



GALE FORCETM
PETROLEUM

MANAGEMENT'S DISCUSSION AND ANALYSIS

For the year ended June 30, 2014

Prepared as at October 27, 2014



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BASIS OF PRESENTATION

Throughout this document, Gale Force Petroleum Inc. is referred to as “Gale Force Petroleum”, “we” or the “Company”. This management’s discussion and analysis of the financial condition and results of operations (“MD&A”) describes our business, the business environment, our vision and strategy as well as the critical accounting policies used by the Company, which should help the reader understand our financial statements, the principal factors affecting the results of operations, and the Company’s liquidity and capital resources. This discussion should be read in conjunction with the Company’s annual consolidated financial statements, including the notes, as at and for the years ended June 30, 2014 and June 30, 2013.

The Company’s accounting policies are in accordance with International Financial Reporting Standards (“IFRS”). All dollar amounts herein are in U.S. dollars unless otherwise indicated.

Except as otherwise specified, references herein to the exercise or the year indicate the fiscal year ended June 30, 2014, and all comparisons are to the fiscal year ended June 30, 2013.

FORWARD-LOOKING STATEMENTS

All statements in this MD&A that do not directly and exclusively relate to historical facts constitute “forward-looking statements”. These statements represent the Company’s intentions, plans, expectations and beliefs, and are subject to risks, uncertainties and other factors, of which many are beyond the control of the Company. These factors could cause actual results to differ materially from such forward-looking statements. These factors include and are not restricted to general economic and business conditions, industry conditions, volatility of commodity prices, currency exchange rate fluctuations, imprecision of reserve estimates, environmental risks, competition from other explorers, stock market volatility, the ability to access sufficient capital, the timing and size of new contracts, acquisitions and other corporate developments, the ability to attract and retain qualified employees, contractors, managers and members of the board, and other risks identified in the MD&A, as well as assumptions regarding the foregoing. The words “believe,” “estimate,” “expect,” “intend,” “anticipate,” “foresee,” “plan,” and similar expressions and variations thereof, identify certain of such forward-looking statements, which speak only as of the date on which they are made. In particular, statements relating to future performance are forward-looking statements. The Company disclaims any intention or obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise. Readers are cautioned not to place undue reliance on these forward-looking statements. You will find more information about the risks that could cause our actual results to significantly differ from our current expectations in the Risks and Uncertainties section.

DEFINITIONS, NOTES AND OTHER CAUTIONARY STATEMENTS

In this document, the abbreviations set forth below have the following meanings:

bbl	Barrel.
Mcf	Thousand cubic feet.
MMcf	Million cubic feet.
BOEs	Barrel of Oil Equivalent. <i>BOEs may be misleading, particularly if used in isolation. The BOE conversion ratio of 6 Mcf:1 bbl is based on an energy equivalency and does not represent a value equivalency at the wellhead.</i>

OVERVIEW OF THE COMPANY

Gale Force Petroleum Inc. (the “**Company**”) is a publicly-traded oil and gas company with working interests in conventional oil and gas properties in Texas, and membership interests in an LLC that owns producing Marcellus shale gas in West Virginia.

As of the end of the year ended June 30, 2014, the Company was producing 175 BOE per day (to its working interests before royalties). On August 27, 2014, the Company sold a majority interest of its Texas Reef Properties, and has signed a binding agreement to sell its Thunder Properties prior to the end of 2014. Excluding these properties, the Company is now producing 105 BOE per day (to its working interests before royalties). Also excluding these properties, as at June 30, 2014, the Company had *proved and probable* reserves of 281,000 net bbls of oil and 304,000 net Mcfs of natural gas, with the net present value of these reserves being estimated at approximately \$8.1 million using a 10% discount rate.

STRATEGY, OBJECTIVES AND PLANS

The Company’s business plan since May 2010 has been to acquire and develop oil and gas properties in the southern U.S., taking advantage the general undervaluation and underinvestment that existed in the Southern U.S. following the financial crisis and oil price collapse in 2008-2009. The funding for these acquisitions and property development projects came from a combination of equity raised through Canadian markets and low-interest U.S. bank debt.

Between May, 2010 and January, 2013, the Company completed ten important acquisitions, various smaller transactions and a land acquisition program, which, in the aggregate, increased the Company’s reserves and grew the Company’s total oil and gas production from zero to a high in 2012 of approximately 650 BOE per day (to its working interests before royalties).

However, the macroeconomic conditions that helped make the Company’s business plan initially successful have changed. Firstly, the Canadian dollar has declined by roughly 15%, reducing the buying power of funds raised from equity issued in Canada. Also, since the fall of 2012, there has been a significant reduction in demand for the shares of micro and junior oil and gas companies, resulting in a self-fulfilling cycle of decreasing liquidity, and increasing difficulty for junior oil and gas companies to raise new equity financing at reasonable or attractive valuations. At the same time, there is no longer a general undervaluation in the Southern U.S.: as the effects of the 2009 U.S. financial crisis have faded, the private oil and gas property market in the Southern U.S. is back in balance.

The Company therefore believes that its business plan to acquire and aggregate smaller properties in the Southern U.S. is no longer appropriate in view of these market trends, and continuing to pursue this business plan would be unlikely to create shareholder value. As a result, the Board of Directors of the Company initiated a strategic review last year, and has since then sold several assets to pay down debts and free-up capital, while searching for a strategic option that will provide the greatest shareholder value.

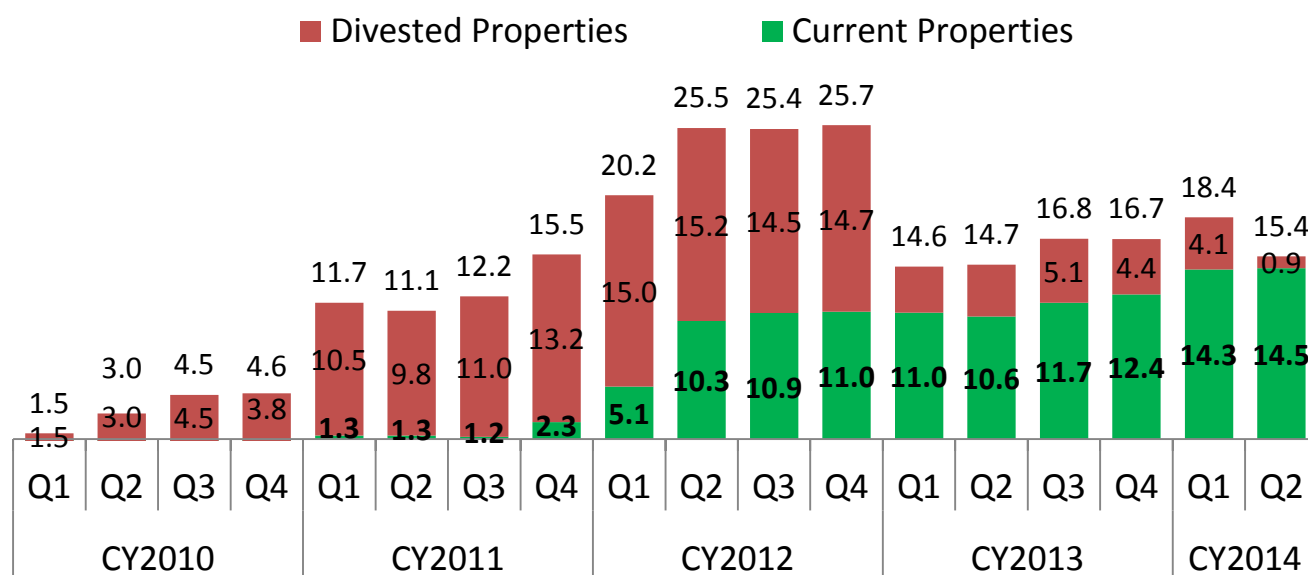
Strategic Alternative Review Process

The Company has not found an *en bloc* buyer of the Company’s assets, but has found a high level of interest in its individual properties. As a result, the Company has been selling its assets to pay down debts and free-up capital, making itself more attractive for acquisition or merger to strategic counterparts averse to debt and needing cash. The Company is currently actively evaluating various oil and gas companies or assets in North America, where there would be significant scalability in operations, and where the Company’s combination of cash and near-cash assets would have the most impact in creating value.

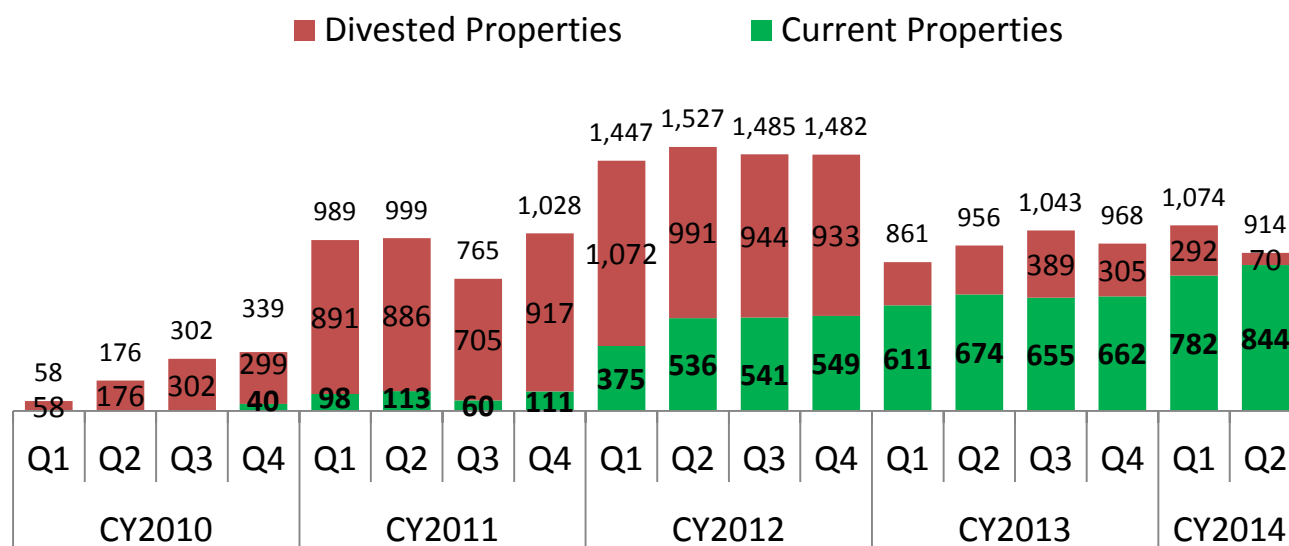
RESULTS OF OPERATIONS

The following charts illustrate the Company's growth in production and revenues in the past four and one-half years. The first chart shows production growth (gross production before royalties are deducted), and the second chart shows oil and gas revenues (after royalties and taxes are deducted) to the Company's interests:

Quarterly Production (MBOE)



Quarterly Revenue (US\$ 000's)



Comparative Financial Analysis

The following table shows selected condensed consolidated statements of financial position information:

SELECTED INFORMATION
CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

As at	June 30, 2014	June 30, 2013
Assets	\$ 17,548,833	\$ 23,185,606
Property and equipment	14,744,511	18,647,122
Oil and gas investments	1,303,388	1,896,000
Subordinate notes payable	701,255	150,000
Bank facility	4,750,000	5,500,000
Decommissioning liabilities	306,390	863,240
Shareholders' equity	\$ 10,101,909	\$ 13,976,794
Current assets	\$ 1,050,934	\$ 2,157,004
Current liabilities	\$ 2,298,108	\$ 2,845,572

During the fiscal year net property and equipment decreased by \$3.9 million. Acquisitions of \$3.6 million were offset by reductions of \$2.7 million in property sold, \$600,000 in depreciation, depletion, and amortization expense, \$500,000 reduction in capitalized decommissioning liabilities, and \$3.8 million in impairment charges. These impairment charges were generated by reducing property units to current market value as determined by 1) engineering reserve reports and 2) sales agreements made in August 2014.

Notes payable increased by \$551,255 to \$701,255. Proceeds were used to purchase additional interest in the Texas Reef property and for operational expenses. All such notes payable were fully repaid in August 2014 following the sale of a majority interest in the Texas Reef property.

Decommissioning liabilities decreased by \$556,850 due to reductions of \$438,600 attributable to properties sold and \$118,250 due to an engineering evaluation and revision of estimated net plugging liabilities.

The following table shows the Company's consolidated sales and revenues:

CONSOLIDATED REVENUES		
Fiscal years ended June 30	2014	2013
Sales	\$ 4,148,156	\$ 4,995,070
Production taxes	(190,564)	(230,494)
Total revenues	\$ 3,957,592	\$ 4,764,576

For the fiscal year revenues decreased 17% compared to the prior fiscal year. The average sales price increased 6% to \$78.52 per BOE compared to the prior year. However, production increases from the purchase of additional Texas Reef interests mentioned above and activation of additional wells in Wood County were more than offset by the sale of the remaining Gregg & Rusk Counties and non-core Wood County properties, as well as operational problems in South Texas. As a result, annual production decreased 20% compared to the prior fiscal year.

The following table shows the “Cash-Adjusted EBITDA” of the Company, which is a measure to present earnings (loss) after all cash operating expenses, while separating out any non-cash expenses and the effects of capital structure or taxation. It provides better visibility of the Company’s cash requirements and/or its ability to generate cash, exclusive of the costs of depreciation, financing or income taxes.

CASH-ADJUSTED EBITDA

Fiscal years ended June 30	2014	2013	change
Revenues	\$3,957,592	\$4,764,576	-17%
Realized (loss) gain on swaps – payments (made) received	(103,356)	445,319	-123%
Operating expenses	(1,670,431)	(2,934,260)	-43%
General and administrative expenses	(1,188,010)	(1,054,503)	13%
Cash-Adjusted EBITDA	\$ 995,795	\$1,221,132	-18%

Cash-adjusted EBITDA decreased \$225,337, or 18% for the fiscal year compared to the prior year. Realized swaps swung from \$445,319 gain in the prior fiscal year to a \$103,356 loss in the current year. Operating expense decreased \$1,263,829 between comparable periods due to the sale of properties with higher operating costs. An increase of \$133,507 in general and administrative expense between the comparable fiscal years was due principally to higher outside audit, accounting, and legal fees.

The following table shows the earnings (loss) before interest and taxes (EBIT), which is calculated by deducting non-cash operating expenses from Adjusted EBITDA, or by deducting all cash and non-cash operating expenses from revenues. We use EBIT to measure earnings (or losses) after all cash and non-cash expenses, but before taking into account the costs arising from capital structure or taxation.

EBIT

Fiscal years ended June 30	2014	2013	change
Cash-Adjusted EBITDA	\$ 995,795	\$ 1,221,132	-18%
Change in fair value of embedded derivative liabilities	1,005,663	1,940,966	-48%
Depletion, depreciation and amortization	(600,330)	(1,010,976)	-41%
Dissident shareholder dispute expense	-	(150,000)	n/a
Foreign exchange (gain) loss	(9,043)	131,455	107%
Loss on sale of assets	(79,675)	(468,169)	-98%
Loss on impairment or sale of property and equipment	(3,855,645)	(868,870)	347%
Loss on write-off of bad debts	-	(133,651)	-
(Income) loss on change in fair value of oil and gas investments	(592,612)	592,612	-200%
Restructuring costs	(162,000)	-	-
Severance tax incentives	63,193	-	-
Share-based compensation	(131,326)	(14,666)	795%
Unrealized loss on hedges	(592,105)	(930,620)	-36%
Earnings (loss) before interest and taxes	\$(3,958,085)	\$ 309,213	-1,380%

EBIT declined 1,380% to \$3,958,085 loss for the fiscal year compared to the prior year. The principal driver was a \$3,885,645 impairment expense noted above. Property values were written down based on recent reserve studies or as market values were established by sales during the fiscal year or sales agreements executed in the quarter following the end of the fiscal year. During the fiscal year the Company restored the value of its investment in the Marcellus Properties to its original cost. This resulted in the reversal of the prior year gain on change in fair value of oil and gas investments of \$592,612.

The following table shows the consolidated statements of comprehensive income of the Company:

**CONSOLIDATED STATEMENTS OF
OPERATIONS AND COMPREHENSIVE (LOSS) INCOME**

Fiscal years ended June 30	2014	2013
Sales	\$ 4,148,156	\$ 4,995,070
Production taxes	(190,564)	(230,494)
Total revenues	\$ 3,957,592	\$ 4,764,576
Change in fair value of embedded derivative liabilities	(1,005,663)	(1,940,966)
Depreciation, depletion and amortization	600,330	1,010,976
Dissident shareholder dispute expenses	-	150,000
Foreign exchange (gain) loss	9,043	(131,455)
General and administrative expenses	1,188,010	1,054,503
Loss on disposal of assets	79,675	468,169
Loss on impairment or sale of property and equipment	3,855,645	868,870
Loss on write-off of bad debts	-	133,651
Operating expenses	1,670,431	2,934,260
Realized (gain) loss on hedges	103,356	(445,319)
Restructuring costs	162,000	
Severance tax incentives	(63,193)	
Share-based compensation	131,326	14,666
Unrealized (gain) loss on hedges	592,105	930,620
Change in fair value of oil and gas investments	592,612	(592,612)
EBIT	(3,958,085)	309,213
Financial expenses	368,417	473,188
Net comprehensive income (loss)	\$ (4,326,502)	\$ (163,975)

Financial expenses for the fiscal year declined \$104,771, or 22% compared to the prior year.

Net loss for the fiscal year increased to \$4,326,502 compared to \$163,975 for the prior year period as Cash-Adjusted EBITDA (see above table) decreased 18%, or \$225,337 and net non-cash expenses increased \$4,041,961 over the comparable period.

OPERATIONS PERFORMANCE OVERVIEW

The following table shows production and revenue information from the Company's properties:

PRODUCTION SUMMARY

Fiscal years ended June 30	2014	2013	change
Total gross production (BOE)	67,158	80,373	-16%
Average sale price to the Company's revenue interests (\$/BOE)	78.52	73.91	6%
Gross revenues	\$4,148,156	\$4,995,070	-17%
Production taxes	(190,564)	(230,494)	-17%
Total revenues	\$3,957,592	\$4,764,576	-17%

In the Company's financial statements, only revenues, royalties and production taxes to the Company's interests that it receives or pays are accounted for. This difference between the sales price of oil and natural gas and the total revenues reported in the financial statements are reconciled in the table above as the difference between gross revenues and total revenues.

During the fiscal year, 93% of the Company's sales were from oil production and 7% of its sales were from natural gas production. For each barrel sold by the Company during the year, the average sales price was \$94.38. For each Mcf of natural gas sold during the year the average sales price was \$3.94. This calculates to an average sales price per BOE of \$78.42. After royalties and production taxes were paid, the Company received an average \$70.95 per barrel of oil and \$2.94 per Mcf of natural gas, for an average of \$58.93 per BOE.

The following tables show the Company's oil and natural gas netbacks:

OIL AND NATURAL GAS NETBACK

Years ended June 30	2014	2013	change	2014	2013	change
	\$/bbl	\$/bbl		\$/Mcf	\$/Mcf	
Average sale price	94.38	86.71	9%	3.94	4.76	-17%
Royalties and production taxes	23.43	25.32	-7%	1.00	1.19	-16%
Production and operations expenses	31.17	37.74	-17%	.79	1.28	-38%
Netback	39.78	23.65	68%	2.15	2.29	-6%

Oil netbacks significantly improved in the current fiscal year versus last year. This improvement is the result of \$7.67 increase in the average price of oil and the sale of lower-netback non-core properties, which had, on average, higher operating costs per barrel of production.

The average price for natural gas declined \$0.82 to \$3.94 per MCF as production in the Company's more liquids rich South Texas property declined. The sale of non-core properties with higher operating costs reduced natural gas operating expenses by 38% to \$0.79 per Mcf, compared to the prior fiscal year.

QUARTERLY OPERATING INFORMATION

The following tables summarize key financial and operating information by quarter:

QUARTERLY OPERATING INFORMATION

July 1, 2013 to June 30, 2014

Quarters ended	Sep. 30, 2013	Dec. 31, 2013	Mar. 31, 2014	Jun. 30, 2014
Production (BOE) ⁽¹⁾	13,065	13,355	14,492	12,060
Avg. price to Company's interests (\$/BOE)	83.67	76.02	76.02	75.77
Oil and natural gas revenues	\$ 1,093,199	\$ 1,015,237	\$ 1,125,956	\$ 913,764
Production taxes	(49,899)	(47,368)	(51,830)	(41,467)
Total revenues	1,043,300	967,869	1,074,126	872,297
Realized loss (gain) on hedges	(57,706)	30,124	(18,483)	(57,291)
Cash operating expenses	(730,221)	(673,987)	(743,495)	(710,738)
Cash-Adjusted EBITDA	255,373	324,006	312,148	104,268
Non-cash operating expenses	(195,817)	(232,153)	(209,133)	(131,546)
Earnings (loss) before interest and taxes	59,556	91,853	103,015	(27,278)
Financial expenses	(75,507)	(74,267)	(112,913)	(105,730)
Other (income) expenses	227,936	407,165	(113,901)	(4,706,431)
Net comprehensive income (loss)	\$ 211,985	\$ 424,751	\$ (123,799)	\$ (4,839,439)

July 1, 2012 to June 30, 2013

Quarters Ended	Sep. 30, 2012	Dec. 31, 2012	Mar. 31, 2013	Jun. 30, 2013
Production (BOE) ⁽¹⁾	22,314	21,725	12,417	12,449
Avg. price to Company's interests (\$/BOE)	71.71	70.51	69.15	80.49
Oil and natural gas revenues	\$ 1,600,144	\$ 1,531,774	\$ 861,096	\$ 1,002,056
Royalties and production taxes	(74,229)	(71,580)	(39,041)	(45,644)
Total revenues	1,525,915	1,460,194	822,055	956,412
Realized loss (gain) on hedges	134,190	185,234	61,876	64,019
Cash operating expenses	(1,283,694)	(1,398,455)	(525,865)	(1,059,399)
Cash-Adjusted EBITDA	376,411	246,973	358,066	(38,968)
Non-cash operating expenses	(389,715)	(249,414)	(230,145)	(156,368)
Earnings (loss) before interest and taxes	(13,304)	(2,441)	127,921	(195,336)
Financial expenses	(97,161)	(161,845)	(112,048)	(102,134)
Other (income) expenses	165,860	230,355	654,117	(657,959)
Net comprehensive income (loss)	\$ 55,395	\$ 66,069	\$ 669,990	\$ (955,429)

(1) Production (BOEs) are to the Company's working and net revenue interests (this compares with working interest figures in charts on page 5).

The numbers contained in the above two tables differ slightly from those in the prior published management's discussions and analyses, as certain numbers have been reclassified into the same lines for consistency, while others were adjusted to reconcile with the consolidated annual audited financial statements under IFRS for the year ended June 30, 2013.

HEDGING

To hedge risks associated with a decline in oil prices, the Company has entered into “production swaps” and purchased “price floors”, which consist of series of put options. As of the date hereof, the Company has the following hedges:

Contract Month	Production Swaps	
	Avg. Price (\$)	Quantity (bbls/Month)
July 2014 through December 2014	98.25	2,000
January 2015 through December 2015	87.32	2,000

In September, 2014 the Company unwound a portion of its swaps so that it currently has in place swaps for 1,250 barrels per month for the remainder of 2014 and 1,150 barrels per month for each month of 2015, all at the swap prices shown above.

LIQUIDITY AND CAPITAL RESOURCES

Working Capital and Source of Funds

As at June 30, 2014, the current ratio of the Company was 1.15, which is the result of \$1,331,273 of current assets divided by \$1,153,405 of current liabilities (not inclusive of non-cash payables or subordinate notes). This method of calculation is the same used by Green Bank, with which the Company has its \$4.75 million bank loan facility. The bank loan facility had a balance of \$4.75 million on June 30, 2014, but, subsequent to the end of the fiscal year, the Company sold an 81% working interest in its Texas Reef property for \$5.85 million, and, with the proceeds of the sale, repaid \$3.0 million of the bank facility, reducing the balance owing as of the date hereof to \$1.75 million.

Given the current market price for the Company’s shares, the Company generally views issuing equity as highly dilutive and not likely to result in the accretion of value once any funds are invested. However, as at June 30, 2014 and the date hereof, the Company is burning some limited cash each month to sustain operations. That said, the Company has made overhead and payroll reductions that take effect on November 1, 2014, following which the Company will be roughly cash-flow neutral from operations. Any available cash will sparingly be used by the Company to invest in crucial development projects to enhance or protect asset values.

SHARES ISSUED & OUTSTANDING, OPTIONS & WARRANTS

The following table summarizes the equity structure of the Company as of June 30, 2014 and as of the date hereof:

Security	Quantity June 30, 2014	Quantity Oct 27, 2014	Aggregate Strike Value (CA\$)
Common shares	79,043,665	79,366,703	
Preferred shares ⁽¹⁾	10,745,728	10,658,804	
Total direct ownership	89,789,393	90,025,507	
Options at \$0.15 expiring 2018	3,700,000	3,700,000	555,000
Total fully diluted	93,489,393	93,725,507	

(1) The preferred shares are convertible into common shares of the Company on a 1:1 basis.

OUTLOOK

With a view towards a strategic alternative, the Company has invested in additional in-depth engineering and geological studies of key properties, as well as in development capital spending to improve production and profitability of key assets. The Company will be seeking to conclude a strategic transaction in the near-term that will re-value the Company in the market or provide a liquidity event to shareholders at a premium to market.

As always, the Company's value is highly dependent on the strength of oil and natural prices. However, barring any significant decline in these resource prices, the Company's assets are highly-marketable in both the private and public markets. We therefore expect to garner significant interest in a strategic transaction from either prospective buyers or merger candidates, either of which should unlock significant value for shareholders.

ACCOUNTING AND DISCLOSURE

Disclosure Controls and Procedures

Management has designed such disclosure controls and procedures to provide reasonable assurance that material information relating to the Company is made known to us by others, particularly during the quarter covered by this quarterly report. We have designed such internal control over financial reporting, or caused it to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with IFRS. Management has evaluated the effectiveness of the Company's disclosure controls and procedures as of the end of the year covered by the annual filings and have caused the Company to disclose in this MD&A our conclusions about the effectiveness of the disclosure controls and procedures as of the end of the quarter covered by the quarterly filings based on such evaluation. Management has concluded that the disclosure controls and procedures are effective.

Internal Control of Financial Reporting

During the quarter, the Company updated its financial control policies as part of a process of continuous improvement. These changes continue to ensure the quality and integrity of records and accounting as well as improving the timeliness of financial information.

Non-IFRS Measures

This document contains the terms "Cash-Adjusted EBITDA", "Oil Netback" and "Gas Netback", which do not have a standardized meaning prescribed by IFRS and therefore may not be comparable with the calculation of similar measures by other companies. Cash-Adjusted EBITDA, Gas Netback and Oil Netback are used by the Company as key measures of performance. Cash-Adjusted EBITDA and Oil Netback are not intended to represent operating income (or loss) nor should they be viewed as an alternative to cash flow provided by operating activities, net earnings or other measures of financial performance calculated in accordance with IFRS. "Cash-Adjusted EBITDA" is the Company's earnings or losses after cash operating expenses, or conversely, before non-cash operating expenses, including financial expenses, taxes, write-off of deferred development costs, share-based compensation expense, depletion, depreciation and amortization. Cash-Adjusted EBITDA is used as management believes that this measure provides better visibility of our cash requirements and/or our ability to generate cash, exclusive of capital investments, exclusive of the costs to finance our activities and exclusive of income taxes. A reconciliation of this item to its closest IFRS measure may be found below. "Oil Netback" or "Gas Netback" is the average sales price of oil or natural gas less royalties, production taxes, transportation and selling expenses and production expenses. The Oil Netback or Gas Netback is used by management as a measure to provide better visibility of the efficiency our operations and their ability to generate cash, exclusive of capital investments, exclusive of the costs to finance

our activities and exclusive of income taxes. A reconciliation of this item to its closest IFRS measure may be found herein. These non-IFRS financial measures do not have any standardized meaning prescribed by IFRS and are therefore unlikely to be comparable to similar measures presented by other issuers. They should be considered as supplemental in nature and not a substitute for the related financial information prepared in accordance with IFRS.

Critical Accounting Estimates

Management is required to make judgments, assumptions and estimates in the application of IFRS principles that have a significant impact on the financial results of the Company. Capitalized costs relating to the exploration and development of oil and natural gas reserves, along with estimated future capital expenditures required in order to develop proved and probable reserves, are depleted and depreciated on a unit-of production basis using estimated proved reserves. The carrying value of property, plant and equipment is reviewed at least annually for impairment. Impairment occurs when the carrying value of the assets is not recoverable by the future undiscounted cash-flows. The cost recovery ceiling test is based on estimates of proved reserves, production rates, oil and natural gas prices, future costs and other relevant assumptions. By their nature, these estimates are subject to measurement uncertainty and the impact on the financial statements could be material. Liability recognition for decommissioning liabilities associated with oil and natural gas well sites and facilities are determined using estimated costs discounted based on the estimated life of the asset. These capitalized costs are amortized on a unit-of-production basis, consistent with depletion and depreciation. Over time, the liability is accreted up to the actual expected cash outlay to perform the abandonment and reclamation. In order to recognize share-based compensation expense, the Company estimates the fair value of stock options granted using assumptions related to interest rates, expected life of the option, volatility of the underlying security and expected dividend yields. These assumptions may vary over time. The determination of the Company's income and other tax liabilities requires interpretation of complex laws and regulations often involving multiple jurisdictions. All tax filings are subject to audit and potential reassessment after the lapse of considerable time. Accordingly, the actual income tax liability (or asset) may differ significantly from that estimate recorded on the Company's annual consolidated financial statements.

RISKS AND UNCERTAINTIES

The Company's exploration and production activities are concentrated in areas where activity is highly competitive and includes a variety of different sized companies ranging from smaller junior producers, intermediate and senior producers and royalty trust organizations, to the much larger integrated petroleum companies. The Company is subject to a number of risks that are also common to other organizations involved in the oil and gas industry. Such risks include the possibility of not being able to find and/or to develop oil and natural gas reserves economically, mis-estimating amounts of recoverable reserves, being unable to produce oil and natural gas in commercial quantities, being unable to market oil and natural gas produced, being subject to fluctuations in commodity prices, not being able to secure adequate financing and/or obtain the liquidities to discharge near-term liabilities, incurring environmental or health and safety liabilities.

Liquidity

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they become due. The Company manages this risk by monitoring its cash flows to ensure that it has enough on hand to meet its maturing liabilities.

Substantial Capital Requirements

The Company anticipates making substantial capital expenditures for the acquisition, exploration, development and production of oil and natural gas reserves in the future. As the Company may not be able to finance all such capital expenditures, the Company may be required to reduce capital expenditures. In addition, the recent global credit crisis exposes the Company to additional access to capital risk. There can be no assurance that debt or equity financing, or cash

generated by operations will be available or sufficient to meet these requirements or for other corporate purposes or, if debt or equity financing is available, that it will be on terms acceptable to the Company. The inability of the Company to access sufficient capital for its operations could have a material adverse effect on the Company's business, financial condition, results of operations and prospects.

Capital Markets

As a result of the weakened global economic situation, the Company has restricted access to capital and may face increased borrowing costs. The lending capacity of all financial institutions has diminished and risk premiums have increased independent of the Company's business and asset base. As future capital expenditures will be financed out of cash generated from operations and possible future equity sales or borrowings, the Company's ability to do so is dependent on, among other factors, the overall state of capital markets and investor demand for investments in the energy industry and in the Company's securities in particular. To the extent that external sources of capital become limited or unavailable or available on onerous terms, the Company's ability to make capital investments and maintain existing assets may be impaired, and its assets, liabilities, business, financial condition and results of operations may be materially and adversely affected as a result.

Volatility of Currency Exchange Rates, Oil and Natural Gas Prices

The Company's results of operations and financial condition will be dependent on the prices received for the Company's oil and natural gas production. Oil and natural gas prices have fluctuated widely during recent years and are subject to fluctuations in response to relatively minor changes in supply, demand, market uncertainty and other factors that are beyond the Company's control. These factors include, but are not limited to, worldwide political instability, foreign supply of oil and natural gas, the level of consumer product demand, government regulations and taxes, the price and availability of alternative fuels and the overall economic environment. Any decline in oil or natural gas prices could have a material adverse effect on the Company's operations, financial condition, proved reserves and the level of expenditures for the development of its oil and natural gas reserves. No assurance can be given that oil and natural gas prices will be at levels which will generate profits for the Company. The economics of producing from some of the Company's wells may change as a result of lower oil and natural gas prices, which could result in reduced production of oil or natural gas and a reduction in the volumes of the Company's reserves. See "Risk Factors – Significant Factors or Uncertainties Affecting Reserves or Resource Data". The Company might also elect not to produce from certain wells at lower oil and natural gas prices. All of these factors could result in a material decrease in the Company's future net production revenue, causing a reduction in its oil and gas acquisition and development activities.

The Company is exposed to market risk to the extent that the demand for oil and natural gas produced by the Company exists within Canada and the United States. External factors beyond the Company's control may affect the marketability of oil and natural gas produced. These factors include commodity prices and variations in the Canada-United States currency exchange rate, which in turn respond to economic and political circumstances throughout the world. Oil prices are affected by worldwide supply and demand fundamentals while natural gas prices are affected by North American supply and demand fundamentals.

Oil and natural gas prices are expected to remain volatile for the near future as a result of market uncertainties over the supply and demand of these commodities due to the current state of the world economies, OPEC actions and the ongoing global credit and liquidity concerns.

Global Financial Crisis

Recent market events and conditions, including disruptions in the international credit markets and other financial systems and the deterioration of global economic conditions, have caused significant volatility to commodity prices. These conditions worsened in 2008, continued in 2009, and are continuing in 2010, causing a loss of confidence in the broader Canada, U.S. and global credit and financial markets and resulting in the collapse of, and government intervention in, major banks, financial institutions and insurers and creating a climate of greater volatility, less liquidity, widening of credit spreads, a lack of price transparency, increased credit losses and tighter credit conditions. Notwithstanding various actions by governments, concerns about the general condition of the capital markets, financial instruments, banks, investment banks, insurers and other financial institutions caused the broader credit markets to further deteriorate and stock markets to decline substantially. These factors have negatively impacted company valuations and will impact the performance of the global economy going forward. These factors may impact the ability of the Company to obtain equity or debt financing in the future and, if obtained, on terms favourable to the Company. If these increased levels of volatility and market turmoil continue, the Company's operations could be adversely impacted and the trading price of Common Shares could continue to be adversely affected.

The Company is Dependant on its Key Personnel

The Company is dependent upon its President and CEO, its COO, its CFO and its contracted personnel responsible for exploration and development of the Company's properties. The loss of services of any member of the management team could have a material adverse impact on the Company. The Company faces significant competition for qualified personnel and there can be no assurance that it will be able to attract and retain such personnel. The Company does not currently have a formal succession program or management training program in place for succession or training of management.

Changes to Government Taxes and Royalties

In addition to U.S. and Canadian federal regulations, each state and province has legislation and regulations which govern corporate taxation, land tenure, royalties, production rates, environmental protection and other matters. The corporate taxes, severance taxes, production taxes and government royalties payable are significant factors in the profitability of producing crude oil, natural gas liquids and natural gas production. With or without notice, any of these bodies may make changes to corporate taxation, land tenure, royalties, production rates, environmental protection and other matters, which could have a material impact on the business of the Company.

Significant Factors or Uncertainties Affecting Reserves and Resource Data

There are numerous uncertainties inherent in estimating quantities of proved reserves, including many factors beyond the control of the Company. The reserve and resource data included herein represent estimates only. In general, estimates of economically recoverable oil and natural gas reserves and the future net cash flows therefrom are based upon a number of variable factors and assumptions, such as historical production from the properties, the assumed effects of regulation by governmental agencies and future operating costs, all of which may vary considerably from actual results. Accordingly, estimates of the economically recoverable oil and natural gas reserves attributable to any particular group of properties, classification of such reserves based on risk of recovery and estimates of future net revenues expected therefrom, prepared by different engineers or by the same engineers at different times, may vary substantially. The actual production, revenues, taxes and development and operating expenditures of the Company with respect to these reserves will vary from such estimates, and such variances could be material. Estimates with respect to proved reserves that may be developed and produced in the future are often based upon volumetric calculations and upon analogy to similar types of reserves rather than actual production history. Estimates based on these methods are generally less reliable than those based on actual production history. Subsequent evaluation of the same reserves based upon production history will result in variations, which may be substantial, in the estimated reserves. Consistent with the securities disclosure legislation and policies of

Canada, as interpreted by the securities regulatory authorities in Canada, the Company has used forecast prices and costs in calculating reserve quantities included herein. Actual future net cash flows also will be affected by other factors such as actual production levels, supply and demand for oil and natural gas, curtailments or increases in consumption by oil and natural gas purchasers, changes in governmental regulation or taxation and the impact of inflation on costs. The reserve value may be affected by changes in corporate, production or severance taxes or government royalties. The Company is required to perform a ceiling test annually to determine any impairment concerns on its oil and natural gas assets.

Competitive Conditions

The Company actively competes for reserve acquisitions, exploration leases, licenses and concessions and skilled industry personnel with a substantial number of other oil and gas companies, many of which have significantly greater financial resources and personnel than the Company. The Company's competitors include major integrated oil and gas companies and numerous other independent oil and gas companies and individual producers and operators. The oil and gas industry is highly competitive. Certain of the Company's customers and potential customers are themselves exploring for oil and natural gas, and the results of such exploration efforts could affect the Company's ability to sell or supply oil or natural gas to these customers in the future. The Company's ability to successfully bid on and acquire additional property rights, to discover reserves, to participate in drilling opportunities and to identify and enter into commercial arrangements with customers will be dependent upon developing and maintaining close working relationships with its future industry partners and joint operators and its ability to select and evaluate suitable properties and to consummate transactions in a highly competitive environment.

Business Cycle and Seasonality

The Company's revenue from the sale of natural gas is highly seasonal, with demand for natural gas rising during cold winter months and hot summer months.

Need to Replace and Grow Reserves

The Company's future oil and natural gas reserves and production, and therefore its cash flows, are highly dependent upon success in exploring and/or exploiting its current reserve base and acquiring or discovering additional reserves. Without reserve additions through exploration, acquisition or development activities, the Company's reserves and production will decline over time as reserves are exploited. The business of exploring for, developing or acquiring reserves is capital intensive. To the extent cash flows from operations are insufficient and external sources of capital become limited or unavailable, the Company's ability to make the necessary capital investments to maintain and expand its oil and natural gas reserves will be impaired. In addition, there can be no assurance that the Company will be able to find and develop or acquire additional reserves to replace production at acceptable costs.

Environmental Protection Requirements

All phases of the oil and gas business present environmental risks and hazards and are subject to environmental regulation pursuant to a variety of international conventions and federal, state, provincial, county, and municipal laws and regulations. Environmental legislation provides for, among other things, restrictions and prohibitions on spills, releases or emissions of various substances produced in association with oil and gas operations. The legislation also requires that wells and facility sites be operated, maintained, abandoned and reclaimed to the satisfaction of applicable regulatory authorities. Compliance with such legislation can require significant expenditures and a breach may result in the imposition of fines and penalties, some of which may be material. Environmental legislation is evolving in a manner expected to result in stricter standards and enforcement, larger fines and liability and potentially increased capital expenditures and operating costs. The discharge of oil, natural gas or other pollutants into the air, soil or water may give rise to liabilities to foreign governments and third parties and may require the Company to incur costs to remedy such discharge. No assurance can be given that

environmental laws will not result in a curtailment of production or a material increase in the costs of production, development or exploration activities or otherwise adversely affect the Company's financial condition, results of operations or prospects.

Operating Hazards and Other Uncertainties

Acquiring, developing and exploring for oil and natural gas involves many risks, which even a combination of experience, knowledge and careful evaluation may not be able to overcome. These risks include, but are not limited to, encountering unexpected formations or pressures, premature declines of reservoirs, blow-outs, equipment failures and other accidents, cratering, sour gas releases, uncontrollable flows of oil, natural gas or well fluids, adverse weather conditions, pollution, other environmental risks, fires and spills. Although the Company intends to maintain insurance in accordance with customary industry practice, the Company is not fully insured against all of these risks. Losses resulting from the occurrence of these risks could have a material adverse impact on the Company. Like other oil and gas companies, the Company attempts to conduct its business and financial affairs so as to protect against political and economic risks applicable to operations in the jurisdictions where the Company operates but there can be no assurance that the Company will be successful in so protecting itself. The Company is also subject to deliverability uncertainties related to the proximity of its reserves to pipeline and processing facilities and the possible inability to secure space on pipelines, which deliver oil and natural gas to commercial markets.

Issuance of Debt

From time to time, the Company may enter into transactions to acquire assets or the shares of other companies. These transactions may be financed partially or wholly with debt, which may increase the Company's debt levels above industry standards. Neither the Company's articles nor its by-laws limit the amount of indebtedness that the Company may incur. The level of the Company's indebtedness from time to time could impair the Company's ability to obtain additional financing in the future on a timely basis to take advantage of business opportunities that may arise.

Conflicts of Interest

Certain of the directors of the Company are also directors and officers of other companies, and conflicts of interest may arise between their duties as directors of the Company and as officers and directors of such other companies.

Dilution and Future Issuances of Common Shares

The Company may issue additional common or preferred shares in the future, which may dilute a shareholder's holdings in the Company. The Company's articles permit the issuance of an unlimited number of Common Shares and an unlimited number of Preferred Shares, which are issuable in series, and the Company shareholders will have no pre-emptive rights in connection with such further issuances. The Company's Board has the discretion to determine the provisions attaching to any series of Preferred Shares and the price and the terms of issue of further issuances of such shares.

Governmental Regulation

The oil and gas business is subject to regulation and intervention by governments in such matters as the awarding of exploration and production interests, the imposition of specific drilling obligations, environmental protection controls, control over the development and abandonment of fields (including restrictions on production) and possibly expropriation or cancellation of contract rights. As well, governments may regulate or intervene with respect to prices, taxes, royalties and the exportation of oil and natural gas. Such regulation may be changed from time to time in response to economic or political conditions. The implementation of new regulations or the modification of existing regulations affecting the oil and

gas industry could reduce demand for oil and natural gas, increase the Company's costs and have a material adverse impact on the Company.

Management of Growth


The business plan of the Company includes the acquisition of additional oil and natural gas properties. This will place additional strains on the Company's financial and human resources. The future success of the Company is dependent upon its ability to successfully manage the integration of such new properties and the required expansion of its management and financial resources that will result.

ADDITIONAL INFORMATION

The Company is an issuer in accordance with the securities legislations of all the Canadian provinces; therefore it has the obligation to deliver financial statements, proxy circulars and annual notices to the various regulating authorities. You can obtain a copy of such documents free of charge by sending your requests to the Company or by visiting www.SEDAR.com.



Michael McLellan, CFA
Chief Executive Officer



Don DeMoss, CPA
Chief Financial Officer