

GUARDIAN EXPLORATION INC.

Management's Discussion & Analysis

As at December 31, 2008 for the Year Ended
December 31, 2008

MANAGEMENT'S DISCUSSION AND ANALYSIS

The following management discussion and analysis ("MD&A") of financial conditions and results of operations is as of April 28, 2009 and should be read in conjunction with the audited consolidated financial statements of Guardian Exploration Inc. ("Guardian" or the "Company") for the years ended December 31, 2008 and 2007. There has been no comparison provided for the fourth quarter of 2008's operating results to the fourth quarter of 2007's operating results due to the fact that the Company was largely inactive from an operational perspective during the fourth quarter of 2007. As a result this comparison was not considered to be meaningful. Additional information relating to the Company can be found on the SEDAR website at www.sedar.com.

Discussion with regard to Guardian's 2009 outlook 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.

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 June 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

2008 was an eventful year for Guardian as the Company raised \$6 million in common share capital and warrants in a variety of issuances throughout the first half of the year, spending the majority of these funds on the drilling, completing, and equipping of 3 (net 1.6) successful oil wells in the Girouxville area of Alberta (via a farm-in agreement with Breaker Energy Inc. signed in late 2007), with the balance of the funds spent largely on existing assets in the Kotcho Lake area in northern B.C., including the construction of a pipeline and separator to tie in the Company’s existing wells in the area to an adjacent dehydration facility from the facility that ceased accepting third party gas in the first quarter of 2007, thereby allowing Guardian’s Kotcho Lake wells to begin producing gas again.

These efforts allowed the Company to greatly increase its revenue and cash flows during the first nine months of the year as the combination of strong initial production, high commodity prices and royalty holidays provided the Company with over \$3 million in funds flow from operations, reducing the Company’s working capital deficiency in the process. Unfortunately the fourth quarter of 2008 saw a number of negative factors, including a sharp decrease in commodity prices, reduced production from the Company’s gas wells and an increase in royalties arising from a retroactive reclassification in 2009 of one of the three Girouxville area wells, combine to produce a more modest funds flow from operations result for the quarter, conditions that have continued into the first quarter of 2009.

As a result of these conditions and the continued weakness in the equity markets, the board of directors has approved a decision by management to engage an agent to commence the sale of substantially all of the Company’s property and equipment. With the sale of these assets in 2009, the Company hopes to eliminate its working capital deficiency and be able to satisfy its remaining spending obligations under the 2008 flow-through share issuance.

SELECTED INFORMATION

	Year Ended December 31	
	2008	2007
Petroleum and natural gas revenue, before royalties	\$7,133,555	\$777,004
Funds flow from (used in) operations	\$3,548,396	(\$3,048,772)
Funds flow from (used in) operations per share - basic	\$0.10	(\$0.15)
Funds flow from (used in) operations per share - diluted	\$0.10	(\$0.15)
Net loss	(\$1,902,672)	(\$1,704,270)
Net loss per share - basic	(\$0.05)	(\$0.08)
Net loss per share - diluted	(\$0.05)	(\$0.08)
Capital expenditures	\$5,904,341	\$2,256,328
Working capital deficit	(\$1,335,143)	(\$3,934,186)
Total Assets	\$7,160,816	\$5,496,057
Production (boe/d)	250	34

RESULTS OF OPERATIONS

PRODUCTION

	Year Ended December 31	
	2008	2007
Production		
Crude oil (bbl/d)	151	28
Natural gas (Mcf/d)	593	37
Oil equivalent production (boe/d)	250	34

The increase in crude oil production is attributed primarily to three wells in the Girouxville area that were completed and placed on production in 2008 under the farm-in agreement with Breaker. The three wells produced an average of 118 boe/day during the year. Aside from this, the Company's Montana Cutbank field produced 33 boe/day during the year compared to 28 boe/day in 2007, with the increase arising from well productivity improvement initiatives undertaken by the Company.

Guardian's gas production was significantly impacted for most of 2007 and the first quarter of 2008 after the producing Kotcho field was shut-in after January 2007 due to third party processing capacity restrictions and the well remained shut-in until April 2008 when a 100% owned natural gas pipeline was constructed and put into service to transport the Kotcho wells' production to a third party processing facility. The average production of 593 Mcf/day in 2008 was achieved from two wells during this eight-month period following the April start-up. The Company's independent reserve engineers have determined that these two wells no longer have any economic proven reserves at December 31, 2008 and in February 2009 they were shut-in due to uneconomic conditions.

PRICING

Benchmark Prices

	Year Ended December 31	
	2008	2007
Crude oil – WTI (US\$ per Bbl)	\$99.57	\$72.27
Crude oil – Edmonton Par Price (\$ per Bbl)	\$103.26	\$77.78
Natural gas – AECO Spot (\$/Mcf)	\$8.16	\$6.45
Exchange rate (\$US/\$Cdn)	1.067	0.93

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 dollars exchange rate and local demand and supply influences. For the year ended December 31, 2008, crude oil prices averaged US\$99.57 per barrel for WTI and \$103.26 per barrel at Edmonton as global political instability and concerns regarding crude oil supply levels pushed global oil prices to historical highs in mid-2008, but these conditions reversed course in the latter half of 2008, culminating with the oil price for December 2008 averaging US\$41.02 per barrel for WTI and \$42.43 per barrel at Edmonton

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 \$8.18/Mcf for the for the year ended December 31, 2008 with natural gas prices exceeding \$10.00/Mcf in July 2008, but decreasing in the latter half of 2008, averaging \$7.17/Mcf during December 2008.

Realized Prices

	Year Ended December 31	
	2008	2007
Average Prices		
Crude oil (\$/bbl)	\$98.96	\$66.77
Natural gas (\$/Mcf)	\$7.57	\$6.74
Oil equivalent (\$/boe)	\$77.82	\$61.36

Guardian's average realized price for its crude oil at Girouxville was \$100.76/barrel for the year ended December 31, 2008 with no corresponding oil production for the same period in 2007. Guardian's average realized price for its crude oil at Cutbank, Montana was US\$86.76/barrel for the year ended December 31, 2008 compared to US\$71.80/barrel for the same period in 2007. For the year-ended December 31, 2008 the Company's average realized price for its natural gas was \$7.57/Mcf, which was achieved in the last eight months of the year, compared to \$6.74/Mcf realized for the year-ended December 31, 2007, which latter period only represented production during the first month of 2007 after which the Kotcho field was shut-in due to third party capacity restrictions.

REVENUES

	Year Ended December 31	
	2008	2007
Production Revenue		
Crude oil	\$5,489,739	\$686,727
Natural gas	\$1,643,816	\$90,277
Total production revenue	\$7,133,555	\$777,004

The increase in crude oil revenue is a result of \$4,385,249 in new oil sales from the Company's three Girouxville area wells drilled under the Breaker farm-in agreement and brought on production in 2008 with crude oil sales from the Company's Montana Cutbank property increasing by \$417,762 in 2008, arising both from productivity improvements and price increases.

The increase in natural gas revenue is attributable to the increase in natural gas production following the Company's Kotcho property being shut-in as a result of third party processing restrictions from February 2007 to April 2008 until the construction of a 100% Company operated pipeline to another third party processing facility allowed the Kotcho property to begin producing again. Subsequent to year-end the two wells were shut-in due to uneconomic conditions. The Company's independent reserve engineers have since determined that these two wells no longer have any economic proven reserves at December 31, 2008. The third Kotcho area well remains shut-in pending the resolution of an appropriate pipeline fee arrangement with the 67.5% joint venture partner on the well.

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

ROYALTIES

	Year Ended December 31	
	2008	2007
Royalties	\$837,317	\$163,049
As a percentage of revenue	12%	21%

The decrease in royalty percentage from 2007 to 2008 is due to the fact that two of the Company's three wells at Girouxville qualified for the one year, \$1 million Alberta royalty holiday, which holiday limit was reached for one well in December 2008 and for the other expired in January 2009. The third well was believed to qualify for the royalty holiday throughout 2008, but in April 2009 the operator informed Guardian that the well was evaluated by

the regulatory authorities and that it did not qualify for the royalty holiday. As a result, the Company has accrued \$379,000 at December 31, 2008 for the Company's estimated share of retroactive 2008 royalties that will be owed to the operator. In addition, as a result of the Company obtaining its own BC Oil and Gas Commission (OGC) facility number for its Kotcho facility, in April 2009 the BC regulatory authorities have had to calculate the appropriate Producer Cost of Sales (PCOS) allowance for Guardian's OGC facility, as opposed to that allowance applicable under the OGC number of the processing facility that Guardian sold gas under until obtaining its own OGC number. As a result of a retroactive adjustment in the PCOS allowance rate for 2008, the Company has accrued \$103,000 as at December 31, 2008 for the additional crown royalties owed on the Kotcho wells in 2008. The Company's royalties as a percentage of sales on its Cutbank, Montana production remained consistent with 2007 levels.

On October 25, 2007, the Alberta government announced the New Royalty Framework that will come into effect on January 1, 2009, which was in response to the Alberta Royalty Review Panel's recommendations announced on September 18, 2007. As a result of the higher royalty rates applicable under this framework and the fact that all Girouxville wells are now off of the royalty holiday, the Company expects a significant increase in the royalties as a percentage of sales in 2009. Subsequent to year-end, the two Kotcho producing gas wells were shut-in due to uneconomic conditions; conditions that the Company does not foresee improving materially in the future, especially given the increased royalty rate environment applicable for these wells.

OPERATING EXPENSES

	Year Ended December 31	
	2008	2007
Operating expenses	\$1,809,047	\$420,535
Operating expenses per boe	\$19.74	\$33.89
As a percentage of petroleum and natural gas revenue	25%	54%

The decrease in operating costs per boe and as a percentage of revenue during the year ended December 31, 2008 is a result of the fact that the Girouxville wells, which comprised over 60% of the Company's sales in 2008 versus nil in 2007, have much lower operating costs relative to the Montana properties, which are older properties and have relatively low production per well resulting in higher per unit operating costs. Additionally, the Kotcho wells, although having high operating costs relative to the average gas well, still have much lower operating costs than the Montana oil properties, for which much of the 2007 comparative figure is based upon.

GENERAL AND ADMINISTRATIVE EXPENSES

	Year Ended December 31	
	2008	2007
General and administrative ("G&A") expenses	\$1,461,879	\$1,241,289
G&A per boe	\$15.95	\$100.30
As a percentage of petroleum and natural gas revenue	21%	160%

The increase in overall G&A expenses is due to the utilization of increased staffing, compensation and consulting levels in 2008 arising from the increased operational activities of the Company during the year, including increased professional fees required to deal with legal and regulatory matters and an overall increase in the cost of maintaining a publicly traded company. On a per boe and percentage of revenue basis the G&A expenses decreased considerably from 2007 levels due to the increased revenue base of the Company.

STOCK-BASED COMPENSATION

Stock-based compensation expense is the amortization over the vesting period of the 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. During the year ended December 31, 2008, the

Company issued 1,800,000 stock options. For the year ended December 31, 2008, stock-based compensation was \$517,794 as compared to the \$318,982 for the year ended December 31, 2007. The increase in stock-based compensation expense is a result of the increase in the numbers of options issued and the increased volatility of the Company's stock price in 2008 as compared to the same periods in 2007.

INTEREST EXPENSE

Interest and financing expense for the year ended December 31, 2008 was \$11,537 compared with \$390,319 for the year ended December 31, 2007. During 2007, the Company recorded \$382,500 in interest expense on the Part XII.6 tax associated with the issuance of the 2006 flow-through shares. During 2008 this amount was reduced by \$17,500 arising from a more accurate determination of the appropriate liability, which reduction served to partially offset the interest expense incurred on the debenture issuance in 2008, along with other interest expense.

DEPLETION, DEPRECIATION AND ACCRETION

	Year Ended December 31	
	2008	2007
Depletion and depreciation expense	\$2,902,515	\$128,125
Accretion expense	\$77,212	\$97,252
Impairment provision for oil and gas properties	\$2,740,000	\$427,490
Total	\$5,719,727	\$652,867

The increase in depletion is a result of higher production volumes in 2008 as compared with 2007 due to the three Girouxville area oil wells coming on production in January, March and July of 2008 and the two Kotcho area wells coming on production in April of 2008, whereas in 2007 the Kotcho wells were shut-in after January.

At December 31, 2008, the impairment recognition portion of the ceiling test on the Canadian properties indicated the estimated undiscounted future cash flows from proved reserves was less than the carrying amount of producing petroleum and natural gas properties. In the second stage of the AcG-16 impairment test, the discounted future cash flows from the proved plus probable reserves were compared to the carrying amount of the oil and gas properties to determine a ceiling test impairment. An impairment of \$1,740,000 was included in depletion, depreciation and amortization for the year ended December 31, 2008.

At December 31, 2008, an impairment provision of \$1,000,000 was recorded for the US undeveloped properties, arising from the fact that the Company received notification from the Blackfeet Nation during the year that the agreement related to these lands was terminated.

The Company follows the full cost method of accounting for its operations as described in the CICA's accounting guideline 16, "Oil and Gas Accounting - Full Cost". Accordingly, the cost of all wells, both successful and unsuccessful, are added to the Company's capital base and are depleted on the unit of production method based on estimated gross proved reserves at forecast prices and costs as determined by independent engineers and the Company's internal estimates. Costs of unproven properties, seismic and undeveloped land, net of impairments, are excluded from the depletion calculation and future capital costs associated with proved undeveloped reserves are included in the depletion calculation.

In recognizing an asset retirement obligation "ARO" associated with the retirement of a tangible long-lived asset, the Company records a liability in the period in which it is incurred and becomes determinable, with an offsetting increase in the carrying amount of the associated asset. The cost of the tangible asset, including the initially recognized ARO is depleted such that the cost of the ARO is recognized over the useful life of the asset. The ARO is recorded at fair value and accretion expense is recognized over time as the discounted liability is accreted to its expected settlement value.

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 total future value of its asset retirement obligations at December 31, 2008 is \$1,830,106. Current expenditures for actual abandonment and site restoration in the year ended December 31, 2008 were \$nil.

BAD DEBT EXPENSE

Bad debt recoveries for the year ended December 31, 2008 was \$279,440 as compared with a bad debt expense of \$1,629,695 for the year ended December 31, 2007. During 2007, two joint venture partners of the Company experienced financial difficulties and were unable to pay outstanding amounts due to the Company for joint venture operations operated by the Company. A \$289,299 payment from one of these customers was received during 2008.

TAXES

During the year ended December 31, 2008, the Company recorded a future income tax recovery of \$694,000 (2007 - \$1,200,000) arising from the recognition of a future income tax asset.

The Company paid no cash taxes during the years ended 2008 and 2007.

As of December 31, 2008, the Company has approximately \$10 million in Canadian tax pools available to offset future taxable income. In February 2009, the Company renounced \$1 million of CEE, thereby reducing these tax pools to approximately \$9 million.

NET LOSS AND COMPREHENSIVE LOSS

	Year Ended December 31	
	2008	2007
Net loss	(\$1,902,672)	(\$1,704,270)
Net loss - per basic share	(\$0.05)	(\$0.08)
Net loss - per diluted share	(\$0.05)	(\$0.08)
Weighted average shares outstanding - basic	34,691,134	20,079,422
Weighted average shares outstanding - diluted	34,691,134	20,079,422

For the years ended December 31, 2008 and 2007, 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 loss in the table below:

	Year Ended December 31	
	2008	2007
Net loss	(\$1,902,672)	(\$1,704,270)
Add back (subtract) items not effecting cash:		
Depletion, depreciation and accretion	\$5,719,727	\$652,867
Stock-based compensation	\$517,794	\$318,982
Foreign exchange loss (gain)	\$(92,453)	\$32,219
Loss on sale of property and equipment	-	\$351,893
Future income tax recovery	(\$694,000)	(\$1,200,000)
Income attributable to settlement of accounts payable	-	(1,500,463)
Funds flow from (used in) operations	\$3,548,396	(\$3,048,772)
Funds flow from (used in) operations - per share - basic	\$0.10	(\$0.15)
Funds flow from (used in) operations - per share - diluted	\$0.10	(\$0.15)

Due to the drilling program undertaken at Girouxville, the investment in pipeline and related assets at Kotcho Lake and the strong commodity markets in 2008 the Company was able to generate over \$3 million of funds flow from operations in 2008 compared to 2007 when the Company was largely inactive from a revenue standpoint and

incurred significant funds flow used in operations arising from royalties, operating and general and administrative expenses in excess of revenues combined with over \$1.6 million in bad debts expense.

SHARE CAPITAL

	Year Ended December 31	
	2008	2007
Outstanding common shares		
Weighted average outstanding common shares		
Basic	34,691,134	20,079,422
Diluted	34,691,134	20,079,422

Due to the anti-dilutive effect of Guardian's net loss for the years ended December 31, 2008 and 2007, the diluted number of shares is equivalent to basic number of shares.

Outstanding Securities	Outstanding at December 31	
	2008	2007
Common shares	39,737,877	20,079,422
Stock options	2,950,000	1,350,000
Warrants	8,871,300	-
Agent warrants	1,816,600	-
Debenture warrants	783,613	783,613

As of the date of this MD&A, there were 39,737,877 common shares issued and outstanding.

For the years ended December 31, 2008 and 2007, all outstanding stock options and warrants are anti-dilutive and have been excluded in calculating the diluted shares outstanding.

CAPITAL EXPENDITURES

	Year Ended December 31	
	2008	2007
Canada	\$5,844,341	\$1,278,838
United States	\$60,000	\$977,490
Total	\$5,904,341	\$2,256,328

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 its existing assets in the Kotcho Lake area in northern B.C., including the construction of a pipeline and separator to tie in the Company's existing wells in the area to an adjacent dehydration facility from the facility that ceased accepting third party gas in the first quarter of 2007, thereby allowing Guardian's Kotcho Lake wells to begin producing gas again.

LIQUIDITY AND CAPITAL RESOURCES

At December 31, 2008, the Company had no bank credit facility and had a working capital deficit of \$1,335,143. 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 the audited annual consolidated financial statements, and receiving the continuing financial support from its creditors. In 2009 Guardian engaged an agent to commence the sale of substantially all of the property and equipment assets of the Company. With the sale of these assets, the Company hopes to eliminate its working capital deficiency and be able to satisfy its remaining spending obligations under the 2008 flow-through share issuance.

The capital intensive nature of the Company's activities may create a negative working capital position in 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. During the year ended December 31, 2007, the Company experienced bad debts of \$1,629,695 due to joint venture partner's inability to pay the outstanding amounts due to the Company. During 2008, \$289,229 of this balance was recovered.

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.

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 therefrom are based upon a number of variable factors and assumptions, such as commodity prices, projected production from the properties, the assumed affects 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 therefrom, 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. At December 31, 2008, the Company incurred a \$1,740,000 ceiling test write-down on its Canadian properties and an additional \$1,000,000 write-down in its US properties.

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.

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 favourable 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 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. Under the new royalty framework, royalty rates will be increased on conventional oil, natural gas and the oil sands. The Government of Alberta estimates that the overall royalties will be increased by approximately \$1.4 billion over its previously estimated royalty revenues for 2010.

The implementation of the proposed changes to the royalty regime in Alberta is subject to certain risks and uncertainties. The significant changes to the royalty regime requires new legislation, changes to existing legislation and regulation and development of proprietary software to support the calculation and collection of royalties. An increase in the royalties payable by Guardian in addition to the costs of modifying the Corporation's existing infrastructure to deal with the changes to the royalty regime will result in higher costs to Guardian and therefore reduced profitability.

Related Party Transactions

The Company obtained helicopter services in conjunction with the servicing and drilling of natural gas wells in Northern B.C. from a company controlled by a major shareholder and officer of the Company, for which the Company was charged \$273,329 (2007 - \$136,147). The Company also recorded management fees of \$Nil (2007 - \$13,102) to the same company. All of these amounts were paid in 2008.

The Company obtained engineering consulting services in the amount of \$190,575 (2007 - \$Nil) from a company controlled by a Company director, who was appointed in 2008. Of this amount, \$180,729 is included in accounts payable and accrued liabilities at December 31, 2008 (2007 - \$Nil).

Legal fees in the amount of \$77,287 (2007 - \$64,310) have been charged by a legal firm of which a Company director, who was appointed in 2006, is a partner. Of this amount, \$4,358 is included in accounts payable and accrued liabilities at December 31, 2008 (2007 - \$6,195).

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 May and June 2008, the Company is committed to incur \$2,777,110 of qualified expenditures by December 31, 2009. At December 31, 2008, approximately \$1,000,000 of the obligation has been fulfilled. The costs were renounced to investors in February 2009.

b) Office lease obligation

The Company had a five year office lease agreement which expired on October 31, 2008. The Company extended this lease agreement for a six month period expiring April 30, 2009. The following table outlines the Company's estimated lease commitments over the life of the agreement:

	\$
2009	50,000

c) 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%.

GUARANTEES, CONTINGENCIES AND OFF-BALANCE SHEET ARRANGEMENTS

a) Flow-through shares

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. At December 31, 2007, \$2,150,000 of the obligation had been fulfilled. Subsequent to the 2007 year-end, the Company expended the remaining \$1,850,000 obligation.

Since the Company did not make the expenditures by December 31, 2007 as required under the income tax rules, the unexpended flow-through amount could be reassessed by the tax authorities and the Company could potentially be liable for investor income taxes and penalty interest thereon of approximately \$950,000 if an arrangement cannot be made to remedy this contingency.

Notwithstanding, 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 for estimated Part XII.6 interest and penalties in the amount of \$365,000.

b) Litigation

During 2008, the Company was named as a defendant in a lawsuit in which a company that signed a farmout agreement regarding one of the Company's operated wells in Northern BC (the "Plaintiff") is

claiming, amongst other things, that it 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 is claiming that it earned its 100% working interest upon completion of the well and that the remaining amounts due by it, which amounts it contests, can 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 claims that it is entitled to a declaration that it earned and should recover 100% of the net production revenues on the basis that, it alleges, the Company was negligent in exceeding the AFE estimates for drilling and completion of the well. The Plaintiff also claims, 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.

The Plaintiff is seeking various remedies in its statement of claim including:

- a declaration that it earned a 100% BPO interest subject to the Company's 15% gross overriding royalty which is convertible to a 50% working interest after pay out (“APO”);
- damages in the amount of \$1,050,000, or
- the return of all or a portion of the \$2.1 million in funds advanced by the Plaintiff on the basis of a claim for unjust enrichment.

At December 31, 2008, the Company has recorded the \$688,000 in costs incurred to complete this well and allow it to be able to produce as property and equipment and has included these costs within its depletion calculation. For the year-ended December 31, 2008 the Company has recorded \$241,000 in net revenues from this well, after royalties and operating costs, but before depletion expense. The gas well was shut-in subsequent to December 31, 2008 due to uneconomic conditions. The well has been determined by the Company’s independent reserve engineers to no longer have any economic proven reserves at December 31, 2008.

The Company is vigorously defending this lawsuit and is seeking in its statement of defence to have the Court determine that the Plaintiff forfeited any interest in this well by virtue of its failure to fulfill its obligation under the farmout agreement to pay 100% of the costs to drill and complete the well. The Company's Statement of Defence seeks, in the alternative, full payment by the Plaintiff of the \$688,000 not paid by the Plaintiff, plus a penalty of 300% of this amount in accordance with Canadian Association of Petroleum Landmen (CAPL) industry standards, before the Plaintiff earns a 100% BPO interest in this well. The Company denies that it has ever received any funding from the Plaintiff for the pipeline or that the Plaintiff has any interest in the pipeline.

If it is ultimately determined by a Court that the Plaintiff has in fact earned an interest in this well, subject to their payment of outstanding amounts, a position that the Company denies, the result of this will effectively be the same from a financial statement perspective as the Company’s present accounting treatment. That result being that the resulting accounts receivable of \$688,000 for capital costs incurred by the Company in excess of the Plaintiff’s funding is still owed by the Plaintiff and that only \$241,000 of earnings from the well have been achieved during 2008, leaving a shortfall of \$447,000, for which, based on the Company’s reserve report information, there will be no future recovery possibilities from this well’s earnings. Consequently, the Company would continue to carry the Plaintiff's payment obligation in accounts receivable. As the Plaintiff has no other material assets in Alberta the accounts receivable from the Plaintiff of \$447,000 would, in accordance with Generally Accepted Accounting Principles, have to be allowed and provided for as a bad debt expense versus the present accounting treatment wherein additional depletion expense has been recognized for this \$447,000 amount arising from the application of the ceiling test explained in note 7 to the audited financial statements.

c) Mineral Management Services

The Mineral Management Service (“MMS”), a bureau of the US Department of the Interior that manages that nation's natural gas and oil resources, alleged during the year that a subsidiary of the Company had been deficient in various administrative filing requirements in the past and that, as a result, civil penalties

of approximately \$611,500 (US\$500,000) were being levied against the subsidiary. The subsidiary is disputing these penalties and, along with its legal counsel, has been negotiating with MMS, its collection agencies and its counsel towards a satisfactory resolution of this matter.

A provision of \$45,863 (US\$37,500) has been made for these civil penalties. This provision has been based on a probationary settlement arrangement with MMS, which has yet to be finalized, but has been agreed to in principle for a portion of these penalties still within MMS's jurisdiction, representing approximately 80% of the total amounts at issue, with the balance of the penalties no longer in MMS's jurisdiction the subject of an equivalent settlement offer by the subsidiary to the collection agencies involved.

The probationary settlement arrangement with MMS involves a total repayment of \$36,690 (US\$30,000) in equal monthly installments over 36 months, plus interest, and requires that the subsidiary remains compliant with its payment and reporting requirements over this time frame, otherwise the full amount of the penalties, reduced on a declining basis for the period of compliance, will be owing to MMS. The Company believes that this settlement arrangement will be acceptable to all parties and further that the proportionate settlement offer made to the collection agencies will be acceptable to them.

FUTURE ACCOUNTING PRONOUNCEMENTS

In February 2008, the CICA issued Section 3064, Goodwill and Intangible Assets. Various changes have been made to other sections of the CICA Handbook for consistency purposes. This section establishes standards for the recognition, measurement, presentation and disclosure of goodwill subsequent to its initial recognition and of intangible assets by profit-oriented enterprises. The new Section is applicable to financial statements relating to fiscal years beginning on or after October 1, 2008. Accordingly, the Company will adopt the new standard for its fiscal year beginning January 1, 2009. The adoption of the new section does not have a significant impact on the Company's financial statements.

In January 2009, the CICA issued new accounting standards, Section 1582 Business Combinations and Section 1601 Consolidated Financial Statements, replacing Section 1501 Business Combinations and Section 1600 Consolidated Financial Statements. The CICA also issued new Section 1602 on Non-Controlling Interests. Section 1582 establishes standards for accounting for a business combination. Section 1601 establishes standards for the preparation of consolidated financial statements. Section 1602 establishes standards for accounting for a non-controlling interest in a subsidiary in consolidated financial statements subsequent to a business combination. These new standards become effective for the Corporation's fiscal year beginning on January 1, 2011 and earlier adoption of all three Sections concurrently is permitted. The adoption of these new sections does not have a significant impact on the Company's financial statements.

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., 550, 435 – 4th Avenue S.W., Calgary, Alberta, T2P 3A8.

GUARDIAN EXPLORATION INC.

Consolidated Financial Statements

December 31, 2008 and 2007



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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, 2008 and the consolidated statements of loss, comprehensive loss and deficit and cash flows for year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit 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, 2008 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

The consolidated financial statements as at and for the year ended December 31, 2007 were audited by another firm of Chartered Accountants which expressed an opinion without reservation on these financial statements in their report dated May 23, 2008.

A handwritten signature in black ink that reads "Deloitte & Touche LLP".

April 23, 2009 except as to note 19(d), which is as of April 28, 2009

Chartered Accountants

**GUARDIAN EXPLORATION INC.
CONSOLIDATED BALANCE SHEETS**

As of December 31

	2008	2007
	\$	\$
ASSETS		
Current assets		
Cash	693,056	72,026
Accounts receivable (note 4)	404,248	1,376,500
Due from related company (notes 5 and 19(d))	449,951	-
Prepaid expenses	50,640	54,615
	<u>1,597,895</u>	<u>1,503,140</u>
Deposit (note 6)	438,380	345,825
Future income taxes (note 11)	694,000	-
Property and equipment (note 7)	4,430,541	3,647,091
	<u>7,160,816</u>	<u>5,496,057</u>
LIABILITIES AND SHAREHOLDERS' EQUITY (DEFICIT)		
Current liabilities		
Accounts payable and accrued liabilities	2,933,038	4,739,267
Due to related company (note 5)	-	451,967
Due to shareholder (note 9)	-	246,092
	<u>2,933,038</u>	<u>5,437,326</u>
Asset retirement obligations (note 10)	1,161,783	876,947
	<u>4,094,821</u>	<u>6,314,273</u>
Going Concern, Commitments and Contingencies (notes 1, 14 & 16)		
Shareholders' equity (deficiency)		
Share capital (note 12)	11,021,365	6,903,838
Warrants (note 12)	1,618,440	673,600
Contributed surplus (note 12)	1,603,505	878,990
Deficit	(11,177,315)	(9,274,643)
	<u>3,065,995</u>	<u>(818,215)</u>
	<u>7,160,816</u>	<u>5,496,057</u>

See accompanying notes to the consolidated financial statements

Approved on behalf of the Board of Directors

Graydon Kowal
Director

Scott Reeves
Director

GUARDIAN EXPLORATION INC.
CONSOLIDATED STATEMENTS OF LOSS, COMPREHENSIVE LOSS AND DEFICIT
FOR THE YEARS ENDED DECEMBER 31, 2008 AND 2007

	2008	2007
	\$	\$
Revenue		
Petroleum and natural gas	7,133,555	777,004
Royalties	(837,317)	(163,049)
Interest income	19,922	19,112
	<u>6,316,160</u>	<u>633,066</u>
Expenses		
Operating	1,809,047	420,535
General and administrative	1,461,879	1,241,289
Bad debts (recovery) (note 4)	(279,440)	1,629,695
Interest and financing fees	11,537	390,319
Stock-based compensation (note 12)	517,794	318,982
Depletion, depreciation, impairment and accretion (notes 7 and 10)	5,719,727	652,867
Foreign exchange (gain) loss	(85,712)	32,219
	<u>9,154,832</u>	<u>4,685,906</u>
Loss from operations	(2,838,672)	(4,052,840)
Loss on sale of property and equipment (note 7)	-	351,893
Settlement of accounts payable (note 12)	(242,000)	(1,500,463)
Loss before income taxes	(2,596,672)	(2,904,270)
Future income tax recovery (note 11)	(694,000)	(1,200,000)
Net loss and comprehensive loss	(1,902,672)	(1,704,270)
Deficit, beginning of year	(9,274,643)	(7,570,373)
Deficit, end of year	<u>(11,177,315)</u>	<u>(9,274,643)</u>
Net loss per share (note 12)		
Basic	(\$0.05)	(\$0.08)
Diluted	(\$0.05)	(\$0.08)

See accompanying notes to the consolidated financial statements

**GUARDIAN EXPLORATION INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2008 AND 2007**

	2008	2007
	\$	\$
Cash and cash equivalents provided by (used in)		
Operating activities		
Net loss	(1,902,672)	(1,704,270)
Items not effecting cash:		
Depletion, depreciation, impairment and accretion	5,719,727	652,867
Stock-based compensation	517,794	318,982
Foreign exchange (gain) loss	(92,453)	32,219
Future income tax recovery	(694,000)	(1,200,000)
Loss on sale of property and equipment	-	351,893
Settlement of accounts payable	-	(1,500,463)
	3,548,396	(3,048,772)
Changes in non-cash working capital items (note 13)	(534,285)	162,895
	3,014,111	(2,885,877)
Financing activities		
Debenture issued (note 8)	400,000	-
Debenture repaid (note 8)	(400,000)	(1,000,000)
Advances from (payments to) related company	(901,918)	75,666
Issuance of share capital	4,765,685	-
Issuance of warrants	944,840	-
Share issue costs	(575,712)	-
Advances from (payments to) shareholder	(246,092)	108,092
Changes in non-cash working capital items (note 13)	-	(100,836)
	3,986,803	(917,078)
Investing activities		
Expenditures on property and equipment	(5,904,341)	(2,256,778)
Proceeds on sale of property and equipment	-	6,500,000
Change in non-cash working capital items (note 13)	(475,543)	(469,797)
	(6,379,884)	3,773,425
Change in cash	621,030	(29,530)
Cash, beginning of year	72,026	101,556
Cash, end of year	693,056	72,026
Supplemental cash flow information (note 13)		

See accompanying notes to the consolidated financial statements

**GUARDIAN EXPLORATION INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEARS ENDED DECEMBER 31, 2008 AND 2007**

1. GOING CONCERN

These consolidated financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles and accordingly, have been prepared using the same principles as those for a going concern. As at December 31, 2008, the Company had a working capital deficiency of \$1,335,143 and an accumulated deficit of \$11,177,315. Should the Company be unsuccessful in realizing 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.

In 2008 the global credit market crisis, volatility in the price of oil and natural gas, the recession in North America and the slowdown of economic growth in the rest of the world has created a substantially more volatile business environment. The conditions will limit certain of the Company's previously planned business development activities and will continue to provide uncertainty for the Company in the future.

The Company'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 will, largely, depend on its continued ability to finance the development of existing projects and finance the acquisition and development of new projects in the next year, including the proceeds realized from the divestiture of its petroleum and natural gas property and equipment (see subsequent events note 19).

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.

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 June 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) Consolidation

These consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries, K2 America Corp. and K2 Operating Corp. They 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) Basis of presentation

The Company's financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles. The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and reported amounts of revenue and expenses during the period. Actual results could differ from these estimates.

**GUARDIAN EXPLORATION INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEARS ENDED DECEMBER 31, 2008 AND 2007**

c) 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.

d) 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.

**GUARDIAN EXPLORATION INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEARS ENDED DECEMBER 31, 2008 AND 2007**

e) 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.

f) 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.

g) 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.

h) 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.

i) 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.

j) 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.

k) 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.

**GUARDIAN EXPLORATION INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEARS ENDED DECEMBER 31, 2008 AND 2007**

l) 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.

m) 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.

**GUARDIAN EXPLORATION INC.
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEARS ENDED DECEMBER 31, 2008 AND 2007**

n) 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.

At January 1, 2008 and December 31, 2008, 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, due to related company, due to shareholder and convertible debenture are designated as “other financial liabilities” and are initially measured at fair value and subsequently at amortized cost using the effective interest rate method.

o) Hedges

The Company currently does not utilize hedges or other derivative financial instruments in its operations, and as a result, the adoption of CICA Section 3865 had no impact on the financial statements of the Company.

Changes in Accounting Policies

CICA Section 1535, “Capital Disclosures” is effective for annual periods beginning on or after October 1, 2007 and established standards for disclosing information about the Company’s capital and how it is managed. It requires disclosures of the Company’s objectives, policies and processes for managing capital, the quantitative data about what the Company regards as capital, whether the Company has complied with any capital requirements and if it has not complied, the consequences of such non-compliance. The Company adopted this standard effective January 1, 2008.

CICA Section 1400, “General Standards of Financial Statements” is effective January 1, 2008, and requires management to make an assessment of the Company’s ability to continue as a going concern, and to disclose any material uncertainties related to events or conditions that may cast significant doubt upon the entity’s ability to continue as a going concern.

CICA Section 3862 – “Financial Instruments – Disclosures” describes the required disclosure for the assessment of the significance of financial instruments for an entity’s financial position and performance and of the nature and extent of risks arising from financial instruments to which the entity is exposed and how the entity manages those risks. This section and Section 3863, Financial Instruments – Presentation” replaced Section 3861, “Financial Instruments – Disclosure and Presentation” (see note 18).

CICA Section 3863 – “Financial Instruments – Presentation”, establishes standards for presentation of financial instruments and non-financial derivatives (see note 18).

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Future Accounting Pronouncements

In February 2008, the CICA issued Section 3064, Goodwill and Intangible Assets. Various changes have been made to other sections of the CICA Handbook for consistency purposes. This section establishes standards for the recognition, measurement, presentation and disclosure of goodwill subsequent to its initial recognition and of intangible assets by profit-oriented enterprises. The new Section is applicable to financial statements relating to fiscal years beginning on or after October 1, 2008. Accordingly, the Company will adopt the new standard for its fiscal year beginning January 1, 2009. The adoption of the new section is not expected to have a significant impact on the Company's financial statements.

In January 2009, the CICA issued new accounting standards, Section 1582 Business Combinations and Section 1601 Consolidated Financial Statements, replacing Section 1501 Business Combinations and Section 1600 Consolidated Financial Statements. The CICA also issued new Section 1602 (on-Controlling Interests. Section 1582 establishes standards for accounting for a business combination. Section 1601 establishes standards for the preparation of consolidated financial statements. Section 1602 establishes standards for accounting for a non-controlling interest in a subsidiary in consolidated financial statements subsequent to a business combination. These new standards become effective for the Corporation's fiscal year beginning on January 1, 2011 and earlier adoption of all three Sections concurrently is permitted. The adoption of these new sections are not expected to have a significant impact on the Company's financial statements.

International Financial Reporting Standards

The Accounting Standards Board has confirmed the convergence of Canadian GAAP with International Financial Reporting Standards ("IFRS") will be effective January 1, 2011. We are currently assessing the impact of the convergence of Canadian GAAP with IFRS on our results of operations, financial position and disclosure.

4. ACCOUNTS RECEIVABLE

- a) In 2008, the Company entered into a settlement agreement with a joint venture partner that owed the Company \$1,487,255 for joint venture operations. The settlement agreement included a cash payment of \$150,000 and an undivided working interest in an unproven property with no identifiable value. As a result of this agreement, the remaining outstanding balance of \$1,337,255 was included as bad debt expense in the Company's 2007 financial statements.
- b) During 2008 the Company recovered \$289,299 from a joint venture partner for an accounts receivable that was provided for as a bad debt expense during 2007.

5. DUE FROM RELATED COMPANY / DUE TO RELATED COMPANY

Amounts owed by and owing to a company related by common management are unsecured, bear no interest, and have no fixed terms of repayment (Note 19(d)).

6. DEPOSIT

As part of the finalization of the Third Amended Agreement with the Blackfeet Nation, the Company has placed a deposit of \$438,380 (USD\$ 360,000) (2007 - \$345,825; USD \$340,000), 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.

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7. PROPERTY AND EQUIPMENT

	2008	2007
	\$	\$
Petroleum and natural gas properties and equipment	16,952,474	10,526,510
Accumulated depletion and depreciation and impairment	(12,521,933)	(6,879,419)
	4,430,541	3,647,091

Canadian cost center

For the years ended December 31, 2008 and 2007, there were no capitalized general and administrative expenses.

Unproven property costs of \$40,000 (2007 - \$1,148,000) have been excluded from capitalized costs subject to depletion.

In January 2007, the Company disposed of certain petroleum and natural gas properties for cash consideration of \$6,500,000. A portion of the Canadian full cost pool was allocated to the sale of the property in accordance with AcG-16. As a result of the allocation, the Company recorded a loss on the disposal in the amount \$351,893.

The Company performed a ceiling test calculation as at December 31, 2008 to assess the recoverable amount of the petroleum and natural gas properties. The oil and natural gas future prices are based on the December 31, 2008 commodity price forecast of the Company's independent reserve engineers, adjusted for the Company's price and quality differentials, as outlined in the following table. Based on these assumptions, the carrying value of the petroleum and natural gas properties as at December 31, 2008 exceeded the discounted value of future net revenues from the Company's estimated proved and probable reserves and a \$1,740,000 impairment amount was included in depletion, depreciation, impairment and accretion expense.

The following table outlines the benchmark prices used in the ceiling test calculation at December 31, 2008:

	Crude Oil	Natural Gas
	Edmonton Ref. Price	B.C. Spot Price
	(Cdn\$/bbl)	(Cdn\$/mmbtu)
2009	\$70.18	\$5.78
2010	\$77.21	\$6.42
2011	\$83.93	\$6.75
2012	\$90.34	\$7.06
2013	\$98.65	\$7.57
Escalation thereafter ⁽¹⁾	2%	2-4%

⁽¹⁾ Percentage change represents the change in each year after 2013 to the end of the reserve life

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United States cost center

The Company performed a ceiling test calculation as at December 31, 2008 to assess the recoverable amount of the petroleum and natural gas properties resulting in an impairment in the US cost center of \$1,000,000 (2007 - \$427,490), which was included in depletion, depreciation, impairment and accretion expense.

At December 31, 2008, the Company had unproven property costs of \$Nil (2007 - \$1,000,000).

For the years ended December 31, 2008 and 2007, there were no capitalized general and administrative expenses.

8. CONVERTIBLE DEBENTURES

a) Resilient

Prior to the amalgamation of Guardian and Resilient Resources Ltd. in April 2006, the Company issued a convertible debenture (the "debenture financing") in the amount of \$4,500,000 to mature 18 months from the date of issuance and bearing interest at an annual rate of 7%, increasing to an annual rate of 10% if the principal amount has not been re-paid within one year of its issuance. If the Company was to go in default, the interest rate would increase to 14% per annum.

In conjunction with the debenture financing the lender immediately received 650,000 common shares of the Company, valued at \$422,500, as a finance fee. The lender also received warrants to acquire 1,600,000 common shares of the Company. Upon amalgamation these converted to warrants to acquire 783,613 common shares of the Company, at an exercise price of \$1.53 per common share expiring 42 months from the date of issuance. See note 12(f).

On August 18, 2006 the Company repaid \$3,500,000 of the debenture financing. The remaining amount of \$1,000,000 was subject to a restructuring agreement whereby all terms as indicated in the original agreement remained with only the interest terms changed to be fixed at an annual rate of 7% and if the Company was to go in default, the interest rate would increase to 14% per annum. The balance of the convertible debenture was repaid in January 2007.

b) Guardian

During 2008 the Company closed a private placement of \$400,000 principal amount of convertible secured debentures. The debentures bore interest at a rate of 8% per annum payable monthly in arrears, were due on June 30, 2008 and were convertible into certain interests in the Company properties at any time on the earlier of July 2, 2008 or in the event of default. No value was attributed to the conversion option due to the short term nature of these debentures. Of this amount, \$200,000 in convertible debentures was issued to a relative of an officer and director of the Company. A \$40,000 financing fee was paid on these transactions, including \$20,000 to the relative of an officer and director of the Company. During 2008 these debentures were repaid.

9. DUE TO SHAREHOLDER

Amounts owed to a significant shareholder of the Company at December 31, 2007 were unsecured, bore no interest, and had no fixed terms of repayment. The amounts were repaid by the Company during 2008.

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10. 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, 2008 are estimated to be \$1,830,000 (December 31, 2007 - \$1,420,000). These obligations are expected to be settled at various times until 2016. The credit-adjusted risk free rate at which the estimated cash flows were discounted was 8% during the year ended December 31, 2008 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:

	2008	2007
	\$	\$
Asset retirement obligation, beginning of year	876,947	1,207,667
Obligations incurred	37,020	-
Acquisitions	34,481	10,980
Dispositions	-	(526,682)
Revisions to obligations	136,122	(87,730)
Accretion expense	77,213	97,252
Asset retirement obligation, end of year	1,161,783	876,947

During 2008, the Company recorded asset retirement obligations of \$37,020 related to the drilling of 3 (1.6 net) producing oil wells in the Girouxville area. During 2008, the Company recorded an increase in its asset retirement obligation of \$34,481 related to the purchase of a joint interest partner's 35% interest in a producing gas well in Kotcho Lake, BC, now owned 100% by the Company. During 2008, the Company recorded asset retirement obligations of \$136,122 related to revisions of estimates in its asset retirement obligations.

During 2007, in response to a court order against the Company due to non-payment of a contractual obligation, the Company entered into a settlement agreement with an industry partner to transfer ownership of certain wells and facilities to the industry partner and a payment of \$55,000 in cash. Asset retirement obligations with a fair value of \$427,972 were transferred to the partner as part of the settlement and were removed from the Company's asset retirement obligation.

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11. INCOME TAXES

The recovery of income tax recorded in the financial statements differs from the amount which would be obtained by applying the statutory tax rate to the loss before tax as followings:

	2008	2007
	\$	\$
Loss before income taxes	\$(2,596,672)	\$ (2,904,270)
Statutory income tax rate	29.50%	31.00%
Expected income tax recovery	\$(766,000)	\$(900,324)
Tax effect of non-deductible amounts related to:		
Stock-based compensation	152,749	98,884
Valuation allowance and other	(80,749)	(398,560)
Future income taxes recovery	\$ (694,000)	\$ (1,200,000)

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

	2008	2007
	\$	\$
Petroleum and natural gas properties	650,000	\$(38,600)
Share issue costs	390,000	300,900
Asset retirement obligations	290,000	263,100
Non-capital losses	250,000	1,009,000
Valuation allowance	(886,000)	(1,534,400)
Future income tax asset	694,000	-

In 2008, the tax benefit recognized relates only to the future tax to be renounced for the flow-through shares issued during the year.

The Company is in the process of assessing 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 the 2008 and 2007 net future income tax assets as disclosed above do not include the tax pools related to its wholly owned subsidiaries.

For income tax purposes, the Company's loss carried forward in Canada of \$1 million can be applied to reduce future years' taxable income and expires between 2026 and 2028.

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12. SHAREHOLDER'S 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, 2006	20,079,422	8,103,838
Tax effect of flow-through shares	-	(1,200,000)
Balance, December 31, 2007	20,079,422	6,903,838
Private placements of common shares for cash	18,901,000	4,749,616
Issuances of shares for debt	683,955	134,175
Exercise of Agent warrants	73,500	22,388
Share issue costs	-	(788,652)
Balance, December 31, 2008	39,737,877	11,021,365

Warrants	Number of Warrants	Amount \$
Balance, December 31, 2006 and 2007	-	673,600
Private placements of warrants for cash	8,871,300	944,840
Balance, December 31, 2008	8,871,300	1,618,440

- 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.

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- 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:

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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) 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, 2006	1,275,000	\$1.10
Granted	800,000	\$0.15
Cancelled	(725,000)	(\$1.10)
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
Exercisable, December 31, 2008	2,150,000	\$0.38

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Exercise Prices	Stock options outstanding			Stock options exercisable	
	Outstanding Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (Years)	Options Exercisable	Weighted Average Exercise Price
\$0.150	800,000	\$0.150	4.1	800,000	\$0.150
\$0.220	200,000	\$0.220	4.3	150,000	\$0.220
\$0.230	250,000	\$0.230	4.9	62,500	\$0.230
\$0.285	800,000	\$0.285	3.0	600,000	\$0.285
\$0.295	350,000	\$0.295	4.8	87,500	\$0.295
\$1.100	550,000	\$1.100	2.7	450,000	\$1.100
	2,950,000	\$0.400	3.4	2,150,000	\$0.381

During the year-ended December 31, 2008, 1,800,000 stock options were granted (2007 – 800,000) with a fair value of \$0.214 (2007 - \$0.106) per option as determined using the Black-Scholes model. The stock options granted vest over a period of 12 months and expire between 2009 and 2013. The fair value of each stock option granted was estimated on the date of grant using the Black Scholes option pricing model with the following assumptions:

	2008	2007
Risk-free interest rate	4.5-5.0%	5.0%
Expected life	5 years	5 years
Expected volatility range	84%-112%	87%
Expected dividend	Nil	Nil

d) Warrants

	Number of Options	Weighted Average Exercise Price
Balance, December 31, 2006	237,502	\$5.83
Expired	(237,502)	(\$5.83)
Balance, December 31, 2007	-	-
Issued pursuant to private placement	5,500,000	\$0.30
Issued pursuant to private placement	3,371,300	\$0.35
Balance, December 31, 2008	8,871,300	\$0.32

e) Agent Warrants

	Number of Options	Weighted Average Exercise Price
Balance, December 31, 2007 and 2006	-	-
Issued to agents pursuant to private placement	550,000	\$0.22
Issued to agents pursuant to private placement	1,002,970	\$0.30
Issued to agents pursuant to private placement	337,130	\$0.32
Exercise of warrants	(73,500)	(\$0.22)
Balance, December 31, 2008	1,816,600	\$0.28

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f) Debenture warrants

	Number of Options	Weighted Average Exercise Price
Balance, December 31, 2007 and 2008	783,613	\$1.53

g) Contributed surplus

	2008 \$	2007 \$
Balance, beginning of year	878,990	529,890
Stock-based compensation	517,794	318,982
Issuance of agent warrants	212,939	-
Exercise of agent warrants	(6,318)	-
Equity portion of debenture repaid	-	30,118
Balance, end of year	1,603,505	878,990

h) Earnings per share

Basic per share amounts are calculated using the weighted average number of shares outstanding of 34,691,134 (December 31, 2007 – 20,079,422).

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

13. SUPPLEMENTAL CASH FLOW INFORMATION

	2008 \$	2007 \$
Changes in non-cash working capital		
Change in accounts receivable	658,252	1,296,087
Change in prepaid expenses and deposits	3,975	27,298
Change in accounts payable and accrued liabilities	(1,672,055)	(1,731,123)
	(1,009,828)	(407,738)
Relating to:		
Operating activities	(534,285)	162,895
Financing activities	-	(100,836)
Investing activities	(475,543)	(469,767)
	(1,009,828)	(407,738)
Cash interest paid	29,037	20,821
Cash taxes paid	-	-

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14. COMMITMENTS

a) Flow-through share issuance

Pursuant to a flow-through share issuance completed in May and June 2008, the Company is committed to incur \$2,777,110 of qualified expenditures by December 31, 2009. At December 31, 2008, approximately \$1,000,000 of the obligation has been fulfilled. The expenditures were renounced to investors in February 2009.

b) Office lease obligation

The Company had a five year office lease agreement which expired on October 31, 2008. The Company extended this lease agreement for a six month period expiring April 30, 2009. The following table outlines the Company's estimated lease commitments over the life of the agreement:

	\$
2009	50,000

c) 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%.

15. RELATED PARTY TRANSACTIONS

- a) The Company obtained helicopter services in conjunction with the servicing and drilling of natural gas wells in Northern B.C. from a company controlled by a major shareholder and officer of the Company, for which the Company was charged \$273,329 (2007 - \$136,147). The Company also recorded management fees of \$Nil (2007 - \$13,102) for management services from the same company. All of these amounts were paid in 2008.
- b) The Company obtained engineering consulting services in the amount of \$190,575 (2007 - \$Nil) from a company controlled by a Company director, who was appointed in 2008. Of this amount, \$180,729 is included in accounts payable and accrued liabilities at December 31, 2008 (2007 - \$Nil).
- c) Legal fees in the amount of \$77,287 (2007 - \$64,310) have been incurred from a legal firm of which a Company director, who was appointed in 2006, is a partner. Of this amount, \$4,358 is included in accounts payable and accrued liabilities at December 31, 2008 (2007 - \$6,195).

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.

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16. CONTINGENCIES

a) Flow-through shares

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. At December 31, 2007, \$2,150,000 of the obligation had been fulfilled. Subsequent to the 2007 year-end, the Company spent the remaining \$1,850,000 obligation.

Since the Company did not make the expenditures by December 31, 2007 as required under the income tax rules, the unexpended flow-through amount 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 \$950,000 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 for estimated Part XII.6 interest and penalties in the amount of \$365,000.

b) Litigation

During 2008, the Company was named as a defendant in a lawsuit in which a company that signed a farmout agreement regarding one of the Company's operated wells in Northern BC (the "Plaintiff") is claiming, amongst other things, that it 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 is claiming that it earned its 100% working interest upon completion of the well and that the remaining amounts due by it, which amounts it contests, can 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 claims that it is entitled to a declaration that it earned and should recover 100% of the net production revenues on the basis that, it alleges, the Company was negligent in exceeding the AFE estimates for drilling and completion of the well. The Plaintiff also claims, 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.

The Plaintiff is seeking various remedies in its statement of claim including:

- a declaration that it earned a 100% BPO interest subject to the Company's 15% gross overriding royalty which is convertible to a 50% working interest after pay out ("APO");
- damages in the amount of \$1,050,000; or
- the return of all or a portion of the \$2.1 million in funds advanced by the Plaintiff on the basis of a claim for unjust enrichment.

At December 31, 2008, the Company has recorded the \$688,000 in costs incurred to complete this well and allow it to be able to produce as property and equipment and has included these costs within its depletion calculation. For the year-ended December 31, 2008 the Company has recorded \$241,000 in net revenues from this well, after royalties and operating costs, but before depletion expense. The gas well was shut-in subsequent to December 31, 2008 due to uneconomic conditions. The well has been determined by the Company's independent reserve engineers to no longer have any economic proven reserves at December 31, 2008.

The Company is vigorously defending this lawsuit and is seeking in its statement of defence to have the Court determine that the Plaintiff forfeited any interest in this well by virtue of its failure to fulfill its obligation under the farmout agreement to pay 100% of the costs to drill and complete the well. The Company's Statement of Defence seeks, in the alternative, full payment by the Plaintiff of the \$688,000 not paid by the Plaintiff, plus a penalty of 300% of this amount in accordance with Canadian Association of Petroleum Landmen (CAPL) industry standards, before the Plaintiff earns a 100% BPO interest in this well. The Company denies that it has ever received any funding from the Plaintiff for the pipeline or that the Plaintiff has any interest in the pipeline.

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If it is ultimately determined by a Court that the Plaintiff has in fact earned an interest in this well, subject to their payment of outstanding amounts, a position that the Company denies, the result of this will effectively be the same from a financial statement perspective as the Company's present accounting treatment. That result being that the resulting accounts receivable of \$688,000 for capital costs incurred by the Company in excess of the Plaintiff's funding is still owed by the Plaintiff and that \$241,000 of earnings from the well during 2008, leaves a shortfall of \$447,000, for which, based on the Company's reserve report information, there will be no future recovery possibilities from this well's earnings. Consequently, the Company would continue to carry the Plaintiff's payment obligation in accounts receivable. As the Plaintiff has no other material assets in Alberta the accounts receivable from the Plaintiff of \$447,000 would, in accordance with Generally Accepted Accounting Principles, have to be allowed and provided for as a bad debt expense versus the present accounting treatment wherein additional depletion expense has been recognized for this \$447,000 amount arising from the application of the ceiling test explained in note 7.

c) Mineral Management Services

The Mineral Management Service ("MMS"), a bureau of the US Department of the Interior that manages that nation's natural gas and oil resources, alleged during the year that a subsidiary of the Company had been deficient in various administrative filing requirements in the past and that, as a result, civil penalties of approximately \$611,500 (US\$500,000) were being levied against the subsidiary. The subsidiary is disputing these penalties and, along with its legal counsel, has been negotiating with MMS, its collection agencies and its counsel towards a satisfactory resolution of this matter.

A provision of \$45,863 (US\$37,500) has been made for these civil penalties. This provision has been based on a probationary settlement arrangement with MMS, which has yet to be finalized, but has been agreed to in principle for a portion of these penalties still within MMS's jurisdiction, representing approximately 80% of the total amounts at issue, with the balance of the penalties no longer in MMS's jurisdiction the subject of an equivalent settlement offer by the subsidiary to the collection agencies involved.

The probationary settlement arrangement with MMS involves a total repayment of \$36,690 (US\$30,000) in equal monthly installments over 36 months, plus interest, and requires that the subsidiary remains compliant with its payment and reporting requirements over this time frame, otherwise the full amount of the penalties, reduced on a declining basis for the period of compliance, will be owing to MMS. The Company believes that this settlement arrangement will be acceptable to all parties and further that the proportionate settlement offer made to the collection agencies will be acceptable to them.

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.

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17. SEGMENTED DISCLOSURES

For the year ended December 31, 2008

	Canada	United States	December 31, 2008
Petroleum and natural gas revenue	\$6,029,065	\$1,104,490	\$7,133,555
Interest expense	\$615	\$10,922	\$11,537
Depletion, depreciation and accretion	\$4,621,059	\$1,098,668	\$5,719,727
Loss for the period	\$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

For the year ended December 31, 2007

	Canada	United States	December 31, 2007
Petroleum and natural gas revenue	\$90,277	\$686,727	\$777,004
Interest expense	\$387,603	\$2,716	\$390,319
Depletion, depreciation and accretion	\$106,135	\$546,732	\$652,867
Loss for the period	\$1,276,008	\$428,261	\$1,704,269
Property and equipment	\$2,200,216	\$1,446,875	\$3,647,091
Capital expenditures	\$1,278,838	\$977,490	\$2,256,778

18. FINANCIAL INSTRUMENTS AND CAPITAL MANAGEMENT

a) Fair value of financial assets and liabilities

The Company's carrying value of cash, accounts receivable, accounts payable, due to / from related company and due to shareholder and convertible debenture approximates its fair value due to the immediate or short-term maturity of these instruments.

b) Interest rate risk

At December 31, 2008, the Company is not exposed to interest rate risk.

c) Commodity price risk

The nature of the Company's operations results in an exposure to fluctuations in commodity prices. At December 31, 2008, 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.

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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 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, 2007.

The capital structure of the Company is as follows:

	2008	2007
	\$	\$
Total shareholders' equity (deficiency)	3,065,995	(818,215)
Total shareholders' equity (deficit) as a percentage of total capital	70%	(26%)
Working capital deficiency	1,335,143	3,934,186
Total indebtedness	1,335,143	3,943,186
Total indebtedness as a percentage of total capital	30%	126%
Total Capital	4,401,138	3,115,971

f) Credit Risk

Credit risk arises when a failure by counter parties to discharge their obligations could reduce the amount of future cash inflows from financial assets on hand at the balance sheet date. A majority of the Company's credit risk arises when a failure by counter parties 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 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 assesses quarterly if there has been any impairment of the financial assets of the Company. During the year ended December 31, 2008 there was a \$13,000 impairment provision required on the financial assets of the Company. The Company does not have any significant credit risk exposure to any single counterparty other than to the operator of its Girouxville area wells. As at December 31, 2008, the receivable from this company represented approximately 80% of the Company's total accounts receivable balance. This balance was collected subsequent to year-end. Mitigating this credit risk is the fact that the Company had an offsetting payable to this company in excess of this accounts receivable.

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.

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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. All financial liabilities mature within one year.

19. SUBSEQUENT EVENTS

a) Flow-Through Share Renouncement

In February 2009, the Company renounced \$2,777,110 of eligible expenditures pursuant to its flow-through share issuance in 2008 (see notes 12 and 14). As a result, in the first quarter of 2009 share capital will be decreased and future income tax liabilities will be increased by \$694,000 for the tax effect of this renouncement.

b) Stock options

Subsequent to December 31, 2008, 350,000 and 250,000 stock options respectively were cancelled or expired unexercised upon the resignation of an officer of the Company and the termination of a consultant to the Company. The exercise price of the stock options was \$0.295 per share and \$0.23 per share respectively.

c) Property and equipment sale

Subsequent to December 31, 2008, the Company engaged an agent to commence the sale of all of the Company's petroleum and natural gas property and equipment assets.

d) Due from related company

On April 28, 2009, the full balance owing from the related company was repaid.