

MANAGEMENT DISCUSSION & ANALYSIS

YEAR ENDED DECEMBER 31, 2008

The following management discussion and analysis (“MD&A”) is prepared as of March 17, 2009. This MD&A, as provided by the management of PetroFalcon Corporation (“PetroFalcon”, the “Company” or “we”), should be read in conjunction with the Company’s audited consolidated financial statements for the years ended December 31, 2008, and 2007. These financial statements have been prepared in accordance with Canadian generally accepted accounting principles (“Canadian GAAP”). Estimates and forward-looking information are based on assumptions of future events and actual results may vary from these estimates; see “Cautionary Statement Regarding Forward-Looking Information”. All dollar amounts are expressed in US dollars (“USD”).

In 2007, the Company reviewed the accounting for foreign currency transactions in Venezuela due to the increasing spread between the official rate and the implied market rate in Venezuela. It was determined that as a consequence of the rapid decline in the valuation of the Venezuelan Bolivar (“Bs”) as reflected in the implied market for foreign currencies in Venezuela that the method of translation from Bolivars to US dollars using the official rate was no longer appropriate. In addition, effective January 1, 2008, the currency unit of the monetary system of Venezuela dropped three zeros, and all amounts are now denominated in a new smaller scale of Bolivars. For the years ended December 31, 2008, and 2007, the Bolivar balances were translated at implied market rates of 5.70 Bs/USD and 5.74 Bs/USD, respectively.

For the purposes of calculating Mixed Company production, natural gas has been converted to a barrel of oil equivalent (“boe”) using a conversion rate of six thousand cubic feet (“mcf”) equal to one barrel (6:1) based on an energy equivalency conversion method primarily applicable at the burner tip and which does not represent a value equivalency at the wellhead. This conversion to boe may be misleading, particularly if used in isolation.

CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING INFORMATION

Forward-looking information and statements are included throughout this MD&A and include, but are not limited to, statements with respect to the Venezuelan joint venture mixed companies, PetroCumarebo and Baripetrol (“Mixed Companies”); royalty payments; oil and natural gas production; general and administrative expenses; future income tax; future drilling; planned growth and development; contractual obligations; new projects; forecasted production; future plans, objectives and results. The above constitute forward-looking information, within the meaning of applicable Canadian securities legislation, which involves risks, uncertainties and assumptions, including, without limitation, risks associated with operating exclusively in a foreign jurisdiction; being a minority partner in a Mixed Company; being dependent on dividends from a Mixed Company; the imposition of higher royalties and income taxes; the impact of general economic conditions in Venezuela and world-wide industry conditions, including the adoption of environmental, tax and other laws and changes in how they are interpreted and enforced; the existence of operating risks in finding, developing and producing oil and natural gas; volatility of oil and natural gas prices; oil and natural gas product supply and demand; processing facility access; risks inherent in the ability to generate sufficient cash flow from operations to meet current and future obligations; stock market volatility; commodity prices; interest rates; opportunities available to or pursued by the Company; and other factors, many of which are beyond our control.

All such forward-looking information is based on certain assumptions and analyses made by us in light of our experience and perception of historical trends, current conditions and expected future developments, as well as other factors we believe are appropriate in the circumstances. The foregoing factors, assumptions and risks are not exhaustive and are further discussed in PetroFalcon’s most recent annual information form available on SEDAR at www.sedar.com. Actual results, performance or achievements could differ materially from those expressed in, or implied by, such forward-looking information and, accordingly, no assurance can be given that any of the events anticipated by the forward-looking information will transpire or occur, or if any of them do so, what benefits will be derived from them. Investors should not place undue reliance on forward-looking information. Statements relating to “reserves” are also deemed to be forward-looking information as they involve the implied assessment, based on certain estimates and assumptions that the reserves described can be profitably produced in the future. Except as required by law, PetroFalcon and its subsidiary do not intend to update or revise any forward-looking information, whether as a result of new information, future events or otherwise. The information contained in this MD&A is expressly qualified by this cautionary statement.

PETROFALCON'S BUSINESS ENVIRONMENT

Description of Business

PetroFalcon Corporation is engaged in the exploration, development, production and management of oil and natural gas properties. Through its wholly-owned Venezuelan subsidiary, Vinccler Oil and Gas, C.A. (“Vinccler Venezuela”), PetroFalcon owns 40% of PetroCumarebo, S.A. (“PetroCumarebo”) and 5% of Baripetrol, S.A. (“Baripetrol”). PetroFalcon previously held its interest in Baripetrol through another Venezuelan subsidiary, Lundin Latina de Petr leos, S.A. (“Lundin Venezuela”), which was merged with Vinccler Venezuela on December 31, 2008, and ceased to exist.

PetroCumarebo holds all of the operating rights to the East and West Falcon blocks, an area of approximately 838,000 acres in north-western Venezuela. The Falcon area is strategically located in close proximity to the Paraguana Refinery Complex (“PRC”), one of the largest refinery complexes in the world. The oil and gas produced from the East and West Falcon blocks is sold to the state-owned oil and gas company, Petr leos de Venezuela, S.A. (“PDVSA”), and is either trucked or shipped by pipelines to the PRC.

Baripetrol holds all of the operating rights to the Colon Block, an area of approximately 297,000 acres in western Venezuela. The oil and gas produced from the Colon Block is sold to PDVSA and shipped by pipelines to PDVSA’s distribution network.

PDVSA has announced its intention to decrease the number of mixed companies by merging individual mixed companies that have common characteristics, such as location and the types of crude oil produced, into new, larger mixed companies. PDVSA will maintain a 60% participation in these new mixed companies, and the private parties will negotiate their pro forma interest based on each private party’s estimated fair value derived from the potential future dividends from the mixed companies. It is not yet known whether this consolidation will impact PetroCumarebo or Baripetrol.

PetroFalcon’s Industry Performance

There was a severe decline in global crude oil prices during the second half of 2008, decreasing the oil prices received by the Mixed Companies. Given the current market conditions, management expects a reduction in the potential dividends from our Venezuelan investments over the next twelve months. The stability of future oil markets is subject to a variety of factors including political considerations, worldwide economic conditions and actions of the Organization of Petroleum Exporting Countries (“OPEC”) and other major oil producing countries. It is very difficult to correctly project future prices in the current economic environment, and the Company anticipates a significant level of volatility over the next twelve to twenty-four months.

The Company’s management performed impairment tests for its investments in oil and gas companies as of December 31, 2008, and identified an impairment loss of \$6.8 million from its investment in Baripetrol when comparing book value to the fair value at projected oil prices. Please see “Critical Accounting Policies and Estimates”.

PETROFALCON'S SIGNIFICANT ACQUISITIONS AND BUSINESS UPDATE

Lundin Transaction

On February 1, 2008, PetroFalcon acquired 100% of the issued and outstanding shares of Lundin Venezuela, a holding company incorporated in Venezuela. Lundin Venezuela owned 5% of Baripetrol, a Venezuelan mixed company between PDVSA, Tecpetrol de Venezuela, S.A. and Perenco Oil and Gas International Limited. Baripetrol operates the Colon Block in western Venezuela and has current onshore production of oil and natural gas.

The Company acquired Lundin Venezuela from Lundin Petroleum BV (“Lundin BV”), a wholly-owned subsidiary of Lundin Petroleum AB (“Lundin Petroleum”), in consideration for the issuance of 57,254,505 common shares of the Company at a deemed price of CDN\$0.80 per share. At closing, Lundin Venezuela had approximately \$22 million in cash.

Concurrent with the acquisition, Lundin BV subscribed for 6,665,995 units of PetroFalcon at a purchase price of CDN\$0.80 per unit, resulting in additional proceeds to the Company of approximately \$5.1 million. Each unit consists of one common share and approximately 0.75 warrants, such that Lundin BV now holds an aggregate of 5 million warrants. Each whole warrant expires on February 1, 2010, and is exercisable for one common share of PetroFalcon upon payment of CDN\$1.20 per share.

In total, Lundin BV acquired 63,920,500 common shares, representing 42% of the issued and outstanding common shares of PetroFalcon on an undiluted, post-closing basis, plus 5 million warrants of the Company. All of PetroFalcon's outstanding stock options vested immediately at the closing of the transactions with Lundin BV due to the change of control provision in the stock option agreements.

As part of the transactions with Lundin Petroleum, PetroFalcon appointed two members to the Board of Directors of the Company: Ashley Heppenstall, President and CEO of Lundin Petroleum, and John Craig, a partner of Cassels Brock & Blackwell LLP, a law firm in Toronto.

During the year ended December 31, 2008, Lundin Venezuela received \$2.9 million in dividends from Baripetrol for operations between January and December 2007. According to the sale and purchase agreement between PetroFalcon and Lundin BV, all 2007 Baripetrol dividends received by Lundin Venezuela were for the benefit of PetroFalcon. The dividends have been credited against the historical cost of the investment instead of being recognized as income during the year ended December 31, 2008, because the dividends were related to earnings before the closing of the transaction.

Anadarko Transaction

On April 7, 2008, PetroFalcon announced the signing of a binding sale and purchase agreement for the acquisition of 100% of the issued and outstanding shares of Anadarko Venezuela Company (“Anadarko Venezuela”) from an affiliate of Anadarko Petroleum Corporation (“Anadarko Petroleum”) for \$200 million in cash. The agreement was subject to the approval of the Venezuelan Ministry of Energy and Petroleum (“MEP”). Anadarko Venezuela indirectly

owns 18% of Petroritupano, S.A. (“Petroritupano”), a mixed company with PDVSA and Petrobras Energia, S.A.

Upon executing the sale and purchase agreement with Anadarko Petroleum, PetroFalcon delivered \$5 million (or 2.5% of the purchase price) in cash to Anadarko Petroleum as a guarantee for the transaction.

At PetroFalcon’s request, Lundin Petroleum provided a guarantee to Anadarko Petroleum for the full purchase price. In consideration for the guarantee, PetroFalcon agreed to issue 17.1 million common shares of the Company to Lundin Petroleum or one of its subsidiaries, subject to regulatory approval. On April 11, 2008, PetroFalcon issued 7.1 million of these shares to Lundin Petroleum. The initial shares were expensed by the Company as stock-based financing fees over the effective period of the sale and purchase agreement. The remaining 10 million shares that would have been due at closing were not issued, in accordance with the agreement with Lundin Petroleum.

On October 8, 2008, the Company announced in a press release that it had been advised that MEP denied approval for the acquisition of Anadarko Venezuela because PDVSA intended to acquire Anadarko Petroleum’s interest in Petroritupano. On October 17, 2008, Anadarko Petroleum returned \$5.1 million to PetroFalcon, including the cash deposit and accrued interest.

Chevron – Cardon III Block

On February 26, 2007, Vinccler Venezuela and Chevron Corporation (“Chevron”) announced the signing of a Heads of Terms agreement whereby Vinccler Venezuela would acquire a 30% interest from Chevron in the offshore natural gas license for the Cardon III Block (“Cardon III”) in the Gulf of Venezuela.

On March 9, 2007, Vinccler Venezuela paid Chevron \$2.2 million, which included 30% of all Chevron’s costs related to the Cardon III Block before the effective date of the transaction. On April 9, 2008, Vinccler Venezuela paid Chevron an additional \$3.2 million for its 30% share of costs related to the Cardon III Block in 2007. The transaction was subject to the approval of MEP.

On December 29, 2008, the Company terminated the agreement to acquire a 30% interest in the Cardon III Block due to the tightening global capital markets. On January 19, 2009, Chevron returned \$5.8 million to Vinccler Venezuela, which included all amounts paid to Chevron plus accrued interest.

Repsol YPF – Cardon IV Block

On March 12, 2008, PetroFalcon announced the signing of a letter of intent with Repsol YPF, S.A. (“Repsol”), whereby Vinccler Venezuela intended to acquire 25% of the Cardon IV Block (“Cardon IV”) in the Gulf of Venezuela. The transaction was subject to the approval of MEP, as well as the negotiation and execution of a sale and purchase agreement.

The Company has since terminated the negotiation of the sale and purchase agreement with Repsol. PetroFalcon chose not to proceed with Cardon IV due to the increased risk associated

with the block after a detailed review of the 3D seismic data. PetroFalcon made no payments to Repsol for Cardon IV expenses, and the Company has no ongoing capital commitment for Cardon IV.

PETROCUMAREBO AND BARIPETROL 2008 Q4 PRODUCTION

The following tables outline the gross production for the Venezuelan mixed companies in which PetroFalcon holds interests.

PetroCumarebo Production Summary:

	Three months ended Dec 31, 2008	Three months ended Dec 31, 2007
Average daily production		
Oil - bbls/d	814	903
Natural gas - mcf/d	13,952	9,678
Total – boe/d	3,139	2,516

Note: Production is shown before royalties of 33.33%. PetroFalcon owns 40% of PetroCumarebo.

As detailed in the table above, PetroCumarebo’s average gross production from both the East and West Falcon blocks for the three months ended December 31, 2008, was 3,139 boe/d. For the comparable period ended December 31, 2007, PetroCumarebo’s average gross production was 2,516 boe/d.

PetroCumarebo produces light sweet crude oil that sells at a premium to most of the oil produced in Venezuela. PetroCumarebo’s oil production from the East and West Falcon blocks is delivered to PDVSA at a weighted average price of approximately 100% of the price of West Texas Intermediate (“WTI”) crude oil.

Effective April 15, 2008, the Law of Special Contribution to Extraordinary Prices at the Hydrocarbons International Market (“Windfall Profits Tax”) was implemented by the Venezuelan government. The Windfall Profits Tax establishes a special tax payable to the Venezuelan government when the average of the Venezuelan basket of crude oil prices as published by MEP exceeds \$70 per barrel. The tax is calculated as 50% of the increment between \$70 and \$100 per barrel for the Venezuelan basket plus 60% of the increment above \$100 per barrel for the Venezuelan basket. Given the severe decline in oil prices in the second half of 2008, the Windfall Profits Tax was not applicable for most of the fourth quarter of 2008.

Payment from PDVSA to PetroCumarebo is 100% in US dollars for crude oil and natural gas liquids and 100% in Bolivars for methane gas. Potential dividends from PetroCumarebo to PetroFalcon will be in US dollars and are at the discretion of the shareholders of PetroCumarebo, depending on net and available profits. To date, PetroFalcon has not received any dividends from PetroCumarebo for the Company’s 40% interest in PetroCumarebo. Management expects to receive dividends for PetroCumarebo’s operations in 2007 and 2008, but the timing of these dividends is uncertain.

Baripetrol Production Summary:

	Three months ended Dec 31, 2008	Three months ended Dec 31, 2007
Average daily production		
Oil - bbls/d	8,907	9,060
Natural gas - mcf/d	6,567	5,560
Total – boe/d	10,001	9,987

Note: Production is shown before royalties of 33.33%. PetroFalcon owns 5% of Baripetrol, but the comparable period is before the closing of the acquisition on February 1, 2008.

As detailed in the table above, Baripetrol's average gross production from the Colon Block for the three months ended December 31, 2008, was 10,001 boe/d. For the comparable period ended December 31, 2007, Baripetrol's average gross production was 9,987 boe/d. Production has been maintained at consistent levels recently due to work-over jobs and pump changes, with two work-over rigs and one pulling unit under long-term contract.

Baripetrol's oil production is delivered to PDVSA at an average price that is approximately 92% of WTI.

Payment from PDVSA to Baripetrol is 100% in US dollars for crude oil and natural gas liquids and 100% in Bolivars for methane gas. Dividends from Baripetrol to PetroFalcon are paid in US dollars and are at the discretion of the shareholders of Baripetrol, depending on net and available profits. During the year ended December 31, 2008, PetroFalcon received \$2.9 million in dividends from Baripetrol for operations between January and December 2007. The dividends were credited against the historical cost of the investment instead of being recognized as income during the year ended December 31, 2008, because the dividends were related to pre-acquisition earnings. Management expects to receive a dividend for Baripetrol's 2008 operations, but the timing of the dividend is uncertain.

PETROCUMAREBO AND BARIPETROL 2008 CAPITAL EXPENDITURES

During 2008, the following capital expenditures for PetroCumarebo and Baripetrol were met by the Mixed Companies' respective cash flow or other sources of financing, without cash calls to PetroFalcon.

PetroCumarebo 2008 Capital Expenditures:

(\$000s)	Gross Initial Budget 2008	Gross Actual Incurred 2008
Drilling and Work-overs		
- La Vela	9,400	14,541
- Cumarebo	8,700	21,549
- West Falcon	400	-
- Total Drilling and Work-overs	18,500	36,090
Processing Facilities and Infrastructure		
- La Vela	4,230	600
- Cumarebo	3,770	945
- West Falcon	3,500	3,065
Total Processing Facilities and Infrastructure	11,500	4,610
Total Capital Budget	30,000	40,700

PetroCumarebo's initial capital expenditures budget of \$30 million was revised in the second half of 2008 to \$42.5 million due to operational delays and the strengthening of the implied market rate for the Bolivar against the US dollar (approximately 80% of drilling costs are Bolivar-based). Actual capital spending for 2008 was \$40.7 million.

During 2008, PetroCumarebo drilled a total of seven wells: three development wells and two appraisal wells in the Cumarebo Field and two development wells in the La Vela Field. This drilling campaign resulted in two successful oil wells in the southern part of the La Vela Field, one successful gas well, one non-commercial gas well, two wells that failed to meet their main objective but that will be tested in other sands, and one dry hole in the Cumarebo Field. PetroCumarebo's gross production increased from a monthly average of 2,221 boe/d in January 2008 to 2,808 boe/d in December 2008.

During the fourth quarter of 2008, PetroCumarebo drilled the LV-23 development well in La Vela to a depth of 6,550 feet. The objective was to develop the proven reserves of the Cerro Pelado LV-6 reservoir, already productive in LV-6X, located north of LV-23 in the same structural block. According to logs, the well encountered 60 feet of oil sands in Cerro Pelado, 11 feet in the Cauderalito Member of the Agua Clara formation and 31 feet in the Pedregoso Superior 1A.

On December 1, 2008, the LV-23 well was shot in several intervals of Pedregoso Superior 1A, Cauderalito and Cerro Pelado. The well was completed in Pedregoso Superior 1A and the Cauderalito Member, with an initial production of 560 bbls/d of oil.

In the fourth quarter of 2008, PetroCumarebo also performed two work-overs on the CU-171 and CU-173 wells in the Cumarebo Field in order to re-complete the wells in high prospective intervals. Both wells will be perforated with propellant (“stim gun” technology) and evaluated during the first quarter of 2009.

Baripetrol 2008 Capital Expenditures:

(\$000s)	Gross Initial Budget 2008	Gross Actual Incurred 2008
Seismic, Drilling and Work-overs		
- Rosario	1,910	-
- La Palma	33,500	8,560
- Socuavo	13,290	4,070
- Los Manueles	1,890	4,680
- Bonito	370	990
- West Tarra	590	3,040
- Total Drilling and Work-overs	51,550	21,340
Processing Facilities and Infrastructure		
- Rosario	1,640	-
- La Palma	2,350	560
- Socuavo	1,430	-
- Los Manueles	1,140	-
- Bonito	1,000	-
- West Tarra	990	-
- Total Processing Facilities and Infrastructure	8,550	560
Total Capital Budget	60,100	21,900

A drilling rig was scheduled to begin operations with Baripetrol in 2008. Due to delays in securing the rig, and in the start-up of the 3D seismic survey, Baripetrol did not spend its full capital budget in 2008. The 2008 budget was subsequently revised to \$22 million. Baripetrol’s actual capital spending was \$21.9 million, which included twenty-three work-overs in the Rosario, La Palma, Socuavo, Los Manueles, Bonito and West Tarra fields. Gross production in Baripetrol fell from a monthly average of 10,083 boe/d in January 2008 to 9,550 boe/d in December 2008.

PETROCUMAREBO AND BARIPETROL 2009 CAPITAL EXPENDITURES

The Mixed Companies, PetroCumarebo and Baripetrol, operate as independent entities with seconded technical staff from shareholders. The Mixed Companies fund their capital expenditures through their own cash flow, to the extent available, or through cash calls to shareholders, including PetroFalcon, if no other sources of financing are available. The Mixed Company shareholders intend that PetroCumarebo and Baripetrol be self-funding and rely on internally-generated cash flow to fund operations. To date, the Mixed Companies have not made a cash call to PetroFalcon for capital expenditures. This could change if oil and gas price realizations decrease and will be further addressed in future filings if necessary.

Based on prior experience and current oil prices, total 2009 capital expenditures are expected to be self-funded by the Mixed Companies' respective cash flow, and we would not expect the Mixed Companies to make cash calls to PetroFalcon to fund their capital programs.

If oil prices continue to decline and PetroCumarebo and Baripetrol are not able to fund their capital expenditures through their respective cash flow or other forms of financing, the Company's maximum expected commitment for 2009 capital expenditures is limited to the Company's share of the capital expenditure budgets outlined below.

PetroCumarebo 2009 Capital Expenditures:

(\$000s)	Gross Initial Budget 2009
Drilling and Work-overs	
- La Vela	18,110
- Cumarebo	6,610
- West Falcon	-
- Total Drilling and Work-overs	24,720
Processing Facilities and Infrastructure	
- La Vela	2,233
- Cumarebo	1,600
- West Falcon	537
Total Processing Facilities and Infrastructure	4,370
Total Capital Budget	29,090

Note: PetroFalcon owns 40% of PetroCumarebo. Budgeted capital expenditures are shown on a gross basis for PetroCumarebo. PetroFalcon does not expect cash calls from PetroCumarebo for any portion of the 2009 capital expenditures. However, if PetroCumarebo's cash flow is not sufficient to cover its capital expenditures, or if no other sources of financing are available, PetroFalcon could be responsible for 40% of such expenditures.

PetroCumarebo's 2009 capital budget is \$29.1 million, which includes drilling three development wells in La Vela, the San Patricio exploration well and performing one work-over in the Cumarebo Field. PetroCumarebo also plans to construct La Vela and Cumarebo central process de-bottlenecking facilities.

PetroCumarebo is currently drilling the LV-24 well in the La Vela Field.

Historically, PetroCumarebo has been able to fund its capital expenditures budget through its own cash flow or other forms of financing without cash calls to PetroFalcon.

Baripetrol 2009 Capital Expenditures:

(\$000s)	Gross Initial Budget 2009
Seismic, Drilling and Work-overs	
- Rosario	-
- La Palma	30,351
- Socuavo	-
- Los Manueles	-
- Bonito	-
- West Tarra	-
- Total Drilling and Work-overs	30,351
Processing Facilities and Infrastructure	
- Rosario	-
- La Palma	-
- Socuavo	3,200
- Los Manueles	-
- Bonito	-
- West Tarra	-
- Colina Station	800
- Total Processing Facilities and Infrastructure	4,000
Total Capital Budget	34,351

Note: PetroFalcon owns 5% of Baripetrol. Budgeted capital expenditures are shown on a gross basis for Baripetrol. PetroFalcon does not expect cash calls from Baripetrol for any portion of the 2009 capital expenditures. However, if Baripetrol's cash flow is not sufficient to cover its capital expenditures, or if no other sources of financing are available, PetroFalcon could be responsible for 5% of such expenditures.

Baripetrol's 2009 gross capital budget is \$34.4 million, which includes drilling four development wells in La Palma, the construction of a natural gas dehydration plant for the Socuavo Field's gas production and the upgrading of facilities in the La Colina flow station. At current oil prices, Baripetrol is expected to fund these capital expenditures from operating cash flow without cash calls to PetroFalcon.

Baripetrol is currently drilling the LPT-16 well in the La Palma Field.

Historically, Baripetrol has been able to fund its capital expenditures budget through its own cash flow or other forms of financing without cash calls to PetroFalcon.

PETROFALCON FINANCIAL STATEMENTS

The following table contains selected consolidated financial information for PetroFalcon over the last eight quarters:

(\$000s, except per share amounts)	2008					2007				
	Q1	Q2	Q3	Q4	Total	Q1	Q2	Q3	Q4	Total
Revenue	Nil	Nil	Nil	Nil	Nil	Nil	Nil	Nil	Nil	Nil
Net loss	(1,675)	(4,412)	(7,121)	(9,982)	(23,190)	(801)	(1,050)	(119)	(1,617)	(3,587)
Loss per share basic and diluted	(0.01)	(0.03)	(0.04)	(0.07)	(0.15)	(0.01)	(0.01)	(0.00)	(0.02)	(0.04)

Under the cost method of accounting, PetroFalcon does not recognize its share of revenues, expenses, assets or liabilities from PetroCumarebo or Baripetrol and instead only recognizes income from these investments to the extent that dividends are received from PetroCumarebo or Baripetrol. As a result, PetroFalcon has no revenues for the years ended December 31, 2008, and 2007. See “Critical Accounting Policies and Estimates”.

During the year ended December 31, 2008, PetroFalcon received \$2.9 million in dividends from Baripetrol for operations between January and December 2007. The dividends were credited against the historical cost of the investment instead of being recognized as income during the year ended December 31, 2008, because the dividends were related to pre-acquisition earnings.

PetroFalcon’s financial results and position

For the year ended December 31, 2008, the Company reported a net loss of \$23.2 million (loss per share of \$0.15) compared to a net loss of \$3.6 million (loss per share of \$0.04) for the year ended December 31, 2007.

The net results of the year ended December 31, 2008, were negatively impacted by the following non-cash items that had no impact on cash flow: (a) the Company’s adoption of the cost method of accounting whereby PetroFalcon does not recognize income from its oil and gas investments until such time as dividends are received; (b) the recognition of a \$7.9 million stock-based financing fee for the corporate guarantee provided by Lundin Petroleum AB to Anadarko Petroleum Corporation for the proposed acquisition of Anadarko Venezuela Company; and (c) the recognition of a \$6.8 million impairment loss in the carrying value of the investment in Baripetrol.

As of December 31, 2008, PetroFalcon had \$26.7 million in cash and short-term deposits, working capital of \$32.9 million and no debt. After terminating the agreement to acquire a 30% interest in the Cardon III Block and receiving \$5.8 million from Chevron for past expenses and accrued interest related to Cardon III, the Company has approximately \$31 million in cash, no debt and no expected cash calls from its oil and gas investments in Venezuela for 2009 capital expenditures.

GENERAL AND ADMINISTRATIVE (“G&A”) EXPENSE

(\$000s)	Three months ended December 31, 2008	Three months ended December 31, 2007
Salary and compensation benefits	743	435
Corporate and professional fees	478	401
Technical service agreement	140	112
Insurance	278	128
Travel expenses	162	79
Write-offs of receivables and other assets	883	122
Office, listing and filing expenses	169	263
Total Expenses	2,853	1,540

(\$000s)	Year ended December 31, 2008	Year ended December 31, 2007
Salary and compensation benefits	2,913	1,745
Corporate and professional fees	1,705	1,028
Technical service agreement	497	315
Insurance	577	381
Travel expenses	571	266
Write-offs of receivables and other assets	1,306	908
Office, listing and filing expenses	649	422
Total Expenses	8,218	5,065

Please see “Critical Accounting Policies and Estimates”.

PetroFalcon’s G&A expenses were \$2,853,490 during the three months ended December 31, 2008, as compared to \$1,539,572 during the three months ended December 31, 2007. PetroFalcon’s G&A expenses were \$8,217,813 during the year ended December 31, 2008, compared to \$5,065,369 during the year ended December 31, 2007.

The increase in G&A expenses during the three months and year ended December 31, 2008, is primarily due to an increase in accounting, tax and legal expenses and technical assistance fees due to compliance and acquisition-related work, along with an increase in salary expenses due to an increase in the number of employees.

PetroFalcon does not capitalize general and administrative expenses.

DEPRECIATION, DEPLETION AND AMORTIZATION (“DD&A”) EXPENSE

(\$000s)	Three months ended December 31, 2008	Three months ended December 31, 2007
Depreciation, depletion and amortization	26	27

(\$000s)	Year ended December 31, 2008	Year ended December 31, 2007
Depreciation, depletion and amortization	113	124

Please see “Critical Accounting Policies and Estimates”.

For the three months ended December 31, 2008, PetroFalcon’s DD&A expense was \$25,537, compared to \$26,683 for the three months ended December 31, 2007. PetroFalcon’s DD&A expense was \$112,964 during the year ended December 31, 2008, compared to \$123,938 during the year ended December 31, 2007.

STOCK-BASED COMPENSATION EXPENSE

(\$000s)	Three months ended December 31, 2008	Three months ended December 31, 2007
Stock-based compensation	14	277

(\$000s)	Year ended December 31, 2008	Year ended December 31, 2007
Stock-based compensation	797	2,047

During the three months ended December 31, 2008, the Company recorded \$13,819 in stock-based compensation expense compared to \$276,934 during the three months ended December 31, 2007. During the year ended December 31, 2008, the Company recorded \$797,365 in stock-based compensation expense compared to \$2,046,665 during the year ended December 31, 2007.

As of December 31, 2008, the number of outstanding stock options was 9,333,660, compared to 10,796,494 outstanding stock options as of December 31, 2007. The decrease in stock options outstanding, due mainly to the forfeiture of options held by departed employees and former directors, resulted in lower stock-based compensation expenses during the year ended December 31, 2008.

PetroFalcon’s stock option agreements have a change of control provision that causes all stock options to vest immediately when more than 20% of the Company is purchased. As a result, all of the Company’s outstanding stock options immediately vested at the closing of the Lundin transaction on February 1, 2008.

INTEREST INCOME AND EXPENSE

(\$000s)	Three months ended December 31, 2008	Three months ended December 31, 2007
Interest income (expense)	438	(591)

(\$000s)	Year ended December 31, 2008	Year ended December 31, 2007
Interest income (expense)	890	(1,135)

At December 31, 2008, PetroFalcon had \$26.7 million in cash and short-term deposits compared to \$4.8 million at December 31, 2007. At December 31, 2008, PetroFalcon had no short-term debt compared to \$2.5 million at December 31, 2007.

During the three months ended December 31, 2008, the Company recorded interest income in the amount of \$437,753 compared to \$590,859 of interest expense during the three months ended December 31, 2007. During the year ended December 31, 2008, PetroFalcon recorded interest income in the amount of \$890,377 compared to \$1,334,779 of interest expense during the year ended December 31, 2007.

The interest expense decreased primarily due to lower short-term debt during 2008 plus interest received from Anadarko Petroleum and Chevron in connection with the termination in 2008 of the respective purchase agreements.

The Company recorded stock-based financing expenses of \$7.9 million related to the Anadarko guarantee fee paid to Lundin Petroleum during the year ended December 31, 2008.

INCOME TAXES

(\$000s)	Three months ended December 31, 2008	Three months ended December 31, 2007
Consolidated current income tax expense	-	82
Future income tax	-	-

(\$000s)	Year ended December 31, 2008	Year ended December 31, 2007
Consolidated current income tax expense	-	82
Future income tax	-	-

During the three months ended December 31, 2008, PetroFalcon recorded no income tax expense since the Company had no taxable income for this period, compared to \$81,927 for income tax expense related to a former subsidiary of the Company recorded during the three months ended December 31, 2007. During the year ended December 31, 2008, PetroFalcon recorded no income

tax expense since the Company had no taxable income for this period, compared to \$81,927 for tax expense in the year ended December 31, 2007.

At December 31, 2008, the Company had consolidated carry forward losses of \$8,361,620 (equivalent to Bs 47,661,232 at the implied market rate) from Vinccler Venezuela. The Company did not recognize any future income tax asset related to these carry forward losses since it is not likely that the Company will be able to utilize these losses before they begin to expire in 2009.

During the three months ended December 31, 2008, and 2007, the Company realized no future income tax assets or liabilities. During the year ended December 31, 2008, and 2007, the Company realized no future income tax assets or liabilities.

LIQUIDITY AND CAPITAL RESOURCES

As of December 31, 2008, PetroFalcon had \$26.7 million in cash and short-term deposits, \$32.9 million of working capital and no debt. At December 31, 2007, PetroFalcon had \$4.8 million in cash, \$1.3 million of working capital, \$2.5 million of short-term debt and no long-term debt.

At December 31, 2008, PetroFalcon had \$7 million in current accounts receivable compared to \$1.6 million at December 31, 2007. At December 31, 2008, the Company had \$0.9 million in accounts payable compared to \$3.6 million at December 31, 2007.

As of March 17, 2009, PetroFalcon had 158,501,120 issued and outstanding common shares and 172,384,780 common shares on a fully diluted basis. As of December 31, 2008, PetroFalcon had 158,501,120 issued and outstanding common shares and 172,384,780 common shares on a fully diluted basis. As of December 31, 2007, PetroFalcon had 86,581,336 issued and outstanding common shares and 97,377,830 common shares on a fully diluted basis.

PetroFalcon's Liquidity Analysis

PetroFalcon has substantial cash on hand and expects to generate cash flow by receiving dividends from its oil and gas investments. As of March 17, 2009, PetroFalcon has approximately \$31 million in net cash. In 2009, PetroFalcon expects to receive a total of approximately \$8 million in dividends from Baripetrol and PetroCumarebo for 2008 operations. If these dividends are delayed, the Company's cash on hand more than covers its cash requirements for the foreseeable future. Based on prior experience and current oil prices, PetroFalcon does not expect cash calls from PetroCumarebo or Baripetrol for 2009 capital expenditures. PetroFalcon's only expected cash commitment for 2009 is therefore its corporate G&A expense, which is estimated at \$4 million for 2009. PetroFalcon has a local currency credit facility in order to cover local currency needs for G&A expenses. This credit facility is backed by US Dollar deposits and is unlikely to be terminated. If the Company makes acquisitions or if oil and gas price realizations are significantly reduced, financing requirements may change, and potential sources of financing would be further addressed in future filings.

PetroCumarebo and Baripetrol are operating as independent entities and fund their capital expenditures through cash flow to the extent available. The Mixed Companies' capital expenditures are expected to be "self-funded" because we do not expect the Mixed Companies to make cash calls to PetroFalcon to fund their capital programs. This could change as oil and gas

price realizations decrease and will be further addressed in future filings if necessary. The 2009 capital expenditure budgets for PetroCumarebo and Baripetrol are discussed under the heading, “PetroCumarebo and Baripetrol 2009 Capital Expenditures”.

RISK FACTORS

The Company’s activities expose it to a variety of financial risks: credit risk, liquidity risk, market risk (including interest rate, foreign currency and commodity price risk) and other risks. Risk management is carried out by the Company’s management team with guidance from the Audit Committee under policies approved by the Board of Directors. The Board of Directors also provides regular guidance for overall risk management.

Credit risk

Credit risk is the risk of loss associated with a counterparty’s inability to fulfill its payment obligations. The Company’s credit risk is primarily attributable to value-added tax receivables and tax credits of the wholly-owned subsidiary with the Venezuelan tax authorities and third parties. The Company has no concentration of credit risk. Value added tax receivables are collectable from the Venezuelan government and are in good standing as of December 31, 2008. Management believes that the credit risk with respect to financial instruments attributable to value added tax receivables is moderate.

In addition, the majority of the Company’s cash and cash equivalents are on deposit with one highly-rated bank in Canada. A lesser amount is held in a bank in Curacao.

Liquidity risk

At December 31, 2008, the Company had sufficient funds to settle current liabilities. All of the Company’s accounts payable and accrued liabilities have contractual maturities of less than 30 days, except for severance employee benefits, and are subject to normal trade terms. The Company’s subsidiary’s line of credit is based on contractual terms between related companies and with a Venezuelan financial institution. This bank credit facility is backed by US dollar deposits.

Market risk

Market risk is the risk of loss that may arise from changes in market factors such as interest rates, foreign exchange rates and oil prices.

(i) Interest rate risk

PetroFalcon has significant cash balances and short-term investments, with the latter having variable annual interest rates from 3.08% to 0.80%. The Company’s current policy is to invest excess cash in investment grade short-term deposit certificates issued by banks. The Company periodically monitors the investments it makes and is satisfied with the credit ratings of its banks.

Vinccler Venezuela’s line of credit is based on contractual terms with its parent company and on contractual terms with a Venezuelan financial institution, bearing annual interest of 3% and 28%,

respectively. The Company periodically monitors and evaluates the interest between related parties and interest rates for loans in the Venezuelan market to adjust its leverage strategy as necessary.

(ii) Foreign currency risk

PetroFalcon's functional currency is the US dollar. Any annual dividends from its oil and gas investments are in US dollars, and major purchases are transacted in US dollars. The Company maintains US dollar bank accounts in Canada and Curacao. The Company funds some of its subsidiary's operating and administrative expenses in Venezuelan Bolivars from its US dollar bank accounts.

During 2007, the Company's management determined that as a consequence of the rapid decline in the valuation of the Venezuelan Bolivar as reflected in the implied market for foreign currencies in Venezuela that the method of translation from Bolivars to US dollars using the official rate was no longer appropriate. The Company recognizes the foreign currency transactions of its Venezuelan subsidiary at the implied market rate in Venezuela, which had a spread of 165% over the official rate as of December 31, 2008. The Company has exposure to the volatility of the implied market rate in Venezuela that may result in significant foreign exchange gains or losses from its Venezuelan subsidiary.

(iii) Commodity price risk

Oil price risk is the potential adverse impact on the Company's dividends from its oil and gas investments due to oil price movements and volatility. The Company closely monitors oil prices to determine the appropriate course of action to be taken by the Company, to the extent possible, through its participation on the board of directors of PetroCumarebo and in the private party consortium in Baripetrol.

Other risks

International operations

PetroFalcon participates in oil and gas projects located in Venezuela. Oil and gas exploration, development and production activities, including joint ventures in emerging markets, are subject to significant political and economic uncertainties that may adversely affect the Company's performance. Uncertainties include, but are not limited to, expropriation, nationalization, renegotiation or nullification of existing or future concessions and contracts, a change in crude oil or natural gas pricing policies, a change in taxation policies, and the imposition of currency controls. These uncertainties, all of which are beyond the Company's control, could have a material adverse effect on PetroFalcon's business prospects and results of operations. In addition, if legal disputes arise related to oil and gas concessions acquired by the Company, PetroFalcon could be subject to the jurisdiction of courts other than those of Canada. The Company's recourse may be very limited in the event of a breach by a government or government authority of an agreement governing a concession in which PetroFalcon acquires an interest. The Company may require licenses or permits from various governmental authorities to carry out future exploration, development and production activities. There can be no assurance that PetroFalcon will be able to obtain all necessary licenses and permits when required.

Dividends

PetroFalcon does not have traditional working interests in oil and gas properties. PetroFalcon's only source of near-term revenues is potential dividends from its 40% interest in PetroCumarebo and its 5% interest in Baripetrol. Under Venezuelan law, dividends can only be declared to the extent a company has net and available profits as stated in its approved financial statements. Therefore, if there are sufficient net and available profits, subject to prior approval of shareholders, PetroFalcon, through Vinccler Venezuela, may receive annual dividends in US dollars, or quarterly loans against those projected dividends. If the Mixed Companies' boards of directors do not propose dividends, the Mixed Companies' shareholders do not approve dividends, or the Mixed Companies do not have net and available profits to declare dividends, PetroFalcon cannot expect to receive payment from the Mixed Companies. Dividends from the Mixed Companies must be proposed by four out of the five board members (80%), and each of Vinccler Venezuela and Baripetrol's private party consortium (which includes Tecpetrol, Perenco and Vinccler Venezuela) have two out of five board seats (40%) in the respective Mixed Companies. Dividends proposed by the board of the Mixed Companies must be approved by a qualified majority (75%) of its respective shareholders, and Vinccler Venezuela and Baripetrol's private party consortium each only account for 40% of the respective shareholders. Furthermore, given the current economic environment and its potential impact on the oil and gas business, PDVSA and the Venezuelan government, the timing and amount of dividends from the Mixed Companies is uncertain.

SPECIAL OIL AND GAS DISCLOSURES

Benchmark Prices

The Company used the following oil price projections for the next five years, beginning in 2009, for the impairment tests of PetroFalcon's oil and gas investments carried at cost in Venezuela. These pricing assumptions are based on information provided by PetroFalcon's petroleum consultants.

(\$/bbl)	2009	2010	2011	2012	2013
West Texas Intermediate (WTI)	57.00	65.50	71.05	65.00	65.00

Development of Proved and Probable Undeveloped Reserves

Proved and probable undeveloped reserves have been estimated in accordance with procedures and standards contained in the Canadian oil and gas evaluation handbook. The Company's oil and gas interests have areas where multiple zones have been assigned reserves in a well. Once the currently producing zones are depleted, capital will be spent re-completing the wells in another zone. Some of these expenditures are planned to occur in 2010 and beyond, the timing to be dictated by the predicted reserve life for the currently producing zones.

Funding for Estimated Future Development Cost

Future development costs attributable to proved reserves include drilling and completion, pipeline and facilities and abandonment costs. PetroCumarebo has estimated a \$29 million capital program to fund its exploration and development activities for 2009. Baripetrol has estimated a \$34 million capital program to fund its exploration and development activities for 2009. PetroCumarebo and Baripetrol have three sources of funding available to finance their capital expenditures programs: internally generated cash flow from operations, debt financing when appropriate and cash calls to shareholders, including PetroFalcon.

PetroFalcon has several sources of funding available to finance its portion of PetroCumarebo's and Baripetrol's capital expenditures program, if required: cash on hand, dividends from PetroCumarebo and Baripetrol and debt financing and new equity issues, if available on favorable terms.

Development of Uneconomic Properties

The process of estimating and producing reserves is complex. It requires significant judgments and decisions based on available geological, geophysical, engineering and economic data. These estimates may change substantially as additional data from ongoing development activities and production performance becomes available and as economic conditions impacting oil and gas prices and costs change. In the event that oil and gas properties become uneconomic, according to the Mixed Company and PDVSA accounting policies, those development cost will be impaired and recognized as such in the financial statements. However, based on current economic and technical information, the Company's management does not expect that future development costs could make a property uneconomic.

RELATED PARTY TRANSACTIONS

Pacific Oil and Gas, LLC ("Pacific Oil and Gas") and Venezolana de Inversiones y Construcciones Clerico, C.A. ("Vinccler Construction") are controlled by officers of PetroFalcon. These related party transactions are in the normal course of operations and are measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties.

Pacific Oil and Gas, LLC

Pacific Oil and Gas is controlled by PetroFalcon's Vice Chairman, Clarence Cottman, and PetroFalcon's President and CEO, William Gumma. For the three months ended December 31, 2008, and 2007, the Company paid Pacific Oil and Gas for professional services in the amount of \$178,000 and \$135,000, respectively. The Company paid Pacific Oil and Gas for the year ended December 31, 2008, and 2007, \$613,000 and \$540,000, respectively. These payments include the salaries of Mr. Gumma and PetroFalcon's Chief Financial Officer, Garrett Soden, as well as administrative services from Pacific Oil and Gas.

Vinccler Construction

PetroFalcon occasionally receives construction services from Vinccler Construction, an independent operating construction company controlled by the Company's Chairman, Juan Francisco Clerico. During the year ended December 31, 2008, and 2007, PetroFalcon did not receive services from Vinccler Construction. On August 25, 2006, Vinccler Construction paid on behalf of Vinccler Venezuela the amount of \$350,000 to purchase the data package for the Delta Caribe offshore natural gas bid process in Venezuela. On March 27, 2008, Vinccler Venezuela repaid this amount plus interest.

Lundin Services BV

PetroFalcon also receives technical services from Lundin Services BV, a wholly-owned subsidiary of Lundin Petroleum. Lundin Petroleum indirectly owns 45% of PetroFalcon, and Lundin Petroleum's CEO, Ashley Heppenstall, is a board member of PetroFalcon. For the three months ended December 31, 2008, and 2007, the Company paid Lundin Services BV for professional services in the amount of \$80,170 and nil, respectively. The Company paid Lundin Services BV for the year ended December 31, 2008, and 2007, \$80,170 and nil, respectively. These payments for professional services include oil and gas geology, reserve and legal advice for PetroFalcon's business development activities.

Lundin Petroleum

Lundin Petroleum provided a guarantee to Anadarko Petroleum for the full purchase price of the proposed acquisition of Anadarko Venezuela. In consideration for the guarantee, PetroFalcon agreed to issue 17.1 million common shares of the Company to Lundin Petroleum or one of its subsidiaries, subject to regulatory approval. On April 11, 2008, PetroFalcon issued 7.1 million of these shares to Lundin Petroleum, with a fair value of \$1.11 (CDN\$1.12) per share for a total amount of \$7,878,842. The remaining 10 million shares were due at closing and, according to the agreement, were not issued. The initial shares were expensed by the Company as a stock-based financing fee.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

The Company made assumptions in applying the following critical accounting estimates that were uncertain at the time the accounting estimate was made and may have a significant effect on the financial statements of the Company.

Investments in Oil and Gas Companies

Investments in oil and gas companies are recognized in the financial statements using the equity method or the cost method of accounting. If the Company holds less than 20% of the voting interest in the investee, it is presumed that the Company does not have the ability to exercise significant influence and the cost method is used, unless such influence is clearly demonstrated. If the Company holds 20% or more of the voting interest in the investee, the equity method would normally be used although it does not in itself confirm the ability to exercise significant influence. Investments where the Company does not have significant influence are classified as financial

assets and, in the absence of a quoted price in an active market, carried at cost. Under the cost method, PetroFalcon does not recognize its share of revenues, expenses, assets or liabilities from investees and instead only recognizes income from the investment to the extent that dividends are received.

Interests in jointly controlled entities are recognized in the Company's financial statements using the proportionate consolidation method. As of December 31, 2008, and 2007, the Company had no interests in jointly controlled entities.

PetroCumarebo Accounting

In 2007, PetroFalcon re-evaluated its relationship with PetroCumarebo and concluded that, for accounting purposes, PetroFalcon's investment in PetroCumarebo does not meet the criteria for proportionate consolidation or equity method accounting. Accordingly, PetroFalcon has accounted for PetroCumarebo using the cost method of accounting for the years ended December 31, 2008, and 2007. Under the cost method, PetroFalcon does not recognize its 40% share of revenues, expenses, assets or liabilities from PetroCumarebo and instead only recognizes income from the investment to the extent that dividends are received from PetroCumarebo. As a result, PetroFalcon has no revenues for the years ended December 31, 2008, and 2007.

Active Operations

Despite the adoption of the cost method of accounting, PetroFalcon continues to be an oil and gas company carrying on active operations. PetroFalcon is engaged directly or indirectly in "oil and gas activities" as defined in National Instrument 51-101, such as the search for crude oil or natural gas and the acquisition of property rights for the purpose of further exploring for or removing oil or gas from reservoirs on those properties.

Specifically, the Company continues to be an oil and gas company carrying on active operations because PetroFalcon employs technical personnel participating in the search for oil and gas in PetroCumarebo's operating properties. In addition, PetroFalcon has technical and financial staff actively looking for new oil and gas properties for PetroFalcon to operate.

Management of PetroFalcon has determined that, because PetroFalcon continues to be an oil and gas company carrying on active operations, it is important to provide comparative and relevant oil and gas information in its public disclosures, where possible. Such disclosure will provide relevant oil and gas information in respect of PetroCumarebo and Baripetrol on a gross basis to the extent possible. This information will be based upon unaudited information provided by PetroCumarebo and Baripetrol to management and upon National Instrument 51-101 compliant independent technical reports obtained by PetroFalcon's management.

Baripetrol Accounting

PetroFalcon's investment in Baripetrol is recognized under the cost method of accounting. During the year ended December 31, 2008, PetroFalcon received \$2.9 million in dividends from Baripetrol for operations between January and December 2007. The dividends have been credited against the historical cost of the investment instead of being recognized as income during the year

ended December 31, 2008, because the dividends were related to earnings before the closing of the transaction.

Financial Assets Carried at Cost – Impairment Test

The current economic and market conditions represent circumstances that are likely to affect the carrying amount of assets, including financial assets carried at cost. There has been a significant decrease in the Company's share price in 2008, as well as a significant adverse change in the business climate of the oil and gas industry.

The Company evaluates the carrying amount of its investment when there is objective evidence that a financial asset might be impaired. In measuring and recognizing impairment losses, the Company compares the investment carrying amount against its share participation in the sum of the undiscounted cash flows expected to result from the production of proved reserves associated with its oil and gas interests. If the carrying amount exceeds the undiscounted cash flows, then the Company compares the carrying amount against its share participation in the discounted cash flows of proved and probable reserves (fair value) associated with its oil and gas interests. Impairment losses are measured as the amount by which the carrying value of the investment exceeds the Company's share participation in the fair value. Estimated undiscounted future cash flows after taxes and contributions used to measure the recoverability of PetroFalcon's investments were prepared based on current and future assumptions about the use of oil and gas assets by PetroCumarebo and Baripetol considering all available evidence, such as current and expected oil and gas production according to the business plans and independent reserves certification, current and expected oil and gas prices as indicated by the Company's petroleum advisors, capital expenditures and operating expenses to maintain and produce proved reserves.

Management conducted an impairment test of its oil and gas investments for the year ended December 31, 2008, and concluded that the carrying amount of the investment in Baripetrol exceeds its fair value. The fair value calculation considers the Company's 5% share participation in the discounted future after-tax cash flow projections of the proved and probable reserves associated with Baripetrol's assets covering the period until the end of Baripetrol's contract. As a result, management recorded an impairment loss of \$6.8 million against the carrying value of the investment, included in the statement of operations

Stock-Based Compensation

The Company uses the fair value method of accounting for its stock-based compensation expense associated with its stock option plan. Compensation expense is based on the fair value of stock options at the grant date using the Black-Scholes option pricing model. The Black-Scholes model requires estimates for the expected volatility of the Company's stock, a risk-free interest rate, expected dividends on the stock and the expected life of the option. Changes in these estimates may result in the actual compensation expense being materially different than the compensation expense recognized. However, this expense is not subsequently adjusted for changes in these factors.

CONCLUSION REGARDING EFFECTIVENESS AND DESIGN OF DISCLOSURE CONTROLS AND PROCEDURES AND INTERNAL CONTROL OVER FINANCIAL REPORTING

Year Ended December 31, 2008

The Chief Executive Officer and Chief Financial Officer of PetroFalcon have carried out an evaluation of the effectiveness of PetroFalcon's disclosure controls and procedures and assessed the design of its internal control over financial reporting for the period ended December 31, 2008, pursuant to the requirements of National Instrument 52-109. Based on the evaluation conducted, the Chief Executive Officer and Chief Financial Officer have concluded that the design and operation of PetroFalcon's disclosure controls and procedures and internal control over financial reporting were effective as at the end of the period ended December 31, 2008.

Year Ended December 31, 2007

Management concluded that, as of December 31, 2007, weaknesses existed in the design of internal control over financial reporting. These weaknesses were considered as weaknesses in the Company's disclosure controls and procedures. During 2008, management took appropriate remediation steps to address these weaknesses, such as: (a) hiring qualified staff to correct the weaknesses in Canadian GAAP expertise; and (b) implementing additional and risk-based controls in the use of Excel spreadsheets.

Management has observed that the remediation actions taken during 2008 have improved significantly the Company's financial reporting process.

It is the policy of PetroFalcon's management and Board of Directors to transparently and completely disclose its reporting process. Therefore, the existence of internal control over financial reporting and disclosure and procedures control weaknesses in a business with a small number of employees and limited resources, such as PetroFalcon, need not necessarily be interpreted as evidence of a lack of integrity, of unsound business practices or of unacceptable risks to shareholders and other related parties.

During the three months ended December 31, 2008, there were no changes to internal control over financial reporting that have materially affected, or are reasonably expected to materially affect, the Company's internal control over financial reporting, except for the remediation of the material weaknesses noted above.

INTERNATIONAL FINANCIAL REPORTING STANDARDS ("IFRS")

In January 2006, the CICA's Accounting Standards Board ("AcSB") formally adopted the strategy of replacing Canadian GAAP with IFRS for Canadian enterprises with public accountability. The current conversion timetable calls for financial reporting under IFRS for accounting periods commencing on or after January 1, 2011. On February 13, 2008, the AcSB confirmed that the use of IFRS will be required in 2011 for publicly accountable profit-oriented enterprises. IFRS will be required for PetroFalcon's interim and annual financial statements for the fiscal year beginning January 1, 2011. The Company is currently assessing the impact of IFRS on its consolidated financial statements.

ADDITIONAL INFORMATION

Additional information regarding the Company, including its annual information form, reserves information and annual report, may be found on the SEDAR website at www.sedar.com or by visiting the Company's website at www.petrofalcon.com.