

Interim Consolidated Financial Statements
(Expressed in United States dollars)

BUCKING HORSE ENERGY INC.

For the Periods ended September 30, 2009 and August 31, 2008

NOTICE OF NO AUDITOR REVIEW OF INTERIM FINANCIAL STATEMENTS

Under National Instrument 51-102, Part 4, subsection 4.3(3), if an auditor has not performed a review of the interim financial statements, they must be accompanied by a notice indicating that the financial statements have not been reviewed by an auditor.

The accompanying unaudited interim financial statements of the Company have been prepared by and are the responsibility of the Company's management. The Company's independent audit has not performed a review of these financial statements in accordance with the standards established by the Canadian Institute of Chartered Accountants for a review of interim financials.

BUCKING HORSE ENERGY INC.

INTERIM CONSOLIDATED BALANCE SHEETS

(Unaudited - Prepared by Management)

(Expressed in United States dollars)

	As at September 30 2009	As at December 31 2008
Assets		
Current assets		
Cash and equivalents	\$ 6,967,651	\$ 8,867,314
Accounts receivable	1,119,587	2,385,081
Promissory note (note 4)	1,466,377	3,734,738
Prepaid expenses	519,192	148
Benefit under derivative instruments (note 5(b))	943,629	4,333,497
Income tax receivable	398,039	2,780,956
	11,414,475	22,101,734
Investments (note 6)	301,298	274,213
Oil and natural gas properties (note 7)	162,174,421	148,295,535
	\$ 173,890,194	\$ 170,671,482
Liabilities and Shareholders' Equity		
Current liabilities		
Accounts payable & accrued liabilities	1,512,906	4,193,096
State resource taxes payable	365,443	978,826
Income taxes payable	793,561	-
	2,671,910	5,171,922
Non-current liabilities		
Bank indebtedness (note 8)	18,500,000	18,500,000
State resource taxes payable	-	581,774
Convertible debentures (note 9)	24,295,969	20,588,752
Asset retirement obligation (note 10)	78,274	69,176
Future income taxes	53,707,153	48,892,325
	96,581,396	88,632,027
SHAREHOLDERS' EQUITY		
Share capital (note 12)	61,648,395	61,648,395
Equity portion of debentures payable	25,329,139	25,329,139
Issuer Bid Purchase	(54,917)	-
Accumulated other comprehensive income	(4,126,421)	(11,239,809)
Retained earnings (deficit)	(8,159,308)	1,129,808
	74,636,888	76,867,533
	\$ 173,890,194	\$ 170,671,482

"Gordon Nielsen"

Director

"Michael Shoen"

Director

See accompanying notes to consolidated financial statements.

BUCKING HORSE ENERGY INC.

INTERIM CONSOLIDATED STATEMENTS OF OPERATIONS AND RETAINED EARNINGS (DEFICIT)

(Unaudited - Prepared by Management)

(Expressed in United States dollars)

	For the nine months ended September 30 2009	For the three months ended September 30 2009	For the nine months ended August 31 2008	For the three months ended August 31 2008
Revenue:				
Oil and natural gas revenue	\$ 9,270,221	\$ 3,135,417	15,575,429	\$ 8,311,241
Direct expenses:				
Depletion, depreciation & accretion	5,072,206	3,384,142	4,141,596	2,853,694
State resource taxes	804,843	245,684	1,651,499	848,964
Royalties	9,886	(614)	80,259	46,575
Operating expenses	4,013,305	1,549,394	2,798,110	1,683,807
	9,900,240	5,178,606	8,671,464	5,433,039
Net operating income	(630,019)	(2,043,189)	6,903,965	2,878,202
Other expenses (income):				
Interest and other	(108,080)	(7,174)	(367,025)	(148,768)
Interest expense	5,093,854	1,768,410	3,591,298	2,145,609
Write down of Promissory Note (note 4)	2,634,579	78,446	-	-
Financing fees	25,000	-	325,000	-
Accretion expense (note 9)	800,645	304,658	929,215	884,721
General & administration	409,520	129,608	857,440	176,264
Professional fees	585,428	153,339	592,489	(208,947)
Foreign exchange loss (gain)	369,383	182,830	186,031	3,827,802
Unrealized loss (gain) on derivative instruments (note 5(b))	3,389,868	2,018,881	(2,927,776)	(3,361,475)
Realized loss (gain) on derivative instruments (note 5(b))	(5,250,394)	(1,697,800)	88,040	88,040
Realized loss (gain) on investment	-	-	421,144	1,595,254
Unrealized loss (gain) on investments	(245)	(69)	53,121	53,121
Adjustment on cancellation of options	-	-	-	2,025,926
	7,949,558	2,931,129	3,748,977	7,077,547
Earnings (loss) before income taxes	(8,579,577)	(4,974,318)	3,154,988	(4,199,345)
Income tax expense (recovery):				
Income tax, current	1,367,499	-	1,150,315	1,150,315
Future income tax expense	(657,960)	(538,739)	1,625,957	482,457
	709,539	(538,739)	2,776,272	1,632,772
Net earnings for the period	(9,289,116)	(4,435,579)	378,716	(5,832,117)
Retained earnings (deficit), beginning of year	1,129,808	(3,723,729)	(570,063)	5,640,770
Excess on cancellation of issued common shares	-	-	(216,758)	(216,758)
Retained earnings (deficit), end of period	\$ (8,159,308)	\$ (8,159,308)	\$ (408,105)	\$ (408,105)
Net Earnings (loss) per Common Share				0
Basic	\$ (0.40)	\$ (0.19)	\$ 0.02	\$ (0.25)
Diluted	\$ (0.40)	\$ (0.19)	\$ 0.02	\$ (0.25)
Weighted average number of shares outstanding	22,994,513	22,994,513	17,997,527	23,061,713

See accompanying notes to consolidated financial statements.

BUCKING HORSE ENERGY INC.

INTERIM CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS

(Unaudited - Prepared by Management)

(Expressed in United States dollars)

	As at September 30 2009	As at December 31 2008
Net earnings (loss) for the period	(9,289,116)	1,599,474
Unrealized loss on available for sale investments, net of tax	(168,504)	(159,014)
Unrealized gains and losses on translating financial statements into reporting currency	7,113,388	(7,877,649)
Comprehensive loss for the period	(2,344,231)	(6,437,189)

INTERIM CONSOLIDATED STATEMENTS OF ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS)

(Expressed in United States dollars)

	As at September 30 2009	As at December 31 2008
Accumulated other comprehensive income (loss), beginning of year	\$ (11,239,809)	\$ (3,203,146)
Unrealized gains and losses on translating financial statements into reporting currency	7,113,388	(7,877,649)
Unrealized loss on available for sale investments, net of tax	(168,504)	(159,014)
Accumulated other comprehensive income (loss), end of period	\$ (4,126,421)	\$ (11,239,809)

See accompanying notes to consolidated financial statements.

BUCKING HORSE ENERGY INC.

INTERIM CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited - Prepared by Management)

(Expressed in United States dollars)

	For the nine months ended September 30 2009	For the three months ended September 30 2009	For the nine months ended August 31 2008	For the three months ended August 31 2008
Cash and cash equivalents provided by (used in):				
Operations:				
Net earnings for the period	\$ (9,289,116)	\$ (4,435,579)	378,716	\$ (5,832,117)
Items not involving cash:				
Depletion, depreciation and accretion	5,072,206	3,428,735	4,141,596	2,853,694
Accretion expense - debentures	800,645	304,658	929,215	884,721
Future income taxes	(657,960)	(538,739)	1,625,957	482,457
Unrealized loss (gain) on investments	(245)	(69)	474,265	474,265
Unrealized loss (gain) on derivative instruments	3,389,868	2,018,881	(2,927,776)	(3,361,475)
Unrealized foreign exchange loss (gain)	369,383	182,830	(274,799)	(337,611)
Non-cash interest and write-down to promissory note	2,546,470	75,821	(424,788)	(289,853)
Changes in non-cash working capital:				
Accounts receivable	1,458,613	327,496	780,752	853,778
Prepaid expenses	(475,054)	(340,566)	(354,672)	(334,433)
Taxes recoverable	1,890,058	(501,315)	103,917	103,917
Future income taxes	(658,340)	(658,340)	-	-
Income taxes payable	1,367,499	1,367,499	-	-
Accounts payable and accrued liabilities	(2,981,129)	412,219	(3,871,195)	(3,840,417)
State resource taxes payable	(1,290,417)	(1,032,636)	925,162	925,162
	1,542,481	610,895	1,506,350	(7,417,912)
Investments:				
Oil and natural gas property expenditures	(5,001,136)	(220,451)	(1,394,858)	(461,460)
Acquisition of Gemini Energy Corp - adjustment	-	-	(19,172,431)	4,680,581
Proceeds on sale of investment	-	-	397,659	397,659
Acquisition of investments	-	-	(235,272)	770,562
	(5,001,136)	(220,451)	(20,404,902)	5,387,342
Financing:				
Long-term credit facility	-	-	13,500,000	-
Subscription Advance	-	-	(7,993,605)	-
Issuance of convertible debenture	-	-	1,707,307	-
Issuance of share capital	-	-	8,094,709	-
Issuer bid purchase	(54,917)	(54,917)	(339,140)	(339,140)
Other accumulated comprehensive income	-	-	-	5,138,752
	(54,917)	(54,917)	14,969,271	4,799,612
Effect of foreign currency translation on cash & cash equivalents	1,613,909	1,734,221	494,798	557,608
Increase in cash and cash equivalents	(1,899,663)	2,069,748	(3,434,483)	3,326,650
Cash and cash equivalents, beginning of period	8,867,314	4,897,903	8,825,606	2,064,473
Cash and cash equivalents, end of period	\$ 6,967,651	\$ 6,967,651	\$ 5,391,123	\$ 5,391,123

See accompanying notes to interim consolidated financial statements.

BUCKING HORSE ENERGY INC.

Notes to Consolidated Financial Statements
(Expressed in United States dollars, unless otherwise noted)

For the Nine Months ended September 30, 2009 and August 31, 2008

1. Nature of operations:

NRG Investments Inc. was incorporated under the laws of British Columbia, Canada on April 28, 2006. Effective March 4, 2008 the Company changed its name to Bucking Horse Energy Inc. (the Company or Bucking Horse) and acquired two additional wholly-owned subsidiaries, Gemini Energy Corp. (Gemini) and its subsidiary, Arrowhead Resources (U.S.A.) Ltd. (Arrowhead), through the purchase of 100% of the issued and outstanding shares of Gemini (note 4).

The Company's principal business activity is the exploration, development and production of petroleum and natural gas reserves located in Canada and the United States of America.

An assumption underlying the preparation of financial statements in accordance with Canadian generally accepted accounting principles is that the Company will be able to realize assets and discharge liabilities in the normal course of business.

Accordingly, it is management's opinion that the going concern assumption is appropriate and all assets and liabilities have been valued accordingly.

2. Change in reporting currency:

Effective March 4, 2008, the Company changed its reporting currency to the US dollar (US\$). This change in reporting currency has been adopted due to the Company's primary focus on acquisition, exploration, development and production of natural gas and oil interests in the United States. The majority of the Company's oil and natural gas property assets are in the United States. Prior to March 4, 2008, the Company reported its annual and quarterly consolidated financial statements in Canadian dollars (C\$). In making this change in reporting currency, the Company followed the recommendations of the Emerging Issues Committee (EIC) of the Canadian Institute of Chartered Accountants (CICA), set out in EIC-130, *Translation Method when the Reporting Currency Differs from the Measurement Currency or there is a Change in the Reporting Currency*.

3. Significant accounting policies:

(a) Basis of consolidation:

The consolidated financial statements of the Company have been prepared in accordance with Canadian generally accepted accounting principles. The consolidated financial statements of the Company include its wholly-owned subsidiaries NRG Holdings Corp., incorporated in the State of Nevada, N Holdings Inc., incorporated in the State of Washington and Gemini, incorporated in the Province of British Columbia and its wholly-owned subsidiary, Arrowhead, incorporated in the State of South Dakota. All inter-company transactions and balances have been eliminated upon consolidation.

BUCKING HORSE ENERGY INC.

Notes to Consolidated Financial Statements
(Expressed in United States dollars, unless otherwise noted)

For the Nine Months ended September 30, 2009 and August 31, 2008

3. Significant accounting policies (continued):

(b) Adoption of new accounting standards:

Effective September 1, 2008, the Company adopted the following new CICA accounting standards:

(i) CICA Handbook Section 1535, *Capital Disclosures*:

This section requires additional disclosures of: (1) an entity's objectives, policies and processes for managing capital; (2) quantitative data about what the entity regards as capital; (3) whether the entity has complied with any capital requirements; and (4) if it has not complied, the consequences of such non-compliance. Refer to note 16 for additional disclosures.

(ii) Revision to CICA Handbook Section 1400, *General Standards of Financial Statement Presentation*:

This revision requires management to assess and disclose an entity's ability to continue as a going concern. Refer to note 1 for additional disclosures.

(iii) CICA Handbook Section 3862, *Financial Instruments - Disclosure*, and CICA Handbook Section 3863, *Financial Instruments - Presentation*:

These new sections revise and enhance the disclosure and presentation requirements and carry forward the presentation requirements for financial instruments from CICA Handbook Section 3861, *Financial Instruments - Disclosure and Presentation*. The significance of financial instruments for the entity's financial position and performance, the nature and extent of the risks arising from financial instruments and how these risks are managed are emphasized. Refer to note 15 for additional disclosures.

(c) Cash and cash equivalents:

Cash and cash equivalents are classified as held-for-trading and include short-term money market instruments with terms of maturity, at the date of acquisition, not exceeding ninety days, that are readily convertible to known amounts of cash, and which are subject to an insignificant risk of change in value.

(d) Financial instruments:

(i) Financial instruments:

Financial assets and liabilities classified as held-for-trading are measured at fair value with realized and unrealized gains and losses recognized in net earnings. Financial assets classified as held-to-maturity, loans and receivables, and financial liabilities other than those classified as held-for-trading, are measured at amortized cost. Financial assets classified as available for sale are measured at fair value with unrealized gains or losses recognized in accumulated other comprehensive income until the asset is sold and the gain or loss realized. The purchase and sale of a financial asset, where the contract requires the asset to be delivered within an established time frame, are recognized on a trade-date basis. Generally, all derivatives, including embedded derivatives that must be accounted for separately from their host contract, generally must be classified as held-for-trading and recorded at fair value in the consolidated balance sheet. Transaction costs for financial instruments classified as other than held-for-trading are expensed as incurred.

BUCKING HORSE ENERGY INC.

Notes to Consolidated Financial Statements
(Expressed in United States dollars, unless otherwise noted)

For the Nine Months ended September 30, 2009 and August 31, 2008

3. Significant accounting policies (continued):

(d) Financial Instruments (continued):

The Company classifies its financial instruments into categories as follows:

Cash and cash equivalents	held for trading
Accounts receivable	loans and receivables
Promissory note	loans and receivables
Benefit under derivative financial instrument	held for trading
Investment in shares of a related entity	available for sale
Investment in warrants of a related entity	held for trading
Accounts payable and accrued expenses	other financial liabilities
Amounts payable to related parties	other financial liabilities
Convertible debentures	other financial liabilities
Bank indebtedness	other financial liabilities
Embedded derivatives	held for trading

(ii) Embedded derivatives:

The Company has identified no embedded derivatives other than the conversion option in the convertible debentures (note 9) to be separately accounted for at September 30, 2009.

(iii) Derivative financial instruments:

The Company utilizes derivative financial instruments to manage interest rate and price risk. Derivative financial instruments are measured at fair value with gains and losses recorded in net earnings (loss) for the year.

(e) Investments:

Investments include investments in shares and warrants of companies as described in note 6. The Company's investments in shares of related entities are classified as available-for-sale and are measured at cost. The Company's investment in warrants of a related entity is classified as held-for-trading and is measured at fair value with gains and losses recorded through the statement of operations. The carrying values of the investments are regularly reviewed for possible other than temporary impairment. When there is a loss in value that is other than a temporary decline, the investment is written down to recognize the loss with the write down recorded as a charge to income.

BUCKING HORSE ENERGY INC.

Notes to Consolidated Financial Statements
(Expressed in United States dollars, unless otherwise noted)

For the Nine Months ended September 30, 2009 and August 31, 2008

3. Significant accounting policies (continued):

(f) Oil and natural gas properties:

The Company follows the full cost method of accounting for oil and natural gas operations whereby all costs associated with the acquisition, exploration for and development of oil and natural gas reserves are capitalized. Such costs include land acquisition costs, geological and geophysical expenses, carrying charges on non-producing properties, costs of drilling both productive and non-productive wells and overhead charges directly related to acquisition, exploration and development activities.

The capitalized costs, together with the costs of production equipment, are depleted and depreciated on the unit-of-production method based on the estimated gross proven reserves as determined by external experts. Oil and natural gas reserves and production are converted into equivalent barrels of oil based upon the estimated relative energy content.

Costs of acquiring and evaluating unproven properties are initially excluded from the costs subject to depletion and depreciation. These unproven properties are assessed periodically to ascertain whether or not proved reserves are attributable to the properties or impairment has occurred. When proved reserves are attributed to the unproven properties or the property is considered to be impaired, the cost of the property or the amount of the impairment is added to the costs subject to depletion and depreciation.

The Company evaluates the carrying amounts for impairment annually. The carrying value is not considered to be impaired when the sum of the undiscounted net cash flows expected from the production of proved reserves, less any impairment, of unproved properties and related major development projects exceeds the carrying amount of the cost centre (the "ceiling test"). When the carrying amount is not determined to be recoverable, an impairment loss is recognized to the extent that the carrying amount of the cost centre exceeds the sum of the discounted net cash flows expected from the production of proved and probable reserves, the cost, less any impairment of unproven properties and related major development projects. The cash flows are estimated using expected future product prices and costs based on best information available and are discounted at an interest rate of 10%.

Proceeds from the sale of oil and natural gas properties are applied against capitalized costs, with no gain or loss recognized, unless such a sale would significantly alter the rate of depletion and depreciation.

Substantially all of the Company's exploration, development and production activities are conducted jointly with others and accordingly these consolidated financial statements reflect only the Company's proportionate interest in such activities.

BUCKING HORSE ENERGY INC.

Notes to Consolidated Financial Statements
(Expressed in United States dollars, unless otherwise noted)

For the Nine Months ended September 30, 2009 and August 31, 2008

3. Significant accounting policies (continued):

(g) Asset retirement obligations:

The Company uses the fair value method of recording the obligation associated with closure, reclamation and restoration of oil and natural gas properties and other asset retirement costs. The fair value of the liability for the Company's asset retirement obligation is recorded in the period in which it is incurred, discounted to its present value using the Company's credit-adjusted, risk-free interest rate and the corresponding amount is capitalized to the carrying amount of the related oil and natural gas properties. The liability amount is increased each reporting period due to the passage of time and the amount of this accretion is charged to earnings in the period. Revisions to the estimated timing of cash flows or to the original estimated undiscounted cost could also result in an increase or decrease to the obligation. Actual costs incurred upon settlement of the retirement obligation are charged against the obligation to the extent of the liability recorded.

(h) Revenue recognition:

Revenues from oil and natural gas operations are recognized when persuasive evidence of a sales agreement exists, the title and risk is transferred to the customer, collection is reasonably assured, and the price is reasonably determinable.

(i) Foreign currency translation:

The Company's functional currency is Canadian dollars and its reporting currency is U.S. dollars. Accordingly, the consolidated financial statements are translated into U.S. dollars using the current rate method.

The Company's investments in NRG Holdings Corp. and N Holdings Inc. are accounted for as integrated foreign operations and accordingly are translated into Canadian dollars using the temporal method. Under this method, monetary items denominated in foreign currencies are translated to Canadian dollars at the exchange rate in effect at the balance sheet date and non-monetary items are translated at the month end rate of exchange in effect when the assets were acquired or obligations incurred. Revenue and expense items are translated at the average exchange rate for the year. Foreign exchange gains and losses are included in net earnings (loss) for the year.

Arrowhead is accounted for as a self sustaining foreign operation and accordingly is translated into Canadian dollars in accordance with the current rate method. Assets and liabilities are translated at the exchange rates prevailing at the balance sheet dates, and revenue and expenses are translated on the basis of average exchange rates during the periods. Any recognized and unrecognized gains or losses arising from the translation of these accounts are recorded in accumulated other comprehensive income (loss). An applicable portion of gains and losses is transferred to net earnings when there is a reduction of the net investment.

BUCKING HORSE ENERGY INC.

Notes to Consolidated Financial Statements
(Expressed in United States dollars, unless otherwise noted)

For the Nine Months ended September 30, 2009 and August 31, 2008

3. Significant accounting policies (continued):

(j) Stock-based compensation:

The Company has a stock option plan. The Company accounts for all stock-based payments using the fair value based method. Consideration paid on the exercise of stock options is recorded as share capital.

Under the fair value based method, stock-based payments to non-employees are measured at the fair value of the consideration received, or the fair value of the equity instruments issued, or liabilities incurred, whichever is more reliably measurable. The fair value of stock-based payments to non-employees is periodically re-measured until counterparty performance is complete, and any change therein is recognized over the period and in the same manner as if the Company had paid cash instead of paying with or using equity instruments. The cost of stock-based payments to non-employees that are fully vested and non-forfeitable at the grant date is measured and recognized at that date.

Under the fair value based method, compensation cost for grants to employees is measured at fair value at the grant date and recognized over the vesting period. For awards that vest at the end of the vesting period, compensation cost is recognized on a straight-line basis; for awards that vest on a graded basis, compensation cost is recognized on a pro-rata basis over the vesting period.

(k) Earnings per share:

Basic earnings per share are computed by dividing net earnings (loss) by the weighted average number of shares outstanding during the year. Diluted earnings per share are computed using the treasury stock method.

(l) Income taxes:

The Company uses the asset and liability method of accounting for income taxes. Under the asset and liability method, future tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Future tax assets and liabilities are measured using enacted or substantively enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. A valuation allowance is recorded against any future income tax asset if it is more likely than not that the asset will not be realized. The effect on future tax assets and liabilities of a change in tax rates is recognized in earnings in the same period the substantive enactment occurred.

(m) Use of estimates:

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Significant areas requiring the use of estimates is the evaluation of impairment of oil and natural gas properties, valuation of financial instruments, determination of asset retirement obligation, valuation allowance applied against the future income taxes assets and rates for depreciation and depletion. Actual results could differ from those estimates.

BUCKING HORSE ENERGY INC.

Notes to Consolidated Financial Statements
(Expressed in United States dollars, unless otherwise noted)

For the Nine Months ended September 30, 2009 and August 31, 2008

3. Significant accounting policies (continued):

(n) Comparative figures:

Certain of the Company's comparative figures have been reclassified to conform to the financial statement presentation adopted in the current year.

(o) Recent accounting pronouncements:

(i) International Financial Reporting Standards (IFRS)

In 2006, the Canadian Accounting Standards Board (AcSB) published a new strategic plan that will significantly affect financial reporting requirements for Canadian companies. The AcSB strategic plan outlines the convergence of Canadian generally accepted accounting principles with IFRS over an expected five year transitional period. In February 2008, the AcSB announced that 2011 is the changeover date for publicly-listed companies to use IFRS, replacing Canada's own generally accepted accounting principles. The date is for interim and annual financial statements relating to fiscal years beginning on or after January 1, 2011. The transition date of January 1, 2011 will require the restatement for comparative purposes of amounts reported by the Company for the year ended December 31, 2010. While the Company has begun assessing the adoption of IFRS for 2011, the financial reporting impact of the transition to IFRS cannot be reasonably estimated at this time.

4. Business combination:

On March 4, 2008, Bucking Horse closed an arrangement transaction (the Arrangement), pursuant to which it acquired 100% of the issued and outstanding shares and options of Gemini. The assets and liabilities of Gemini and its wholly-owned subsidiary Arrowhead were recorded at their fair values using the purchase method of accounting.

The following table summarizes the estimated fair values of the assets acquired and liabilities assumed at the date of acquisition.

Purchase price:

Issue of 12,836,713 common shares of Bucking Horse	\$ 51,572,778
Cash	19,959,029
Reduction in promissory note	9,537,381
Issue of convertible debentures	47,508,293
Acquisition costs	290,007

\$ 128,867,488

BUCKING HORSE ENERGY INC.

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(Expressed in United States dollars, unless otherwise noted)

For the Nine Months ended September 30, 2009 and August 31, 2008

4. Business combination (continued):

Net assets acquired:	
Cash and cash equivalents	\$ 1,076,605
Promissory note	15,106,980
Accounts receivable	3,290,390
Income tax receivable	1,490,340
Oil and gas properties	168,269,586
Investments (note 6)	918,552
Accounts payable and accrued liabilities	(5,832,168)
Asset retirement obligations	(41,144)
Future income taxes	(55,411,653)
	<hr/>
	\$ 128,867,488

Under the terms of the Arrangement, Bucking Horse acquired all of the 24,608,642 issued and outstanding common shares of Gemini and all of the 320,000 existing stock options. The acquisition was funded through the issuance of common shares of the Company, the issuance of convertible debentures, the reduction of a promissory note receivable, the draw down of the credit facility and the remainder in cash as described further below. Gemini is now a wholly owned subsidiary of the Company and its shares have been delisted from the TSX.

Prior to closing the Arrangement, Gemini had four secured convertible debentures outstanding held by two major shareholders of the Company (the Debenture Holders), each in the principal amount of C\$5,000,000. Prior to the Arrangement, Gemini was a related party of the Company as the Debenture Holders were also significant shareholders of Gemini. Two of these debentures were issued in March 2004 (the March Debentures) and the other two were issued in August 2004 (the August Debentures).

The March Debentures were convertible into units of Gemini at a conversion price of C\$2.50 per unit, with each unit consisting of one Gemini common share and one share purchase warrant. Each of the March Debentures was converted concurrent with the closing of the Arrangement and the shares issued upon conversion were sold to the Company, together with the share purchase warrants, for the total sum of \$19,083,600 (C\$19,000,000), as contemplated under the Arrangement. The \$19,083,600 was paid by the issuance of two new convertible debentures by the Company (note 9).

The August Debentures were convertible into Gemini units at a conversion price of C\$4.00 per unit. The August Debentures were cancelled and replaced with two new convertible debentures at the closing of the Arrangement for a total sum of \$10,044,000 (C\$10,000,000) having the same terms as the August Debentures, except that they are convertible into units of the Company (note 9).

At the closing of the Arrangement, two additional new debentures for the total sum of \$20,088,000 (C\$20,000,000) were issued to the Debenture Holders as consideration for the 2,500,000 and 2,075,043 Gemini shares acquired from the Debenture Holders at C\$4.00 per share and as consideration for the \$1,707,307 (C\$1,699,828) cash received from one of the Debenture Holders which was used to fund a portion of the cash required to complete the Arrangement (note 9).

BUCKING HORSE ENERGY INC.

Notes to Consolidated Financial Statements
(Expressed in United States dollars, unless otherwise noted)

For the Nine Months ended September 30, 2009 and August 31, 2008

4. Business combination (continued):

As a result of the issuance of the new debentures and the assumption of the August Debentures, the Company has outstanding convertible debentures in the aggregate principal amount of \$49,215,600 (C\$49,000,000) held by the Debenture Holders (note 9).

Prior to closing the Arrangement, Gemini completed the sale of 12,000,000 (pre-consolidated) common shares of XXL Energy Corp., (XXL) an entity related to the Company by virtue of common directors, to Q Investments Ltd. (QIL), a major shareholder of the Company which is controlled by the Debenture Holders. The total consideration of \$15,106,980 (C\$15,040,800) was initially paid by QIL's issuance of a promissory note in favour of Gemini which was acquired by the Company pursuant to the Arrangement. The amount owing under the promissory note was reduced by \$9,537,381 (C\$9,495,600) as consideration for the 2,373,900 Gemini shares acquired from QIL at C\$4.00 per share pursuant to the Arrangement. The amount owing under the promissory note was further reduced through the cancellation of the Company's pre-existing loan payable to QIL of \$1,506,600 (C\$1,500,000) together with accrued interest. The resulting promissory note receivable was C\$4,045,200; the settlement of which is currently under negotiation. The note has been written down to \$1,275,111 (C\$1,365,261), in accordance with a business valuation performed by Evans & Evans, Inc., chartered business valuers, who were engaged by Bucking Horse and QIL to prepare a Comprehensive Valuation Report on the note payable due to Bucking Horse by QIL.

The promissory note is secured by a fixed charge over XXL shares purchased by QIL. Interest of \$191,267 (C\$204,789) has been accrued at period end, the value of which is also under negotiation.

The remaining 5,000,000 (pre-consolidated) common shares and 3,000,000 (pre-consolidated) warrants of XXL held by Gemini were acquired by the Company.

The Company issued 12,836,713 common shares of Bucking Horse to former Gemini shareholders, including 1,645,350 shares issued to one of the Debenture Holders, in exchange for 12,836,713 of the Gemini shares acquired at a deemed value of C\$4.00 per share for total consideration of \$51,572,778 (C\$51,346,852).

The Company paid cash of \$19,376,829 (C\$19,291,944) to acquire the remaining 4,822,986 of the Gemini shares. The Company also paid the aggregate sum of \$582,200 (C\$579,650) in exchange for the surrender and cancellation of existing Gemini stock options and incurred \$290,007 (C\$288,737) in transaction costs associated with the Arrangement.

5. Financial instruments:

- (a) The carrying values of cash and cash equivalents, accounts receivable, promissory note, income tax receivable and accounts payable and accrued liabilities approximate their fair values due to the short terms to maturity of these financial instruments.

The fair value of the bank indebtedness has been estimated by management by discounting the future contractual cash flows under current financing arrangements at discount rates which represent borrowing rates presently available to the Company for a loan with similar terms, risks and maturities. Management estimates that at September 30, 2009, the fair value of the bank indebtedness is equal to the carrying value reflecting the actual interest rates incurred by the Company being the same as equivalent current rates.

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5. Financial instruments (continued):

The fair value of the convertible debentures is not readily determinable due to their related party nature and the absence of a market for such investments.

(b) Derivative instruments:

The Company has entered into the following open commodity derivative financial contracts to manage price risk on a portion of its natural gas production for the periods referenced below.

Type	Volume MMBTU/Day	Contract period	Price US\$/MMBTU
Swap ⁽¹⁾	2,500	Calendar 2009	\$9.66 / MMBTU
Swap ⁽¹⁾	2,500	Calendar 2009	\$3.62 / MMBTU
Swap ⁽²⁾	2,500	Calendar 2010	\$6.20 / MMBTU
Swap ⁽²⁾	1,000	Calendar 2010	\$6.48 / MMBTU
Swap ⁽²⁾	3,000	Calendar 2011	\$7.23 / MMBTU

⁽¹⁾ Panhandle Eastern basis

⁽²⁾ Dominion Appalachia basis

On June 11, 2009, the Company entered into two new commodity swap contracts, committing an additional 1,000 MMBTU / day in calendar 2010 and 3,000 MMBTU / day in calendar 2011 at prices of \$6.48 and \$7.23 per MMBTU respectively.

The Company has engaged in currency hedging activities and on November 25, 2008 contracted to purchase C\$6,113,000 during the calendar 2009 at an exchange rate of C\$1.2226 per US\$. On March 5, 2009, the Company contracted to purchase C\$4,584,600 during calendar 2010 at an exchange rate of C\$1.2735 per US\$. In May, 2009, the company realized a \$760,731 gain through the early settlement of its currency contracts and as at September 30, 2009 has no currency contracts outstanding.

As at September 30, 2009, the unrealized loss on outstanding derivative financial contracts was \$3,389,868 (August 31, 2008 – gain of \$2,927,776).

The net gain on derivative financial contracts for the nine months ended September 30, 2009 of \$5,250,394 (August 31, 2008 – loss of \$88,040) has been included in other income in the statement of operations.

On October 19, 2009 three additional commodity swap contracts were committed to as follows:

Type	Volume MMBTU/Day	Contract period	Price US\$/MMBTU
Swap ⁽²⁾	1,000	Calendar 2010	\$6.50 / MMBTU
Swap ⁽²⁾	1,000	Calendar 2011	\$7.11 / MMBTU
Swap ⁽²⁾	3,500	Calendar 2012	\$7.22 / MMBTU

⁽²⁾ Dominion Appalachia basis

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6. Investments:

	Number of Shares	As at September 30 2009	As at December 31 2008
Investment in shares of Giant Energy Limited (Giant)	1,000,000	\$ 233,492	\$ 205,254
Investment in warrants of XXL	150,000	798	466
Investment in shares of XXL	333,700	67,008	68,493
		\$ 301,298	\$ 274,213

On May 21, 2008, the Company participated in a private placement conducted by Giant pursuant to which the Company acquired 1,000,000 common shares of Giant at a price of C\$0.25 per shares for a total cost of \$235,272 (C\$250,000). This is a non-arm's length transaction by virtue of a common officer of both companies and a common shareholder. The investment in shares of Giant is carried at cost as there is no active market for Giant's shares.

As at September 30, 2009, the Company holds 150,000 warrants of XXL, each of which entitles the Company to purchase one common share of XXL at an exercise price of \$20.00 per share. The warrants expire August 18, 2010. XXL is a related party by virtue of common directors. These warrants are classified as held-for-trading and are marked-to-market on an ongoing basis with changes in fair value recognized in net earnings.

7. Oil and natural gas properties:

	As at September 30 2009	As at December 31 2008
Proven, explored and impaired properties:		
Exploration and drilling costs	\$ 67,985,650	\$ 64,074,594
Acquisition and lease costs	97,437,864	83,269,064
Well equipment	8,549,135	7,311,890
Asset retirement	62,712	60,649
	174,035,361	154,716,197
Less accumulated depletion and depreciation	(11,860,940)	(6,420,662)
	\$ 162,174,421	\$ 148,295,535

For the nine months ended September 30, 2009, the Company has not capitalized any general and administrative expenses.

The Company has agreements to participate in the exploration of certain oil and natural gas leases. Failure by the Company to pay its share of a proposed capital program could result in the dilution or forfeiture of the Company's interest in these properties.

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8. Bank indebtedness:

In connection with the Arrangement, Bucking Horse and Gemini (Guarantors) and Arrowhead (Borrower) entered into a credit agreement dated March 4, 2008 for a five year senior revolving credit facility in the aggregate principal amount of up to \$100,000,000, with an initial borrowing base of \$30,000,000, available pursuant to the terms set out in the Credit Agreement. The debt is secured by mortgages on the oil and gas properties of Arrowhead.

The facility has an interest rate that floats, based on both the LIBOR rate and a spread, which will increase based on the percentage of availability drawn, resulting in a current interest rate of approximately 3.00%. The Company currently has drawn \$18,500,000 from the Credit Facility, of which \$10,500,000 was drawn on March 4, 2008 to fund a portion of the cash required to complete the Arrangement (note 4) and has \$11,500,000 left available as at September 30, 2009.

The Company is required to ensure that Arrowhead's interest coverage ratio is greater than 2.5 to 1.0, that Arrowhead's ratio of total indebtedness to earnings before interest income taxes, depletion, depreciation and accretion, and exploration expenses is greater than 3.5 to 1.0, and that the Company's current ratio is greater than 1.0 to 1.0.

9. Convertible debentures:

	For the nine months ended September 30, 2009	For the four months ended December 31, 2008
First Debentures (a)	\$ 17,745,400	\$ 15,599,343
Second Debentures (b)	9,339,684	8,210,181
Third Debentures (c)	18,679,369	16,420,361
	45,764,453	40,229,885
Less cumulative accretion remaining	(21,468,484)	(19,641,133)
	\$ 24,295,969	\$ 20,588,752

(a) On March 4, 2008 as part of the Arrangement, two convertible debentures (the First Debentures) were issued by the Company to the Debenture Holders. Each of the First Debentures is in the principal amount of \$8,872,700 (C\$9,500,000). The First Debentures mature on March 4, 2018, bear interest at a rate of 10% during the first six years and 15% during the remaining four years and are convertible into units during the first five years at a conversion price of C\$4.875 per unit and into shares at a conversion price of C\$4.875 per share during the last five years. Each unit consists of one common share of the Company and one share purchase warrant. Each share purchase warrant entitles the holder to purchase one additional common share of the Company for C\$4.875 until the fifth anniversary of the date of issuance, at which date these share purchase warrants will expire. The Debenture Holders may elect to accelerate the maturity date to the sixth anniversary date at any time during the first five years. Effective May 16, 2008, as a result of an interest rate acceleration provision, the interest rate applicable to the First Debentures increased from 10% to 15%.

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9. Convertible debentures (continued):

Repayment of the First Debentures is guaranteed by the Company's subsidiary Arrowhead, which has provided a mortgage and security agreement to each of the Lenders which is subordinated to other debt under the credit facility. The First Debentures are redeemable by the Company upon thirty days written notice without penalty or bonus; however, the Debenture Holders may elect to convert all or any of the First Debentures during the thirty day notice period.

The equity portion of the First Debentures was assigned a total value of \$10,103,765 (C\$10,054,257) upon issuance of the First Debentures, which was recorded in equity portion of debentures payable. The First Debentures were initially recorded net of the Conversion Option and are being accreted to their face value over their term. For the nine months ended September 30, 2009, accretion of \$211,645 (four months ended December 31, 2008 - \$78,243) has been included in accretion expense. Accretion of the First Debentures is calculated using an effective interest rate of 39.36%.

- (b) On March 4, 2008 as part of the Arrangement, two additional convertible debentures (the Second Debentures) were issued by the Company to Debenture Holders. Each of the Second Debentures is in the principal amount of \$4,669,842 (C\$5,000,000). The Second Debentures mature on August 4, 2014, bear interest at a rate of 10% up to August 4, 2010 and 15% during the last four years and are convertible into units up to August 4, 2009 at a conversion price of C\$4.00 per unit and into shares at a conversion price of C\$4.00 per share during the last five years. Each unit consisted of one common share of the Company and one share purchase warrant. Each share purchase warrant entitled the holder to purchase one additional common share of the Company for C\$4.00 until August 4, 2009, at which date these share purchase warrants expired. The Debenture Holders may elect to accelerate the maturity date to August 4, 2010 at any time up to August 4, 2009. Effective May 16, 2008, as a result of an interest rate acceleration provision, the interest rate applicable to the First Debentures increased from 10% to 15%.

Repayment of the Second Debentures is guaranteed by the Company's subsidiary Arrowhead, which has provided a mortgage and security agreement to each of the Lenders which is subordinated to other debt under the credit facility. The Second Debentures are redeemable by the Company upon thirty days written notice without penalty or bonus; however, the Debenture Holders may elect to convert all or any of the Second Debentures during the thirty day notice period.

The equity portion of the Second Debentures was assigned a total value of \$4,589,831 (C\$4,567,341) upon issuance of the Second Debentures, which was recorded in equity portion of debentures payable. The Second Debentures were initially recorded net of the Conversion Option and are being accreted to their face value over their term. For the nine months ended September 30, 2009, accretion of \$366,216 (four months ended December 31, 2008 - \$135,077) has been included in accretion expense. Accretion on the Second Debentures is calculated using an effective interest rate of 39.94%

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9. Convertible debentures (continued):

(c) On March 4, 2008 as part of the Arrangement, two more convertible debentures (the Third Debentures) were issued by the Company to the Debenture Holders. Each of the Third Debentures is in the principal amount of \$9,339,684 (C\$10,000,000). The Third Debentures mature on March 4, 2018, bear interest at a rate of 10% during the first six years and 15% during the last four years and are convertible into units during the first five years at a conversion price of C\$4.875 per unit and into shares at a conversion price of C\$4.875 per share during the last five years. Each unit consists of one common share of the Company and one share purchase warrant. Each share purchase warrant entitles the holder to purchase one additional common share of the Company for C\$4.875 until the fifth anniversary of the date of issuance, at which date these share purchase warrants will expire. The Debenture Holders may elect to accelerate the maturity date to the sixth anniversary date at any time during the first five years. Effective May 16, 2008, as a result of an interest rate acceleration provision, the interest rate applicable to the Third Debentures increased from 10% to 15%.

Repayment of the Third Debenture is guaranteed by the Company's subsidiary Arrowhead, which has provided a mortgage and security agreement to each of the Lenders which is subordinated to other debt under the credit facility. The Third Debentures are redeemable by the Company upon thirty days written notice without penalty or bonus; however, the Debenture Holders may elect to convert all or any of the Third Debentures during the thirty day notice period.

The equity portion of the Third Debentures was assigned a total value of \$10,635,543 (C\$10,583,428) upon issuance of the Third Debentures, which was recorded in equity portion of debentures payable. The Third Debentures were initially recorded net of the Conversion Option and are being accreted to their face value over their term. For the nine months ended September 30, 2009, accretion of \$222,783 (four months ended December 31, 2008 - \$82,361) has been included in accretion expense. Accretion on the Third Debentures is calculated using an effective interest rate of 39.36%.

10. Asset retirement obligations:

The Company's asset retirement obligations result from net ownership interest in oil and gas properties including well sites, gathering systems and processing facilities. The Company estimates the total undiscounted amount of cash flows required to settle its asset retirement obligations is approximately \$1,433,800. The majority of the costs will be incurred after 2050. An inflation factor of 2.0% has been applied to the estimated asset retirement costs. A rate of 10% was used to calculate the fair value of the asset retirement obligations. A reconciliation of the asset retirement obligations is provided below:

	At at September 30 2009	As at December 31 2008
Balance, beginning of year	\$ 69,176	\$ 44,066
Additions during the year	-	18,225
Accretion expense	9,098	6,885
Balance, end of year	\$ 78,274	\$ 69,176

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11. Earnings per share:

As at September 30, 2009, the conversion feature of the convertible debentures into 10,500,000 common shares would be anti-dilutive. Therefore, diluted net earnings (loss) per common share equals basis net earnings (loss) per common share.

12. Share capital:

(a) Share transactions:

Authorized capital at September 30, 2009 and December 31, 2008 consists of unlimited common shares without par value.

Share transactions for the nine months ended September 30, 2009 and year ended December 31, 2008 were as follows:

	Number of shares	Amount (net)
Outstanding shares at August 31, 2008	23,017,013	61,708,718
Shares repurchased	(22,500)	(60,323)
Balance, December 31, 2008	22,994,513	61,648,395
Balance, September 30, 2009	22,994,513	61,648,395

During the four months ended December 31, 2008, the Company repurchased 22,500 shares through a normal course issuer bid at a cost of \$121,884. The excess cost of the shares over the assigned value totaled \$61,561 and has been charged to retained earnings. The shares repurchased were cancelled and returned to treasury on November 17 (14,600 shares) and December 23, 2008 (7,900 shares).

During the nine months ended September 30, 2009, the Company repurchased 19,600 shares through a normal course issuer bid at a cost of \$54,917 (C\$58,800). To date the shares have not been returned to treasury for cancellation.

(b) Stock option plan:

The Company has a stock option plan for its key employees, directors and certain other persons under certain conditions. Under the plan, options may be granted to purchase up to 10% of the outstanding shares of the Company to a maximum of 822,500 options. Options granted under the plan vest at a rate of 25% per year and expire five years after the date of grant. The exercise price of options granted may not be less than the closing trading price of the Company's shares on the last trading day preceding the date on which the options are granted. As at December 31, 2008 and September 30, 2009, no stock options have been issued under the plan.

The stock option plan was amended to increase the maximum number of options available to be granted to 2,306,000 options. The Company received regulatory approval December 1, 2008.

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13. Related party transactions:

Related party transactions are in the normal course of operations and measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties.

Related party transactions for the periods ended September 30, 2009 and August 31, 2008 are as follows:

	For the nine months ended September 30, 2009	For the nine months ended August 31, 2008
General and administrative expenses:		
Office, rent, administration and professional services charged by a company controlled by one of the Debenture Holders	\$ 344,751	\$ 211,268
Directors fees	3,847	7,935
Interest paid to Debenture Holders	4,712,344	3,138,834

Amounts due to or prepaid to related parties as at September 30, 2009 and August 31, 2008 are as follows:

	For the nine months ended September 30, 2009	For the nine months ended August 31, 2008
General and administrative expenses:		
Prepaid office, rent, administration and professional services charged by a company controlled by one of the Debenture Holders	519,192	37,813
Amount receivable from Giant providing oil and gas consulting, operational, technical and business management services	275,436	225,072

In addition to the amount receivable from Giant, the Company has an investment in Giant shares as disclosed in note 6. The Company terminated its agreement with Giant during the period under which Giant provided oil and gas consulting, operations, technical and business management services to the Company. The Company is currently in negotiations with Giant in respect of recovering the amount receivable as at September 30, 2009. There is no active market for the Company's investment in Giant shares. The recoverability of the amount due from Giant is dependent upon the profitable operation of its business and/or the ability of Giant to raise additional financing.

On November 10, 2006, the Company entered into a loan agreement with QIL pursuant to which QIL provided the Company with a loan in the principal amount of \$1,327,434 (C\$1,500,000). The loan was cancelled as part of the Arrangement. As part of the Arrangement, a promissory note was given by QIL to the Company for a principal amount of \$15,106,980 (note 4). The amount owing was further reduced by \$9,537,381 (C\$9,495,600) as consideration for the 2,373,900 Gemini shares acquired from QIL at C\$4.00 as part of the Arrangement. The resulting promissory note receivable was C\$4,045,200; the value of which is currently under negotiation for settlement.

Other related party transactions are disclosed in notes 4, 6 and 9.

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14. Contingency:

During the second quarter of 2006, Arrowhead and other unrelated defendants were served with a lawsuit alleging that certain properties, including some of the properties owned by Arrowhead, are subject to a 5% net profits interest owned by the plaintiffs and that all of the defendants, including Arrowhead, are in default of their obligations under this 5% net profits interest to pay money to the plaintiffs. On May 25, 2007, Arrowhead obtained a declaratory order from the trial court quieting title with respect to some of the property owned by Arrowhead. After we obtained this order quieting title, Arrowhead leases that remain encumbered by this lawsuit consist of five Warbonnet leases totaling 2,040 gross acres (867 net acres) and at the time, 13 developed wells (5.5 net). On August 6, 2007, the trial court granted partial summary judgment in favor of the plaintiffs, holding that the net profits contract did not terminate with the Pinedale Unit, a federal exploration unit formed in 1953 and terminated in 1981, and that the obligation to pay the net profits is a "lease based" obligation which runs with the land. On August 10, 2007, the trial court granted another partial summary judgment in favor of the plaintiffs, holding that they owned the net profits contract. Trial on the issue of whether the defendants owe any compensatory damages and on our affirmative defenses was held in October 2007. At trial, the Judge dismissed the plaintiffs' claim that the defendants, including Arrowhead, had breached any implied covenant of good faith and he dismissed the plaintiffs' claims against Arrowhead brought under the Wyoming Royalty Payment Act (a Wyoming statute providing for interest on unpaid royalty payments). The Court also dismissed the plaintiffs' claims before March of 2006, the month after the plaintiffs notified the operators of their claim. On April 14, 2008, the Judge entered a judgment in the amount of \$4,896,589 against the defendants, jointly and severally. The Judge denied the defendants' Motions to Alter or Amend the Judgment on May 21, 2008. The Company filed its Notice of Appeal with the Wyoming Supreme Court on June 16, 2008. On July 1, 2008, the Judge issued an order granting the plaintiffs' Motion for Attorney Fees and entered a judgment in the amount of \$3,917,289 against the operator Defendants. Arrowhead is not an operator and therefore not subject to this judgment. The Appeal was argued on May 14, 2009 and a decision is pending. We will continue to update our disclosure with respect to this lawsuit as events require.

15. Financial risk exposure and risk management:

The Company is exposed in varying degrees to a number of risks arising from financial instruments. The Board of Directors has overall responsibility for the establishment and oversight of the Company's risk management framework. Management's close involvement in the operations allows for the identification of risks and variances from expectations. The Board approves and monitors the risk management process.

The types of risk exposure and the way in which such exposures are managed are as follows:

(a) Credit risk:

Credit risk is the risk of financial loss to the Company if a counterparty to a financial instrument fails to meet its payment obligations. The Company's exposure to credit risk includes cash and cash equivalents, accounts receivable, promissory note, and derivative instruments. The risk exposure is limited to their carrying amounts at the balance sheet date.

Cash and cash equivalents and derivative instruments are maintained with one financial institution. The risk is mitigated because the financial institution is a major institution with high credit rating.

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15. Financial risk exposure and risk management (continued):

(a) Credit risk (continued)

Accounts receivable primarily consist of revenues due from the sale of oil and gas. To reduce credit risk, the Company regularly reviews the collectability of the accounts receivable and there is no indication that these amounts will not be fully recoverable. Canadian currency accounts receivables account for \$73,193 (C\$78,368) of the Company's total accounts receivable.

The promissory note is due from QIL, which has sufficient assets to pay any amount negotiated on the note.

(b) Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they become due. The Company manages its liquidity risk by actively forecasting, planning, reviewing and monitoring expenditures and commitments and anticipated financial requirements.

Cash and cash equivalents on hand at September 30, 2009 and expected cash flows for the next 12 months are sufficient to fund the Company's ongoing operational needs.

In addition, the Company maintains a \$30,000,000 line of credit with the Bank of Montreal, of which it had drawn down \$18,500,000 at the end of the period.

Contractual Obligations (US\$)	Payments Due by Period				
	Total	Less than 1 year	1 – 3 years	4 – 5 years	After 5 years
Long Term Debt ⁽¹⁾	45,764,453	nil	nil	nil	45,764,453
Accounts Payable and Accrued Liabilities	1,512,906	1,512,906	nil	nil	nil
State Resource Taxes Payable	365,443	365,443	nil	nil	nil
Income Taxes Payable	793,561	793,561	nil	nil	nil
Capital Lease Obligations	nil	nil	nil	nil	nil
Operating Leases	nil	nil	nil	nil	nil
Purchase Obligations	nil	nil	nil	nil	nil
Other Long Term Obligations ⁽²⁾	78,274	nil	nil	nil	78,274
Line of Credit	18,500,000	nil	nil	18,500,000	nil
Total Contractual Obligations	67,014,637	2,671,910	0	18,500,000	45,842,727

⁽¹⁾ First, second and third convertible debentures (C\$49,000,000 translated at current exchange rate)

⁽²⁾ Asset retirement obligation

(c) Market risk

Market risk is the risk that changes in market prices, such as natural gas prices, foreign exchange rates and interest rates will affect the Company's income. The object of market risk management is to manage and control market risk exposures within acceptable parameters, while optimizing the return on risk.

The Company buys and sells derivatives in the ordinary course of business in order to manage market risks.

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15. Financial risk exposure and risk management (continued):

(c) Market risk (continued)

(i) Commodity risk

The Company is exposed to fluctuations in the price of oil and natural gas. It mitigates its risk by negotiating hedging contracts for up to 50% of its production (note 5(b))

A 10% change in the price of natural gas during the period would have changed equity and net income by \$403,000.

(ii) Currency risk

The Company is exposed to the financial risk related to the fluctuation of foreign exchange rates. The Company operates in Canada and the United States and a portion of its expenses are incurred in Canadian dollars. A significant change in the currency exchange rates between the US dollar relative to Canadian dollar could have an effect on the Company's results of operations, financial position or cash flows.

At September 30, 2009, the Company is exposed to currency risk through the following assets and liabilities denominated in Canadian dollars:

	September 30, 2009	December 31, 2008
Cash and cash equivalents	\$ 3,584,011	\$ 1,650,526
Accounts receivable	78,368	136,299
Promissory note	1,570,050	4,548,911
Prepaid expenses	161,663	180
Investments	322,600	333,992
Oil and natural gas properties	120,935,460	123,325,309
Accounts payable and accrued liabilities	(8,502)	(205,944)
Convertible debentures	(26,013,694)	(25,077,100)
Asset retirement obligation	(23,010)	(21,405)
	<u>\$ 100,606,945</u>	<u>104,690,768</u>
US dollar equivalent (period end)	93,963,711	85,953,011

A 10% change in the Canadian dollar against the United States dollar at September 30 would result in a change of \$942,000 to net income (December 31, 2008 - \$256,000) and \$9,484,000 to other comprehensive income (December 31, 2008 - \$8,070,000).

(iii) Interest rate risk

The majority of the Company's debt is in fixed rate debentures; however, the Company's income and cash flow is impacted by interest rate fluctuations on its bank loan of \$18,500,000. As at September 30, 2009, the Company did not have any interest rate hedges.

A change of 100 basis points in interest rates would have increased or decreased net income by \$218,000.

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16. Capital management:

The Company considers its capital structure to include working capital and shareholders' equity. Management's objective is to ensure that there is sufficient capital to minimize liquidity risk and to continue as a going concern. Management reviews its capital management approach on an ongoing basis and believes that its approach, given the relative size of the Company is reasonable.

The Company's objectives when managing capital are to:

- ensure there are adequate capital resources to safeguard the Company's ability to continue as a going concern;
- maintain adequate levels of funding to support the acquisition, exploration and development of petroleum and natural gas properties; and
- provide returns for shareholders and benefits for other stakeholders.

The Board of Directors does not establish quantitative return on capital criteria for management, but rather relies on the expertise of the Company's management to sustain future development of the business. There were no changes in the Company's approach to capital management during the period. Neither the Company nor any of its subsidiaries are subject to externally imposed capital requirements.

17. Segmented information:

The Company's activities consist of the exploration and development of oil and natural gas properties in Canada and the United States.

Selected segmented information is as follows:

Nine months ended September 30, 2009	Canada	United States	Total
Oil & Gas Revenue	\$ 122,720	\$ 9,147,501	\$ 9,270,221
Operating earnings (loss)	(69,468)	(560,551)	(630,019)
Capital expenditures	3,523	4,997,613	5,001,136
Total assets	6,640,075	167,250,119	173,890,194

Nine months ended August 31, 2008	Canada	United States	Total
Oil & Gas Revenue	\$ 513,595	\$ 15,061,834	\$ 15,575,429
Operating earnings (loss)	212,119	6,691,846	6,903,965
Capital expenditures	0	1,501,379	1,501,379
Total assets	7,620,657	169,631,680	177,252,337

The Company's revenues are derived from sales to customers in the oil and gas industry. One customer buys all of the oil and gas produced by the Canadian property. The sales of the United States properties are made to three customers.