Consolidated Financial Statements of

MADALENA VENTURES INC.

As at and for the years ended December 31, 2009 and 2008

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AUDITORS' REPORT TO THE SHAREHOLDERS

We have audited the consolidated balance sheets of Madalena Ventures Inc. as at December 31, 2009 and 2008 and the consolidated statements of operations, comprehensive loss and deficit and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we 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 financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Corporation as at December 31, 2009 and 2008 and the consolidated results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

KPMG LLP

Chartered Accountants
Calgary, Canada
April 21, 2010

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MADALENA VENTURES INC.

Consolidated Balance Sheets

As at December 31	2009	2008
Assets		
Current assets		
Cash and cash equivalents	$ 10,131,040	$ 7,861,868
Accounts receivable	272,010	185,689
Prepaid expenses	70,155	140,399
	10,473,205	8,187,956
Property and equipment (note 4)	17,224,696	13,491,472
Property and equipment related to discontinued operations (note 5)	-	2,195,519
	$ 27,697,901	$ 23,874,947
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities	$ 1,601,212	$ 944,595
Asset retirement obligations related to discontinued operations (note 6)	-	100,088
Asset retirement obligations (note 6)	355,338	256,290
	1,956,550	1,300,973
Shareholders' equity		
Share capital (note 7)	38,345,561	31,491,768
Warrants (note 7)	2,380,678	-
Contributed surplus (note 8)	7,005,506	6,709,251
Deficit	(21,990,394)	(15,627,045)
	25,741,351	22,573,974
	$ 27,697,901	$ 23,874,947

Commitments (note 12) and subsequent event (note 15)

See accompanying notes to the consolidated financial statements

On behalf of the Board:

[signed] “Ray Smith”

Ray Smith
Chairman

[signed] “Michael Lock”

Michael Lock
Director

MADALENA VENTURES INC.

Consolidated Statements of Operations, Comprehensive Loss and Deficit

For the years ended December 31	2009	2008
Revenue		
Interest income	$ 9,412	$ 264,478
Foreign exchange gain/(loss)	(556,300)	1,299,708
	(546,888)	1,564,186
Expenses		
General and administrative	1,964,104	1,946,419
Stock-based compensation	260,860	648,956
Depreciation and accretion	60,371	30,746
Write-down of Tunisia pre-production costs	2,110,666	-
	4,396,001	2,626,121
Loss from continuing operations	(4,942,889)	(1,061,935)
Loss from discontinued operations (note 5)	(1,420,460)	(771,856)
Net loss and other comprehensive loss	(6,363,349)	(1,833,791)
Deficit - beginning of the year	(15,627,045)	(13,793,254)
Deficit - end of the year	$ (21,990,394)	$ (15,627,045)
Loss from continuing operations per share:		
Basic	$ (0.044)	$ (0.010)
Diluted	(0.044)	(0.010)
Loss from discontinued operations per share:		
Basic	$ (0.013)	$ (0.007)
Diluted	(0.013)	(0.007)
Net loss and other comprehensive loss per share:		
Basic	$ (0.057)	$ (0.017)
Diluted	(0.057)	(0.017)

See accompanying notes to the consolidated financial statements

MADALENA VENTURES INC.

Consolidated Statements of Cash Flows

For the years ended December 31	2009	2008
Cash provided by (used in):		
Operating activities		
Loss from continuing operations	$ (4,942,889)	$ (1,061,935)
Items not involving cash:		
Stock-based compensation	260,860	648,956
Depreciation and accretion	60,371	30,746
Write-down of pre-production costs	2,110,666	-
Foreign exchange loss (gain)	3,904	(1,638,433)
	(2,507,088)	(2,020,666)
Change in non-cash working capital items (note 11)	(233,781)	116,890
	(2,740,869)	(1,903,776)
Discontinued operations (note 5)		
Income (loss) from discontinued operations	(1,420,460)	(771,856)
Items not involving cash:		
Depletion included in discontinued operations	1,576,147	1,157,800
Gain on sale of property and equipment	(27,708)	-
Non-cash adjustments to purchase price	14,056	-
Abandonment costs	(2,570)	(20,635)
Additions to discontinued property and equipment	(21,628)	(166,956)
Proceeds on sale of property and equipment	554,000	-
Change in non-cash working capital (note 11)	(6,619)	225,600
	665,218	423,953
Financing activities		
Issue of common shares	10,000,050	2,450,000
Share issue costs	(765,579)	-
Change in non-cash working capital items (note 11)	124,014	-
	9,358,485	2,450,000
Investing activities		
Additions to property and equipment	(5,766,684)	(8,258,998)
Change in non-cash working capital items (note 11)	911,659	434,911
	(4,855,025)	(7,824,087)
Change in cash and cash equivalents	2,427,809	(6,853,910)
Cash and cash equivalents, beginning of the year	7,861,868	13,082,472
Impact of foreign exchange on cash balances	(158,637)	1,633,306
Cash and cash equivalents, end of the year	$ 10,131,040	$ 7,861,868

See accompanying notes to the consolidated financial statements

1. Nature of business and basis of presentation

Madalena Ventures Inc. ("Madalena" or the "Company") is incorporated pursuant to the laws of the Province of Alberta. Madalena is based in Calgary, Alberta and is involved in the exploration, development and production of petroleum and natural gas in Argentina. In August 2009 and March 2010, the Company sold its Canadian and Tunisian oil and gas assets, respectively.

These consolidated financial statements have been prepared on the basis that the Company is a going concern and will realize assets and discharge liabilities in the normal course of operations for the foreseeable future. Presently, Madalena has minimal production and limited cash flow from operating activities. The Company currently relies on equity financing to pay for exploration activities and overhead expenses. Therefore, the Company's ability to continue operations is dependent on identifying commercial oil and gas reserves, generating profitable operations and raising sufficient capital to complete planned exploration and development activities. The outcome of these matters cannot be predicted at this time.

These consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP"), within reasonable limits of materiality and the framework of significant accounting policies described below. Certain comparative information has been reclassified to be consistent with current year presentation. The Company's reporting currency is Canadian dollars ($).

2. Significant accounting policies

Consolidation

These consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries, Madalena Austral S.A., Madalena Ventures International Holding Company Inc. and Madalena Ventures International Inc.

Cash and cash equivalents

Cash and cash equivalents consist of cash deposits and short-term money market investments with an original maturity of less than three months.

Property and equipment

The Company follows the full cost method of accounting for expenditures on petroleum and natural gas properties. All costs associated with the exploration for and the development of oil and gas reserves are capitalized in country-based cost centers. Capitalized costs include drilling costs, lease rentals on non-producing properties, tangible production equipment, asset retirement obligations, and general and administrative expenses directly attributable to exploration and development activities.

Costs accumulated in each cost center together with an estimate of future costs to develop proved reserves are depleted using the unit of production method, based on estimated proved petroleum and natural gas reserves, before royalties. Reserves and production are converted to equivalent units of petroleum based on relative energy content of six thousand cubic feet of natural gas to one barrel of petroleum. Costs of acquiring and evaluating significant unproved petroleum and natural gas interests are excluded from the depletion calculation until it is determined that proved reserves are attributable to such interests, or until impairment occurs.

Cost centers with associated proved reserves are subject to a ceiling test to determine if the net accumulated costs are recoverable. Costs are considered recoverable if the sum of the undiscounted cash flows expected from proved reserves plus the cost, less any impairment, of unproved petroleum and natural gas interests exceeds the carrying amount of the cost centre. If the carrying amount is not recoverable an impairment loss is recognized equal to the excess of the cost center carrying amount over the sum of the discounted cash flows from the production of proved and probable reserves and the cost, less any impairment, of unproved petroleum and natural gas interests. The volumes and cash flows associated with proved and probable reserves are determined by independent engineers, using expected future product prices and costs and discounted using a risk-free interest rate.

Costs centers where planned principal operations have not commenced are considered to be in the pre-production stage whereby costs associated with exploration for and evaluation of oil and gas reserves, net of any preliminary testing revenue, are capitalized but excluded from the calculation of depletion and the ceiling test. Instead, these costs are evaluated at each reporting period to determine if the costs recorded are recoverable. Any costs that are considered unlikely to be recovered are written off.

Proceeds on sale or disposition of oil and gas properties are credited to the applicable cost center unless this results in a change in the depletion and depreciation rate by 20 percent or more, in which case a gain or loss is recognized.

Office furniture, equipment and other assets are recorded at cost less accumulated depreciation. Depreciation is provided over the estimated useful lives of the assets using a 20% declining balance basis for Canadian office furniture and equipment, a straight line basis over 3 - 10 years for Argentine office furniture and equipment, and a straight line basis over the term of the lease for all leasehold improvements.

Asset retirement obligations

The Company recognizes an asset retirement obligation in the period in which a well is drilled and a reasonable estimate of the fair value of the future costs associated with removal, site restoration and asset retirement, can be made. The fair value of the estimated asset retirement obligation is recorded as a long-term liability with a corresponding increase in the carrying amount of the related cost center. These costs are then amortized using the unit of production method and included in depletion, depreciation, and accretion expense. The carrying amount of the liability is increased each reporting period due to the passage of time with the related accretion included in depletion, depreciation and accretion expense. Revisions to the estimated timing of cash flows or to the original estimated undiscounted cost could also result in an increase or decrease to the obligation and charge to Property and Equipment. Actual costs incurred upon settlement of the retirement obligation are charged against the obligation to the extent of the liability recorded. Any difference between the actual costs incurred upon settlement of the asset retirement obligation and the recorded liability is recognized in the Company's earnings in the period in which the settlement occurs.

Future income taxes

The Company uses the asset and liability method of accounting for future income taxes. Under this method, future income tax assets and liabilities are recorded based on the difference between the financial accounting and tax basis of the Company's assets and liabilities, and measured using the substantively enacted tax rates and laws anticipated to apply to the years in which the differences will reverse. The effect of a change in income tax rates on future tax liabilities and assets is recognized in income in the period that the change is substantively enacted. The Company records a future income tax asset only when it is more likely than not to be realized in the future.

Revenue recognition

Petroleum and natural gas revenues are recognized when title and risks pass to the purchaser and payment is reasonably assured.

Stock-based compensation

The Company follows the fair value method of accounting for stock options. The fair value of each option is calculated based on the Black-Scholes option pricing model and is charged to income over the vesting period of the option, with a corresponding increase recorded in contributed surplus. Upon exercise of the stock option, the consideration received plus the amount previously recorded in contributed surplus is recorded as an increase to share capital.

The fair value of stock options issued to non-employees is re-measured at each reporting date until the consultants' performance, or the amortization period is complete (which ever is shorter). Changes to the fair value are amortized over the remaining vesting period of the options.

Per share amounts

Basic per share amounts are computed by dividing period earnings by the weighted average number of common shares outstanding during the period. Diluted amounts are computed using the treasury stock method. Under the treasury stock method, only "in the money" dilutive instruments impact the diluted calculations in computing diluted per share amounts.

Joint interests

Substantially all of the Company's operations are conducted jointly with others, and accordingly, the financial statements reflect only the Company's interest in such activities.

Foreign currency translation

The Company has petroleum exploration and development operations in Tunisia and Argentina. Both locations are considered "integrated foreign operations" for accounting purposes and the financial results of each are translated to Canadian dollars using the temporal method. Under the temporal method, foreign denominated monetary assets and liabilities are translated at the exchange rate prevailing at the period end; non-monetary assets, liabilities and related depletion, depreciation and accretion are translated at historic rates; and revenues and expenses are translated at the rate in effect at the time of the transaction. Foreign exchange gains or losses arising from the translation of these balances are included in net income in the period.

Measurement uncertainty

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses and the disclosure of contingencies. These financial statements include amounts recorded for depletion, depreciation and accretion, asset retirement obligations and future income taxes in addition to assumptions used in the ceiling test calculation and pre-production stage cost center recoverability assessment, which are based on estimates of proven reserves, future production rates, oil and natural gas prices, future costs, and other relevant assumptions. Accruals for revenues and expenses are based on estimates, if actual results are not available, and stock-based compensation amounts are calculated using certain assumptions as more fully described in Note 7. Actual results could differ from the assumptions and estimates used in determining each of these amounts. In addition, the effect on the financial statements of changes in such estimates in future periods could be significant.

Financial instruments

The Company recognizes a financial asset or liability when it becomes a party to the contractual provisions of a financial instrument. Financial assets and financial liabilities are initially measured at fair value. After initial recognition, financial assets and liabilities held for trading are measured at fair value with the unrealized gains and losses recorded in income, loans and receivables are carried at amortized cost, while all other financial liabilities are subsequently measured at amortized cost using the effective interest method. Transaction costs on financial instruments are included in the fair value assessment of each financial asset and financial liability.

3. Recent accounting pronouncements

Goodwill and intangible assets

Effective January 1, 2009, the Company adopted a new Canadian accounting standard for "*Goodwill and Intangible Assets*", clarifying the criteria for the recognition of assets, intangible assets and internally developed intangible assets. The adoption of this standard had no impact on the Company's consolidated financial statements.

Credit risk and the fair value of financial assets and financial liabilities

Effective January 1, 2009, the Company adopted a new Canadian accounting abstract for "Credit Risk and Fair Value of Financial Assets and Financial Liabilities". The abstract provides guidance on the implications of credit risk in determining the fair value of an entity's financial assets and financial liabilities. The guidance clarifies that an entity's own credit risk and the credit risk of counterparties should be taken into account in determining the fair value of financial assets and liabilities, including derivative instruments, for presentation and disclosure purposes. The adoption of this abstract had no impact on the Company's consolidated financial statements.

Business combinations, Non-controlling interests, Consolidated financial statements

Effective January 1, 2011 the Company will be required to adopt the new Canadian accounting standards for "*Business Combinations*", "*Non-controlling Interests*" and "*Consolidated Financial Statements*". All three new standards were issued in contemplation of convergence with International Financial Reporting Standards ("IFRS") as discussed below. The new standards address accounting for business combinations, both at the time of acquisition and subsequent to the initial purchase accounting, and includes guidance on accounting for non-controlling interests and subsequent preparation of consolidated financial statements. The Company has no transactions that are affected by these new standards. Early adoption of the standards is allowed, and will be considered if and when applicable transactions arise.

4. Property and equipment

As at December 31, 2009		Cost		Accumulated depletion and depreciation		Net book value
Argentina pre-production costs	$	13,081,079	$	-	$	13,081,079
Tunisia pre-production costs		6,191,580		(2,110,666)		4,080,914
Furniture and fixtures		167,063		(104,360)		62,703
	$	19,439,722	$	(2,215,026)	$	17,224,696

As at December 31, 2008		Cost		Accumulated depletion and depreciation		Net book value
Argentina pre-production costs	$	7,752,732		-	$	7,752,732
Tunisia pre-production costs		5,645,649		-		5,645,649
Furniture and fixtures		160,398		(67,307)		93,091
	$	13,558,779	$	(67,307)	$	13,491,472

At December 31, 2009 the cost centers for Argentina and Tunisia were considered to be in the pre-production stage and all costs directly attributable to these centers were capitalized and excluded from costs subject to depletion and depreciation. The amounts capitalized for Argentina in 2009 include $491,380 of Value Added Tax (“VAT”) (2008 - $865,143). VAT is payable on goods and services supplied to the Company and is not recoverable from the Government of Argentina, however the Company is allowed to retain VAT on any sales that it collects to the extent of the VAT recorded and paid on previous expenditures.

Revenues and operating expenses realized from the testing of wells in the pre-production stage cost centers is recorded in the full cost pool. During the year ended December 31, 2009, there was $250,042 of net operating costs charged to Argentina pre-production costs and $198,160 of net operating revenue credited to Tunisia pre-production costs. For the year ended December 31, 2008 there was $142,867 of net operating revenue credited to Argentina pre-production costs.

Stock-based compensation totaling $35,395 directly related to exploration and development activities was capitalized in the year ended December 31, 2009 (2008 - $88,370).

In March 2010, the Company sold its interest in the Remada Sud Permit in Tunisia for cash consideration of US$4 million. As a result of the sale and disposal of the Company’s Tunisia cost center, the Company recorded a write-down and reduced the carrying value of the Tunisia cost center at December 31, 2009 by $2,110,666.

At December 31, 2008, a ceiling test calculation was performed to determine if the Canadian cost center carrying values were impaired. In undertaking the ceiling test calculation the Company relied on the net present value of expected future cash flows from proved plus probable reserves discounted at a risk free interest rate and calculated using forecast prices as determined by independent petroleum consultants as of March 31, 2009. As a result of the ceiling test calculations, the Company reduced the carrying value of the Canadian cost center to its expected present value of $2,195,519 at December 31, 2008 and included the resulting write-down totaling $795,000 in 2008 depletion expense.

5. Discontinued operations

On August 27, 2009, the Company completed the sale of all of its Canadian petroleum and natural gas properties for cash proceeds of $554,000 prior to closing adjustments. The sale resulted in the Company's depletion rate changing by more than 20% as a result of the disposal of the Company's entire Canadian cost center. Therefore, Madalena has recorded a gain on sale of the Canadian properties, has reclassified the property and equipment and asset retirement obligations associated with the Canadian properties as separate assets and liabilities on the balance sheet, and has reclassified the net loss from discontinued operations as a separate item on the income statement, including all comparative figures.

The following table provides a summary of the loss from discontinued operations for the years ended December 31, 2009 and 2008.

Loss from discontinued operations for the year ended December 31	2009	2008
Petroleum and natural gas revenues	$ 244,786	$ 764,700
Royalties	(31,322)	(214,568)
Operating costs	(85,485)	(164,188)
Depletion	(1,576,147)	(1,157,800)
Loss from discontinued operations	(1,448,168)	(771,856)
Gain on sale of property and equipment	27,708	-
Loss from discontinued operations	$ (1,420,460)	$ (771,856)

The depletion calculation for Canadian petroleum and natural gas properties for the year ended December 31, 2009 included future development costs of proved reserves of $441,250 (2008 - $441,250).

The following table summarizes the gain on sale of property and equipment used in discontinued operations.

Cash proceeds	$ 554,000
Asset retirement obligations	100,656
Working capital adjustments	14,056
Net book value of property and equipment related to discontinued operations	(641,004)
Gain on sale of property and equipment used in discontinued operations	$ 27,708

6. Asset retirement obligations

Asset retirement obligations result from net ownership interests in petroleum and natural gas assets including well sites, gathering systems and processing facilities. At December 31, 2008, the estimated total undiscounted amount of cash flows required to settle the Company's asset retirement obligations are approximately $1,100,000 USD (2008 – $900,000 USD) in Argentina and $270,000 USD in Tunisia (2008 - $270,000 USD). These costs are expected to be incurred over the next 15 - 25 years in Argentina and 25 years in Tunisia. A credit adjusted risk-free interest rate of 8% and an inflation rate of 7.85% was used to calculate the fair value of the asset retirement obligations in Argentina, and a credit-adjusted risk-free interest rate of 8% and an inflation rate of 4% was used to calculate the fair value of the asset retirement obligations in Tunisia.

A reconciliation of the total asset retirement obligations is provided below:

	2009	2008
Balance, beginning of year	$ 356,378	$ 114,913
Obligations accrued	78,865	256,290
Accretion expense	23,321	5,810
Costs incurred	(2,570)	(20,635)
Reversed on dispositions	(100,656)	-
Balance, end of year	$ 355,338	$ 356,378

7. Share capital

a) Common Shares

Authorized

The authorized share capital of the Company consists of an unlimited number of common shares without nominal or par value.

Issued and outstanding

The following table provides a summary of the issued and outstanding common share activity:

	Common shares	
	Number	Amount
Balance - December 31, 2007	107,368,699	$ 29,041,768
Private placement	4,375,003	2,450,000
Balance - December 31, 2008	111,743,702	31,491,768
Public offering	66,667,000	7,890,040
Share issue costs	-	(1,036,247)
Balance - December 31, 2009	178,410,702	$ 38,345,561

On April 4, 2008 the Company closed a non-brokered private placement for the issuance 4,375,003 common shares at $0.56 per share for total proceeds of $2,450,000, with no associated issue costs.

In December 2009, the Company completed a public offering of 66,667,000 units at an issue price of $0.15 per unit for gross proceeds to Madalena of $10,000,050. Each unit consisted of one common share and one-half (1/2) common share purchase warrant. Each whole warrant issued entitles the holder thereof to purchase one common share at a price of $0.25 per share until December 30, 2010. The Company also issued 3,333,350 agents' warrants. Each agent warrant entitles the holder thereof to purchase one common share at a price of $0.15 per share until December 30, 2010.

b) Warrants

	Warrants Number		Warrants Amount		Average Exercise Price
Balance - December 31, 2007	12,577,625	$	2,900,000	$	0.90
Warrants expired	(12,577,625)		(2,900,000)		(0.90)
Balance - December 31, 2008	-		-		-
Public offering	33,333,500		2,110,010		0.25
Agents' warrants	3,333,350		270,668		0.15
Balance - December 31, 2009	36,666,850	$	2,380,678	$	0.24

The fair value of the warrants at the issue date was estimated using the Black Scholes option pricing model with the following assumptions: Risk free interest rate – 1.46%; expected life – 12 months; expected volatility – 147%; expected dividend yield – nil.

c) Stock options

Under the Company's stock option plan, directors, officers, employees and consultants are eligible to receive options to acquire common stock. The exercise price of each stock option is the average market price of the Company's stock for the five trading days prior to the grant date. Total options granted cannot exceed 10% of the issued and outstanding common shares of the Company.

Options granted to directors vest immediately. Options granted to officers, employees, and consultants vest equally over three years on each anniversary of the grant date. All options expire five years from the grant date.

The following table presents the Company's stock option activity:

	2009			2008		
	Number of options		Weighted average exercise price	Number of options		Weighted average exercise price
Outstanding - beginning of year	11,155,000	$	0.57	10,150,000	$	0.62
Granted	300,000		0.13	1,055,000		0.11
Forfeited	(1,050,000)		0.61	(50,000)		(0.85)
Outstanding - end of year	10,405,000	$	0.55	11,155,000	$	0.57
Exercisable - end of year	9,468,333	$	0.58	7,608,333	$	0.58

The following table presents the estimated remaining life of outstanding stock options and the number of shares that may be issued at December 31, 2009:

	Outstanding		Exercisable
Exercise Price ($)	Number of options	Weighted average remaining life (years)	Number of options
0.105	975,000	3.91	375,000
0.120	1,000,000	0.76	1,000,000
0.125	300,000	4.41	300,000
0.405	30,000	3.08	10,000
0.410	300,000	0.99	300,000
0.600	1,450,000	2.47	1,166,667
0.660	4,300,000	1.15	4,300,000
0.700	100,000	2.80	66,667
0.730	800,000	1.22	800,000
0.850	1,150,000	1.79	1,150,000
	10,405,000	1.78	9,468,333

Stock-based compensation

The Company accounts for its stock-based compensation using the fair value method. The fair value of each stock option granted is estimated using the Black-Scholes option pricing model with the following weighted average assumptions at December 31, 2009: risk free interest rate of 0.92% (2008 – 3.37%), expected life of 3.00 years (2008 – 3.59 years), expected volatility of 171.0% (2008 – 79.6%) and 0% dividend yield (2008 – 0%). The grant date weighted average fair value of stock options granted in the year ended December 31, 2009 was $0.11 per option (granted in 2008 - $0.10 per option). The fair value, estimated at the grant date for options issued to directors, officers and employees and the measurement date for options issued to consultants, is expensed on a straight-line basis over the vesting terms of the options.

d) Per share information

	2009	2008
Basic common shares outstanding as at December 31	178,410,702	111,743,702
Dilutive effect of:		
Share options outstanding	10,405,000	11,155,000
Shares issuable for warrants	33,333,500	-
Shares issuable for agents' warrants	3,333,350	-
Fully diluted common shares outstanding	225,482,552	122,898,702
Weighted average shares outstanding	112,109,001	110,608,114
Dilutive effect of options, warrants and agents' warrants	-	-
Diluted weighted average shares outstanding	112,109,001	110,608,114

At December 31, 2009 and 2008, all share options, warrants and agents’ warrants were excluded from the calculation of diluted weighted average shares outstanding as they were anti-dilutive.

8. Contributed surplus

	2009	2008
Balance - beginning of the year	$ 6,709,251	$ 3,071,925
Stock-based compensation expensed	260,860	648,956
Stock-based compensation capitalized	35,395	88,370
Balance transferred on expiration of warrants	-	2,900,000
Balance - end of the year	$ 7,005,506	$ 6,709,251

9. Segmented information

The Company has determined its three operating segments to be Canada, Argentina and Tunisia. Financial information pertaining to these operating segments is presented in the following tables:

	2009		
	Revenue	Loss	Identifiable Assets
Canada	$ 254,181	$ (3,097,921)	$ 9,545,014
Argentina	-	(1,082,597)	13,655,546
Tunisia	17	(2,182,831)	4,497,341
Total	$ 254,198	$ (6,363,349)	$ 27,697,901

	2008		
	Revenue	Loss	Identifiable Assets
Canada	$ 1,029,090	$ (1,716,666)	$ 9,431,467
Argentina	-	(2,827)	8,771,874
Tunisia	88	(114,298)	5,671,606
Total	$ 1,029,178	$ (1,833,791)	$ 23,874,947

10. Income taxes

The amount of income taxes computed by applying the combined Canadian federal and provincial income tax rates to income before taxes differs from the amount recorded in the financial statements. The differences are summarized as follows:

	2009	2008
Net loss before income taxes	$ (6,363,349)	$ (1,833,791)
Combined federal and provincial income tax rate	29.0%	29.5%
Computed "expected" income tax recovery	(1,845,371)	(540,968)
Effect of foreign tax rates	522,644	34,298
Stock-based compensation	75,649	191,442
Change in valuation allowance	1,054,780	381,505
Canadian tax rate adjustments	110,682	43,933
Non-taxable differences on foreign operations	32,039	(118,877)
Other	49,577	8,667
	$ -	$ -

The components of the Company's future tax assets and liabilities at December 31, 2009 and 2008 are as follows:

	2009	2008
Future Income Tax Assets (Liabilities)		
Canada:		
Foreign exchange	$ (371,858)	$ (371,858)
Property and equipment	837,111	429,812
Non-capital loss carryforwards	2,821,502	2,421,186
Share issue costs	237,344	172,795
Asset retirement obligations	-	25,022
Valuation allowance	(3,524,099)	(2,676,957)
	$ -	$ -
Argentina:		
Loss carryforwards	$ 474,935	$ 132,328
Valuation allowance	(474,935)	(132,328)
	$ -	$ -
Tunisia:		
Loss carryforwards	$ 61,526	$ 5,101
Valuation allowance	(61,526)	(5,101)
	$ -	$ -

At December 31, 2009 the Company had the following non-capital loss carryforwards:

	Expiry Dates		Amount
Canada	2014 - 2029	$	11,286,000
Argentina	2013 - 2014		1,356,900
Barbados	2017 - 2018		2,461,000
Total		$	15,103,900

11. Supplemental cash flow information

		2009		2008
Accounts receivable	$	(1,504)	$	120,592
Prepaid expenses		(14,573)		(82,210)
Accounts payable and accrued liabilities		656,617		733,892
Impact of foreign exchange on working capital		154,733		5,127
Change in non-cash working capital	$	795,273	$	777,401
Attributable to:				
Operating activities	$	(233,781)	$	116,890
Discontinued operations		(6,619)		225,600
Financing activities		124,014		-
Investing activities		911,659		434,911
	$	795,273	$	777,401

12. Commitments

The Company's commitment for office space and rental accommodation is as follows:

Year	Amount
2010	$198,635
2011	71,911
2012	-
2013	-
2014	-

On acquisition of the Argentine exploration properties the Company and its joint venture partners agreed to work programs with the Province of Neuquen in Argentina. The work programs require that a total of $10,500,000 USD be spent by November 2010 of which Madalena's share is $8,722,222 USD. The Company and its partners are entitled to apply for a minimum one year extension to the November 2010 deadline.

At December 31, 2009, the Company estimates that its share of the remaining amount to be spent to satisfy the total dollar value of the Argentina work program is $155,000 USD which the Company expects to exceed if further planned expenditures are undertaken by the Company. At Cortadera and Curamhuele, if one well is not drilled on each block by November of 2010, or if an application to extend the deadline is accepted and the wells are not drilled prior to the extension deadline, the Company could forfeit its right to the non-producing portions of the Cortadera and Curamhuele exploration blocks.

13. Financial risk and capital management

The Company is exposed to various risks that arise from its business environment and the financial instruments it holds. The Board of Directors has overall responsibility for the establishment and oversight of the Company's risk management framework, policies and procedures. The following outlines the Company's risk exposures and explains how these risks and its capital structure are managed.

Capital management

The Company's objective is to maintain a strong capital position in order to execute on its exploration and development plans and maximize shareholder value.

The Company currently defines its capital as shareholders' equity. Changes to the relative weighting of the capital structure is driven by our business plans, changes in economic conditions and risks inherent in the oil and gas industry. In order to maintain or adjust the capital structure, the Company may consider any or all of the following activities, depending on existing economic conditions and access to external capital sources:

- Issue new shares through a public offering or private placement
- Raise fixed or floating interest rate debt
- Consolidate outstanding common shares
- Farm-out existing exploration opportunities
- Sale of assets

The Company is not subject to any external restrictions on its capital structure and has no debt facilities.

The Company periodically reviews its capital structure in relation to its expected exploration and development budgets. As the Company is primarily in the exploration phase, certain quantitative measures used by industry peers, such as return on equity, return on capital employed and debt to equity ratios, are not relevant measures for the Company.

The current global economic conditions, including lower interest rates, the fluctuating Canadian dollar, lower commodity prices and the limited access to external debt and equity financing markets has required Madalena to refocus its capital management policies and processes. The Company's capital management is currently focused on conserving cash balances and focusing on high impact, low capital cost exploration and development programs.

Credit risk

The Company is exposed to credit risk in relation to its cash and cash equivalents and accounts receivable.

Cash and cash equivalents are held with highly rated Canadian and international banks, and therefore the Company does not believe these financial instruments are subject to material credit risk.

The Company's accounts receivable are exposed to the risk of financial loss if the counterparty fails to meet its contractual obligations. The Company's accounts receivable include amounts due from its Argentine operators which are subject to normal industry credit risk. The carrying amounts of cash and cash equivalents and accounts receivable represents the Company's maximum credit exposure. The Company does not record an allowance for doubtful accounts and has not written off any accounts receivable in the year ended December 31, 2009 and 2008.

Liquidity risk

Liquidity risk is the risk that the Company will not meet its financial obligations as they fall due. The Company manages its liquidity risk through management of its capital structure and annual budgeting of its revenues, expenditures, and cash flow. As of December 31, 2009, the Company has a working capital surplus of $8,871,993 (2008 - $7,243,361) which given planned capital expenditures, administrative overhead requirements and commitments, is sufficient to meet all financial obligations in the current year.

Market risk

Changes in commodity prices, interest rates and foreign currency exchange rates can expose the Company to fluctuations in its net earnings and in the fair value of its financial assets and liabilities.

Commodity price risk

Price fluctuations for both crude oil and natural gas are determined by world and North American supply and demand factors. The Company has no influence over the pricing of oil and natural gas and has not attempted to mitigate commodity price risk through the use of financial derivatives.

Interest rate risk

The Company is exposed to interest rate fluctuations on its investments of excess cash in short-term discount notes issued by international banks.

Foreign currency exchange rate risk

A substantial portion of the Company's exploration and development activities are conducted in foreign jurisdictions and a portion of the Company's cash and cash equivalents are denominated in US dollars (USD) and Argentine Pesos (ARS). Consequently, the Company is exposed to foreign currency exchange risk on a substantial portion of its financial assets. The Company has not entered into derivative exchange rate contracts to mitigate this risk.

Sensitivity analysis

The following table presents an estimate of the impact on net earnings of the market risk factors discussed above and is calculated based on the noted change in the market factor applied to the balance at the end of the period.

Market risk	Change in market factor	Increase (decrease) in loss before tax
Foreign exchange - effect of strengthening CAD $		
USD denominated financial assets and liabilities	3%	(11,200)
ARS denominated financial assets and liabilities	3%	4,500

Fair value of financial instruments

The Company's financial instruments include cash and cash equivalents, accounts receivable and accounts payable and accrued liabilities, the carrying values of which approximate their fair values due to their short-term nature. The Company has no bank indebtedness.

Cash and cash equivalents are categorized as held-for-trading assets and are measured at fair value with any change in fair value recognized in net loss during the period. Accounts receivable are categorized as loans and receivables and accounts payable and accrued liabilities are categorized as other financial liabilities; all of which are recorded at amortized cost.

The following table provides information on the foreign currency denominated financial instruments held by the Company at December 31, 2009:

	Balance denominated in		Total CAD
	USD	ARS	equivalent
Cash and cash equivalents	396,702	1,169,149	$ 734,124
Accounts receivable	-	516,579	140,148
Prepaid expenses	-	389,115	105,567
Accounts payable and accrued liabilities	751,905	1,515,995	$ 1,201,541

14. Related party transactions

In 2009, the Company incurred fees of $156,931 payable to a law firm in which a director of the Company is a partner.

15. Subsequent event

In March 2010, the Company sold its interest in the Remada Sud Permit in Tunisia for cash consideration of $4 million USD.