mining properties. As at December 31, 2007, the Company holds the Villedieu and Lindsay properties located in Canada.

2 Going concern assumption

These consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles on a going concern basis whereby it is assumed that the Company will realize its assets and assume its liabilities in the normal course of business.

The Company is in the process of exploring its mineral properties and has not yet determined whether these properties contain ore reserves. The recoverability of the amounts shown for mineral properties and related deferred expenditures is dependent upon the ability of the Company to obtain the necessary financing to complete exploration and development and upon future profitable production or proceeds from the disposition of properties. The Company will have to raise additional funds to complete the development phase of its programs and, while it has been successful in doing so in the past, there can be no assurance that it will be able to do so in the future. The application of generally accepted accounting principles on a going concern basis may be inappropriate, since there is a significant doubt as to the going concern assumption.

The financial statements do not reflect the adjustments to the carrying value of assets and liabilities, the reported amounts of revenues and expenses and the classification of balance sheet items if the going concern assumption were inappropriate, and these adjustments could be material. Management did not take these adjustments into account as it believes in the validity of the going concern assumption.

3 New accounting standards

Accounting standards newly adopted

On January 1, 2007, the Company adopted four new accounting standards related to accounting changes, financial instruments, comprehensive income and hedges that were issued by the Canadian Institute of Chartered Accountants ("CICA"). The new CICA standards are as follows.

i) Section 1506, "Accounting Changes"

This Section establishes criteria for changes in accounting policies, accounting treatment and disclosure regarding changes in accounting policies, estimates and corrections of errors. In particular, this Section allows for voluntary changes in accounting policy only when they result in the financial statements providing more reliable and more relevant information. Furthermore, this Section requires disclosure of when an entity has not applied a new source of Canadian generally accepted accounting principles ("GAAP") that has been issued but is not yet effective. Such disclosures are provided below. The adoption of this Section had no further effect on the consolidated financial statements for the year ended December 31, 2007.

ii) Section 3855, "Financial Instruments – Recognition and Measurement"

This Section establishes standards for recognizing and measuring financial assets and financial liabilities and non-financial derivatives. All financial instruments are required to be measured at fair value on initial recognition, except for certain related party transactions. Measurement in subsequent periods depends on whether the financial instrument has been classified as held for trading, available for sale, held to maturity, loans and receivables, or other liabilities.

Financial assets and financial liabilities classified as held for trading are required to be measured at fair value, with gains and losses recognized in net income.

Financial assets classified as held to maturity, loans and receivables, and financial liabilities (other than those held for trading) are required to be measured at amortized cost using the effective interest method.

Available-for-sale financial assets are required to be measured at fair value, with unrealized gains and losses recognized in other comprehensive income. Investments in equity instruments classified as available for sale that do not have a quoted market price in an active market should be measured at cost.

The Company has implemented the following classifications:

- Cash is classified as held for trading.
- The Company's accounts receivable are classified as loans and receivables.
- Accounts payable and accrued liabilities are classified as other liabilities.

iii) Section 1530, "Comprehensive Income"

This Section establishes standards for reporting and presenting comprehensive income which is defined as the change in equity from transactions and other events from non-owner sources. Other comprehensive income refers to items recognized in comprehensive income that are excluded from net income.

The classification of the Company's financial instruments as at January 1, 2007 and their subsequent changes as at December 31, 2007 have resulted in no gains or losses that require separate presentation in other comprehensive income. There was no effect on opening equity as of January 1, 2007 or on subsequent measurements as a result of applying this new standard.

iv) Section 3865, "Hedges"

This Section establishes the standard of how hedge accounting may be applied. The Company currently does not have any hedges in place, and therefore this standard has no impact on its consolidated financial statements.

New accounting standards not yet adopted

i) Section 1400, "General Standards of Financial Statement Presentation"

In June 2007, the CICA amended Section 1400 to include requirements to assess an entity's ability to continue as a going concern and disclose any material uncertainties that cast doubt on its ability to continue as a going concern. This new requirement will be effective January 1, 2008. The Company has already performed such assessment and provided adequate disclosure.

ii) Section 1535, "Capital Disclosures"

On December 1, 2006, the CICA issued this new accounting standard which will be effective January 1, 2008. Section 1535 specifies the disclosure of information that enables users of an entity's financial statements to evaluate qualitative information about its objectives, policies and processes for managing capital, summary quantitative data about what the entity manages as capital, whether it has complied with any capital requirements and, if it has not complied, the consequences of non-compliance.

iii) Section 3862, "Financial Instruments – Disclosures", and Section 3863, "Financial Instruments – Presentation"

These sections will replace Section 3861, "Financial Instruments – Disclosure and Presentation", revising and enhancing disclosure requirements while carrying forward its presentation requirements. These new sections will place increased emphasis on disclosure about the nature and extent of risks arising from financial instruments and how the entity manages those risks. The mandatory effective date is for annual and interim periods in fiscal years beginning on or after October 1, 2007. The Company will begin application of these sections effective January 1, 2008.

It is not anticipated that the adoption of sections 1535, 3862 and 3863 will impact the amounts reported in the Company's consolidated financial statements as they relate primarily to disclosure.

4 Significant accounting standards

Accounting principles

These consolidated financial statements are prepared in accordance with GAAP. The Canadian dollar is the functional and reporting currency.

Basis of consolidation

These consolidated financial statements include the accounts of the Company and its fully integrated foreign subsidiaries, Minera Reina Isabel, S.A. de C.V. ("Minera Reina") and Minera Tatemas, S.A. de C.V. ("Minera Tatemas"), which were incorporated to carry out mineral exploration and development programs in Mexico and are currently inactive.

Use of estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Significant areas where management judgment is applied are the useful life of assets for amortization purposes, the valuation of mineral properties and deferred expenditures, future income tax and valuation of stock-based compensation and warrants. Actual results could differ from those estimates.

Cash and cash equivalents

Cash and cash equivalents consist of cash on hand, bank balances and short-term deposits maturing within 90 days of the original date of acquisition.

Mining properties and deferred exploration expenses

The Company records its interests in mineral properties and areas of geological interest at cost less option payments received and other recoveries. Exploration and development costs and royalties relating to these interests and projects are capitalized on the basis of specific claim blocks or areas of geological interest until the properties to which they relate are placed into production, sold, allowed to lapse or become impaired. The Company expenses all administration costs incurred during the year. Management reviews the net carrying value of resource assets when events or changes in circumstances indicate that the carrying amount may not be recoverable.

Senior management reviews quarterly the carrying value of mining properties and deferred exploration expenses to assess whether there has been any impairment in value. In the event that mineral deposits are determined to be uncertain to recover the carrying value of any property, the carrying value is written down to fair value or written off, as appropriate. Uncertainty is defined as either when there are no financial resources available for development of mining properties for three consecutive years or when the results of the exploration work do not justify further investment.

Although management takes steps to verify title to mineral properties in which the Company may have an interest, in accordance with industry standards for the current stage of exploration of such properties, these procedures do not guarantee the Company's title. Property title may be subject to unregistered prior agreements and be in non-compliance with regulatory requirements.

Mineral property option agreements

Option payments are made at the discretion of the optionee and, accordingly, are accounted for when received. Option payments received will be treated as a reduction of the carrying value of the related mineral property and as deferred costs until the Company's costs are recovered. Option payments received in excess of costs incurred will be credited to income.

Asset retirement obligations

The Company follows the recommendations of the CICA in accounting for asset retirement obligations. Under its standards, the fair values of asset retirement obligations are recorded as liabilities on a discounted basis when they are incurred. Amounts recorded for the related assets are increased by the amount of these obligations. The liabilities will be accreted over time for the change in their present value, and the initial capitalized costs will be depleted and amortized over the useful lives of the related assets. As at December 31, 2007, the Company has no asset retirement obligations that will affect its consolidated financial statements.

Income taxes

The Company provides for income taxes using the liability method of tax allocation. Under this method, future income tax assets and liabilities are determined based on deductible or taxable temporary differences between financial statement values and tax values of assets and liabilities using substantively enacted income tax rates expected to be in effect for the year in which the differences are expected to reverse.

The Company establishes a valuation allowance against future income tax assets if, based on available information, it is more likely than not that some or all of the assets will not be realized.

Flow-through shares

The Company finances some exploration expenditures through the issuance of flow-through common shares. The resource expenditure deductions for income tax purposes are renounced to investors in accordance with the appropriate income tax legislation. The Company recognizes future income tax liability and reduces shareholders' equity when the expenditures are renounced and when the renunciation forms are filed with the tax authorities.

Foreign currency transactions and integrated foreign subsidiary

The financial statements of integrated foreign operations and transactions denominated in currencies other than the functional currency are translated into the functional currency using the temporal method. Under this method, monetary assets and liabilities in foreign currencies are translated into the functional currency at exchange rates in effect at the balance sheet date. Non-monetary assets and liabilities are translated at historical rates, unless such assets and liabilities are carried at market value, in which case, they are translated at the exchange rate in effect at the date of the balance sheet. Revenues and expenses denominated in foreign currencies are translated at the rate of exchange prevailing on each transaction date. Gains and losses on translation are included in the consolidated statement of operations.

Income (loss) per share per common share

Income (loss) per common share is calculated using the weighted average number of common shares issued and outstanding during each year. Basic and diluted income (loss) per share are the same, as the effect of exercising share options and warrants would be anti-dilutive.

Share and warrant issue expenses

Share and warrant issue expenses are recorded as a decrease in capital stock and warrants in the year in which they are incurred.

Stock-based compensation

The Company applies the fair value method to account for options granted to its directors, officers and employees. Stock-based compensation is recognized over the vesting period. Any consideration paid on exercise of stock options is credited to capital stock. The contributed surplus resulting from stock-based compensation is transferred to capital stock when the options are exercised.

5 Cash

As at December 31, 2007, cash includes an amount of $273,170 (2006 – nil) reserved for new exploration activities to be conducted in Canada before December 31, 2008 (note 13).

6 Mining properties

	Balance December 31, 2006 $	Additions $	Balance December 31, 2007 $
Villedieu (100%)	-	544,570	544,570
Lindsay (100%)	-	431,294	431,294
	-	975,864	975,864

All mining properties are located in Canada.

7 Deferred exploration expenses

	Balance December 31, 2006 $	Increase $	Balance December 31, 2007 $
Villedieu (100%)	-	600	600
Lindsay (100%)	-	46,830	46,830
	-	47,430	47,430

	2007 $	2006 $
Exploration costs		
Accommodations	2,920	-
Expediting	-	1
Maps, printing and drafting	-	841
Consulting	600	-
Assay and geochemical analysis	13,368	-
Geology	24,115	-
Geophysics	3,660	-
Project management fees	2,767	88
Property acquisition costs	-	953
Salaries and wages	-	259
Increase in deferred exploration expenses	47,430	2,142
General exploration expenses	-	(969)
Writeoff of exploration expenses	-	(219)
Writeoff of mining property expenses	-	(954)
Total deferred exploration expenses and balance – End of year	47,430	-

8 Capital stock and warrants

Capital stock

Authorized
Unlimited common shares without par value

Changes in the Company's capital stock were as follows:

	Number of shares	Amount $
Balance – December 31, 2005	3,636,433	21,811,752
Paid in cash[5]	2,500	1,375
Balance – December 31, 2006	3,638,933	21,813,127
Private placement[1]	1,000,000	205,000
Flow-through and non-flow-through private placement[4]	559,999	254,228
Mining properties[2]	1,250,000	950,500
Debt settlement[3]	327,739	183,534
Share issuance expenses[6]	-	(210,869)
Balance – December 31, 2007	6,776,671	23,195,520

Warrants

The following table details the changes in the Company's warrants:

	Number of warrants	Amount $
Balance – Beginning of year	-	-
Private placement[1]	1,000,000	355,000
Flow-through and non-flow-through private placement[4]	587,998	156,185
Balance – End of year	1,587,998	511,185

On February 23, 2007, the Company changed its name from Canadian Empire Exploration Corp. to X-Terra Resources Corporation and consolidated its capital stock as to 10 old shares of Canadian Empire Exploration Corp. for 1 new share of X-Terra Resources Corporation. All the opening figures related to the number of common shares, warrants and options outstanding have been modified to reflect this consolidation.

(1) On May 10, 2007, the Company completed a private placement of 1,000,000 units at a deemed price of $0.56 per unit for cash consideration of $560,000. Each unit consists of one common share and one common share purchase warrant. Each purchase warrant entitles the holder to purchase one common share of a price of $0.70 until May 10, 2009. From the total compensation received, $355,000 was assigned to warrants and $205,000 to capital stock, according to their respective estimated fair value.

(2) On May 10, 2007 and August 24, 2007, the company issued, in connection with the Villedieu and Lindsay properties, a total of 1,250,000 common shares at a fair value of $950,500 and a cash payment of $25,000.

(3) On May 14, 2007, the Company issued 327,739 common shares at a deemed price of $0.56 per share in settlement of $183,534 of indebtedness comprising promissory notes entered into during 2006 with private companies owned by certain individuals who were directors and/or senior officers of the Company until June 14, 2007.

(4) On October 3, 2007, the Company closed a private placement of 133,333 non-flow-through units and 426,666 flow-through units at a price of respectively $0.60 and $0.75 per unit for cash consideration of $400,000. Each non-flow-through unit consists of one non-flow-through common share and one common share purchase warrant. Each purchase warrant entitles the holder to purchase one non-flow-through common share at a price of $0.75 until October 3, 2009.

Each flow-through unit consist of one flow-through common share and one common share purchase warrant. Each purchase warrant entitles the holder to purchase one non-flow-through common share at a price of $1.00 until October 3, 2009.

From the total compensation received, $156,185 was assigned to warrants and $254,228 to capital stock, according to their respective estimated fair value.

Share issue expenses include 27,999 finder options. Each finder option consists of one non-flow-through common share and one non-transferable common share purchase warrant. Each finder option entitles the holder to purchase one non-flow-through common share of a price of $0.60 and one non-transferable common share purchase warrant at a price of $0.75 until October 3, 2009.

(5) On May 17, 2006, the Company issued 2,500 common shares on the exercise of warrants in connection with the McBride property, for gross proceeds of $1,375.

(6) Share issue expenses were not allocated on each individual transaction but on an aggregated basis. These include $86,000 for the future effect on income taxes related to flow-through shares when the renunciation forms have been filed (note 12).

Information relating to warrants outstanding as at December 31, 2007 is as follows:

Expiry date	Number of warrants outstanding	Exercise price $
May 2009	1,000,000	0.70
October 2009*	161,332	0.75
October 2009	426,666	1.00
	1,587,998	

* These include 27,999 finder options which expire in October 2009. Each finder option entitles the holder to subscribe for an equal number of units in consideration for $0.60, composed of one share and one warrant at a price of $0.75.

The fair value of the finder option was estimated using a binomial pricing model based on the following assumptions: dividend yield of 0%, volatility of 100%, risk-free interest rate of 4.14% and an expected life of two years. As a result, the fair value of the finder options was estimated at $10,414.

Except for the finder options, the warrants, when granted, are accounted for at their fair value determined by the Black-Scholes pricing model, based on the vesting period and on the following weighted average assumptions:

	2007	2006
Average dividend per share	0%	-
Volatility	94.87%	-
Risk-free interest rate	4.33%	-
Weighted average expected life	2 years	-
Weighted average fair value of warrants granted	$0.32	-

Stock options

In 2002, the Company adopted a stock option plan (the "Option Plan"), as amended, authorizing the granting of stock options to qualified optionees to purchase a total maximum of 10% of the number of outstanding issued common shares of the Company at any time. This is referred to as a "rolling plan".

Under the Option Plan, the term of stock options granted may not exceed five years following the date of grant, and the stock options must vest for a period of not less than 18 months from the date of grant, to be released and available for exercise at a rate of 25% of the number of options at the beginning of the first quarter commencing on the date of grant and at a rate of 12.5% at the beginning of each quarter thereafter.

The Company applies the fair value method of accounting for stock options, and accordingly the fair value of the vested portion of stock options granted in 2007 of $71,940 (2006 – $22,263) has been included in other expenses.

The following table summarizes the information relating to the share purchase options for the year ended December 31, 2007:

	Options outstanding	Weighted average exercise price $
Balance – December 31, 2006	392,300	1.20
Granted during the year	165,000	1.10
Cancelled	(372,400)	1.19
Balance – December 31, 2007	184,900	1.11

Information relating to options outstanding and exercisable as at December 31, 2007 is as follows:

Exercise price $	Options outstanding	Weighted average remaining contracted life (years)	Options exercisable	Weighted average remaining contracted life (years)
1.50	7,500	0.01	7,500	0.01
1.00	12,400	0.12	12,400	0.21
1.10	165,000	3.98	82,500	3.58
	184,900	4.09	102,400	3.80

The options, when granted, are accounted for at their fair value determined by the Black-Scholes option pricing model based on the vesting period and on the following weighted average assumptions:

	2007	2006
Average dividend per share	0%	-
Volatility	111%	-
Risk-free interest rate	4.71%	-
Weighted average expected life	5 years	-
Weighted average fair value of options granted	0.87	-

9 Contributed surplus

The following table details the changes in the Company's contributed surplus:

	2007 $	2006 $
Balance – Beginning of year	460,854	438,591
Stock-based compensation	71,940	22,263
Balance – End of year	532,794	460,854

10 Cash flow information

The changes in non-cash operating working capital items are as follows:

	2007 $	2006 $
Decrease (increase) in accounts receivable	(15,518)	3,220
Decrease (increase) in restricted cash	(500)	-
Increase (decrease) in accounts payable and accrued liabilities	18,897	(104,155)
	2,879	(100,935)

11 Related party transactions

Related party transactions occurred in the normal course of business and were recorded at the exchange values which is the consideration determined and agreed to by the related parties.

Until June 14, 2007, the Company was party to management agreements with Badger & Co. Management Corp., a private company owned by certain individuals who were directors and/or senior officers of the Company until that date. Pursuant to these agreements, the Company paid $15,010 during the period from January 1 to June 14, 2007.

During the period from January 1 to December 31, 2007, the Company paid $4,947 for the provision of administrative services to a company controlled by a director and $22,202 for legal services provided by a law corporation controlled by a director.

12 Income taxes

A reconciliation of the combined Canadian federal and provincial income taxes at statutory rates and the Company's effective income tax expense are as follows:

	2007 $	2006 $
Income taxes at statutory rates	(120,850)	18,538
Non-deductible (income) expenses	23,255	(25,379)
Reduction in federal tax rates and other	321,363	446,538
Change in valuation allowance	(309,768)	(439,697)
Future income tax recovery	(86,000)	-

Under the provision of Canadian Institute of Chartered Accountants ("CICA") Emerging Issues Committee ("EIC") 146 in respect of flow-through shares, a future income tax liability must be recognized and shareholders' equity reduced on the date that the company renounces the tax credits associated with flow-through expenditures, provided that there is reasonable assurance that the expenditures will be made.

Where the company has unrecognized future tax assets and the taxable temporary differences relating to the flow-through shares are expected to reverse during the loss carryforward period, these tax assets can be applied against the full taxable temporary difference. The recognition of the benefits results in a future income tax recovery.

The Company issued flow-through units for gross proceeds of $320,000 (2006 – nil). Under the flow-through share agreements, the Company agreed to renounce $320,000 of qualifying expenditures to the investors effective December 31, 2007 although, under Canadian tax law, the expenditures may actually be incurred up to December 31, 2008.

The Company is required to record a provision at the time the renunciation is filed with tax authorities, by an increase in the share and warrant issue expenses relating to the flow-through shares, for future income taxes related to the tax deductions the Company has foregone. The Company filed its renunciation with the authorities in 2007, therefore, estimated future income taxes of $86,000 were recorded as at December 31, 2007 (2006 – nil). Consequenty, the Company has recognized such expenses as share and warrant issue expenses in 2007 (2006 – nil).

The components of future tax assets are as follows:

	2007 **$**	**2006** **$**
Resource assets	694,175	360,481
Non-capital loss carryforwards	241,830	570,270
Capital losses	1,539,187	1,773,785
Other deductible tax pools	26,916	-
	2,502,108	2,704,536
Less: Valuation allowance	2,502,108	2,704,536
Future income tax recovery	-	-

At December 31, 2007, the Company has accumulated non-capital losses for income tax purposes amounting to approximately $898,000. These losses will expire as follows:

		$
Years ending December 31,	2008	263,000
	2009	-
	2010	46,000
	2014	65,000
	2015	85,000
	2026	91,000
	2027	348,000

The Company's balance of capital losses amounts to approximately $11,444,000 and can be carried forward indefinitely against capital gains.

The unamortized balance for tax purposes of share and warrant issue expenses amounting to approximately $100,000 is deductible over the next four years.

13 Commitments

The Company is committed to incurring Canadian exploration expenses of $320,000 by December 31, 2008, with regard to the transfer of these expenditures to the subscribers of its flow-through share underwriting completed on October 3, 2007. As at December 31, 2007, $46,830 has been incurred against this commitment.

14 Financial instruments

Fair value

The carrying amount of all financial assets and liabilities, as reported on the consolidated balance sheet, approximate their fair value due to the relatively short-term maturities of these instruments.

Interest rate risk

The Company's cash bears interest at variable rate. All other financial assets and liabilities are non-interest bearing.

Foreign currency risk

The Company is not exposed to currency risk as all financial assets and liabilities are denominated in Canadian dollars as are all its activities.

Credit risk

The Company has reduced its credit risk by investing its cash with a Schedule 1 Canadian chartered bank.

15 Comparative figures

Certain comparative figures have been reclassified to conform to the presentation adopted for the year ended December 31, 2007.