

Frontera Resources Corporation and Subsidiaries

**Condensed Consolidated Financial Statements
Six Months Ended June 30, 2014 and 2013**

Frontera Resources Corporation and Subsidiaries
Index
June 30, 2014 and 2013

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Frontera Resources Corporation and Subsidiaries

Condensed Consolidated Balance Sheets *(Unaudited)*

	June 30, 2014	December 31, 2013	June 30, 2013
Assets			
Current assets			
Cash and cash equivalents	\$ 360,311	\$ 1,363,533	\$ 628,337
Accounts receivable, net	390,528	242,543	1,366,310
Inventory	5,237,337	6,324,391	5,526,091
Prepaid expenses and other current assets	233,224	258,618	1,274,776
Total current assets	6,221,400	8,189,085	8,795,514
Property and equipment, net	4,874,309	2,116,417	1,122,746
Oil and gas properties, full cost method			
Properties being depleted	127,011,545	126,416,399	126,232,319
Less: Accumulated depletion	(120,570,850)	(119,988,427)	(119,469,624)
Net oil and gas properties	6,440,695	6,427,972	6,762,695
Other assets			
	175,153	285,075	131,378
Total assets	\$ 17,711,558	\$ 17,018,549	\$ 16,812,333
Liabilities and Stockholders' Deficit			
Current liabilities			
Accounts payable	\$ 2,171,332	\$ 1,152,688	\$ 1,288,807
Accrued liabilities	6,397,797	5,168,004	4,444,532
Current derivative stock warrant liabilities	-	20	16,115
Related party notes payable (Note 4)	10,592,000	4,040,000	7,205,000
Current maturities of notes payable	2,032,902	2,502,108	175,000
Total current liabilities	21,194,031	12,862,820	13,129,454
Convertible notes payable, less current portion	24,160,630	22,936,466	21,759,757
Related party notes payable (Note 4)	300,000	4,835,000	-
Derivative stock warrant liabilities	-	-	364
Total liabilities	45,654,661	40,634,286	34,889,575
Commitments and contingencies (Note 6)			
Stockholders' deficit			
Common stock	103,043	98,130	98,130
Additional paid-in capital	400,298,437	399,001,895	398,997,145
Accumulated deficit	(428,344,583)	(422,715,762)	(417,172,517)
Total stockholders' deficit	(27,943,103)	(23,615,737)	(18,077,242)
Total liabilities and stockholders' deficit	\$ 17,711,558	\$ 17,018,549	\$ 16,812,333

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

Frontera Resources Corporation and Subsidiaries
Condensed Consolidated Statements of Comprehensive Loss *(Unaudited)*

	Six Months Ended	
	June 30,	
	2014	2013
Revenue - crude oil and gas sales	\$ 3,263,214	\$ 3,146,390
Operating expenses		
Field operating and project costs	2,584,596	2,435,286
General and administrative	3,397,211	3,692,991
Depreciation, depletion and amortization	661,372	760,611
Total operating expenses	6,643,179	6,888,888
Loss from operations	(3,379,965)	(3,742,498)
Other income (expense)		
Interest expense, net	(2,224,312)	(1,859,847)
Derivative income (loss)	20	(12,288)
Other expense, net	(24,564)	(31,357)
Total other income (expense)	(2,248,856)	(1,903,492)
Net loss	(5,628,821)	(5,645,990)
Other comprehensive loss	-	-
Total comprehensive loss	\$ (5,628,821)	\$ (5,645,990)
Loss per share		
Basic and diluted	\$ (0.00)	\$ (0.00)
Number of shares used in calculating loss per share		
Basic and diluted	2,562,965,758	2,348,796,503

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

Frontera Resources Corporation and Subsidiaries
Condensed Consolidated Statement of Stockholders' Deficit *(Unaudited)*

	Common Stock	Additional Paid-in Capital	Accumulated Deficit	Total Stockholders' Deficit
Balances at December 31, 2013	\$ 98,130	\$ 399,001,895	\$ (422,715,762)	\$ (23,615,737)
Issuance of common stock	4,913	1,304,047	-	1,308,960
Stock based compensation expense	-	(7,505)	-	(7,505)
Net loss for the six-month period ended June 30, 2014	-	-	(5,628,821)	(5,628,821)
Balances at June 30, 2014	<u>\$ 103,043</u>	<u>\$ 400,298,437</u>	<u>\$ (428,344,583)</u>	<u>\$ (27,943,103)</u>

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

Frontera Resources Corporation and Subsidiaries
Condensed Consolidated Statements of Cash Flows *(Unaudited)*

	Six Months Ended June 30,	
	2014	2013
Cash flows from operating activities		
Net loss	\$ (5,628,821)	\$ (5,645,990)
Adjustments to reconcile net loss to net cash used in operating activities		
Depreciation, depletion and amortization	661,372	760,611
Debt issuance cost amortization	158,431	116,320
Noncash interest expense	2,058,152	1,720,548
Stock based compensation	(7,505)	8,615
Derivative expense (income)	(20)	12,288
Changes in operating assets and liabilities:		
Accounts receivable	(147,985)	(131,291)
Inventory	1,087,054	123,317
Prepaid expenses and other current assets	25,394	(149,841)
Accounts payable	858,500	436,534
Accrued liabilities	395,804	557,123
Net cash used in operating activities	<u>(539,624)</u>	<u>(2,191,766)</u>
Cash flows from investing activities		
Investment in oil and gas properties	(594,681)	(194,372)
Investment in property and equipment	<u>(2,677,162)</u>	<u>(197,974)</u>
Net cash used in investing activities	<u>(3,271,843)</u>	<u>(392,346)</u>
Cash flows from financing activities		
Proceeds from notes payable	698,924	—
Repayment of borrowings	(1,168,130)	(984,998)
Proceeds from issuance of common stock and warrants	1,308,960	—
Cost of debt issuance	(48,509)	—
Proceeds from related party notes payable	2,017,000	3,485,000
Net cash provided by financing activities	<u>2,808,245</u>	<u>2,500,002</u>
Net decrease in cash and cash equivalents	(1,003,222)	(84,110)
Cash and cash equivalents		
Beginning of year	1,363,533	712,447
End of period	<u>\$ 360,311</u>	<u>\$ 628,337</u>
Supplemental cash flow information		
Cash paid for interest	\$ 114,409	\$ 36,212
Non-cash investing and financing activities		
Issuance of convertible notes in lieu of interest payments	\$ 1,181,253	\$ 1,068,998
Issuance of stock in lieu of interest payments	—	1,032
Change in accrued investment in oil and gas properties	465	55,084
Change in accrued investment in non-oil and gas properties	159,679	—

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

Frontera Resources Corporation and Subsidiaries

Notes to Condensed Consolidated Financial Statements June 30, 2014 *(Unaudited)*

1. Nature of Operations

Frontera Resources Corporation, a Cayman Islands corporation, and its subsidiaries (collectively “Frontera” or the “Company”) are engaged in the development of oil and gas projects in emerging marketplaces. Frontera was founded in 1996 and is headquartered in Houston, Texas. The Company emphasizes development of reserves in known hydrocarbon-bearing basins, and is attracted to projects that have significant exploration upside. Since 2002, the Company has focused substantially all of its efforts on the exploration and development of oilfields within the Republic of Georgia (“Georgia”), a member of the former Soviet Union.

In June 1997, the Company entered into a 25-year production sharing agreement with the Ministry of Fuel and Energy of Georgia and State Company Georgian Oil (“Georgian Oil”), which gives the Company the exclusive right to explore, develop and produce crude oil in a 5,500 square kilometer area in eastern Georgia known as Block 12, hereafter referred to as the “Block 12 PSA”. The Block 12 PSA can be extended if commercial production remains viable upon its expiration in June 2022.

Under the terms of the Block 12 PSA, the Company is entitled to conduct exploration and production activities and is entitled to recover its cumulative costs and expenses from the crude oil produced from Block 12. Following recovery of cumulative costs and expenses from Block 12 production, the remaining crude oil sales, referred to as “Profit Oil,” are allocated between Georgian Oil and Frontera in the proportion of 51% and 49%, respectively.

Under the terms of the Block 12 PSA, Frontera is exempt from all taxes imposed by the government of Georgia, and any taxes imposed on the Company are paid by Georgian Oil on behalf of the Company from Georgian Oil’s 51% share of Profit Oil. Taxes are defined by the Block 12 PSA to mean all levies, duties, payments, fees, taxes or contributions payable to or imposed by any government agency, subdivision, municipal or local authorities within the government of Georgia.

On August 2, 2011, the Company completed a merger with and into a new Cayman Islands exempted company (“Frontera Cayman”), with Frontera Cayman being the surviving entity (the “Merger”). By operation of the Merger, all assets, liabilities, properties, corporate acts, plans, policies, contracts, approvals and authorizations of each of the Company and Frontera Cayman and their respective shareholders, boards of directors, committees elected or appointed thereby, officers and agents, which were effective immediately before the Merger, were vested in, assumed by or taken, as applicable, for all purposes as the acts, plans, policies, contracts, approvals and authorizations of Frontera Cayman and are effective and binding on Frontera Cayman in the same manner as they were with respect to the Company or Frontera Cayman, as the case may be, before the Merger.

Simultaneously with the Merger, Frontera Cayman entered into a Standby Equity Distribution Agreement (“SEDA”) with YA Global Master SPV, Ltd. (“YAGM”), pursuant to which YAGM has agreed (subject to certain conditions) to make available a facility (the “SEDA facility”) of up to £21.6 million (\$35.0 million) in consideration for the issue of Frontera Cayman Shares. As of June 30, 2014, approximately \$30.0 million was available to drawdown upon this facility.

Frontera Resources Corporation and Subsidiaries

Notes to Condensed Consolidated Financial Statements June 30, 2014 *(Unaudited)*

In April 2014, the Company's wholly-owned subsidiary, Frontera Resources Georgia Corporation, has signed a farmout agreement with Varang Exploration Limited ("Varang Exploration"), a wholly owned subsidiary of a privately held independent natural resources investment group, for the farmout of up to a 50% working interest in Frontera's Taribani Field and Taribani Field Complex, situated within Block 12 in Georgia. In consideration for this transaction, Frontera will receive a carry on its future expenditure on the Taribani Field and the greater Taribani Field Complex of up to approximately US\$36 million for the costs associated with a seven well drilling program over three phases. Frontera will continue to act as managing Operator for all planned operations. The Company will retain 100% working interest throughout the balance of its Block 12 holdings.

2. Liquidity and Capital Resources

The following key financial measurements reflect the Company's financial position and capital resources as of June 30, 2014, December 31, 2013, and June 30, 2013 (USD):

	June 30, 2014	December 31, 2013	June 30, 2013
Cash and cash equivalents	\$ 360,311	\$ 1,363,533	\$ 628,337
Working capital	(14,972,631)	(4,673,735)	(4,333,940)
Total debt	37,085,532	34,313,574	29,139,757

Frontera's future revenues depend on operating results from its operations in Georgia. The success of Frontera's operations is subject to various contingencies beyond management control. These contingencies include general and regional economic and political conditions, prices for crude oil, competition and changes in regulation. Frontera is subject to various additional political and economic uncertainties in Georgia which could include restrictions on transfer of funds, import and export duties, quotas and embargoes, domestic and international customs and tariffs, and changing taxation policies, foreign exchange restrictions, political conditions and regulations.

The Company has incurred net losses and negative cash flows from operations in most fiscal periods since inception. Management plans to continue to mitigate costs and raise additional financing to continue to facilitate the Company's 2014 and 2015 operating plan. Commencement of production from its Mtsarekhavi gas field in second quarter of 2014, together with periodic access to the SEDA facility (see discussion in Notes 1 and 4) should provide positive cash flows for the foreseeable future.

Notwithstanding management's plan to reduce costs and raise additional financing, the Company's viability is dependent upon producing oil and gas in sufficient quantities and marketing such oil and gas at sufficient prices to provide positive operating cash flow to the Company.

Frontera Resources Corporation and Subsidiaries

Notes to Condensed Consolidated Financial Statements June 30, 2014 *(Unaudited)*

The Company is solely responsible for providing all of the funding for the development of Block 12 in Georgia and will require additional funding in order to obtain certain levels of production and generate sufficient cash flows to meet future capital and operating spending requirements. This is dependent upon, among other factors, achieving significant increases in production, production of oil and gas at costs that provide acceptable margins, reasonable levels of taxation from local authorities, and the ability to market the oil and gas produced at or near world prices.

Management's plan for addressing the above uncertainties is partially based on forward looking events which have yet to occur, including the successful completion of its development program, and accordingly, there is no assurance that those events will transpire as initially contemplated.

3. Basis of Presentation and Summary of Significant Accounting Policies

The condensed consolidated balance sheet of the Company at December 31, 2013 was derived from the Company's audited consolidated financial statements as of that date, but does not include all disclosures required by accounting principles generally accepted in the United States of America ("US GAAP"). The condensed consolidated balance sheet at June 30, 2014 and June 30, 2013, the condensed consolidated statements of operations for the six month periods ended June 30, 2014 and 2013, the condensed consolidated statement of changes in stockholders' deficit for the six month period ended June 30, 2014, and the condensed consolidated statements of cash flows for the six month periods ended June 30, 2014 and 2013 were prepared by the Company.

In the opinion of Company management, all adjustments, consisting of normal recurring adjustments, necessary to state fairly the consolidated financial position, results of operations and cash flows were recorded. The results of operations for the six month period ended June 30, 2014 are not necessarily indicative of the operating results for a full year or of future operations.

Certain information and footnote disclosures normally included in financial statements presented in accordance with US GAAP have been condensed or omitted. The accompanying condensed consolidated financial statements should be read in conjunction with the financial statements and notes thereto contained in the Company's consolidated financial statements for the year ended December 31, 2013.

For a description of the Company's accounting policies, refer to Note 3 of the Company's 2013 consolidated financial statements.

Use of Estimates

The preparation of the condensed consolidated financial statements in conformity with US GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent asset and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

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Notes to Condensed Consolidated Financial Statements June 30, 2014 *(Unaudited)*

Estimates of oil and natural gas reserves and their values, future production rates and future costs and expenses are inherently uncertain for numerous reasons, including many factors beyond the Company's control. Reservoir engineering is a subjective process of estimating underground accumulations of oil and natural gas that cannot be measured in an exact manner. The accuracy of any reserve estimate is a function of the quality of data available and of engineering and geological interpretation and judgment. In addition, estimates of reserves may be revised based on actual production, results of subsequent exploitation and development activities, prevailing commodity prices, operating costs and other factors. These revisions may be material and could materially affect the Company's future depletion, depreciation and amortization expenses.

The Company's revenue, profitability, and future growth are substantially dependent upon the prevailing and future prices for oil and natural gas, which are dependent upon numerous factors beyond its control such as economic, regulatory developments and competition from other energy sources. The energy markets have historically been volatile and there can be no assurance that oil and natural gas prices will not be subject to wide fluctuations in the future. A substantial or extended decline in oil and natural gas prices could have a material adverse effect on the Company's financial position, results of operations, cash flows and quantities of oil and natural gas reserves that may be economically produced.

Impairment

Under the full cost method of accounting, the net book value of natural gas and crude oil properties may not exceed a calculated "ceiling." The ceiling limitation is the discounted estimated future net revenue from proved natural gas and crude oil properties plus the cost of properties not subject to amortization. In calculating future net revenues, costs used are those as of the end of the appropriate period. The prices used are the unweighted average first-day-of-the-month commodity prices for the prior twelve months. These prices are not changed except where different prices are fixed and determinable from applicable contracts for the remaining term of those contracts.

The net book value is compared to the ceiling limitation on both a quarterly and annual basis. Any excess of the net book value is written off as impairment expense. Impairment expense recorded in one period may not be reversed in a subsequent period even though higher natural gas and crude oil prices may have increased the ceiling limitation in the subsequent period. As the full cost ceiling exceeded the net capitalized costs at June 30, 2014, December 31, 2013 and June 30, 2013, there was no such reduction of the Company's carrying value of its natural gas and crude oil properties during the six month periods ended June 30, 2014 and 2013.

Fair Value Measurements

The Company's financial instruments consist primarily of cash and cash equivalents, trade receivables, trade payables, long-term debt and derivative stock warrant liabilities. Management considers the carrying values of cash and cash equivalents, trade receivables and trade payables to be representative of their respective fair values. As such, the measurement was categorized as a Level 3 measurement per the fair value hierarchy. Additionally, the derivative warrant liabilities are recorded at fair value in the accompanying balance sheets.

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The authoritative guidance related to fair value defines a hierarchy of inputs to valuation techniques based upon whether those inputs reflect assumptions other market participants would use based upon market data obtained from independent sources (observable inputs). The Company performed an analysis on its derivative warrant liabilities as of the balance sheet date. The fair value of the combined derivative stock warrant liabilities on June 30, 2014 was nil, within Level 2 of the fair value hierarchy. Refer to the fair value of debt disclosed in Note 4. The Company does not have any assets or liabilities classified within Level 3 of the fair value hierarchy.

4. Debt

Debt consists of the following:

	June 30,	
	2014	2013
Related party notes payable	\$ 10,892,000	\$ 7,205,000
Convertible notes payable	24,160,630	21,759,757
Other notes payable	2,032,902	175,000
Total debt	37,085,532	29,139,757
Less: Current notes payable	12,624,902	7,380,000
Total long-term debt	\$ 24,460,630	\$ 21,759,757

Related Party Notes Payable

On January 11, 2011, a revolving credit facility ("Credit Facility") was put in place by and between the Company, Steve C. Nicandros, a Director of the Company, and Zaza Mamulaishvili, member of the Company's senior management team (together, the "Lenders") in the amount of \$2,000,000. The \$2,000,000 borrowing limit pursuant to the Credit Facility was removed on October 30, 2012. Accordingly, during 2014 and 2013, the Company entered into a series of further notes payable governed by this Credit Facility with the Lenders in the aggregate amounts of \$2.1 million and \$5.2 million, respectively. These notes have a one-year term, bear interest of 15%, and are classified within Related Party Notes Payable on the consolidated Balance Sheet. As of June 30, 2014, the fair value of the related party notes was approximately \$9.5 million.

The further draw-downs under the Credit Facility as noted above, constitute related party transactions pursuant to the AIM Rules for Companies as the Lenders are directors or applicable employees of the Company, as the case may be. The independent directors of the Company, being all the directors excluding Steve Nicandros, consider, having consulted with finnCap, the Company's nominated adviser, that the further draw downs pursuant to the credit facility as detailed above, are fair and reasonable insofar as the Company's shareholders are concerned.

Convertible Notes Payable

During May 2007, the Company raised approximately \$67.0 million through a private placement of convertible unsecured notes due May 2012 ("2012 Notes"). The 2012 Notes were issued at par and bear interest at 10% per annum, payable quarterly in arrears in cash or in kind at the Company's discretion. The 2012 Notes are convertible into shares of common stock at conversion price of \$1.67 per share. The 2012 Notes will be automatically converted into common stock at the conversion price if the stock price exceeds two times the conversion price for at least 20 consecutive trading days. On August 2, 2011, 85.1% of the 2012 Notes were converted into common stock and another 14.6% were exchanged for the 2016 Notes (as defined below) and the remaining portion was subsequently repaid.

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Notes to Condensed Consolidated Financial Statements June 30, 2014 *(Unaudited)*

On July 3, 2008, the Company raised \$23.5 million through a private placement of convertible unsecured notes due July 2013 ("2013 Notes"). The notes were issued at par and bear interest at 10% per annum, payable quarterly in arrears in cash or in kind at the Company's discretion. The notes are convertible into common stock at a conversion price of \$1.71 per share. On August 2, 2011 84.0% of the 2013 Notes were converted into common stock and another 16.0% were exchanged for the 2016 Notes (as defined below).

On August 2, 2011, note holders exchanged \$18.2 million of 2012 and 2013 Notes into new notes issued under the 2016 Note Purchase Agreement due 2016 ("2016 Notes"). The 2016 Notes accrue interest at the rate of 10% per annum, mature five years from the date of issuance and are convertible into Frontera Cayman Shares, at the option of the holder, at a conversion rate of \$0.25 per share.

During the six month periods ended June 30, 2014 and 2013, the Company elected to pay the quarterly interest payments in kind and issued approximately \$1.2 million and \$1.1 million, respectively, in additional convertible notes in accordance with terms of the note purchase agreements.

Other Notes Payable

On June 28, 2011 the Company entered into the SEDA facility with YA Global Master SPV Ltd, an investment fund managed by Yorkville Advisors LLC providing for up to approximately £21.6 million (US\$35 million) of additional equity investment, through the issue of the new shares in the Company. As of June 30, 2014 approximately \$30 million of commitment amount was still available for drawdown. The term of the agreement is through December 31, 2015.

The Company drew down from their SEDA-backed loan agreements with YA Global Master SPV Ltd. Under these drawdowns, \$2.0 million and \$2.2 million remained outstanding as of June 30, 2014 and 2013, respectively. As of June 30, 2014, the carrying value of the other notes payable approximates fair value. The outstanding amount has the ability to be settled in cash or issuance of new shares. Future principal maturities as of June 30, 2014 for debt obligations are, as follows for the periods ending December 31:

2014		\$ 5,545,375
2015		7,379,527
2016		24,160,630
2017		-
2018		-
Total future principal payments on debt		\$ 37,085,532

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Notes to Condensed Consolidated Financial Statements June 30, 2014 *(Unaudited)*

5. Derivative Stock Warrant Liabilities

In July 2008, the Company solicited consents from holders of its 10% convertible notes due May 2012 to amend the note purchase agreements governing such notes to permit the issuance of the new notes and to release escrowed proceeds of \$5.0 million from the May 2007 private placement. In connection with the solicitation, each consenting holder received a warrant exercisable into shares of common stock in an amount equal to 7.5% of the number of shares of common stock into which such consenting holder's existing notes were convertible. The warrants are exercisable for 3,151,000 shares in the aggregate. Each warrant entitled the holder to purchase one share of common stock at a price of \$3.50 per share. Due to anti-dilution provisions contained in the warrant agreements, as of June 30, 2013 the warrants became exercisable into 77,557,078 shares in the aggregate at an exercise price of £0.089 per share. The warrants have a five-year term and include a cashless exercise provision along with other customary terms and provisions. The issuance date fair value of these warrants was estimated to be \$0.9 million and was recorded as a derivative stock warrant liability. The warrants were valued on the issuance date using the following assumptions: risk-free interest rate of 3.42%, expected volatility of 146.3%, no expected dividend yield and a term of 5 years. All of these warrants expired on July 3, 2013.

On February 8, 2011 the Company issued a warrant instrument entitling Arbuthnot, broker of Company, to purchase 500,000 Shares of Common Stock at an exercise price of £0.06 per share. These warrants expired on February 8, 2013.

On August 2, 2011 as part of the fees and commissions payable to Arbuthnot, OPL and Strand Hanson for their respective roles in the Placing, Company has issued 12,558,307 warrants with an exercise price of £0.04 per share with terms ranging from 2 to 3 years. Of these warrants, 11,870,807 expired on August 2, 2013 and 687,500 expire on August 2, 2014.

Under the terms of SEDA-backed loan agreement in respect of Initial Advance in January 2012 Yorkville had been granted 15,000,000 warrants exercisable within 2 years with an exercise price of £0.018 per share. These warrants expired on January 31, 2014.

The change in the aggregate fair value of the warrants resulted in derivative expense of \$0.00 million and \$0.01 million for the six months ended June 30, 2014 and 2013, respectively.

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Notes to Condensed Consolidated Financial Statements June 30, 2014 *(Unaudited)*

6. Commitments and Contingencies

ARAR Arbitration

In January 2008, Frontera Eastern Georgia Limited ("FEGGL") served a notice of arbitration and claim on ARAR, Inc. ("ARAR"), for breach of contract under a drilling services contract dated May 2007, specifically for, among other things, failure to commence work by the time specified in the contract, failure of the drilling rig to meet required specifications and failure to reconcile advance payments made by FEGGL with work actually performed. FEGGL terminated the contract after ARAR failed to mobilize the rig to the required location and failed to commence work as otherwise required under the contract. FEGGL claimed damages of approximately \$7.0 million in the arbitration. ARAR denied FEGGL's claims and filed counterclaims against FEGGL, seeking payments of approximately \$7.1 million for, among other things, standby charges for the period of time the rig was undergoing inspection and repairs to bring it into contract specification, early termination fees and demobilization fees. The parties entered into a settlement agreement in December 2008 pursuant to which ARAR was required to make a series of payments to FEGGL through December 2009 in the aggregate amount of \$1.25 million. The settlement resolved all outstanding claims and counterclaims between Frontera and ARAR arising out of the drilling services contract. Beginning in August 2009, ARAR defaulted on its monthly payments and remained in default on payments due August - December 2009. FEGGL applied to the arbitration panel for entry of an agreed award pursuant to the settlement agreement. The panel held a hearing on FEGGL's application in March 2010, and in April 2010 entered a final, binding award in the amount of \$1.43 million in favor of FEGGL ("Final Award").

In April 2010, FEGGL filed an action in the U.S. District Court for the Southern District of Texas ("District Court") seeking confirmation of the Final Award pursuant to the Convention on Recognition and Enforcement of Foreign Arbitral Awards of June 10, 1958 as a precursor to further enforcement action in the U.S. In May 2010, ARAR filed a counterclaim in the District Court seeking to deny confirmation and to vacate the Final Award. On August 15, 2011, the District

Court entered final judgment ("Final Judgment") confirming the Final Award and granting FEGGL total amount of \$1,552,707.01, which include total amount of the Final Award and FEGGL's attorney's fees and expenses. On September 13, 2011, ARAR appealed the Final Judgment with the United States Court of Appeals for the Fifth Circuit ("Court of Appeals"). On July 16, 2012, Court of Appeals dismissed ARAR's appeal and affirmed District Court's Judgment in its entirety. ARAR attempted to further appeal Court of Appeal's decision via "motion for rehearing"; on August 16, 2012, Court of Appeals denied ARAR's motion and affirmed its earlier decision.

In order to enforce the Final Award against assets of ARAR located in Turkey, in July 2010 FEGGL filed an enforcement action in the 4th Commercial Court in Ankara, Turkey. 4th Commercial Court conducted a series of hearings on the enforcement action, and by its order dated November 23, 2012, rejected FEGGL's request for enforcement. FEGGL filed its appeal of the court order with the appeals court in Ankara on June 7, 2013, and expects that the appeals court will reverse the lower court order. Appeals court's decision is expected sometime during the third quarter of 2013. In parallel, in July 2010 an affiliate of ARAR filed a lawsuit against FEGGL in the 7th Commercial Court in Ankara, Turkey claiming damages of \$0.3 million in connection with the exportation of the drilling rig from Georgia. On July 5, 2012, 7th Commercial Court dismissed ARAR's lawsuit in its entirety.

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In parallel to the enforcement action in Turkey, on January 13, 2012, FEGL filed a petition in the High Court of Justice, Queens Bench Division, in London, UK ("London High Court"), seeking enforcement of the Final Award in the UK against the defendants' assets located in the UK. Additionally, FELG sought an injunction prohibiting the defendants to dispose of any assets in the UK while the enforcement action is pending. On January 31, 2012, the London High Court entered an order granting FEGL's both petition for enforcement and motion for injunction. Defendants vigorously contested the court order and filed a response requesting to vacate it. On January 23, 2013, the London High Court issued its Final Charging Order affirming its earlier decision and dismissing defendants' contentions.

The Company has not recognized a receivable as of June 30, 2014 for these ongoing proceedings.

7. Subsequent Events

Events occurring after June 30, 2014 were evaluated through September 23, 2014, the date these financial statements were available to be issued, to ensure that any subsequent events meeting the criteria for recognition or disclosure were included.

In July 2014, the Company successfully completed an equity fund raising initiative of GBP 350,000. The funds have been raised through a subscription by Shard Capital Partners, LLP of 48,611,111 new ordinary shares of GBP 0.72 each in the Company.

8. Recently Issued Accounting Pronouncements

In May 2014, the FASB issued updated guidance on the reporting and disclosure of revenue recognition. The update requires that an entity recognize revenue to depict the transfer of goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. This update also requires new qualitative and quantitative disclosures about the nature, amount, timing and uncertainty of revenue and cash flows arising from customer contracts, including significant judgments and changes in judgments, information about contract balances and performance obligations, and assets recognized from costs incurred to obtain or fulfill a contract. The Partnership is currently evaluating the potential impact of this authoritative guidance on its financial condition, results of operations, cash flows and related disclosures. This guidance will be effective for the Partnership beginning in the first quarter of 2017.

In June 2014, the FASB issued new guidance related to stock compensation. The new standard requires that a performance target that affects vesting, and that could be achieved after the requisite service period, be treated as a performance condition. As such, the performance target should not be reflected in estimating the grant date fair value of the award. This update further clarifies that compensation cost should be recognized in the period in which it becomes probable that the performance target will be achieved and should represent the compensation cost attributable to the periods for which the requisite service has already been rendered. The Partnership does not expect this requirement to have a significant impact on its financial condition, results of operations, cash flows and related disclosures. This guidance will be effective for the Partnership beginning in the first quarter of 2016, with early adoption optional.