PACIFIC RUBIALES ENERGY CORP.

Interim Consolidated Financial Statements

For the three and nine months ended September 30, 2010 and 2009
(Unaudited)
(In United States dollars)

The accompanying unaudited interim consolidated financial statements of the Company have been prepared by and are the responsibility of the Company's management. The Company's independent auditors have been engaged to perform a review of these financial statements but they were unable to complete their review procedures by the filing date. The primary reason for this result is due to the timing of the available information.

PACIFIC RUBIALES ENERGY CORP.
Interim Consolidated Balance Sheet
(Unaudited)

(In thousands of U.S. dollars)	**As at September 30 2010**	**As at December 31 2009**
ASSETS		
Current		
Cash and cash equivalents	$ 618,150	$ 438,117
Restricted cash	8,220	8,712
Accounts receivable (note 14 a)	318,751	173,652
Inventories	32,303	38,228
Risk management asset (note 14)	19,690	-
Income tax receivable	1,740	5,048
Prepaid expenses	4,766	4,449
Future income tax	-	2,693
	1,003,620	670,899
Property, plant and equipment (note 3)	2,166,670	1,991,425
Intangible assets (note 9)	176,430	-
Restricted cash	-	2,059
Investments and other assets (note 4)	119,392	74,758
Goodwill	100,636	100,636
	$ 3,566,748	$ 2,839,777
LIABILITIES		
Current		
Accounts payable and accrued liabilities	$ 456,517	$ 257,051
Risk management liability (note 14 e)	11,868	23,538
Income tax payable	83,615	2,721
Current portion of long-term debt (note 6)	949	13,310
Current portion of obligations under capital lease (note 7)	4,238	1,920
Future income tax	2,803	846
	559,990	299,386
Long-term debt (note 6)	433,699	442,159
Obligations under capital lease (note 7)	35,459	38,521
Convertible debentures (note 8)	177,946	165,611
Risk management liability (note 14 e)	5,744	1,720
Future income tax	416,735	382,625
Asset retirement obligation (note 5)	10,633	8,778
	1,640,206	1,338,800
SHAREHOLDERS' EQUITY		
Common shares (note 10 a)	1,671,317	1,364,687
Contributed surplus	118,967	136,934
Equity component of convertible debentures (note 8)	66,118	66,130
Accumulated other comprehensive income	24,234	229
Retained earnings (deficit)	45,906	(67,003)
	1,926,542	1,500,977
	$ 3,566,748	$ 2,839,777

See accompanying notes to the consolidated financial statements

PACIFIC RUBIALES ENERGY CORP.
Interim Consolidated Statements of Operations
(Unaudited)

	Three months ended September 30		Nine months ended September 30	
	2010	2009	2010	2009
(In thousands of U.S. dollars, except for share and per share amounts)				
Revenues				
Oil and gas sales	$ 372,525	$ 156,557	$ 1,112,748	$ 427,551
Trading revenue	32,896	-	32,896	-
	405,421	156,557	1,145,644	427,551
Cost of operations				
Oil and gas operating	128,583	75,357	394,111	202,400
Underlift	(1,237)	(22,322)	(5,073)	(3,542)
Trading operating	32,166	-	32,166	-
Depletion, depreciation and amortization	70,549	46,898	204,199	133,432
	230,061	99,933	625,403	332,290
Earnings before undernoted	175,360	56,624	520,241	95,261
Expenses				
General and administrative	26,306	20,836	72,547	47,900
Stock-based compensation (note 10 b)	652	351	73,327	662
	26,958	21,187	145,874	48,562
Operating income	148,402	35,437	374,367	46,699
Other (expenses) income				
Foreign exchange loss	(20,373)	(69,279)	(41,557)	(93,582)
Income from equity investment (note 4)	1,553	-	80	-
Interest expense	(21,382)	(11,284)	(55,783)	(25,194)
(Loss) gain on risk management contracts (note 14 e)	(10,639)	7,282	(478)	(15,399)
Other expense	(3,493)	(4,590)	(5,769)	(15,317)
	(54,334)	(77,871)	(103,507)	(149,492)
Net income (loss) before income taxes	94,068	(42,434)	270,860	(102,793)
Income tax expense				
Current	35,558	10,840	122,298	17,767
Future	25,654	9,833	35,653	8,451
	61,212	20,673	157,951	26,218
Net income (loss)	$ 32,856	$ (63,107)	$ 112,909	$ (129,011)
Net income (loss) per share (note 15)				
- Basic	$ 0.12	$ (0.29)	$ 0.43	$ (0.61)
- Diluted	$ 0.11	$ (0.29)	$ 0.39	$ (0.61)

See accompanying notes to the consolidated financial statements

PACIFIC RUBIALES ENERGY CORP.
Interim Consolidated Statements of Comprehensive Income
(Unaudited)

(In thousands of U.S. Dollars)	Three months ended September 30 2010	Three months ended September 30 2009	Nine months ended September 30 2010	Nine months ended September 30 2009
Net income (loss)	$ 32,856	$ (63,107)	$ 112,909	$ (129,011)
Other comprehensive income, net of nil tax				
Unrealized foreign currency translation adjustment (note 4)	3,705	-	14,508	-
Unrealized gain on cash flow hedges (note 14 c)	11,698	-	21,721	-
Realized gain on cash flow hedges transferred to net income (note 14 c)	(10,526)	-	(12,224)	-
	4,877	-	24,005	-
Comprehensive income (loss)	$ 37,733	$ (63,107)	$ 136,914	$ (129,011)

See accompanying notes to the consolidated financial statements

PACIFIC RUBIALES ENERGY CORP.
Interim Consolidated Statements of Changes in Shareholders' Equity
(Unaudited)

	Three months ended September 30		Nine months ended September 30	
(In thousands of U.S. Dollars)	**2010**	**2009**	**2010**	**2009**
Common shares				
Balance, beginning of period	1,637,244	1,202,799	1,364,687	1,187,925
Issued on Pacific Stratus acquisition	-	-	-	3,262
Issued on exercise of warrants	-	-	257,182	235
Issued on exercise of options	34,073	10,196	49,404	21,573
Issued on conversion of convertible debentures (note 8)	-	-	44	-
Balance, end of period	1,671,317	1,212,995	1,671,317	1,212,995
Contributed surplus				
Balance, beginning of period	130,774	156,440	136,934	158,660
Exercise of warrants	-	-	(62,328)	-
Exercise of options	(12,459)	(4,473)	(28,966)	(7,004)
Stock-based compensation (note 10 b)	652	351	73,327	662
Balance, end of period	118,967	152,318	118,967	152,318
Equity component of convertible debentures				
Balance, beginning of period	66,118	66,130	66,130	66,130
Conversion to common shares (note 8)	-	-	(12)	-
Balance, end of period	66,118	66,130	66,118	66,130
Accumulated other comprehensive income				
Balance, beginning of period	19,357	229	229	229
Other comprehensive income	4,877	-	24,005	-
Balance, end of period	24,234	229	24,234	229
Retained earnings (deficit)				
Balance, beginning of period	13,050	20,667	(67,003)	86,571
Net income (loss)	32,856	(63,107)	112,909	(129,011)
Balance, end of period	45,906	(42,440)	45,906	(42,440)
Total shareholders' equity	1,926,542	1,389,232	1,926,542	1,389,232

See accompanying notes to the consolidated financial statements

PACIFIC RUBIALES ENERGY CORP.
Interim Consolidated Statements of Cash Flows
(Unaudited)

(In thousands of U.S. dollars)	Three months ended September 30 2010	Three months ended September 30 2009	Nine months ended September 30 2010	Nine months ended September 30 2009
CASH FLOWS FROM OPERATING ACTIVITIES				
Net income	$ 32,856	$ (63,107)	$ 112,909	$ (129,011)
Items not affecting cash:				
Depletion, depreciation and amortization	70,549	46,898	204,199	133,432
Asset retirement obligation accretion (note 5)	305	512	861	1,489
Unrealized loss (gain) on risk management contracts	9,520	(7,279)	(9,161)	15,402
Stock-based compensation (note 10 b)	652	351	73,327	662
Future income tax	25,654	9,833	35,653	8,451
Unrealized foreign exchange loss	25,768	64,538	51,210	87,524
Other	(5,291)	3,931	(3,422)	8,210
Changes in non-cash working capital (note 12)	70,231	8,906	113,775	(18,363)
Net cash provided by operating activities	230,244	64,583	579,351	107,796
CASH FLOWS FROM INVESTING ACTIVITIES				
Additions to oil and gas properties and equipment	(198,868)	(88,141)	(376,121)	(272,604)
Additions to intangible assets (note 9)	-	-	(190,000)	-
Decrease in restricted cash	1,945	(153)	2,551	3,253
Equity investments (note 4)	(26,000)	-	(26,000)	-
Other	(407)	-	(300)	1,395
Net cash used in investing activities	(223,330)	(88,294)	(589,870)	(267,956)
CASH FLOWS FROM FINANCING ACTIVITIES				
Advances from long-term debt	-	84,191	4,851	303,791
Repayment of long-term debt	(15,647)	(42,763)	(22,295)	(91,276)
Proceeds from the exercise of warrants and options	21,614	5,723	215,292	14,804
Other	(1,440)	-	(4,756)	-
Net cash provided by financing activities	4,527	47,151	193,092	227,319
Effect of exchange rate changes on cash and cash equivalents	2,621	3,403	(2,540)	7,839
Change in cash and cash equivalents during the period	14,062	26,843	180,033	74,998
Cash and cash equivalents, beginning of the period	604,088	138,546	438,117	90,391
Cash and cash equivalents, end of the period	$ 618,150	$ 165,389	$ 618,150	$ 165,389
Cash and cash equivalents are comprised of:				
Cash	$ 577,287	$ 141,484	$ 577,287	$ 141,484
Short-term money market instruments	40,863	23,905	40,863	23,905
	$ 618,150	$ 165,389	$ 618,150	$ 165,389

See accompanying notes to the consolidated financial statements

1. SIGNIFICANT ACCOUNTING POLICIES AND BASIS OF PRESENTATION

Pacific Rubiales Energy Corp. (the "Company"), is a publicly traded oil and gas company engaged in the exploration, development and production of heavy crude oil and natural gas in Colombia, Guatemala and Peru.

These unaudited interim consolidated financial statements of the Company which include the accounts of the Company and its subsidiaries have been prepared by management in accordance with Canadian generally accepted accounting principles ("GAAP"). The unaudited interim consolidated financial statements have been prepared following the same accounting policies and methods of computation as the audited consolidated financial statements for the fiscal year ended December 31, 2009, except as noted in note 2. The unaudited interim consolidated financial statements do not include all of the disclosures included in the annual audited consolidated financial statement and accordingly should be read in conjunction with the audited annual consolidated financial statements and the notes thereto in the Company's annual report for the year ended December 31, 2009.

2. CHANGES IN AND ADOPTION OF ACCOUNTING POLICIES

a) Business Combinations/Consolidated Financial Statements/Non-Controlling Interests

In January 2009, the CICA issued Handbook Sections 1582, "Business Combinations" ("Section 1582"), 1601, "Consolidated Financial Statements" ("Section 1601") and 1602, "Non-controlling Interests" ("Section 1602"). Section 1582 replaces CICA Handbook Section 1581, "Business Combinations", and establishes standards for the accounting for business combinations that are equivalent to the business combination accounting standard under IFRS. Section 1582 is applicable 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 1, 2011, with early adoption permitted. Section 1601 together with Section 1602 replaces CICA Handbook Section 1600, "Consolidated Financial Statements". Section 1601 establishes standards for the preparation of consolidated financial statements and Section 1602 establishes standards for accounting for a non-controlling interest in a subsidiary in consolidated financial statements subsequent to a business combination. Sections 1601 and 1602 are applicable for interim and annual consolidated financial statements relating to fiscal years beginning on or after January 1, 2011, with early adoption permitted. An entity must adopt Section 1582, 1601 and 1602 at the same time. The Company has adopted these standards effective January 1, 2010 and the adoption did not have a material impact on the results of operations or financial position.

b) Intangible assets

Intangible assets are recorded at their fair value on the date of acquisition. Intangible assets with finite useful lives are amortized over their useful lives. The Company's intangible asset consists of rights to the available capacity of a pipeline system in Colombia. The intangible asset is amortized based on the usage of the 160 million barrel capacity over the term of the agreement. The Company does not have intangible assets with an infinite life which would not be subject to amortization. The Company applies an impairment test to the carrying value of the intangible asset to ensure that such costs do not exceed the estimated amount ultimately recoverable. Any reduction in the carrying value, as a result of the impairment test, is included in depletion, depreciation and amortization.

c) Segment disclosures

During the three months ended September 30, 2010, the Company entered into a new business of purchasing and marketing third-party crude oil (crude trading business). The Company purchases light crude oil from local producers and markets the products in the international markets. The Company recognizes revenues on the sale of crude oil when these are delivered and the title passes to the buyers and collection is reasonably assured. The crude trading business is identified as a reportable segment as of September 30, 2010, with revenue and operating expenses presented in the statement of operations.

3. PROPERTY, PLANT AND EQUIPMENT

	September 30, 2010		
	Cost	Accumulated DD & A	Net Book Value
Oil and gas properties and equipment	$ 2,608,652	$ 495,106	$ 2,113,546
Corporate and other	29,290	11,657	17,633
Power generation unit under capital lease	38,783	3,292	35,491
	$ 2,676,725	$ 510,055	$ 2,166,670

	December 31, 2009		
	Cost	Accumulated DD & A	Net Book Value
Oil and gas properties and equipment	$ 2,251,675	$ 309,725	$ 1,941,950
Corporate and other	20,393	8,092	12,301
Power generation unit under capital lease	38,783	1,609	37,174
	$ 2,310,851	$ 319,426	$ 1,991,425

As of September 30, 2010, $707 million (December 31, 2009 – $1.07 billion) in future capital expenditures has been included in the calculation of depletion, depreciation and amortization. The cost of oil and gas properties and equipment was reduced by the tax benefit of $151.5 million (December 31, 2009 - $100.3 million) arising from the 30% (40% before 2010) special tax deduction on qualified expenditures in Colombia.

During 2009 the Company entered into a power generation arrangement to supply electricity to three of its oil fields in Colombia. The arrangement is accounted for as a capital lease. Under this accounting treatment, the Company has recorded its proportionate share of the leased asset and obligation. The asset is amortized using the unit of production method over the term of the lease. For the three and nine months ended September 30, 2010, amortization expense of $1 million and $2.8 million respectively (three and nine months ended September 30, 2009 - $0.7 million) related to the leased property is charged to depletion, depreciation and amortization.

Included in oil and gas properties and equipment is $238 million (December 31, 2009 – $191 million) of unproved properties that were excluded from the depletion, depreciation and amortization calculation.

4. INVESTMENTS AND OTHER ASSETS

The investments and other assets consist of the following:

	ODL (1)	Ronter & PII (2)	Pacific Coal (3)	Other	Total
As at December 31, 2009	$ 64,245	$ 9,943	$ -	$ 570	$ 74,758
Acquisition (disposition)	-	-	-	138	138
Income (loss) from equity investment	(138)	174	-	-	36
Foreign currency translation	4,590	-	-	-	4,590
As at March 31, 2010	$ 68,697	$ 10,117	$ -	$ 708	$ 79,522
Acquisition (disposition)	-	3,500	-	1	3,501
Income (loss) from equity investment	(1,604)	95	-	-	(1,509)
Foreign currency translation	6,213	-	-	-	6,213
As at June 30, 2010	$ 73,306	$ 13,712	$ -	$ 709	$ 87,727
Acquisition (disposition)	-	2,000	24,000	407	26,407
Income from equity investment	1,501	52	-	-	1,553
Foreign currency translation	3,705	-	-	-	3,705
As at September 30, 2010	$ 78,512	$ 15,764	$ 24,000	$ 1,116	$ 119,392

(1) The investment represents a 35% interest in ODL Finance S.A. (“ODL”), a special purpose Panamanian company with a Colombian branch that has constructed an oil pipeline for the transportation of heavy crude oil produced out of the Rubiales field. The remaining 65% interest is owned by Ecopetrol S.A., the national oil company of Colombia. The investment is accounted for using the equity method and the Company’s share of net income or loss is included as income (loss) from equity investment.

4. INVESTMENTS AND OTHER ASSETS (continued)

ODL's functional currency is the Colombian peso and is accounted for as a self-sustaining operation. The currency translation adjustment upon conversion to US dollars has been recorded in other comprehensive income as at September 30, 2010. As at December 31, 2009 ODL was accounted for as an integrated operation. Subsequently ODL's operations became self-sustaining when the pipeline was fully operational upon the completion of phase two of the construction of the pipeline.

The Company has ship or pay contracts with ODL for the transportation of crude oil from the Rubiales field to Colombia´s oil transportation system, for a total commitment of $336 million over a seven-year period.

(2) The investment in Ronter Inc. ("Ronter") represents a 21.7% indirect interest in Promotora de Energia Electrica de Cartagena & Cia, S.C.A. ESP ("Proelectrica"). Proelectrica is a private, Cartagena, Colombia-based 90 megawatt electrical utility peak demand supplier to the local Cartagena utility. This investment is accounted for using the equity method and the Company's share of Proelectrica's net income or loss is included as income (loss) from equity investment.

In April 2010 the Company acquired a 9.4% interest for $3.5 million in Lando (now called Pacific Infrastructure Inc. ("PII")), a company that was previously fully owned by Ronter. In September 2010, the Company acquired an additional 4% interest for $2 million from a shareholder of PII that was not related to the Company. As of September 30, 2010, PII is 13.4% owned by the Company, 25% owned by Ronter, 47.98% owned by Blue Pacific Assets Corp. ("Blue Pacific", see note 17 a), a corporation related to the Company, 6.87% owned by Orinoquia Holdings Corp., a company that two directors of the Company control or provide advice to, and 6.75% owned by an unrelated party. The total interest in PII held by the Company directly and indirectly is 18.75%, or $5.5 million. The investment in PII is recorded at cost as its fair value is not readily determinable as at September 30, 2010.

(3) During the three months ended September 30, 2010, the Company acquired a 19.05% interest in Pacific Coal S.A. ("Pacific Coal"), a private company incorporated in Panama, for $24 million. Pacific Coal is engaged in the acquisition and development of coal mining assets and related businesses in Colombia. Four directors and one officer of the Company are also directors of Pacific Coal. The investment is accounted for using the equity method, and the Company's share of Pacific Coal's net income or loss is included as income (loss) from equity investment.

5. ASSET RETIREMENT OBLIGATION

The amount required to settle the future asset retirement obligation was estimated by management based on the Company's net ownership interest in all wells and facilities, estimated costs to reclaim those wells and facilities and estimated timing of the costs to be incurred in future periods. The Company has estimated its total asset retirement obligations to be $10.6 million (December 31, 2009 - $8.8 million) based on a total undiscounted future liability of $39.2 million as of September 30, 2010 (December 31, 2009 - $39.4 million), and annual inflation rates ranging from 3.2% to 6.0% until the time the liability is settled. The obligation is expected to be settled at the end of the useful lives of the underlying assets determined by the expiration date in concession agreements, which is expected to be incurred subsequent to 2016. The obligation has been discounted using credit-adjusted risk-free interest rates ranging from 11% to 15% as of September 30, 2010 (December 31, 2009 – 12% to 15%).

Changes to the asset retirement obligation during the period were:

	Three months ended September 30		Nine months ended September 30	
	2010	2009	2010	2009
Balance, beginning of the period	$ 9,334	$ 15,648	$ 8,778	$ 14,671
Obligation incurred during the period	994	654	994	654
Accretion expense	305	512	861	1,489
Balance, end of the period	$ 10,633	$ 16,814	$ 10,633	$ 16,814

6. LONG-TERM DEBT

	Maturity	Currency	Interest Rate	September 30 2010	December 31 2009
Prommisory note (1)	October 1, 2010	COP	10.48%	$ 949	$ 1,205
Prommisory note (1)	December 24, 2010	COP	10.00%	-	7,338
Prommisory note (1)	November 30, 2010	COP	9.70%	-	3,812
Prommisory note (1)	March 30, 2010	COP	9.70%	-	955
Senior notes	(2)	USD	8.75%	436,560	442,159
Deferred transaction cost (3)				(2,861)	-
				$ 434,648	$ 455,469
Current portion				$ 949	$ 13,310
Long-term debt				433,699	442,159
				$ 434,648	$ 455,469
Convertible debenture (note 8)				177,946	165,611
				$ 612,594	$ 621,080

(1) Unsecured, repayable in equal monthly instalments.
(2) November 10, 2014 (33.3%), November 10, 2015 (33.3%), and November 10, 2016 (33.4%).
(3) Capitalized transaction costs related to revolving credit facility.

Senior notes

The Company has outstanding senior notes with an aggregate principal amount of $450 million and maturity dates of November 10, 2014 (33.3%), November 10, 2015 (33.3%), and November 10, 2016 (33.4%). The interest rate on the notes is 8.75%, payable on May 10 and November 10 of each year. The notes may be redeemed in whole (but not in part) at any time at the discretion of the Company with a redemption price equal to the greater of (1) 100% of the principal amount of the notes to be redeemed, and (2) the sum of the present values of the remaining scheduled payments of principal and interest discounted to the date of redemption on a semi-annual basis at the applicable treasury rate plus 75 basis points, in each case plus accrued and unpaid interest on the outstanding principal amount. The notes are senior unsecured and will rank equal in right of payment with all of the Company's existing and future senior unsecured debt. The notes are on the Official List of the Luxembourg Stock Exchange and trade on the Euro MTF. Under the terms of the notes, the Company is required to maintain (1) an interest coverage ratio of greater than 2.5; and (2) a debt to EBITDA ratio of less than 3.5. The covenants would not apply during any period of time if the notes have an investment grade rating from at least two rating agencies. The Company was compliant with the covenants during the period.

The senior notes are carried at amortized cost using the effective interest rate method with note discount and transaction costs netted against the principal of the revolving credit facility. For the three and nine months ended September 30, 2010, $10.4 million and $25.4 million respectively (2009 – $nil) in interest expense related to the senior notes has been recorded in the statements of operations.

On June 30, 2010 the Company solicited consents to amend the indenture relating to its senior notes to provide the Company with needed flexibility to invest in minority equity investments in, and provide guarantees for, joint venture entities. This solicitation was approved by a majority of the note holders on July 15, 2010.

Revolving credit facility

During April 2010, the Company closed the syndication of a $250 million unsecured revolving credit facility. As of September 30, 2010, no borrowing has been made on the facility. The interest rate for the facility is determined in accordance with the ratings assigned to the Company's senior debt securities by Standard & Poor's Ratings Group and Fitch Inc. Based on the Company's rating as of September 30, 2010, the interest rate would be LIBOR plus 3.25%. In addition, the Company is required to pay commitment fees of 1% on the unutilized portion of any outstanding commitments under the facility. Subject to customary acceleration events set out in the credit agreement, or unless terminated earlier by the Company without penalty, repayment of the outstanding principal on the facility will be made in full on April 26, 2012. Under the terms of the credit facility, the Company is required to maintain (1) a debt to EBITDA ratio of less than 3.5; and (2) an EBITDA to interest expense ratio of greater than 3. The Company was compliant with the covenants during the period.

7. OBLIGATIONS UNDER CAPITAL LEASE

The Company has entered into a power generation arrangement to supply electricity for three of its oil fields in Colombia until June 2016. The arrangement has been accounted for as a capital lease with an effective interest rate of 18.9%. Under this arrangement, the Company's proportionate share of annual minimum lease payments is as follows:

	September 30 2010	December 31 2009
Within 1 year	$ 11,306	$ 9,524
Year 2	11,337	11,306
Year 3	11,306	11,337
Year 4	11,306	11,306
Year 5	11,306	11,306
Thereafter	8,488	16,944
Total minimum lease payments	$ 65,049	$ 71,723
Amounts representing interest	(25,352)	(31,282)
Present value of net minimum lease payments	39,697	40,441
Current portion	4,238	1,920
Long-term portion	35,459	38,521
Total obligations under capital lease	$ 39,697	$ 40,441

For the three and nine months ended September 30, 2010, interest expense of $1.9 million and $5.7 million respectively (three and nine months ended September 30, 2009 – $1.2 million) was incurred on the capital lease.

8. CONVERTIBLE DEBENTURES

On August 28, 2008, the Company issued $228.2 million (C$240 million) of convertible unsecured subordinated debentures due August 29, 2013 and convertible into common shares of the Company at C$13 per share. The debentures bear interest at 8% annually and are payable semi-annually in arrears on June 30 and December 31.

The debentures have been classified into their debt and equity components. The fair value of the equity component was valued using the Black-Scholes option pricing model using a risk free rate of 3.65%, no dividends paid, expected life of 5 years and an expected volatility of 50% with the residual of the cash received allocated to the debt component. As a result, on the issuance of the debentures, $149.7 million (net of $8.5 million issuance costs) was classified as the debt component and $66.1 million (net of $3.8 million issuance costs) was classified as the equity component. The debt component will accrete up to the principal balance over the term of the debenture using the effective interest method. The accretion and interest paid are expensed as interest expense yielding an effective annual rate of 18%.

	Three months ended September 30		Nine months ended September 30	
	2010	2009	2010	2009
Balance, beginning of the period	$ 168,667	$ 143,472	$ 165,611	$ 132,001
Conversion to common shares	-	-	(32)	-
Accretion expense	3,411	2,745	9,916	7,421
Foreign exchange loss	5,868	13,105	2,451	19,900
Balance, end of the period	$ 177,946	$ 159,322	$ 177,946	$ 159,322

During the nine months ended September 30, 2010, $44 (C$45) of the convertible debentures were converted to 3,460 of the Company's common shares. The debt component of $32 and the equity component of $12 of the converted debentures were transferred to common shares.

9. INTANGIBLE ASSETS

	Three months ended September 30		Nine months ended September 30	
	2010	2009	2010	2009
Balance, beginning of the period	$ 181,938	$ -	$ -	$ -
Additions	-	-	190,000	-
Amortization	(5,508)	-	(13,570)	-
Balance, end of the period	$ 176,430	$ -	$ 176,430	$ -

In January 2010 the Company entered into an agreement with Oleoducto Central S.A. ("OCENSA") whereby the Company acquired preferential rights to the available capacity on the OCENSA pipeline system for up to 160 million barrels of its oil for a 10 year period beginning February 1, 2010, for a one-time payment of $190 million. The intangible asset is amortized based on the usage of the barrel capacity over the term of the agreement. The amortization is included in depletion, depreciation and amortization.

10. SHARE CAPITAL

(a) Authorized, issued and fully paid common shares

Unlimited number of common shares with no par value.

Continuity schedule of share capital:

	Number of Shares	Amount
Balance, January 1, 2009	210,566,340	$ 1,187,925
Issued on the Pacific Stratus Acquisition	538,334	3,262
Issued on exercise of warrants	16,893,209	133,520
Issued on exercise of options	4,906,889	39,980
Balance, December 31, 2009	232,904,772	$ 1,364,687
Issued on exercise of warrants	27,106,081	223,079
Issued on exercise of options	2,022,119	24,889
Issued on conversion of convertible debentures	3,460	44
Balance, March 31, 2010	262,036,432	$ 1,612,699
Issued on exercise of warrants	3,000	30
Issued on exercise of options	1,611,671	24,515
Balance, June 30, 2010	263,651,103	$ 1,637,244
Issued on exercise of options	2,886,135	34,073
Balance, September 30, 2010	266,537,238	$ 1,671,317

(b) Stock options

The Company has established a "rolling" Stock Option Plan (the "Plan") in compliance with the TSX policy for granting stock options. Under the Plan, the maximum number of shares reserved for issuance may not exceed 10% of the total number of issued and outstanding common shares. The exercise price of each option shall not be less than the market price (as defined under TSX Policy) of the Company's stock at the date of grant.

10. SHARE CAPITAL (continued)

A summary of the changes in stock options is presented below:

	Outstanding	Weighted average exercise price
Balance, January 1, 2009	19,747,748	C$ 5.94
Granted during the period	4,596,500	C$12.81
Cancelled during the period	(214,228)	C$5.70
Exercised during the period	(4,906,889)	C$5.88
Balance, December 31, 2009	19,223,131	C$ 7.60
Granted during the period	6,296,500	C$14.10
Exercised during the period	(2,022,119)	C$ 8.61
Balance, March 31, 2010	23,497,512	C$ 9.25
Granted during the period	3,198,500	C$20.63
Exercised during the period	(1,611,671)	C$10.08
Balance, June 30, 2010	25,084,341	C$10.65
Granted during the period	56,000	C$27.58
Exercised during the period	(2,886,135)	C$7.78
Balance, September 30, 2010	22,254,206	C$11.09

The following table summarizes information about the stock options outstanding and exercisable.

Outstanding & Exercisable	Exercise price	Expiry date	Remaining contractual life
1,237,253	C$ 2.22	August 21, 2011	0.9
2,343,206	C$ 4.70	October 23, 2013	3.1
166,667	C$ 5.70	May 9, 2017	6.6
370,002	C$ 6.30	July 10, 2017	6.8
946,042	C$ 6.78	April 20, 2012	1.6
5,622,502	C$ 7.38	February 11, 2013	2.4
6,251	C$ 8.46	May 3, 2012	1.6
9,583	C$ 8.46	April 16, 2013	2.5
10,000	C$ 10.86	July 30, 2014	3.8
3,065,200	C$ 13.09	October 12, 2014	4.0
7,500	C$ 14.57	January 6, 2014	4.3
5,241,500	C$ 14.08	February 9, 2015	4.4
18,000	C$ 19.00	March 16, 2015	4.5
5,000	C$ 19.47	April 14, 2015	4.5
3,068,500	C$ 20.56	April 23, 2015	4.6
21,000	C$ 20.09	May 17, 2015	4.6
60,000	C$ 24.41	June 22, 2015	4.7
56,000	C$ 27.58	September 30, 2015	5.0
22,254,206	C$ 11.09		3.5

10. SHARE CAPITAL (continued)

The following stock options with a 5 year life were granted to employees, directors and consultants.

	Number of options granted	Weighted average exercise price	Weighted average fair value
For the three months ended March 31, 2010	6,296,500	C$14.10	C$6.94
For the three months ended June 30, 2010	3,198,500	C$20.63	C$9.96
For the three months ended September 30, 2010	56,000	C$27.58	C$12.03
Total	9,551,000	C$16.37	C$7.97

The fair values of the stock options issued for the three months ended September 30, 2010 have been calculated using the Black-Scholes option pricing model, based on the following assumptions:

Weighted average risk-free interest rate:	1.35%
Expected life:	2.5 years
Weighted average expected volatility:	77%
Expected dividend yield:	0

(c) Warrants

Each warrant outstanding is exercisable into one common share.

The following table summarizes information about the warrants outstanding and exercisable at September 30, 2010.

Outstanding & exercisable	Exercise price	Expiry date
611,682	C$7.80	July 12, 2012

A summary of the changes in warrants is presented below.

	Outstanding & exercisable	Weighted average exercise price
Balance, January 1, 2009	44,803,552	C$7.72
Exercised during the year	(16,893,209)	C$7.59
Balance, December 31, 2009	27,910,343	C$7.80
Exercised during the period	(27,295,661)	C$6.30
Balance, March 31, 2010	614,682	C$7.80
Exercised during the period	(3,000)	C$7.80
Balance, June 30 and September 30, 2010	611,682	C$7.80

On December 14, 2009, the Company's proposed offer of a cash payment of C$1.50 per warrant as an incentive for holders of the warrants to exercise their warrants during an early exercise period was approved by shareholders and warrantholders. The period commenced on December 14, 2009 and expired January 20, 2010. Warrantholders were able to exercise their warrants within this period to acquire one common share of the Company per warrant at an exercise price of C$6.30 instead of the original C$7.80 exercise price. As of December 31, 2009, 16,361,293 warrants had been exchanged for common shares under the early exercise program.

10. SHARE CAPITAL (continued)

On January 12, 2010, the Company announced that greater than 66 2/3% of its publicly-traded warrants outstanding as of December 14, 2009 had been exercised pursuant to the early exercise transaction. As a result of reaching the 66 2/3% threshold, each warrant that had not been so exercised during the 30-day early exercise period was deemed automatically exchanged by the warrantholder, without any further action or payment of additional consideration on the part of the warrantholder (including payment of the exercise price thereof), for consideration payable by the Company of C$0.75 (the "Exchange Payment") plus a fraction of a common share (collectively, the "Exchange Shares") equal to: (A) the volume weighted average trading price of the common shares on the TSX for the five trading days immediately prior to the early exercise expiry date (the "Market Price") minus (B) current exercise price, divided by (C) the Market Price. Warrants that were held by U.S. warrantholders were not subject to the automatic exchange. In total, 27,295,661 warrants were exchanged after December 31, 2009, for C$170 million in cash and 27,106,081 common shares of the Company.

11. CAPITAL DISCLOSURES

The Company's objectives when managing capital are: (i) to maintain a flexible capital structure, which optimizes the cost of capital at acceptable risk; and (ii) to maintain investor, creditor and market confidence to sustain the future development of the business.

The Company manages its capital structure and makes adjustments to it in light of changes in economic conditions and the risk characteristics of its underlying assets. To maintain or adjust the capital structure, the Company may from time to time issue shares, raise debt and/or adjust its capital spending to manage its current and projected debt levels.

The Company monitors capital based on the following non-standardized GAAP measures: current and projected ratios of debt to cash flow from operations and debt to capital employed. The Company's objective, which is currently met, is to maintain a debt to cash flow from operations ratio of less than three times. The ratio may increase at certain times as a result of acquisitions. To facilitate the management of this ratio, the Company prepares annual budgets, which are updated depending on varying factors such as general market conditions and successful capital deployment. The Company's share capital is not subject to external restrictions.

There were no changes in the Company's approach to capital management from the previous year.

The Company defines its capital as follows:

	September 30 2010	December 31 2009
Shareholders' equity	$ 1,926,542	$ 1,500,977
Long-term debt	434,648	455,469
Convertible debt	177,946	165,611
Working capital surplus	(444,579)	(384,823)
	2,094,557	$ 1,737,234

12. SUPPLEMENTAL DISCLOSURE WITH RESPECT TO CASH FLOWS

Changes in non-cash working capital, net of foreign exchange gains or losses, were as follows.

	Three months ended September 30		Nine months ended September 30	
	2010	2009	2010	2009
(Increase) decrease in accounts receivable	$ (49,549)	$ 9,210	$ (139,978)	$ (43,414)
(Increase) decrease in income taxes receivable	(675)	-	3,880	-
Increase (decrease) in accounts payable and accrued liabilities	94,178	(8,764)	163,344	26,752
Decrease (increase) in inventory	6,212	(342)	6,693	(2,992)
Increase (decrease) in income taxes payable	20,803	9,024	80,153	(4,471)
Decrease in prepaid expenses and other	(738)	(222)	(317)	5,762
	$ 70,231	$ 8,906	$ 113,775	$ (18,363)

Included in accounts payable and accrued liabilities are amounts related to additions to property, plant, and equipment of $189.5 million as at September 30, 2010 (December 31, 2009 - $91.3 million).

Non-cash financing transactions for the nine months ended September 30, 2010 included the conversion of $32 of convertible debenture ($45 in face value) to 3,460 of the Company's common shares.

Other cash flow information:	Three months ended September 30		Nine months ended September 30	
	2010	2009	2010	2009
Cash income taxes paid	$ 701	$ -	$ 3,276	$ 3,681
Cash interest paid	291	3,378	911	4,878
Cash interest received	644	1,750	1,346	8,592

13. CONTINGENCIES AND COMMITMENTS

A summary of the Company's undiscounted commitments by calendar year is presented below.

	2010	2011	2012	2013	2014	Subsequent to 2014	Total
Operating leases	$ 773	$ 1,710	$ 840	$ -	$ -	$ -	$ 3,323
Transportation and processing commitments	11,745	46,980	46,980	46,980	46,980	124,740	324,405
Minimum work commitments	136,671	52,511	1,850	-	-	-	191,032
Accounts payable	456,517	-	-	-	-	-	456,517
Abandonment obligations	2,331	1,180	393	106	2,402	32,758	39,170
Long-term debt and bank indebtedness	949	-	-	-	149,985	300,015	450,949
Convertible debentures - principal	-	-	-	233,183	-	-	233,183
Obligations under capital lease	2,850	11,306	11,337	11,306	11,306	16,944	65,049
Total	$ 611,836	$ 113,687	$ 61,400	$ 291,575	$ 210,673	$ 474,457	$ 1,763,628

The Company has various guarantees in place in the normal course of business. As at September 30, 2010, the Company has issued letters of credit and guarantees for exploration and operational commitments for a total of $262.1 million (December 31, 2009 – $110.3 million).

Association contracts

Certain association contracts signed before 2003 with Ecopetrol include clauses in which Ecopetrol may commence participating in the operation of new discoveries made by the Company at any time, without prejudice to the Company's right to be reimbursed for the investments made on their sole account and risk (back-in right). The contract provides that if Ecopetrol decides to declare the commerciality of the field and participate in the

13. CONTINGENCIES AND COMMITMENTS (continued)

commercial phase of the association contract, the Company shall have the right to be reimbursed for 200% of the total costs incurred during the exploration phase of the contract. Once the reimbursement has been made, Ecopetrol is entitled to acquire a 50% share of the oil production of the fields. The back-in rights were not exercised as at September 30, 2010.

Contingencies

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

Natural gas supply agreements

Since the discovery of the La Creciente field in early 2007, the Company has focused on developing a commercial strategy to service the domestic market while concurrently exploring export opportunities. The Company has entered into the following take or pay contracts, and interruptible contracts, totaling 60 MMBTU per day for the period 2010-2011:

		2010		2011	
Client	*Contract*	Quantity (MMBTUD)	Price (1) ($/MMBTU)	Quantity (MMBTUD)	Price (1) ($/MMBTU)
GECELCA	Take or pay	45,000	RMP + 28%	45,000	RMP + 28%
PROELECTRICA	(2)	5,000	RMP + 12%	5,000	(RMP + 88%)+$ 0.10/MBTU
Interruptible supply		10,000	RMP	10,000	RMP - 20%
Total		60,000	RMP + 19%	60,000	RMP + 29%

(1) RMP represents the Colombian Regulated Market Price.

(2) Up to 14,000 MBTUD

The Company anticipates having sufficient production to meet all future delivery commitments.

14. FINANCIAL RISK MANAGEMENT

The nature of oil and natural gas operations and the related issuance of debt expose the Company to fluctuations in commodity prices, foreign currency exchange rates and interest rates. The Company manages these risks through periodic use of derivative instruments. The Board of Directors periodically reviews the results of all risk management activities and all outstanding positions.

(a) Credit risk

The Company actively limits the total exposure to individual client counterparties and holds a trade credit insurance policy for indemnification for losses from non-collection of trade receivables. Two (December 31, 2009 – two) of the Company's customers had accounts receivable that were greater than 10% of total trade accounts receivable. The Company's credit exposure to these customers was $45 million and $5.4 million or 73% and 9% of trade accounts receivable, respectively (December 31, 2009 - two customers at $30.9 million and $10.5 million or 50% and 17% respectively). Revenues from these customers were $45 million and $19.9 million or 5.9% and 2.6% of net revenue, respectively (December 31, 2009 - $65.5 million and $17.5 million or 10.2% and 2.7% respectively).

14. FINANCIAL RISK MANAGEMENT (continued)

The Company's accounts receivables are as follows:

	September 30 2010	December 31 2009
Trade accounts receivable		
Not past due (less than 45 days)	$ 60,198	$ 35,458
Past due (0-30 days)	1,412	26,641
Past due (31-120 days)	-	-
Past due (over 120 days)	778	-
Allowance for doubtful accounts	(989)	(1,225)
Total trade accounts receivable	61,399	60,874
VAT and withholding taxes recoverable	100,614	46,988
Advances and deposits	25,708	30,603
Joint ventures partners	99,784	26,325
Other	31,246	8,862
	$ 318,751	$ 173,652

(b) Interest rate risk

The Company is exposed to interest rate risk on its outstanding variable rate revolving credit borrowings due to fluctuations in market interest rates. The Company monitors its exposure to interest rates. As of September 30, 2010 the Company does not have outstanding borrowings under the variable rate revolving credit.

(c) Foreign currency exchange risk

The Company is exposed to foreign currency fluctuations in Colombian pesos (COP) and Canadian dollars relative to US dollars.

In addition, as of September 30, 2010, the Company has COP 793 billion, or $439.5 million of future income tax liabilities related to proved and unproved properties arising from the Rubiales, Pacific Stratus, and Kappa acquisitions in 2007 and 2008 (December 31, 2009 – COP 845.2 billion, or $413.5 million). The future income tax liabilities are denominated in COP as the assets to which the future income tax liabilities relate are located in Colombia. The future income tax liabilities are monetary items, which are revalued each period end at the current exchange rates, with the unrealized foreign exchange gain or loss recorded in net income (loss) in the period. Based on the net exposure and foreign exchange rates at September 30, 2010, a 10% depreciation or appreciation of the Colombian Peso against the US dollar would result in a $40.3 million (December 31, 2009 - $41.4 million) increase or decrease in the Company’s after-tax net income.

The Company has convertible debentures outstanding with a face amount of C$239,955 as at September 30, 2010. The debentures have been classified into debt and equity components, with the debt component being revalued each period end at the current exchange rates and the unrealized foreign exchange gain or loss recorded in net income (loss). Based on the debt balance and foreign exchange rates as of September 30, 2010, a 10% depreciation or appreciation of the Canadian dollar against the US dollar would result in a $16.2 million (December 31, 2009 - $16.5 million) increase or decrease in the Company’s after-tax net income.

To reduce its foreign currency exposure associated with operating expense incurred in COP, the Company may enter into currency risk management contracts such as foreign exchange forwards, options, and costless collars. The Company has the following currency risk management contracts outstanding as at September 30, 2010 that qualify for cash flow hedge accounting:

Instrument	**Settlement date**	**Notional amount ($)**	**Floor-ceiling (COP/$)**	**Fair value ($)**
Currency collars	October 25, 2010	38,825	2000-2050 and 2000-2060	4,280
Currency collars	November 26, 2010	40,131	2000-2050 and 2000-2060	4,423
Currency collars	December 23, 2010	86,019	2000-2050 and 2000-2060	9,472
	Total	**$ 164,975**		**$ 18,175**

14. FINANCIAL RISK MANAGEMENT (continued)

The effective portion of the change in the fair value of the above currency hedges is recognized in other comprehensive income as unrealized gains or losses on cash flow hedges. The effective portion is reclassified from other comprehensive income to operating expenses in the same period as the hedged operating expenses are incurred. During the three and nine months ended September 30, 2010, $11.7 million and $21.7 million (2009 - $nil) of unrealized gains were recorded in other comprehensive income respectively, and $10.5 million and $12.2 million (2009 – $nil) of realized hedge gains were reclassified against operating expenses. The Company excludes changes in fair value due to the time value of options and records these amounts along with hedge ineffectiveness in foreign exchange gains or losses in the period that they arise. During the three and nine months ended September 30, 2010, $4.7 million and $5.7 million of ineffectiveness respectively were recorded as foreign exchange losses (2009 - $nil).

(d) Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they become due. The Company's process for managing liquidity risk includes ensuring, to the extent possible, that it will have sufficient liquidity to meet its liabilities when they become due. The Company prepares annual capital expenditure budgets which are monitored and updated as required. In addition, the Company requires authorizations for expenditures on projects to assist with the management of capital.

The following are the contractual maturities of financial liabilities (undiscounted):

Financial liability due in	2010	2011	2012	2013	2014	Subsequent to 2014	Total
Accounts payable and accrued liabilities	$ 456,517	$ -	$ -	$ -	$ -	$ -	$ 456,517
Long-term debt and bank indebtedness	949	-	-	-	149,985	300,015	450,949
Convertible debentures - principal (1)	-	-	-	233,183	-	-	233,183
Obligations under capital lease (2)	2,850	11,306	11,337	11,306	11,306	16,944	65,049
Total	$ 460,316	$ 11,306	$ 11,337	$ 244,489	$ 161,291	$ 316,959	$ 1,205,698

(1) The principal of C$239,955 of convertible debentures is due on August 29, 2013. The balance due is converted to US dollars using the exchange rate on September 30, 2010.

(2) Obligations arising from the power generation arrangement to supply electricity to the Company from August 2009 to June 2016. The arrangement has been accounted for as a capital lease.

(e) Commodity price risk management

Commodity price risk is the risk that the cash flows and operations of the Company will fluctuate as a result of changes in commodity prices. Significant changes in commodity prices can also impact the Company's ability to raise capital or obtain additional debt financing. Commodity prices for crude oil are impacted by world economic events that dictate the levels of supply and demand. From time to time the Company may attempt to mitigate commodity price risk through the use of financial derivatives. The Company recognizes the fair value of its derivative instruments as assets or liabilities on the balance sheet. None of the Company's commodity price derivates currently qualify as fair value hedges or cash flow hedges, and accordingly, changes in their fair value are recognized in net income.

The Company had the following commodity price risk management contracts outstanding:

Assets as of September 30, 2010

Instrument	Term	Volume	Floor/Ceiling ($/bbl)	Benchmark	Fair value
Zero cost collars	Oct 1, 2010 - Dec 31, 2010	525,000	75/102	WTI	$ 528
Zero cost collars	Jan 1, 2011- Mar 31, 2011	525,000	75/100	WTI	987
	Total	**1,050,000**			**$ 1,515**

14. FINANCIAL RISK MANAGEMENT (continued)

Liabilities as of September 30, 2010

Instrument	Term	Volume	Floor/Ceiling ($/bbl)	Benchmark	Fair value
Zero cost collars	Oct 1, 2010 - Dec 31, 2010	525,000	65/88	WTI	$ (432)
Zero cost collars	Oct 1, 2010 - Dec 31, 2010	525,000	65/88	WTI	(420)
Zero cost collars	Oct 1, 2010 - Dec 31, 2010	525,000	65/88	WTI	(414)
Zero cost collars	Jan 1, 2011- Dec 31, 2011	1,842,000	70/98	WTI	(967)
Zero cost collars	Jan 1, 2011- Dec 31, 2011	1,842,000	70/98	WTI	(888)
Zero cost collars	Jan 1, 2011- Dec 31, 2011	1,842,000	70/98	WTI	(1,060)
Zero cost collars	Apr 1, 2011- Dec 31, 2011	2,070,000	75/102	WTI	(6,909)
Zero cost collars	Apr 1, 2011- Dec 31, 2011	2,739,000	70/98	WTI	(2,153)
	Total	**11,910,000**			**(13,243)**

Instrument	Term	Volume	Strike Price ($/bbl)	Benchmark	Fair value
Call option	Nov 1, 2010 - Nov 30, 2010	166,667	89.50	WTI	$ (105)
Call option	Dec 1, 2010 - Dec 31, 2010	300,000	95.30	WTI	(221)
	Total	**466,667**			**(326)**

Instrument	Term	Volume	Strike Price ($/bbl)	Premium ($/bbl)	Fair value
Put option	Oct 1, 2010 - Dec 31, 2010	300,000	40	2.45	(735)
Put option	Oct 1, 2010 - Dec 31, 2010	292,500	40	1.91	(558)
Put option	Jan 1, 2011 - Jul 31, 2011	700,000	40	2.45	(1,664)
Put option	Jan 1, 2011 - Jun 30, 2011	585,000	40	1.91	(1,086)
	Total	**1,877,500**			**(4,043)**
	Total				**$ (17,612)**
	Short-term				(11,868)
	Long-term				(5,744)
	Total				**$ (17,612)**

14. FINANCIAL RISK MANAGEMENT (continued)

As of December 31, 2009

Type of Instrm.	Term	Volume	Strike Price ($/bbl)	Benchmark	Fair value
Call option	Jan 1, 2010 - Feb 28, 2010	300,000	80.0	WTI	$ (805)
Call option	Mar 1, 2010 - Apr 30, 2010	300,000	76.1	WTI	(2,577)
Call option	May 1, 2010 - May 31, 2010	152,000	80.0	WTI	(1,238)
Call option	Jun 1, 2010 - Aug 31, 2010	504,000	90.0	WTI	(2,844)
Call option	Sep 1, 2010 - Nov 30, 2010	500,001	89.5	WTI	(4,022)
Call option	Jan 1, 2010 - May 31, 2010	785,000	80.0	WTI	(4,111)
Call option	Jun 1, 2010 - Jul 30, 2010	304,000	80.0	WTI	(2,956)
	Total	**2,845,001**			**(18,553)**

Type of Instrm.	Term	Volume	Strike Price ($/bbl)	Premium ($/bbl)	Fair value
Put option	Jan 1, 2010 - Apr 30, 2010	600,000	40	$1.16	$ 1
Put option	May 1, 2010 - Jun 30, 2010	300,000	40	$1.95	(547)
Put option	Jul 1, 2010 - Dec 31, 2010	600,000	40	$2.45	(1,228)
Put option	Jan 1, 2010 - Jun 30, 2010	900,000	40	$1.41	(1,223)
Put option	Jan 1, 2010 - Jun 30, 2010	900,000	40	$1.28	(1,106)
Put option	Jul 1, 2010 - Dec 30, 2010	585,000	40	$1.91	(882)
Put option	Jan 1, 2011 - Jul 30, 2011	700,000	40	$2.45	(1,097)
Put option	Jan 1, 2011 - Jun 30, 2011	585,000	40	$1.91	(623)
	Total	**5,170,000**			**(6,705)**
	Total				**$ (25,258)**
	Short-term				$ (23,538)
	Long-term				(1,720)
	Total				**$ (25,258)**

For the three and nine months ended September 30, 2010, the Company recorded losses of $10.6 million and $0.5 million respectively (September 30, 2009 - $7.3 million in gain and $15.4 million in losses respectively) on commodity price risk management contracts in net income. Included in these amounts were $9.5 million of unrealized losses and $9.2 million of unrealized gains (September 30, 2009 - $7.3 million in gain and $15.4 million in losses) representing the change in the fair value of the contracts, and $1.1 million and $9.6 million of realized losses (Septemeber 30, 2009 - $0.3 million loss and $0.4 million gain). The fair value of the contracts includes any deferred premiums outstanding as of the period.

If the forward WTI crude oil price estimated at September 30, 2010 had been $1/bbl higher or lower, the unrealized loss on these contracts would change by approximately $1.5 million (2009 – $1.7 million) and would be reflected in the statement of operations of the Company.

(f) Fair value risk

The Company's financial instruments are cash and cash equivalents, restricted cash, accounts receivable and accounts payable and accrued liabilities, risk management assets and liabilities, bank debt and convertible debentures on the balance sheet. The carrying value and fair value of these financial instruments is disclosed below by financial instrument category, as well as any related gain (loss) and interest income (expense).

14. FINANCIAL RISK MANAGEMENT (continued)

	As at September 30,		For the three months ended September 30, 2010		For the Nine months ended September 30, 2010	
Financial Instrument	**Carrying value**	**Fair value**	**Gain (loss)**	**Interest income (expense)**	**Gain (loss)**	**Interest income (expense)**
Assets held for trading						
Cash and cash equivalents	618,150	618,150	-	589	-	1,143
Restricted cash	8,220	8,220	-	-	-	-
Loans and receivables						
Accounts receivable and other current assets	318,751	318,751	-	-	-	-
Derivatives designated as cash flow hedges						
Foreign currency hedges (1)	18,175	18,175	(4,700)	-	(5,716)	-
Assets held for trading						
Commodity price hedges (2)	1,515	1,515	1,515	-	1,515	-
Liabilities held for trading						
Commodity price hedges (2)	17,612	17,612	(12,154)	-	(1,992)	-
Other Liabilities						
Accounts payable and accrued liabilities	456,517	456,517	-	-	-	-
Long-term debt	434,648	490,080	-	(10,434)	-	(25,484)
Convertible debtentures (3)	177,946	434,188	-	(7,776)	-	(23,488)
Obligations under capital lease	39,697	39,697	-	(1,884)	-	(5,706)

(1) Loss represents the hedge ineffectiveness and time value of options recorded in net income as unrealized foreign exchange loss.

(2) Gains for the three and nine months ended September 30, 2010 included in these amounts were $9.5 million of unrealized losses and $9.2 million of unrealized gains (September 30, 2009 - $7.3 million in gain and $15.4 million in losses) representing the change in the fair value of the contracts, and $1.1 million and $9.6 million of realized losses (September 30, 2009 - $0.3 million loss and $0.4 million gain).

(3) The closing price of the convertible debenture (PRE.DB – TSX) at September 30, 2010 represented 244% of the face value of the convertible debenture (December 31, 2009 – 144%).

When drawn, bank debt bears interest at a floating rate and accordingly the fair value approximates the carrying value. Due to the short term nature of cash and cash equivalents, accounts receivable and other current assets, accounts payable and accrued liabilities, their carrying values approximate their fair values.

The following table summarizes the Company's financial instruments that are carried at fair value, in accordance with the classification of fair value input hierarchy included in CICA Handbook Section 3862, *Financial Instruments – Disclosures*.

	Fair value as at September 30, 2010			
	Level 1	**Level 2**	**Level 3**	**Total**
Risk management assets	$ -	$ 19,690	$ -	$ 19,690
Risk management liabilities	-	(17,612)	-	(17,612)
Total	$ -	$ 2,078	$ -	$ 2,078

14. FINANCIAL RISK MANAGEMENT (continued)

	Fair value as at December 31, 2009			
	Level 1	**Level 2**	**Level 3**	**Total**
Risk management liabilities	$ -	$ (25,258)	$ -	$ (25,258)
Total	$ -	$ (25,258)	$ -	$ (25,258)

The Company uses Level 2 inputs to measure the fair value of its risk management contracts. The fair values of these contracts are estimated using discounted cash flows based on quoted forward prices and quotes obtained from counterparties, taking into account the creditworthiness of those counterparties.

15. WEIGHTED AVERAGE SHARES AND FULLY DILUTED SHARES OUTSTANDING

	Three months ended September 30		Nine months ended September 30	
(in thousands)	2010	2009	2010	2009
Weighted average number of shares - basic	264,065,489	214,158,123	261,265,786	212,254,026
Dilution effect of stock options and warrants	31,538,329	-	24,944,293	-
Weighted average number of shares - diluted	295,603,818	214,158,123	286,210,079	212,254,026

All options, warrants and convertible debt that are anti-dilutive are excluded from the calculation of diluted weighted average number of shares.

16. SEGMENT DISCLOSURES

The Company currently has two reporting segments as at September 30, 2010, being the exploration, development and production of heavy crude oil and gas in Colombia, and the crude trading business as described in note 2c. Revenue and operating expenses for both segments are presented in the statement of operations. The crude trading segment does not have material assets and liabilities as at September 30, 2010.

As at September 30, 2010 all of the Company's assets are located in Colombia except for $229.4 million (December 31, 2009 - $224.6 million) in cash and cash equivalents which are held in Canada and the United States and $4 million (December 31, 2009 - $3.2 million) of property, plant and equipment in Peru. The crude trading business has no reportable assets and liabilities as at September 30, 2010.

The Company's revenues by geographical region for the period were as follows:

	Three months ended September 30		Nine months ended September 30	
	2010	2009	2010	2009
Colombia	$ 39,464	$ 51,674	$ 182,187	$ 120,652
North America	272,725	70,475	588,246	272,491
South America	48,140	34,408	48,140	34,408
Europe	45,092	-	117,370	-
Asia	-	-	135,846	-
Africa	-	-	73,855	-
	$ 405,421	$ 156,557	$ 1,145,644	$ 427,551

17. RELATED-PARTY TRANSACTIONS

a) In June 2007, the Company entered into a 5-year lease agreement with Blue Pacific, a British Virgin Islands corporation, for administrative office space in one of its Bogota, Colombia locations. Monthly rent expense of $55 is payable to Blue Pacific under this agreement. Three directors and officers of the Company control, or provide investment advice to the holders of, 75% of the shares of Blue Pacific. In addition, the Company has a receivable of $16 from Blue Pacific related to certain administrative costs paid by the Company on behalf of Blue Pacific.

b) As at September 30, 2010, the Company had trade accounts receivable of $1.7 million (December 31, 2009 - $10.5 million) from Proelectrica, in which the Company has a 21.7% indirect interest and which is 31.49% owned by Blue Pacific. The Company's and Blue Pacific's indirect interests are held through Ronter. Revenue from Proelectrica in the normal course of the Company's business was $2.3 million and $12.5 million for the three and nine months ended September 30, 2010 respectively (September 30, 2009 - $10.5 million and $5.9 million respectively).

c) During the three and nine months ended September 30, 2010, Transportadora Del Meta S.A. ("Transmeta"), a variable interest entity indirectly 100% owned by a director of the Company, paid a dividend of $1.3 million and $3.5 million respectively to its shareholder. The Company does not own any shares in Transmeta, but is the primary beneficiary and therefore consolidates Transmeta. The Transmeta dividend is included in other expense on the statement of operations.

d) The Company has an accounts receivable in the amount of $127 (December 31, 2009 - $173) from Medoro Resources Ltd., a company related by way of a director and one officer in common. The receivable balance is related to the Company's share of general and office expenses, including administrative support and office premises in Canada. This amount was repaid in full in October 2010.

e) Loans receivable in the aggregate amount of $481 (December 31, 2009 – $290) are due from two directors and four officers (December 31, 2009 – two officers) of the Company. The loans are non-interest bearing and payable in equal monthly payments over 48-month terms.

f) On April 19, 2010, the Company acquired a 9.4% interest in PII, a company that was previously fully owned by Ronter, for $3.5 million. In September 2010, the Company acquired an additional 4% interest in PII for $2 million from an unrelated party (see note 4).

g) During the three months ended September 30, 2010, the Company acquired a 19.05% interest in Pacific Coal, a company controlled by Blue Pacific, for $24 million. Four directors and one officer of the Company are also directors of Pacific Coal (see note 4).

All these transactions are measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties.

18. SUBSEQUENT EVENTS

a) Subsequent to September 30, 2010, the Company issued letters of credit and guarantees for exploration and operational commitments for a total of $230.5 million.

b) On October 18, 2010, the Company announced that it has executed a farm-in agreement with Flamingo Energy Investment (BVI) Ltd., Chx Guatemala Limitada, and Compañia Petrolera del Atlantico, S.A., through which the Company will earn-in a 55% participating interest, as well as operatorship, in the "7-98" contract in the Republic of Guatemala. Under the agreement, the Company is required to execute agreed-upon activities related to seismic data, geological and geophysical studies, and the drilling of an exploratory well, for a total commitment of $22.2 million.

19. COMPARATIVE FINANCIAL STATEMENTS

The comparative consolidated financial statements have been reclassified from statements previously presented to conform to the presentation of the current consolidated financial statements.

The Company has presented its joint operations on a gross basis from the proportionate consolidate basis in prior periods. As a result, the Company has reclassified its cash and restricted cash, accounts receivable, income tax receivable and payable, and accounts payable to their gross amounts.