



Management's Discussion and Analysis ("MD&A")

March 31, 2009

Dated May 14, 2009

**Epsilon Energy Ltd.
150 Jardin Drive, Suite 9
Concord, ON, Canada L4K 3P9**

(866) 384-8774

www.epsilonenergy ltd.com

EPSILON ENERGY LTD.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Overview

This Management's Discussion and Analysis ("MD&A") is intended to assist in the understanding of trends and significant changes in or results of operations and the financial condition for the periods presented. The MD&A has been prepared by management as at May 14, 2009 in accordance with GAAP and should be read in conjunction with the unaudited interim consolidated financial statements (three months ended and as at March 31, 2009 and the three months ended and as at March 31, 2008), the audited consolidated financial statements as at December 31, 2008 and 2007, respectively, together with accompanying notes, the Statement of Reserves Data and Other Oil and Gas Information on December 31, 2008 and the Annual Information Form dated April 1, 2009. These documents and additional information about Epsilon Energy Ltd. are available on SEDAR at www.sedar.com. Unless stated otherwise, all references to monetary values are in United States dollars.

Cautionary Statement Regarding Forward Looking Information and Statements

Certain statements contained in this report constitute forward-looking statements. The use of any of the words "anticipate", "continue", "estimate", "expect", "may", "will", "project", "should", "believe" and similar expressions and statements relating to matters that are not historical facts constitute "forward looking information" within the meaning of applicable Canadian securities legislation. These statements involve known and unknown risks, uncertainties and other factors that may cause actual results or events to differ materially from those anticipated. Such forward-looking statements are based on reasonable assumptions but no assurance can be given that these expectations will prove to be correct and the forward-looking statements included in this report should not be unduly relied upon. These statements are made only as of the date of this report.

In particular, this report contains forward-looking statements including, but not limited to, the following:

- oil and natural gas production rates;
- commodity prices for crude oil or natural gas;
- supply and demand for oil and natural gas;
- the estimated quantity of oil and natural gas reserves, including reserve life;
- capital expenditure programs;
- future exploration, development and production costs;
- timing of drilling plans;
- planned construction and expansion of facilities;
- plans for and results of exploration and development activities;
- expectations regarding the Corporation's ability to raise capital and to continually add to oil and natural gas reserves through acquisitions, exploration and development; and
- treatment under governmental regulatory regimes and tax laws.

The Corporation's actual results could differ materially from those anticipated in these forward-looking statements as a result of the risk factors set forth below and elsewhere in this report:

- general economic, political, market and business conditions;
- risks inherent in oil and natural gas operations;
- uncertainties associated with estimating oil and natural gas reserves;
- competition for capital, acquisitions of reserves, undeveloped lands, drilling equipment and skilled personnel;

- geological, technical, drilling and processing problems;
- incorrect assessments of the value of acquisitions;
- the availability of capital on acceptable terms;
- volatility in market prices for oil and natural gas;
- reliance on key operational and management personnel;
- actions by governmental authorities, including regulatory, environmental and taxation policies;
- fluctuations in foreign exchange, interest rates and stock market volatility; and
- other risk factors discussed under “*Risk Factors*” within the Corporation’s Annual Information Form dated April 1, 2009.

These factors are not all inclusive. Except as required under applicable securities laws, the Corporation undertakes no obligation to update or revise any forward-looking statements.

Corporate Overview

The Corporation is engaged in the acquisition, exploration, development and production of oil and natural gas reserves in North America, the Middle East and Africa. The Corporation’s strategy involves exploiting a well-balanced inventory of oil and natural gas projects with the goal of converting its leasehold interests into proven oil and natural gas reserves, followed by production that optimizes cash flow and return on investment. Also refer to “*Risk Factors*” in the Corporation’s Annual Information Form dated April 1, 2009.

Overall Performance

During the first quarter of 2009, the Corporation continued to explore, develop and expand its oil and gas interests. For the first quarter of 2009, the Corporation generated a net loss of \$835,000, as compared to a \$283,000 net loss for the same period of 2008. The primary variance between the first quarter of 2009 and 2008 was other income and expense, which was a negative \$73,000 for the three months ended March 31, 2009, as compared to a positive \$427,000 for the same period of 2008, due primarily to lower interest income earned on overall lower cash, cash equivalents and restricted cash balances. At March 31, 2009, the Corporation continued to have adequate funds for its ongoing operations with working capital (inclusive of restricted cash) of \$3,960,000, as compared to \$15,862,000 of working capital at December 31, 2008. The \$11,902,000 decrease in working capital at March 31, 2009, as compared to December 31, 2008 was partially comprised of the following cash flow related items: (1) \$6,273,000 of cash used in operations; (2) \$8,300,000 spent on oil and gas properties; and (3) \$5,805,000 additional draws on the Corporation’s loan facilities that were offset by a reduction of \$8,683,000 reduction in restricted cash. Key developments during the first quarter of 2009 and through the date of this report by country include:

United States – The Corporation expects to commence natural gas production on its Highway 706 project covering the Marcellus shale in northeastern Pennsylvania very shortly. Phase 1 of the pipeline is now operational. Initially, the Poulson #1H will be placed on-line for natural gas production, to be followed by the Poulson #2H. Both wells lie between the compressor site to the north and the tap into the Tennessee Gas Pipeline to the south. Epsilon is currently extending its gathering system to the north of the compressor site in order to bring on three wells that have previously yielded a combined natural gas production rate of 8.5 Mmcf per day (Larue #1A, Larue #1H and Larue #2H). This section of the gathering system is expected to be completed in approximately 60 – 90 days. The Corporation currently has compression facilities on location and expects to have the ability increase its compression capacity as warranted in order to handle increased production as more wells come online. At March 31, 2009, the Corporation’s average natural gas production was approximately 2.2 Mmcf/d, consisting solely of non-operated natural gas production from its interests in West Virginia, New York and Ohio.

Republic of Yemen (“**Yemen**”) – During the first quarter of 2009, the Corporation drilled the Mukulla #1, which was subsequently determined to be uneconomical. The Corporation is currently evaluating the data gathered from operations to date to determine future exploration

plans in Yemen, if any. As at March 31, 2009, Oil and Gas Mine Company, a non-operated joint interest owner in Block 41, owed the Corporation \$6,503,000, which covered their pro-rata share of costs pertaining to Block 41 in Yemen as of that date. Of that amount, \$5,591,000 was in default. On April 20, 2009, Oil and Gas Mine Company paid the Corporation \$2,000,000 and verbally agreed to pay the remaining amount in default within thirty days.

Federal Democratic Republic of Ethiopia (“Ethiopia”) – On May 14, 2009, the Corporation announced that it had signed a Production Sharing Agreement (“PSA”) with the Ministry of Mines and Energy (the “Ministry”) in Democratic Republic of Ethiopia. The PSA covers an area of 79,345 square kilometers in northwest Ethiopia. Terms of the PSA include an initial three-year exploration period that includes a minimum financial commitment of \$3,000,000 to drill one exploratory well and to acquire a minimum of 200 kilometers of 2D seismic. In the event the Company makes a commercial discovery, the initial percentage split of profit oil and/or gas will be 80% for Epsilon and 20% for the Ministry.

Sultanate of Oman (“Oman”) – In January 2009, the Corporation acquired a 100% working interest in Block 55 in Oman. The initial exploration period includes a commitment to spend \$25,500,000 over a three year period. The Corporation does not anticipate incurring any significant capital expenditures in Oman during 2009 and is currently evaluating whether to bring in an industry partner, obtain third party financing, or a combination of both to fully fund its commitment.

Going Concern

The unaudited consolidated financial statements of the Corporation for the three months ended and as at March 31, 2009 and the three months ended March 31, 2008 have been prepared on a going concern basis, which presumes that the Corporation will be able to realize its assets and discharge its liabilities in the normal course of business for the foreseeable future. The Corporation is relying upon its ability to continue to achieve profitable oil and natural gas production from its projects to continue as a going concern. Given the lead time associated with many of its exploration and development activities, the Corporation’s ability to continue as a going concern is dependent on many factors. Those factors include the results of future exploration, development and production activities, the timing, scope and pace of such activities, and events outside of the Corporation’s direct control, such as the global credit market crisis and oil and gas commodity price volatility.

As at March 31, 2009 the Corporation had a negative working capital balance of \$21.1 million, incurred a net loss of \$0.8 million and had negative cash flow from operations of \$6.3 million. The Corporation currently anticipates incurring substantial expenditures to further its capital development program. Factors that will affect the Corporation’s ability to continue as a going concern include:

- Continued commercial production from its existing producing properties;
- Commencement of commercial production and profitable operations from exploration and development properties;
- Managing future international exploratory activities in a cost effective manner;
- Effectively managing the timing, pace, scope and the allocation of funds for capital expenditures within currently available capital resources;
- The continued support and cooperation of its lender; and
- Raising additional capital, as warranted, to accelerate or supplement the Corporation’s capital expenditures by bringing in industry partners, additional debt financing, equity financing, sale of full or partial property interests, or a combination thereof.

The unaudited consolidated financial statements of the Corporation for the three months ended and as at March 31, 2009 and the three months ended March 31, 2008 do not include any adjustments that might result if the Corporation is unable to continue as a going concern. Such adjustments could be material.

Reportable Geographical Operating Segments

As of March 31, 2008, the Corporation held interests in the following countries: United States, Canada, Yemen, Ethiopia, and Oman. From its inception through the first three months of 2009, the Corporation's oil and natural gas revenues were derived solely from the Appalachian basin in the United States.

	Three Months Ended March 31,	
	2009	2008
Reportable Segments:		
United States:		
Revenues	\$ 1,708,000	\$ 1,537,000
Operating costs.....	\$ 467,000	\$ 281,000
Capital expenditures.....	\$ 7,059,000	\$ 7,708,000
Canada:		
Revenues	\$ -	\$ -
Operating costs.....	\$ -	\$ -
Capital expenditures.....	\$ 10,000	\$ -
Yemen:		
Revenues	\$ -	\$ -
Operating costs.....	\$ -	\$ -
Capital expenditures.....	\$ 1,873,000	\$ 634,000
Ethiopia:		
Revenues	\$ -	\$ -
Operating costs.....	\$ -	\$ -
Capital expenditures ⁽¹⁾	\$ (414,000)	\$ -
Oman:		
Revenues	\$ -	\$ -
Operating costs.....	\$ -	\$ -
Capital expenditures.....	\$ 2,631,000	\$ -

Notes:

- (1) The negative amount for the three months ended March 31, 2009 includes an accrual adjustment for prior period costs.

Selected Financial Information

Selected financial information follows (amounts rounded to thousands, except per share amounts):

	Three Months Ended March 31,	
	2009	2008
<i>Statement of operations:</i>		
Revenues	\$ 1,708,000	\$ 1,537,000
Cost of operations	2,470,000	2,247,000
Operating income or (loss).....	(762,000)	(710,000)
Other income.....	(73,000)	427,000
Net income or (loss).....	<u>\$ (835,000)</u>	<u>\$ (283,000)</u>
<i>Per Common Share data:</i>		
Basic and net income or (loss) per share.....	\$ (0.02)	\$ (0.01)
Basic weighted number of shares outstanding	50,315,323	45,698,323
Dividends per share.....	\$ -	\$ -
<i>Cash Flows:</i>		
Net cash used in operating activities	\$ (6,273,000)	\$ (498,000)
Net cash (used in) or provided by investing activities	\$ 385,000	\$ (6,793,000)
Net cash provided by financing activities	\$ 5,802,000	\$ -
Effect of currency rates on cash and cash equivalents	\$ (957,000)	\$ (1,601,000)
	As at	As at December
	March 31,	31,
	2009	2008
<i>Balance Sheet:</i>		
Total assets.....	\$ 135,136,000	\$ 134,070,000
Current liabilities	\$ 36,312,000	\$ 33,836,000
Long-term debt	\$ 16,000	\$ 19,000
Other liabilities	\$ 2,938,000	\$ 2,920,000
Total liabilities	\$ 39,266,000	\$ 36,775,000
Shareholders' equity	\$ 95,870,000	\$ 97,295,000

Summary of Quarterly Results

Summary quarterly information for the years ended December 31, 2008 and 2007, respectively, are presented in the table below. Please refer to “*Selected Financial Information*” for 2009 amounts. All amounts rounded to thousands of dollars, except for per share amounts. See “*Selected Financial Information*” for 2009 amounts.

	Quarter Ended				Year Ended
	March 31	June 30	September 30	December 31	December 31
2008:					
Total revenues	\$ 1,537,000	\$ 2,374,000	\$ 2,476,000	\$ 1,913,000	\$ 8,300,000
Net income or (loss)	\$ (284,000)	\$ 4,158,000	\$ (148,000)	\$ (37,414,000)	\$ (33,688,000)
Net income per share	\$ (0.01)	\$ 0.09	\$ 0.00	\$ (0.79)	\$ (0.71)
Total assets	\$ 116,969,000	\$ 124,061,000	\$ 154,013,000	\$ 134,070,000	\$ 134,070,000
Long-term debt	\$ -	\$ 30,000	\$ 24,000	\$ 19,000	\$ 19,000
Shareholders’ equity	\$ 106,064,000	\$ 111,434,000	\$ 142,079,000	\$ 97,295,000	\$ 97,295,000
Dividends paid	\$ -	\$ -	\$ -	\$ -	\$ -
2007:					
Total revenues	\$ 883,000	\$ 1,085,000	\$ 678,000	\$ 1,024,000	\$ 3,670,000
Net income or (loss)	\$ 285,000	\$ (98,000)	\$ (337,000)	\$ (2,074,000)	\$ (2,224,000)
Net income per share	\$ 0.01	\$ 0.00	\$ (0.01)	\$ (0.08)	\$ (0.08)
Total assets	\$ 21,812,000	\$ 35,522,000	\$ 65,937,000	\$ 117,323,000	\$ 117,323,000
Long-term debt	\$ -	\$ -	\$ -	\$ -	\$ -
Shareholders’ equity	\$ 20,058,000	\$ 33,512,000	\$ 34,614,000	\$ 107,640,000	\$ 107,640,000
Dividends paid	\$ -	\$ -	\$ -	\$ -	\$ -

Operational Outlook and Property Overview

A summary of Epsilon’s projects by country are as follows:

United States

Appalachian basin - Overview

In the United States, the Corporation is focused on the Appalachian basin, where it is developing its Marcellus shale acreage in Pennsylvania and New York and has built a solid production base comprised of unconventional natural gas production in West Virginia from Devonian-aged shale gas zones and conventional natural gas production in New York from the Trenton-Black River formation. During 2008, the Corporation began to focus the majority of its Appalachian basin exploration and development efforts on its Marcellus shale acreage holdings and expects to continue to do so during 2009 and beyond.

The Marcellus Shale stretches from southern New York through western Pennsylvania into eastern Ohio and across West Virginia, where the Corporation has approximately 124,000 gross (54,000 net) leasehold acres, including approximately 47,000 gross (31,000 net) leasehold acres in highly prospective areas within Pennsylvania and New York. Industry publications, such as the January 2009 issue of the *Oil & Gas Investor*, continue to be very bullish on the Marcellus Shale, including recently published estimates of an average of 3.30 Bcf of gross natural gas reserves per well, average finding and development costs of \$1.42/Mcfe and average internal rates of return of 86% based on average capital costs of \$2,500 per mineral acre and average drilling costs of \$3.75 million per well. Based on the Corporation’s operations to date, the Corporation expects to achieve results within the range of the aforementioned metrics.

Pennsylvania

As of March 31, 2009 the Corporation has acquired approximately 15,403 gross (15,184 net) leasehold acres in northeastern Pennsylvania where the Corporation is operator, holds a 100% working interest and is focused on the Marcellus shale, an unconventional Devonian-aged shale gas zone. The Corporation's Marcellus shale acreage appears to be in an over-pressured environment with upper (Cherry Valley) and lower (Onondaga) limestone frac barriers present. As such, hydraulic frac stimulations are generally very effective in this geological environment.

The Corporation expects to commence natural gas production on its Highway 706 project covering the Marcellus shale in northeastern Pennsylvania very shortly. Phase 1 of the pipeline is now operational. Initially, the Poulson #1H will be placed on-line for natural gas production, to be followed by the Poulson #2H. Both wells lie between the compressor site to the north and the tap into the Tennessee Gas Pipeline to the south. Epsilon is currently extending its gathering system to the north of the compressor site in order to bring on three wells that have previously yielded a combined natural gas production rate of 8.5 Mmcf per day (Larue #1A, Larue #1H and Larue #2H). This section of the gathering system is expected to be completed in approximately 60 – 90 days. The Corporation currently has compression facilities on location and expects to have the ability increase its compression capacity as warranted in order to handle increased production as more wells come online.

Through the date of this MD&A, the Corporation had drilled eight wells on its Highway 706 project. The current status of those wells is as follows:

- Poulson #2H – drilled horizontally, completed and waiting to be hooked up;
- Poulson #1H – drilled horizontally, completed and waiting to be hooked up;
- Larue #1A - drilled vertically, completed and waiting to be hooked up;
- Larue #1H - drilled horizontally, completed and waiting to be hooked up;
- Larue #2H - drilled horizontally, completed and waiting to be hooked up;
- Larue #1B - drilled vertically, waiting on completion;
- Pierson #1 - drilled vertically, waiting on completion;
- Hardic #1H - drilled horizontally, waiting on completion;

For 2009, the Corporation has a capital expenditure budget of approximately \$21,000,000 for its Highway 706 project.

New York

Within New York, the Corporation is focused on exploration and development of the Trenton-Black River formation (conventional gas) and the Marcellus shale (unconventional gas). The Corporation's acreage position covers primarily Schuyler, Steuben, Chemung and Tioga counties, consisting of approximately 31,834 gross (15,548 net) leasehold acres. The Corporation has a 50% working interest in its New York acreage, with two privately held companies each holding a 25% working interest. See "*Related Party Transactions – Director and former President and Chief Executive Officer*".

NY Marcellus Shale

In New York, competitor companies are actively permitting Marcellus shale wells in and around the Corporation's leasehold acreage. The Corporation continues to evaluate potential exploration, development and production opportunities in the Marcellus shale, including but not limited to, participating in competitor wells, developing its existing leasehold acreage and/or entering in joint ventures with other companies.

During 2008, the Corporation participated in drilling one non-operated well (.03 net) in the Marcellus shale, which had a favorable production test and is currently shut in waiting on production infrastructure. Based on the positive test results from that well, the Corporation has commenced staking its first four

company-operated Marcellus shale test wells within its Park Place project. Drilling operations on those wells are expected to commence during late 2009.

NY Trenton-Black River

The Corporation is also focused on exploration of the prolific Trenton-Black River formation, a conventional natural gas reservoir target. The Corporation holds various non-operated working interests with multiple operators in well units from less than 1%, up to approximately 12%. The Corporation has leveraged the expertise of local area operators, including utilizing 3D seismic and horizontal drilling techniques. Production rates from the Trenton-Black River can range from 3.0 MMcf/d to 40.0 MMcf/d on a gross basis.

Within the Trenton-Black River formation, 9 gross (0.34 net) wells were producing and 4 gross (0.08 net) wells were shut in waiting on pipeline connection at March 31, 2009. In addition, 4 gross (0.03 net) non-participating wells had not paid out and the Corporation had drilled 14 gross (0.42 net) exploratory dry holes since its inception. At March 31, 2009, net production from Trenton-Black River formation was approximately 816 Mcf/d. See “*Commitments and Contingencies – New York – Trenton-Black River Well Units*”.

NY 2009 Outlook

Due to its current focus on the Marcellus shale in Pennsylvania and New York, the Corporation is not allocating a significant amount of capital to fund participation in drilling future wells targeting the Trenton-Black River formation in New York. During 2009, the Corporation expects to selectively participate in two or more Trenton-Black River wells with a small working interest and drill four Marcellus shale wells with a 50% working interest at an overall net cost of approximately \$1,300,000.

West Virginia

The Corporation currently has two medium-to-low risk Devonian-aged shale gas project areas in West Virginia; Amber Bank and Blue Jacket. Hard Rock Exploration Inc., a local operator, is the operator of each of these projects.

The Amber Bank project is located in Jackson and Roane counties and consists of approximately 25,957 gross (8,463 net) leasehold acres, in which the Corporation holds working interests ranging from 30% to 60%. In the Amber Bank project, the Corporation is focused on targets in three shallow unconventional Devonian-aged shale gas zones; the Lower Huron, Rhinestreet, and Marcellus. Collectively, these Devonian-aged shale gas zones represent approximately 850 feet of prospective gas bearing shale.

The Blue Jacket project is located in Cabell county and consists of approximately 10,227 gross (6,042 net) leasehold acres, in which the Corporation holds a 63% working interest. In the Blue Jacket project, the Corporation is focused on two shallow unconventional Devonian-aged shale gas zones; the Lower Huron and Rhinestreet. Collectively, these Devonian-aged shale gas zone represent approximately 400 feet of prospective gas bearing shale.

Through March 31, 2009, the Corporation had participated in drilling 112 gross (59.59 net) wells in West Virginia with a 100% success rate, including 111 gross (58.99 net) producing wells and 1 gross (0.60 net) well that was shut in awaiting hook-up. Natural gas production from West Virginia was approximately 1,324 Mcfe/d net to the Corporation as of March 31, 2009. Due to its current focus on the Marcellus shale in Pennsylvania and New York, the Corporation does not anticipate allocating any funds to continue participating in drilling wells on its West Virginia projects during 2009.

Ohio

The Bailey’s Mill project is located in Belmont and Monroe counties and consists of approximately 40,155 gross (8,840 net) leasehold acres, in which the Corporation holds a 25% working interest. PC Exploration

Inc. is the operator and also holds a 75% working interest in the Bailey's Mill project. The Corporation is focused on the Marcellus, a shallow unconventional Devonian-aged shale gas zone. The Marcellus Devonian-aged shale gas zone represents approximately 80 feet of prospective gas bearing shale. Through March 31, 2009, the Corporation had drilled three gross (0.75 net) wells, all of which were producing gas on an intermittent basis at the rate of approximately 34 Mcf/d net to the Corporation. Due to its current focus on the Marcellus shale in Pennsylvania and New York, the Corporation does not anticipate allocating a significant amount of funds to continue participating in drilling future wells on its Bailey's Mill project.

Canada

Saskatchewan

On August 28, 2008, the Corporation entered into an agreement with a private Canadian company covering joint oil and natural gas exploration and development activities in a 63,360 gross acre AMI covering the Bakken oil play in southeast Saskatchewan province. Under the terms of the agreement the Company has the ability to earn a 50% interest in approximately 8,960 gross (7,806 net) acres within the AMI. The private Canadian company is the operator of the AMI and drilling operations on the first well are expected to commence during the last half of 2009. The Corporation estimates it will spend a minimum amount of \$5.0 million on this project. The project lies within the favorable Saskatchewan province royalty area. See "*Commitments and Contingencies – Bakken Shale Drilling Commitment*".

On October 9, 2008, the Corporation acquired additional prospective Bakken oil play interests in approximately 31,370 gross (13,775 net) acres for approximately \$439,000 via a competitive bid at the Saskatchewan crown lease sale with the same private company.

Quebec

The Corporation has an elective participating interest of up to 25% in Gastem, Inc.'s (TSXV: GMR) holdings in approximately 1,184,000 gross (249,000 net) leasehold acres. The leasehold acreage includes 452,000 gross (66,000 net) leasehold acres in the St. Lawrence Lowlands covering Utica shale, and Trenton-Black River targets and 733,000 (183,000 net) leasehold acres in the Gaspé Peninsula covering Silurian and Devonian targets. Within the St. Lawrence Lowlands leasehold acreage, Forest Oil Corporation has committed to spend CDN\$10 million to earn a 60% interest in approximately 112,000 gross acres held by Gastem Inc, which is referred to as the Yamaska project. The Corporation elected to not participate in the first two wells drilled on the Yamaska project. However, the Corporation has elected to participate in future operations with a 5% working interest and does not expect to spend a significant amount of capital.

Yemen – Block 41

During 2007, the Corporation acquired a 57.14% paying interest and 50% undivided percentage interest in the rights, duties, interests and obligations under the Block 41 Production Sharing Agreement ("**Block 41 PSA**") covering approximately 5,600 square kilometers (1.4 million acres), which is located onshore in Yemen. The Corporation is the operator of Block 41. As of the date of this report, the Corporation had fulfilled all obligations pertaining to the Farm-in Agreement except for the \$3.0 million due upon the Declaration of Commerciality, an event that has yet to occur. There is one field discovery, the Al Waya 1, which was drilled by the prior operator in 2002 and tested at 473 barrels per day ("**bbbls/d**") of 34° API gravity oil from the Naifa formation and had significant shows in lower formations.

From mid-2008 through the first quarter of 2009, the Corporation drilled four exploratory wells (Al Waya #2, Kaninah #1, West Mahrawa #2 and Mukulla #1) on Block 41, all of which were non-commercial despite having encouraging oil and gas shows. The Corporation is currently evaluating the data obtained to date from its operations on Block 41 to determine the most effective way to proceed with its future exploration activities on Block 41, if any.

As of the date of this report, substantially all seismic activity has been focused on the western half of the middle portion of Block 41 where the Al Waya field discovery is located, which represents approximately one-third of the concession. There has been little or no exploratory activity conducted on the other portions of Block 41. As such, management believes there may be potential for substantial oil and natural gas resources yet to be exploited on Block 41 beyond the prospects identified on 2D seismic to date.

Oil and Gas Mine Company (“OGMC”) Default

As at March 31, 2009, Oil and Gas Mine Company, a non-operated joint interest owner in Block 41, owed the Corporation \$6,503,000, which covered their pro-rata share of costs pertaining to Block 41 in Yemen as of that date. Of that amount, \$5,591,000 was in default. On April 20, 2009, Oil and Gas Mine Company paid the Corporation \$2,000,000 and verbally agreed to pay the remaining amount in default within thirty days.

Ethiopia – Northwest Area Study Agreement

On June 12, 2008, the Corporation entered into an exclusive Study Agreement, referred to as the Northwest Area Study Agreement, with the Ministry of Mines and Energy in Ethiopia. The Northwest Area Study Agreement covers 154,871.53 square kilometers (96,232.7 square miles) in the northwestern sector of the country for an initial one year term and includes an exclusive right to negotiate an agreement or agreements to further explore for oil and natural gas on any or all of the land covered by the Northwest Area Study Agreement by obtaining an oil and natural gas concession or concessions from the Ministry of Mines. Since signing the Northwest Study Agreement, the Corporation has acquired detailed stream drainage maps and Landsat imagery over the study area. Based on that data, 13 large surface high areas have been identified.

On May 14, 2009, the Corporation announced that it had signed a Production Sharing Agreement (“PSA”) with the Ministry of Mines and Energy (the “Ministry”) in Democratic Republic of Ethiopia. The PSA covers an area of 79,345 square kilometers in northwest Ethiopia. Terms of the PSA include an initial three-year exploration period that includes a minimum financial commitment of \$3,000,000 to drill one exploratory well and to acquire a minimum of 200 kilometers of 2D seismic. In the event the Company makes a commercial discovery, the initial percentage split of profit oil and/or gas will be 80% for Epsilon and 20% for the Ministry.

The Hosan Field, located approximately 300 kilometers west in Sudan, is the nearest commercial oil and gas field, which reportedly has estimated recoverable gas reserves of approximately 350 BCFE. Other nearby Sudanese oil and gas fields have estimated recoverable oil reserve sizes ranging from 100 to 600 MMBO. The Company’s Ethiopian acreage has technical similarities to the Sudan oil and gas fields. As compared to Sudan, the political risk in Ethiopia is drastically different, as the Ethiopian government appears to be much more stable, easy to work with and is encouraging foreign investment.

Oman - Block 55

On January 26, 2009, the Corporation was awarded a 100% working interest in Block 55, an onshore oil and natural gas concession in Oman that covers approximately 7,564 square kilometers (1,869,105 acres). In management’s opinion, Block 55 is prospective for commercial oil and natural gas exploitation. Exploration plans during the initial three year exploration program include acquiring 800 kilometers of seismic data, reprocessing 4,133 kilometers of existing seismic data and a drilling program covering a minimum of four initial exploratory wells designed to exploit Block 55’s oil and natural gas potential.

Within Block 55 four exploratory wells have been previously drilled, including the Ameerq-1, which is a discovery well that may contain crude oil reserves in the range of one to ten Mbbls. Two of the three remaining exploratory wells previously drilled on Block 55 encountered oil and natural gas shows but failed to yield commercial quantities of oil. Adjacent to and within 20 kilometers of Block 55, there are approximately 27 discoveries, including 12 fields comprising approximately 158 wells that are currently productive. In addition, OilEx, who operates an adjacent block, has reported a significant oil discovery

near the southern border of Block 55. Other oil and natural gas operators in Oman include PDO, EnCana, Hunt Oil, Reliance Industries, MOL, Sinopec and Occidental.

Terms of the Exploration and Production Sharing Agreement (“**EPSA**”) include an initial bonus payment of \$2,000,000 and a commitment to spend a minimum of \$25,500,000 over an initial three-year exploration period comprising the following items:

- 3D seismic: acquire 300 square kilometers; reprocess 133 square kilometers
- 2D seismic: acquire 500 square kilometers, reprocess 4,000 square kilometers
- Drill four wells

At the Corporation’s option, the initial exploration period can be extended for an additional three year period provided the Corporation commits to spend \$28,500,000, comprising the following items:

- Acquire 600 square kilometers of 3D seismic or 500 square kilometers of 2D seismic
- Drill three wells

Commercial crude oil production carries a contractual term of 20 years and will be allocated as follows:

- 40% of crude oil production is designated for cost recovery.
- 60% of crude oil production is designated as profit oil and will be allocated as follows:
 - Up to 10,000 bbls/d - 80% government of Oman; 20% Operator
 - 10,000 to 20,000 bbls/d - 82.5% government of Oman; 17.5% Operator
 - Over 20,000 bbls/d - 83.5% government of Oman; 16.5% Operator

The Corporation is obligated to pay income taxes to the government of Oman. However, under terms of the Block 55 EPSA, the government of Oman undertakes to pay such taxes on behalf of the Corporation from the government of Oman's share of crude oil and/or gas.

The Corporation is the official operator of Block 55 and is considering bringing in industry partners, raising additional capital, or a combination of both to fund the exploitation of this concession. Leaving aside the \$2,000,000 bonus payment, the Corporation does not expect to spend a significant amount of capital towards this concession until 2010 or later.

Critical Accounting Estimates

The preparation of the consolidated financial statements in accordance with Canadian generally accepted accounting principles requires management to make estimates that affect reported amounts of assets and liabilities, the disclosure of any contingent assets and liabilities as of the date of the consolidated financial statements, as well as the reported amounts of revenues and expenses during the reported periods. By their nature, these estimates, including those related to future cash flows are subject to measurement uncertainty and the impact on the current and future consolidated financial statements resulting from changes in such estimates could be significant. Due to the use of estimates, actual results could differ significantly from those reported. Management believes the estimates used within the consolidated financial statements are reasonable as of the date of these consolidated financial statements.

The amounts recorded for depletion and amortization of property and equipment, stock based compensation, stock options, warrants, income taxes, asset retirement obligations, and other accruals are based on estimates. The Ceiling Test is based on estimates of oil and natural gas reserves, production rates, oil and natural gas prices, future costs and other relevant assumptions. Stock compensation, stock options, and warrants are valued using the Black-Scholes option pricing model which includes volatility assumptions that contain measurement uncertainty. The valuation allowance for income taxes is subject to measurement uncertainty pertaining to projected future production levels, future capital expenditures, future commodity prices and future operating costs, all of which could vary significantly from actual results. Asset retirement obligations contain plugging and abandonment estimates, productive well life

estimates, and other factors for which actual results may vary significantly from original estimates. Also see Note 3 – “*Accounting Pronouncements*” within the annual consolidated financial statements for the year ended December 31, 2008.

Full Cost Accounting

The Corporation utilizes the full cost method of accounting for its crude oil and natural gas properties. Accordingly, all costs related to the exploration for and development of crude oil and natural gas reserves, whether successful or not, are capitalized. The capitalized costs and future capital costs are depleted on the unit-of-production method based on estimated proved reserves. Costs of significant unproved properties, net of impairments, are excluded from the amortization, depletion and accretion calculation. Properties excluded from the depletion calculation are assessed periodically to ascertain whether impairment has occurred.

The carrying amount of crude oil and natural gas properties may not exceed their recoverable amount (the “**Ceiling Test**”). The costs are assessed to be recoverable if the sum of the undiscounted cash flows expected from the production of proved reserves and the lower of cost or market of unproved properties exceeds the carrying value of the crude oil and natural gas assets. If the carrying value of the crude oil and natural gas assets is assessed to not be recoverable, an impairment loss is recognized to the extent that the carrying value exceeds the sum of the discounted cash flows expected from the production of proved and probable reserves and the lower of cost or market of unproved properties. The cash flows are estimated using future product prices and costs, which are discounted using a risk-free rate of interest. At December 31, 2008, the Ceiling Test for the Corporation’s Yemen oil and natural gas properties failed, resulting in an impairment of \$34,099,000.

The alternative method of accounting for crude oil and natural gas properties is the successful efforts method. The major difference in applying the successful efforts method is that exploratory dry holes and geological and geophysical exploration costs are charged against net earnings in the year they are incurred rather than being capitalized. The use of the full cost method usually results in higher capitalized costs and higher DD&A rates than the successful efforts method.

Crude Oil and Natural Gas Reserves

The Corporation retains qualified independent reserves evaluators to estimate the Corporation's proved and probable crude oil and natural gas reserves. The estimation of reserves involves the exercise of judgment. Forecasts are based on engineering data, expected rates of production and the timing of future capital expenditures, all of which are subject to major uncertainties and interpretations. The Corporation expects that over time its reserve estimates will be revised upward or downward based on updated information such as the results of future drilling, testing and production levels. Reserve estimates can have a significant impact on net earnings, as they are a key component in the calculation of DD&A and for determining potential asset impairment. For example, a revision to the reserve estimate would result in a higher or lower DD&A charge to net earnings. Downward revisions to reserve estimates could also result in a write-down of crude oil and natural gas properties.

When estimating oil and natural gas reserves and their associated net cash flows, there are numerous factors that contain significant measurement uncertainties that are beyond the Corporation’s control. Those factors include, but are not limited to, volumetric reserve estimates, future commodity pricing, future operating costs and the timing of and amount of future capital costs. When assessing the fair market value of reserves, additional factors must be considered such as current market conditions, credit markets, location of reserves, classification of reserves based on risk of recovery, political risk and other factors, all of which may contribute to significant measurement uncertainty. Due to the complexity involved, reserve estimates and fair market value estimates will vary greatly from one party to another.

Asset Retirement Obligations (“ARO”)

The Corporation is required to recognize a liability for future abandonment and site restoration costs associated with the Corporation's crude oil and natural gas properties in accordance with existing laws, contracts or other policies. The fair value of the estimated ARO is recorded as a long-term liability, with a corresponding increase in the carrying amount of the related asset known as the asset retirement cost, which is depleted on a unit-of-production basis over the life of the reserves. The liability is adjusted each reporting period to reflect the passage of time, with the accretion charged to earnings, and for revisions to the estimated future cash flows, if any. Actual costs incurred upon settlement of the obligations are charged against the liability. The ARO is based on estimated costs, taking into account the anticipated method and extent of restoration consistent with legal requirements, technological advances, industry practices and the possible use of the site. Since these estimates are specific to the sites involved, there are many individual assumptions underlying the Corporation's total ARO amount. These individual assumptions can be subject to change based on experience. Restoration technologies and costs are constantly changing, as are regulatory, political, environmental, safety and public relations considerations. The Corporation estimates future retirement costs based on current estimates adjusted for inflation and credit risk. These estimates for inflation and credit risk are also subject to measurement uncertainty.

The Corporation has estimated the net present value of its total ARO for wells drilled on its projects in the Appalachian basin to be \$349,872 and \$334,757 at March 31, 2009 and December 31, 2008, respectively, based on estimated total undiscounted future liabilities of \$1,134,576 and \$1,075,126 at March 31, 2009 and December 31, 2008, respectively. These payments are expected to be made at the end of the associated properties economic life, which is estimated to be approximately 65 years. The Corporation assumed an estimated credit adjusted risk-free rate of 4.25% and an estimated inflation rate of 2% to calculate the net present value of the asset retirement obligations. The total future ARO was estimated based on the Corporation's net ownership interest in all wells and facilities in the Appalachian basin in the U.S, and includes estimated costs to reclaim and abandon the wells and facilities and the estimated timing of the costs to be incurred in future periods.

No provision was made for asset retirement obligations with respect to the Corporation's Yemen properties, where the contracts with the government of Yemen stipulate that all property and equipment will be transferred to the government of Yemen at the end of the contract term. Asset retirement activities during the contract term in Yemen, if any, are fully recoverable from the proceeds of cost oil. The EPSA in Oman contains provisions whereby the operator must fund estimated abandonment costs during the five calendar years prior to the expiration of the EPSA. Since the Corporation has yet to commence drilling operations in Oman, there were no provisions made for ARO liabilities in Oman as of March 31, 2009.

Stock-Based Compensation

The Corporation records stock-based compensation expense using the fair value method. The fair value of an option is calculated at the grant date using the Black-Scholes option pricing model and expensed over the vesting term of the option. The Corporation records the cumulative stock-based compensation as a contributed surplus. When options are exercised, contributed surplus is reduced and share capital is increased by the amount of accumulated stock-based compensation for the exercised option. Any consideration received on the exercise of stock options is credited to share capital. The determination of stock-based compensation expense is based on assumptions regarding stock volatility, risk-free interest rates and the term of the options. These assumptions, by their nature, are subject to measurement uncertainty. An increase in volatility, the risk-free rate or the term would increase the calculated expense.

Income Taxes

The determination of the Corporation's income and other tax liabilities requires the interpretation of complex laws and regulations. All tax filings are subject to audit and potential reassessment after the lapse of considerable time. Accordingly, the actual income tax liability may differ from that estimated and recorded by the Corporation's management. The valuation allowance for income taxes, if any, is subject to measurement uncertainty pertaining to projected future production levels, future capital expenditures,

future commodity prices and future operating costs, all of which could vary significantly from actual results.

International Financial Reporting Standards

In March 2007, the Canadian Institute of Chartered Accountants (“CICA”) announced that Canadian publicly accountable enterprises will adopt International Financial Reporting Standards (“IFRS”) as issued by the International Accounting Standards Board (“IASB”) effective January 1, 2011. IFRS will require increased financial statement disclosure.

Under IFRS, the primary audience is capital markets and, as a result, there is significantly more disclosure required, specifically for quarterly reporting. Further, while IFRS uses a conceptual framework similar to Canadian GAAP, there are significant differences in accounting policy which must be addressed. The Corporation has not completed development of its IFRS changeover plan, which will include project structure and governance, deployment of resources and training, analysis of key GAAP differences and a phased plan to assess accounting policies under IFRS as well as potential IFRS 1 exemptions. The Corporation hopes to complete its project scoping, which will include a timetable for assessing the impact on data systems, internal controls over financial reporting, and business activities, such as financing and compensation arrangements, once the exemptions as described below relating to full cost oil and gas companies have been determined. The IASB has issued an exposure draft relating to certain amendments to IFRS 1 in order to make it more useful to Canadian entities adopting IFRS for the first time. One such exemption relating to full cost oil and gas accounting is expected to result in a reduced administrative transition from the current Canadian AcG-16 to IFRS. It is anticipated that this exposure draft will not result in an amended IFRS 1 standard until late in 2009. The amendment will potentially permit the Corporation to apply IFRS prospectively to its full cost pool, rather than the retrospective assessment of capitalized exploration and development expenses, with the proviso that a ceiling test, under IFRS standards, be conducted at the transition date.

Although IFRS uses conceptual framework similar to GAAP, differences in accounting policies will need to be addressed. One issue of primary concern is that under IFRS, oil and natural gas companies must use a the IFRS compliant Successful Efforts Method of accounting, as compared to the Full Cost Method of accounting currently utilized by the Corporation. If adoption to the Successful Effort Method is required, a conversion from the Full Cost Method of accounting to the Successful Efforts Method of accounting will likely have a material impact on the Corporation’s consolidated financial statements. The Corporation is currently assessing the impact this and other IFRS related issues will have on its consolidated financial statements when the Corporation transitions to IFRS beginning January 1, 2010.

Changes in Accounting Policies, including Initial Adoption

The Corporation has reviewed all recently issued, but not yet adopted, accounting standards by CICA in order to determine their effects, if any, on the Corporation’s results of operations or financial position. Based on that review, the Corporation believes none of the pronouncements, except for the conversion to IFRS that is scheduled to be effective January 1, 2011, will have a significant effect on current or future earnings or operations. As part of IFRS disclosure in 2011, the Corporation must show comparative information for 2010 in the basis of IFRS.

In February 2008, the CICA issued section 3064 of the CICA Handbook “*Goodwill and Intangible Assets*”, which replaces section 3062 of the CICA Handbook “*Goodwill and Other Intangible Assets*” and section 3450 of the CICA Handbook “*Research and Development Costs*”. These new sections of the CICA Handbook are applicable to fiscal years beginning on or after October 31, 2008 and establish standards for recognition, measurement, presentation and disclosure of goodwill subsequent to its initial recognition and of intangible assets by profit-oriented enterprises. Standards concerning goodwill are unchanged from the standards included in the previous section 3062. On January 1, 2009, the Corporation adopted this section. This new standard did not have a material impact on the Corporation’s consolidated financial statements.

Results of Operations

(Dollar amounts are rounded at thousands of U.S. dollars, unless stated otherwise)

The following discussion encompasses the Corporation's revenues and costs of operations. Unless noted otherwise, the discussion pertains to the Corporation's Appalachian basin segment, as all other identified geographical operating segments were essentially in the start-up phase during the first three months of 2009 and the year ended December 31, 2008, and had no reportable revenues or operating costs during those years.

Revenues

Since the commencement of the Corporation's first natural gas production during the third quarter of 2006, the Corporation's oil and natural gas revenues have consisted primarily of natural gas production from its West Virginia and New York projects, both of which are in the Appalachian business segment. Historically, the operator in each of the Corporation's projects has marketed the Corporation's pro-rata share of natural gas produced, primarily at index prices applicable to each area of production. In West Virginia, the Corporation receives, on average, a premium of approximately 15% over the posted natural gas prices due to the high Btu content in the natural gas the Corporation produces. Summary data follows:

	Three Months Ended March 31,	
	2009	2008
	<i>(Unaudited)</i>	
<i>Summary Revenue Data:</i>		
<i>Oil and Natural Gas Production:</i>		
Net oil and natural gas production (Mcf)	201,707	148,567
Realized average natural gas price per MCF.....	\$ 8.13	\$ 9.65
Net oil and natural gas revenues	\$ 1,635,000	\$ 1,537,000
End of period net production exit rate (Mcf/d)...	2,188	1,747
Net natural gas gathering fees	\$ 72,000	-
Total revenues	\$ 1,708,000	\$ 1,537,000

Producing Well Counts

At March 31, 2009, the Corporation had 124 gross (60.1 net) producing wells, including 111 gross (59.0 net) wells in West Virginia, 9 gross (0.3 net) wells in New York, and 3 gross (0.8 net) in Ohio. In addition, the Corporation had 27 gross (10.8 net) shut-in wells waiting on tie-in to facilities and was in the process of drilling 2 gross (1.4 net) wells. At March 31, 2008, the Corporation had 93 gross (46.1 net) producing wells, including 86 gross (45.4 net) wells in West Virginia, 5 gross (0.2 net) wells in New York, and 2 gross (0.5 net) in Ohio. In addition, the Corporation had 27 gross (10.8 net) shut-in wells waiting on tie-in to facilities and was in the process of drilling 2 gross (1.4 net) wells.

Oil and Natural Gas Revenues

During the three months ended March 31, 2009, oil and natural gas revenues were \$1,635,000, an increase of approximately 6%, and oil and natural gas production was 201,707 Mcfe, an increase of approximately 35%, as compared to the same period of 2008. The increase in oil and natural gas revenues was principally due to a higher amount of wells on line during the first quarter of 2009, as compared to the same period of 2008, which was partially offset by a 16% decrease in natural gas prices over the same period.

Other Revenue

Other revenue consists of net natural gas gathering fees from the Corporation's Blue Jacket project in West Virginia. The Corporation owns a 63% working interest in the gathering system that serves the Blue Jacket

project. For the three months ended March 31, 2009, net natural gas gathering fees were \$72,000. There were no net natural gas gathering fees recorded during the same period of 2008.

Cost of Operations

The Corporation's cost of operations has progressively increased as the Corporation continues to expand its business. Cost of operations includes project operating costs, amortization and depletion and general and administrative expenses. For the three months ended March 31, 2009 and all of 2008, substantially all operating costs pertained to the Corporation's Appalachian basin business segment. Summary data follows:

	Three Months Ended March 31,	
	2009	2008
	(Unaudited)	
<i>Project operating costs:</i>		
Production taxes	\$ 63,000	\$ 67,000
Lease operating expenses	402,000	214,000
Royalties.....	2,000	-
Total project operating costs	<u>467,000</u>	<u>281,000</u>
<i>Amortization, Depletion and Accretion ("DD&A"):</i>		
Amortization	27,000	12,000
Depletion.....	666,000	413,000
Accretion.....	4,000	3,000
Total DD&A.....	<u>697,000</u>	<u>428,000</u>
<i>General & Administrative ("G&A"):</i>		
General G&A	938,000	1,229,000
Non-monetary compensation	368,000	309,000
Total G&A	<u>1,306,000</u>	<u>1,538,000</u>
Total operating costs	<u>\$ 2,470,000</u>	<u>\$ 2,247,000</u>

Project Operating Costs

Project operating costs consist of production taxes, lease operating expenses and royalties. Project operating costs were \$467,000 and \$281,000 for the three months ended March 31, 2009 and 2008, respectively. A description of each category comprising project operating costs follows:

- Production taxes are assessed by the state in which production occurs. Substantially all production taxes apply to West Virginia, where the production tax rate is approximately 4% of gross revenues. In New York, the Corporation's wells are exempt from production taxes. Production taxes will vary from period-to-period based on production levels by state and/or oil and natural gas prices.
- Lease operating expenses include the operating costs necessary to extract gas and transport it to a sales point. Lease operating costs were \$1.99/Mcfe and \$1.45/Mcfe for the three months ended March 31, 2009 and 2008, respectively. Lease operating expenses per Mcf or Bbl will vary from period-to-period based on the level of oil and or natural gas production and related expenses. As the Corporation increases its operations, lease operating expenses are expected to increase accordingly in future periods.
- Royalties reflect amounts paid to New York royalty owners for wells in which the Corporation is not yet classified as an integrated participating owner, but the Corporation is required to pay

its share of royalties applicable to integrated royalty owners. See “*Commitments and Contingencies – New York – Trenton-Black River Well Units*”.

Amortization, Depletion and Accretion

Amortization expense was \$27,000 and \$12,000 for the three months ended March 31, 2009 and 2008, respectively. All amortization expense amounts pertained to the Corporation’s office furniture and fixtures, computer hardware and computer software.

Depletion expense was \$666,000 (\$3.30/Mcfe) and \$413,000 (\$2.79/Mcfe) for the three months ended March 31, 2009 and 2008, respectively. Depletion expense was progressively higher due to natural gas production volumes and higher per Mcfe depletion rates, both of which increased period over period. As at March 31, 2009, in accordance with the full cost method for depletion, the Corporation excluded unproved property costs of \$26,645,000 for the United States from the depletion calculation. As at March 31, 2008, in accordance with the full cost method for depletion, the Corporation excluded unproved property costs of \$13,879,000 for the United States from the depletion calculation. Also, the Corporation included \$240,000 and \$237,000 of impaired unproved leasehold costs in its capitalized proved oil and natural gas property depletion base for the three months ended March 31, 2009 and 2008, respectively. Depletion expense will fluctuate from period to period depending upon production levels, the amount of proved reserves, the level of capital expenditures and other factors.

Accretion expense was \$4,000 and \$3,000 for the three months ended March 31, 2009 and 2008, respectively. All accretion expense amounts pertain to the amortization of the Corporation’s asset retirement obligations.

General and Administrative

G&A was \$1,306,000 for the three months ended March 31, 2009, a decrease of \$232,000, as compared to \$1,538,000 for the same period of 2008. G&A was lower during the first three months of 2009 as the Corporation spent less on legal and travel costs, as compared to the same period of 2008. As the Corporation expands its business, G&A expenses are expected to increase accordingly in future periods.

Non-cash compensation included as a G&A component was \$368,000 and \$309,000 for the three months ended March 31, 2009 and 2008, respectively. Non-monetary compensation comprises stock options and Common Shares granted to certain employees, consultants and directors of the Corporation. For stock option awards, the Corporation estimated the fair value of such stock options on the date of grant using the Black-Scholes option pricing model and amortized the fair value to G&A expense over the respective vesting periods. For Common Shares granted for services rendered, the fair value is determined based on the average sales price per Common Share on the date of grant, resulting in a charge to compensation expense in the period granted.

Other Income or (Expense)

Other income (expense) consists of interest earned on cash and cash equivalents, interest expense, gain or loss on sale of assets and other miscellaneous items. The amount of interest earned or interest expense incurred varies from period to period, primarily due to the level of the Corporation’s cash and cash equivalents. Other expense for the three months ended March 31, 2009 was \$72,000, consisting of interest income of \$127,000, purchase discounts of \$11,000 and interest expense of \$210,000. Other income was \$427,000 for the three months ended March 31, 2008 and consisted of \$428,000 of interest income and a loss of \$1,000 from the sale of the Ben Gay project, which consisted of 8,546 gross (1,651 net) unproved leasehold acres in West Virginia. Gross proceeds from the sale of the Ben Gay project was \$126,000 and associated capitalized costs were \$127,000.

Income Taxes

Due to the net losses incurred in the first three months of 2009 and 2008, the Corporation did not incur any income tax expense. The determination of the Corporation's income and other tax liabilities requires the interpretation of complex laws and regulations. All tax filings are subject to audit and potential reassessment after the lapse of considerable time. Accordingly, the actual income tax liability may differ from that estimated and recorded by the Corporation's management.

Comprehensive Income (Loss)

The Corporation's results of operations may vary significantly from period to period based on the factors discussed in "Risk Factors" within the Corporation's Annual Information Form dated as of April 1, 2009 and on other factors such as the Corporation's exploratory and development drilling success. Therefore, the results of any one period may not be indicative of future results.

The Corporation's comprehensive income (loss) consists of its reported net income (loss) plus unrealized foreign currency gains and losses. The Corporation's comprehensive income (loss) for each indicated period follows:

	Three Months Ended March 31,	
	2009	2008
	(Unaudited)	(Unaudited)
<i>Comprehensive Loss:</i>		
Net loss.....	\$ (835,000)	\$ (284,000)
Unrealized foreign currency gains and losses	(957,000)	(1,601,000)
Comprehensive loss.....	<u>\$ (1,792,000)</u>	<u>\$ (1,885,000)</u>

Liquidity and Capital Resources

Working Capital

At March 31, 2009 and December 31, 2008, the Corporation had working capital of \$3,960,000 and \$15,862,000, respectively, inclusive of restricted cash. The Corporation's working capital will fluctuate from period-to-period, depending on the timing of cash receipts and payments, the pace of its operations, investing, financing activities and other factors that may directly affect components of the Corporation's working capital.

Loan Facilities

At March 31, 2009, the Corporation had two credit lines in place totaling \$26,000,000 and had utilized \$24,989,000 of credit that was then available, including \$10,134,000 at Northwestern Bank and \$14,855,000 at TD Bank. A discussion of each loan facility follows:

- *Northwestern Bank, Traverse City, Michigan:* USD\$11,000,000, secured by a lien on the Corporation's New York assets in the amount of \$10,000,000 and a \$1,000,000 minimum deposit at Northwestern Bank. Terms of the credit line include an interest rate of prime less 1/4 percent. As at March 31, 2009, the Corporation had an outstanding amount of \$10,134,000 under the terms of this credit line, leaving \$866,000 of available unused credit.
- *TD Bank, Toronto, Canada:* USD\$15,000,000, secured by Canadian dollar equivalent of 115% of the borrowed amount. At March 31, 2009, the amount of restricted cash and cash equivalents by TD Bank was based on full utilization of the credit line coupled with a reserve for currency fluctuations. Terms of the credit line include an interest rate of prime

plus 0.5%. As at March 31, 2009, the Corporation had an outstanding amount of \$14,855,000 under the terms of this credit line, all of which was secured by \$18,436,000 of restricted cash, leaving \$145,000 of available unused credit.

During the later part of 2008 through the first quarter of 2009, the Corporation utilized its credit lines primarily to manage foreign currency translation volatility resulting from the United States financial crisis that developed during the latter half of 2008. During that time, the foreign currency translation rate changed from approximately 1.0 per Canadian dollar to U.S. dollar to approximately 0.80 per Canadian dollar to U.S. dollar. Prior to the United States financial crisis, the Corporation held a substantial amount of its cash, cash equivalents and short term investments in Canadian dollars.

On April 8, 2009, the Corporation utilized \$5,000,000 of its restricted cash to reduce its line of credit with TD Bank by the same amount.

Letter of Credit - Yemen

Under terms of the Block 41 Production Sharing Agreement (“Block 41PSA”), as operator the Corporation must post a letter of credit in favor of the Ministry of Minerals covering the gross amount of expected expenditures during each calendar year. During 2008, the Corporation initially posted a \$16,000,000 letter of credit secured by \$17,600,000 of restricted cash deposits at TD Bank. The letter of credit was subsequently reduced as documented details pertaining to the work program on Block 41 were presented to the Ministry of Minerals by the Corporation. At March 31, 2009, the balance of that letter of credit had been reduced to \$4,500,000, which was secured by restricted cash of \$5,585,000.

On April 14, 2009, the Ministry of Minerals reduced the Corporation’s line of credit in Yemen by \$4,188,000, leaving a balance outstanding of \$312,000 pertaining to the Yemen line of credit.

Restricted Cash

At March 31, 2009 and December 31, 2008, the Corporation’s restricted cash balances consisted of the following:

	March 31, 2009	December 31, 2008
Restricted Cash:		
Northwestern Bank – loan facility	\$ 1,000,000	\$ 1,000,000
TD Bank – loan facility	18,436,000	21,328,000
TD Bank – Yemen letter of credit	5,585,000	11,375,000
Total	<u>\$ 25,021,000</u>	<u>\$ 33,703,000</u>

Oil and Gas Mine Company Default

As at March 31, 2009, Oil and Gas Mine Company, a non-operated joint interest owner in Block 41, owed the Corporation \$6,503,000, which covered their pro-rata share of costs pertaining to Block 41 in Yemen as of that date. Of that amount, \$5,591,000 was in default. On April 20, 2009, Oil and Gas Mine Company paid the Corporation \$2,000,000 and agreed to pay the remaining amount in default within thirty days.

Cash Flow Discussion and Analysis

A detailed discussion of the Corporation’s cash flows from operations, investing activities, and financing activities follows:

Cash Flows from Operations

During the first three months of 2009, the Corporation used \$6,273,000 in its operating activities, an increase of \$5,775,000, as compared to \$498,000 for the same period of 2008. Cash used in operating

activities during the first three months of 2009 of \$6,273,000 was comprised of a net loss of \$835,000 and \$6,503,000 of negative adjustments pertaining to the Corporation's non-cash balances related to operations, which was partially offset by \$1,065,000 pertaining to positive non-cash add-backs covering amortization, depletion and accretion and stock based compensation. Cash used in operating activities during the first three months of 2008 of \$498,000 was comprised of a net loss of \$284,000 and \$952,000 of negative adjustments pertaining to the Corporation's non-cash balances related to operations, both of which were partially offset by \$738,000 pertaining to positive non-cash add-backs covering amortization, depletion and accretion, stock based compensation and a net loss on assets sold.

Cash Flows from Investing Activities

During the first three months of 2009, the Corporation received \$385,000 from its investing activities, as compared to spending 6,794,000 on its investing activities during the same period of 2008. During the first three months of 2009, the Corporation spent \$8,300,000 on its oil and natural gas properties, spent \$5,000 on office related equipment, received \$8,683,000 from changes in its restricted cash balances and received \$7,000 relating to changes in other assets and liabilities. During the first three months of 2008, the Corporation spent \$6,834,000 on its oil and natural gas properties, invested a net amount of \$85,000 on office equipment and deferred pre-operating costs in the Republic of Yemen and received \$126,000 of proceeds from the sale of the Ben Gay prospect in West Virginia.

Cash Flows from Financing Activities

During the first three months of 2009, the Corporation received \$5,802,000 from its financing activities. There were no cash flows from financing activities during the same period of 2008. During the first three months of 2009, the Corporation received \$5,805,000 of proceeds from drawing on its credit lines and reduced its long-term debt by \$3,000.

Effect of Currency Rates on Cash and Cash Equivalents

The effect of currency rates on cash and cash equivalents included a net unrealized loss of \$957,000 and \$1,601,000 for the three months ended March 31, 2009 and 2008, respectively. Net unrealized gains and losses arising from changes in currency rates on cash and cash equivalents will vary from period to period due to the level of the Corporation's cash and cash equivalents.

Capitalization, Common Shares and Options

At March 31, 2009, the Corporation's share capital was \$138,259,000, consisting of 50,315,323 Common Shares issued and outstanding. Also at March 31, 2009, the Corporation had outstanding unexercised options covering 3,154,751 Common Shares at a weighted average exercise price of approximately CDN\$2.53 per Common Share and a weighted average remaining contractual term of 6.8 years. Of those options, 1,984,476 were fully vested and 1,170,275 were unvested.

2009 Capital Budget

For 2009, the Corporation's Board of Directors approved a capital budget of \$28,800,000. Highlights include:

- Marcellus Shale - \$21,600,000; includes drilling at least two wells in Highway 706, hooking up wells in Highway 706 for production, constructing production infrastructure in Highway 706, and drilling four wells within the Park Place project in New York.
- Yemen - \$3,400,000; includes drilling one exploratory well.
- Oman - \$2,900,000; includes a \$2,000,000 signing bonus pertaining to Block 55.

The amount of capital to be spent in 2009 is mostly discretionary. As such, the Corporation's capital budget is a "fluid" amount and may increase or decrease due to factors such as available capital, operational success or failure, commodity prices and the actual pace of operations. In order to fully fund its

planned operations during 2009, it is likely that the Corporation may need additional capital to obtain its capital expenditure goals.

Future Capital Requirements

Mid 2008 through the end of the first quarter of 2009 resulted in one of the most volatile periods in the oil and natural gas industry. Commodity prices for oil and natural gas reached all time highs and then dipped to multi-year lows. In the last half of 2008, global capital markets tightened and retrenched dramatically. The downward trend in the capital and commodity markets resulted in many oil and natural gas companies reducing their capital budgets substantially due to the reduced availability of capital and reduced economic returns resulting from lower commodity prices. Accordingly, there can be no assurance that the Corporation can successfully raise enough capital to fund its future capital needs outside of its existing available capital at terms acceptable to the Corporation.

Historically, the Corporation has relied on proceeds from the sale of its Common Shares to fund its operations. In order to fully fund or accelerate the Corporation's current planned acquisition, exploration and development activities beyond 2009, the Corporation will need additional capital. The timing, pace, scope and amount of the Corporation's capital expenditures is largely dependent on the availability of capital. The Corporation may obtain funds for future capital investments from strategic alliances with other energy or financial partners, the issuance of additional Common Shares, Preferred Shares, or debt securities, project financing, sale of partial property interests, or other arrangements, all of which may dilute the interest of the Corporation's existing shareholders or the Corporation's interest in the specific project financed. The Corporation may change the allocation of capital among the categories of anticipated expenditures depending upon future events that the Corporation cannot predict. For example, the Corporation may change the allocation of its expenditures based on the actual results and costs of future exploration, appraisal, development, production, property acquisition and other activities. In addition, the Corporation may change its anticipated expenditures if costs of placing any particular discovery into production are higher, if the field is smaller, or if the commencement of production takes longer than expected.

The Corporation regularly forecasts its capital needs on an annual, quarterly and monthly basis. The Corporation's current internally generated cash flows do not provide sufficient capital for the Corporation's current long-range exploration and development plans. However, by prioritizing and adjusting the timing of capital expenditures, management anticipates its 2009 capital expenditures will be fully funded through most or possibly all of 2009 with its capital resources on hand at December 31, 2008, including the use of its existing \$11.0 million line of credit with Northwestern Bank, which is secured by a \$1.0 million minimum cash deposit and a \$10.0 million lien on the Corporation's New York properties. Accordingly, the Corporation anticipates raising additional capital to fully fund its capital needs beyond 2009, including fulfilling its obligations on Block 55 in Oman and to further develop its Marcellus shale properties in the Appalachian basin. Upon commencement of natural gas production from its Highway 706 project in Pennsylvania during mid 2009, the Corporation believes it will have sufficient oil and natural gas reserves required to obtain additional reserve based debt financing. However, tight credit markets, operational delays, or poor project performance could adversely affect the Corporation's ability to obtain such financing. The Corporation has a number of additional options available to it if cash flow does not cover future capital expenditure plans including, but not limited to, i) revising the scope and/or timing of its capital expenditure plans, ii) selling a partial or 100% interest in a property to a third party, iii) obtaining project specific financing from a third party, iv) obtaining additional debt financing, and v) issuing Common Shares, or a combination of these options. Beyond 2009, the Corporation's capital needs are expected to be met through a combination of cash flow and debt. Future debt levels are forecasted to remain within acceptable ratios for conforming reserve based debt.

Commitments and Contingencies

Bakken Shale Drilling Commitment

The Corporation entered into an agreement with a privately held Canadian company on August 28, 2008, whereby the Corporation agreed to pay 100% of the costs to drill a minimum of two horizontal wells in the Bakken shale in order to earn a 50% working interest in acreage controlled by the private company. The agreement was further amended on December 19, 2008, whereby the Corporation agreed to advance to the private company CDN\$2,712,000 prior to September 1, 2009 to drill the first earning well. Should the Corporation fail to do so, the Corporation must pay the private company liquidating damages of CDN\$2,000,000 and forfeit the Corporation's rights under the agreement. In addition, the private company shall then acquire the Corporation's other Bakken shale leasehold (purchased at the October 6, 2008 Saskatchewan Crown land sale and from Spartan on November 9, 2008) for CDN\$564,000. Furthermore, the private company is indebted to the Corporation in the amount of CDN \$439,000, as evidenced by a promissory note dated October, 6, 2008. The private company shall be entitled to offset the full amount that it may owe the Corporation should the Corporation fail to fund the first earning well and pay the liquidated damage amount outlined above.

Yemen- Block 41 PSA

In accordance with the Farm-in Agreement with the Oil and Gas Mine Company dated September 10, 2007, the Corporation is obligated to pay the Oil and Gas Mine Company \$3,000,000 upon a Declaration of Commerciality, which is defined as "*the act of approval by the Ministry of Minerals on the behalf of the Republic of Yemen for an operator to develop a Commercial Discovery under an existing production sharing agreement.*" The \$3,000,000 payment will only be incurred in the event the Corporation makes a commercial oil or natural gas discovery on Block 41 and the Ministry of Minerals grants a license to commercially produce such discovery. Due to the contingent nature of this item, it is not reflected in the Corporation's Balance Sheet at December 31, 2008.

Oman – Block 55 EPSA

On January 26, 2009, the Corporation was awarded Block 55, an onshore oil and natural gas concession in Oman that covers approximately 7,564 square kilometers (1,869,105 acres). Terms of the EPSA include an initial payment of \$2,000,000 and an initial three-year exploration period with a commitment to spend a minimum of \$25,500,000 during that period to drill four exploratory wells, acquire 300 square kilometers of new 3D seismic, reprocess 133 square kilometers of 3D seismic, acquire 500 square kilometers of 2D seismic, and reprocess 4,000 square kilometers of 2D seismic. The Corporation is the official operator of Block 55 and is considering bringing in industry partners, raising additional capital, or a combination of both to fully fund the exploitation of this concession. The Corporation does not expect to spend a significant amount of capital towards this concession until 2010 or later.

New York – Trenton-Black River Well Units

In June 2005, a new integration statute was enacted by the State of New York whereby leasehold interest owners could elect to participate in the drilling of a well by choosing one of the following options:

- 1) Integrated non-participating owner – leasehold owner elects to not pay their proportionate share of costs up-front. The leasehold owner participates in their proportionate share after payout of a non-consent penalty plus costs.
- 2) Integrated participating owner – leasehold owner elects to pay their proportionate share of costs up-front.
- 3) Integrated royalty owner – leasehold interest owner elects to receive a proportionate 12.5% royalty interest.

During 2006, the Department of Environmental Conservation classified the Corporation's interest in several wells drilled, prior to the statute change and by way of public hearing, as an integrated non-participating owner. As a result, the Corporation was charged a non-consent penalty on its pro-rata share of costs to drill and complete various wells by Fortuna, the operator. The Corporation believes its interest in the subject wells should have been classified as an integrated participating owner upon payment of its pro-rata share of costs, effectively negating the non-consent penalty the operator could charge prior to dispersing the Corporation's pro-rata share of profits. The Corporation formally appealed the Department of Environmental Conservation's ruling, and, if successful, will require the non-consent penalty withheld by the operator to be dispersed to the Corporation. As a result there is no anticipated effect on the Corporation's established working interest. As at March 31, 2009, the outcome of the Corporation's appeal was not determinable.

As at March 31, 2009, the Corporation was classified as an integrated non-participating owner in 7 gross (0.10 net) wells, including 3 gross (0.06 net) for which the non-consent penalty had paid out.

Arbitration – Pinpoint Drilling and Directional Services LLC

On November 5, 2008, the Corporation was notified by its contract operator that Pinpoint had served a Notice of Arbitration covering invoices totaling \$1,159,000 for drilling services performed by Pinpoint on the Corporation's Highway 706 project in Pennsylvania during 2008. At December 31, 2008, the Corporation had capitalized the entire disputed amount, including \$546,000 paid near the time the Notice of Arbitration was filed and the \$613,000 for which the Corporation has asserted is invalid due to negligent performance by Pinpoint and, which remained unpaid at year-end. The arbitration will take place in 2009.

Drilling services performed by Pinpoint on Highway 706 to date has been in accordance with a drilling contract dated May 16, 2008 between Pinpoint and the Corporation's contract operator for a term of one year. Under terms of the Contract, the Corporation is subject to a stand-by day rate of \$14,800 per day. On February 17, 2009, the Corporation, through its contract operator, informed Pinpoint that the Corporation's Board of Directors had approved terminating the drilling contract upon completion of drilling the Hardic 2H. Pinpoint completed drilling the Hardic 2H on March 18, 2009.

Office Leases

At March 31, 2009, the Corporation had the following offices:

- Traverse City, Michigan – office lease agreement effective April 1, 2007 with a two year term and monthly lease payments of \$4,000.
- Houston, Texas – office lease agreement effective November 26, 2008 with a five year term and monthly lease payments of \$6,000.
- Sana, Yemen - office lease agreement effective November 1, 2007 with a two year term and monthly lease payments of \$6,000.
- Abu Dhabi, United Arab Emirates: office lease agreement effective December 15, 2008 with a one year term and annual lease payment of \$57,000.
- Toronto, Canada - The Corporation's office in Toronto, Canada is owned by the Executive Chairman and is utilized at no charge to the Corporation. See "*Related Party Transactions – Executive Chairman*".

The future commitments and obligations are summarized in the following table:

	Payments Due by Period (Unaudited)				
	Total	Less than 1 Year	1 – 3 Years	4 – 5 Years	After 5 Years
Future Commitments:					
Accounts payable	\$ 11,307,000	\$11,307,000	\$ -	\$ -	\$ -
Line of credit ⁽¹⁾	24,989,000	24,989,000			
Long-term debt.....	32,000	16,000	16,000	-	-
Operating leases ³	501,000	216,000	152,000	133,000	
Purchase obligations ⁽¹⁾	2,171,000	2,171,000	-	-	-
Other long-term obligations ..	25,500,000	-	25,500,000	-	
Total	\$ 64,500,000	\$38,699,000	\$ 25,668,000	\$ 133,000	\$ -

Notes:

- (1) The line of credit is secured by restricted cash, which will be used to pay off the line of credit. See Note 4 “*Loan Facilities and Letter of Credit*”.
- (2) \$2,171,000 is the USD equivalent of CDN\$2,712,000 at March 31, 2009.

Disclosure Controls and Procedures

The Corporation has evaluated the effectiveness of its disclosure controls and procedures and has concluded based on the Corporation’s evaluation that they are sufficiently effective to provide reasonable assurance that material information relating to the Corporation is made known to management and disclosed in accordance with applicable securities regulations.

The Chief Executive Officer and Chief Financial Officer, together with other members of management, after having designed Internal Controls Over Financial Reporting (“ICFR”) to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial reporting in accordance with GAAP, have not identified any changes to the Corporation’s internal control over financial reporting which would materially affect, or is reasonably likely to materially affect, the Corporation’s internal control over financial reporting.

During 2008, the Corporation documented and tested its entity level and process level controls covering ICFR reporting and concluded that such controls were effective. To help insure continued adherence to established internal controls and related policies, the Corporation has initiated an internal control testing program that will be conducted throughout 2009.

Recent Changes in Accounting Standards

The Corporation has reviewed all recent changes in Accounting Standards, including Section 3064 of the CICA Handbook “*Goodwill and Intangible Assets*”. This Accounting Standard did not have a material effect on the Corporation’s financial results for the three months ended March 31, 2009.

Environmental Issues

Compliance with Environmental and Safety Regulations

All phases of the oil and natural gas business present environmental risks and hazards and are subject to environmental regulation pursuant to a variety of federal, provincial and local laws and regulations. Environmental legislation provides for, among other things, restrictions and prohibitions on spills and releases or emissions of various substances produced in association with oil and natural 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 liabilities, 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 governments and third parties and may require the Corporation to incur costs to remedy such discharge. Although the Corporation believes that it is in material compliance with current applicable environmental regulations, 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 Corporation's financial condition, results of operations or prospects. The Corporation must also conduct its operations in accordance with various laws and regulations concerning occupational safety and health. Currently, the Corporation does not foresee expending material amounts to comply with these occupational safety and health laws and regulations. However, since such laws and regulations are frequently changed, the Corporation is unable to predict the future effect of these laws and regulations.

Middle East and Africa

In emerging nations, such as Yemen, Oman and Ethiopia, where environmental regulations and legislation are evolving, many oil and natural gas exploration and production companies operate in accordance with standards prevailing in established oil and natural gas producing jurisdictions, such as Canada and the United States. The Corporation has yet to conduct any significant on the ground operations in Ethiopia, but intends to adhere to established industry practice standards upon the commencement of such operations.

The Corporation's activities in the Middle East and Africa are in predominately arid desert areas. As such, the environmental impact associated with exploration and production activity in these areas are significantly less than is typical for similar oil and natural gas exploration, development and production activities located in more temperate or tropical environments. The Corporation is committed to conducting its operations in the Middle East and Africa in accordance with environmental standards used by other major international oil and natural gas exploration and production companies. Generally, such standards meet or exceed those imposed by legislation and regulations in Yemen, Oman and Ethiopia.

North America

The Corporation's activities are subject to numerous federal, provincial and state laws and regulations concerning the storage, use and discharge of materials into the environment, the remediation of environmental impacts and other matters relating to environmental protection, all of which may adversely affect the Corporation's operations and the costs of doing business. Federal, provincial and state regulatory authorities also have established rules and regulations requiring permits for drilling, drilling bonds and reports concerning drilling and producing activities. Such regulations also cover the location of wells, the method of drilling and casing wells, the surface use and restoration of well locations, the plugging and abandoning of wells, and other matters. There can be no assurance that future legislation or administrative regulations or interpretations will not impose stricter requirements that could have an adverse impact on the operating costs of the Corporation and the oil and natural gas industry in general. The Corporation believes it is in material compliance with existing environmental laws and regulations and does not currently believe that it will be required to expend material amounts to comply with existing environmental laws and regulations in the future.

Related Party Transactions

The Corporation reports its related party transactions on an exchange amount basis. A summary of such transactions follows:

Executive Chairman

The Corporation utilizes administrative services provided by 706147 Ontario, Inc., a company owned by the Executive Chairman's spouse. In addition, the Corporation shares office space with Capital Z Corporation, a company owned by the Executive Chairman, at no charge. Related party transactions with the Corporation's Executive Chairman were conducted in Canadian dollars and the exchange rate

differences were immaterial. A summary of related party transactions between the Corporation and its Executive Chairman follows:

	Three Months Ended March 31, 2009	Year Ended December 31, 2008
706147 Ontario, Inc.:		
Administrative services.....	\$ 12,000	\$ 57,000

Director

On February 7, 2007, the Corporation obtained a 25% undivided participating interest in Gastem Inc.'s undeveloped oil and natural gas interests covering approximately 1,184,000 acres (249,000 net) in the St. Lawrence Lowlands and in the Gaspé Peninsula of Quebec. Under terms of the agreement, the Corporation may elect to participate on a well-by-well basis with a 25% working interest in any current or future properties Gastem Inc. may acquire in Quebec. In return, the Corporation granted Gastem Inc. the right to participate for 25% of the Corporation's interest in certain future wells to be drilled in the Corporation's Amber Bank project in West Virginia by spending up to \$1.05 million. The Corporation's carrying value of the portion of its Amber Bank project's leasehold attributable to Gastem Inc.'s participation was nominal. The agreement was consummated with the expectation that Raymond Savoie, Gastem Inc.'s President, would become a director of the Corporation. Mr. Savoie became a director of the Corporation on July 16, 2007. Related party transactions with Gastem Inc. were conducted in US dollars. A summary of related party transactions between the Corporation and Gastem Inc. follows:

	Three Months Ended March 31, 2009	Year Ended December 31, 2008
Gastem Inc.:		
Joint venture costs	\$ 17,000	\$ 77,000
Joint venture revenues	\$ 56,000	\$ 310,000
Accounts payable.....	\$ -	\$ 15,000

Director and former President and CEO

Austin Exploration LLC, a company owned by a Director who is also the former President and CEO of the Corporation, is also a participant in the Corporation's Empire project. Western Land Services Inc., a company owned by the same person, provides oil and natural gas lease brokerage services to the Corporation in accordance with a Project Services Agreement between Western Land Services and the Corporation. Under terms of the Project Services Agreement, Western Land Services agreed to provide services to the Corporation at its lowest corporate rates less 10%. Substantially all of the service amounts provided by Western Land Services are capitalized with oil and natural gas properties. Related party transactions with the President of Epsilon Energy USA, Inc. were conducted in US dollars. A summary of related party transactions between the Corporation and its Director who is also the former President and CEO follows:

	Three Months Ended March 31, 2009	Year Ended December 31, 2008
Austin Exploration LLC:		
Accounts receivable.....	\$ 22,000	\$ 110,000
Joint venture costs.....	\$ 166,000	\$ 2,655,000
Joint venture revenues	\$ 234,000	\$ 902,000
Accounts payable.....	\$ -	\$ 75,000
Western Land Services:		
Lease brokerage services	\$ 133,000	\$ 1,668,000
Accounts payable.....	\$ 34,000	\$ 139,000