FALCON OIL & GAS AUSTRALIA LIMITED

ABN 53 132 857 008

31 DECEMBER 2009 FINANCIAL REPORT

All amounts are in USD unless otherwise stated

Acquisition of Beetaloo Permits

On 30 September 2008, Falcon Oil & Gas Limited ("Falcon") and Falcon Oil & Gas Australia Limited (the "Company") consummated the acquisition of an undivided 50% working interest in an aggregate 7,000,000 acres in four exploration permits (the "Permits") in the Beetaloo Basin, Northern Territory (the "Beetaloo Basin Project") pursuant to the terms of a Purchase and Sale Agreement, as amended on October 31, 2008, (the "Beetaloo PSA") with PetroHunter Energy Corporation, PetroHunter Operating Company and Sweetpea Petroleum Pty Ltd. ("Sweetpea") (collectively, "PetroHunter"), each of which is a non-arm's length party for the purposes of the TSX Venture Exchange (the "TSXV").

On 11 June 2009, pursuant to a second Purchase and Sale Agreement (the "Second PSA") with PetroHunter, the Company completed the acquisition of an additional undivided 25% working interest in the Beetaloo Basin Project. Under the terms of the Second PSA, the principal consideration being paid by the Company for this transaction was the exchange of a $5,000,000 note receivable from PetroHunter. In addition, the Company agreed to pay certain vendors who had provided goods or services for the Beetaloo Basin Project, prior to the Company acquiring its 50% interest in September 2008, in exchange for inventory and operator bonds of approximately the same value, and Falcon has relinquished its right to the unexpended testing and completion funds of the Buckskin Mesa Project (as defined below). Upon closing, the Company became operator of the Beetaloo Basin Project, and PetroHunter and Falcon entered into an escrow agreement governing the release of all remaining common shares of Falcon ("Common Shares") previously issued to PetroHunter.

The Permits are subject to a combined governmental royalty of between 10-12% and an overriding royalty to two arm's length third parties in an amount not to exceed 12.1%.

Operational Highlights

PetroHunter had previously drilled one well in 2007, the Shenandoah-1 well, which was cased and suspended at 5,100 feet (1,555 meters). In July 2009, the Company re-entered the Shenandoah-1 well, which reached a depth of 8,904 feet (2,714 meters) on 11 October 2009.

In the Shenandoah-1 well, significant gas shows were encountered in the Lower Kyalla Shale and the Middle Velkerri Shale. Shows were also encountered in the Moroak Sandstone which lies between the two thermally mature gas shales.

A 328-foot (100 meter) interval in the Lower Kyalla Shale encountered significant gas shows, with gas concentrations to 11%, and total gas reaching up to 1,000 units in the most favorable Kyalla gas interval at a depth of 5,167 feet to 5,495 feet (1,575 meters to 1,675 meters). A 433 foot (132 meter) interval in the Middle Velkerri Shale from 7,890 feet to 8,386 feet (2,405 meters to 2,556 meters) had similar gas shows. Several intervals in the Moroak Sandstone also had gas shows in a composite 295 foot (90 meter) interval in what appears to be a conventional structural trap.

Cores from both the Lower Kyalla and Middle Velkerri shales were taken for desorption analyses. Preliminary results indicate the shales are good gas reservoirs comparable to or exceeding recent gas shale desorption results in U.S. basins for Paleozoic source rocks.

The Shenandoah-1 well indicates a significant shallow oil zone within the Upper Kyalla Shale at a depth from 3,110 feet to 3,346 feet (948 meters to 1,020 meters). These oil and gas shows in the Shenandoah-1 well support the recent Ryder Scott evaluations (see below) of the conventional and unconventional oil and gas potential in the Precambrian sediments of the Beetaloo Basin, Northern Territory, Australia (see below).

Resource Estimates

In August 2009, the Company received a Resource Analysis Report from Ryder Scott Company - Canada (the "**Ryder Scott Report**") on the Beetaloo Basin Project, dated 5 August 2009 and effective as of 1 July 2009. The Ryder Scott Report on the hydrocarbon resource potential of the Beetaloo Basin describes a possible distribution of the un-risked prospective (recoverable) portion of un-risked "Undiscovered in-place Resources," as defined by the COGEH, and does not represent an estimate of reserves or contingent resources. The Ryder Scott Report has been prepared in accordance with the Canadian standards set out in the COGEH and is compliant with NI 51-101. Ryder Scott's resource evaluation of the Beetaloo Basin is as follows:

Table 1: Total Undiscovered and Prospective (Recoverable) Oil Resources in the Beetaloo Basin, Australia (1) (2)

	Un-risked Undiscovered Oil-In-Place (Bstb)			**Un-risked Prospective (Recoverable) Oil Resources (Bstb)**		
	Low	**Best**	**High**	**Low**	**Best**	**High**
Hayfield	0.049	0.088	0.148	0.005	0.010	0.018
Jamison	8.220	11.920	16.402	0.800	1.337	2.153
Conventional subtotal	8.269	12.008	16.550	0.805	1.347	2.171
Upper Kyalla shale oil	127.4	180.9	256.0	11.3	17.8	27.4
Shale oil subtotal	127.4	180.9	256.0	11.3	17.8	27.4
Total oil resource within the Beetaloo Basin	135.67	192.91	272.55	12.11	19.15	29.57

Based upon their review of the preliminary results from the re-entry and deepening of the Shenandoah-1 well, Ryder Scott Company – Canada provided correspondence dated 23 October 2009 that confirmed the findings in the above resource evaluation.

Table 2: Total Undiscovered and Prospective (Recoverable) Gas Resources in the Beetaloo Basin, Australia(1) (2)						
	Un-risked Undiscovered Gas-In-Place (Tscf)			Un-risked Prospective (Recoverable) Gas Resources (Tscf)		
	Low	**Best**	**High**	**Low**	**Best**	**High**
Hayfield (associated solution)	0.013	0.025	0.046	0.002	0.004	0.009
Jamison (associated solution)	2.041	3.330	5.349	0.313	0.585	1.066
Moroak	0.800	1.437	2.346	0.607	1.048	1.731
Conventional subtotal	2.85	4.79	7.74	0.92	1.64	2.81
Moroak BCGA	21.00	29.61	40.85	3.18	4.85	7.23
Bessie Creek BCGA	159.4	210.0	275.0	23.8	34.4	49.4
BCGA subtotal	180.39	239.58	315.81	27.02	39.28	56.64
Lower Kyalla shale gas	12.70	15.80	19.20	1.90	2.60	3.50
Middle Velkerri shale gas	94.6	125.1	160.4	14.2	20.4	29.0
Shale gas subtotal	107.3	140.9	179.6	16.1	23.0	32.5
Total gas resource within the Beetaloo Basin	290.54	385.27	503.16	44.05	63.91	91.94

(1) Tables 1 and 2 are from the Ryder Scott Report. The total oil and gas resource is an arithmetic summation of the multiple estimates of the individual reservoir resources. Undiscovered Petroleum Initially-In-Place (equivalent to undiscovered resources) is that quantity of petroleum that is estimated, on a given date, to be contained in accumulations yet to be discovered. Prospective Resources are those quantities of petroleum estimated, as of a given date, to be potentially recoverable from undiscovered accumulations by application of future development projects. Prospective resources have both an associated chance of discovery and a chance of development. There is no certainty that any portion of the undiscovered resources will be discovered and that, if discovered, it may not be economically viable or technically feasible to produce any of the resources,

(2) Estimates are as of 1 July 2009, the effective date of the Ryder Scott Report.

Future Operations

Under a work program approved by the Northern Territory Government, Department of Resources, on 31 March 2010, and subsequently amended on 25 June 2010, the Company was obligated to complete the following minimum work requirements:

Permit	Permit Year Start	Permit Year End	Minimum Work Requirement	Estimated Expenditure
EP 76	January 2009	December 2010	Geologic studies Reservoir assessment	A$200,000
	January 2011	December 2011	Drill 1 well, complete if warranted	A$3,700,000
EP 98	January 2010	December 2011	Complete & test well Geological studies	A$6,200,000
EP 99	January 2010	December 2011	G&G studies Geophysical re-evaluation	A$100,000
	January 2012	December 2012	Drill two wells	A$3,700,000
EP 117	January 2010	December 2011	Basin modelling re-evaluation	A$100,000
	January 2012	December 2012	G&G studies Reservoir assessment Drill & complete 1 well	A$1,300,000

The Directors have the pleasure in submitting their report together with the financial report of the Company and the auditor's report thereon for the period 21 August 2008 to 31 December 2009.

All amounts referred to in this report and the accompanying Financial Statements are in US dollars, unless stated otherwise.

Directors

The names of directors of the Company holding office at any time during or since the end of the financial period are:

Robert C Macaulay	Chairman appointed 31 July 2010
Evan Wasoff	Director since 21 August 2008
Martin Oring	Director appointed 31 July 2010
Kym P Livesley	Director appointed 31 July 2010
John W Carroll	Director appointed 31 July 2010
Marc Bruner	Director 21 August 2008 to 10 November 2010
Carmen J Lotito	Director 21 August 2008 to 31 July 2010
John L. Blue	Director 21 August 2008 to 14 May 2010

Robert Macaulay, PEng- Non-Executive Director, Chairman

Mr. Macaulay has 26 years' industry experience in petroleum engineering, field development planning and business development and currently provides consulting services in these areas. He is a director of PetroGlobe Inc. (TSX – PGB), serving on the compensation committee and as chairman of the reserves committee. He held the post of V.P. Engineering and Production at Centurion Energy International Inc., a Canadian company active in Egypt which was sold at over 30,000 boepd in 2007. His past experience includes positions of increasing responsibility at Vermilion Resources (petroleum engineering for France properties and business development in Europe), Shell (reservoir engineering in Canada and the Sultanate of Oman) and PanCanadian Petroleum Ltd.

He holds a BSc (Hons) in Chemical Engineering from Queen's University, Ontario and MBA degrees from Queen's and from Cornell University, New York (with distinction). He is a member of APEGGA and SPE.

Evan Wasoff - Non-Executive Director

Mr. Wasoff has been Chief Financial Officer of Falcon Oil & Gas Ltd. since 1 April 2005. Mr. Wasoff has over 30 years of experience as a Certified Public Accountant. In 1985, he founded Wheeler Wasoff, P.C., a Denver, Colorado CPA firm specializing in companies filing with the U.S. Securities and Exchange Commission between 1985 and 2005. Mr. Wasoff has been a consultant to Chartered Accounting firms in Calgary, Alberta, and Vancouver, British Columbia in securities matters and financial reporting issues in Canada and the United States. Prior to forming Wheeler Wasoff, P.C., he was a member of the audit staffs of Pannell, Kerr, Forster & Co. and Price Waterhouse. Mr. Wasoff holds an MBA in Finance from the University of Colorado and a BS in Accounting from the State University of New York at Albany. He is a licensed CPA in Colorado and a member of the American Institute of Certified Public Accountants and the Colorado Society of Certified Public Accountants.

Martin B Oring, Non-Executive Director

Mr. Oring has been the Chairman of the Board of Directors of PetroHunter Energy Corporation since April 2009, its President and Chief Executive Officer since May 2009. Mr. Oring is an executive in the financial services and energy industries. Prior to forming his current business in 2001, Wealth Preservation, LLC, he had extensive experience as a member of management in several companies, including Prudential Securities (Managing Director of Executive Services), Chase Manhattan Corporation (Manager of Capital Planning), and Mobil Corporation (Manager, Capital Markets & Investment Banking). He has served as a director of Parallel Petroleum

Corporation, located in Midland, Texas, and currently serves as Chairman, CEO and President of Searchlight Minerals Corp., located in Henderson, Nevada. Mr. Oring received a B.S. degree in mechanical engineering from the Carnegie Institute of Technology in 1966 and an M.B.A. degree in production management, finance and marketing from Columbia University in 1968.

Kym Pelham Livesley- Non-Executive Director

Kym Livesley is a corporate lawyer with 32 years experience. Kym has substantial expertise in mergers and acquisitions, capital markets, takeovers and general corporate and commercial advice. Kym maintains an industry focus in the energy and resources sectors, for listed and private corporates in the Asia-Pacific region.

Kym also has experience in capital raising, IPOs, directors' duties, dual listings (AIM, TSX) and corporate governance.

Kym has a Bachelor of Laws from the University of Adelaide. Among other affiliations, Kym is a former National President of the Australian Mining and Petroleum Law Association (AMPLA), member of the Minerals Council NSW and is a fellow of the Australian Institute of Company Directors (AICD).

John Carroll - Non-Executive Director

Mr Carroll is a private consultant specialising in government relations and major project facilitation and has more than 40 years experience in a wide cross-section of public sector positions in Canberra, Queensland and the Northern Territory. Mr Carroll was Chief Executive Officer of the NT Department of Industries and Business from March 2000 until November 2001. Following that he was General Manager, Business and Trade Development, and Deputy Chief Executive and General Manager, Minerals and Energy, NT Department of Business Industries and Resource Development. In May 2005 he was appointed Chief Executive, NT Department of Primary Industry, Fisheries and Mines.

Prior to his time in the Northern Territory, Mr Carroll was Deputy Director-General, Business, Innovation and Trade in Queensland’s Department of State Development. From 1996 he worked in that State’s Department of Economic Development and Trade where he was Director-General until July 1998.

His earlier public sector appointments include managing the Business Regulation Review Unit in Queensland, Administration Manager, Australian National Gallery and a number of years at the Commonwealth Public Service Board, Canberra. Mr Carroll was President of the NT Branch of the Institute of Public Administration from 2001 to 2004 and in 2006/7. In November 2004 the National Council made him a Fellow of the Institute.

Company Secretary

Stephen Peterson – appointed 5 August 2008.

Mr Peterson is currently Chief Financial Officer and Company Secretary. He provides financial and administrative services on a contract basis to a number of companies in the resources industry. He has over 25 years experience in senior financial roles and as company secretary with listed public companies primarily in the resources industry in Australia.

Directors' meetings

The number of directors' meetings held, including meetings held by telephone, and the number of those meetings attended by each of the directors of the Company, while a director, during the financial period are as follows:

	Board meetings	
	Number of meetings held	Number of meetings attended
Robert C Macaulay	-	-
Evan Wasoff	1	1
Martin Oring	-	-
Kym P Livesley	-	-
John Carroll	-	-
Marc Bruner	2	2
Carmen J Lotito	2	2
John L Blue	2	2

Principal activities

The principal activity of the Company in the course of the period was exploration for oil and gas in the Beetaloo basin of the Northern Territory.

Financial results

The net loss after income tax attributable to members of the Company for the period from 21 August 2008 to 31 December 2009 was US$600,000.

Dividends

There were no dividends paid or declared by the Company during the period ended 31 December 2009.

State of affairs

There were no significant changes in the state of affairs of the Company that occurred during the financial period under review.

Operating and financial review

The operating and financial review of the Company during the period is detailed on pages 1 to 3 of this report.

Environmental regulation

The Company's operations are subject to Australian Commonwealth and Northern Territory environmental regulations and legislation. The Board believes the Company has adequate systems in place for the management of its environmental requirements and is not aware of any significant breach of those environmental requirements as they apply to the Company.

Events subsequent to balance date

There has not arisen in the interval between the end of the financial period and the date of this report any item, transaction or event of a material and unusual nature likely, in the opinion of the directors of the Company, to affect significantly the operations of the Company, the results of those operations, or the state of affairs of the Company, in future financial years, other than matters discussed in the Operating and Financial Review and the following matters:

- On 7 December 2009, Falcon Oil & Gas Limited ("Falcon") and the Company entered into a Binding Heads of Agreement (the "Agreement") with PetroHunter Energy Corporation and Sweetpea Petroleum Pty Ltd ("Sweetpea") wherein the Company agreed to issue to Sweetpea ordinary shares in consideration for the transfer of Sweetpea's undivided 25% working interest in the Permits. Falcon will enter into a Master Services Agreement (the "MSA") related to the operations of the Permits. Under the terms of the Agreement, Falcon will be issued 149,999,999 ordinary shares in the Company for conversion of a portion

($30,000,000) of the Company's debt payable to Falcon, which approximates Falcon's initial acquisition cost previously paid to Sweetpea for the 75% working interest in the Permits held by the Company as of the date of the Agreement. Sweetpea will be issued 50 million shares in the Company for its remaining 25% working interest in the Permits. On April 23, 2010, the Company received notice (the "Notice") from the Department of Resources, Northern Territory Government, that the registration of the transfer of the remaining 25% interest in the Permits was completed, satisfying all conditions precedent to closing. Pursuant to the Notice, the Company now owns 100% of the Permits.

- On 4 June 2010 the Company announced the closure of the first tranche of a private placement raising a total of US$4,895,659. On 1 December 2010 a further $1,217,578 was raised under the second tranche of the private placement, which is now closed. Under the terms outlined in the offer memorandum, each share allotted came with a free attached option. Each option entitles the holder to acquire one fully paid ordinary share at an exercise price of US$1.25 for a period of three years from the date of issue.

Likely developments

Further information as to likely developments in the operations of the Company and the expected results of those operations in subsequent years has not been included in this report because disclosure of this information would be likely to result in unreasonable prejudice to the Company.

Indemnification of officers and auditors

During or since the end of the financial year, the Company has not indemnified or made a relevant agreement to indemnify an officer or auditor of the Company against a liability incurred by such an officer or auditor.

In addition, the Company has not paid or agreed to pay, a premium in respect of a contract insuring against a liability incurred by an officer or auditor.

Options

During the year and to the date of this report, there were no unissued ordinary shares of the Company under option.

Lead Auditor's Independence Declaration under Section 307C of the Corporations Act 2001

The lead auditor's independence declaration is set out on page 8 and forms part of the directors' report for the period ended 31 December 2009.

Signed at Sydney this 10 day of December 2010 in accordance with a resolution of the Board of Directors:

RMacaulay

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Robert Macaulay
Director

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Auditor's Independence Declaration to the Directors of Falcon Oil and Gas Australia Pty Ltd

In relation to our audit of the financial report of Falcon Oil & Gas Australia Pty Ltd for the financial year ended 31 December 2009, to the best of my knowledge and belief, there have been no contraventions of the auditor independence requirements of the *Corporations Act 2001* or any applicable code of professional conduct.

Ernst & Young

Ernst & Young

Scott Jarrett
Partner
Sydney

10 December 2010

FALCON OIL & GAS AUSTRALIA LIMITED

Statement of Comprehensive Income for the financial period ended 31 December 2009

	Notes	21 August 2008 To 31 December 2009 US$'000
Revenue		
Revenue		**0**
Expenses		
Accounting & Audit Fees		**54**
Consultants Fees		**61**
Directors Fees		**16**
Management Fees		**232**
Legal Expenses		**88**
Travel Expenses		**334**
Miscellaneous		**6**
Results from operating activities		**(791)**
Financial income		**-**
Financial expenses		
- Foreign Currency Exchange Gains		**191**
Net financing gains		**191**
Impairment loss		**-**
Loss before tax		**(600)**
Income tax		**-**
Loss for the period		**(600)**
Other Comprehensive Income		**-**
Total Comprehensive Loss for the period		**(600)**

FALCON OIL & GAS AUSTRALIA LIMITED

Statement of Financial Position as at 31 December 2009

	Notes	31 December 2009 US$'000
Current assets		
Cash and Cash Equivalents	4	**144**
Receivables	5	**2,829**
Total current assets		**2,973**
Non-current assets		
Property Plant & Equipment	6	**1,666**
Exploration and Evaluation Assets	7	**37,648**
Other	8	**1,027**
Total non-current assets		**40,341**
Total assets		**43,314**
Current liabilities		
Payables and Accruals	9	**211**
Related Party Loan	10	**43,463**
Total current liabilities		**43,674**
Non-current liabilities		
Other	11	**240**
Total non-current liabilities		**240**
Total liabilities		**43,914**
Net liabilities		**(600)**
Equity		
Issued Capital	12	**-**
Retained Losses	12	**(600)**
Total equity		**(600)**

Statement of Cash Flows for the financial period ended 31 December 2009

	Notes	21 August 2008 to 31 December 2009 US$'000
Cash flows from operating activities		
Cash payments in the course of operations		**(3,218)**
Net cash flows from operating activities	13	**(3,218)**
Cash flows from investing activities		
Property, Plant & Equipment		**(1,666)**
Exploration & evaluation		**(37,408)**
Other non current assets		**(1,027)**
Net cash flows from investing activities		**(40,101)**
Cash flows from financing activities		
Proceeds from related party loans		**43,463**
Net cash flows from financing activities		**43,463**
Net increase in Cash and Cash Equivalents		**144**
Cash and Cash Equivalents at the beginning of the financial period		**-**
Effect of exchange rate fluctuations on Cash and Cash Equivalents		**-**
Cash and Cash Equivalents at the end of the financial period	4	**144**

Statement of Changes in Equity for the financial period ended 31 December 2009

	Notes	Issued Capital US$'000	Retained Earnings US$'000	Total Equity US$'000
Balance 21 August 2008		**-**	**-**	**-**
Loss for the year		-	(600)	(600)
Other comprehensive income		-	-	-
Total comprehensive income		-	(600)	(600)
Issue of share capital		-	-	-
Balance as at 31 December 2009		**-**	**(600)**	**(600)**

NOTE 1 - REPORTING ENTITY

Falcon Oil & Gas Australia Limited (the 'Company') is a company domiciled in Australia. The Company was incorporated on 21 August 2008.

NOTE 2 - BASIS OF PREPARATION

This represents the first financial report of Falcon Oil & Gas Australia Limited (formerly Falcon Oil & Gas Australia Pty Limited) which was incorporated on 21 August 2008.

(a) Statement of compliance

The special purpose financial report has been prepared in accordance with the requirements of the Corporations Act 2001 and the recognition and measurement aspects of all applicable Australian Accounting Standards ("AASBs") adopted by the Australian Accounting Standards Board ("AASB"). The directors have determined that the Company is not a reporting entity.

The financial report does not include the disclosure requirements of all AASBs except for the following minimum requirements:

- AASB 101 Presentation of Financial Statements
- AASB 107 Cash Flow Statements
- AASB 108 Accounting Policies, Changes in Accounting Estimates and Errors
- AASB 1048 Interpretation and Application of Standards.

The financial report was authorised for issue by the directors on 18 November 2010.

(b) Basis of measurement

The financial statements have been prepared on the historical cost basis.

(c) Functional and presentation currency

These financial statements are presented in United States dollars, which is the Company's functional currency.

(d) Use of estimates and judgements

The preparation of financial statements requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future periods affected.

In particular, information about significant areas of estimation uncertainty and critical judgements in applying accounting policies that have the most significant effect on the amount recognised in the financial statements are described in the following notes:

- Note 7 – Exploration and Evaluation Assets
- Note 11 – Asset Retirement Obligation

(e) Going Concern

The financial statements as of 31 December 2009 have been prepared on the basis that the Company is a going concern. That is, be able to pay its debts as and when they fall due.

NOTE 2 - BASIS OF PREPARATION (Continued)

The Company is reliant on its shareholders for ongoing financial assistance, in the form of the shareholder loans in order to operate as a going concern.

In the near term, the Company's ability to continue as a going concern is dependent upon the continued financial support from Falcon Oil & Gas Limited as detailed in note 10 and its ability to access cash to finance its upcoming capital commitments. Additional capital may be sought from existing shareholders, the issuance of shares to other parties or the disposal of certain or parts of certain assets.

Management is of the view that the Company will be able to access such funds in the near future. This assumption is also based on the successful private placement in 2010 (Subsequent Events Note). However, there is no assurance such additional capital will be available.

NOTE 3 - SIGNIFICANT ACCOUNTING POLICIES

The accounting policies set out below have been applied consistently to all periods presented in financial report.

Trade and other receivables
Trade and other receivables are stated at their amortised cost less provision for doubtful debts.

Cash and cash equivalents
Cash and cash equivalents comprise cash balances and call deposits.

Property Plant & Equipment
Items of property, plant and equipment are stated at cost, less accumulated depreciation and accumulated impairment charges.

Exploration and Evaluation Costs
Once the legal right to explore has been acquired, exploration and evaluation expenditure is charged to the statement of comprehensive income, unless directors conclude that a future economic benefit is more likely than not to be realised. These costs include materials, fuel, drilling costs and payments made to contractors and providers of services.

In evaluating if expenditures meet the criteria to be capitalised, several different sources of information are utilised. The information that is used to determine the probability of future benefits depends on the extent of exploration and evaluation that has been performed.

Impairment
The carrying amounts of the Company's assets, other than deferred tax assets, are reviewed at each balance sheet date to determine whether there is any indication of impairment. If any such indication exists, the asset's recoverable amount is estimated.

An impairment loss is recognised whenever the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. Impairment losses are recognised in the statement of comprehensive income, unless an asset has previously been re-valued, in which case the impairment loss is recognised as a reversal to the extent of that previous revaluation with any excess recognised through profit or loss.

NOTE 3 - SIGNIFICANT ACCOUNTING POLICIES (Continued)

Calculation of recoverable amount

The recoverable amount of assets is the greater of their fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate largely independent cash inflows, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

Reversals of impairment

An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

Share capital

Transaction costs

Transaction costs of an equity transaction are accounted for as a deduction from equity, net of any related income tax benefit.

Dividends

Dividends are recognised as a liability in the period in which they are declared.

Interest bearing borrowings

Interest bearing borrowings are recognised initially at fair value less attributable transaction costs. Subsequent to initial recognition, interest bearing borrowings are stated at amortised cost with any difference between cost and redemption value being recognised in the statement of comprehensive income over the period of the borrowings on an effective interest basis.

Trade and other payables

Trade and other payables are stated at their amortised cost. Trade payables are non-interest bearing and are normally settled on 30-day terms.

Revenue

Sales revenue is recognised in the statement of comprehensive income when the significant risks and rewards of ownership have been transferred to the buyer.

Expenses

Net financing costs

Net financing costs comprise interest payable on borrowings calculated using the effective interest method, and interest earned.

Interest revenue is recognised in the statement of comprehensive income as it accrues, using the effective interest method. Dividend income is recognised in the statement of comprehensive income on the date the entity's right to receive payments is established.

Income tax

Income tax on the statement of comprehensive income for the period comprises current and deferred tax. Income tax is recognised in the statement of comprehensive income except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

Current tax is the expected tax payable on the taxable income for the period, using tax rates enacted or substantially enacted at the balance sheet date, and any adjustment to tax payable in respect of the previous period.

NOTE 3 - SIGNIFICANT ACCOUNTING POLICIES (Continued)

Deferred tax is provided using the balance sheet liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The following temporary differences are not provided for: the initial recognition of assets or liabilities that affect neither accounting nor taxable profit, and differences relating to investments in subsidiaries to the extent that they will probably not reverse in the foreseeable future. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted at the balance sheet date.

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

Additional income taxes that arise from the distribution of dividends are recognised at the same time as the liability to pay the related dividend.

Goods and services tax

Revenue, expenses and assets are recognised net of the amount of goods and services tax (GST), except where the amount of GST incurred is not recoverable from the taxation authority. In these circumstances, the GST is recognised as part of the cost of acquisition of the asset or as part of the expense.

Receivables and payables are stated with the amount of GST included. The net amount of GST recoverable from, or payable to, the ATO is included as a current asset or liability in the balance sheet.

Cash flows are included in the statement of cash flows on a gross basis. The GST components of cash flows arising from investing and financing activities which are recoverable from, or payable to, the ATO are classified as operating cash flows.

Determination of fair values

A number of the Company’s accounting policies and disclosures require the determination of fair value, for both financial and non-financial assets and liabilities. Fair values have been determined for measurement and/or disclosure purposes based on the following methods. Where applicable, further information about the assumptions made in determining fair values is disclosed in the notes specific to that asset or liability.

Trade and other receivables

The fair value of trade and other receivables is estimated as the present value of future cash flows, discounted at the market rate of interest at the reporting date.

Non-derivative financial liabilities

Fair value, which is determined for disclosure purposes, is calculated based on the present value of future principal and interest cash flows, discounted at the market rate of interest at the reporting date.

New standards and interpretations not yet adopted

New Australian Accounting Standards that have been issued, but are not yet effective, are not expected to have a material impact on the Company.

	Notes	21 August 2008 to 31 December 2009 US$'000
NOTE 4 – CASH & CASH EQUIVALENTS		
Cash at bank		**144**
NOTE 5 – RECEIVABLES		
Current		
Accounts receivables		**2,148**
Prepayments		**212**
Other Receivables		**469**
		2,829
NOTE 6 – PROPERTY PLANT & EQUIPMENT		
Cost		
Opening balance		-
Additions in the period		**1,666**
Balance as at 31 December 2009		**1,666**
Depreciation		
Opening balance		-
Depreciation		-
Balance as at 31 December 2009		-
Net Book Value at 31 December 2009		**1,666**
NOTE 7 – EXPLORATION & EVALUATION ASSETS		
Cost		
Opening balance		-
Acquisition of interests in exploration licences		**31,628**
Expenditure in the period		**6,020**
Balance as at 31 December 2009		**37,648**
Depletion & Impairment		
Opening balance		-
Depletion & Impairment		-
Balance as at 31 December 2009		-
Net Book Value at 31 December 2009		**37,648**

NOTE 7 – EXPLORATION & EVALUATION ASSETS (continued)

On 30 September 2008, the Company acquired an undivided 50% working interest in an aggregate 7,000,000 acres in four exploration permits (the "Permits") in the Beetaloo Basin of the Northern Territory pursuant to the terms of a Purchase and Sale Agreement with PetroHunter Energy Corporation, PetroHunter Operating Company and Sweetpea Petroleum Pty Ltd.

On 11 June 2009, pursuant to a second Purchase and Sale Agreement the Company completed the acquisition of an additional undivided 25% working interest in the Beetaloo Basin Project with PetroHunter and Sweetpea wherein the Company will issue to Sweetpea ordinary shares of Falcon Australia in consideration for the transfer of Sweetpea's undivided 25% working interest in the Permits.

On 7 December 2009, the Company entered into a Binding Heads of Agreement with PetroHunter and Sweetpea wherein the Company will issue to Sweetpea ordinary shares in Falcon Australia in consideration for the transfer of Sweetpea's undivided 25% working interest in the Permits. This transaction had not completed at 31 December 2009. An independent valuation of the Permits was however prepared as part of the transaction subject to the Binding Heads of Agreement resulting in a value of between US$48 and US$60 million. Directors do not believe there has been any impairment in the carrying value of the Beetaloo Permits as at 31 December 2009.

	21 August 2008 to 31 December 2009 US$'000	
NOTE 8 – OTHER NON CURRENT ASSETS		
Deferred asset acquisition costs	407	
Deferred share issue costs	138	
Security deposits	482	
	1,027	
NOTE 9 – PAYABLES & ACCRUALS		
Trade payables	**210**	
Accruals	**1**	
	211	
NOTE 10 – LOANS		
Mako Energy Corporation	487	Current
Falcon Oil & Gas Limited	42,976	Current
	43,463	

The Company's acquisition and exploration expenditure has been primarily funded by way of loans from its holding company, Falcon Oil & Gas Limited and related entity Mako Energy Corporation. These loans have been advanced on an interest free basis.

NOTE 10 – LOANS (continued)

The Company is dependent upon the financial support of Falcon Oil & Gas Limited to support the ongoing operations of the Company . The financial support referred to is for a period of 12 months from the date of these financial statements, has been confirmed in writing by Falcon Oil & Gas Limited, and includes:

- Obligations and commitments as may be required from time to time to enable the Company to finance its ongoing operating, financing and investing activities and to enable it to meet all of its debts and liabilities in the normal course of business as and when they fall due;
- An indemnity to cover any and all losses incurred by the Company;
- Make available to the Company when required sufficient funds to allow the repayment of loans raised by the Company.

NOTE 11 – OTHER LIABILITIES

Asset retirement obligation	**240**
	240

The Company makes provision for the rehabilitation of drill sites on a discounted basis. The rehabilitation provision represents the present value of estimated rehabilitation expenditure which would be required to rehabilitate the site at the conclusion of current exploration activities.

NOTE 12 – CAPITAL & RESERVES

	31 December 2009 Number
Share capital	
On issue	-
Ordinary shares on issue – fully paid	-

The Company has one share on issue as at 31 December 2009 which is held by Falcon Oil & Gas Limited. Holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at shareholders' meetings. The Company does not have authorised capital or par value in respect of its issued shares.

In the event of winding up of the Company, ordinary shareholders rank after creditors and are fully entitled to any proceeds of liquidation.

Options

There were no options granted, exercised or lapsed unexercised during the period ended 31 December 2009.

Dividends

There were no dividends paid or declared by the Company during the period ended 31 December 2009.

	Note	Share capital US$'000	Reserves US$'000	Retained losses US$'000	Total equity US$'000
Balance at 21 August 2008		-	-	-	-
Total recognised income and expense		-	-	(600)	(600)
Balance at 31 December 2009		-	-	(600)	(600)

	Notes	21 August to 31 December 2009 US$
NOTE 13 – STATEMENT OF CASH FLOWS		
Reconciliation of loss for the period to net cash from operating activities		
Loss for the period		**(600)**
Decr/(incr) in receivables		**(2,829)**
Incr/(decr) in payables		**211**
Net cash from operating activities		**(3,218)**

NOTE 14 – CAPITAL COMMITMENTS

Under a work program approved by the Northern Territory Government, Department of Resources, on 31 March 2010, and subsequently amended on 25 June 2010, the Company is obligated to complete the following minimum work requirements in order to retain the exploration permits in the Beetaloo Basin:

Permit	Permit Year Start	Permit Year End	Minimum Work Requirement	Estimated Expenditure
EP 76	January 2009	December 2010	Geologic studies Reservoir assessment	A$200,000
	January 2011	December 2011	Drill 1 well, complete if warranted	A$3,700,000
EP 98	January 2010	December 2011	Complete & test well Geological studies	A$6,200,000
EP 99	January 2010	December 2011	G&G studies Geophysical re-evaluation	A$100,000
	January 2012	December 2012	Drill two wells	A$3,700,000
EP 117	January 2010	December 2011	Basin modelling re-evaluation	A$100,000
	January 2012	December 2012	G&G studies Reservoir assessment Drill & complete 1 well	A$1,300,000

NOTE 15 – SUBSEQUENT EVENTS

On 7 December 2009, Falcon Oil & Gas Limited ("Falcon") and the Company entered into a Binding Heads of Agreement (the "Agreement") with PetroHunter Energy Corporation and Sweetpea Petroleum Pty Ltd ("Sweetpea") wherein the Company will issue to Sweetpea ordinary shares in consideration for the transfer of Sweetpea's undivided 25% working interest in the Permits. Falcon will enter into a Master Services Agreement (the "MSA") related to the operations of the Permits. Under the terms of the Agreement, Falcon will be issued 149,999,999 ordinary shares in the Company for conversion of a portion ($30,000,000) of the Company's debt payable to Falcon, which approximates Falcon's initial acquisition cost previously paid to Sweetpea for the 75% working interest in the Permits held by the Company as of the date of the Agreement, and Sweetpea will be issued 50 million shares in the Company for its remaining 25% working interest in the Permits.

NOTE 15 – SUBSEQUENT EVENTS (continued)

On April 23, 2010, the Company received notice (the “Notice”) from the Department of Resources, Northern Territory Government, that the registration of the transfer of the remaining 25% interest in the Permits was completed, satisfying all conditions precedent to closing. Pursuant to the Notice, the Company now owns 100% of the Permits.

On 4 June 2010 the Company announced the closure of the first tranche of a private placement raising a total of US$4,895,659. On 1 December 2010 a further $1,217,578 was raised under the second tranche of the private placement, which is now closed. Under the terms outlined in the offer memorandum, each share allotted came with a free attached option. Each option entitles the holder to acquire one fully paid ordinary share at an exercise price of US$1.25 for a period of three years from the date of issue.

Directors' Declaration

1 In the opinion of the directors of Falcon Oil & Gas Australia Limited:

(a) the Company is not a reporting entity;

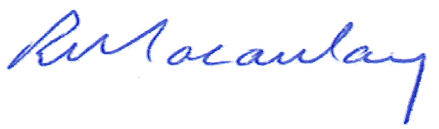
(b) the financial statements and notes, set out on pages 9 to 20, are in accordance with the Corporations Act 2001, including:

(i) giving a true and fair view of the financial position of the Company as at 31 December 2009 and of its performance, as represented by the results of its operations and its cash flows, for the financial year ended on that date in accordance with the statement of compliance and basis of preparation described in Notes 2 and 3; and

(ii) complying with Australian Accounting Standards and other mandatory professional reporting requirements to the extent described in Notes 2 and 3 and the Corporations Regulations 2001; and

(c) there are reasonable grounds to believe that the Company will be able to pay its debts as and when they become due and payable

Signed at Sydney this 10th day of December 2010 in accordance with a resolution of the Board of Directors:



Robert Macaulay
Director

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Independent auditor's report to the members of Falcon Oil & Gas Australia Pty Ltd

Report on the Financial Report

We have audited the accompanying financial report of Falcon Oil & Gas Australia Pty Ltd, which comprises the statement of financial position as at 31 December 2009, and the statement of comprehensive income, statement of changes in equity and statement of cash flows for the year ended on that date, a summary of significant accounting policies, other explanatory notes and the directors' declaration.

Directors' Responsibility for the Financial Report

The directors of the company are responsible for the preparation and fair presentation of the financial report in accordance with the Australian Accounting Standards (including the Australian Accounting Interpretations) and the *Corporations Act 2001*. This responsibility includes establishing and maintaining internal controls relevant to the preparation and fair presentation of the financial report that is free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor's Responsibility

Our responsibility is to express an opinion on the financial report based on our audit. We conducted our audit in accordance with Australian Auditing Standards. These Auditing Standards require that we comply with relevant ethical requirements relating to audit engagements and plan and perform the audit to obtain reasonable assurance whether the financial report is free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial report. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the financial report, whether due to fraud or error. In making those risk assessments, we consider internal controls relevant to the entity's preparation and fair presentation of the financial report 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 controls. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors[2], as well as evaluating the overall presentation of the financial report.

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

Independence

In conducting our audit we have met the independence requirements of the *Corporations Act 2001*. We have given to the directors of the company a written Auditor's Independence Declaration, a copy of which is included in the directors' report. The Auditor's Independence Declaration would have been expressed in the same terms if it had been given to the directors at the date this auditor's report was signed.

ERNST & YOUNG

Auditor's Opinion

In our opinion:

1. the financial report of Falcon Oil & Gas Australia Pty Ltd is in accordance with the *Corporations Act 2001*, including:
   (i) giving a true and fair view of the financial position of Falcon Oil & Gas Australia Pty Ltd at 31 December 2009 and of its performance for the year ended on that date; and
   (ii) complying with Australian Accounting Standards (including the Australian Accounting Interpretations) and the *Corporations Regulations 2001*.

2. the financial report also complies with International Financial Reporting Standards as issued by the International Accounting Standards Board.

Ernst & Young

Ernst & Young

Scott Jarrett
Partner
Sydney

10 December 2010