

MANAGEMENT'S DISCUSSION AND ANALYSIS

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis of our operating results and financial position should be read in conjunction with our unaudited financial statements for the period ended June 30, 2008, and related notes (collectively, "financial statements"), which have been prepared in accordance with accounting principles generally accepted in Canada ("GAAP"). This discussion and analysis is current for the Company through August 14, 2008.

Forward-Looking Statements

Certain information in this discussion and analysis contains forward-looking statements and assumptions, such as those related to results of operations and financial condition, capital spending, financial sources, commodity prices, costs of production, results of acquisition projects, environmental risks, regulatory matters, and the magnitude of oil and gas reserves. The reader is also directed to statements regarding future wells to be drilled in our Beta and Alaska operations including our joint drilling program with Chevron, Corsair discussions, discussions regarding negotiations with our lenders, and statements related to our ability become earnings positive at some time in the future. These should all be treated as forward looking statements derived by management's opinion and the use of outside consultants. By their nature, forward-looking statements are subject to numerous risks and uncertainties that could significantly affect anticipated results in the future and accordingly actual results may differ materially from those predicted as a result of a variety of factors, including without limitation, those described in the "Risk Factors" section of our most recent Annual Information Form and the following:

- prices of oil and natural gas have been and are expected to continue to be subject to significant fluctuations;
- operating results following our acquisitions may not be as expected;
- competitive pressure among companies in the industry in which we operate may increase significantly;
- costs or difficulties related to the integration of businesses we acquire may be greater than expected;
- changes in the interest rate environment may adversely affect our asset values or increase our borrowing costs;
- general economic conditions, whether nationally or in the market areas in which we conduct business, may be less favorable than expected;
- legislation or regulatory changes may adversely affect the business in which we are engaged;



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- the effects of technological changes or obsolescence relating to our products and services;
- the effects of government regulation or shifts in government policy;
- the uncertainty of the productivity of drilled oil and natural gas wells may adversely affect our ability to produce oil and/or natural gas in commercial quantities;
- if we cannot meet our substantial capital requirements, our growth and operations may be hindered;
- weather disturbances or natural occurrences such as earthquakes could disproportionately affect our production or transportation due to our geographic concentration;
- significant changes in the cost or availability of gathering systems, pipelines and processing facilities may affect our ability to produce and market oil and natural gas;
- adverse changes may occur in the securities markets generally;
- conditions in the equity and debt markets or our financial condition may render us unable to achieve desired reductions in our debt burden or overall cost of debt; and
- the uncertainty surrounding our ability to successfully negotiate revised credit agreements could have a significant impact on future earnings and cash flow.

In addition, we are currently in violation of certain debt covenants and although we are renegotiating our credit agreements, there is no assurance that this will be successful.

Readers are cautioned that the assumptions used in the preparation of such information, although considered reasonable at the time of preparation, may prove to be imprecise and as such, undue reliance should not be placed on forward-looking statements. We disclaim any intention or obligation to update or revise these forward-looking statements, whether as a result of new information, future events, or otherwise, subject to our obligations under applicable securities laws.

Overview

We are an independent oil and gas production and development company with operations offshore California and Alaska. We are focused on the acquisition, exploitation, exploration and development of oil and gas properties. Our strategy is two fold: first, to develop our large inventory of proved undeveloped reserves and second, and to focus on acquiring assets with low risk exploitation and development potential (proved undeveloped reserves). We plan to supplement this low risk exploitation strategy from time to time by participating in exploration projects.

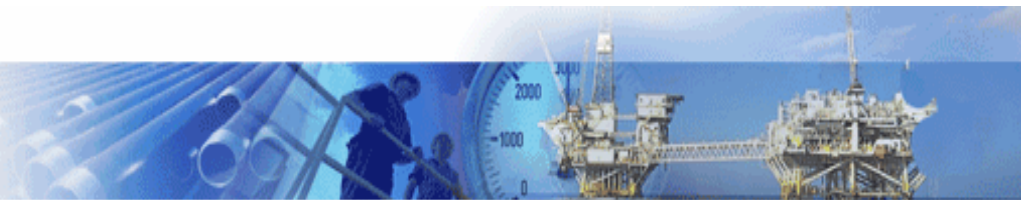


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Summary

We are pleased to report on a number of fronts the accomplishments of the second quarter of 2008.

- Oil and gas production revenue from continuing operations increased to a record \$69.7 million for the second quarter of 2008.
- April saw the partial return of Platform Eureka to production after only 13 months as operator. The platform had been shut in since 1999.
- In May 2008 we announced the \$135 million onshore California asset sale as part of our debt reduction program. The two transactions closed within 75 days of the announcement for gross proceeds of approximately \$135 million (less customary closing adjustments). Approximately \$63 million was used to pay down debt with an additional \$30 million used to extinguish hedge contracts.
- In June 2008 we announced that we met our phase I production targets for Platform Eureka achieving production in excess of 1,200 barrels of oil equivalent per day ("boe/d") for a combined Beta Field output in excess of 2,950 boe/d.
- We appointed Joe Kilchrist as General Manager of our Alaska operations signifying the strategic importance of our Alaska operations. Alaska production has since increased in excess of 400 boe/d year to date due to well work-overs and submersible pump replacements. In addition, we are well underway with the Chevron plan of development for our non-operated assets which are expected to produce incremental production in the late 2008 or early 2009 timeframe.
- We hired Gerry Tywoniuk as our new Chief Financial Officer effective August 15, 2008, adding his experience in oil and gas, capital markets and accounting to our organization.
- We continued to make solid progress on replacing our cash-funded performance bonds with a surety line, with the goal to free up a significant amount of cash for debt repayment and capital programs.



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Beta Assets (offshore Long Beach, California)

In April 2008, we announced that the return to production of Platform Eureka had begun representing a significant milestone. This platform had been shut in since 1999 and was returned to production in 13 months from the date we took over as operator. Since that time, we have increased production to our next goal of in excess of 1,000 boe/d, and are now looking ahead to our next target of 2,000 boe/d by the end of the third quarter 2008. We have identified the wells that will be targeted for work-overs based on their performance prior to being shut in, and are currently performing rig upgrades necessary to pull the wells. Once these upgrades are complete, we believe we can return the next 7-10 wells to producing status within four weeks from that time which is currently expected in the September 2008 timeframe. Additional wells are still planned to be drilled from Platform Ellen in the late 2008 to early 2009 timeframe.

Alaska Operations

Operated Assets: Development drilling on our operated assets is expected to begin in the second quarter of 2009, this is a delay of approximately six months due to rig availability and weather related logistics with the drilling season. Development will begin with drilling of proved undeveloped ("PUD") locations off of platform Osprey in the Redoubt Shoal field.

Non-Operated Assets: Our joint redevelopment plan in Alaska with Chevron is ongoing. Development drilling in our non-operated assets is expected to begin in the first quarter of 2009. Development will begin with PUD drilling off of platform Steelhead in the MacArthur River field.

Alaska Exploration

Our Cook Inlet exploration prospects represent a potentially significant upside to our shareholders. As such, we have been working diligently to preserve these assets as well as exploit them in a timely and economical manner. Our first prospect is the Corsair Unit which we plan to drill during the 2009 drilling season.

The Corsair Unit consists of four state leases totally approximately 27,000 acres of which we hold a 100% working interest. In addition, we applied to include some expansion acreage in the Corsair Unit, but this was not approved by the State. We have appealed this decision, and as of this writing, await an answer.

The Corsair Unit has several specific obligations to the State of Alaska that we must meet in order to maintain the lease. Several of these obligations must be met under very tight timelines due to the obligations that we inherited from Forest Oil as part of the acquisition. The obligations for the remaining core lease include evidence of a rig capable of drilling the prospect, evidence of transportation for the rig, and drilling of the prospect that must commence during the 2009 drilling season by June 30, 2009. We have successfully demonstrated contractual evidence of a rig to drill the Corsair prospect, and have been granted an extension until September 29, 2008 to show evidence of a transport vessel. We have been in discussions for several months with various transportation



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companies, and believe that we can reasonably satisfy the State's requirement by the extended deadline.

The outcome of our appeal with the State of Alaska could have an impact on the decision we make to drill these leases. While we believe that the original Corsair Unit has significant stand-alone economic merit, the decision of the State not to include the additional leases could have a negative impact on the overall economics of the project.

Our efforts to secure a rig and arrange for mobilization are a direct reflection of our intention and desire to exploit these leases. While the core Corsair acreage is attractive as an exploration target, the costs and complexity of arranging for a jack up rig and mobilizing to the Cook Inlet are significant. In any outcome, we expect to share in these costs through some sort of joint venture or farm out arrangement, with the objective of minimizing our up front capital outlay.

LA Basin and San Joaquin Basin Divestiture

As previously announced, we completed the sale of these assets during the month of July 2008 for a total sales price (before customary purchase price adjustments) of \$135 million. While we are hesitant to sell any of our proved reserves, we felt the transaction presented the best way to achieve our debt reduction goal of 20-25% by year end 2008 as well as streamline our focus of operations. We believe this price represented a fair value for our assets on a proved PV-10 basis (proved reserves discounted at a 10% rate) as well as a premium on a producing barrel basis. Based on the multiples achieved in the sales transaction, we believe significant shareholder value remains with our existing asset base. The sales proceeds went towards debt repayment, hedge buy downs, and general working capital.

Wyoming Green River Basin Update

At this time, we have not been able to come to any new economic terms with our joint venture partner on this project. Given the opportunity of our exploration prospects in the Cook Inlet Alaska, we are more encouraged by their risk profile and potential upside. While we believe there may still be economic viability on the Wyoming Baxter shale, we do not have any drilling planned or other capital committed for the second half of this year in the Wyoming Green River Basin project. To date, we have not earned any acreage through the participation agreement.

Form S-1 Registration Statement

On February 12, 2008, we filed on Form S-1 a Registration Statement with the U.S. Securities and Exchange Commission ("SEC") in fulfillment of our registration rights obligations. Since that filing, we have held several discussions with the SEC to address their comments. We have prepared an amendment to our registration statement for submission. We have not yet filed the amendment due to the required additional disclosures resulting from the sale of our onshore California assets. Now that the sale transaction has closed, we are proceeding to update the document and re-submit. We expect to file our amendment with the SEC in the third or fourth quarter of 2008. The registration process can take several months before a registration statement is declared effective.



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Once effective, the filing represents the opportunity for us to pursue a U.S. listing of our equity although there is no assurance that we will meet the minimum requirements to complete a listing in the short term. We believe this may provide greater liquidity to current investors as well as access to additional U.S. investors.

Results of Operations

Results of Operations—For Period ending June 30, 2008

Factors Affecting Comparability

We acquired the Beta Unit in March 2007 and the Alaska properties in August 2007. Our results of operations from period to period are not comparable because of the effects of these acquisitions and our limited history of operating these assets. As such we have included comparisons to our operating results for the June 30, 2008 quarter to the March 31, 2008 quarter in addition to the year ago quarter ended June 30, 2007. The table below reflects this comparison.



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(000)	Second Quarter June 30, 2008	First Quarter March 31, 2008	Second Quarter June 30, 2007
REVENUES			
Oil and gas production revenue	\$69,721	\$52,704	\$9,660
Production expenses	(22,885)	(26,087)	(6,408)
Transportation expense	(1,098)	(1,072)	(329)
Royalties	(15,533)	(10,050)	(2,595)
Realized gain (loss) on derivatives	(18,095)	(10,486)	-
Interest and dividends	1,452	2,204	69
Loss from nonconsolidated subsidiary	(228)	(220)	-
Other revenue	36	20	391
	<u>13,370</u>	<u>7,013</u>	<u>788</u>
EXPENSES			
General and administrative	2,703	4,151	954
Stock compensation expense	1,860	1,343	313
Liquidated damages	1,400	1,840	-
Interest - cash	17,437	21,002	1,547
Interest - non-cash	7,106	12,371	1,871
Accelerated expensing of accretion and amortization of deferred financing costs	-	48,398	-
General exploration	769	221	-
Depreciation, depletion and amortization	7,001	6,429	5,365
	<u>38,276</u>	<u>95,755</u>	<u>10,050</u>
LOSS FROM CONTINUING OPERATIONS BEFORE INCOME TAX			
	(24,906)	(88,743)	(9,263)
Income tax expense	-	-	(10)
	<u>(24,906)</u>	<u>(88,743)</u>	<u>(9,273)</u>
NET LOSS FROM CONTINUING OPERATIONS			
	(24,906)	(88,743)	(9,273)
Loss from Operations Held for Sale	<u>(8,432)</u>	<u>555</u>	<u>(3,019)</u>
Net Loss	<u>(\$33,338)</u>	<u>(\$88,188)</u>	<u>(\$12,292)</u>

On July 10 and July 30, 2008, we closed the sale of our two onshore California assets, LA Basin and San Joaquin respectively for a combined gross consideration of \$135 million less customary adjustments. The discussion below presents the sold properties as assets held for sale for all historical periods and only discusses comparisons from continuing operations. Note that the first quarter to second quarter of 2008 compares only from continued operations.

Revenues

Revenue for the quarter ended June 30, 2008 of \$69.7 million was up 32.3% compared to the first quarter of 2008 and up 621.7% from the second quarter of 2007. Production from continuing operations was up 16.8% from the first quarter of 2008 while the average realized price for our crude oil was up 25.7% from the same quarter. Production in the second quarter of 2008 was up 133.2% from the second quarter of 2007 reflecting the addition of Alaska production (net of production lost



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from discontinued operations).

Oil production from Alaska for the second quarter of 2008 was up 6.7% from the first quarter of 2008 with an increase in realized price for oil of 24.2% for the same period respectively. The increase in Alaska production is the result of well work-overs and the replacement of some submersible pumps increasing the throughput of gross fluids.

Production from the Beta Field for the second quarter of 2008 was up 37.2% from the first quarter of 2008 with an increase in realized price for oil of 32.2% for the same period respectively. This increase is the result of the partial return to production of Platform Eureka.



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Oil production from the Beta Field now accounts for approximately 38.1% of our total production from continuing operations, and is expected to grow to become greater than 45% of our total oil production as Platform Eureka is ramped up to a full return to production.

Second Quarter 2008	Alaska	Beta Unit	Total	Discontinued Operations	Total
Oil Production (bbls)	364	225	590	84	673
Oil Production (bbls per day)	4,004	2,475	6,479	921	7,400
Sold Production (bbls)	346	225	571	83	655
Realized Price per Barrel	\$119.39	\$112.27	\$116.67	\$115.95	\$116.58
Oil Revenue	\$ 43,505	\$ 25,284	\$ 68,789	\$ 9,715	\$ 78,504
Gas Revenue	924	-	924	7	931
Total Gross Revenue	\$ 44,429	\$ 25,284	\$ 69,713	\$ 9,722	\$ 79,435
% of Field Contribution \$'s	55.93%	31.83%	87.76%	12.24%	100%
% of Field Contribution Barrels	54.11%	33.44%	87.56%	12.44%	100%
Lease Operating Expense (LOE)	\$ 16,144	\$ 7,495	\$ 23,639	\$ 1,531	\$ 25,170
LOE per Barrel	\$44.30	\$33.28	\$40.09	\$18.27	\$37.38
(thousands except bbls per day amounts)					

The difference between oil production and sold production is due to the timing of liftings and shipping. We recognize revenue only once the oil has been shipped to a refinery.

Production Expenses

Production expenses decreased to \$22.9 million for the second quarter of 2008 from \$26.1 million in the first quarter of 2008, and from 49.5% of revenue down to 32.8% of revenue respectively. The expense increased by 257.1% from the second quarter of 2007 due to the increase in production brought on by the Alaska acquisition. The difference between production expense and lease operating expense ("LOE") is the transportation expense of our crude and gas is included in LOE. LOE for the Beta Unit increased 11.2% from the first quarter of 2008 and decreased 18.8% on a per barrel basis from the first quarter of 2008. LOE for our operated and non-operated assets in Alaska remained flat from the first quarter of 2008 and decreased 6.4% on a per barrel basis from the first quarter of 2008. LOE from continuing operations increased on a company wide basis by 3.4% from the first quarter of 2008 and decreased 11.4% on a per barrel basis. This decrease on a per barrel basis is expected to continue as a result of improved operational synergies most notably from the Beta Field as a result of increased output from Platform Eureka.

Transportation Expense

Transportation expense is primarily due to the tariff paid to the Cook Inlet Pipe Line Company (CIPL) of which we are a 50% owner. The expense is recognized as revenue on the financial statements of CIPL. The transportation expense remained flat with a 2.4% increase from the first quarter of 2008 reflecting a slight increase in Alaska production.



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Royalties

Royalties increased from \$10.0 million in the first quarter of 2008 to \$15.5 million for the second quarter of 2008 (up 54.6%). The increase in expense is due to the increased production from both the Beta Field (Platform Eureka) and a slight increase in production for the quarter in Alaska. Royalty expense is up from the second quarter of 2007 by 498.6% since the Alaska acquisition closed in August of 2007 and there was no production from Platform Eureka.

Hedging Expense

Our exposure to gains and losses on hedging is primarily due to the hedges we have in place for the Beta Unit and Alaska properties production. See the Financial and Other Instruments section for a schedule of the hedge contracts currently in place. We have not entered into any new hedges during the second quarter of 2008.

Our realized loss on derivative contracts for oil production increased from \$10.5 million in the first quarter of 2008 to \$18.1 million for the second quarter of 2008 representing a 72.6% increase. Increases in realized losses are offset by increases in oil revenue for the equivalent barrels hedged. We did not have any significant realized hedging losses in the second quarter of 2007. The increase from the first quarter of 2008 is a direct result of the 25.7% increase in the realized price received for our crude oil production up from a first quarter 2008 average of \$92.80 to \$116.67 per barrel for the second quarter of 2008. We do not have any hedges in place for our gas production.

General and Administrative Expenses

General and Administrative (“G&A”) expenses decreased from \$4.2 million for the first quarter of 2008 to \$2.7 million for the second quarter of 2008 representing a decrease of 34.9%. Of the \$1.5 million decrease, \$0.7 million is attributable to an increased allocation to our production expenses while an additional \$867,000 is due to the elimination of the management fee payable to Forest Oil during the operational transition. The change from the second quarter of 2007 was an increase of 183.3%. The increase is a reflection of the additional staff and office space taken on as part of the Alaska acquisition.

Stock Compensation

Stock Compensation expense increased 38.5% from \$1.3 million for the first quarter of 2008 to \$1.9 million for the second quarter of 2008. The increase is the result of additional options issued to new and existing employees and directors. This expense represents approximately 4.9% of our total operating expenses. This expense was up from the second quarter of 2007 by 494.2%. The increase from the second quarter of 2007 was the result of hiring the employees in the Alaska assets acquisition (all employees hired were granted stock options), additional option grants to existing employees and the result of hiring other employees as we have grown.



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Liquidated Damages

As part of the private placement that closed in January 2007, certain registration rights were granted along with the shares. These registration rights obligated us to file a Form S-1 Registration Statement with the SEC by the end of August 2007. Because this deadline was not met, we became obligated to issue liquidated damages shares under the agreement payable in the amount of 1% per month of the total shares issued, to shareholders who had not sold before the statement was filed. The Liquidated Damages expense represents the fair value of the underlying shares that we issued. The amount ceases once 10% of the total shares issued in January 2007 is reached.

The Liquidated Damages expense decreased to \$1.4 million in the first quarter from \$1.8 million in the second quarter of 2008 (23.9%) due to a reduced number of shares issued, and a lower stock price. There was no Liquidated Damage expense for the year ago period.

Interest Expense - Cash

Interest Expense - Cash decreased from \$21.0 million in the first quarter of 2008 to \$17.4 million in the second quarter of 2008. This was attributable to the absence in the second quarter of a \$6.0 million fee on the Alaska facility incurred in the first quarter of 2008, partly offset by higher interest rates under the credit agreements. The expense is up substantially from the second quarter of 2007 (1,027.1%), as the Alaska purchase did not close until August 2007.

Interest Expense – Non Cash

Interest Expense – Non-cash decreased from \$12.4 million in the first quarter of 2008 to \$7.1 million in the second quarter of 2008. This is due to the first quarter 2008 expensing of unamortized deferred financing cost and acceleration of accretion expense discussed below, which eliminated expensing of these items in the second quarter of 2008 and beyond. This expense is up significantly from the second quarter of 2007 (279.8%) as the Alaska acquisition had not closed.

Interest Expense – Accelerated Accretion and Amortization of Deferred Financing Costs

In the first quarter of 2008, unamortized discount and deferred financing costs related to the Goldman and Silver Point notes payable were written off in the amount of \$48.4 million, as a result of classifying the entire note balance in current liabilities, in order to bring the carrying value up to face value.



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Depreciation, Depletion, and Amortization

Depreciation, Depletion, and Amortization (“DD&A”) expense increased from \$6.4 million for the first quarter of 2008 to \$7.0 million for the second quarter of 2008 (8.9%). This increase was the result of production increases from Platform Eureka. DD&A from the second quarter of 2007 increased 30.5% from \$5.4 million to \$7.0 million for the second quarter of 2008 as a result of the production and facilities from the Alaska assets as well as increased production from the Beta Field.

Net Loss

We recorded a \$24.9 million net loss from continuing operations for the quarter ended June 30, 2008 up 168.9% from the quarter ended June 30, 2007 (\$8.4 million adjusted to be continuing operations only), but down from \$88.8 million in the first quarter 2008 (which included a \$48.4 million non-cash acceleration of expense to write off deferred financing costs and unamortized discount on notes payable). Achieving profitability is dependent on the following factors. We believe we are making good progress increasing our production and bringing our production expenses down on a per barrel basis. As we bring on additional unhedged production and as our hedged volumes decline over the next few years, we expect our average realized price per barrel net of hedging losses to increase. In addition, it is important to reduce our leverage ratio in order to reduce our interest expense and to access lower cost debt.

Balance Sheet

Our cash position was \$6.4 million as of June 30, 2008. Our total assets were \$707.3 million, largely unchanged from December 31, 2007.

Debt is discussed below under “Capital Resources and Liquidity” and under “Capital Structure”.

Capital Resources and Liquidity

Our future growth depends on the development and exploration of our oil and natural gas properties and the acquisition of additional properties, each of which requires large capital expenditures. We have projected these capital expenditures for our next phase of capital programs to be in excess of \$45 million for the remainder of 2008 and into 2009. Given our cash position of approximately \$12.8 million as of August 8, 2008 and our projected cash flow, we will need to raise money to fund these planned capital expenditures. Based on our current credit agreements, we have several sources of liquidity that we may need to consider accessing, including approximately \$80 million and \$12 million available under our credit facilities (subject to lender approvals), access to a portion of the investment account for abandonment via surety bond options, cash flow from incremental production, and potential additional asset divestitures. Each of our existing and projected sources of cash are affected by operational and financial risks that influence the overall amount of cash generated and the capital available, including, among other things, changes in commodity prices.



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If we are unsuccessful in accessing any or all of these additional sources of liquidity, we may be required to adjust our capital program..

The Company's primary sources of borrowings are pursuant to three credit agreements with affiliates of The Goldman Sachs Group, Inc. ("Goldman") and Silver Point Finance LLC ("Silver Point"). These affiliates are also owners of a significant number of common shares and warrants. An affiliate of Goldman is the counterparty for the Company's commodity swaps. The credit and swap agreements contain covenants and restrictions, including a requirement that all cash receipts are to be deposited into lockboxes and require the Company to obtain Goldman or Silver Point approval for the disbursement of funds out of the lockboxes.

As at June 30, 2008 and as of the date of this report, the Company was not in compliance with all covenants under these agreements, and accordingly all amounts due under the credit agreements have been classified as current liabilities as of June 30, 2008 in accordance with accounting requirements. In addition, the long term portion of the derivative liability to Goldman has been classified as a current liability instead of as a long term liability as the swap agreement is linked to the credit agreements through cross defaults.

Neither Goldman nor Silver Point has expressed any demand for repayment of amounts outstanding under the credits agreements nor expressed any demands under the swap agreements. Negotiations for amendment of the agreements are underway. We aim to emerge from these discussions with a more flexible credit agreement as well as increased short term liquidity sufficient to fund our near term projects including the full return to production of Platform Eureka.

Our credit facilities currently require that we raise an additional \$85 million by March 31, 2009 from the sale of our common stock (or, upon approval by the lenders, preferred stock or convertible debt), lender-approved divestitures or other capital-raising activities as may be reasonably satisfactory to the lenders. Of the proceeds raised by March 31, 2009, at least \$85 million must be used to prepay indebtedness under the Alaska second lien credit agreement. Proceeds in excess of \$85 million that are not used to prepay the second lien credit agreement must be deposited into our credit facility lockbox accounts and may be used for exploration and development and working capital purposes as permitted by the approved plan of development or as otherwise permitted by our credit facilities.

The Company's ability to continue operations as planned, including capital spending on the schedule desired, is dependent upon a successful amendment of these agreements with Goldman and Silver Point.

We are also required under our credit agreements to hedge against the interest rate risk associated with the variable portion of our long term debt facilities. We are currently evaluating strategies for providing protection against the risk of rising interest rates. Per our current credit agreements and the associated amendments, we were required to enter into interest rate hedges on or before March 22, 2008. We have currently not entered into any interest rate hedges at this time. We



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have been in discussions with our lenders to discuss the appropriate strategy, timing, and amount of interest to swap based on the anticipated restructuring of our credit agreements.

We believe our primary capital requirements for the remainder of 2008 and into 2009 will be used for the following projects:

- Approximately \$25 million is expected to be required to complete the rig upgrades and perform the necessary well work-overs on the remaining wells in order to return Platform Eureka to full production (defined as production of approximately 4,000 boe/d).
- Approximately \$20 million will be used to perform the necessary topside work and other drill site preparation to drill two wells off of Platform Osprey. The actual drilling costs from drilling both wells are also included in this number, although part of the costs may roll over into the early part of 2009.

Funding for these projects is expected to come from cash flow from operations from increased Beta production, partial use of proceeds from our two onshore California divestitures, release of monies from our abandonment accounts when replaced with sureties and an expected restructuring of our credit facilities.

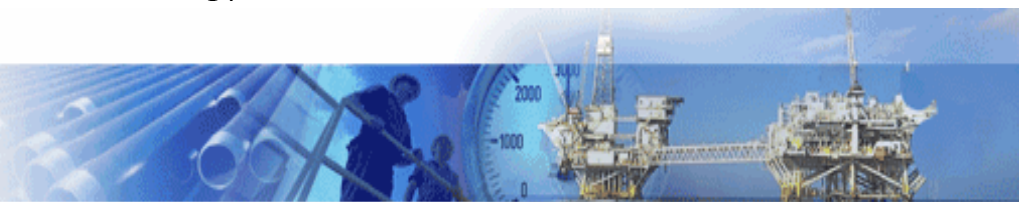
The exploitation of the Corsair Unit has significant cost and complexity including but not limited to the procurement of a rig, mobilization of the rig to the Cook Inlet in a timely manner, and staffing requirements for rig crews. Although we currently maintain a 100% working interest in this prospect, we expect to fund the above activities through a sell down of our working interest or other farm out arrangement, as well as through sub-lease arrangements of the jack up rig to other operators in the area who also require the use of a jack up rig to exploit their leases.

Cash Flows for the six months ending June 30, 2008 and June 30, 2007

The following table summarizes our net cash provided by or used in our operating activities, investing activities and financing activities for the six months ended June 30, 2008 and June 30, 2007 adjusted for continuing operations (these do not include the cash received from the onshore California asset sales).

	2008	2007
Net cash provided by (used in) operating activities	(\$2,883)	(\$7,500)
Net cash provided by (used in) investing activities	(\$21,645)	(\$19,824)
Net cash provided by financing activities	\$20,129	\$25,909
Net change in cash	(\$2,063)	(\$312)

Net cash used in operating activities was \$2.9 million compared to net cash used by operating activities of \$57.5 million from the second quarter of 2007. The change in net cash used in operating



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activities is still the result of our high cost of debt. The reduction in net cash used is a reflection of increased production and higher realized prices from our unhedged production, however, we are still negatively impacted on a cash flow basis by our current hedging program.

Net cash used in investing activities increased slightly from the second quarter of 2007 from \$19.8 million to \$21.6 million for the second quarter of 2008 but was relatively flat from the first quarter of 2008.

Net cash provided by financing activities decreased from the second quarter of 2007 from \$25.9 million down to \$20.1 million for the second quarter of 2008. The primary source for this second quarter 2008 cash was a \$1 million note payable and cash received from common shares issued.

Debt

The following schedule provides some detail of our current outstanding debt including both interest bearing and non-interest bearing obligations.

As a partial use of proceeds from the sale of both of our onshore California assets that closed subsequent to the second quarter, we made two debt payments: \$18.0 million went to payoff the full outstanding balance of the Laurus note (included in liabilities held for sale), and \$45.0 million was used to partially repay the Beta Senior secured note (part of the Goldman And Silver Point notes payable). The following table does not reflect the \$45 million pay-down of Goldman and Silver point debt.



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Notes Payable

Description	6/30/2008	12/31/2007
Goldman Sachs and Silver Point Financial		
Beta senior secured	\$ 65,000	\$ 65,000
Alaska first lien	108,000	108,000
Alaska second lien	277,000	277,000
Accrued interest - paid in kind	19,906	8,269
Face value of notes payable to		
Goldman Sachs and Silver Point Financial	469,906	458,269
Forest zero coupon note	31,368	29,976
Unsecured shareholder	1,000	-
Total face value of debt	\$ 502,274	\$ 488,245
Unamortized discounts		(27,097)
Unamortized debt issue costs		(27,277)
Book value of debt	\$ 502,274	\$ 433,871
Current portion of long term debt	(470,906)	(430)
Long term portion of note payable	\$ 31,368	\$ 433,441
Transferred to Discontinued Operations	(18,038)	(20,656)

Capital Structure

Our Goldman and Silver Point debt balance of \$469.9 million reflects the debt portion (as of June 30, 2008) of the funding of acquisitions of the Alaska assets in August 2007 and Beta Unit in March 2007, and the funding of the first stages of a significant capital expenditure program to develop these assets to increase production. We plan to reduce to this amount by 20-25% during the balance of 2008. The first part of this reduction recently occurred, with \$45 million of the proceeds from the July 2008 asset sale (Note 13) used to repay a portion of this indebtedness. In addition, we are working towards the establishment of a surety line to allow us to replace approximately half of the approximate \$100 million in cash we have on deposit for abandonment liability and performance deposits. If we are able to secure a new surety line, a portion of the cash freed up as a result thereof would also be used to repay a portion of this indebtedness. Finally, operating cash flow is being used to partially fund capital expenditures to increase production and revenues. Further alternatives to reduce our leverage ratio include additional asset sales, securing third party investors for a portion of our capital program and equity sales. These alternatives are under review to determine the best course of action to increase shareholder value.

As disclosed above, we are currently renegotiating our credit agreements with Goldman and Silver Point, although no assurance can be given that we will achieve our objectives in such renegotiation.



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Over time, once our leverage ratio is reduced, we expect to refinance our then-remaining Goldman and Silver Point notes payable with a conventional reserve-based loan at a significantly lower interest rate; however, no assurance can be given that conventional financing at desirable rates will be available at such time. Currently, a fluctuation in interest rates of 1.0% would change interest expense by \$4.7 million per year based on the outstanding floating rate debt as of June 30, 2008.

Warrants Exercised

The following table shows warrants that were exercised in the six months ended June 30, 2008:

2008 Warrants Exercised	Number		APIC		\$/Share
Exercised (1/9/08)	10,000	\$	15,000	\$	1.50
Exercised (1/15/08)	625		938	\$	1.50
Total Exercised in 2008	10,625	\$	15,938	\$	1.50

(APIC stands for additional paid in capital)

This table is current as of August 14, 2008 as no warrant exercises occurred subsequent to the end of the second quarter through August 14, 2008.

Cash & Cash Equivalents

As of August 8, 2008, we had a cash balance of approximately \$12.8 million. In addition we have approximately \$101 million in performance bonds and other abandonment based obligations. We believe that we are in a position to access the surety market to receive a portion of this cash back within the second half of this year.

Future Dividends

We have not declared or paid any cash dividends on our capital stock in the past, and we do not anticipate declaring or paying cash dividends on our common stock in the foreseeable future. In addition, our credit facilities prohibit the payment of dividends without lender consent.

We will pay dividends on our common stock only if and when declared by our board. Our board's ability to declare a dividend is subject to restrictions imposed by Delaware law. In determining whether to declare dividends, our board will consider these restrictions as well as our financial condition, results of operations, working capital requirements, future prospects and other factors it considers relevant.

Off-Balance Sheet Arrangements

We have entered into crude oil hedging contracts which are discussed below in the Financial



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and Other Instruments section in more detail. These production and swap contracts require us to make a settlement payment for any rise in the market price of crude oil above the contract price (schedule below) regardless of our actual production levels. While we believe we have an appropriate mix of hedged and unhedged crude oil production, we are at risk in the event of a decrease in our actual realized production volumes below our hedged production volumes. In other cases, higher prices received on physical production that has been hedged will generally be offset by settlement payments to our counterparty pursuant to the swap contract (and vice versa).

Related Party Transactions

Transactions with related parties are measured at their fair value as determined by management. The transactions listed below are unsecured and due under normal trade terms.

- a) In April 2008, the Company received a \$1.0 million unsecured loan from a shareholder. The loan is payable on demand at 9% annual interest, and was used for general working capital purposes.
- b) As of June 30, 2008, the Company owed \$76 thousand to Basin Supply. This Company is owned and controlled by Vladimir Katic, our CEO. Basin Supply is a surplus parts company that existed at the time the Company first acquired the LA Basin assets. It was used from time to time to acquire parts required for maintenance work. As the LA Basin assets have recently been sold, we do not expect to incur any additional costs associated with this related party.
- c) During the first six months of 2007, the Company incurred legal costs of approximately \$152 thousand with Devlin Jensen. Pat Devlin is a member of our board of directors and was a named partner with Devlin Jensen, who acts as our Canadian legal counsel, until October 31, 2007. We continue to use the services of Devlin Jensen on an ongoing basis for Canadian legal services.

Changes in Accounting Policy

There were no changes to any significant accounting policies during the second quarter of 2008.

Financial and Other Instruments

Our financial assets and liabilities consist of cash, derivatives, short-term investments, receivables, accounts payables, notes payable, and accrued liabilities. We have placed our cash and cash equivalents in liquid bank deposits, which provide a variable rate of interest. We have significant bonding obligations for several of our operations which require the purchase of some form of surety. To date we have funded our bonding obligations by placing cash in restricted accounts and securing our obligation 100% by the estimated bonding amount. We have engaged an outside firm to secure a surety line as a means to free up some of the restricted cash which currently is in excess of



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\$100 million.

Due to the historical volatility of crude oil and natural gas prices, as well as credit agreement requirements, we have an ongoing hedging strategy aimed at reducing the variability of the prices we receive on our production and providing a calculable minimum revenue stream. Currently, we have entered into production swaps aimed at ensuring a minimum amount of revenue is realized sufficient to cover our existing debt burden. As we layer on incremental and new production, we will review the appropriate level of our commodity hedging strategies..

The total derivative liability of \$240.5 million as of June 30, 2008 increased by \$150.5 million from March 31, 2008. The classification of this liability as a current liability is the result of cross default provisions relating to covenant violations in our Goldman and Silver Point credit facilities, although the counterparty, Goldman, has express no demands for settlement. The increase in this balance, which is reflected in the change in accumulated other comprehensive income on the balance sheet, is the result of the increase in the market price of crude oil and its effect on our hedge position for future crude oil sales. Generally accepted accounting principles require the derivative to be marked to market, but do not allow for the related increase in the present value of our hedge oil reserves to be recorded and offset against the derivative liability. We have hedged only a fraction of our total proved reserve base.

The following table provides an overview of our hedging contracts currently in place. These cover both Alaska and Beta operations. We did not enter into any new hedge contracts during the second quarter of 2008



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Hedge Position as of June 30, 2008

Alaska

Type	Amount	BPD	Term	Price (\$/bbl) ^(A)	Type
Swap	503,577	2,737	June 30 - December 31, 2008	\$ 68.16	Financial
Swap	907,999	2,488	January 1 - December 31, 2009	\$ 67.21	Financial
Swap	675,422	1,850	January 1 - December 31, 2010	\$ 67.21	Financial
Swap	272,416	746	January 1 - December 31, 2011	\$ 67.21	Financial
Swap	132,812	363	January 1 - September 30, 2012	\$ 67.21	Financial

(A) Swap price based on WTI

Beta

Type	Amount	BPD	Term	Price (\$/bbl) ^(B)	Type
Swap	144,500	785	June 30 - December 31, 2008	\$ 58.17	Financial
Swap	262,986	721	January 1 - December 31, 2009	\$ 57.26	Financial
Swap	241,794	662	January 1 - December 31, 2010	\$ 57.14	Financial
Swap	296,884	813	January 1 - December 31, 2011	\$ 55.90	Financial
Swap	173,948	475	January 1 - September 30, 2012	\$ 55.52	Financial

(B) Swap price based on Midway Sunset

Total -

Type	Amount	BPD	Term	Price (\$/bbl)	Type
Swap	648,077	3,522	June 30 - December 31, 2008	\$ 65.93	Financial
Swap	1,170,985	3,208	January 1 - December 31, 2009	\$ 64.98	Financial
Swap	917,216	2,513	January 1 - December 31, 2010	\$ 64.55	Financial
Swap	569,300	1,560	January 1 - December 31, 2011	\$ 61.31	Financial
Swap	306,760	838	January 1 - September 30, 2012	\$ 60.58	Financial

Swaps for assets held for sale are not included, as the contracts were terminated with the sale of assets in July 2008. The above contracts terminate on the last date shown.



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We are also required under our credit agreements to hedge against the interest rate risk associated with the variable portion of our long term debt facilities. We are currently evaluating strategies for providing protection against the risk of rising interest rates. Per our current credit agreements and the associated amendments, we were required to enter into interest rate hedges on or before March 22, 2008. We have currently not entered into any interest rate hedges at this time. We have been in discussions with our lenders to discuss the appropriate strategy, timing, and amount of interest to swap based on the anticipated restructuring of our credit agreements.

Outstanding Share Data

The following table represents our outstanding share data as of June 30, 2008. Following the end of the second quarter of 2008, an additional 692,951 shares were issued as damages shares. This is expected to be the final issuance of damages shares.

Corporate Common Share Capitalization Table

	June 30, 2008	December 31, 2007
Total share outstanding	200,230	185,994
Shares issued for damages	4,546	648
Total shares underlying warrants	89,459	90,041
Stock options	18,546	12,002
Potential fully diluted stock count	312,781	288,685

Selected Quarterly Information

The following tables show revenue and income data of the most recent eight quarters:

	For the Three Months Ended			
	30-Sep-07	31-Dec-07	31-Mar-08	30-Jun-08
Total Oil & Gas Revenue	\$31,829	\$60,435	\$52,704	\$69,721
Net Income (Loss)	(\$20,309)	(\$63,453)	(\$88,187)	(\$24,906)
Net Income (Loss) per share (basic)	(\$0.14)	(\$0.56)	(\$0.44)	(\$0.12)

Note: June 30, 2008 shown without discontinued operations

	30-Sep-06	31-Dec-06	31-Mar-07	30-Jun-07
Total Oil & Gas Revenue	\$3,803	\$3,271	\$3,283	\$9,660
Net Income (Loss)	(\$900)	(\$10,498)	(\$5,714)	(\$9,273)
Net Income (Loss) per share (basic)	(\$0.01)	(\$0.18)	(\$0.05)	(\$0.08)

Subsequent Events

We are required to submit quarterly and annual certificates of compliance to each of our lenders stating that we believe we are in compliance of all required loan covenants or what our plan of action may be in the event we are not fully in compliance with one or more loan covenants. We are



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not in compliance with several financial ratios, including debt to EBITDA and the current ratio (the ratio of current assets to current liabilities), and several non-financial covenants. We are currently in negotiations with Goldman and Silver Point to amend our credit agreements.

In the event that we are unable to cure these violations or receive waivers, and the lenders were to call our debt, and/or the potential violations remained outstanding, we could be required to seek alternative capital or engage in additional asset sales in order to reduce or pay off that debt or pursue a restructuring of the company if no proceeds could be raised to pay off the called debt.

The other subsequent event, being the closing of the sale of the two onshore California assets, has been described above and in the accompanying notes to the unaudited financial statements.

Business Risks & Risks Management

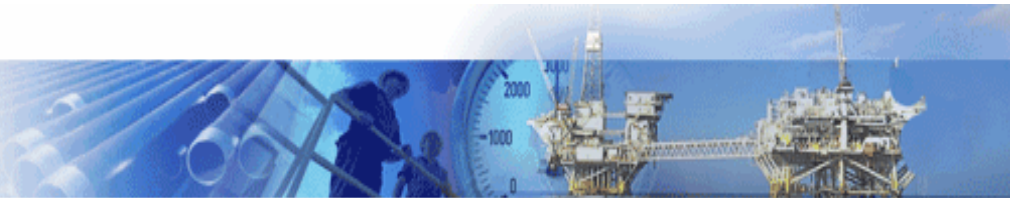
Except for historical information contained in this discussion and analysis, disclosure statements contained herein are forward-looking, which statements are subject to risks and uncertainties, which could cause actual results to differ materially from those in such forward-looking statements. Our long-term commercial success depends on our ability to find, acquire, develop, and commercially produce oil reserves. We attempt to reduce these risks through the combination of experienced personnel with local knowledge and careful evaluation. For example, in our two primary areas of operation, offshore California and Cook Inlet Alaska, we have retained personnel with historical knowledge of both the assets and the areas of operations. In some cases these personnel were retained through our acquisitions as key employees. In other cases we actively recruited for these personnel.

External factors beyond our control may affect the marketability of the oil and gas produced, however, we believe we have selected appropriate personnel to monitor field operations and have automated some field information where possible so that difficulties and operational issues can be assessed and dealt with on a timely basis and production maximized as much as possible.

Oil and gas exploration, development, and production operations are subject to all the risks and hazards typically associated with such operations, including hazards such as fire, explosion, blowouts and spills, each of which could result in damage to wells, production facilities, other property and environment, or in personal injury. In accordance with industry practice, we insure against most of these risks (although not all such risks are insurable). We maintain liability insurance in an amount that we consider consistent with industry practice; although the nature of these risks is such that liabilities could potentially exceed policy limits.

Future Prospects

We are optimistic about the growth potential of the Company and acknowledge that of critical importance to realize our potential will require us to restructure our capital structure to decrease our leverage and lower our cost of debt. We have a large number of proven undeveloped



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locations in inventory to be drilled. The prospect of returning Platform Eureka to full production is expected to add substantial growth in proved developed reserves and production in the second half of 2008 and beyond. We have a significant acreage position in the Cook Inlet Alaska with attractive exploration targets and we are pursuing strategic relationships to exploit our exploration projects in this area. Although there are some mechanical and operational challenges inherent in areas of our operations, with proper risk management and careful evaluation, we believe that we can achieve growth in production, reserves, and cash flow. We continue to actively evaluate and pursue potential producing reserve acquisitions in our strategic areas of operation.

Internal Disclosure Controls

We place considerable importance on the appropriate capture and reporting of financial information. We further recognize the need for timeliness with respect to management reporting to the appropriate internal personnel including the Chief Executive Officer, the President and the Chief Financial Officer among others, and the importance of effectively communicating relevant information to the investor community. With that in mind, we have designed internal controls specifically aimed at providing a reasonable level of assurance that material transactions are reported, accounted for properly, and effectively communicated to key decision makers within the organization. No internal control system will prevent intentional omissions or fraud.

We have determined we have a number of material weaknesses in our internal reporting systems as a result of our increased complexity and small corporate staff. We believe these deficiencies are the result of a less than adequate number of qualified accounting staff and reserve engineers. Concurrent with the filing of our financial reports for the second quarter of 2008, we filed restated first quarter 2008 financial statements and management's discussion and analysis. Additionally, we have recently been subject to a periodic review by a regulatory authority and expect to file an amended 2007 Annual Information Form, National Instrument 51-101 Oil and Gas Disclosure Form 51-101 and Business Acquisition Report (dated November 9, 2007) on completion of their review. We have already provided this regulatory authority a response to their inquiries. We also have already begun addressing the above mentioned deficiencies by the hiring of a new Chief Financial Officer with extensive public company reporting experience, whose mandate includes strengthening controls over financial reporting, and are looking to add more expertise in oil and gas reserve reporting. At this time, we conclude that our internal controls are less than adequate for our current size and complexity, but are confident that we have a plan to augment these controls to a level more than appropriate for our future growth.

In accordance with Multilateral Instrument 52-109, our Chief Executive and Chief Financial Officers are required to sign individual Certifications of the Annual Filings. These have been filed separately from the Management Discussion and Analysis and are available for viewing on SEDAR.com.

