UNREALIZED**POTENTIAL**
OPPORTUNITYDRIVEN

cequence
energy ltd

HIGHLIGHTS

	Three months ended December 31		Year ended December 31	
(000s except per share amounts)	2009	2008	2009	2008
Financial ($)				
Production revenue, including realized hedge	$ 8,847	$ 8,079	$ 27,983	$ 46,953
Net loss	(2,656)	(987)	(8,654)	(8,179)
Per share, basic and diluted	(0.07)	(0.10)	(0.41)	(0.84)
Funds flow from operations [(1)]	3,161	1,278	3,927	20,589
Per share, basic and diluted	0.08	0.13	0.19	2.11
Funds flow from operations before reorganization expenses [(2)]	3,161	1,278	7,222	20,589
Per share, basic and diluted	0.08	0.13	0.34	2.11
Production volumes				
Natural gas (mcf/d)	10,696	9,480	8,348	12,139
Crude oil (bbls/d)	230	186	151	210
Natural gas liquids (bbls/d)	76	122	85	115
Total (boe/d)	2,089	1,887	1,627	2,349
Sales prices				
Natural gas, including realized hedges ($/mcf)	$ 6.97	$ 7.34	$ 7.46	$ 8.06
Crude oil ($/bbl)	71.65	53.55	65.09	93.64
Natural gas liquids ($/bbl)	68.82	67.98	53.91	93.57
Total ($/boe)	$ 46.05	$ 46.52	$ 47.12	$ 54.61
Operating netbacks ($/boe)				
Price	$ 46.05	$ 46.52	$ 47.12	$ 54.61
Royalties	(4.21)	(5.15)	(5.33)	(6.69)
Transportation	(4.07)	(1.97)	(2.65)	(1.55)
Operating costs	(14.06)	(16.30)	(16.52)	(14.85)
Operating netback	$ 23.71	$ 23.10	$ 22.62	$ 31.52
Capital expenditures	16,526	6,095	24,836	37,429
Corporate acquisition	380	(14,437)	38	(14,437)
Property acquisitions	5,994	-	21,757	-
Property dispositions	-	(71)	-	(21,262)
Total capital expenditures	22,900	(8,413)	46,631	1,730
Net working capital (deficiency) [(3)]	6,010	(33,305)	6,010	(33,305)
Long-term debt related to investments [(4)]	(18,054)	-	(18,054)	-
Weighted average shares outstanding (basic and diluted)	38,152	9,698	21,085	9,753
Undeveloped land (net acres)	145,229	121,000	145,229	121,000

(1) Funds flow from operations is calculated as net income plus non controlling interest, unrealized derivate gains and losses, depletion, accretion, future income taxes, stock compensation expense, valuation allowances and loan premium amortization.

(2) Funds flow before reorganization expense is calculated as funds flow plus the reorganization expenses of $3,295.

(3) Net working capital is calculated cash, net working capital less derivative contract asset and demand credit facilities.

(4) The long-term debt related to investments is a stand-alone credit facility with Cequence's lender to provide short term liquidity to the Company in light of the restructuring of the asset backed MAV II notes.

MANAGEMENT'S DISCUSSION AND ANALYSIS

This Management's Discussion and Analysis ("MD & A") of the financial and operating results for Cequence Energy Ltd. ("Cequence" or the "Company") should be read in conjunction with the Company's audited consolidated financial statements (the "Financial Statements") and related notes for the years ended December 31, 2009 and 2008.

Additional information relating to the Company, including its quarterly MD & A for the year and the annual information form for the year are available on SEDAR at www.sedar.com.

This MD & A is dated March 17, 2010.

BASIS OF PRESENTATION

The financial data presented below has been prepared in accordance with Canadian Generally Accepted Accounting Principles ("GAAP"). The financial information presented reflects the consolidated financial statements of Cequence. In accordance with Canadian GAAP, the consolidated statements of Cequence include 100 percent of HFG Holdings Inc. ("HFG") with the minority interest reflected as a 'non-controlling interest' on the income statement for the period prior to acquisition of the entirety of HFG's shares by Cequence.

The reporting and the measurement currency is the Canadian dollar. For the purpose of calculating unit costs, natural gas is converted to a barrel equivalent ("boe") using six thousand cubic feet of natural gas equal to one barrel of oil, unless otherwise stated. The term barrels of oil equivalents ("BOE") may be misleading, particularly if used in isolation. A BOE conversion ratio for gas of 6 mcf:1 boe is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead.

Unless otherwise stated and other than per unit items, all figure are presented in thousands.

NON-GAAP MEASUREMENTS

Within the MD & A references are made to terms commonly used in the oil and gas industry. Netback is not defined by GAAP in Canada and is referred to as a non-GAAP measure. Netbacks equal total revenue less royalties, operating costs and transportation costs. Management utilizes this measure to analyze operating performance.

Funds flow from operations is a non-GAAP term that represents net income (loss) adjusted for non-cash items including depletion, depreciation, accretion, future income taxes, stock-based compensation, unrealized hedge gains (losses), valuation allowances, loan premium amortization, asset write-downs, gains (losses) on sale of assets and non-controlling interest and before adjustments for changes in working capital. The Company evaluates its performance based on earnings and funds flow from operations. The Company considers funds flow from operations a key measure as it demonstrates the Company's ability to generate the cash flow necessary to fund future growth through capital investment and to repay debt. The Company's calculation of funds flow from operations may not be comparable to that reported by other companies. Funds flow from operations per share is calculated using the same weighted average number of shares outstanding used in the calculation of income (loss) per share.

Non-GAAP financial measures do not have a standardized meaning prescribed by GAAP and are therefore unlikely to be comparable to similar measures presented by other issuers.

OVERVIEW

REORGANIZATION OF SABRETOOTH

On July 30, 2009, the shareholders of Cequence (formerly Sabretooth Energy Ltd.) approved certain reorganization transactions to recapitalize the Company with new equity, appoint new management and restructure the board of directors. Also as part of the transaction the Company changed its name to Cequence Energy Ltd. and affected a four for one share consolidation (the "reorganization transactions"). These transactions were approved by the shareholders of the Company at the annual and special meeting of shareholders held on July 29, 2009.

The reorganization transactions included a private placement to new management, employees, directors and consultants; a rights offering to existing shareholders and a subscription receipt offering. Total cash proceeds from the equity offerings totalled $65,315, a portion of which was used to eliminate the outstanding operating bank line and complete three property acquisitions in the year. At December 31, 2009, the Company was in strong financial condition to pursue further acquisition and drilling opportunities with positive cash and working capital and access to a $45,000 credit facility.

Due to the nature of the reorganization, all of the legal, severance and banking costs have been expensed in the period. These costs totalled $3,295 and are not recurring.

ACQUISITION OF HFG

On November 12, 2009, the Company acquired all of the issued and outstanding shares of HFG not already held by Cequence, for consideration of 2,645 common voting shares. The transaction was accounted for using the purchase method. The elimination of the non-controlling interest through an acquisition at a purchase price greater than HFG's book value in the Company's consolidated financial statements had the effect of increasing property and equipment assets, and decreasing future income tax assets. The accounts of the Company include the results of HFG for the year ended December 31, 2009. The non-controlling interest presented on the statement of operations includes the non-controlling interest's share of the operations of HFG to the date of the acquisition.

The cost of acquisition was satisfied by 2,645 shares valued at $3.97 per share based on the average trading price of the Company's stock during the three days before and three days after the announcement of the transaction. Transaction costs were $380 for total acquisition cost of $10,882. The fair value assigned to assets and liabilities acquired was allocated as $8,486 to non-controlling interest at date of acquisition, $3,123 to property and equipment and a reduction of $727 to future income tax asset for a total of $10,882.

The attributed values of the common shares issued have been excluded from the consolidated statement of cash flows as non-cash transactions.

SELECTED FINANCIAL INFORMATION

Cequence recorded a loss of $8,654 for the year ended December 31, 2009. Net income and funds flow from operations for the period were negatively impacted by reorganization costs of $3,295. In addition, low natural gas prices and high operating costs contributed to the net loss for the year ended December 31, 2009.

Funds flow from operations was $3,927 for the year compared to $20,589 in 2008. The decrease in funds flow is due to the reorganization costs expensed in the year, higher royalty and operating costs and a decrease in sales volumes and prices from the prior year.

	Year ended December 31		
$(000s)	2009	2008	2007
Production revenue[1]	$ 27,983	$ 46,953	$ 32,821
Funds flow from operations	3,927	20,589	14,524
Per share – basic and diluted	0.19	2.11	2.13
Net income (loss)	(8,654)	(8,179)	3,775
Per share – basic and diluted	(0.41)	(0.84)	0.55
Total Assets	208,111	164,646	169,610
Demand credit facilities	-	47,970	46,256
Long-term debt related to investments	$ 18,054	$ -	$ -

(1) Includes realized gains and losses on derivative commodity contracts.

A reconciliation of funds flow from operations is as follows:

	Three months ended December 31		Year ended December 31	
$(000s)	2009	2008	2009	2008
Net loss	$ (2,656)	$ (987)	$ (8,654)	$ (8,179)
Depletion, depreciation and amortization	4,370	4,494	14,349	20,285
Accretion	74	39	207	212
Stock based compensation	139	157	712	918
Valuation allowance on investments	(331)	(410)	213	8,052
Unrealized loss (gain) on derivative financial instruments	1,604	(2,482)	1,632	(2,191)
Loan premium amortization	(17)	-	(50)	-
Future income tax (recovery)	(22)	483	(4,494)	1,508
Non-controlling interest	-	(16)	12	(16)
Funds flow from operations	$ 3,161	$ 1,278	$ 3,927	$ 20,589

RESULTS OF OPERATIONS

PRODUCTION

Production for the year ended December 31, 2009 averaged 1,627 boe/d compared to production of 2,349 boe/d in 2008. The decrease in production is due to natural production declines and the sale of approximately 545 boepd of production in July and August of 2008. The property acquisitions completed in 2009 did not have a material impact on average production as the major acquisition closed on September 24, 2009.

Production for the three months ended December 31, 2009 averaged 2,089 boe/d compared to production of 1,887 boe/d in the fourth quarter of 2008. Average production volumes for the three and twelve month periods ended December 31, 2009 and 2008 are outlined below:

	Three months ended December 31			
		2009		2008[1]
	Total	Per Day	Total	Per Day
Natural gas (mcf)	984,063	10,696	872,201	9,480
Crude oil (bbls)	21,163	230	17,090	186
NGLs (boe)	6,979	76	11,180	122
Total (boe)	192,153	2,089	173,646	1,887

	Year ended December 31			
		2009		2008[1]
	Total	Per Day	Total	Per Day
Natural gas (mcf)	3,046,959	8,348	4,443,003	12,139
Crude oil (bbls)	54,981	151	76,970	210
NGLs (boe)	31,018	85	42,262	115
Total (boe)	593,825	1,627	859,780	2,349

(1) Includes royalty volumes.

PRICING

Benchmark natural gas and crude oil prices decreased from the comparative periods in 2008. Cequence realized natural gas price for the three and twelve month periods ended December 31, 2009 of $6.97 and $7.46. The realized prices are significantly above prevailing market prices as a significant portion of the Company's natural gas production in the quarter was sold at a price of $7.85 under a fixed price contract. Cequence's production is approximately 86 percent natural gas and fluctuations in natural gas prices have a significant impact on the Company.

Oil prices for the fourth quarter of 2009 were $71.65 per barrel up 34 percent from the same time period in 2008. For the year ended December 31, 2009, realized oil prices decreased 30 percent to $65.09 per boe. Natural gas liquids prices for the fourth quarter of 2009 were $68.82 per barrel, consistent with the same time period in 2008. For the year ended December 31, 2009 realized natural gas liquids prices decreased 42 percent to $53.91 per boe.

The following tables detail the Company's average sales prices and benchmark indices:

Average Selling Price	Three months ended December 31		Year ended December 31	
	2009	2008	2009	2008
Natural gas ($/mcf)	$ 4.96	$ 6.59	$ 4.40	$ 8.44
Realized natural gas hedge ($/mcf)	2.01	0.75	3.06	(0.38)
Natural gas including realized hedge gains and losses ($/mcf)	6.97	7.34	7.46	8.06
Crude oil (per bbl)	71.65	53.55	65.09	93.64
Natural gas liquids (per bbl)	68.82	67.98	53.91	93.57
Average sales price before hedge (per boe)	$ 35.78	$ 42.74	$ 31.43	$ 56.61
Average sales price including hedge (per boe)	$ 46.05	$ 46.52	$ 47.12	$ 54.61

Benchmark Pricing	Three months ended December 31		Year ended December 31	
	2009	2008	2009	2008
AECO –C Spot (CDN$/Mcf)	4.62	6.75	3.99	8.21
WTI crude oil (US$/bbl)	76.13	59.08	62.09	99.75
Edmonton par price (CDN$/bbl)	77.05	64.63	66.83	103.47
US$/CDN$ exchange rate	0.95	0.83	0.88	0.94

COMMODITY PRICE MANAGEMENT

Cequence has a commodity price risk management program and will enter into derivative and physical commodity contracts to protect future cash flows or planned capital expenditures. The Company has a natural gas contract in place until the end of March 2010 for the sale of 6,000 gj per day of natural gas for a price of $7.85 per gj. The fair value of derivative commodity contracts at December 31, 2009 is $1,420 compared to $3,034 in 2008. As at December 31, 2009, an increase in gas price of $0.50/gj results in a decrease in the fair value of the commodity contract of $267 ($190 after tax).

	Three months ended December 31		Year ended December 31	
	2009	2008	2009	2008
Realized gain (loss) on commodity contracts	1,973	657	9,319	(1,721)
Unrealized gain (loss) on commodity contracts	(1,613)	2,482	(1,614)	2,191
Total	360	3,139	7,705	470

REVENUE

Total revenue was $8,847 in the fourth quarter of 2009 compared to $8,079 for the comparable period in 2008. The increase in revenue is mainly attributable to the 11 percent increase in production. For the year ended December 31, 2009 total revenue decreased 40 percent to $27,983 from $46,953 in the prior year. The decrease in revenue for the year is a result of a 31 percent decrease in production volumes and a 14 percent decrease in sales price.

	Three months ended December 31		Year ended December 31	
$(000s)	2009	2008	2009	2008
Natural gas	$ 4,879	$ 5,747	$ 13,413	$ 37,511
Realized gains (losses) on natural gas contracts	1,973	657	9,319	(1,721)
Total natural gas	6,852	6,404	22,732	35,790
Oil	1,516	915	3,579	7,208
Natural gas liquids	479	760	1,672	3,955
Total revenue	$ 8,847	$ 8,079	$ 27,983	$ 46,953

ROYALTY EXPENSE

Royalty expense in the fourth quarter of 2009 was $809 or 12 percent of revenue compared to $894 or 13 percent of revenue in the fourth quarter of 2008. Royalties as a percentage of revenue are consistent for the fourth quarter of 2009 compared to 2008. For the year ended December 31, 2009 royalties as a percentage of revenue were 17 percent compared to 12 percent in the comparative period in 2008. On a per barrel basis royalties decreased in the year primarily due to lower natural gas prices. Based on the nature of the Company's production and facilities, at current commodity prices Cequence reduces a significant portion of its crown royalties with gas cost allowance. The Company expects that based on forecast oil and gas prices that royalties will be approximately 10 percent of revenue in 2010.

	Three months ended December 31		Year ended December 31	
$(000s)	2009	2008	2009	2008
Royalties ($)	$ 809	$ 894	$ 3,164	$ 5,753
As a % of sales, before hedging activity	12%	13%	17%	12%
Per unit of production ($/boe)	$ 4.21	$ 5.15	$ 5.33	$ 6.69

TRANSPORTATION EXPENSE

Transportation costs for the year ended December 31, 2009 were $2.65 per boe, an increase of 71 percent from the comparative period in 2008. In the fourth quarter of 2009 transportation costs increased to $4.07 per boe from $1.97 in the comparative period due to a transportation agreement acquired in a property acquisition. Beginning in the fourth quarter, approximately 2,800 mcf/d of natural gas is being shipped on the Alliance pipeline. The approximate transportation charge for this transportation is $1.50 per mcf. Cequence expects transportation to average approximately $3.50 per boe in 2010.

	Three months ended December 31		Year ended December 31	
$(000s)	2009	2008	2009	2008
Transportation ($)	$ 781	$ 342	$ 1,575	$ 1,336
Per unit of production ($/boe)	$ 4.07	$ 1.97	$ 2.65	$ 1.55

OPERATING COSTS

Operating costs during the fourth quarter of 2009 were $2,702 or $14.06 per boe compared to $2,831 or $16.30 per boe for the same time period in 2008. For the year ended December 31, 2009 operating costs increased to $16.52 per boe from $14.85 in the comparative period. The increase in operating costs per boe for the year ended December 31, 2009 were a result of decreased production while fixed costs remained constant. Operating costs decreased in the fourth quarter of 2009 compared to 2008 as production levels increased and through lower operating costs on the properties acquired in the third quarter. Cequence expects operating costs to be approximately $13-$15/boe in 2010.

	Three months ended December 31		Year ended December 31	
$(000s)	2009	2008	2009	2008
Operating costs ($)	$ 2,702	$ 2,831	$ 9,809	$ 12,771
Per unit of production ($/boe)	$ 14.06	$ 16.30	$ 16.52	$ 14.85

OPERATING NETBACKS

Cequence's netback for the fourth quarter of 2009 increased to $23.71 per boe in 2009 from $23.10 in 2008. For the year ended December 31, 2009 netback decreased to $22.62 per boe from $31.52 in the comparative period. In comparison to 2008, the decrease in the netback in the twelve month period is primarily due to the lower average selling prices and higher transportation and operating expenses.

	Three months ended December 31		Year ended December 31	
	2009	2008	2009	2008
Production revenue, including realized hedge gains (losses)	$ 46.05	$ 46.52	$ 47.12	$ 54.61
Royalty expense	(4.21)	(5.15)	(5.33)	(6.69)
Transportation expense	(4.07)	(1.97)	(2.65)	(1.55)
Operating costs	(14.06)	(16.30)	(16.52)	(14.85)
Netback, $/boe	$ 23.71	$ 23.10	$ 22.62	$ 31.52
Netback, excluding realized hedge gains (losses) $/boe	$ 13.44	$ 19.32	$ 6.93	$ 33.52

GENERAL AND ADMINISTRATIVE EXPENSES

For the year ended December 31, 2009, G&A expenses increased to $4,667 from $3,962 in 2008. On a per barrel basis, general and administrative costs increased for the year ended December 31, 2009 compared to 2008 as the production base of the Company has declined.

General and administrative ("G&A") expenses were $1,125 or $5.85 per boe for the three months ended December 31, 2009, including $561 or $2.92 per boe of one time charges associated with the settlement of lawsuits stemming from the Bear Ridge acquisition in 2007. On a per barrel basis, G&A expenses decreased 11 percent to $5.85 per boe from the same period in 2008. As a result of the reorganization transactions and subsequent acquisitions, G&A expenses were lower in the fourth quarter of 2009 compared to 2008. Cequence expects G&A expenses to be $3.00 - $3.75 per boe in 2010.

For the three and twelve months ended December 31, 2009, Cequence capitalized $256 and $1,441 of G&A expenses related to exploration and development.

	Three months ended December 31		Year ended December 31	
$(000s)	2009	2008	2009	2008
G&A expenses ($)	$ 1,125	$ 1,135	$ 4,667	$ 3,962
Total G&A ($/boe)	$ 5.85	$ 6.54	$ 7.86	$ 4.61

REORGANIZATION EXPENSES

The twelve month period ended December 31, 2009, includes all of the costs of the reorganization transactions completed on July 30, 2009. These one-time costs relate primarily to the legal, investment banking and severance costs incurred to restructure the Company and totalled $3,295.

INTEREST EXPENSE

Interest expense for the three months ended December 31, 2009, was $168 compared to $465 for the comparative period. For the year ended December 31, 2009 interest expense was $1,405 compared to $2,543 in 2008. The decrease in interest expense in both periods is attributable to the decrease in bank debt and lower interest rates. Interest expense includes $41 and $285 of part XII.6 tax related to the outstanding flow through obligations for the three and twelve month periods ended December 31, 2009. As part of the reorganization of Sabretooth the Company repaid all of its outstanding current debt and; as a result, interest expense has decreased in the fourth quarter of 2009.

	Three months ended December 31		Year ended December 31	
$(000s)	2009	2008	2009	2008
Interest expense ($)	$ 168	$ 465	$ 1,405	$ 2,543
Per unit of production ($/boe)	$ 0.87	$ 2.68	$ 2.37	$ 2.96

DEPLETION, DEPRECIATION AND AMORTIZATION ("DD&A")

DD&A expense for the three months ended December 31, 2009 was $4,370 or $22.74 per boe. For the year ended December 31, 2009 DD&A was $14,349 or $24.16 per boe. DD&A rates are comparable with the prior year.

	Three months ended December 31		Year ended December 31	
$(000s)	2009	2008	2009	2008
Depletion expense ($)	$ 4,370	$ 4,494	$ 14,349	$ 20,285
Per unit of production ($/boe)	$ 22.74	$ 25.88	$ 24.16	$ 23.59

ASSET RETIREMENT OBLIGATIONS

Total asset retirement obligations at December 31, 2009 were $4,059 compared to $2,515 at December 31, 2008. Additions to asset retirement obligations in the fourth quarter totalled $168 of which $36 related to the one property acquisition and $132 to drilling activity and facility additions. During the three and twelve month periods ended December 31, 2009, the Company recorded accretion expense of $74 and $207, respectively.

STOCK-BASED COMPENSATION

The Company recognizes stock-based compensation expense for stock options and performance warrants. For the three months ended December 31, 2009, Cequence recorded $139 (2008 - $157) in stock-based compensation expense, with a corresponding increase to contributed surplus. For the year ended December 31, 2009 stock-based compensation was $712 compared to $918 in 2008. As part of the reorganization, substantially all the outstanding stock options were forfeited on July 30, 2009. In total, 731 options were forfeited and $421 of previously recognized stock compensation expense was reversed in the third quarter.

The Company issued 900 options in the year. Total stock-based compensation expense of $1,548 was determined using the Black-Scholes option pricing model and will be expensed over the four year vesting period of the options.

As part of the reorganization, certain officers and directors of the Company were awarded a total of 5,200 performance warrants that are exercisable into a non-voting share of Cequence at a price of $1.88. At the time the performance warrants were negotiated the market price of the Company's shares was $1.48. The performance warrants are divided into three equal tranches with the first one-third having a four year term and vest once the 20 day weighted average share price of Cequence exceeds $3.20. The second tranche has a 4.5 year term and vests if the 20 day weighted average share price of Cequence exceeds $4.40. The final third of the performance warrants have a five year term and vest if the 20 day weighted average share price of Cequence exceeds $5.60. The performance warrants are convertible to non-voting shares of Cequence.

The performance warrants are considered stock based compensation and have been valued using a Black-Scholes option pricing model. As of December 31, 2009, the first two performance criteria had been met, and the Company recognized the full compensation expense related to the first two tranches of the performance warrants. The Company recognized $520 of stock-based compensation for the performance warrants in the year ended December 31, 2009.

COMMON SHARES OUTSTANDING

Issued common voting shares (000s)	Number		Stated Value
Balance, December 31, 2008	9,665		192,849
Repurchase of shares - NCIB, January 7, 2009	(50)		(997)
Private placement, July 30, 2009	6,377		9,438
Corporate acquisition, July 30, 2009	380		562
Subscription receipts, July 30, 2009	13,398		46,087
Rights offering, August 14, 2009	6,615		9,790
Issue of flow-through shares, October 26, 2009	500		2,025
Corporate acquisition, November 12, 2009	2,645		10,502
Share issue costs (net of tax of $884)	-		(2,348)
Balance, December 31, 2009	39,530	$	267,908

As part of the corporate reorganization in July 2009, the Company was recapitalized through a series of transactions, as described below. In total 26,770 common shares were issued for consideration of $65,877 before issue costs.

The new management, directors, certain employees and consultants of the Company (as well as a former officer of the Company) purchased 6,377 common shares of the Company at a price of $1.48 per share for aggregate subscription proceeds of $9,438 (the "Private Placement"). Existing shareholders of the Company were granted rights to acquire a maximum of 6,757 common shares at a price of $1.48 until August 14, 2009. A total of 6,615 rights were exercised for total consideration of $9,790 (the "Rights Offering").

On May 27, 2009 the Company entered into an agreement to sell on a private placement basis 13,398 subscription receipts at a price of $3.44 per subscription receipt for total proceeds of $46,087. The subscription receipts were convertible to Cequence common shares without further consideration upon shareholder approval of the reorganization transactions and regulatory approval. Upon closing of the Transactions, the Company's subscription receipts previously issued on June 18, 2009 were converted, for no additional consideration and without further action, into common shares of the Company. Holders of the subscription receipts received one common share of the Company for each subscription receipt held.

The Company also acquired all the shares of a private oil and gas company owned by certain members of the new management team in exchange for the issuance of an aggregate of approximately 380 common shares of the Company at a price of $1.48 per share for total consideration of $562. The purchase price was allocated to cash and working capital of $335, property and equipment of $321 and future income tax liability of $94. The private oil and gas company has a CEE flow through share commitment of $400 that was spent, as required, prior to the end of 2009.

As part of the reorganization, the Company consolidated its common shares on a four for one basis. All historical amounts have been restated.

As of the date of this MD&A, Cequence had the following securities outstanding: 39,530 common voting shares, 5,200 warrants and 1,022 stock options.

CAPITAL EXPENDITURES

	Three months ended December 31		Year ended December 31	
$(000s)	2009	2008	2009	2008
Property acquisitions	$ 5,994	$ -	$ 21,757	$ -
Property dispositions	-	(71)	-	(21,262)
Corporate acquisitions	380	$ (14,437)	38	(14,437)
Land	969	13	1,580	5,944
Geological & geophysical and capitalized overhead	1,503	407	2,715	2,516
Drilling, completions and workovers	13,671	4,729	19,062	24,306
Equipment and facilities	319	946	1,415	4,668
Office furniture & equipment	64	-	64	(5)
Total capital expenditures	$ 22,900	$ (8,413)	$ 46,631	$ 1,730

Total capital expenditures for the year ended December 31, 2009, increased significantly from 2008 when the Company disposed of $35,699 of oil and gas assets. Capital expenditures in 2009 were concentrated in the time period following the recapitalization of the Company.

Three property acquisitions were completed in 2009 for total consideration of $21,757. The acquisitions were for oil and natural gas properties in the Peace River Arch area of Northwest Alberta. Corporate acquisitions consisted of the acquisition of a small private company for total consideration of $562 and the acquisition of the remaining interest of a subsidiary, HFG. On November 12, 2009, the Company acquired all of the issued and outstanding shares of HFG not already held by or on behalf of Cequence for consideration of 10,882. The transaction was accounted for using the purchase method.

For the year ended December 31, 2009, drilling activities totalled $19,062 and included the drilling of three net horizontal wells and two net vertical wells in the Sinclair and Gordondale areas of north western Alberta. In the year ended December 31, 2009, the Company earned Alberta crown drilling credits that reduced the amount of drilling capital by $3,112 in the year.

INCOME TAXES

At December 31, 2009, a future income tax asset of $5,575 (2008 - $6,825) has been recognized as the Company believes, based on estimated cash flows, it is more likely than not to be realized. There is also a current future income tax liability recognized at December 31, 2009 of $424 (2008 - $696). At December 31, 2009, Cequence has the following tax pools:

Classification		Amount $(000s)
UCC	$	22,169
COGPE		33,963
CEE		41,170
CDE		6,021
Share issue costs		3,981
SRED		22,704
Non-capital losses		32,218
ITCs		3,981
	$	166,207

The non-capital losses and investment tax credits expire as follows:

Year of expiry		Non-capital losses $(000s)		Investment tax credits $(000s)
2010	$	-	$	930
2011		-		1,280
2012		-		672
2013		6,812		761
2014		2,791		338
2015+		22,615		-
	$	32,218	$	3,981

Based on the Company's expected cash flow and available tax pools, Cequence does not expect to be taxable in 2010.

INVESTMENTS

The Company owns Asset Backed Notes ('MAV Notes') with a face value of $24,142. These Notes were issued in replacement of Third Party Asset Backed Commercial Paper ('ABCP') formerly held by the Company. In August 2007, this ABCP matured but was not redeemed as a result of liquidity issues in the ABCP market. The outstanding ABCP became the subject of a restructuring process overseen by the Pan Canadian Investor Committee. The restructuring was concluded on January 21, 2009 when the ABCP was replaced with long term asset backed securities - the MAV Notes.

Using publicly available information received from the Pan Canadian Investor Committee, Blackrock,the asset administrator, and Ernst & Young, the court appointed monitor of the restructuring, the Company has been able to determine the key characteristics of each class of MAV Notes it received: par value; credit rating; interest rate and projected interest payments; and maturity date. The Company then engaged an ABCP expert to help it estimate the return that a prospective investor would require for each class of MAV Notes (Required Yield). Lastly, it calculated the net present value of the cash flows for each class of MAV Notes using the Required Yield as the discount factor.

During the year, the Fair Market Value of the MAV Notes has been impacted – both positively and negatively – by a number of factors.

Positively, there has been a continued improvement in general corporate credit market conditions over this time period. This decrease in credit risk impacts the intrinsic value of the MAV Notes due to a general lowering of default risk and a decrease in the likelihood that credit risk limits built into the MAV Notes will be exceeded (specifically, the spread-based margin triggers). Accordingly, the Required Yields on the MAV Notes has been generally reduced to reflect easing in the credit markets.

It is anticipated that the MAV2 Pooled Notes – and specifically Classes A-1 and A-2 – will continue to miss interest payments as long as the prevailing interest rates remain at the currently very low levels. Given statements of the Bank of Canada, and given that there was sufficient cash inflows to the MAV for the payment period ending October 7 to enable full payment of amounts accrued and owing, the Company projects that both the A-1 and A-2 Notes will miss payments for the next 3 quarters. Previously, it was anticipated that these Notes would miss more payments; this change in assumption causes an increase in the valuation of the A-1 and A-2 Notes.

Another positive factor is the simple passage of time. As with all debt instruments, the value of these MAV Notes will approach par as the date of maturity approaches, assuming that they do not default. The reduction in the time-to-maturity is a factor that increases the Fair Market Value of the MAV Notes this period.

The offsetting negative factor that influenced the valuation of the MAV Notes was the increased risk of default of the MAV2 Class C Notes due to idiosyncratic defaults among the assets within the MAV2 Pool. While the improvement in credit market conditions has generally strengthened the risk profile of the Pooled assets, a small number of those assets weakened during Q4 due to concentrated risk exposure to underperforming sectors of the US economy. If these assets default, it is likely that losses within the Pool will exceed the value of the C Notes rendering them valueless and somewhat impair the redemption value of the B Notes. The subordination 'cushion' against losses for the more-senior Notes would also be reduced. Thus, the Company has increased the discount rate for the MAV2 C, B and A-2 Notes, which reduced prices of these Notes from levels they otherwise would have been.

For the valuation as at December 31, 2009, the Company engaged an ABCP expert and it has adopted the valuation model of that advisor. The methodology used takes into consideration market and other events affecting the MAV Notes and is expected to reflect the evolution of these Notes on a going-forward basis. The net impact of these positive and negative factors was an increase in fair market value in the fourth quarter of $331. As a result of this analysis, the Company has estimated the fair market value of its MAV Notes investment to be $13,738 as at December 31, 2009. Accordingly, the Company has recorded an impairment of long-term investments of $213 in the year.

Management believes that an appropriate methodology has been used to estimate fair value; however, given the volatility of global credit markets there can be no assurance that management's estimate of potential recovery as at December 31, 2009 is accurate. Subsequent adjustments, either materially higher or lower, may be required in future reporting periods. Management will continue to seek all avenues to recover the maximum value from the original investments and interest due. The secondary market for the MAV Notes is showing signs of developing but there remain a small number of disclosed transactions. It is uncertain if or when a more liquid secondary market for the MAV Notes will develop.

There are currently no market quotations available for the ABCP or the new MAV 2 notes and uncertainties exist regarding the value of the assets which underlie the MAV 2 notes, the amount and timing of cash flows, the evolution of the liquidity of the market for the new notes issued following the restructuring and the evolution of the prevailing economy could give rise to a further change in the value of the Company's investment in the MAV 2 notes. It is reasonably possible that changes in future conditions in the near term could require a material change in the recognized amount. A 1.0 percent increase in the discount rate will decrease the fair value of the MAV 2 notes by approximately $830 before tax.

LIQUIDITY AND CAPITAL RESOURCES

The Company has established two credit facilities with a Canadian chartered bank. Credit facility A is a $40,000 revolving operating demand loan by way of prime rate based loans, Banker's Acceptances and letters of credit/ guarantee, which bears interest at the bank prime rate plus 0.25 percent to 2.5 percent on a sliding scale, depending on the Company's debt to cash flow ratio (ranging from being less than 1.0:1.0 to greater than or equal to 3:1). Credit facility B is a $5,000 non-revolving acquisition/development demand loan, which bears interest at the bank prime rate plus 0.75 percent to 3.0 percent on the same sliding scale as credit facility A. Both credit facilities are subject to periodic review by the bank and are secured by a general assignment of book debts and a $165,000 demand debenture with a first floating charge over all assets of the Company. The Company is required to meet certain financial based covenants under the terms of this facility. The Company is also required to hedge no more than 70 percent of its production under the lending agreement. As at December 31, 2009, the Company has not drawn on either credit facility. The next scheduled bank review is expected to take place in March 2010.

On March 31, 2009, the Company's bank provided the Company with an additional credit facility to provide liquidity in respect to the MAV 2 Notes. The credit facility is structured to a maximum of $18,120 with an initial maturity date of March 30, 2012 with an option to extend the term to seven years on a year by year basis if agreed to by both parties. The facility provides lending against the restructuring notes held by the Company and was computed in two tranches:

Tranche A: $10,854 revolving credit facility, which represents an amount equal to approximately 45 percent of the face value of the restructuring notes.

Tranche B: $7,200 revolving credit facility, which represents an amount equal to approximately 30 percent of the face value of the restructuring notes.

Interest is payable at preferred rates. Prime rate loans are at the bank prime rate less 1 percent or by bankers acceptance at discounted bankers' acceptance rates plus a stamping fee of 0.65 percent. The credit facility is secured by the MAV 2 Notes as well as a hypothecation/pledge of the notes and all cash proceeds the Company receives on the sale of MAV 2 Notes will reduce the available amount of the facility commencing with Tranche A. The Company is required to meet certain financial based covenants under the terms of this facility. The credit facility provides for the ability of the Company to assign to the bank the MAV 2 Notes in payment of the principal due under Tranche A only.

At December 31, 2009 the company had borrowed $18,054 using this facility. The effective interest rate for the year ended December 31, 2009 was 1.13 percent.

CONTRACTUAL OBLIGATIONS

	2010	2011	2012	2013	2014+	Total
Office lease	325	363	144	-	-	832
Pipeline transportation	1,592	1,592	1,592	1,592	3,050	9,418
Drilling services commitment	1,500	1,500	-	-	-	3,000
Total	3,417	3,455	1,736	1,592	3,050	13,250

The Company acquired a pipeline transportation contract in a property acquisition that expires on November 30, 2015.

CONTINGENCIES

The Bear Ridge acquisition that occurred on August 21, 2007 resulted in one dissenting shareholder. The shareholder holds 449 Bear Ridge shares and 389 Bear Ridge warrants with a strike price of $1.41. The value ascribed to the above of $919 was included in the purchase price at the date of acquisition. Subsequent to December 31, 2009, the parties have reached a settlement for total consideration of $1,280. The incremental $361 has been accrued at December 31, 2009 and is included as general and administration expenses for the year then ended.

During the year ended December 31, 2008, the Company received a Statement of Claim and Notice from a service provider of the Company for damages of $1,039. Subsequent to December 31, 2009, a settlement was reached for $200 in damages, which has been accrued at December 31, 2009 and is included as general and administration expenses for the year then ended. In addition, Cequence is committed to use the services of the Claimant, at fair market value, in the amount of $3,000 over the two years following the date of settlement.

DISCLOSURE CONTROLS AND INTERNAL CONTROLS OVER FINANCIAL REPORTING

The President and Chief Executive Officer and the Vice President, Finance and Chief Financial Officer are responsible for designing internal controls over financial reporting or causing them to be designed under their supervision in order to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with Canadian GAAP. The Company's Chief Executive Officer and Chief Financial Officer have designed, or caused to be designed under their supervision, disclosure controls and procedures to provide reasonable assurance that: (i) material information relating to the Company is made known to the Company's Chief Executive Officer and Chief Financial Officer by others, particularly during the period in which the annual filings are being prepared; and (ii) information required to be disclosed by the Company in its annual filings, interim filings or other reports filed or submitted by it under securities legislation is recorded, processed, summarized and reported within the time period specified in securities legislation.

The COSO framework provides the basis for management's design of internal controls over financial reporting. Management and the Board work to mitigate the risk of a material misstatement in financial reporting; however, a control system, no matter how well conceived or operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met and it should not be expected that the disclosure and internal control procedures will prevent all errors or fraud.

As at December 31, 2009, the Chief Executive Officer and the Chief Financial Officer have concluded, based on their evaluation of the design and operating effectiveness of the Company's disclosure controls and internal controls over financial reporting ("IFCR") that disclosure controls and ICFR are not effective due to the material weaknesses described below.

The Company will note material weaknesses with regards to: (i) the lack of segregation of duties and (ii) the lack of financial reporting expertise in the certification for the year ended December 31, 2009. As a result of the internal reporting structure and the personnel of the Company at certain times in 2008 and 2009, it was not feasible to achieve complete segregation of incompatible duties nor did the Company have a sufficient number of qualified finance personnel to address all complex and non-routine accounting transactions, which may lead to the possibility of inaccuracies in financial reporting.

The Company underwent significant changes effective July 30, 2009, including the replacement of management. In the time period following the reorganization, management began to introduce additional internal control procedures, accounting systems and accounting expertise through the hiring of additional finance and accounting employees. Management believes these changes, which occurred in late 2009 and through early 2010, will be successful in addressing the internal control weakness and expects to review the effectiveness of these changes in 2010.

QUARTERLY INFORMATION

FINANCIAL

($ thousands except per share data)	2009 Q4	2009 Q3	2009 Q2	2009 Q1	2008 Q4	2008 Q3	2008 Q2	2008 Q1
Production revenues including realized gains (losses) on financial commodity contract	$ 8,847	$ 5,962	$ 6,548	$ 6,627	$ 8,079	$11,503	$13,228	$14,143
Royalties	809	1,170	385	800	894	1,437	1,350	2,072
Operating expenses	2,702	2,609	2,212	2,286	2,831	3,995	2,782	3,163
Transportation expenses	781	309	238	247	342	319	329	346
Reorganization expenses	-	3,295	-	-	-	-	-	-
Net income (loss)	(2,656)	(6,994)	(2,444)	3,440	(987)	6,113	(2,486)	(10,819)
Per share - basic	(0.07)	(0.26)	(0.25)	0.36	(0.10)	0.63	(0.25)	(1.11)
Per share - diluted	(0.07)	(0.26)	(0.25)	0.36	(0.10)	0.63	(0.25)	(1.11)
Funds flow	3,161	(2,663)	1,517	1,912	1,278	4,900	6,558	7,853
Per share - basic	0.08	(0.10)	0.16	0.20	0.13	0.50	0.67	0.80
Per share - diluted	0.08	(0.10)	0.16	0.20	0.13	0.50	0.67	0.80
Capital expenditures, net	16,526	3,334	209	4,767	6,024	(11,983)	9,522	12,604
Acquisition, net	6,374	15,421	-	-	(14,437)	-	-	-
Total expenditures	$22,900	$18,755	$ 209	$ 4,767	$ (8,413)	$(11,983)	$ 9,522	$12,604

OPERATIONS

Production volumes	2009 Q4	2009 Q3	2009 Q2	2009 Q1	2008 Q4	2008 Q3	2008 Q2	2008 Q1
Natural gas (mcf/day)	10,696	6,734	8,077	8,164	9,480	10,918	12,422	15,773
Oil (bbl/day)	230	128	106	140	186	197	179	278
NGLs (bbl/day)	76	67	96	104	122	107	107	125
Total boe/day	2,089	1,317	1,548	1,602	1,887	2,123	2,357	3,032
Average selling price								
Natural gas ($per mcf)	6.97	7.69	7.50	7.71	7.34	8.33	8.91	7.63
Oil ($per bbl)	71.65	66.85	68.00	50.26	53.55	112.39	125.19	87.57
NGLs ($per bbl)	68.82	66.76	52.12	35.28	67.98	112.16	113.55	86.02
Combined ($per boe)	46.05	49.20	47.00	45.97	46.52	58.88	61.67	51.25
Royalties ($per boe)	4.21	9.66	2.76	5.55	5.15	7.36	6.29	7.51
Operation expense ($per boe)	14.06	21.53	15.88	15.86	16.30	20.45	12.97	11.46
Transportation ($per boe)	4.07	2.55	1.71	1.71	1.97	1.63	1.53	1.25
Netback ($per boe)	23.71	15.46	26.65	22.85	23.10	29.44	40.88	31.03

CHANGES IN ACCOUNTING POLICIES AND FUTURE ACCOUNTING PRONOUNCEMENTS

i) Goodwill and Intangible Assets

Effective January 1, 2009, the Company adopted the Canadian Institute of Chartered Accountants ("CICA") Section 3064, "Goodwill and Intangible Assets", which has replaced previous Handbook Sections 3062, "Goodwill and Other Intangible Assets" and 3450, "Research and Development Costs". This new guidance reinforces a principles-based approach to the recognition of costs as assets in accordance with the definition of an asset and the criteria for asset recognition under Handbook Section 1000, "Financial Statement Concepts". Under this new guidance, fewer items meet the criteria for capitalization. The implementation of this section had no impact on the Company's consolidated financial statements.

ii) Credit Risk and the Fair Value of Financial Assets and Financial Liabilities

Effective January 1, 2009, the Company adopted the Emerging Issues Committee (“EIC”) abstract 173, "Credit Risk and the Fair Value of Financial Assets and Financial Liabilities" which provides further information on the determination of the fair value of financial assets and financial liabilities under Section 3855, entitled “Financial Instruments – Recognition and Measurement”. EIC 173 is to be applied retrospectively without restatement of prior periods to all financial assets and liabilities measured at fair value in interim and annual financial statements for periods ending on or after the date of issuance of this abstract. The implementation of this section resulted in no change to the Company’s consolidated financial statements.

iii) Financial Instrument Disclosures

In June 2009, the CICA issued amendments to CICA Handbook Section 3862, Financial Instruments – Disclosures. The amendments include enhanced disclosures related to the fair value of financial instruments and the liquidity risk associated with financial instruments. The amendments are effective for annual financial statements for fiscal years ending after September 30, 2009. The amendments are consistent with recent amendments to financial instrument disclosure standards in IFRS. The Company has included these incremental disclosures in its annual consolidated financial statements for the year ending December 31, 2009.

FUTURE ACCOUNTING PRONOUNCEMENTS

In addition, the Company has assessed new and revised accounting pronouncements that have been issued that are not yet effective and determined that the following may have an impact on the Company:

i) Business Combinations, Consolidated Financial Statements and Non-controlling Interests

In January 2009, the CICA issued Sections 1582, “Business Combinations”, 1601, “Consolidated Financial Statements”, and 1602, “Non-controlling Interests” which replace CICA Handbook Sections 1581 “Business Combinations” and 1600 “Consolidated Financial Statements”. Section 1582 establishes standards for the accounting for business combinations that is equivalent to the business combination accounting standard under IFRS. Section 1601 together with Section 1602 establishes standards for the preparation of consolidated financial statements. These Sections apply to interim and annual consolidated financial statements relating to fiscal years beginning on or after January 1, 2011, and should be adopted concurrently. Earlier adoption is permitted. Cequence is currently assessing the impact of these standards.

ii) International Financial Reporting Standards

On January 1, 2011, International Financial Reporting Standards (“IFRS”) will become the generally accepted accounting principles in Canada. The adoption date of January 1, 2011, will require the restatement, for comparative purposes, of amounts reported by Cequence for the year ended December 31, 2010, including the opening balance sheet as at January 1, 2010. Throughout 2009, the Company has assessed the impact of adopting IFRS and is continuing to implement plans for transition. The project is being managed by in-house accounting professionals who have engaged in IFRS educational programs and continue to develop the Company’s adoption to IFRS. The Company’s auditors will be involved throughout the process to ensure the Company’s policies are in accordance with these new standards.

Management has not yet finalized its accounting policies and as such is unable to quantify the impact on the financial statements of adopting IFRS. In addition, due to anticipated changes to IFRS and International Accounting Standards prior to Cequence’s adoption of IFRS, Management’s plan is subject to change based on new facts and circumstances that arise after the date of the MD&A.

In July 2009, an amendment to IFRS 1 First Time Adoption of International Reporting Standards was issued that applies to oil and gas assets. The amendment allows an entity that used full cost accounting under its previous GAAP to elect, at its time of adoption, to measure exploration and evaluation assets at the amount determined under the entity’s previous GAAP and to measure oil and gas assets in the development and production phases by allocating the amount determined under the entity’s previous GAAP for those assets to the underlying assets pro rata using reserve volumes or reserve values as of that date. Cequence currently anticipates that it will use this exemption. IFRS 1 also provides a number of other optional exemptions and mandatory exceptions in certain areas to the general requirement for full retrospective application. Management is analyzing the various accounting policy choices available and will implement those determined to be the most appropriate for the Company which other than the full cost accounting exemption noted above are:

Business Combinations – IFRS 1 would allow Cequence to use the IFRS rules for business combinations on a prospective basis rather than re-stating all business combinations.

Borrowing Costs – IFRS 1 would allow Cequence to apply the transitional provisions of IAS 23 in lieu of full retrospective application.

The transition from Canadian GAAP to IFRS is significant and may materially affect our reported financial position and results of operations. At this time, Cequence has identified key differences that will impact the financial statements as follows:

- Exploration and Evaluation ("E&E") expenditures – On transition to IFRS Cequence will re-classify all E&E expenditures that are currently included in the PP&E balance on the Consolidated Balance Sheet. This will consist of the book value of undeveloped land that relates to exploration properties. E&E assets will not be depleted and must be assessed for impairment when indicators of impairment exist.
- Depletion expense – On transition to IFRS Cequence has the option to base the depletion calculation on either proved reserves or proved and probable reserves. Cequence has not concluded at this time which method it will use.
- Impairment of PP&E assets – Under IFRS, impairment tests of PP&E must be performed on specific portions of PP&E as opposed to the entire PP&E balance which is currently required under Canadian GAAP through the full cost ceiling test. Impairment calculations will be performed at the cash generating unit level using either total proved or proved plus probable reserves.
- Due to the recent withdrawal of the exposure draft on IAS 12 Income Taxes in November 2009 and the issuance of the exposure draft on IAS 37 Provisions, Contingent Liabilities and Contingent Assets in January 2010, Management is still determining the impact of these revised standards on its IFRS transition.

In regards to internal controls over financial reporting ("ICOFR"), Cequence will be determining which additional changes to ICOFR will be required to deal with the changes in accounting policies. This will be ongoing through 2010 to ensure all changes in accounting polices include appropriate additional controls and procedures for future IFRS reporting requirements.

In regards to disclosure controls and procedures, Cequence will be assessing stakeholders' information requirements and ensure that appropriate and timely information is provided once available.

The Company is currently evaluating updates to its systems in regards to IFRS, which primarily involved updates to its accounting system. The modifications are not anticipated to be significant, however, they will allow the Company to report both Canadian GAAP and IFRS statements and track E&E costs, transfers from E&E to PP&E and allocation of PP&E into cash generating units.

Due to the change in management resulting from the reorganization transaction, management is evaluating a timeline and milestones for the implementation of the above and plans to have such a timeline in the first quarter of 2010.

The Company will have an opening January 1, 2010 balance sheet, which is in accordance with IFRS. The Company will maintain both Canadian GAAP and IFRS compliant financial statements in 2010.

APPLICATION OF CRITICAL ACCOUNTING ESTIMATES

The significant accounting policies used by Cequence are disclosed in Note 3 to the Annual Consolidated Financial Statements. Certain accounting policies require that management make appropriate decisions with respect to the formulation of estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses. Management reviews its estimates on a regular basis. The emergence of new information and changed circumstance may result in actual results or changes to estimate amounts that differ materially from current estimates. The following discussion identifies the critical accounting policies and practices of the Company and helps assess the likelihood of materially different results being reported.

RESERVES

Oil and gas reserves are estimates made using all available geological and reservoir data, as well as historical production data. All of the Company's reserves were evaluated and reported on by an independent qualified reserves evaluator. However, revisions can occur as a result of various factors including: actual reservoir performance, change in price and cost forecasts or a change in the Company's plans. Reserve changes will impact the financial results as reserves are used in the calculation of depletion and are used to assess whether asset impairment occurs. Reserve changes also affect other Non-GAAP measurements such as finding and development costs; recycle ratios and net asset value calculations.

DEPLETION

The Company follows the full cost method of accounting for oil and natural gas properties. Under this method, all costs related to the acquisition of, exploration for and development of oil and natural gas reserves are capitalized whether successful or not. Depletion of the capitalized oil and natural gas properties and depreciation of production equipment which includes estimated future development costs less estimated salvage values are calculated using the unit-of-production method, based on production volumes in relation to estimated proven reserves.

An increase in estimated proved reserves would result in reduction in depletion expense. A decrease in estimated future development costs would also result in a reduction in depletion expense.

UNPROVED PROPERTIES

The cost of acquisition and evaluation of unproved properties are initially excluded from the depletion calculation. An impairment test is performed on these assets to determine whether the carrying value exceeds the fair value. Any excess in carrying value over fair value is impairment. When proved reserves are assigned or a property is considered to be impaired, the cost of the property or the amount of the impairment will be added to the capitalized costs for the calculation of depletion.

CEILING TEST

The ceiling test is a cost recovery test intended to identify and measure potential impairment of assets. An impairment loss is recorded if the sum of the undiscounted cash flows expected from the production of the proved reserves and the lower of cost and market price of unproved properties does not exceed the carrying values of the petroleum and natural gas assets. An impairment loss is recognized to the extent that the carrying value exceeds the sum of the discounted cash flows expected from the production of proved and probable reserves and the lower of cost and market price of unproved properties. The cash flows are estimated using the future product prices and costs and are discounted using the risk free rate. By their nature, these estimates are subject to measurement uncertainty and the impact on the financial statements could be material. Any impairment as a result of this ceiling test will be charged to operation as additional depletion and depreciation expense.

ASSET RETIREMENT OBLIGATIONS

The Company records a liability for the fair value of legal obligations associated with the retirement of petroleum and natural gas assets. The liability is equal to the discounted fair value of the obligation in the period in which the asset is recorded with an equal offset to the carrying amount of the asset. The liability then accretes to its fair value with the passage of time and the accretion is recognized as an expense in the financial statements. The total amount of the asset retirement obligation is an estimate based on the Company's net ownership interest in all wells and facilities, the estimated costs to abandon and reclaim the wells and facilities and the estimated timing of the costs to be incurred in future periods. The total amount of the estimated cash flows required to settle the asset retirement obligation, the timing of those cash flows and the discount rate used to calculate the present value of those cash flows are all estimates subject to measurement uncertainty. Any change in these estimates would impact the asset retirement liability and the accretion expense.

STOCK-BASED COMPENSATION

The Company uses fair value accounting for stock-based compensation. Under this method, all equity instruments awarded to employees and the cost of the service received as considerations are measured and recognized based on the fair value of the equity instruments issued. Compensation expense is recognized over the period of related employee service, usually the vesting period of the equity instrument awarded.

INCOME TAXES

The determination of income and other tax assets and liabilities requires interpretation of complex laws and regulations. All tax filings are subject to audit and potential reassessment after the lapse of considerable time. Accordingly, the actual income tax asset may differ significantly from that estimated and recorded by management.

The recognition of a future income tax asset is also based on estimates of whether the Company is "more likely than not" to realize these assets. This estimate, in turn, is based on estimates of proved and probable reserves, future oil and natural gas prices, royalty rates and costs. Changes in these estimates could materially impact net income and the future income tax asset recognized.

LONG-TERM INVESTMENT

See "Investments" section for an in-depth discussion of the estimates used to value the MAV 2 Notes held by the Company.

ACQUISITIONS

The value assigned to common shares issued to acquire the remaining shares of HFG and the allocation of the purchase price to the net assets of HFG at the acquisition date are based on estimates of numerous factors affecting valuation including discount rates, proved and probable reserves, future petroleum and natural gas prices and other factors.

COMMODITY CONTRACTS

The fair value of commodity contracts and the resultant unrealized gain (loss) on commodity contracts is based on estimates of future natural gas prices.

OTHER ESTIMATES

The accrual method of accounting requires management to incorporate certain estimates including estimates of revenues, royalties, capital, drilling credits and operating costs as at a specific reporting date, but for which actual revenues and costs have not yet been received. In addition, estimates are made on capital projects which are in progress or recently completed where actual costs have not been received by the reporting date. The Company obtains the estimates from the individuals with the most knowledge of the activity and from all project documentation received. The estimates are reviewed for reasonableness and compared to past performance to assess the reliability of the estimates. Past estimates are compared to actual results in order to make informed decisions on future estimates.

FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

The Company's financial instruments, including derivative financial instruments and embedded derivative financial instruments, recognized in the consolidated balance sheet consist of cash, accounts and interest receivable, commodity contracts, investments, other derivative financial instruments, demand credit facilities, accounts payable and accrued liabilities and long-term debt related to investments.

The Company's cash, accounts and interest receivable, demand credit facilities, accounts payable and accrued liabilities and long-term debt related to investments approximate their carrying values due to their short terms to maturity and the floating interest rate on the Company's debt.

The fair value of commodity contracts is determined by discounting the difference between the contracted price and published forward price curves as at the balance sheet date, using the remaining contracted petroleum and natural gas volumes.

The fair value of the Company's investment in MAV 2 notes, as discussed in ' Investments', is determined by probability-weighted discounted cash flows considering the best available public information regarding market conditions and other factors that a market participant would consider for such investments.

The fair value of other derivative financial instruments is determined using a Black-Scholes valuation model and the fair value of the underlying MAV 2 notes as at December 31, 2009.

The Company is engaged in the exploration, development, production and acquisition of crude oil and natural gas. This business is inherently risky and there is no assurance that hydrocarbon reserves will be discovered and economically produced. Financial risks associated with the petroleum industry include fluctuations in commodity prices, interest rates and currency exchange rates along with the credit risk of the Company's industry partners. Operational risks include reservoir performance uncertainties, the reliance on operators of our non-operated properties, competition, environmental and safety issues, and a complex and changing regulatory environment.

The primary risks and how the Company mitigates them are as follows:

Commodity Price and Exchange Rate Volatility

Revenues and consequently cash flows fluctuate with commodity prices and the US/Canadian dollar exchange rate. Commodity prices are determined on a global basis and circumstances that occur in various parts of the world are outside of the control of the Company. The Company protects itself from fluctuations in prices by maintaining an appropriate hedging strategy, diversifying its asset mix and strengthening its balance sheet in order to take advantage of low price environments by making strategic acquisitions. We enter into commodity price contracts to actively manage the risks associated with price volatility and thereby protect our cash flows used to fund our capital program. We have used costless collars and swap contracts to manage these risks and to take advantage of market conditions. Net earnings for the year ended December 31, 2009 included $9,319 of realized gains and $1,614 of unrealized losses on these transactions.

Cequence is also exposed to fluctuations in the exchange rate between the Canadian and US dollar. Most commodity prices are based on U.S. dollar benchmarks that results in our realized prices being influenced mainly by the Canadian/U.S. currency exchange rates. As at December 31, 2009, the Company has a pipeline commitment in US dollars and sells certain quantities of natural gas in the US dollar. There are no other forward contracts, foreign exchange contracts or other significant items denominated in foreign currencies.

Interest Rate Risk

The Company is exposed to interest rate risk to the extent that changes in market interest rates impact its borrowings under the floating rate credit facilities. The floating rate debt is subject to interest rate cash flow risk, as the required cash flows to service the debt will fluctuate as a result of changes in market rates. The Company has no interest rate swaps or financial contracts in place as at or during the three months ended December 31, 2009.

Based on debt outstanding at December 31, 2009, a 1 percent change in interest rate with all other variables held constant, earnings for the quarter would have changed by $45 ($32 after tax).

Credit Risk

Credit risk is the risk of financial loss to the Company if a counterparty to a financial instrument fails to meet its contractual obligation. The company is exposed to credit risk with respect to its accounts receivables, cash, commodity contracts and investments.

The majority of the Company's accounts receivable are due from joint venture partners in the oil and gas industry and from marketers of the Company's petroleum and natural gas production. The Company mitigates its credit risk by entering into contracts with established counterparties that have strong credit ratings and reviewing its exposure to individual counterparties on a regular basis. At December 31, 2009, the Company has an allowance for doubtful accounts of $274 (2008 – $nil).

The Company also has credit risk related to its long-term investment in commercial paper as further described in 'Investments' section. There is currently no market quotations for the long term investment and uncertainties exist regarding the values of the assets which underlie the MAV 2 notes.

Liquidity Risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they are due. The nature of the oil and gas industry is capital intensive and the Company maintains and monitors a certain level of cash flow to finance operating and capital expenditures. The Company believes it has sufficient credit facilities to satisfy its financial obligations as they come due and does not expect there will be a material adverse impact on its business as a result of the current third party MAV 2 note liquidity issue.

The Company's ongoing liquidity is impacted by various external events and conditions, including commodity price fluctuations and the global economic downturn.

The timing of cash flows relating to financial liabilities as at December 31, 2009 is as follows:

	< 1 Year	1 – 2 Years	2 – 5 Years	Thereafter
Accounts payable and accrued liabilities	23,175	-		-
Long-term debt related to investments	-	-	18,054	-
	23,175	-	18,054	-

Access to Capital Risk

The Company anticipates making substantial capital expenditures for the acquisition, exploration, development and production of oil and natural gas reserves in the future. As the Company's revenues may decline as a result of decreased commodity pricing, it may be required to reduce capital expenditures. In addition, uncertain levels of near term industry activity coupled with the present global credit crisis exposes the Company to additional access to capital risk. There can be no assurance that debt or equity financing, or cash generated by operations will be available or sufficient to meet these requirements or for other corporate purposes or, if debt or equity financing is available, that it will be on terms acceptable to the Company. The inability of the Company to access sufficient capital for its operations could have a material adverse effect on the Company's business financial condition, results of operations and prospects.

Operational Matters

The ownership and operation of oil and natural gas wells, pipelines and facilities involves a number of operating and natural hazards which may result in blowouts, environmental damage and other unexpected or dangerous conditions resulting in damage to the Company's natural gas and oil properties and assets, as well as possible liability to third parties. The Company may become liable for damages arising from such events against which it cannot insure or against which it may elect not to insure because of high premium costs or other reasons. Costs incurred to repair such damage or pay such liabilities will reduce the cash flow of the Company. The Company employs prudent risk management practices and maintains suitable liability insurance.

Environmental Concerns

The oil and natural gas industry is subject to environmental regulation pursuant to local, provincial and federal legislation. A breach of such legislation may result in the imposition of fines or issuance of clean up orders in respect of Cequence or its working interests. Such legislation may be changed to impose higher standards and potentially more costly obligations on Cequence. Furthermore, management believes the federal political parties, appear to favor new programs for environmental laws and regulation, particularly in relation to the reduction of emissions, and there is no assurance that any such programs, laws or regulations, if proposed and enacted, will not contain emission reduction targets which Cequence cannot meet, and financial penalties or charges could be incurred as a result of the failure to meet such targets. In particular there is uncertainty regarding the Federal Government's Regulatory Framework for Air Emissions ("Framework"), as issued under the Canadian Environmental Protection Act.

Regulatory Risk

There can be no assurance that government royalties, income tax laws, environmental laws and regulatory requirements relating to the oil and gas industry will not be changed in a manner which adversely affects the Company or its shareholders. Although the Company has no control over these regulatory risks, it continuously monitors changes in these areas by participating in industry organizations and conferences, exchanging information with third party experts and employing qualified individuals to assess the impact of such changes on the Company's financial and operating results.

Current Economic Conditions

Recent market events and conditions, including disruptions in the international credit markets and other financial systems and the deterioration of global economic conditions, have caused significant volatility to commodity prices. These conditions persisted throughout 2009, causing a loss of confidence in the global credit and financial markets and resulting in the collapse of, and government intervention in, major banks, financial institutions and insurers, and created a climate of greater volatility, less liquidity, widening of credit spreads, a lack of price transparency, increased credit losses and tighter credit conditions. Notwithstanding, various actions by governments, concerns about the general condition of the capital markets, financial instruments, banks, investment banks, insurers and other financial institutions caused the broader credit markets to further deteriorate and stock markets to decline substantially. These factors have negatively impacted company valuations and will impact the performance of the global economy going forward. Petroleum and natural gas prices are expected to remain volatile for the near future as a result of market uncertainties over the supply and demand of these commodities due to the current state of the world economies, OPEC actions and the ongoing global credit and liquidity concerns.

ROYALTY REGIMES

Alberta

On October 25, 2007, the Alberta government announced the New Royalty Framework ("new framework"), which took effect on January 1, 2009. The new framework is based on a new royalty formula for natural gas that operates on a sliding scale determined by commodity prices, well productivity and drilling depth.

On November 19, 2008, the Alberta government announced that in response to the global economic crisis and a slowdown in crude oil and natural gas drilling throughout the province; it has implemented a transitional royalty program in which, companies drilling certain new wells after November 19, 2008, have a one-time option of selecting the transitional royalty program or the new framework. All wells drilled between 2009 and 2013 that adopt the transitional royalty program will be required to shift to the new framework on January 1, 2014. The Company does not anticipate a significant benefit from the TRP in 2009 as the majority of the Company's wells converted to the NRF on January 1, 2009.

On March 3, 2009 the Alberta government made a third announcement regarding royalties which provided incentives for the energy sector in response to the current global economic slowdown. The incentives include a drilling royalty credit for new conventional oil and natural gas wells of up to $200 per meter drilled and a maximum five percent royalty rate for the first year of production from new oil or gas wells brought on production after April 1, 2009. On June 25, 2009, the Alberta government extended these incentives to March 31, 2011. The drilling royalty credit may be reduced depending on the amount of Alberta production on crown lands and how much crown royalties are paid. Cequence is continuing to assess the impact of the incentives and will adjust drilling plans and the timing of bringing wells on production accordingly. As at December 31, 2009, approximately $3,100 in Alberta drilling credits have been earned and recognized as a reduction to capital spending.

On March 11, 2010 the Alberta government announced that the new framework was being modified. The details of the program have yet to be finalized but the government has announced that Alberta crown royalties will be capped at 36 percent for natural gas and 40 percent for oil. In addition, a five percent royalty will apply to the first 50 mboe of production or the first year of production on new oil and gas wells. Final details of the new royalty program are expected to be release in May 2010.

British Columbia

On August 6, 2009 the government of BC announced an oil and gas stimulus package to enhance BC's competitive business climate and encourage continued oil and gas development and exploration. The package is comprised of two parts; a two percent royalty relief program and a change to the deep royalty credit program. The two percent royalty relief program applies to all natural gas wells drilled in a 10 month window (August 31, 2009 to July 1, 2010). The two percent royalty will apply to the first 12 months of production where production must commence before December 31, 2010.

The change to the deep royalty credit program includes an increase of 15 percent to the existing royalty deductions for natural gas deep drilling and the inclusion of horizontal wells drilled between 1,900 and 2,300 metres. The change applies to wells spudded after August 31, 2009.

The two percent royalty relief program and the deep royalty credit program will co-exist but a company will only receive the benefits of one program at a time. The deep royalty credit will apply first. If it is exhausted before 12 months of production, the two percent royalty will be in effect for the remainder of the 12 months. If the deep royalty credit is not exhausted before 12 months, the two percent royalty program will not apply.

Cequence is continuing to review the incentives available in both Alberta and BC and has considered the benefits of each program in its current and future drilling plans.

FORWARD-LOOKING STATEMENTS

Certain statements contained within this MD & A constitute forward-looking statements. These statements related to future events or our future performance. All statements other than statements of historical fact may be forward-looking statements. Forward-looking statements are often, but not always, identified by the use of words such as "seek", "anticipate", "budget", "plan", "continue", "estimate", "expect", "forecast", "may", "will", "project", "predict", "potential", "targeting", "intend", "could", "might", "should", "believe", and similar expressions. Forward-looking statements in this MD & A include, but are not limited to, statements with respect to: the potential impact of implementation of the Alberta and British Columbia Royalty Frameworks on Cequence's condition and projected 2010 capital investments; the Company's ability to realize its investments in MAV 2 Notes; projections with respect to growth of natural gas production; the projected impact of land access and regulatory issues; projections relating to the volatility of crude oil prices in 2010 and beyond and reasons therefore; the Company's projected capital investment levels for 2010 and the source of funding therefore; the effect of the Company's risk management program, including the impact of derivative financial instruments; the Company's defence of lawsuits; the impact of the climate change initiatives on operating costs; the impact of Western Canada pipeline constraints; projections that the Company will fully recover from its MAV 2 Notes. Readers are cautioned not to place undue reliance on forward-looking statements, as there can be no assurance that the plans, intentions or expectations upon which they are based will occur.

By their nature, forward-looking statements involve numerous assumptions, known and unknown risks and uncertainties, both general and specific, that contribute to the possibility that the predictions, forecast, projects and other forward-looking statements will not occur, which may cause the Company's actual performance and financial results in future periods to differ materially from any estimates or projects of future performance or results expressed or implied by such forward-looking statements. These assumptions, risks and uncertainties include, among other things: volatility of and assumptions regarding oil and gas prices; assumptions based upon Cequence's current guidance; fluctuations in currency and interest rates; the Company's ability to realize its investment in MAV 2 Notes; product supply and demand; market competition; risk inherent in the Company's marketing operations, including credit risks; imprecision of reserves estimates and estimates of recoverable quantities of oil, natural gas and liquids from resource plays and other sources not currently classified as proved; the Company's ability to replace and expand oil and gas reserves; the Company's ability to generate sufficient cash flow from operations to meet its current and future obligations; the Company's ability to access external sources of debt and equity capital; the timing and cost of well and pipeline constructions; the Company's ability to secure adequate product transportation; changes in royalty, tax, environmental and other laws or regulations or the interpretations of such laws or regulations; risks associated with existing and potential future lawsuits and regulatory actions made against the Company; and other risks and uncertainties described from time to time in the reports and filings made with securities regulatory authorities by Cequence. Statements relating to "reserves" are deemed to be forward-looking statements, as they involve the implied assessment, based on certain estimates and assumptions that the resources and reserves described can be profitably produced in the future.

Financial outlook information contained in this MD & A about prospective results of operations, financial position or cash flows is based on assumptions about future events, including economic conditions and proposed courses of action, based on management's assessment of the relevant information currently available. Readers are cautioned that such financial outlook information contained in this MD & A should not be used for purposes other than for which it is disclosed herein.

Although Cequence believes that the expectations represented by such forward-looking statements are reasonable, there can be no assurance that such expectation will prove to be correct. Readers are cautioned that the foregoing list of important factors is not exhaustive. Furthermore, the forward-looking statements contained in this MD & A are made as of the date of this MD & A, and except as required by law Cequence does not undertake any obligation to update publicly or to revise any of the included forward-looking statements, whether as a result of new information, future events or otherwise. The forward-looking statements contained in this MD & A are expressly qualified by this cautionary statement.

AUDITORS' REPORT

TO THE SHAREHOLDERS OF CEQUENCE ENERGY LTD.:

We have audited the consolidated balance sheet of Cequence Energy Ltd. (formerly Sabretooth Energy Ltd.) as at December 31, 2009 and the consolidated statements of operations, comprehensive loss and deficit and cash flows for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2009 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

The financial statements as at December 31, 2008 and for the year then ended were audited by other auditors who expressed an opinion without reservation on those financial statements in their report dated March 6, 2009.

Deloitte & Touche LLP

Chartered Accountants

Calgary, Alberta
March 16, 2010

CEQUENCE ENERGY LTD.

(formerly Sabretooth Energy Ltd.)

CONSOLIDATED BALANCE SHEETS

December 31, 2009 and 2008

(Expressed in thousands of Canadian dollars)		2009		2008
ASSETS				
CURRENT				
Cash	$	18,128	$	15,437
Accounts receivable		10,144		7,232
Interest receivable (Note 8)		-		1,218
Deposits and prepaid expenses		913		1,549
Commodity contracts (Note 20)		1,420		3,034
		30,605		28,470
Investments (Note 8)		13,738		13,968
Other derivative financial instrument (Note 11)		182		-
Property and equipment (Note 9)		158,011		115,383
Future income taxes (Note 13)		5,575		6,825
		208,111		164,646
LIABILITIES				
CURRENT				
Demand credit facilities (Note 10)		-		47,970
Accounts payable and accrued liabilities		23,175		10,771
Future income taxes (Note 13)		424		696
		23,599		59,437
Long-term debt related to investments (Note 11)		18,054		-
Loan premium (Note 11)		150		-
Asset retirement obligations (Note 12)		4,059		2,515
Non-controlling interest (Note 7)		-		8,474
		45,862		70,426
CONTINGENCIES AND COMMITMENTS (Notes 18 and 19)				
SHAREHOLDERS' EQUITY				
Share capital (Notes 5 and 14)		267,908		192,849
Warrants (Note 14)		-		598
Contributed surplus (Note 16)		7,818		5,596
Deficit		(113,477)		(104,823)
		162,249		94,220
	$	208,111	$	164,646

The accompanying notes are an integral part of these consolidated financial statements

APPROVED BY THE BOARD

"Donald Archibald"
Donald Archibald, Director

"Doug Dafoe"
Doug Dafoe, Director

CEQUENCE ENERGY LTD.

(formerly Sabretooth Energy Ltd.)

CONSOLIDATED STATEMENTS OF OPERATIONS,COMPREHENSIVE LOSS AND DEFICIT

For the Years Ended December 31, 2009 and 2008

(Expressed in thousands of Canadian dollars except per share amounts)		2009		2008
REVENUE				
Production revenue	$	18,664	$	48,674
Royalties		(3,164)		(5,753)
Realized gain (loss) on derivative financial instruments (Note 20)		9,319		(1,721)
Unrealized gain (loss) on derivative financial instruments (Notes 11 and 20)		(1,632)		2,191
Interest income		131		1
		23,318		43,392
EXPENSES				
Accretion expense (Note 12)		207		212
Depletion, depreciation, and amortization (Note 9)		14,349		20,285
General and administrative (Notes 9 and 18)		4,667		3,962
Interest		1,405		2,543
Operating costs		9,809		12,771
Reorganization expenses (Note 5)		3,295		-
Stock-based compensation (Note 15)		712		918
Transportation		1,575		1,336
Valuation allowance on investment (Note 8)		213		8,052
		36,232		50,079
LOSS BEFORE INCOME TAXES		(12,914)		(6,687)
INCOME TAXES (Note 13)		(4,272)		1,508
LOSS BEFORE NON-CONTROLLING INTEREST		(8,642)		(8,195)
Non-controlling interest		(12)		16
NET LOSS AND COMPREHENSIVE LOSS		(8,654)		(8,179)
DEFICIT, BEGINNING OF YEAR		(104,823)		(96,644)
DEFICIT, END OF YEAR		(113,477)		(104,823)
Loss per share, basic and diluted (Note 17)	$	(0.41)	$	(0.84)

The accompanying notes are an integral part of these consolidated financial statements

CEQUENCE ENERGY LTD.

(formerly Sabretooth Energy Ltd.)

CONSOLIDATED STATEMENTS OF CASH FLOWS

For the Years Ended December 31, 2009 and 2008

(Expressed in thousands of Canadian dollars)	2009	2008
CASH FLOWS RELATED TO THE FOLLOWING ACTIVITIES:		
OPERATING		
Net loss	$ (8,654)	$ (8,179)
Adjustments for non-cash items:		
Depletion, depreciation, and amortization	14,349	20,285
Accretion expense	207	212
Stock-based compensation	712	918
Valuation allowance on investment (Note 8)	213	8,052
Unrealized loss (gain) on derivative financial instruments	1,632	(2,191)
Loan premium amortization (Note 11)	(50)	-
Future income taxes (recovery) (Note 13)	(4,494)	1,508
Non-controlling interest	12	(16)
	3,927	20,589
Asset retirement expenditures (Note 12)	(75)	(816)
Net change in non-cash working capital (Note 21)	9,676	2,373
	13,528	22,146
INVESTING		
Corporate acquisitions (Notes 5 and 7)	(38)	14,437
Property and equipment expenditures, net	(24,836)	(37,429)
Acquisition of assets (Note 6)	(21,757)	-
Proceeds from sale of assets	-	21,262
Principal Repayments of Investments (Note 8)	17	-
Net change in non-cash working capital (Note 21)	1,670	(6,506)
	(44,944)	(8,236)
FINANCING		
Proceeds from bank indebtedness, net	-	1,714
Repayment of demand credit facilities	(47,970)	-
Proceeds from long-term debt related to investments	18,054	-
Issue of common shares (Note 14)	67,340	-
Share issue costs (Note 14)	(3,232)	-
Exercise of options for common shares	-	100
Repurchase of common shares under NCIB (Note 14)	(85)	(183)
Repurchase of stock options	-	(104)
	34,107	1,527
NET INCREASE IN CASH	2,691	15,437
CASH, BEGINNING OF YEAR	15,437	-
CASH, END OF YEAR	18,128	15,437
SUPPLEMENTARY INFORMATION		
Income taxes paid	7	-
Interest paid	$ 1,125	$ 2,543

The accompanying notes are an integral part of these consolidated financial statements

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

Years Ended December 31, 2009 and 2008
(All figures expressed in thousands except per share amounts unless otherwise noted)

1. NATURE OF OPERATIONS

Cequence Energy Ltd. is engaged in the acquisition, exploration, development and production of petroleum and natural gas reserves in Western Canada.

2. BASIS OF PRESENTATION

At the annual and special meeting of Sabretooth Energy Ltd. on July 29, 2009, the shareholders approved transactions to refinance the company, appoint new management, restructure the board of directors and acquire a private oil and gas company. As part of the reorganization the company effected a name change to Cequence Energy Ltd. (the "Company" or "Cequence") and completed a 4:1 share consolidation (the "reorganization transactions"). All share and per share comparative numbers have been restated to reflect the share consolidation. The reorganization transactions are described in more detail in Note 5 below.

These consolidated financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles ("Canadian GAAP"). These statements include all assets, liabilities, revenues and expenses of Cequence and its wholly-owned subsidiary, 1175043 Alberta Ltd. At January 1, 2009, the Company owned approximately 71 percent of HFG Holdings Inc. ("HFG"). As described in Note 7, on November 12, 2009, the Company acquired all of the remaining issued and outstanding shares of HFG. In accordance with Canadian GAAP, the consolidated statements of Cequence include 100 percent of HFG Holdings Inc., with the minority interest reflected as a 'non-controlling interest' on the income statement to the date of acquisition.

3. SIGNIFICANT ACCOUNTING POLICIES

Financial Instruments

A financial instrument is any contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity. Financial assets and financial liabilities are recognized on the consolidated balance sheet at the time the Company becomes a party to the contractual provisions. Upon initial recognition, financial instruments are measured at fair value. Measurement in subsequent periods is dependent on the classification of the financial instrument.

The Company has made the following classifications:

a) Cash and investments are classified as financial assets held for trading and are measured at fair value. Gains and losses from revaluation are recognized in net income.

b) Accounts and interest receivable are classified as loans and receivables and are initially measured at fair value. Subsequent to this they are recorded at amortized cost using the effective interest method.

c) Demand credit facilities, accounts payable and accrued liabilities and long-term debt related to investments are classified as other liabilities and are initially measured at fair value. Subsequent to this they are recorded at amortized cost using the effective interest method.

d) Derivative instruments, including embedded derivative instruments, that do not qualify as hedges, or are not designated as hedges on the balance sheet, including commodity contracts and other derivative financial instruments, are recorded at fair value with changes in fair value recognized in net loss. Commodity contracts are classified as held for trading. Derivative instruments are used by the Company to manage economic exposure to market risks relating to commodity prices. Cequence's policy is not to utilize derivative financial instruments for speculative purposes.

Transaction costs related to financial instruments, derivative financial instruments and embedded derivative financial instruments are expensed as incurred.

Canadian GAAP establishes a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The three levels of the fair value hierarchy are described below:

Level 1: Values based on unadjusted quoted prices in active markets that are accessible at the measurement date for identical assets or liabilities.

Level 2: Values based on quoted prices in markets that are not active or model inputs that are observable either directly or indirectly for substantially the full term of the asset or liability.

Level 3: Values based on prices or valuation techniques that require inputs that are both unobservable and significant to the overall fair value measurement.

When the inputs used to measure fair value fall within different levels of the hierarchy, the level within which the fair value measurement is categorized is based on the lowest level input that is significant to the fair value measure in its entirety.

Property, Plant and Equipment

Cost

The Company follows the full cost method of accounting whereby all costs relating to the acquisition of, the exploration for and development of petroleum and natural gas reserves are initially capitalized and accumulated in cost centers by country. Costs capitalized include land acquisition costs, geological and geophysical expenditures, rentals on undeveloped and non-producing properties, costs of drilling productive and non-productive wells and lease and well equipment.

Gains and losses on disposals of petroleum and natural gas properties are recognized only when crediting the proceeds to the full cost pool would result in a change of 20 percent or more in the depletion and depreciation rate.

Other property and equipment are recorded at cost.

Depletion, depreciation and amortization

Capitalized costs of petroleum and natural gas properties, and related equipment are depleted and depreciated using the unit-of-production method based on the Company's share of gross proved petroleum and natural gas reserves, as determined by independent engineers. For the purpose of this calculation, production and reserves of petroleum and natural gas are converted to a common unit of measurement on the basis of their relative energy content, where six thousand cubic feet of natural gas equates to one barrel of oil.

Costs of acquiring and evaluating unproved properties are excluded from costs subject to depletion and depreciation until it is determined whether proved reserves are attributable to the properties or impairment has occurred.

Other property and equipment are amortized over 3 to 5 years on a straight line basis.

Impairment (ceiling test)

Petroleum and natural gas assets are evaluated in each reporting period to determine that the costs are recoverable and do not exceed the fair value of the properties. The costs are assessed to be recoverable if the sum of the undiscounted cash flows expected from the production of proved reserves and the lower of cost and market of unproved properties exceed the carrying value of all petroleum and natural gas assets. If the carrying value of the petroleum and natural gas assets is not assessed to be recoverable, an impairment loss is recognized to the extent that the carrying value exceeds the sum of the discounted cash flows expected from the production of proved and probable reserves and the lower of cost and market of unproved properties. The cash flows are estimated using future prices and costs and are discounted using a market adjusted interest rate.

Asset Retirement Obligations

The Company recognizes the fair value of a liability for an asset retirement obligation in the period in which it is incurred and records a corresponding increase in the carrying value of the related long-lived asset. Fair value is estimated using the present value of the estimated future cash outflows to abandon the asset at the Company's credit-adjusted risk-free interest rate. The fair value is determined through a review of engineering studies, industry guidelines, and management's estimates on a site-by-site basis. The liability is subsequently adjusted for the passage of time, and is recognized as an accretion expense in the statement of operations. The liability is also adjusted due to revisions in either the timing or the amount of the original estimated cash flows associated with the liability. The increase in the carrying value of the asset is depleted using the unit-of-production method based on estimated gross proved reserves as determined by independent engineers.

Non-Controlling Interest

Non-controlling interest represents the minority shareholders' interest in the carrying values of HFG. When HFG issues its own shares to outside interests, a dilution gain or loss arises as a result of the difference between the Company's share of the proceeds and the carrying value of the underlying equity. As described in note 7, on November 12, 2009, the Company acquired all of the remaining issued and outstanding shares of HFG. As a result, the portion of the net assets of HFG that was fully consolidated but not wholly-owned by Cequence at the date of acquisition was eliminated as part of the purchase equation, while the portion of net income attributable to such non-controlling interest to the date of acquisition is shown separately on the consolidated statement of operations.

Flow-Through Shares

The Company, from time to time, issues flow-through shares to finance a portion of its capital expenditure program. Pursuant to the terms of the flow-through share agreements, the tax deductions associated with the expenditures are renounced to the subscribers. Accordingly, share capital is reduced and a future tax liability is recorded equal to the estimated amount of future income taxes payable by the Company as a result of the renunciations, when the expenditures are renounced with the Canada Revenue Agency.

Per Share Amounts

Basic per share amounts are computed by dividing the net income by the weighted average number of common shares outstanding during the period. Diluted per share amounts are calculated giving effect to the potential dilution that would occur if stock options and warrants were exercised. The treasury stock method is used to determine the dilutive effect of stock options and warrants. The treasury stock method assumes that proceeds received from the exercise of options and warrants for which the exercise price is less than market price plus the unamortized portion of stock-based compensation are used to repurchase common shares at the average market price for the period.

Revenue Recognition

Revenue from the sale of petroleum and natural gas is recognized based on volumes delivered to customers at contractual delivery points and rates. The costs associated with the delivery, including operating and maintenance costs, transportation and production-based royalty expenses are recognized in the same period in which the related revenue is earned and recorded.

Revenue from interest income is recognized when earned.

Joint Venture Accounting

A significant portion of the Company's exploration, development and production activities are conducted jointly with others. These financial statements reflect only the Company's proportionate interest in such activities.

Stock-Based Compensation

The Company has a stock option plan and issues stock options and performance warrants to directors, officers, employees and other service providers. Compensation costs attributable to stock options and performance warrants granted are measured at fair value at the date of grant and are expensed over the vesting period with a corresponding increase in contributed surplus. When stock options and warrants are exercised, the cash proceeds together with the amount previously recorded as contributed surplus is recorded as share capital. The Company incorporates an estimated forfeiture rate for stock options and performance warrants that will not vest, and adjusts for actual forfeitures as they occur.

Income Taxes

Income taxes are accounted for using the liability method of income tax allocation. Under the liability method, income tax assets and liabilities are recorded to recognize future tax inflows and outflows arising from the settlement or recovery of assets and liabilities at their carrying values. Income tax assets are also recognized for the benefits from tax losses and deductions that cannot be identified with particular assets or liabilities. Future income tax assets and liabilities are determined based on the substantively enacted tax laws and rates that are anticipated to apply in the periods of realization with changes in tax rates or tax laws recognized in earnings in the period of substantive enactment. A valuation allowance is recorded to the extent that the tax benefits are not more likely than not to be realized. Corporate tax returns are subject to audit and reassessment by the Canada Revenue Agency. The results of any reassessment will be accounted for in the year in which they are determined.

Measurement Uncertainty

The preparation of financial statements in accordance with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting periods. Such estimates relate primarily to unsettled transactions and events as of the date of the consolidated financial statements. Actual results could differ from these estimates and the differences could be material.

The amounts recorded for depletion, depreciation and amortization of property and equipment, the provision for asset retirement obligations, and the valuation of property and equipment are based on estimates of proved and probable reserves, production rates, future petroleum and natural gas prices, future costs and the remaining lives and period of future benefit of the related assets.

The amount recorded relating to the fair value of investment in commercial paper is based on a variety of estimates as further described in note 8.

Amounts recorded from joint venture partners are based on the Company's interpretation of underlying agreements and may be subject to joint approval. The Company has recorded balances due from its joint venture partners based on costs incurred and its interpretation of allowable expenditures. Any adjustment required as a result of joint venture audits are recorded in the period of settlement with joint venture partners.

The amounts recorded for future income tax assets and future tax expense (recovery) are based on estimates of the probability of the Company utilizing certain tax pools and assets which, in turn, is dependent on estimates of proved and probable reserves, production rates, future petroleum and natural gas prices, and changes in legislation, tax rates and interpretations by taxation authorities.

The fair value of commodity contracts and the resultant unrealized gain (loss) on commodity contracts is based on estimates of future natural gas prices.

4. CHANGES IN ACCOUNTING POLICIES AND PRACTICES AND FUTURE ACCOUNTING PRONOUNCEMENTS

Goodwill and Intangible Assets

Effective January 1, 2009, the Company adopted the Canadian Institute of Chartered Accountants ("CICA") Section 3064, "Goodwill and Intangible Assets", which has replaced previous Handbook Sections 3062, "Goodwill and Other Intangible Assets" and 3450, "Research and Development Costs". This new guidance reinforces a principles-based approach to the recognition of costs as assets in accordance with the definition of an asset and the criteria for asset recognition under Handbook Section 1000, "Financial Statement Concepts". Under this new guidance, fewer items meet the criteria for capitalization. The implementation of this section had no impact on the Company's consolidated financial statements.

Credit Risk and the Fair Value of Financial Assets and Financial Liabilities

Effective January 20, 2009, the Company adopted the Emerging Issues Committee ("EIC") Abstract 173, "Credit Risk and the Fair Value of Financial Assets and Financial Liabilities" which provides further information on the determination of the fair value of financial assets and financial liabilities under Section 3855, "Financial Instruments - Recognition and Measurement". EIC 173 is to be applied retrospectively without restatement of prior periods to all financial assets and liabilities measured at fair value in interim and annual financial statements for periods ending on or after the date of issuance of this abstract. The implementation of this section resulted in no change to the Company's consolidated financial statements.

Financial Instrument Disclosures

In June 2009, the CICA issued amendments to CICA Handbook Section 3862, "Financial Instruments — Disclosures". The amendments include enhanced disclosures related to the fair value of financial instruments and the liquidity risk associated with financial instruments. The amendments are effective for annual financial statements for fiscal years ending after September 30, 2009. The Company has included these incremental disclosures in its annual consolidated financial statements for the year ended December 31, 2009 at note 20.

Future Accounting Pronouncements

In addition, the Company has assessed new and revised accounting pronouncements that have been issued that are not yet effective and determined that the following may have an impact on the Company:

i) Business Combinations, Consolidated Financial Statements and Non-controlling Interests

In January 2009, the CICA issued Sections 1582, "Business Combinations", 1601, "Consolidated Financial Statements", and 1602, "Non-controlling Interests" which replace CICA Handbook Sections 1581, "Business Combinations" and 1600, "Consolidated Financial Statements". Section 1582 establishes standards for the accounting for business combinations that is equivalent to the business combination accounting standard under IFRS. Section 1601 together with Section 1602 establishes standards for the preparation of consolidated financial statements. These Sections apply to interim and annual consolidated financial statements relating to fiscal years beginning on or after January 1, 2011, and should be adopted concurrently. Earlier adoption is permitted. Cequence is currently assessing the impact of these standards.

5. REORGANIZATION TRANSACTIONS

On July 29, 2009, the shareholders of Cequence approved certain reorganization transactions to recapitalize the Company with new equity, appoint new management and restructure the board of directors.

The new management, directors, certain employees and consultants of the Company (as well as a former officer of the Company) purchased 25,500 common shares (6,377 post-consolidation) of the Company at a price of $0.37 per share ($1.48 post-consolidation) for aggregate subscription proceeds of $9,438 (the "Private Placement"). Existing shareholders of the Company were granted rights to acquire a maximum of 27,027 common shares (6,757 post-consolidation) at a price of $0.37 per share ($1.48 post-consolidation) until August 14, 2009. A total of 26,460 rights (6,615 post-consolidation) were exercised for total consideration of $9,790 (the "Rights Offering").

The Company also acquired all of the issued and outstanding shares of a private oil and gas company owned by certain members of the new management team, in exchange for the issuance of an aggregate of approximately 1,519 common shares (380 post-consolidation) of the Company at a price of $0.37 per share ($1.48 post-consolidation) for total consideration of $562, which approximated the fair value of the assets and liabilities acquired. The purchase price was allocated to cash and working capital of $335, property and equipment of $321 and future income tax liability of $94. The private oil and gas company has a CEE flow through share commitment of $400 that was spent, as required, prior to the end of 2009. The $0.37 price per share ($1.48 post-consolidation) was determined based on the approximate trading price of the Company at the time the Private Placement was agreed.

On May 27, 2009, the Company entered into an agreement to sell, on a private placement basis, 53,592 subscription receipts (13,398 post-consolidation) at a price of $0.86 per subscription receipt ($3.44 post-consolidation) for total proceeds of $46,087. The subscription receipts were convertible to Cequence common shares without further consideration upon shareholder approval of the reorganization transactions and regulatory approval. Upon closing of the reorganization transactions, the Company's subscription receipts previously issued on June 18, 2009 were converted, for no additional consideration and without further action, into common shares of the Company. Holders of the subscription receipts received one common share of the Company for each subscription receipt held.

75 percent of the shares issued to the new management and directors of the Company through the private placement and acquisition of the private oil and gas company have been deposited into escrow with one-third of the escrowed shares being released on each of the first, second and third anniversaries of the closing of the reorganization transactions on July 30, 2009.

As part of the completion of the transactions, the new management and certain directors were issued 20,800 performance warrants (5,200 post-consolidation) which are convertible into non-voting shares of the Company. Each performance warrant has an exercise price of $0.47 per non-voting share ($1.88 post-consolidation) and is exercisable upon reaching certain common share trading price thresholds. The performance warrants are considered stock-based compensation as described in Note 15.

Costs of the reorganization of $3,295 relate primarily to legal, investment banking and severance and have been expensed in the year. Share issue costs associated with the private placement, rights offering and subscription receipts totalled $3,168 and are included in share capital.

6. PROPERTY ACQUISITIONS

Valhalla assets

On November 13, 2009, the Company closed the acquisition of natural gas properties in the Valhalla area of Northwest Alberta. The purchase price, subject to final adjustments, was $6,102. An asset retirement obligation of $36 has been recognized as part of the acquisition.

Peace River assets

On September 24, 2009, the Company closed the acquisition of certain oil and natural gas properties and related facilities in the Peace River Arch area of Northwest Alberta. The purchase price, subject to a final statement of adjustments, was approximately $11,758. An asset retirement obligation of $1,074 has been recognized as part of the acquisition.

Gordondale assets

On August 21, 2009, the Company closed the acquisition of natural gas properties in the Gordondale area of Northwest Alberta. The purchase price, subject to final adjustments, was $3,992. An asset retirement obligation of $55 has been recognized as part of the acquisitions.

The results of operations from these properties have been included in the consolidated financial statements from the closing date of the respective acquisitions. The acquisitions were financed through available cash.

7. CORPORATE ACQUISITIONS

a) Sale of assets to HFG

On December 24, 2008, pursuant to an Agreement of Purchase and Sale, the Company sold 59 net sections of Montney petroleum rights located in Northeastern British Columbia and Northwestern Alberta and a $1,000 tie-in commitment at Red Creek in addition to certain Montney wells and seismic access (the "Assets") in exchange for 156,547 common shares of HFG with a market value of $31,309. In addition, the Company subscribed for 5,000 common shares of HFG at $0.20 per share, for an aggregate subscription price of $1,000.

On December 24, 2008, HFG also raised approximately $15,221 issuing 60,885 common shares on a flow-through basis at $0.25 per share to external parties. The Company's interest in HFG was reduced through the issuance of these additional shares by HFG to third parties.

As a result of the transactions described above, the Company held approximately 71 percent of the outstanding common shares of HFG and effectively disposed of approximately 29 percent of the Assets to non-controlling interest shareholders. Accordingly, the sale of Assets and the corresponding sale of shares by HFG is, in substance, a sale of oil and gas properties. No gain or loss has been recorded as crediting the sale proceeds to the full cost pool did not result in a change of 20 percent or more in the depletion rate of the Company.

Prior to the transactions described above, HFG was classified as a Capital Pool Company as defined in Policy 2.4 of the TSX Venture Exchange (the "Exchange"), had no operations or business activities. As a result, HFG did not meet the definition of a business and, therefore, the acquisition of HFG has not been accounted for as a business combination, but as an asset acquisition. The results of HFG are recorded by the Company from December 24, 2008 forward.

b) Purchase of HFG

On November 12, 2009, the Company acquired all of the issued and outstanding shares of HFG not already held by or on behalf of Cequence for consideration of 2,645 common voting shares. The shares were valued based on the average trading price of the Company's stock during the three days before and three days after the announcement date of the transaction. The transaction was accounted for using the purchase method. The elimination of the non-controlling interest through an acquisition at a purchase price greater than HFG's book value in the Company's consolidated financial statements had the effect of increasing property and equipment assets by $3,123, and decreasing future income tax assets by $727. The accounts of the Company include the results of HFG for the year ended December 31, 2009. The non-controlling interest presented on the statement of operations includes the non-controlling interest's share of the operations of HFG to the date of the acquisition.

The estimated purchase price equation is as follows:

Cost of Acquisition

(000s)	
Common shares (2,645 at $3.97)	10,502
Transaction costs	380
Total	**10,882**

Fair Value of the Assets and Liabilities Acquired

(000s)	
Non-controlling interest at date of acquisition	8,486
Property and equipment	3,123
Future income tax assets	(727)
Total	**10,882**

The attributed values of the common shares issued have been excluded from the consolidated statement of cash flows as a non-cash transaction.

8. INVESTMENTS

As at December 31, 2009, the Company held long-term floating rate notes (“MAV 2” notes) with a carrying value of $13,738 (December 31, 2008 - $13,968). The MAV 2 notes are a result of the restructuring of the Company’s holdings of asset-backed commercial paper (“ABCP") that matured during the third quarter of 2007 but, as a result of the liquidity issues in the ABCP market, did not settle on maturity. The ABCP had an original cost of $24,147 and an interest rate of 4.52 percent. At the dates the Company acquired these investments, they were rated R1 (High) and backed by R1 (High) rated assets and liquidity agreements.

On January 21, 2009, the Pan-Canadian Investors Committee announced that the restructuring had been completed to extend the maturity of the ABCP to provide for a maturity similar to that of the underlying assets. The transactions of the ABCP conduits supported solely by leveraged collateralized debt and a combination of synthetic and traditional securitized assets, have been pooled into the Master Asset Vehicles "MAV" 1 and 2, which are class A1 and class A2 senior long-term notes that will bear interest at floating rates and class B and C subordinated long-term notes that will also bear interest at floating rates.

As a result of the restructuring, the Company received MAV 2 notes, including senior notes (Class A1 and A2) and subordinated Class B and C notes, which have not been rated by DBRS Limited. MAV 2 notes means that the Company will not finance margin calls, but will receive a reduced coupon. The Class A1 and A2 notes will pay interest and Class B and C notes will accrue interest with payments to be made only after the Class A1 and A2 notes have been fully repaid.

The following are the face value of the new notes received from the restructuring at December 31, 2009:

MAV2	Class A1	$	6,700
MAV2	Class A2		14,149
MAV2	Class B		2,568
MAV2	Class C		725
		$	24,142

As at January 21, 2009, the carrying value of the previous notes was removed from the consolidated balance sheet and replaced with the new notes at fair value. No gain or loss on exchange was recognized because the total fair value of the MAV 2 notes and the expected interest payments net of restructuring costs was equal to the carrying value of the ABCP investments at January 21, 2009.

For the year ended December 31, 2009, the Company received $1,305 of interest on the ABCP related to the previous year of which $1,218 is presented on the consolidated balance sheet as at December 31, 2008 as interest receivable. The balance was recognized in income in 2009. Interest for the period January 22, 2009 to December 31, 2009 has not been accrued as a result of low current interest rates and was considered nominal.

The valuation technique used by the Company to estimate the fair value of its investment in MAV 2 notes at December 31, 2009 and ABCP at December 31, 2008, incorporates probability-weighted discounted cash flows considering the best available public information regarding market conditions and other factors that a market participant would consider for such investments. Discount rates used in the valuation at December 31, 2009 were 7.12 percent for Class A1 notes, 10.57 percent for Class A2 notes, 26.09 percent for Class B notes and 31.84 percent for subordinated notes (8.4 and 14.4 percent were used at December 31, 2008 for the senior and subordinated notes respectively). Due to current bankers’ acceptance rates, the MAV 2 notes are not currently paying interest. As a result, a zero coupon rate has been assumed on the B and C notes for the entire term and on the A1 and B1 notes for the first three quarters of 2010.

Discount rates have been estimated using benchmark bond rates plus expected credit spread premiums for lack of liquidity, uncertainty for future payments, lack of transparency and the nature of the underlying assets.

Assumptions have been made as to the long-term interest rates to be received from the long-term floating rate notes. The remaining term of the notes is estimated to be approximately seven years which approximates the maturity of the assets backing the notes.

Interest on Class A1 notes is to be accrued and paid currently, with interest on all other Classes to be accrued, but only paid after interest on higher ranking Classes is paid. The probability weighted discounted cash flows resulted in an estimated fair value of the Company's MAV 2 notes of $13,738 (December 31, 2008 - $13,968), a cumulative reduction of $10,404 to the original cost of the ABCP. As the estimated fair value was reduced during the year, $213 was charged to income (December 31, 2008 - $8,052 – net of gain on interest accrued of $1,218).

A summary of changes to the carrying value is as follows:

	December 31, 2009	December 31, 2008
Opening balance	$ 13,968	$ 23,238
Principal repayments	(17)	-
Writedown of investments[1]	(213)	(9,270)
Ending balance	$ 13,738	$ 13,968

(1) Amount is gross of interest accrued at December 31, 2008 of $1,218.

There are currently no market quotations available for the ABCP or the new MAV 2 notes and uncertainties exist regarding the value of the assets which underlie the MAV 2 notes, the amount and timing of cash flows, the evolution of the liquidity of the market for the new notes issued following the restructuring and the evolution of the prevailing economy could give rise to a further change in the value of the Company's investment in the MAV 2 notes. It is reasonably possible that changes in future conditions in the near term could require a material change in the recognized amount. A 1.0 percent increase in the discount rate will decrease the fair value of the MAV 2 notes by approximately $830 before tax.

9. PROPERTY AND EQUIPMENT

	December 31, 2009	December 31, 2008
Petroleum and natural gas properties	224,525	167,547
Accumulated depletion, depreciation and amortization	(66,514)	(52,164)
	158,011	115,383

Unproved properties and seismic not subject to depletion amounted to approximately $17,653 at December 31, 2009 (2008 - $26,421).

The Company capitalized general and administrative costs related to exploration and development of approximately $1,441 for the year ended December 31, 2009 (2008 - $1,874).

Costs subject to depletion include $30,169 of estimated future capital costs (2008 - $16,168).

The benchmark escalated prices on which the December 31, 2009 ceiling test is based, are as follows:

	Natural Gas AECO Spot ($/mmbtu)	**Condensate** Edmonton Pentanes Plus ($/bbl))	**Crude Oil** Edmonton Par ($/bbl)
2010	5.96	84.93	83.26
2011	6.79	88.15	86.42
2012	6.89	91.37	89.58
2013	6.95	94.59	92.74
2014	7.05	97.82	95.90
2015	7.16	99.79	97.84
2016	7.42	101.81	99.81
2017	7.95	103.86	101.83
2018	8.52	105.96	103.88
2019	8.69	108.10	105.98

Prices increase at a rate of approximately 2.0 percent per year for natural gas, condensate and crude oil after 2019. Adjustments were made to the benchmark prices, for purposes of the ceiling test, to reflect varied delivery points and quality differentials in the products delivered. There was no impairment as at December 31, 2009.

10. DEMAND CREDIT FACILITIES

The Company has established two credit facilities with a Canadian chartered bank. Credit facility A is a $40,000 revolving operating demand loan by way of prime rate based loans, Banker's Acceptances and letters of credit/guarantee, which bears interest at the bank prime rate plus 0.25 percent to 2.5 percent on a sliding scale, depending on the Company's debt to cash flow ratio (ranging from being less than 1.0:1.0 to greater than or equal to 3:1). Credit facility B is a $5,000 non-revolving acquisition/development demand loan, which bears interest at the bank prime rate plus 0.75 percent to 3.0 percent on the same sliding scale as facility A. Both credit facilities are subject to periodic review by the bank and are secured by a general assignment of book debts and a $165,000 demand debenture with a first floating charge over all assets of the Company. The Company is required to meet certain financial based covenants under the terms of this facility. The Company is also permitted to hedge up to 70 percent of its production under the lending agreement. As at December 31, 2009, the Company has not drawn amounts under either facility and is in compliance with all covenants. The effective interest rate for the year ended December 31, 2009 was 2.45 percent (2008 – 4.05 percent). The next scheduled review is to take place in March 2010.

11. LONG-TERM DEBT RELATED TO INVESTMENTS

On March 31, 2009, the Company's bank provided the Company with an additional credit facility to provide liquidity in respect to the MAV 2 notes (Note 8). The credit facility is structured as follows:

Tranche A: $10,854 revolving credit facility, which represents an amount equal to approximately 45 percent of the face value of the restructuring notes.

Tranche B: $7,200 revolving credit facility, which represents an amount equal to approximately 30 percent of the face value of the restructuring notes.

The borrowings under the credit facility are first allocated to Tranche A and the balance allocated to Tranche B. The maturity date is March 30, 2012 with an option to extend the term to seven years on a year by year basis if agreed to by both parties. Interest is payable on prime rate loans at the bank prime rate less 1.0 percent or by Bankers Acceptance at discounted Bankers' Acceptance rates plus a stamping fee of 0.65 percent. The credit facility is secured by the MAV 2 notes as well as a hypothecation/pledge of the notes and all cash proceeds the Company receives on the sale of MAV 2 notes will reduce the available amount of the facility commencing with Tranche A. The Company is required to meet certain financial based covenants under the terms of this facility. As at December 31, 2009, the Company is in compliance with all covenants. The effective interest rate for the year ended December 31, 2009 was 1.13 percent. Interest expense on long-term debt related to investments included as interest expense in the consolidated statement of operations for the year ended December 31, 2009 was $153 (2008 - $nil).

Under the terms of the credit facility and subject to certain conditions, the Company has the option to repay the outstanding loan amount under Tranche A at the maturity date in exchange for the MAV 2 notes. This option is considered an embedded derivative, classified as held for trading, and is recorded at fair value using a Black-Scholes valuation model using current market rate assumptions, a discount rate reflective of the credit profile of the financial institution and the fair value of the underlying MAV 2 notes as at December 31, 2009. At inception the asset had a fair value of $200 and was recorded as a derivative financial instrument asset with an offsetting loan premium liability. At December 31, 2009, this option has a fair value of $182. For the year ended December 31, 2009 the unrealized loss recognized was $18 on the revaluation of the derivative instrument and the interest recovery was $50 on the amortization of the loan premium. A variation of 1.0 percent in the discount rate would impact the option fair value by approximately $32 before tax.

12. ASSET RETIREMENT OBLIGATIONS

The following table summarizes the changes in asset retirement obligations for the years ended December 31, 2009 and 2008:

	December 31, 2009	December 31, 2008
Balance - beginning of year	2,515	4,560
Property acquisitions (Note 6)	1,165	-
Property disposition	-	(1,729)
Accretion expense	207	212
Liabilities incurred	190	278
Abandonment cost incurred	(75)	(816)
Revision in estimated cash flows	57	10
Balance - end of year	4,059	2,515

The total estimated, undiscounted cash flows, inflated at 2 percent, required to settle the obligations are $13,648 (2008 - $7,694) which have been discounted using a weighted average credit-adjusted risk-free interest rate of 7.47 percent (2008 – 6.25 percent). The Company expects these obligations to be settled in approximately 2 to 19 years. As at December 31, 2009, no funds have been set aside to settle these obligations.

13. INCOME TAXES

a) The following table sets forth the components of the Company's future income tax asset at December 31, 2009 and 2008:

	2009	2008
Excess of net book value of property and equipment and assets retirement obligations over related tax pools	(14,856)	(6,953)
Unrealized gain on financial instrument	(424)	(819)
Non-capital loss carry-forwards	10,226	2,903
Scientific research and development expenses and investment tax credits	8,943	9,036
Other tax assets	1,262	1,962
Total net tax assets	5,151	6,129
Current future income tax liability	(424)	(696)
Non-current future income tax asset	5,575	6,825

At December 31, 2009, Cequence has total tax pools of $166,207.

b) Income tax expense differs from that which would be expected from applying the effective Canadian federal and provincial tax rates of 29 percent (2008 – 29.5 percent) to loss before income taxes as follows:

	Year ended December 31, 2009	Year ended December 31, 2008
Expected income tax recovery	(3,753)	(1,973)
Effect of valuation allowance on investment in commercial paper, net of interest	62	2,735
Effect of stock-based compensation	207	271
Change in value of reserves and losses due to reassessments	(1,368)	375
Change in effective tax rate applied	269	(13)
Other	89	113
Future income tax expense (recovery)	(4,494)	1,508
Current income tax expense	222	-
Income tax expense (recovery)	(4,272)	1,508

c) The Company has non-capital loss carry-forwards, investment tax credit carry-forwards and Scientific Research and Experimental Development expenses available to reduce future years' income for tax purposes. The Scientific Research and Development expenses of approximately $22,704 available for carry-forward do not expire. The non-capital loss and investment tax credit carry-forwards expire as follows:

Year of Expiry	Non-capital losses $	Investment tax credits $
2010	-	930
2011	-	1,280
2012	-	672
2013	6,812	761
2014	2,791	338
2015+	22,615	-
	32,218	3,981

14. SHARE CAPITAL

Cequence has an unlimited number of common voting shares and common non-voting shares.

Issued common voting shares	2009		2008	
	Number (000s)	Stated Value $	Number (000s)	Stated Value $
Balance, beginning of year	9,665	192,849	9,767	196,263
Exercise of options	-	-	12	115
Repurchase of shares	(50)	(997)	(114)	(2,260)
Private placement	6,377	9,438	-	-
Corporate acquisition	380	562	-	-
Subscription receipts	13,398	46,087	-	-
Rights offering	6,615	9,790	-	-
Issue of flow-through shares	500	2,025	-	-
Corporate acquisition	2,645	10,502	-	-
	39,530	270,256	9,665	194,118
Share issue costs, net of taxes of $884 (2008 - $611)	-	(2,348)	-	(1,269)
Balance, end of year	39,530	267,908	9,665	192,849

On August 21, 2009 Cequence completed a four for one share consolidation. All share and per share amounts have been adjusted retroactively for the consolidation.

On October 28, 2008, the Company repurchased 114 common shares of the Company under a Normal Course Issuer Bid ("NCIB") for $183. The stated value of the shares was debited to share capital, with the excess of stated value over the cost of the re-acquisition of $2,077 credited to contributed surplus.

Pursuant to a flow-through share offering by HFG on December 24, 2008 (see Note 7), the Company is committed to incur a total of $15,221 in CEE qualifying expenditures by December 31, 2009. As at December 31, 2009, the Company had incurred all of the qualifying expenditures.

On January 1, 2009, the Company had 263 warrants outstanding that entitled the holder to acquire one common share on a CDE "flow-through" basis under the Income Tax Act (Canada) at a price of $15.24 per share. The warrants expired on March 31, 2009 unexercised, with the deemed value of $598 credited to contributed surplus.

On January 7, 2009, the Company repurchased 50 common shares of the Company under a NCIB for $85. The stated value of the shares was debited to share capital, with the excess of stated value over the cost of the re-acquisition of $912 credited to contributed surplus.

On May 27, 2009, the Company entered into an agreement to sell on a private placement basis 53,592 subscription receipts (13,398 post-consolidation) at a price of $0.86 per subscription receipt ($3.44 post-consolidation) for total proceeds of $46,087. The subscription receipts were convertible to Cequence common shares without further consideration upon shareholder approval of the reorganization transactions and regulatory approval. Upon closing of the Transactions, the Company's subscription receipts previously issued on June 18, 2009 were converted, for no additional consideration and without further action, into common shares of the Company. Holders of the subscription receipts received one common share of the Company for each subscription receipt held.

On July 30, 2009, the shareholders of the Company approved reorganization transactions that included the issuance of 25,500 common shares (6,377 post-consolidation) to new employees, directors and officers of Cequence for total consideration of $9,438. Also, shareholders approved the issuance of 1,519 common shares (380 post-consolidation) for total consideration of $562 to purchase a private oil and gas company owned by certain officers of Cequence.

As part of the reorganization, existing shareholders of the Company were offered rights to purchase common shares of Cequence for a price of $0.37 per share ($1.48 post-consolidation) up to a maximum of 27,027 common shares (6,757 post-consolidation). The rights offering expired on August 14, 2009 and a total of 26,460 common shares (6,615 post-consolidation) were issued for total consideration of $9,790.

On October 26, 2009, the Company issued 500 common shares on a CDE "flow-through" basis for total proceeds of $2,025. Under the terms of the agreement, Cequence is required to renounce $2,025 of CDE expenditures in February 2010. As at December 31, 2009 the Company had incurred all of the qualifying expenditures.

On November 12, 2009, the Company completed the acquisition of HFG (note 7 (b)) and issued 2,645 common voting shares with a deemed value of $3.97 per share for total deemed proceeds of $10,502.

As at December 31, 2009, there were no issued or outstanding non-voting shares (December 31, 2008 – none).

15. STOCK BASED COMPENSATION PLANS

Stock options

The Company has a stock option plan for directors, officers, employees and consultants of the Company and its subsidiaries. The number of common shares granted with respect to options may not exceed a rolling maximum of 10 percent of the Company's outstanding common shares. Options typically vest over a four year period and expire five years from the date of grant. During the year, 850 options were forfeited due mainly to the reorganization of the Company.

On August 16, 2009 the Company issued 900 stock options at a price of $4.32 to employees and directors. The options have a five year life and 25 percent vest annually commencing in one year following the grant date. The Company utilized a Black-Scholes option pricing model to price the options.

In the first quarter of 2008, 57 vested options were repurchased for approximately $104. The amount paid to repurchase the options was charged to contributed surplus.

A summary of the inputs used to value stock options is as follows:

	December 31, 2009 $	December 31, 2008 $
Risk-free interest rate	2.7%	3.03 to 3.76%
Expected life of options	5 years	4 years
Expected volatility	50%	52%
Expected dividend rate	0%	0%
Expected forfeiture rate	14%	0%
Weighted average fair value	$2.00	$1.05

The forfeiture rate has been adjusted to 14 percent in light of actual forfeitures during the fourth quarter of 2009. The Company expenses options using the graded vesting method.

A summary of the status of the Company's stock option plan and changes during the year ended December 31, 2009 is as follows:

	December 31, 2009		December 31, 2008	
	Number of Options (000s)	Weighted Average Exercise Price, $	Number of Options (000s)	Weighted Average Exercise Price, $
Outstanding, beginning of year	789	8.56	773	8.64
Granted	900	4.32	173	9.56
Exercised	-	-	(12)	8.24
Repurchased	-	-	(57)	8.96
Forfeited	(850)	8.19	(88)	11.20
Cancelled	-	-	-	-
Outstanding, end of year	839	4.40	789	8.56

The following table summarizes information about stock options outstanding at December 31, 2009:

	Options Outstanding			Options Exercisable	
Range of Exercise Price $	Weighted Average Exercise Price $	Number of Options Outstanding (000s)	Weighted Average Contractual Life Remaining (years)	Number of Options (000s)	Weighted Average Exercise Price $
4.32	4.32	825	4.7	0	0
8.36-10.68	8.93	14	8.0	6	8.71
	4.40	839	4.72	6	8.71

During the year ended December 31, 2009, $192 (2008 - $918) in compensation expense related to stock options has been recognized in the consolidated statement of operations.

Performance warrants

As part of the reorganization, certain officers and directors of the Company were awarded a total of 20,800 (5,200 post-consolidation) performance warrants that are exercisable into a common share of Cequence at a price of $0.47 ($1.88 post-consolidation). At the time the performance warrants were negotiated the market price of the Company's shares was $0.37 ($1.48 post-consolidation). The performance warrants are divided into three equal tranches with the first one-third having a four year term and vest once the 20 day weighted average share price of Cequence exceeds $3.20. The second tranche has a 54 month term and vests if the 20 day weighted average share price of Cequence exceeds $4.40. The final third of the performance warrants have a five year term and vest if the 20 day weighted average share price of Cequence exceeds $5.60. The performance warrants are convertible to non-voting shares of Cequence.

As of December 31, 2009, the first two performance criteria had been met and the Company has recognized the full compensation expense related to the first two tranches of the performance warrants. The Company recognized $520 of stock based compensation for the performance warrants in the year ended December 31, 2009.

The Company utilized a Black-Scholes option pricing model to price the warrants. A fair value of $0.12 per warrant was determined using an expected volatility of 40 percent, an average life of 4.5 years, a dividend rate of zero percent and a risk free interest rate of 2.28 percent.

16. CONTRIBUTED SURPLUS

	December 31, 2009		December 31, 2008	
Opening balance	$	5,596	$	2,720
Stock-based compensation expensed (note 15)		712		918
Stock options exercised (note 14)		-		(15)
Share repurchase under NCIB (note 14)		912		2,077
Repurchase of stock options (note 14)		-		(104)
Warrants unexercised (note 14)		598		-
Ending balance	$	7,818	$	5,596

17. LOSS PER SHARE

Net loss per share has been calculated based on the weighted average number of common shares outstanding during the period. The following table reconciles the denominators used for the basic and diluted net loss per share calculations. No stock options or warrants have been included in the calculation of diluted shares outstanding for the year ended December 31, 2009 (2008 – none) as their inclusion would be anti-dilutive.

	2009	2008
Basic weighted average shares	21,085	9,753
Effect of dilutive stock options and warrants	-	-
Diluted weighted average shares	21,085	9,753

18. CONTINGENCIES

The Bear Ridge acquisition that occurred on August 21, 2007 resulted in one dissenting shareholder. The shareholder holds 449 Bear Ridge shares and 389 Bear Ridge warrants with a strike price of $1.41. The value ascribed to the above of $919 was included in the purchase price at the date of acquisition. Subsequent to December 31, 2009, the parties have reached a settlement for total consideration of $1,280. The incremental $361 has been accrued at December 31, 2009 and is included as general and administration expenses for the year then ended.

During the year ended December 31, 2008, the Company received a Statement of Claim and Notice from a service provider of the Company for damages of $1,039. Subsequent to December 31, 2009, a settlement was reached for $200 in damages, which has been accrued at December 31, 2009, and is included as general and administration expenses for the year then ended. In addition, Cequence is committed to use the services of the Claimant, at fair market value, in the amount of $3,000 over the two years following the date of settlement.

19. COMMITMENTS

	2010	2011	2012	2013	2014+	Total
Office lease	325	363	144	-	-	832
Pipeline transportation	1,592	1,592	1,592	1,592	3,050	9,418
Drilling services	1,500	1,500	-	-	-	3,000
Total	3,417	3,455	1,736	1,592	3,050	13,250

The Company acquired a pipeline transportation contract in a property acquisition that expires on November 30, 2015.

As discussed in Note 18, the Company has a commitment to use the services of the Claimant at fair market value, in the amount of $3,000 over the two years following the date of settlement. Cequence is obligated to spend a minimum of $1,500 in each of the two years following the date of settlement to avoid any penalties under the commitment.

20. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

The Company's financial instruments, including derivative financial instruments and embedded derivative financial instruments, recognized in the consolidated balance sheet consist of cash, accounts and interest receivable, commodity contracts, investments, other derivative financial instruments, demand credit facilities, accounts payable and accrued liabilities and long-term debt related to investments.

The Company's cash, accounts and interest receivable, demand credit facilities, accounts payable and accrued liabilities and long-term debt related to investments approximate their carrying values due to their short terms to maturity and the floating interest rate on the Company's debt.

The following table presents the Company's fair value hierarchy for those assets and liabilities measured at fair value as of December 31, 2009:

	Level 1	Level 2	Level 3	Total
Cash	18,128	-	-	18,128
Commodity contracts	-	1,420	-	1,420
Investment in MAV 2 Notes	-	-	13,738	13,738
Other derivative financial instruments	-	-	182	182
	18,128	1,420	13,920	33,468

The fair value of derivative contracts is determined by discounting the difference between the contracted price and published forward price curves as at the balance sheet date, using the remaining contracted petroleum and natural gas volumes.

The fair value of the Company's investment in MAV 2 notes, as disclosed in note 8, is determined by probability-weighted discounted cash flows considering the best available public information regarding market conditions and other factors that a market participant would consider for such investments.

The fair value of other derivative financial instruments, as disclosed in Note 11, is determined using a Black-Scholes valuation model and the fair value of the underlying MAV 2 notes as at December 31, 2009.

The nature of these financial instruments and the Company's operations expose the Company to market risk, credit risk and liquidity risk. The Company manages its exposure to these risks by operating in a manner that minimizes these risks. Senior management employs risk management strategies and policies to ensure that any exposure to risk is in compliance with the Company's business objectives and risk tolerance levels. The Board of Directors has overall responsibility for the establishment and oversight of the Company's risk management framework. The Board has established policies in setting risk limits and controls and monitors these risks in relation to market conditions.

a) Market risk

Market risk is the risk that changes in market prices, such as foreign exchange rates, commodity prices, and interest rates will affect the Company's net earnings, to the extent the Company has outstanding financial instruments. These risks are generally outside the control of the Company. The objective of the Company is to mitigate market risk exposures within acceptable limits, while maximizing returns.

Commodity price risk

The nature of the Company's operations results in exposure to fluctuations in commodity prices. Management continuously monitors commodity prices and initiates instruments to manage exposure to these risks when it deems appropriate. As a means of managing commodity price volatility, the Company enters into various derivative financial instrument agreements and physical contracts. Collars ensure that the commodity prices realized will fall into a contracted range for a contracted sale volume based on the monthly index price. Monthly gains and losses are determined based on the differential between the AECO daily index and the AECO monthly index when the monthly index price falls in between the floor and the ceiling. Derivative financial instruments are marked-to-market and are recorded on the consolidated balance sheet as either an asset or liability with the change in fair value recognized in net earnings.

The following information presents all outstanding positions for commodity derivative financial instruments at December 31, 2009.

	Volume	Price	Basis
January 1, 2010 to March 31, 2010	6,000 GJ/day	$7.85	AECO

For the year ended December 31, 2009, realized gains from commodity derivative contracts recognized in income were $9,319 compared to a loss of $1,721 in the prior year.

The fair value of the commodity contracts outstanding at December 31, 2009 was an asset of $1,420 (2008 - $3,034). For the year ended December 31, 2009, the Company recorded an unrealized loss of $1,614 from derivative commodity contracts compared to a gain of $2,191 in the prior year. An estimate of credit risk has been made in the valuation of all derivative commodity contracts.

As at December 31, 2009, an increase in gas price of $0.50/gj results in a decrease in the fair value of the commodity contract of $267 ($190 after tax) and a commensurate increase to net loss.

Foreign exchange risk

The Company is exposed to foreign currency fluctuations as crude oil and natural gas prices are referenced to U.S. dollar denominated prices. As at December 31, 2009 the Company had no forward, foreign exchange contracts in place, nor any significant working capital items denominated in foreign currencies.

Interest rate risk

The Company is exposed to interest rate risk to the extent that changes in market interest rates impact its borrowings under the floating rate credit facilities. The floating rate debt is subject to interest rate cash flow risk, as the required cash flows to service the debt will fluctuate as a result of changes in market rates. The Company has no interest rate swaps or financial contracts in place as at or during the year ended December 31, 2009.

As at December 31, 2009, a 1.0 percent change in interest rates on the Company's outstanding debt, with all other variables constant, would result in a change in net loss of $181 ($129 after tax).

b) Credit risk

Credit risk is the risk of financial loss to the Company if a counterparty to a financial instrument fails to meet its contractual obligation. The Company is exposed to credit risk with respect to its accounts receivables, cash and investments.

The majority of the Company's accounts receivable are due from joint venture partners in the oil and gas industry and from marketers of the Company's petroleum and natural gas production. The Company mitigates its credit risk by entering into contracts with established counterparties that have strong credit ratings and reviewing its exposure to individual counterparties on a regular basis.

As at December 31, 2009, the accounts receivable balance was $10,144 of which $964 was past due. The Company considers all amounts greater than 90 days past due. These past due accounts are considered to be collectible, except as provided in the allowance for doubtful accounts. When determining whether past due accounts are uncollectible, the Company factors in the past credit history of the counterparties. At December 31, 2009 the Company has an allowance for doubtful accounts of $274 (2008 – $nil). As at December 31, 2009, 24 percent of the total receivables balance is due from one marketer, and 30 percent is due from the Government of Alberta relating to Alberta drilling incentives.

Cash consists of bank balances. The Company manages the credit exposure of cash by selecting financial institutions with high credit ratings.

The Company has credit risk related to its investments as further described in Note 8. There are currently no market quotations available for MAV 2 notes and uncertainties exist regarding the values of the assets which underlie the MAV 2 notes. The Company has the option to repay a portion of the long-term debt related to investments with the outstanding MAV 2 notes (Note 11).

As at December 31, 2009, the maximum exposure to credit risk was $43,430 (2008 - $40,889) being the carrying value of its cash, accounts receivable, commodity contracts and investments.

c) Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they are due. The nature of the oil and gas industry is capital intensive and the Company maintains and monitors a certain level of cash flow to finance operating and capital expenditures. Refer to Note 22 for disclosure related to the management of capital.

The timing of cash flows relating to financial liabilities as at December 31, 2009 is as follows:

	< 1 Year	1 – 2 Years	2 – 5 Years	Thereafter
Accounts payable and accrued liabilities	23,175	-	-	-
Long-term debt related to investments	-	-	18,054	-
	23,175	-	18,054	-

21. CHANGES IN NON-CASH WORKING CAPITAL

	2009 $	2008 $
Accounts receivable	(1,694)	1,956
Deposits and prepaid expenses	636	371
Accounts payable and accrued liabilities	12,404	(6,460)
Net change in non-cash working capital	11,346	(4,133)
Allocated to:		
Operating activities	9,676	2,373
Investing activities	1,670	(6,506)
	11,346	(4,133)

22. CAPITAL MANAGEMENT

Cequence's objectives are to maintain a flexible capital structure in order to meet its financial obligations and to execute on strategic opportunities throughout the business cycle. The Company's capital comprises shareholders' equity, demand credit facilities and working capital. As described in Note 11, the Company has long-term debt with the specific purpose of providing short-term liquidity in light of the restructuring of the Company's ABCP for MAV 2 notes. As the long-term debt is related specifically to the MAV 2 notes, both the long-term debt and MAV 2 notes are excluded from what Cequence determines to be capital for the purposes of capital management. Cequence manages the capital structure and makes adjustments in light of economic conditions and the risk characteristics of the underlying assets.

In order to maintain or adjust the capital structure, Cequence may issue new common shares, issue new debt or replace existing debt, adjust capital expenditures and acquire or dispose of assets.

The Company evaluates its capital structure based on the non-GAAP measure of net debt to cash flow from operating activities and the current credit available to Cequence compared to its budgeted capital expenditures. At December 31, 2009 Cequence has a positive net consolidated working capital of $7,430 (2008 – 30,271 deficit), including the fair value of the commodity contract.

Net debt to cash flow provides a measure of the Company's ability to manage its debt levels under current operating conditions. The ratio is calculated as net debt, defined as current debt, long term debt excluding the long-term debt related to investments and working capital excluding commodity derivative assets or liabilities, divided by cash flow from operations before asset retirement expenditures and changes in non-cash working capital for the most recent quarter.

It is the Company's objective to maintain a net debt to annualized cash flow ratio of less than 2:1. As at December 31, 2009, the ratio was calculated as 0:1 (2008 – 5.92:1) based on annualized fourth quarter results.

The Company's current borrowing capacity is based on the lenders' semi-annual review of the Company's oil and natural gas reserves. The Company is also subject to various covenants including a minimum adjusted working capital ratio of 1:1, defined as currents assets adjusted for unrealized hedging gains and undrawn availability under the credit facility over current liabilities less current portion of bank debt, under its credit facilities. Compliance with these covenants is monitored on a regular basis and at December 31, 2009 the adjusted working capital was calculated as 2.99:1 (2008 – 6.08:1).

CORPORATE INFORMATION

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Vice President, Finance & CFO

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Nathan MacBey
Vice President, Land

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