



LOON ENERGY CORPORATION
CONSOLIDATED FINANCIAL STATEMENTS
FOR THE YEARS ENDED DECEMBER 31, 2010 AND 2009



Management's Report

The Consolidated Financial Statements of Loon Energy Corporation and related financial information were prepared by, and are the responsibility of Management. The Consolidated Financial Statements have been prepared in accordance with Canadian generally accepted accounting principles. The Consolidated Financial Statements and related financial information reflect amounts which must of necessity be based upon informed estimates and judgments of Management with appropriate consideration to materiality. The Company has developed and maintains systems of controls, policies and procedures in order to provide reasonable assurance that assets are properly safeguarded, and that the financial records and systems are appropriately designed and maintained, and provide relevant, timely and reliable financial information to Management.

KPMG LLP are the external auditors appointed by the shareholders, and they have conducted an independent examination of the corporate and accounting records in order to express an Auditors' Opinion on these Consolidated Financial Statements.

The Board of Directors has established an Audit Committee. The Audit Committee reviews with Management and the external auditors any significant financial reporting issues, the Consolidated Financial Statements, and any other matters of relevance to the parties. The Audit Committee meets quarterly to review and approve the interim financial statements prior to their release, as well as annually to review the Company's annual Consolidated Financial Statements and Management's Discussion and Analysis and to recommend their approval to the Board of Directors. The external auditors have unrestricted access to the Company, the Audit Committee and the Board of Directors.

"Signed"

Norman W. Holton
Chief Executive Officer

"Signed"

Paul H. Rose, CA
Chief Financial Officer

April 20, 2011



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INDEPENDENT AUDITORS' REPORT

To the Shareholders of Loon Energy Corporation

We have audited the accompanying consolidated financial statements of Loon Energy Corporation, which comprise the consolidated balance sheets as at December 31, 2010 and 2009, the consolidated statements of operations and deficit, and cash flows for the years then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with Canadian generally accepted accounting principles, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained in our audits is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated balance sheet of Loon Energy Corporation as at December 31, 2010 and 2009, and the results of its consolidated operations and its consolidated cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Emphasis of Matter

Without qualifying our opinion, we draw attention to Note 2 in the consolidated financial statements which describes that Loon Energy Corporation will require capital to fund the development of its Colombian resource properties. These conditions, as described in Note 2, indicate the existence of a material uncertainty that may cast significant doubt about Loon Energy Corporation's ability to continue as a going concern.

KPMG LLP

Chartered Accountants
Calgary, Canada

April 20, 2011

Loon Energy Corporation
Consolidated Balance Sheets
 US\$

		December 31 2010	December 31, 2009
	Assets		
Current			
Cash and cash equivalents		\$ 575,782	\$ 1,969,109
Accounts receivable		<u>971,449</u>	<u>64,139</u>
		1,547,231	2,033,248
Property and equipment	(note 5)	<u>660,588</u>	<u>1,726,457</u>
		<u>\$ 2,207,819</u>	<u>\$ 3,759,705</u>
	Liabilities		
Current			
Accounts payable and accrued liabilities		\$ 759,446	\$ 584,306
Income taxes payable		<u>-</u>	<u>175,631</u>
		759,446	759,937
Asset retirement obligation	(note 6)	<u>256,310</u>	<u>126,109</u>
		<u>1,015,756</u>	<u>886,046</u>
	Shareholders' Equity		
Share capital	(note 8)	15,591,236	15,139,980
Contributed surplus	(note 10)	1,687,325	1,291,873
Deficit		(16,150,144)	(13,621,840)
Accumulated other comprehensive income		<u>63,646</u>	<u>63,646</u>
		<u>1,192,063</u>	<u>2,873,659</u>
		<u>\$ 2,207,819</u>	<u>\$ 3,759,705</u>
Future operations	(note 2)		

Loon Energy Corporation
Consolidated Statements of Operations and Deficit
 US\$

	For the year ended December 31,	
	2010	2009
Petroleum and natural gas sales	\$ -	\$ 46,114
Less: Royalties	-	(3,689)
	-	42,425
 Expenses		
Operating	-	271,231
General and administrative	972,902	544,650
Capital tax expense	16,000	-
Foreign exchange (gain) loss	68,731	(105,813)
Stock based compensation	(note 9) 395,452	-
Depletion and accretion	(note 6) 10,201	98,822
Impairment of petroleum and natural gas properties	(note 5) 1,186,804	-
	2,650,090	808,890
 Loss before income taxes	(2,650,090)	(766,465)
 Current income tax (recovery) expense	(note 13) <u>(121,786)</u>	<u>75,631</u>
 Net loss and comprehensive loss	(2,528,304)	(842,096)
 Deficit, beginning of year	<u>(13,621,840)</u>	<u>(12,779,744)</u>
 Deficit, end of year	<u>\$ (16,150,144)</u>	<u>\$ (13,621,840)</u>
 Net loss per share		
Basic and diluted	<u>\$ (0.03)</u>	<u>\$ (0.01)</u>

Loon Energy Corporation
Consolidated Statements of Cash Flows
US\$

		For the year ended December 31,	
		2010	2009
Operating activities			
Net loss		\$ (2,528,304)	\$ (842,096)
Items not involving cash:			
Depletion and accretion	(note 6)	10,201	98,822
Impairment of petroleum and natural gas properties	(note 5)	1,186,804	-
Shares granted for compensation	(note 8)	451,256	-
Stock based compensation		395,452	-
Foreign exchange loss		68,731	-
		(415,860)	(743,274)
Changes in non-cash working capital		(633,195)	324,791
		(1,049,055)	(418,483)
Investing			
Property and equipment expenditures		(289,276)	(780,702)
Changes in working capital related to capital expenditures		(54,996)	64,702
		(344,272)	(716,000)
Change in cash and cash equivalents		(1,393,327)	(1,134,483)
Cash and cash equivalents, beginning of year		1,969,109	3,103,592
Cash and cash equivalents, end of year		\$ 575,782	\$ 1,969,109
Supplemental cash flow information			
Taxes paid	(note 13)	\$ 61,543	\$ -

Loon Energy Corporation
Notes to Consolidated Financial Statements
For the years ended December 31, 2010 and 2009
US\$

1. Basis of preparation

Loon Energy Corporation (the “**Company**”) was incorporated pursuant to the provisions of the *Business Corporation Act* (Alberta) on October 30, 2008 in conjunction with the reorganization of Loon Energy Inc. (“**Loon**”). The reorganization of Loon resulted in the Company receiving the net assets associated with resource properties located in Colombia and Peru, where operations commenced in 2005 and 2007 respectively, and \$3,150,000 of cash. Upon implementation of the re-organization, Loon’s name was changed to Kulczyk Oil Ventures Inc (“**Kulczyk Oil**”).

The Company’s consolidated financial statements are presented in United States dollars and are in accordance with accounting principles generally accepted in Canada.

2. Future operations

The Company is an oil and gas exploration and development company with properties principally located in Colombia. Of the Company’s properties in Colombia, the Delta-1 well is in the development stage with two other wells in the exploration stage. The properties have no proved reserves at December 31, 2010. The Company does not generate production from operations to fund the continued exploration and development of all of the Company’s oil and gas properties.

These consolidated financial statements have been prepared on a going concern basis, which contemplates the realization of assets and settlement of liabilities in the normal course of business and do not reflect adjustments that would otherwise be necessary if the going concern assumption was not valid. To date, the Company’s exploration and development operations have been financed by way of equity issuances and by farm-out arrangements with third parties who pay for all or a portion of the Company’s expenditures to earn a portion of the Company’s ownership interests. The Company’s cash and existing farm-out arrangements are not sufficient to fund the exploration and development program over the next twelve months. Additional equity or farm-out arrangements will be required to fund the exploration and development program and there are no guarantees that additional equity or farm-out arrangements will be available when needed.

3. International operations

Colombia

Buganviles Association Contract

Through a farm-in agreement, the Company earned a 20% non-operated participating interest in the Buganviles Association Contract, an area which includes one suspended oil well. The Company has fulfilled its required work commitments with respect to this contract. The remaining lands held under this contract will expire in the second quarter of fiscal 2011, subject to extension which must be obtained from the Colombian national oil company. The Operator, Pacific Rubiales, has applied for an extension and the Company does not foresee any issue with obtaining the license extension and continuing with exploration as planned.

In September 2010, Loon Energy entered into a farm-out agreement with Petrodorado South America S.A. (“**Petrodorado**”) under which Petrodorado agreed to pay the Company’s 20% share of the authorized costs to drill and complete two wells in Colombia to earn 75% (net 15%) of the Company’s interest in the Buganviles Association Contract. The Company exercised its option to earn a reversionary interest equal to a 5% working interest through a payment by the Company of 50% of the authorized completion costs for both wells. As such, the working interest earned by Petrodorado under the terms of the farm-out agreement was reduced from 15% to 10%. As at December 31, 2010, the Company holds a 10% working interest in the Buganviles Association Contract.

Abanico Association Contract

The Company owns a 49% non-operated working interest in the area covered by the Abanico Association Contract that includes one suspended natural gas well. The Company fulfilled its required work commitments with respect thereto in 2007. The Company does not have any plans for further work in the Abanico Association Contract area.

Loon Energy Corporation
Notes to Consolidated Financial Statements
For the years ended December 31, 2010 and 2009
US\$

3. International operations and commitments

To date, the Company has received cash calls from the operator to fund the drilling and completion of these two wells. Upon the execution of the farm-out agreement in September 2010, the amounts became payable by Petrodorado. Petrodorado has paid a total of \$2 million under the farm-out. As such, the Company has recorded a receivable from Petrodorado for \$429,156 under the farm-out agreement in respect of the amount payable to the Colombian operator for the remaining amount due to fund the drilling of these two wells. The \$429,156 represents the unpaid cash calls to be paid by Petrodorado on behalf of the Company under the terms of the farm-out agreement and forms a portion of the accounts receivable and accounts payable balances.

Peru

In 2007, the Company's subsidiary, Loon Peru Limited ("Loon Peru"), signed an exploration license contract with PERUPETRO S.A. granting Loon Peru the right to explore for and produce hydrocarbons from Block 127 in the Marañon Basin area of northeast Peru. CEPSA Peru ("CEPSA") earned 80% of Loon Peru's interest in Block 127 in return for consideration consisting of the payment of the first \$10.75 million of expenditures incurred in fulfilling the minimum work commitment for the first exploration period. In 2010, the Phase 1 work commitments were satisfied. CEPSA also became operator pursuant to the agreement. The Company's share of total expenditures related to the first exploration period, including the seismic acquisition, was \$931,625.

CEPSA has elected, with Loon's concurrence, to not proceed into the second exploration phase and allowed the license for Block 127 to expire on November 16, 2010. CEPSA and the Company are currently developing and executing an abandonment plan for Block 127, which is expected to be completed by the end of 2011.

4. Significant accounting policies

(a) Principles of consolidation

The accompanying consolidated financial statements of the Company include the accounts of the Company and its wholly owned subsidiaries.

(b) Foreign currency

The reporting and functional currency of the Company and all its subsidiaries is the United States dollars ("US\$" or "\$"). Transactions in foreign currencies are translated to United States dollars at exchange rates as of the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies are translated to the Company's functional currency at the period-end exchange rate. Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are translated to the functional currency at the exchange rate at the date that the fair value was determined. Foreign currency differences arising on translation are recognized in profit or loss.

(c) Property and equipment

The Company follows the full-cost method of accounting for its resource activities, and accordingly all costs related to the exploration for and development of petroleum and natural gas reserves are accumulated in one cost centre for each country. Capitalized costs include: land, lease acquisition and concession costs, geological and geophysical expenditures, the carrying costs associated with undeveloped and non-producing properties, drilling and completion costs of productive and non-productive properties, and related production, gathering and plant equipment costs. A portion of overhead charges directly related to acquisition, exploration and development activities is capitalized. Proceeds received from the disposition of properties are normally credited to the cost centre without recognition of a gain or loss unless such treatment would result in a change of 20% or more to the depletion rate.

Loon Energy Corporation
Notes to Consolidated Financial Statements
For the years ended December 31, 2010 and 2009
US\$

4. Significant accounting policies (continued)

The Company performs a cost recovery test for each cost centre at least annually to evaluate and if appropriate, recognize impairment when the carrying value of property and equipment exceeds the undiscounted future cash flows from proven reserves using estimated future commodity prices. The amount of any impairment to be recognized is determined as the excess of the carrying value over fair value. Fair value is determined using proven and probable reserves together with undeveloped land, and is based on the present value of expected future cash flows discounted at the cost of capital relevant to the geographical location of the reserves.

The Company also completes an analysis of the carrying value of undeveloped properties at least annually to ensure there are no indicators of impairment. These indicators would include, but are not limited to, results of seismic reprocessing and acquisition, licence expirations, dry wells drilled and if management determines a project or property is no longer economically feasible.

(d) Depletion and depreciation

Depletion and depreciation of petroleum and natural gas properties and equipment is provided using the unit-of-production method and proved reserves. Expenditures on undeveloped properties are excluded from the depletion provision until related reserves are proven or impairment is recognized. Volumes are converted to equivalent units on the basis that one barrel of oil is equivalent to six thousand cubic feet of natural gas.

(e) Cash and cash equivalents

Cash and cash equivalents include cash on hand and short-term, highly liquid investments with original maturities of three months or less.

(f) Asset retirement obligations

The Company recognizes the fair value of its asset retirement obligation as a liability at the time it incurs an obligation for the future abandonment and reclamation costs resulting from its resource operations. The asset retirement obligation is initially measured at its estimated fair value, which is the discounted future value of the liability, with the liability then accreting each subsequent period until the obligation is settled. The estimated fair value of the asset retirement obligation is capitalized to the petroleum and natural gas properties and equipment accounts, and is depleted over the estimated useful life of these assets.

(g) Joint operations

The Company conducts all of its exploration, development and production activities with partners, and accordingly these consolidated financial statements reflect only the Company's proportionate interest in such activities.

(h) 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.

Loon Energy Corporation
Notes to Consolidated Financial Statements
For the years ended December 31, 2010 and 2009
US\$

4. Significant accounting policies (continued)

Financial assets and financial liabilities held-for-trading are measured at fair value with changes in fair values recognized in net earnings or loss. Financial assets available-for-sale are measured at fair value, with changes in fair values recognized in other comprehensive income. Financial assets held-to-maturity, loans and receivables and other financial liabilities are measured at amortized cost using the effective interest method of amortization.

Cash including short-term deposits are designated as held-for-trading and are measured at carrying value which approximates fair value due to the short-term nature of these instruments. Accounts receivable are designated as loans and receivables. Accounts payable and accrued liabilities are designated as other financial liabilities.

The fair value of cash and cash equivalents, accounts receivable and accounts payable approximates the carrying value. The Company does not hold any other financial instruments.

(i) Revenue recognition

Revenue derived from the sale of the Company's petroleum and natural gas products is recognized when title to the product passes from the Company to its customer and when collection is reasonably assured.

(j) Income taxes

Income taxes are calculated using the asset and liability method. Temporary differences arising from the difference between the tax basis of an asset or liability and its carrying amount on the balance sheet are used to calculate future income taxes and liabilities. Future income tax assets and liabilities are calculated using tax rates that are substantively enacted and are expected to apply in the periods that the temporary differences are expected to reverse. To the extent that management does not consider it more likely than not that a future income tax asset will be realized, a valuation allowance is provided.

(k) Stock based compensation

Options are accounted for using the fair value method which estimates the value of the options at the date of grant using the Black-Scholes option pricing model. The fair value thus established is recognized as an expense over the vesting period of the options with a corresponding increase to contributed surplus. When the options are exercised, the proceeds received and the applicable amount in contributed surplus are credited to share capital.

(l) Loss per share

Basic loss per share is calculated by dividing net loss by the weighted average number of common shares outstanding during the year. Diluted loss per share, when appropriate, is calculated using the treasury stock method which adjusts the weighted average shares outstanding to recognize the effect, if any, of in-the-money stock options.

(m) Use of estimates

In preparing the Company's consolidated financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities, the measurement and disclosure of contingent assets and liabilities at the date of the consolidated financial statements together with the reported amounts of revenues and expenses for the reporting periods then ended. Actual results could differ from these estimates. Estimates and judgements used are based on management's experience and the assumptions used are believed to be reasonable given the circumstances that exist at the time the consolidated financial statements are prepared. Predicting the outcome of future events cannot be done with certainty however, and therefore estimates used may change as new events occur, additional experience is acquired or the Company's operating environment changes.

Loon Energy Corporation
Notes to Consolidated Financial Statements
For the years ended December 31, 2010 and 2009
US\$

4. Significant accounting policies (continued)

Future Accounting Policy Changes

On February 13, 2008, the Canadian Accounting Standards Board confirmed that publicly accountable profit-oriented enterprises will be required to use International Financial Reporting Standards (“IFRS”) in interim and annual financial statements for fiscal years beginning on or after January 1, 2011. As such, the Company will adopt IFRS beginning January 1, 2011.

5. Property and equipment

	<u>December 31, 2010</u>	<u>December 31, 2009</u>
Petroleum and natural gas properties	\$ 9,266,709	\$ 9,145,774
Accumulated depletion and depreciation	(8,606,121)	(7,419,317)
	<u>\$ 660,588</u>	<u>\$ 1,726,457</u>

Petroleum and natural gas properties net book value by segment

Colombia	\$ 660,588	\$ 930,226
Peru	-	796,231
	<u>\$ 660,588</u>	<u>\$ 1,726,457</u>

The Company had no production from its Colombian properties in 2010 and the independent reserve evaluator has classified all reserves as probable. Until such time as production commences and proven reserves are assigned, no depletion will be taken on the Colombian petroleum and natural gas properties. The reduction in the balance of petroleum and natural gas properties in Colombia arises from an agreement with the Colombian operator to settle the outstanding account balance for an amount less than was previously recorded.

The Operator and the Company decided not to enter into the second exploration phase of the concession agreement resulting in a withdrawal from Block 127 in Peru. With the planned withdrawal of the Company from Block 127 in Peru, all previously capitalized petroleum and natural gas property expenditures related to Block 127 have been fully written off as at December 31, 2010 and an impairment charge of \$1,186,804 recorded.

6. Asset retirement obligation

The Company’s asset retirement obligations result from its working interest ownership in petroleum and natural gas properties in Colombia and Peru, including well sites, gathering systems and processing facilities. The Company’s estimate of the total undiscounted cash flows required to settle the asset retirement obligations is \$325,144 (December 31, 2009 - \$174,287) which is expected to be incurred between 2011 and 2016. A credit-adjusted risk-free rate of 9.0 percent and inflation at a rate of 2.0 percent were used to calculate the fair value of the asset retirement obligations.

	<u>December 31, 2010</u>	<u>December 31, 2009</u>
Balance beginning of year	\$ 126,109	\$ 111,293
Accretion	10,201	14,816
Additions	120,000	-
Balance, end of year	<u>\$ 256,310</u>	<u>\$ 126,109</u>

Loon Energy Corporation
Notes to Consolidated Financial Statements
For the years ended December 31, 2010 and 2009
US\$

7. Capital Management

As at December 31, 2010, the Company's working capital amounted to \$787,785 (December 31, 2009 - \$1,273,311). Consistent with prior years, the Company manages its capital structure to maximize financial flexibility making adjustments in light of changes in economic conditions and risk characteristics of the underlying assets. Further, each potential acquisition and investment opportunity is assessed to determine the nature and total amount of capital required together with the relative proportions of debt and equity to be deployed. The Company does not presently utilize any quantitative measures to monitor its capital.

8. Share capital

The Company is authorized to issue an unlimited number of common shares and an unlimited number of preferred shares.

	Number of Shares	Carrying amount
December 31, 2008 and December 31, 2009	95,991,364	\$ 15,139,980
Shares issued for compensation	3,500,000	451,256
December 31, 2010	99,491,364	\$ 15,591,236
	Years ended December 31	
	2010	2009
Weighted average number of shares outstanding	96,336,569	95,991,364

On November 25, 2010, a total of 3,500,000 shares were issued as compensation for services rendered by certain Officers and Directors of the company. The Company has not issued any preferred shares.

9. Stock based compensation

During the year ended December 31, 2010, the Company recorded \$395,452 (2009 - nil) of stock based compensation expense with respect to 9,580 000 options issued during the fourth quarter of fiscal 2010. The options were granted to Directors and other key individuals that provided technical and management services to the Company. The options vest annually with one third vesting immediately and one third vesting on the first and second anniversary of the grant date. The options have a term of five years. The Company has not capitalized any of the stock based compensation expense recorded.

The following table summarizes information about the options outstanding as at December 31, 2010:

Options outstanding			Options exercisable	
Exercise price	Options	Contractual life remaining, years (weighted average)	Options	Exercise price
\$ 0.13	9,580,000	4.90	3,193,333	\$ 0.13

Loon Energy Corporation
Notes to Consolidated Financial Statements
For the years ended December 31, 2010 and 2009
US\$

9. Stock based compensation (continued)

The fair value of each option granted is estimated as of the grant date using the Black-Scholes option pricing model. The following assumptions were used in arriving at the fair value of \$0.12 per option associated with stock options granted during the period:

	<u>December 31, 2010</u>
Risk free interest rate	1.77%
Expected life	2.4 to 3.4 years
Expected volatility	184%
Dividends	Nil

10. Contributed Surplus

	<u>Carrying Amount</u>
Balance, December 31, 2008 and 2009	\$ 1,291,873
Stock based compensation	395,452
Balance, December 31, 2010	<u>\$ 1,687,325</u>

11. Financial instruments

(a) Market Risk

Market risk is the risk that changes in market prices, such as foreign exchange rates and interest rates, will affect the Company's net income or the value of its financial instruments.

1. Interest rate risk

The Company maintains its cash and cash equivalents in instruments that are redeemable at any time without penalty thereby reducing its exposure to interest rate fluctuations thereon. Interest rate risk is not considered material.

2. Foreign currency exchange risk

The Company is exposed to risks arising from fluctuations in currency exchange rates between the Canadian dollar ("CAD") and the United States dollar. At December 31, 2010 and 2009 the Company's primary foreign currency exposure relates to Canadian dollar cash balances net of accounts payable and accrued liabilities in Canada as follows:

	Year ended December 31,	
	<u>2010</u>	<u>2009</u>
	CAD	CAD
Cash and cash equivalents	\$ 14,477	\$ 52,601
Accounts payable and accrued liabilities	(148,945)	(69,530)
Net foreign exchange exposure	<u>\$ (134,468)</u>	<u>\$ (16,929)</u>

At December 31, 2010 and 2009, the Company's net loss is not significantly impacted by changes in the US to Canadian dollar exchange rates.

Loon Energy Corporation
Notes to Consolidated Financial Statements
For the years ended December 31, 2010 and 2009
US\$

11. Financial instruments (continued)

(b) Credit risk

Management monitors credit risk by reviewing the credit quality of the financial institutions that hold the cash and cash equivalents.

The Company's accounts receivable as at December 31, 2010 were comprised largely of cash calls and recoverable value added taxes. The cash calls paid are advances to the joint venture operator in Colombia. The Company does not consider the credit risk relating to the outstanding amounts to be significant as the Company intends to engage in further work commitments with this Operator and any excess cash calls will be applied against future spending.

Additionally, the Company executed a reversionary interest option whereby 50% of completion costs were reimbursed to Petrodorado to re-acquire a 5% interest in two wells, Visure-1X and Tuquque-1X. These costs are considered receivable until such time as the wells have been completed. If the wells are not completed, the reversionary interest payment is refundable to the Company. The Company does not consider the credit risk relating to Petrodorado to be significant as the Company intends to continue in an ongoing partnership with Petrodorado with respect to the Visure-1X and Tuquque-1X wells.

(c) Liquidity risk

The Company monitors its liquidity position regularly to assess whether it has the resources necessary to fund planned exploration commitments on its petroleum and natural gas properties or that viable options are available to fund such commitments from new equity issuances or alternative sources of financing such as farm-out agreements. However, as an exploration company at an early stage of development and without internally generated cash flow, there are inherent liquidity risks, including the possibility that additional financing may not be available to the Company on either a timely or commercial basis or that actual exploration expenditures may exceed those planned. Alternatives available to the Company to manage its liquidity risk include deferring planned capital expenditures that exceed amounts required by work programmes to retain concession licences, farm-out arrangements and securing new equity or debt capital.

12. Related party transactions

The Company has no employees, and management and administrative services are provided by the management and staff of Kulczyk Oil pursuant to a services agreement. Administrative costs incurred by Kulczyk Oil for the benefit of the Company are allocated to the Company based on specific identification and an allocation of administrative costs that relate to both Kulczyk Oil and the Company. For the year ended December 31, 2010 these fees totalled \$11,976 (2009 - \$10,550). At December 31, 2010, the Company owed \$nil (2009 - \$nil) to Kulczyk Oil for these services. Certain expenditures of the Company are paid for by Kulczyk Oil on behalf of the Company and as at December 31, 2010 the Company owed \$nil (2009 - \$28,382) for these costs. During the year ended December 31, 2010 the Company reimbursed Kulczyk Oil for \$18,743 of expenditures paid on behalf the Company.

Kulczyk Oil remains legally responsible for a guarantee issued in August 2007 ("the **Loon Peru Guarantee**") to the Government of Peru regarding the granting of the Block 127 license contract to Loon Peru Limited, a wholly-owned subsidiary of the Company. The Company has entered into an indemnification agreement with Kulczyk Oil in respect of the Loon Guarantee. The transfer of the Loon Peru Guarantee from Kulczyk Oil to the Company requires the formal approval of the Government of Peru which has not yet been obtained. The Company has fulfilled its work commitments under the first phase of the exploration program, and the Company and its operator announced on October 25, 2010 that the joint venture will not proceed to the second exploration phase. As a result, the Company believes there is no longer a material exposure to the guarantee.

The above related party transactions were at exchange amounts agreed to by both parties which approximate fair value.

Loon Energy Corporation
Notes to Consolidated Financial Statements
For the years ended December 31, 2010 and 2009
US\$

13. Income taxes

The differences between the income tax provisions calculated using statutory rates and those reported are as follows:

	Years ended December 31,	
	2010	2009
Loss before income taxes	\$ (2,650,090)	\$ (766,465)
<i>Federal and provincial statutory rate</i>	<i>28.00%</i>	<i>29.00%</i>
Expected income tax recovery	\$ (742,025)	\$ (222,275)
Stock based compensation	110,727	-
Tax rate differences and change in valuation allowance	509,513	297,906
Current income tax expense (recovery)	<u>\$ (121,786)</u>	<u>\$ 75,631</u>

The tax effects of temporary differences that give rise to future tax balances are:

	December 31,	
	2010	2009
Property and equipment	\$ 530,672	\$ 10,609
Asset retirement obligations	77,382	31,541
Non-capital losses (expire up until 2030)	889,971	231,618
	1,498,025	273,768
Less: valuation allowance	(1,498,025)	(273,768)
Future income tax asset/(liability)	<u>\$ -</u>	<u>\$ -</u>

During fiscal 2009, a tax liability in the amount of \$175,631 was recorded with respect to expected taxes owing in Colombia by the Company's wholly-owned subsidiary Loon Colombia Limited for the 2007, 2008 and 2009 taxation years. During the third quarter of fiscal 2010, new information was obtained that indicated that actual tax payable was \$121,786 lower than originally expected. This change in estimate has been adjusted and recorded as a tax recovery in the period.

Loon Energy Corporation
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US\$

14. Segmented information

	For the year ended December 31, 2010			
	Colombia	Peru	Corporate	Total
General and administrative	\$ (231,990)	\$ 8,779	\$ (749,691)	\$ (972,902)
Capital tax expense	\$ (16,000)	\$ -	\$ -	(16,000)
Loss on foreign exchange	(8,964)	-	(59,767)	(68,731)
Stock based compensation	-	-	(395,452)	(395,452)
Depletion and accretion	(10,201)	-	-	(10,201)
Impairment of P&NG properties	-	(1,186,804)	-	(1,186,804)
Loss before income taxes	(267,155)	(1,178,025)	(1,204,910)	(2,650,090)
Current income tax recovery	121,786	-	-	121,786
Loss after income taxes	<u>\$ (145,369)</u>	<u>\$ (1,178,025)</u>	<u>\$ (1,204,910)</u>	<u>\$ (2,528,304)</u>
Capital expenditures	<u>\$ 18,702</u>	<u>\$ 390,574</u>	<u>\$ -</u>	<u>\$ 409,275</u>
Total assets	<u>\$ 1,449,796</u>	<u>\$ 202,058</u>	<u>\$ 555,965</u>	<u>\$ 2,207,819</u>
	For the year ended December 31, 2009			
	Colombia	Peru	Corporate	Total
Petroleum and natural gas sales	\$ 46,114	\$ -	\$ -	\$ 46,114
Royalties	(3,689)	-	-	(3,689)
Operating expenses	(271,231)	-	-	(271,231)
General and administrative	(59,076)	-	(485,574)	(544,650)
Gain on foreign exchange	-	-	105,813	105,813
Depletion and accretion	(98,822)	-	-	(98,822)
Loss before income taxes	(386,704)	-	(379,761)	(766,465)
Current income tax expense	(75,631)	-	-	(75,631)
Loss after income taxes	<u>\$ (462,335)</u>	<u>\$ -</u>	<u>\$ (379,761)</u>	<u>\$ (842,096)</u>
Capital expenditures (recoveries)	<u>\$ 75,011</u>	<u>\$ 705,691</u>	<u>\$ -</u>	<u>\$ 780,702</u>
Total assets	<u>\$ 930,226</u>	<u>\$ 796,231</u>	<u>\$ 2,033,248</u>	<u>\$ 3,759,705</u>