GUARDIAN EXPLORATION INC.

Consolidated Financial Statements

December 31, 2009 and 2008

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Auditors' Report

To the Shareholders of
Guardian Exploration Inc.:

We have audited the consolidated balance sheet of Guardian Exploration Inc. as at December 31, 2009 and 2008 and the consolidated statements of loss, comprehensive loss and deficit and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2009 and 2008 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Signed "Deloitte & Touche LLP"

Calgary, Alberta
April 30, 2010

Chartered Accountants

GUARDIAN EXPLORATION INC.
CONSOLIDATED BALANCE SHEETS

	December 31 2009 $	December 31 2008 $
ASSETS		
Current assets		
Cash	264,214	693,056
Accounts receivable	598,869	404,248
Due from related company (Note 4)	50,000	449,951
Prepaid expenses	21,032	50,640
	934,115	1,597,895
Deposit (Note 5)	376,010	438,380
Future income taxes (Note 9)	-	694,000
Property and equipment (Note 6)	2,663,772	4,430,541
	3,973,897	7,160,816
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities		
Accounts payable and accrued liabilities	2,196,309	2,933,038
Loan from related party (Note 7)	550,000	-
	2,746,309	2,933,038
Asset retirement obligations (Note 8)	1,057,321	1,161,783
	3,803,630	4,094,821
Shareholders' equity		
Share capital (Note 10a,b)	10,349,866	11,021,365
Warrants (Note 10c)	944,840	1,618,440
Contributed surplus (Note 10e)	2,352,708	1,603,505
Deficit	(13,477,147)	(11,177,315)
	170,267	3,065,995
	3,973,897	7,160,816

Going Concern (Note 1)
Commitments (Note 11)
Contingencies (Note 13)

See accompanying notes to the consolidated financial statements

Approved on behalf of the Board of Directors

signed "*Graydon Kowal*"
Graydon Kowal
Director

signed "*Scott Reeves*"
Scott Reeves
Director

GUARDIAN EXPLORATION INC.
CONSOLIDATED STATEMENTS OF LOSS, COMPREHENSIVE LOSS AND DEFICIT
FOR THE YEARS ENDED DECEMBER 31, 2009 AND 2008

	2009	2008
	$	$
Revenue		
Petroleum and natural gas	4,391,264	7,133,555
Royalties	(1,487,625)	(837,317)
	2,903,639	6,296,238
Expenses		
Operating	1,536,360	1,809,047
General and administrative	1,648,174	1,461,879
Bad debts recovery	(8,000)	(279,440)
Stock-based compensation	75,603	517,794
Depletion, depreciation, impairment and accretion (Note 6)	1,876,519	5,719,727
Foreign exchange loss (gain)	42,422	(85,712)
	5,171,078	9,143,295
Loss before other items	(2,267,441)	(2,847,057)
Other items		
Interest expense	(212,244)	(11,537)
Interest income	11,959	19,922
Settlements of accounts payable	167,894	242,000
Loss before income taxes	(2,299,832)	(2,596,672)
Future income tax recovery	-	694,000
Net loss and comprehensive loss	(2,299,832)	(1,902,672)
Deficit, beginning of year	(11,177,315)	(9,274,643)
Deficit, end of year	(13,447,147)	(11,177,315)
Net loss per share (Note 9f)		
Basic	($0.06)	($0.05)
Diluted	($0.06)	($0.05)

See accompanying notes to the consolidated financial statements

GUARDIAN EXPLORATION INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2009 AND 2008

	2009 $	2008 $
Cash and cash equivalents provided by (used in)		
Operating activities		
Net loss for the year	(2,299,832)	(1,902,672)
Items not affecting cash:		
Depletion, depreciation, impairment and accretion	1,876,519	5,719,727
Future income tax recovery	-	(694,000)
Stock-based compensation	75,603	517,794
Income attributable to settlements of accounts payable	(167,894)	-
Foreign exchange loss (gain)	42,422	(92,453)
	(473,182)	3,548,396
Changes in non-cash working capital	(471,720)	(534,285)
	(944,902)	3,014,111
Financing activities		
Debentures issued	-	400,000
Debentures repaid	-	(400,000)
Advances from (repayment to) related party	399,951	(901,918)
Loan from related party	550,000	-
Issuance of share capital, net of costs	-	4,189,973
Issuance of warrants	-	944,840
Advances from (payments to) shareholder	-	(246,092)
	949,951	3,986,803
Investing activities		
Disposition of property and equipment	115,874	-
Expenditures on property and equipment	(281,379)	(5,904,341)
Change in non-cash investing working capital	(268,386)	(475,543)
	(433,891)	(6,379,884)
Change in cash	(428,842)	621,030
Cash, beginning of year	693,056	72,026
Cash, end of year	264,214	693,056
Supplemental cash flow information		
Interest paid	6,890	-
Taxes paid	-	-

See accompanying notes to the consolidated financial statements

1. BASIS OF PREPARATION AND GOING CONCERN

The consolidated financial statements of Guardian Exploration Inc. (the "Company") as at and for the year ended December 31, 2009 are comprised of the Company and its controlled entities. The consolidated financial statements are stated in Canadian dollars and have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP").

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of revenues and expenses, assets and liabilities, and disclosure of contingent assets and liabilities. Key sources of judgment and estimation uncertainty are discussed in Note 3(k).

Going Concern

These consolidated financial statements have been prepared by management in accordance with GAAP on a going concern basis, which contemplates the realization of assets and the settlement of liabilities in the ordinary course of business. Should the Company not realize the value of its current and future projects and successfully raise financing to develop its current and future projects, it may not be able to realize its assets and discharge its liabilities in the normal course of operations.

For the year ended December 31, 2009, the Company reported an after-tax loss of $2.3 million and negative operating cash flows of $0.9 million. As at December 31, 2009, the Company had a working capital deficiency of $1.8 million, an accumulated deficit of $13.5 million, and capital expenditure commitments of approximately $0.6 million. In 2009, continuing volatility in the price of oil and natural gas, and sluggish economic conditions for much of the year created a substantially volatile business environment. These conditions have limited certain of the Company's previously planned business development activities and will continue to provide uncertainty for the Company in the future.

Management's efforts and resources are directed at developing a portfolio of projects and realizing on the value of such projects in the future. Due to numerous risks inherent in these projects, there can be no assurance the Company will be successful. While the Company seeks to mitigate risks by working with joint venture partners and developing a stable production base, the Company's success largely depends on its ability to finance the development of existing projects and finance the acquisition and development of new projects. Financing sources may include proceeds realized from the divestiture of its petroleum and natural gas assets.

The Company's recent operating losses, negative working capital, and uncertainty regarding its ability to obtain financing in a timely manner raises significant doubt as to the Company's ability to continue as a going concern. If the going concern basis is not appropriate, adjustments may be necessary to the carrying amounts and classification of the Company's assets and liabilities. The accompanying consolidated financial statements do not include any adjustments that might result if the Company is unable to continue as a going concern, and such adjustments could be material.

2. NATURE OF OPERATIONS

Guardian Exploration Inc. ("Guardian") was incorporated in Alberta as Guardian Resources Inc. on March 27, 2001. On May 14, 2001, Guardian changed its name to Guardian Exploration Inc. and obtained Extra-provincial Registration in British Columbia on September 22, 2001. On April 21, 2006, Guardian amalgamated with Resilient Resources Ltd. ("Resilient"), a public company listed on the TSX Exchange. The amalgamated company continued under the name Guardian Exploration Inc. (the "Company"). The Company is engaged in the acquisition, exploration, and development of petroleum and natural gas properties in western Canada and the State of Montana.

3. SIGNIFICANT ACCOUNTING POLICIES

a) Principles of consolidation

These consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries, K2 America Corp. and K2 Operating Corp. These subsidiaries were incorporated under the General and Business Corporate Law of the State of Montana on November 16, 1995 and February 12, 1998, respectively. All inter-entity transactions and balances have been eliminated.

b) Property and equipment – Canadian and US Cost Centres

Capitalized costs

The Company follows the full cost method of accounting for its petroleum and natural gas properties. Under this method, all costs related to the acquisition of, exploration for, and development of petroleum and natural gas reserves are capitalized. Costs include lease acquisition costs, geological and geophysical expenses, overhead directly related to exploration and development activities and costs of drilling both productive and non-productive wells.

Proceeds from the sales of properties are applied against capitalized costs, without any gain or loss being realized, unless such sale would alter the rate of depletion and depreciation by 20% or more.

Impairment

The impairment calculation, or "ceiling test", is calculated by comparing the carrying value of property and equipment to the sum of undiscounted cash flows expected to result from the future production of proved reserves and the carrying value of unproved properties, net of any impairments. Estimates of future net revenues are based on expected future commodity prices and costs rather than those existing at the measurement date.

Should the ceiling test result in an excess of carrying value, the Company would then measure the amount of impairment by comparing the carrying value of property and equipment to an amount equal to the estimated discounted net present value of future cash flows from proved plus probable reserves and the carrying value of unproved properties, net of any impairments. Any excess is recorded as a permanent impairment and charged as additional depletion and depreciation.

Undeveloped and unproved properties are assessed periodically to determine whether impairment has occurred.

Depletion

Depletion of petroleum and natural gas properties and depreciation of production equipment is calculated using the unit-of-production method based upon estimated proven petroleum and natural gas reserves, before royalties. In determining its depletion base, the Company includes estimated future costs to be incurred in developing proven reserves and excludes the costs of the unproved properties.

Relative volumes of petroleum and natural gas production and reserves are converted at the energy equivalent conversion rate of six thousand cubic feet of natural gas to one barrel of crude oil.

c) Asset retirement obligations

The fair value of the liability for the Company's asset retirement obligations is recorded in the period it is incurred with a corresponding increase in the carrying value of the related long-lived asset. Fair value is estimated using the present value of the estimated future cash outflows to reclaim and abandon wells and facilities, using the Company's credit-adjusted risk-free interest rate. The liability is subsequently adjusted due to the passage of time and the increase is recorded as an accretion expense. The liability is also

adjusted for revisions in either the timing or the amount of the original estimated cash flows associated with the liability. Actual asset retirement obligations paid are deducted from the liability in the year incurred.

d) Future income taxes

The Company uses the liability method of accounting for income taxes. Temporary differences arising from the difference between the tax basis of an asset or liability and the carrying amount on the balance sheet are used to calculate future income tax assets or liabilities. Future income tax assets or liabilities are calculated using the substantively enacted tax rates anticipated to apply in the period that the temporary differences are expected to reverse. The effect on future tax assets and liabilities of a change in tax rates is recognized in net income in the period in which the change is substantively enacted. To the extent that the Company does not consider it to be more likely than not that a future tax asset will be recovered, it provides a valuation allowance against the excess.

e) Joint ventures

Significantly all of the exploration, development and production activities is conducted jointly with others. These financial statements reflect only the Company's proportionate interest in such activities.

f) Cash and cash equivalents

Cash and cash equivalents include cash on hand, balances with banks and short-term deposits with original maturities of less than three months.

g) Flow-through shares

Resource expenditure deductions funded by flow-through share arrangements are renounced to investors in accordance with income tax legislation. To recognize the foregone tax benefits to the Company, the future income tax liability and the carrying value of the shares issued are adjusted by the effect of the tax benefits renounced to subscribers when the corresponding exploration and development expenditures are renounced.

h) Revenue recognition

Revenue from petroleum and natural gas is recognized based on volumes delivered to customers at contractual delivery points and rates and when collection is reasonably assured. The costs associated with the delivery, including operating, transportation, and production based royalties are recognized in the same period in which the related revenue is earned.

i) Stock-based compensation

The Company follows the fair value method of accounting for stock options granted to directors, officers, employees and consultants. Fair value is determined at the grant date using the Black-Scholes option-pricing model. The value attributed to options is recognized over the vesting period as stock-based compensation expense with a corresponding credit to contributed surplus. The contributed surplus balance is reduced as the options are exercised with the amount initially recorded being credited to share capital.

Warrants to acquire shares are similarly valued at fair value at the grant date using an asset pricing model such as Black-Scholes. Warrants which are issued as part of an equity or debt raising process are accounted for as a reduction in the cost assigned to the equity or debt instrument with a corresponding amount recorded in shareholders' equity.

j) Foreign currency translation

Operations of the Company's subsidiary are considered to be integrated and therefore the financial statements of the subsidiary are included in these consolidated financial statements on the basis that monetary assets and liabilities are translated at the exchange rate in effect at year end, non-monetary assets and liabilities are translated at historical rates and revenues and expenses are translated at the average rate

for the period.

k) Use of estimates and measurement uncertainty

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amount of revenues and expenses during the period. The amounts recorded for depletion of petroleum and natural gas properties and equipment, the provision for asset retirement obligation costs, and the petroleum and natural gas properties and equipment impairment test calculation are based on estimates of gross proven reserves, future production rates, future petroleum and natural gas prices, future costs, and other relevant assumptions. By their nature, these estimates are subject to measurement uncertainty and the effect on the financial statements in future years could be significant.

The Company is subject to various regulatory and statutory requirements relating to the protection of the environment. These requirements, in addition to contractual agreements and management decisions, result in the accrual of estimated asset retirement obligation costs. Any changes in these estimates will affect future earnings.

The financial statements include accruals based on the terms of existing joint venture agreements. Due to varying interpretations of the definition of terms in these agreements, the accruals made by management in this regard may be significantly different from those determined by the Company’s joint venture partners. The effect on the financial statements resulting from such adjustments, if any, will be reflected prospectively.

The Black-Scholes option valuation method was developed for use in estimating the fair value of traded options that were fully tradable with no vesting restrictions. This option valuation model requires the input of highly subjective assumptions including the expected stock price volatility. Because the Company's stock options and warrants have characteristics different from those of traded options and because changes in the subjective input assumptions can materially affect the calculated fair value, such value is subject to measurement uncertainty.

The capital expenditures classification made with respect to the renouncement of flow through shares is based on estimates from geological and geophysical information obtained and the classification of the expenditures may also be challenged by the taxation authorities and in this regard the assessments may be different from that of management. By their nature, these estimates are subject to measurement uncertainty and as such, the effect on the financial statements of changes of estimates in future periods could be significant.

l) Per share information

Per share information is calculated on the basis of the weighted average number of common shares outstanding during the fiscal year. Diluted per share information reflects the potential dilution that could occur if securities or other contracts to issue common shares were exercised or converted to common shares. Diluted per share information is calculated using the treasury stock method that assumes any proceeds received by the Company upon the exercise of in-the-money stock options would be used to buy back common shares at the average market price for the period.

m) Financial instruments

All financial instruments are measured at fair value on initial recognition of the instrument. Measurement in subsequent periods depends on whether the financial instrument has been classified as “held-for-trading,” “available-for-sale,” “held-to-maturity,” “loans and receivables” or “other financial liabilities” as defined by CICA Section 3855: Financial Instruments – Recognition and Measurement.

Cash is designated as “held-for-trading” and is measured at fair value. Gains and losses related to the periodic revaluation are recorded in net income. Accounts receivable, due from related company and refundable deposits, are designated as “loans and receivables” and are initially measured at fair value and subsequently accounted for at amortized cost using the effective interest rate method. Accounts payable and amounts due to a related company are designated as “other financial liabilities” and are initially measured at fair value and subsequently at amortized cost using the effective interest rate method.

n) Changes in Accounting Policies

On January 1, 2009, the Company adopted CICA Handbook Section 3064, “*Goodwill and Intangible Assets”*. The standard replaces CICA sections 3062 and 3450 and provides guidance relating to the recognition, measurement, presentation and disclosure of goodwill and intangible assets. There was no impact on the consolidated financial statements as a result of the adoption of this standard.

On January 20, 2009, the Company adopted Emerging Issues Committee abstract 173 “*Credit Risk and the Fair Value of Financial Assets and Financial Liabilities”*. The abstract requires an entity’s own credit risk and the credit risk of counterparties to be taken into account in determining the fair value of financial assets and financial liabilities. There was no impact on the consolidated financial statements as a result of the adoption of this abstract.

In June 2009, the CICA amended Section 3862 to include additional disclosure requirements about fair value measurement for financial instruments and liquidity risk disclosures. These amendments require a three level hierarchy that reflects the significance of the inputs used in making the fair value measurements. Fair values of assets and liabilities included in Level 1 are determined by reference to quoted prices in active markets for identical assets and liabilities. Assets and liabilities in Level 2 include valuations using inputs other than quoted prices for which all significant outputs are observable, either directly or indirectly. Level 3 valuations are based on inputs that are unobservable and significant to the overall fair value measurement. The adoption of this standard did not have a material impact on the consolidated financial statements. Cash has been classified as Level 1.

Future Changes in Accounting Standards

In January 2009, the CICA issued Section 1582, Business Combinations, which replaces former guidance on business combinations. Section 1582 establishes principles and requirements of the acquisition method for business combinations and related disclosures. This statement applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after January 2011 with earlier application permitted. Management is currently assessing the potential impact of the adoption of this section on the results of operations, financial position and disclosures.

In January 2009, the CICA issued Sections 1601, Consolidated Financial Statements, and 1602, Non-controlling Interests, which replaces existing guidance. Section 1601 establishes standards for the preparation of consolidated financial statements. Section 1602 provides guidance on accounting for a non-controlling interest in a subsidiary in consolidated financial statements subsequent to a business combination. These standards are effective on or after the beginning of the first annual reporting period beginning on or after January 2011 with earlier application permitted. Management is currently assessing the impact of the adoption on the results of operations and financial position.

IFRS Adoption

In February 2008, the AcSB confirmed that all Canadian publicly accountable enterprises will be required to adopt International Financial Reporting Standards (IFRS) for interim and annual reporting purposes for fiscal years beginning on or after January 1, 2011. Management has performed a high-level assessment of the impact of the convergence of Canadian GAAP with IFRS on the results of operations, financial position

and disclosures. The most significant impact relates to the accounting for property, plant and equipment, in particular the impairment assessment process and depletion calculations.

The Company has not yet quantified the impact of transitioning to IFRS.

4. DUE FROM RELATED PARTY

Amounts owed to the Company by a director and a company controlled by that director of the Company are unsecured, bear no interest, and have no fixed terms of repayment.

5. DEPOSIT

As part of the finalization of the Third Amended Agreement with the Blackfeet Nation, the Company has placed a deposit of $376,010 (USD$ 360,000) (2008 - $438,380; USD $360,000) in favor of the Bureau of Indian Affairs-Blackfeet Agency to cover the costs of future site restoration and abandonment liabilities. This deposit is considered to be refundable, subject to application for refund, which may or may not be granted. Accordingly, the deposit is shown as a long-term asset.

6. PROPERTY AND EQUIPMENT

	December 31, 2009 $	December 31, 2008 $
Petroleum and natural gas properties and equipment	16,969,136	16,952,474
Accumulated depletion, depreciation and impairment	(14,305,364)	(12,521,933)
	2,663,772	4,430,541

Canadian and US cost centers

For the years ended December 31, 2009 and 2008, there were no capitalized general and administrative expenses in either the Canadian or US cost center.

Unproven property costs of $348,159 (2008 - $nil) have been excluded from capitalized costs subject to depletion in the Canadian cost center and $nil (2008 - $nil) have been excluded in the US cost center.

At December 31, 2009, the Company performed a ceiling test calculation for both the Canadian and US cost centers using reserve data effective December 31, 2009 (Canadian cost center) to assess the recoverable amount of petroleum and natural gas properties. Assumptions regarding future operating and capital costs were based on historical data and management's estimates. Future oil and natural gas future prices were based on the December 31, 2009 commodity prices forecast of the Company's independent reserve engineers, adjusted for the Company's price and quality differentials, as outlined in the following table:

Price Estimates Used for the Ceiling Test

	Exchange Rate (US$/Cdn$)	BC Natural Gas Stn 2 ($Cdn/Mcf)	Edmonton Ref. Price ($Cdn/Bbl)
2010	0.95	5.62	82.43
2011	0.95	6.09	85.02
2012	0.95	6.57	87.62
2013	0.95	7.08	92.84
2014	0.95	7.60	98.07
>2014	0.95	2%	2%

Based on these assumptions, undiscounted net cash flows from proven reserves exceeded the carrying value of petroleum and natural gas properties in both the Canadian and US cost centers. Therefore, petroleum and natural gas properties are considered recoverable and no impairment was recorded (2008: $2.7 million impairment was recorded, $1.7 million in Canadian cost center and $1.0 million in the US cost center).

7. LOAN FROM RELATED PARTY

In the fourth quarter of 2009, a company controlled by a director of the Company advanced $550,000 to the Company for the purpose of funding the Company's participating interest in two oil and gas development projects. As described in Note 16, the advance was formalized into a secured loan facility in the amount of $1 million subsequent to year end. The loan bears interest at 15% and is due May 31, 2010. The loan is secured by a fixed and floating charge over all present and future personal and real property of the Company. The loan has been approved by the Company's Board of Directors, however TSX Venture Exchange approval is still pending.

8. ASSET RETIREMENT OBLIGATIONS

The Company's asset retirement obligations are based on the Company's net ownership in wells and facilities, management's estimates of costs to abandon and reclaim those wells and facilities, as well as an estimate of the future timing of the costs to be incurred.

The total undiscounted amount of cash flows required to settle the obligations as measured at December 31, 2009 are estimated to be $1,422,000 (December 31, 2008 - $1,830,000). These obligations are expected to be settled at various times until 2017. The credit-adjusted risk free rate at which the estimated cash flows were discounted was 8% during the year ended December 31, 2009 and the estimated inflation rate used to project future costs was 2.5%.

A reconciliation of the Company's asset retirement obligation is provided below:

	Year Ended December 31, 2009 $	**Year ended December 31, 2008 $**
Asset retirement obligation, beginning of year	1,161,783	876,947
Obligations incurred	-	37,020
Acquisitions	-	34,481
Revisions to obligations	(197,547)	136,122
Accretion expense	93,085	77,213
Asset retirement obligation, end of year	1,057,321	1,161,783

9. INCOME TAX

Income tax recorded in the income statement is reconciled to the amount that would be obtained by applying the statutory tax rate to the loss before tax as follows:

	2009 $	2008 $
Loss before income taxes	(2,299,832)	(2,596,672)
Statutory income tax rate	29%	29.5%
Expected income tax recovery	(666,951)	(766,000)
Tax effect of non-deductible amounts related to:		
Stock-based compensation	21,925	152,749
Unrealized foreign exchange losses	12,302	-
Valuation allowance movement	782,000	(80,749)
Prior year/rate adjustments	(149,276)	-
Future income tax recovery	-	(694,000)

The components of the Company's net future income tax asset (liability) are as follows:

(Guardian Exploration only)*	2009 $	2008 $
Petroleum and natural gas properties	715,000	650,000
Share issue costs	332,000	390,000
Asset retirement obligations	160,000	290,000
Non-capital losses	460,000	250,000
Valuation allowance	(1,667,000)	(886,000)
Future income tax asset/(liability)	-	694,000

In February 2009, the Company renounced $2,777,110 of eligible expenditures pursuant to a flow-through share issuance in 2008. As a result, the future income tax asset was decreased by $694,000, with a corresponding reduction in share capital, for the tax effect of this renouncement. A full valuation allowance continues to be taken on the Company's net future income tax asset in Canada and the United States.

* The Company is in the process of completing its income tax filings for its wholly owned subsidiaries K2 America Corp. and K2 Operating Corp. Due to the uncertainty associated with certain tax positions taken by the Company, which remain subject to confirmation from the taxation authorities, a full valuation allowance is being taken. The components of 2009 net future income tax as disclosed above do not include the tax pools related to its wholly owned subsidiaries.

For income tax purposes, the Company's losses carried forward in Canada of $1.8 million can be applied to reduce future years' taxable income and expires between 2026 and 2029.

10. SHAREHOLDERS' EQUITY

a) Authorized

Unlimited number of Class A common voting shares
Unlimited number of Class B non-voting common shares
Unlimited number of Class A voting preferred shares, 7% non-cumulative, redeemable by the Company.

b) Issued and outstanding

Share Capital	**Number of Shares**	**Amount $**
Balance, December 31, 2007	20,079,422	6,903,838
Private placements of common shares for cash (i)(ii)(iv)(v)	18,901,000	4,749,616
Issuances of shares for debt (iii)(vii)	683,955	134,175
Exercise of Agent warrants (vi)	73,500	22,388
Share issue costs	-	(788,652)
Balance, December 31, 2008	39,737,877	11,021,365
Tax effect of flow-through shares	-	(694,000)
Share issue costs	-	22,501
Balance, December 31, 2009	39,737,877	10,349,866

On December 8, 2008, the Corporation announced that it was commencing a Normal Course Issuer Bid (the "Bid") whereby it may purchase for cancellation up to 3,009,322 common shares of the Corporation in the open market, until expiry of the Bid in December 2009. No common shares were repurchased.

Prior year

i) On January 18, 2008, the Company closed a private placement of 5,500,000 units at $0.22 per unit for total gross proceeds of $1,210,000, to an officer and director of the Company. Each unit consists of one common share and one share purchase warrant. Each share purchase warrant is exercisable into one common share at a price of $0.30 for two years from the date of closing. The units issued pursuant to the financing were subject to a four month hold period. In connection with the financing, the Company issued 550,000 agent warrants to the agent, exercisable for a period of two years from the date of closing into common shares of the Company at exercise price of $0.22. To facilitate the offering, pursuant to a share-loan arrangement, an officer and director sold 5,500,000 common shares of the Company from his personal holdings to clients of the agent in exchange for the treasury shares. The total gross proceeds from the issuance have been allocated between share capital and share purchase warrants by estimating the fair value of $0.08 per warrant using the Black Scholes option pricing model under the following assumptions:

Risk-free interest rate	3.1%
Expected life	2 years
Expected volatility	85%
Expected dividend	Nil

The 550,000 agent warrants issued have been valued using the same methodology and $46,530 has been recorded as a share issue cost with an offsetting increase to contributed surplus.

ii) On February 4, 2008, the Company closed a private placement of 3,371,300 units at $0.32 per unit for total gross proceeds of $1,078,816, to an officer and director of the Company. Each unit consists of one common share and one share purchase warrant. Each share purchase warrant is exercisable into one common share at a price of $0.35 for two years from the date of closing. The units issued pursuant to the financing were subject to a four month hold period. In connection with the financing, the company issued 337,130 agent warrants to the agent, exercisable for a period of two years from the date of closing into common shares of the Company at exercise price of $0.32. To facilitate the offering, pursuant to a share-loan arrangement, an officer and director sold 3,371,300 common shares of the Company from his personal holdings to clients of the agent in exchange for the treasury shares. The total gross proceeds from the issuance have been allocated between share capital and share purchase warrants by estimating the fair value of $0.14 per warrant using the Black Scholes option pricing model under the following assumptions:

Risk-free interest rate	3.1%
Expected life	2 years
Expected volatility	85%
Expected dividend	Nil

The 337,130 agent warrants issued have been valued using the same methodology and $47,954 has been recorded as a share issue cost with an offsetting increase to contributed surplus.

iii) On April 29, 2008, the Company issued a total of 407,421 common shares to various creditors of the Company in exchange for their outstanding debts of $224,082. The shares were subject to a four month hold period. The shares have been ascribed a value of $0.28 per share based on the trading price of the shares at the time of the issuance with the share price differential recognized as income attributable to the settlement of accounts payable.

iv) On May 13, 2008, the Company closed the first tranche of a brokered private placement consisting of 600,000 common shares of the Company at a price of $0.30 per common share and 3,185,500 flow-through shares at a price of $0.35 per flow-through share for gross proceeds of $1,294,925. In connection with the financing, the Company issued 378,550 agent warrants to the agents, exercisable for a period of two years from the date of closing into common shares of the Company at exercise price of $0.30. The total gross proceeds from the issuance have been allocated between share capital and share purchase warrants by estimating the fair value of $0.12 per warrant using the Black Scholes option pricing model under the following assumptions:

Risk-free interest rate	3.1%
Expected life	2 years
Expected volatility	68%
Expected dividend	Nil

The 378,550 agent warrants issued have been valued using the same methodology and $44,083 has been recorded as a share issue cost with an offsetting increase to contributed surplus.

v) On June 4, 2008, the Company closed the second and final tranche of a brokered private placement consisting of 1,495,100 common shares of the Company at a price of $0.30 per common share and 4,749,100 flow-through shares at a price of $0.35 per flow-through share for gross proceeds of $2,110,715. In connection with the financing, the Company issued 624,420 agent warrants to the agents, exercisable for a period of two years from the date of closing into common shares of the Company at exercise price of $0.30. The total gross proceeds from the issuance have been allocated between share capital and share purchase warrants by estimating the fair value of $0.12 per warrant using the Black Scholes option pricing model under the following assumptions:

Risk-free interest rate	3.1%
Expected life	2 years

Expected volatility	70%
Expected dividend	Nil

The 624,420 agent warrants issued have been valued using the same methodology and $74,372 has been recorded as a share issue cost with an offsetting increase to contributed surplus.

vi) On July 29, 2008, 73,500 agent warrants were exercised at an exercise price of $0.22 per share. A balance of $6,218 was transferred from contributed surplus to share capital based upon the estimated fair value of the warrants on exercise as outlined in section (i) above.

vii) On October 10, 2008 and November 12, 2008, the Company issued a total of 276,534 common shares to various creditors of the Company in exchange for their outstanding debts of $152,094. The shares were subject to a four month hold period. For accounting purposes, the shares have been ascribed a value of $0.07 per share based on the trading price of the shares at the time of their issuance with the differential in share price recorded as income attributable to the settlement of accounts payable.

c) Warrants

	Number of Warrants	**Amount $**
Balance, December 31, 2007	783,613	673,600
Private placements of warrants for cash (9b(i)(ii)(iv)(v))	10,761,400	944,840
Exercise of warrants (9b(vi))	(73,500)	-
Balance, December 31, 2008	11,471,513	1,618,440
Expiry of debenture warrants	(783,613)	(673,600)
Balance, December 31, 2009	10,687,900	944,840

As at December 31, 2009, the Company had 10,687,900 warrants on hand of which 10,612,804 expire in the first 6 months of 2010, with the remainder expiring in 2011 and 2012. The remaining warrants have a weighted average exercise price of $0.31.

d) Stock options

The Company has a stock option plan under which directors, officers, employees and consultants are eligible to receive stock option grants. The stock options issued shall not exceed 10% of the issued shares of the Company at the time of granting of options. The exercise price and vesting terms of any options granted are fixed by the Board of Directors of the Company at the time of grant. The following table outlines the stock option plan activity:

	Number of Options	**Weighted Average Exercise Price**
Balance, December 31, 2007	1,350,000	$0.54
Granted	1,800,000	$0.29
Forfeited	(200,000)	($0.31)
Balance, December 31, 2008	2,950,000	$0.40
Forfeited	(1,050,000)	($0.27)
Balance, December 31, 2009	1,900,000	$0.44
Exercisable, December 31, 2009	1,900,000	$0.44

	Stock options outstanding			Stock options exercisable	
Exercise Prices	Outstanding Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (Years)	Options Exercisable	Weighted Average Exercise Price
$0.150	800,000	$0.150	2.8	800,000	$0.150
$0.220	200,000	$0.220	3.0	200,000	$0.220
$0.285	400,000	$0.285	0.3	400,000	$0.285
$1.100	500,000	$1.100	1.5	500,000	$1.100
	1,900,000	$0.44	1.6	1,900,000	$0.44

e) Contributed surplus

	2009 $	2008 $
Balance, beginning of year	1,603,505	878,990
Issue/exercise of agent warrants	-	206,621
Expiry of debenture warrants	673,600	-
Stock-based compensation	75,603	517,794
Balance, end of year	2,352,708	1,603,505

f) Loss per share

Basic per share amounts are calculated using the weighted average number of shares outstanding of 39,737,877 for the year ended December 31, 2009 (2008: 34,691,134).

The Company's dilutive instruments have not been included in the computation of loss per share as the effect would be anti-dilutive in 2009 and 2008.

11. COMMITMENTS

a) Flow-through share issuance

Pursuant to a flow-through share issuance completed in 2008, the Company was committed to incur $2,777,110 of qualifying expenditures by December 31, 2009. At December 31, 2009, approximately $2.1 million of the obligation had been fulfilled, with the remainder to be incurred by June 30, 2010.

b) Employment contract

Under the terms of an employment contract with the Chief Executive Officer, the Company is committed to pay severance under certain circumstances equal to 2 years salary plus 15%.

c) Office sub-lease

The Company is committed to sub-lease payments of approximately $2,100 per month through February 2010. A new office lease was signed in March 2010, for a term of 2 years, with monthly lease payments of approximately $3,400.

12. RELATED PARTY TRANSACTIONS

a) At December 31, 2009 an amount of $50,000 was owing to the Company by a company controlled by a director. The balance due from that company was $449,951 at December 31, 2008, and the movement during the year consisted of:

- $445,156 was repaid during the year
- receipt of helicopter services in conjunction with the servicing of natural gas wells in Northern B.C in the amount of $40,190 (2008: $273,329) of which $4,795 was paid via a reduction in the Due from Related Party account. The remaining $35,395 was paid in cash by the Company.
- advance of $100,000 during the third quarter of which $50,000 was repaid in the fourth quarter

b) As described in Note 7, the Company received an advance of $550,000 (subsequently formalized into a loan – refer Note 16) from a Company controlled by a director in the fourth quarter of 2009 to fund capital expenditure.

c) The Company obtained engineering consulting services in the amount of $21,090 for the year ended December 31, 2009 (2008: $190,575) from a company controlled by a Company director, who was appointed in 2008. A balance of $123,888 is included in accounts payable and accrued liabilities at December 31, 2009 (December 31, 2008: $180,729).

d) Legal fees in the amount of $88,948 for the year ended December 31, 2009 (2008: $77,287) have been incurred from a legal firm of which a Company director is a partner. A balance of $50,911 is included in accounts payable and accrued liabilities at December 31, 2009 (December 31, 2008: $4,358).

These transactions are in the normal course of business and are recorded at the exchange amount which is the amount of consideration established and agreed to by the related parties.

13. CONTINGENCIES

a) 2006 Flow-through capital raise – qualifying expenditures

Pursuant to a flow-through share issuance completed in March 2006, the Company was committed to incur $4,000,000 of qualified expenditures by December 31, 2007. By December 31, 2007 the Company had incurred only $2.2 million of qualifying expenditure. The remaining $1.8 million was incurred in 2008.

As the Company did not make the necessary qualifying expenditures by December 31, 2007 as required under the income tax rules, the unexpended flow-through amount (approximately $1.8 million) could be reassessed by the tax authorities and the Company could potentially be liable for investor income taxes and penalty interest thereon of up to $700,000 if an arrangement cannot be made to remedy this contingency.

Notwithstanding this, management is of the opinion that the matter can be resolved through negotiation with the tax authorities, however such reassessment is uncertain. No provision has been made in these consolidated financial statements other than an amount for estimated Part XII.6 interest and penalties.

b) Minerals Management Services

The Minerals Management Service ("MMS"), a bureau of the US Department of the Interior that manages that nation's natural gas and oil resource revenues, alleged during the year that a subsidiary of the Company had been deficient in various administrative filing and payment requirements in the past and that, as a result, civil penalties of approximately $578,000 (US$500,000) were levied against the subsidiary. The subsidiary is disputing these penalties and, along with its legal counsel, has negotiated with MMS, the US Department of Treasury, and their respective counsel/agents.

A provision of $86,900 (US$80,000) has been made for these civil penalties. This provision has been based on a settlement with the US Department of Treasury (US$50,000, which was paid in early 2010), and a settlement made directly with MMS (US$30,000). At present, MMS disputes that a binding settlement agreement ("Settlement Agreement") exists. In the event the Settlement Agreement with MMS is not enforced, the maximum exposure of the subsidiary is US$400,000. However in that scenario, the likely settlement amount would be much less.

The Settlement Agreement with MMS includes a probationary period that requires the subsidiary to remain compliant with its reporting and payment requirements over a 24 month time frame; otherwise the full amount of the penalties, reduced on a declining basis for the period of compliance, will be due immediately to MMS. The subsidiary has been compliant with its reporting requirements since August 2008, and the months of compliance will serve to reduce and eventually eliminate the penalties if the Settlement Agreement is enforced.

c) Litigation

During 2008, the Company was named as a defendant in a lawsuit in which a company that signed a farm-out agreement regarding one of the Company's operated wells in Northern BC (the "Plaintiff") claimed, amongst other things, that it had earned a 100% before pay out ("BPO") working interest in this gas well. Guardian agreed to drill and complete the well; the Plaintiff had agreed to pay 100% of the costs in order to earn a 100% working interest. The Plaintiff paid approximately $1.9 million in advances against the total costs of this well but failed to pay 100% of them. Despite its failure to pay, the Plaintiff claimed that it earned its 100% working interest upon completion of the well and that the remaining amounts due by it, which amounts it contested, could be paid from the well's net production revenues. The Company itself funded the additional $688,000 in costs required to complete this well and allow it to be able to produce. While the Plaintiff took no risk regarding these $688,000 in costs, it claimed that it was entitled to a declaration that it earned and should recover 100% of the net production revenues on the basis that, it alleged, the Company was negligent in exceeding the AFE estimates for drilling and completion of the well. The Plaintiff also claimed, by virtue of its purported payment of $175,000 to a third party, a partial interest in the pipeline constructed by the Company in 2008 in order to allow the Kotcho area wells to begin production.

During 2009 the Company entered into a settlement agreement with the Plaintiff. The settlement agreement provided for mutual release by both parties in exchange for a $40,000 cash payment by the Company to the Plaintiff.

d) Other

The Company is also involved in various other claims arising in the normal course of business. While the outcome of these matters is uncertain and there can be no assurance that such matters will be resolved in the Company's favour, the Company does not currently believe that the outcome of adverse decisions in any proceedings related to these matters or any amount which it may be required to pay would have a material adverse impact on its financial position, results of operations or liquidity.

14. SEGMENTED DISCLOSURES

For the year ended December 31, 2009:

	Canada	United States	December 31, 2009
Petroleum and natural gas revenue	$3,647,774	$743,490	$4,391,264
Interest expense	$205,519	$6,725	$212,244
Depletion, depreciation and accretion	$1,742,336	$134,183	$1,876,519
Loss for the year	$2,216,006	$83,826	$2,299,832
Property and equipment	$2,487,140	$321,632	$2,808,772
Capital expenditures	$281,379	-	$281,379

For the year ended December 31, 2008:

	Canada	United States	December 31, 2008
Petroleum and natural gas revenue	$6,029,065	$1,104,490	$7,135,555
Interest expense	$615	$10,922	$11,537
Depletion, depreciation and accretion	$4,621,059	$1,098,668	$5,719,727
Loss for the year	$1,174,416	$728,256	$1,902,672
Property and equipment	$4,006,138	$424,404	$4,430,542
Capital expenditures	$5,844,341	60,000	$5,904,341

15. FINANCIAL INSTRUMENTS AND CAPITAL MANAGEMENT

a) Fair value of financial assets and liabilities

The Company's carrying value of cash, accounts receivable, accounts payable, and amounts due to/from a related company approximates their fair values due to the immediate or short-term maturity of these instruments. The carrying value of the deposit (Note 5) also does not differ significantly from its fair value.

b) Interest rate risk

At December 31, 2009, the Company is only significantly exposed to interest rate risk in relation to its advance from a related party, which is at a fixed rate of interest. There would be no significant impact on the financial statements at December 31, 2009 if interest rates were higher or lower by one percent.

c) Commodity price risk

The nature of the Company's operations results in an exposure to fluctuations in commodity prices. At December 31, 2009, the Company had no financial derivative or physical delivery contracts in place.

d) Currency risk

Currency risk is the risk to the Company's earnings that arises from fluctuations of foreign exchange rates and the degree of volatility of these rates. The Company is exposed to currency risk on the translation of its U.S. dollar denominated subsidiary. The Company does not use derivative instruments to reduce its exposure to foreign currency risk.

e) Capital Management

The Company's objective when managing capital is to safeguard its ability to continue as a going concern, so that it can continue to provide returns to shareholders and benefits for other stakeholders. The Company defines capital as shareholder equity, working capital and credit facilities when available. The Company manages its capital structure and makes adjustments to it in light of changes in economic conditions and the risk characteristics of the underlying assets. The Company's objective is met by retaining adequate equity to guard against the possibility that cash flows from assets will not be sufficient to meet future cash flow requirements. The Board of Directors does not establish quantitative return on capital criteria for management; but rather promotes year over year sustainable growth in net income and funds flow. There have been no changes to the Company's objectives in managing capital or in management's management of capital since December 31, 2008.

The capital structure of the Company is as follows:

	December 31, 2009 $	December 31, 2008 $
Total shareholders' equity	170,267	3,065,995
Total shareholders' equity as a percentage of total capital	9%	70%
Working capital deficiency	1,812,194	1,335,143
Total working capital deficiency as a percentage of total capital	91%	30%
Total Capital	1,982,461	4,401,138

f) Credit Risk

Credit risk arises when a failure by counterparties to discharge their obligations could reduce the amount of future cash inflows from financial assets on hand at the balance sheet date. The Company is subject to credit risk on its cash and accounts receivable. The Company's cash is held at major financial institutions and as such is subject to only minor credit risk. A majority of the Company's accounts receivable at the balance sheet date arise from crude oil, natural gas liquids and natural gas sales. Industry standard dictates that commodity sales are settled on the 25th day of the month following the month of production. The Company does not have any significant credit risk exposure to any single counterparty regarding is accounts receivable other than to the operator of its Girouxville area wells. As at December 31, 2009, the receivable from this company represented approximately 73% of the Company's total accounts receivable balance. This balance was collected subsequent to year-end. Accounts receivable greater than 90 days at December 31, 2009 was $5,000, for which an allowance has been recorded.

The Company assesses quarterly if there has been any impairment of the financial assets of the Company.

The carrying value of cash and accounts receivable approximates their fair value due to the relatively short periods to maturity on this instrument. The maximum exposure to credit risk is represented by the carrying amount on the balance sheet. There are no material financial assets that the Company considers past due.

g) Liquidity Risk

Liquidity risk includes the risk that, as a result of the Company's operational liquidity requirements:

- The Company will not have sufficient funds to settle a transaction on the due date;
- The Company will be forced to sell financial assets at a value less than what they are worth; or
- The Company may be unable to settle or recover a financial asset at all.

The Company's operating cash requirements, including amounts projected to complete the Company's existing capital expenditure program, are continuously monitored and adjusted as input variables change. These variables include but are not limited to oil and natural gas production from existing wells, results from new wells drilled, commodity prices, cost overruns on capital projects and regulations relating to prices, taxes, royalties, land tenure, allowable production and availability of markets. As these variables change, liquidity risks may necessitate the Company to conduct equity issues, obtain project debt financing, enter into joint venture arrangements or conduct asset divestitures. There is no assurance that adequate funds will be available to the Company in a timely manner (refer Note 1 Going Concern). The loan from a related party is due May 31, 2009 (as disclosed below).

16. SUBSEQUENT EVENTS

a) Exercise of option agreement – Castle Rock

In February 2010, Castle Rock Petroleum Ltd ("Castle Rock"), a wholly owned subsidiary of Arrow Energy Ltd, exercised its option under a Farm-Out and Participation Agreement with the Company to re-purchase a 6% earned interest in certain oil and gas properties in the Pembina region of Alberta. Cash proceeds of $265,000 were received by the Company, reflecting a $15,000 premium on its initial investment in November 2009.

b) Loan Agreement – Related Party

Subsequent to year end, the Company agreed to a secured loan facility from a related party in the amount of $1 million. The loan bears interest at 15% and is due May 31, 2010. The loan is secured by a fixed and floating charge over all present and future personal and real property of the Company. The loan has been approved by the Company's Board of Directors, however TSX Venture Exchange approval is still pending.

c) Warrant and Option Expiry

Subsequent to year end, 9,684,930 warrants expired unexercised. 8,871,300 of these warrants were held by a director. Also subsequent to year end, 600,000 options expired, of which 200,000 were held by a former director who resigned in October 2009.

GUARDIAN EXPLORATION INC.

Management's Discussion & Analysis

For the Year

Ended December 31, 2009

MANAGEMENT'S DISCUSSION AND ANALYSIS

The following management discussion and analysis ("MD&A") of financial conditions and results of operations is as of April 30, 2010 and should be read in conjunction with the audited consolidated financial statements of Guardian Exploration Inc. ("Guardian" or the "Company") for the year ended December 31, 2009. Additional information relating to the Company can be found on the SEDAR website at www.sedar.com.

Discussion with regard to Guardian's current financial position and outlook for 2010 is based on currently available information. The financial data presented below has been prepared in accordance with Canadian generally accepted accounting principles (GAAP). The reporting and operating currency is the Canadian dollar. The information in this MD&A was approved by the Company's Board of Directors on April 30, 2010.

This MD&A contains the terms "funds flow from operations", "funds flow per share" and "operating netback" which do not have standardized meanings prescribed by Canadian GAAP and therefore may not be comparable to performance measures presented by others. Funds flow from operations, as used by the Company, is comprised of cash flow from operating activities before changes in non-cash operating working capital. Operating netback represents revenue less royalties, operating expenses and transportations expenses. These non-GAAP measures may not be comparable to the calculation of similar measures for other entities. The Company believes that operating netback and funds flow from (used by) operations represent indicators of the Company's performance and a key measure of the Company's ability to generate the necessary cash to fund future capital expenditures. Funds from (used by) operations and operating netback as presented is not intended to represent operating cash flow or operating profits for the period nor should they be viewed as an alternative to cash flow from operating activities, net earnings (loss) or other measures of financial performance calculated in accordance with Canadian GAAP. See "Funds Flow from Operations" and "Netbacks".

The term barrels of oil equivalent ("boe") may be misleading, particularly if used in isolation. A boe conversion ratio of 6 thousand cubic feet (mcf) equals 1 barrel (bbl) is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead. All boe conversions in this report are derived by converting gas to oil in the ratio of six thousand cubic feet of gas to one barrel of oil.

SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

Certain information regarding the Company set forth in this report includes forward looking statements. All statements other than statements of historical facts contained in this MD&A, including statements regarding our future financial position, business strategy and plans and objectives of management for future operations, are forward-looking statements. The words "believe," "may," "will," "estimate," "continue," "anticipate," "intend," "should," "plan," "expect" and similar expressions, as they relate to us, are intended to identify forward-looking statements. We have based these forward-looking statements largely on our current expectations and projections about future events and financial trends that we believe may affect our financial condition, results of operations, business strategy and financial needs. These forward-looking statements are subject to a number of risks, uncertainties and assumptions described elsewhere in this report.

Other sections of this report may include additional factors, which could adversely affect our business and financial performance. Moreover, we operate in a very competitive and rapidly changing environment. New risk factors emerge from time to time and it is not possible for our management to predict all risk factors, nor can we assess the impact of all factors on our business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statements.

Readers are cautioned not to place undue reliance on forward-looking statements, as there can be no assurance that the plans, intentions or expectations upon which they are based will occur. By their nature, forward-looking statements involve numerous assumptions, known and unknown risks and uncertainties, both general and specific, that contribute to the possibility that the predictions, forecasts, projections and other forward-looking statements will not occur, which may cause the Company's actual performance and financial results in future periods to differ materially from any estimates or projections of future performance or results expressed or implied by such forward-looking statements.

We undertake no obligation to update publicly or revise any forward-looking statements. The forward-looking statements in this report are expressly qualified by this cautionary statement.

CORPORATE OVERVIEW

Guardian Exploration Inc. ("Guardian") was incorporated in Alberta as Guardian Resources Inc. on March 27, 2001. On May 14, 2001, Guardian changed its name to Guardian Exploration Inc. and obtained Extra-provincial Registration in British Columbia on September 22, 2001. On April 21, 2006, Guardian amalgamated with Resilient Resources Ltd. ("Resilient"), a public company listed on the TSX Exchange. The amalgamated company continued under the name Guardian Exploration Inc. (the "Company"). The Company is engaged in the acquisition, exploration, and development of petroleum and natural gas properties in western Canada and the State of Montana. The Company's shares trade on the TSX Venture Exchange under the symbol "GX".

CORPORATE UPDATE

The fourth quarter of 2009 saw a continuation of the conditions prevailing during the first nine months of the year, including declining oil production from the Company's three main producing wells at Girouxville, offset somewhat by improved oil prices. The Company's natural gas wells in north-eastern British Columbia have been shut-in since February 2009 due to depressed gas prices. The Company recorded a loss for the fourth quarter of $844,946 on revenue of $923,042 and average daily oil production of 133 barrels. For the year ended December 31, 2009 the Company recorded a loss of $2,299,832 on revenue of $4,391,264 and average daily production of 198 boe.

As at December 31, 2009 the Company had a working capital deficiency of 1.8 million and capital expenditure commitments of approximately $0.6 million in relation to flow-through funds raised in 2008.

In order to meet its capital commitments, and more generally to fund future exploration and development activities and corporate administrative costs, the Company requires financing. In April 2009, the Board of Directors approved a decision by management to engage an agent to commence the sale of substantially all of the Company's property and equipment. In September 2009, the Company signed a Letter of Intent with Luxor Oil & Gas Inc. ("Luxor"), an Alberta based private oil and gas company, to amalgamate the two companies. The proposed amalgamation was terminated in November 2009. The Company is continuing to seek and evaluate other offers for the assets of the Company.

During the fourth quarter of 2009, the Company entered into two farm-in agreements to address its capital expenditure commitments related to flow-through funds raised in 2008:

- In October 2009, the Company signed a Farm-Out and Participation Agreement with Castle Rock Petroleum Ltd ("Castle Rock"), a wholly owned subsidiary of Arrow Energy Ltd, whereby in return for a drilling commitment on a particular well ("test well"), the Company could earn a 6% interest in certain property interests held by Castle Rock in the Pembina region of Alberta. The commitment represented 10% of the estimated cost to drill and case the test well, and the Company's share was estimated at $250,000. In November 2009, the Company paid a cash call in the amount of $250,040 to Castle Rock.

  As part of the agreement, the Company provided an option to Castle Rock to re-purchase the 6% earned interest for an amount equivalent to the costs incurred by the Company, plus $15,000. The option was exercised by Castle Rock in February 2010, and the Company received a payment of $265,000.

- In December 2009, the Company signed an agreement with Procyon Energy Corporation to drill and complete a natural gas well in the Peace River Arch area of north-eastern British Columbia. Under the farm-in arrangement, Guardian paid 50% to earn a 50% interest in one section of land, subject to a 12.5% gross overriding royalty, and the right to acquire more land on the project. The Company paid a cash call in the amount of $300,000 in December, and another $140,000 subsequent to year end.

  Testing of the well indicates a final gas rate of 14.9 E3M3/d or 526 mcf/d, with 0.003% H_2S. Stabilized long term rates of 278 mcf/d are expected, similar to offset wells in the area.

The payment of both cash calls described above was funded by an advance from a company controlled by a director. As described in Note 7 to the 2009 consolidated financial statements, the advance was formalized into a $1 million loan facility subsequent to year end. The facility bears interest at 15% and is due May 31, 2010. The facility has been approved by the Company's Board of Directors, however is subject to TSX Venture Exchange approval, which has not yet been received.

In order to repay the facility, the Company is presently seeking debt and/or equity alternatives. If Guardian is unable to obtain such alternative financing on a timely basis, it will seek an extension of the maturity date from the lender. Failing the aforementioned options, the Company will seek to sell certain non-core assets with the proceeds to be used to repay the lender.

Subsequent to year end, Mr Dennis Jonk resigned from the Board of Directors. He was replaced by Mr Carter Kowal in April 2010. Mr Kowal is President of Kowal Construction Alta Ltd, a heavy equipment contractor that services various industries including oil and gas (oilfield construction).

SELECTED INFORMATION

	Three Months Ended December 31		**Year Ended December 31**	
	2009	**2008**	**2009**	**2008**
	$	**$**	**$**	**$**
Petroleum and natural gas revenue, before royalties	923,042	2,154,552	4,391,264	7,133,555
Funds flow from (used in) operations	(559,708)	413,981	(473,182)	3,548,396
Funds flow from (used in) operations per share - basic	($0.01)	$0.01	($0.01)	$0.10
Funds flow from (used in) operations per share - diluted	($0.01)	$0.01	($0.01)	$0.10
Net income (loss)	(844,946)	(4,208,236)	(2,299,832)	(1,902,672)
Net income (loss) per share - basic	($0.02)	($0.00)	(0.06)	($0.05)
Net income (loss) per share - diluted	($0.02)	($0.00)	(0.06)	($0.05)
Capital expenditures (proceeds on disposition and settlement gains)	251,349	(506,622)	281,379	5,904,341

Production (boe/day)	133	460	198	250

	December 31 2009	**December 31 2008**
Working capital deficiency	$1,812,194	$1,335,143
Total assets	$3,973,897	$7,160,816

RESULTS OF OPERATIONS

PRODUCTION

	Three Months Ended December 31		**Year Ended December 31**	
	2009	**2008**	**2009**	**2008**
Production (boe/day)				
Crude oil	133	190	190	151
Natural gas	0	270	8	593
Oil equivalent production	133	460	198	250

The increase in crude oil production for the year ended December 31, 2009 in comparison to the 2008 is attributed primarily to three wells in the Girouxville area that were completed and placed on production throughout various periods in 2008 under the farm-in agreement with Breaker. The three wells produced an average of 155 boe/day during the year ended December 31, 2009 as compared with 119 boe/day over 2008.

Declining production from these wells (in particular the 7-03 well due to increased water levels) by the fourth quarter of 2009 is evident in comparison to the fourth quarter of 2008.

Production from the Company's subsidiary in Montana in 2009 remained consistent with 2008, at approximately 35 boe/day.

Guardian's gas production was shut-in in February 2009 due to uneconomic conditions from increasing amounts of water and decreasing amounts of gas being produced. The Company's independent reserve engineers have attributed reserves to only one of the Company's natural gas wells as at December 31, 2009.

PRICING

Benchmark Prices

	Three Months Ended December 31		Year Ended December 31	
	2009	**2008**	**2009**	**2008**
Crude oil – WTI (US$ per Bbl)	$76.07	$58.37	$61.69	$99.57
Crude oil – Edmonton Par Price ($ per Bbl)	$77.01	$64.18	$66.59	$103.26
Natural gas – AECO Spot ($/mcf)	$4.36	$6.55	$4.19	$8.16
Exchange rate ($US/$Cdn)	1.06	1.21	1.14	1.07

West Texas Intermediate at Cushing, Oklahoma ("WTI") is the benchmark reference price for North American crude oil prices. Canadian crude oil prices are based upon the average of several postings, primarily at Edmonton Alberta, and represents the WTI price adjusted for quality and transportation differentials, the US/CDN dollar exchange rate and local demand and supply influences.

For the three months and year ended December 31, 2009, WTI crude oil prices averaged US$76.07 and $61.69 per barrel and $77.01 and $66.59 respectively per barrel at Edmonton. The recovery in oil prices over the summer months is evident in these figures, although prices overall in 2009 are still well below the very high prices experienced in 2008.

United States natural gas prices are commonly referenced to the New York Mercantile Exchange at Henry Hub in Louisiana ("NYMEX") while Canadian natural gas prices are typically referenced to the AECO Hub in Alberta. Natural gas prices are influenced more by North American supply and demand than global fundamentals. Natural gas prices averaged $4.36/Mcf and $4.19Mcf respectively for the three months and year ended December 31, 2009, reflecting the recessionary conditions and excess supply in the gas market. Natural gas prices are expected to remain at low levels for the duration of 2010.

Realized Prices

	Three Months Ended December 31		Year Ended December 31	
	2009	**2008**	**2009**	**2008**
Average Prices				
Crude oil ($/bbl)	$75.17	$60.38	$62.28	$98.96
Natural gas ($/mcf)	-	$7.36	$4.08	$7.57
Oil equivalent ($/boe)	$75.17	$50.87	$60.78	$77.82

Guardian's averaged realized price for its crude oil was $75.17 and $62.28 per barrel for the three months and year ended December 31, 2009, reflecting the Edmonton benchmark prices described above. Realized prices for the 2009 year are well below 2008, again reflecting the lower price environment in 2009.

For the year ended December 31, 2009 the Company's average realized price for its natural gas was $4.08/mcf compared to $7.57/mcf in the prior year. The year ended December 31, 2009 represented only two months of production because the Kotcho field was shut-in due to uneconomic conditions as noted previously.

REVENUE

	Three Months Ended December 31		Year Ended December 31	
	2009	**2008**	**2009**	**2008**
Production Revenue				
Crude oil	$923,042	$1,056,583	$4,320,962	$5,489,739
Natural gas	-	$1,097,939	$70,302	$1,643,816
Total production revenue	$923,042	$2,154,522	$4,391,264	$7,133,555

The year-to-date decrease in crude oil revenue is largely due to the lower commodity prices in 2009 compared to 2008, which offset higher average production (190bbl/day vs 151bbl/day in 2008). Revenue for the fourth quarter as compared to 2008 reflects primarily lower production, as realized prices were higher as noted above.

The decrease in natural gas revenue is attributable to decreased production following the Company's Kotcho property being shut-in during the first quarter of 2009, as noted previously.

The Company currently has no financial derivatives or physical delivery contracts in place. All production volumes are currently sold into the spot market.

ROYALTIES

	Three Months Ended December 31		Year Ended December 31	
	2009	**2008**	**2009**	**2008**
Royalties	$330,165	$613,345	$1,487,625	$837,317
As a percentage of revenue	36%	28%	34%	12%

The increase in royalties as a percentage of revenue for the three months and year ended December 31, 2009 from the comparative periods in 2008 is due primarily to the fact that the Company's three wells at Girouxville no longer qualify for the one year, $1 million Alberta royalty holiday, which ceased in late 2008 for two of the wells and January 2009 for the other. The Company expects that the royalties as a percentage of sales will remain at or around present levels, barring any significant changes in well productivity levels and/or commodity prices.

The Company's royalties as a percentage of sales on its Cutbank, Montana production remained consistent with 2008 levels.

OPERATING EXPENSES

	Three Months Ended December 31		Year Ended December 31	
	2009	**2008**	**2009**	**2008**
Operating expenses	$331,787	$986,875	$1,536,360	$1,809,047

Operating expenses per boe	$27.02	$23.30	$21.26	$19.74
As a percentage of revenue	36%	46%	35%	25%

Operating costs on a per boe basis were slightly higher in 2009 as compared to 2008, although as a percentage of revenue were lower in 2008 due to the higher commodity prices.

In the fourth quarter of 2009, the impact of fixed operating costs on lower volumes contributed to the higher per boe cost. On a percent of revenue basis, operating costs were very high in the fourth quarter of 2008 due to the low price environment at that time.

GENERAL AND ADMINISTRATIVE EXPENSES

	Three Months Ended December 31		Year Ended December 31	
	2009	**2008**	**2009**	**2008**
General and administrative expenses	$361,633	$530,111	$1,648,174	$1,461,879
As a percentage of revenue	39%	25%	38%	21%

The increase in overall G&A expenses during 2009 is due primarily to the significant consulting and professional fees incurred in relation to the legal and regulatory matters involved in the potential sale of substantially all of the Company's petroleum and natural gas assets. As a percentage of revenue, G&A expenses were also impacted negatively due to the lower commodity prices experienced in 2009 compared to the same periods of 2008.

STOCK-BASED COMPENSATION

	Three Months Ended December 31		Year Ended December 31	
	2009	**2008**	**2009**	**2008**
Stock-based compensation expense (recovery)	$ -	$193,701	$75,603	$517,794

Stock-based compensation expense is the amortization over the vesting period of the fair value of stock options granted to employees, directors, and key consultants of the Company. The fair value of the stock options granted is estimated at the grant date using the Black Scholes option pricing model.

Stock-based compensation for the three months ended December 31, 2009 was $nil as all options were fully vested prior to the start of the quarter. The year-to-date expense of $75,603 is down significantly from 2008, as the majority of options had vested by the start of the year.

INTEREST EXPENSE

	Three Months Ended December 31		Year Ended December 31	
	2009	**2008**	**2009**	**2008**
Interest expense/(recovery)	$467,195	($13,660)	$212,244	$11,537

Interest expense for the three months ended December 31, 2009 includes a year-end increase to the Part XII.6 tax accrual of $0.4 million. $0.3 million of this was the reversal of a first quarter entry to reduce the accrual. Interest expense is therefore better evaluated on a year-to-date basis; the 2009 expense relates primarily to Part XII.6 tax on flow through funds raised in 2008, as well as an adjustment to 2006 Part XII.6 tax of approximately $70,000.

DEPLETION, DEPRECIATION AND ACCRETION

	Three Months Ended December 31		Year Ended December 31	
	2009	**2008**	**2009**	**2008**
Depletion and depreciation	$239,082	$1,553,346	$1,783,432	$2,902,515
Accretion	$22,671	$21,757	$93,087	$77,212
Impairment	-	$2,740,000	-	$2,740,000
Total DD&A	$261,753	$4,315,103	$1,876,519	$5,719,727
Depletion and depreciation per boe	$19.47	$36.67	$24.68	$31.67

Depletion of the Company's oil and gas assets is calculated on a unit of production basis, using estimated proven reserves. The significant decrease in depletion and depreciation expense for the three months and year ended December 31, 2009 as compared to the same period in 2008 primarily reflects production levels. On a per boe basis, year-to-date DD&A is lower than in 2008, reflecting the impact of write-downs of property, plant and equipment recorded at the end of 2008. At December 31, 2008 a $2.7 million write-down ($1.7 million Canadian cost center, $1 million US cost center) was recorded under the ceiling test.

Accretion of the asset retirement obligation contributed approximately $23,000 and $93,000 to DD&A expense for the respective three months and year ended December 31, 2009. This cost reflects the unwinding of the discounted cash flows which form the basis for the asset retirement obligation.

The provision for asset retirement obligations are determined by management in consultation with the Company's independent engineers and are based on prevailing regulations, costs, technology and industry standards. The Company estimates that the present value of its asset retirement obligations at December 31, 2009 is $1,057,000 Current expenditures for actual abandonment and site restoration in the three months and year ended December 31, 2009 were $nil.

TAXES

During the three months and year ended December 31, 2009, the Company recorded no current or future income tax expense or recovery, as the benefit of losses incurred is not considered probable of realization. In 2008, a future tax recovery of $694,000 was recorded, as a result of the use of unrecognized tax pools to offset the $694,000 future tax liability related to flow-through shares issued in 2008. The $694,000 future tax liability was recorded in 2009 (when the tax deduction was renounced to subscribers) drawing down the future tax asset recorded at December 31, 2008 to $nil.

As of December 31, 2009, the Company has approximately $5.0 million in resource tax pools available to offset future taxable income, and estimated carried forward non-capital losses of $1.8 million. Further, there are approximately US$36 million of resource and tax loss pools related to the Company's US subsidiary (none of which have been recognized for accounting purposes as not considered recoverable at this time).

NET INCOME (LOSS) AND COMPREHENSIVE INCOME (LOSS)

	Three Months Ended December 31		Year Ended December 31	
	2009	**2008**	**2009**	**2008**
Net income (loss)	($844,946)	($4,208,236)	($2,299,832)	$1,902,672
Net income (loss) - per basic share	($0.02)	($0.11)	($0.06)	($0.05)
Net income (loss) - per diluted share	($0.02)	($0.11)	($0.06)	($0.05)
Weighted average shares outstanding:				
Basic	39,737,877	39,644,497	39,737,877	34,691,134
Diluted	39,737,877	39,644,497	39,737,877	34,691,134

For all periods in 2009 and 2008, all outstanding stock options and warrants are anti-dilutive and have been excluded in calculating the diluted weighted average shares outstanding.

FUNDS FLOW FROM OPERATIONS

It is management's view that funds flow from operations is a useful measure of performance and a good benchmark when comparing results from period to period. Funds flow from operations is a non-GAAP measure, reconciled with net income (loss) in the table below:

	Three Months Ended December 31		Year Ended December 31	
	2009	**2008**	**2009**	**2008**
Net income (loss)	($844,946)	($4,208,236)	($2,299,832)	($1,902,672)
Add back (subtract) items not affecting cash:				
Depletion, depreciation, impairment and accretion	$261,753	$4,315,103	$1,876,519	$5,719,727
Future income tax expense (recovery)	-	$139,000	-	($694,000)
Stock-based compensation	-	$193,701	$75,603	$517,794)
Gain attributable to settlement of accounts payable	-	-	($167,894)	-
Foreign exchange loss (gain)	$23,485	($25,586)	$42,422	($92,453)
Funds flow from (used in) operations	($559,708)	$413,981	($473,182)	$3,458,396
Funds flow per share - basic	($0.01)	$0.01	($0.01)	$0.10
Funds flow per share - diluted	($0.01)	$0.01	($0.01)	$0.10

Funds from operations were much higher in 2008, as a result of greater revenue from higher realized prices for oil and natural gas. As well, royalty charges and general and administrative costs have been comparatively higher in 2009.

SHARE CAPITAL

	Year Ended December 31	
	2009	**2008**
Outstanding common shares		
Basic	39,737,877	39,737,877
Diluted	52,325,777	54,359,390

Due to the anti-dilutive effect of Guardian's net loss for the three months and year ended December 31, 2009, the diluted number of shares is considered equivalent to the basic number of shares for the purposes of all per share calculations.

Detail of Outstanding Securities	Outstanding at December 31	
	2009	**2008**
Common shares	39,737,877	39,737,877
Stock options	1,900,000	2,950,000
Warrants	8,871,300	8,871,300
Agent warrants	1,816,600	1,816,600
Debenture warrants	-	783,613

As of the date of this MD&A, there were 39,737,877 common shares, 1,002,970 warrants, and 1,300,000 options outstanding. The reduction since December 31, 2009 is due to the expiry of 9,684,930 warrants, of which 8,871, 300 were held by a director, and the expiry of 200,000 options held by a former director.

On December 8, 2008, the Corporation announced that it was commencing a Normal Course Issuer Bid (the "Bid") whereby it may purchase for cancellation up to 3,009,322 common shares of the Corporation in the open market, until expiry of the Bid in December 2009. No common shares were repurchased.

CAPITAL EXPENDITURES

	Year Ended December 31	
	2009	**2008**
Canada	$281,379	$5,844,341
United States	-	$60,000
Total	$281,379	$5,904,341

The majority of capital expenditure incurred in 2009 related to the Castle Rock and Procyon farm-in arrangements described in the Corporate Update section of this report.

In 2008, the Company drilled, completed and equipped three (1.6 net) successful oil wells in the Girouxville area of Alberta (via a farm-in agreement with Breaker Energy Inc. signed in late 2007) and expanded it existing assets in the Kotcho Lake area in northern B.C.

LIQUIDITY AND CAPITAL RESOURCES

At December 31, 2009, the Company had no debt facilities, a working capital deficit of $1.8 million, and capital expenditure commitments of approximately $0.6 million. The future operations of the Company are dependent on the Company's ability to raise capital through debt, equity or through the sale of certain of its assets to support its activities and meet its obligations, as outlined in Note 1 to the consolidated financial statements. Subsequent to year end, the Company entered into a $1 million loan facility with a related party, of which approximately $0.55 million has been drawn as of the date of this report. The facility is due May 31, 2010.

In order to repay the facility, the Company is presently seeking debt and/or equity alternatives. If Guardian is unable to obtain such alternative financing on a timely basis, it will seek an extension of the maturity date from the lender. Failing the aforementioned options, the Company will seek to sell certain non-core assets with the proceeds to be used to repay the lender.

The capital intensive nature of the Company's activities may create a negative working capital position during times of high levels of capital investment. The industry has a pre-arranged monthly clearing day for payment of revenues from all buyers of crude oil and natural gas. This occurs for all the Company's Canadian operations on the 25th day following the month of sale. As a result, the Company's production revenues are collected in an orderly fashion. To the extent that the Company has joint venture partners in its activities it will attempt to collect on a monthly basis the partner's share of capital and operating expenses. These are subject to collection risk. The Company has experienced a significant amount of uncollectible accounts receivable in the past, although with the exception of $5,000 of receivables on which an impairment provision has been recorded, no receivables at December 31, 2009 are past due.

The Company's cash flow and earnings are highly sensitive to changes in commodity prices, exchange rates and other factors that are beyond the control of the Company.

SUMMARIZED QUARTERLY INFORMATION

SELECTED QUARTERLY HIGHLIGHTS (unaudited)	2009				2008			
	Q4 2009	Q3 2009	Q2 2009	Q1 2009	Q4 2008	Q3 2008	Q2 2008	Q1 2008
($000's)								
P&NG net revenue	923	598	883	830	1,542	2,170	2,033	621
Production expense	332	312	375	518	987	347	283	192
DDA/impairment	262	319	467	828	4,315	468	777	159
G&A	362	334	512	440	530	350	350	232
Financing fees/interest	467	31	1	(287)	(13)	6	19	-
Income tax expense (recovery)	-	-	-		133	-	(833)	-
Net Income (loss) for the period	(845)	(175)	(503)	(777)	(4,209)	947	1,066	292
Net Income (loss) per share	(0.02)	(0.00)	(0.01)	(0.02)	(0.12)	0.02	0.04	0.01
Working Capital/(Deficiency)	(1,812)	(958)	(1,012)	(1,299)	(1,335)	(825)	(2,610)	(5,327)

The impact of higher oil and natural gas prices is evident during the first three quarters of 2008, the only recent quarters where the Company has recorded an after-tax profit. The impairment charge of $2.7 million recorded at December 31, 2008 also stands out.

The Company's working capital position has fluctuated over the past eight quarters, dependent primarily on the timing of equity raisings and extent of exploration and development activities.

CRITICAL ACCOUNTING ESTIMATES

Oil and Gas Reserve Estimates

Estimates of economically recoverable oil and natural gas reserves (including natural gas liquids) and the future net cash flows there from are based upon a number of variable factors and assumptions, such as commodity prices, projected production from the properties, the assumed effects of regulation by government agencies and future operating costs. All of these estimates may vary from actual results. Estimates of the recoverable oil and natural gas reserves attributable to any particular group of properties, classifications of such reserves based on risk recovery and estimates of future net revenues expected there from may vary. The Company's actual production, revenues, taxes, development and operating expenditures with respect to its reserves may vary from such estimates, and such variances could be material.

Ceiling Test

The ceiling test calculation is used to assess the valuation of the Company's petroleum and natural gas properties. The first part measures whether impairment has occurred based on undiscounted future cash flows using estimated future prices, costs and proved reserves. When the first part indicates impairment exists, the second part of the test measures the amount of impairment based on discounted estimated future cash flows from proved and probable reserves. The Company reviews the related estimates when it performs its ceiling test on a quarterly basis. The impact of changes in the estimates of future prices and costs applied and the quantity of proved and probable reserves on the financial statements could be material.

Unproven Properties

Costs related to unproven properties are excluded from costs subject to depletion until proved reserves have been determined or their value is impaired. These properties are reviewed quarterly, based on management's estimates of future prospects and any impairment is transferred to the costs being depleted.

Stock-Based Compensation

The Company has a stock-based compensation plan which reserves shares of common stock for issuance to key employees, consultants and directors. The Company accounts for grants issued under this plan using the fair value recognition provisions whereby the cost of options granted to employees is charged to income with a corresponding

increase in contributed surplus, based on an estimate of the fair value determined using the Black-Scholes option pricing model and amortized over the vesting period of the options issued.

Asset Retirement Obligations

The Company records the fair value of an asset retirement obligation as a liability in the period in which it incurs a legal obligation associated with the asset, normally when the asset is purchased or developed. The associated asset retirement costs are capitalized as part of the carrying amount of the long lived asset and depleted and depreciated using a unit-of-production method over the life of the estimated proved reserves. Subsequent to the initial measurement of the asset retirement obligations, the obligations are adjusted at the end of each period to reflect the passage of time and changes in the estimated future cash flows underlying the obligation.

Inherent in the fair value calculation of ARO are numerous assumptions and judgments including the ultimate settlement amounts, inflation factors, credit adjusted discount rates, timing of settlement, and changes in the legal, regulatory, environmental and political environments. To the extent future revisions to these assumptions impact the fair value of the existing ARO liability, a corresponding adjustment is made to the petroleum and natural gas properties balance.

BUSINESS RISKS

Exploration, development and production of petroleum and natural gas involves many risks that even the combination of experience and diligent evaluation may not be sufficient to overcome. Utilizing highly skilled professionals, focusing in areas where the Company has existing knowledge and expertise or access to such expertise, using the most up to date technology, and controlling costs to maximize margins, mitigate these risks. The Company maintains a comprehensive insurance program that insures liability and property consistent with good industry practices. The program is designed to mitigate risks and protect against significant loss. However, the Company is not fully insured against all these risks, nor are all such risks insurable.

The reserve and recovery information contained in the Company's independent reserve evaluation is only an estimate. The actual production and ultimate recovery of reserves from the properties may be greater or less than the estimates prepared by the independent reserve engineers. The reserve report was prepared using forecasted commodity prices as determined by independent engineers. If lower prices for crude oil, natural gas liquids and natural gas are realized by the Company, the present value of the estimated future cash flows for the reserves would be reduced and such reductions could be significant.

Financial risks include exposure to fluctuation in commodity prices, currency exchange rates and interest rates. To mitigate the risks, the Company may enter into physical contracts for the sale of crude oil, natural gas liquids and natural gas at fixed prices. The Company may also institute financial hedging techniques for interest rates, currency exchange rates and commodity prices. If utilized, such transactions would be subject to certain limits on term and amount as established by the Board of Directors. No such transactions have been entered into to date.

Oil and Gas Risk

Inherent in development of oil and gas reserves are risks, among others, of drilling dry holes, encountering production or drilling difficulties or experiencing high decline rates in producing wells. In addition, a major market risk exposure is in the pricing applicable to our oil and gas production. Realized pricing is primarily driven by the prevailing worldwide price for crude oil and spot prices applicable to our oil and natural gas production. Prices received for oil and gas production have been and remain volatile and unpredictable. If oil and gas prices decline significantly, even if only for a short period of time, it is possible that non-cash write-downs of our oil and gas properties could occur under the full-cost accounting method. Under these rules, we review the carrying value of our proved oil and gas properties each quarter to ensure that capitalized costs of proved oil and gas properties, net of accumulated depreciation, depletion and amortization do not exceed the "ceiling." This ceiling is the present value of estimated future net cash flows from proved oil and gas reserves, discounted at 10 percent, plus the lower of cost or fair value of unproved properties included in the costs being amortized, net of related tax effects. If capitalized costs exceed this limit, the excess is charged to additional depletion, depreciation and accretion expense. The calculation of estimated future net cash flows is based on forecasted prices for crude oil and natural gas except for volumes sold

under long-term contracts. Write-downs required by these rules do not impact cash flow from operating activities; however, as discussed above, sustained low prices would have a material adverse effect on future cash flows.

Financial and Liquidity Risks

The Company anticipates that it will make capital expenditures for the acquisition, exploration, development and production of oil and natural gas in the future. On an ongoing basis, the Company will typically plan to utilize three sources of funding to finance its capital expenditure program; internally generated cash flow from operations, debt where deemed appropriate and new equity issues, if available at favorable terms. In addition, the Company may contemplate the sale of producing properties or the sale of other assets to fund its contractual obligations.

Funds flow is influenced by many factors, which the Company cannot control, such as commodity prices, the United States versus the Canadian dollar exchange rate, interest rates and changes to existing government regulations and tax policies. Should circumstances affect cash flow in a detrimental way, the Company may have limited ability to expand the capital necessary to undertake or complete future drilling programs. In such circumstances, the Company would be required to either reduce the level of its capital expenditures or supplement its capital expenditure program with additional debt and/or equity financing. There can be no assurance that debt or equity financing will be available or sufficient to meet these requirements or, if debt or equity is available, that it will be on terms acceptable to the Company. Moreover, future activities may require the Company to alter its capitalization significantly. The inability of the Company to access sufficient capital for its operations could have a material adverse effect on the Company's financial condition, results of operations and prospects.

Issuance of Debt

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

Supply of Service and Production Equipment

The supply of service and production equipment at competitive prices is critical to the ability to add reserves at a competitive cost and produce these reserves in an economic and timely fashion. In periods of increased activity, these supplies and services can be difficult to obtain. Demand for such limited equipment or access restrictions may affect the availability of such equipment to the Company and may delay exploration and development activities. The Company attempts to mitigate this risk by developing strong long-term relationships with suppliers and contractors. There can be no assurances that these relationships will increase the availability of the supplies and services.

Regulatory Changes

On October 25, 2007, the Government of Alberta announced a new royalty framework ("NRF") which took effect on January 1, 2009. The new framework was announced in response to a report released by an independent Royalty Review Panel appointed by the Government of Alberta that recommended an increase in the overall resource charges to oil and gas producers in the Province of Alberta.

Recent changes were announced to the royalty framework in 2010, which will reduce overall royalty charges from that contemplated in the NRF. Changes in royalties legislation and the resultant impact on cash flows is a risk that the Company monitors.

RELATED PARTY TRANSACTIONS

a) At December 31, 2009 an amount of $50,000 was owing to the Company by a company controlled by a director. The balance due from that company was $449,951 at December 31, 2008, and the movement during the year consisted of:

a. $445,156 was repaid during the year

b. receipt of helicopter services in conjunction with the servicing of natural gas wells in Northern B.C in the amount of $40,190 (2008: $273,329) of which $4,795 was paid via a reduction in the Due from Related Party account. The remaining $35,395 was paid in cash by the Company.

c. advance of $100,000 during the third quarter of which $50,000 was repaid in the fourth quarter

b) As described in Note 7 to the consolidated financial statements, the Company received an advance of $550,000 (subsequently formalized into a loan) from a Company controlled by a director in the fourth quarter of 2009 to fund capital expenditure.

c) The Company obtained engineering consulting services in the amount of $21,090 for the year ended December 31, 2009 (2008: $190,575) from a company controlled by a Company director, who was appointed in 2008. A balance of $123,888 is included in accounts payable and accrued liabilities at December 31, 2009 (December 31, 2008: $180,729).

d) Legal fees in the amount of $88,948 for the year ended December 31, 2009 (2008: $77,287) have been incurred from a legal firm of which a Company director is a partner. A balance of $50,911 is included in accounts payable and accrued liabilities at December 31, 2009 (December 31, 2008: $4,358).

These transactions are in the normal course of business and are recorded at the exchange amount which is the amount of consideration established and agreed to by the related parties.

CONTRACTUAL OBLIGATIONS AND COMMITMENTS

a) Flow-through share issuance

Pursuant to a flow-through share issuance completed in 2008, the Company was committed to incur $2,777,110 of qualifying expenditures by December 31, 2009. At December 31, 2009, approximately $2.1 million of the obligation had been fulfilled, with the remainder to be incurred by June 30, 2010.

b) Employment contract

Under the terms of an employment contract with the Chief Executive Officer, the Company is committed to pay severance under certain circumstances equal to 2 years salary plus 15%.

c) Office sub-lease

The Company is committed to sub-lease payments of approximately $2,100 per month through February 2010. A new office lease was signed in March 2010, for a term of 2 years, with monthly lease payments of approximately $3,400.

CONTINGENCIES AND OFF-BALANCE SHEET ARRANGEMENTS

a) 2006 Flow-through capital raise – qualifying expenditures

Pursuant to a flow-through share issuance completed in March 2006, the Company was committed to incur $4,000,000 of qualified expenditures by December 31, 2007. By December 31, 2007 the Company had incurred only $2.2 million of qualifying expenditure. The remaining $1.8 million was incurred in 2008.

As the Company did not make the necessary qualifying expenditures by December 31, 2007 as required under the income tax rules, the unexpended flow-through amount (approximately $1.8 million) could be reassessed by the tax authorities and the Company could potentially be liable for investor income taxes and penalty interest thereon of up to $700,000 if an arrangement cannot be made to remedy this contingency.

Notwithstanding this, management is of the opinion that the matter can be resolved through negotiation with the tax authorities, however such reassessment is uncertain. No provision has been made in these consolidated financial statements other than an amount for estimated Part XII.6 interest and penalties.

b) Minerals Management Services

The Minerals Management Service ("MMS"), a bureau of the US Department of the Interior that manages that nation's natural gas and oil resource revenues, alleged during the year that a subsidiary of the Company had been deficient in various administrative filing and payment requirements in the past and that, as a result, civil penalties of approximately $578,000 (US$500,000) were levied against the subsidiary. The subsidiary is disputing these penalties and, along with its legal counsel, has negotiated with MMS, the US Department of Treasury, and their respective counsel/agents.

A provision of $86,900 (US$80,000) has been made for these civil penalties. This provision has been based on a settlement with the US Department of Treasury (US$50,000, which was paid in early 2010), and a settlement made directly with MMS (US$30,000). At present, MMS disputes that a binding settlement agreement ("Settlement Agreement") exists. In the event the Settlement Agreement with MMS is not enforced, the maximum exposure of the subsidiary is US$400,000. However in that scenario, the likely settlement amount would be much less.

The Settlement Agreement with MMS includes a probationary period that requires the subsidiary to remain compliant with its reporting and payment requirements over a 24 month time frame; otherwise the full amount of the penalties, reduced on a declining basis for the period of compliance, will be due immediately to MMS. The subsidiary has been compliant with its reporting requirements since August 2008, and the months of compliance will serve to reduce and eventually eliminate the penalties if the Settlement Agreement is enforced.

c) Litigation

During 2008, the Company was named as a defendant in a lawsuit in which a company that signed a farm-out agreement regarding one of the Company's operated wells in Northern BC (the "Plaintiff") claimed, amongst other things, that it had earned a 100% before pay out ("BPO") working interest in this gas well. Guardian agreed to drill and complete the well; the Plaintiff had agreed to pay 100% of the costs in order to earn a 100% working interest. The Plaintiff paid approximately $1.9 million in advances against the total costs of this well but failed to pay 100% of them. Despite its failure to pay, the Plaintiff claimed that it earned its 100% working interest upon completion of the well and that the remaining amounts due by it, which amounts it contested, could be paid from the well's net production revenues. The Company itself funded the additional $688,000 in costs required to complete this well and allow it to be able to produce. While the Plaintiff took no risk regarding these $688,000 in costs, it claimed that it was entitled to a declaration that it earned and should recover 100% of the net production revenues on the basis that, it alleged, the Company was negligent in exceeding the AFE estimates for drilling and completion of the well. The Plaintiff also claimed, by virtue of its purported payment of $175,000 to a third party, a partial interest in the pipeline constructed by the Company in 2008 in order to allow the Kotcho area wells to begin production.

During 2009 the Company entered into a settlement agreement with the Plaintiff. The settlement agreement provided for mutual release by both parties in exchange for a $40,000 cash payment by the Company to the Plaintiff.

d) Other

The Company is also involved in various other claims arising in the normal course of business. While the outcome of these matters is uncertain and there can be no assurance that such matters will be resolved in the Company's favour, the Company does not currently believe that the outcome of adverse decisions in any proceedings related to these matters or any amount which it may be required to pay would have a material adverse impact on its financial position, results of operations or liquidity.

e) Off Balance Sheet Arrangements

Disclosure is required regarding all off-balance sheet arrangements such as transactions, agreements or contractual arrangements with unconsolidated entities, structured finance entities, special purpose entities or variable interest entities that are reasonably likely to materially affect the liquidity of or the availability of, or requirements for, capital resources. The Company had no such off-balance sheet arrangements as at December 31, 2009.

FUTURE CHANGES IN ACCOUNTING STANDARDS

In January 2009, the CICA issued Section 1582, Business Combinations, which replaces former guidance on business combinations. Section 1582 establishes principles and requirements of the acquisition method for business combinations and related disclosures. This statement applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after January 2011 with earlier application permitted. Management is currently assessing the potential impact of the adoption of this section on the results of operations, financial position and disclosures.

In January 2009, the CICA issued Sections 1601, Consolidated Financial Statements, and 1602, Non-controlling Interests, which replaces existing guidance. Section 1601 establishes standards for the preparation of consolidated financial statements. Section 1602 provides guidance on accounting for a non-controlling interest in a subsidiary in consolidated financial statements subsequent to a business combination. These standards are effective on or after the beginning of the first annual reporting period beginning on or after January 2011 with earlier application permitted. Management is currently assessing the impact of the adoption on the results of operations and financial position.

IFRS Adoption

In February 2008, the AcSB confirmed that all Canadian publicly accountable enterprises will be required to adopt International Financial Reporting Standards (IFRS) for interim and annual reporting purposes for fiscal years beginning on or after January 1, 2011. Management has performed a high-level assessment of the impact of the convergence of Canadian GAAP with IFRS on the results of operations, financial position and disclosures. The most significant impact relates to the accounting for property, plant and equipment, in particular the impairment assessment process and depletion calculations.

The Company has not yet quantified the impact of transitioning to IFRS. The impact may be material.

ADDITIONAL INFORMATION

Additional information relating to the Company is filed on the SEDAR website at www.sedar.com. Also, information can also be obtained by contacting the Company at Guardian Exploration Inc., 620, 510 – 5th Avenue S.W., Calgary, Alberta, T2P 3S2.