

**Primeline Energy Holdings Inc. (TSX Venture-PEH)
Management Discussion and Analysis for the Year Ended March 31, 2010
(Prepared by Management)**

INTRODUCTION

This management discussion and analysis is dated July 28, 2010 and takes into account information available up to that date. It should be read in conjunction with the Company's audited consolidated financial statements and related notes for the year ended March 31, 2010, which have been prepared in accordance with Generally Accepted Accounting Principles in Canada. All monetary amounts in this discussion and analysis are expressed in Canadian dollars unless otherwise noted.

Cautionary Note Regarding Forward-Looking Statements

Some of the following disclosures contain forward-looking statements, which involve inherent risk and uncertainty affecting the business of Primeline. These statements relate to the time anticipated to submit and gain government approval of the Overall Development Program (referred to herein as the "ODP") for the Lishui 36-1 (or LS 36-1) gas field, the commencement of the development of the LS 36-1 gas field (referred to herein as the "Development"), the Company's expectation that it will enter into a final contract for the sale of gas from the LS 36-1 gas discovery and the results of exploration of the Company's other resources and exploration prospects. They are based on assumptions that submission of the ODP for government approval will be completed and approval gained in a timely fashion, that the Development will be commenced as planned, that funding will be sufficient to pay the costs of the Development, that a final gas sale contract can be concluded on acceptable terms and that the results of further exploration will be favourable. Actual results may vary from those anticipated in such statements. Work may be delayed for technical and other reasons and, if it is, approval of the ODP will also be delayed. Funding may not be sufficient and, if it is not, the Company may be unable to complete some or all of the Development. Costs of the Development may be greater than anticipated. The Company may not be able to conclude a final contract for gas sale on acceptable terms. Exploration for oil and gas is subject to the inherent risk that it may not result in a commercial discovery.

COMPANY AND PROJECT OVERVIEW

Primeline Energy Holdings Inc. (the Company") is focused exclusively on upstream oil and gas opportunities in China. The Company owns rights in and operates an exploration licence of 5,221 sq km in the East China Sea ("Block 25/34") pursuant to a Petroleum Contract dated March 24, 2005 ("Petroleum Contract") entered into between China National Offshore Oil Corporation ("CNOOC"), Primeline Energy China Ltd. ("PECL"), a wholly owned subsidiary of the Company, and Primeline Petroleum Corporation ("PPC"), an affiliated company wholly owned by Victor Hwang, the Company's chairman and majority shareholder. PECL and PPC act jointly as the "Contractor" under the Petroleum Contract and PECL and PPC own 75% and 25% respectively of the Contractor's interests in the Petroleum Contract. Primeline Energy Operations International Ltd. ("PEOIL"), another wholly owned subsidiary of the Company, is designated as "Operator" under the Petroleum Contract. References in this MD&A to 'Primeline' refer generally to the Company, PECL, PEOIL and PPC and references to the Company include its subsidiaries PECL and PEOIL. References to the "Contractor" are to PECL and PPC acting jointly.

Pursuant to the Petroleum Contract, the Contractor is required to fund all exploration costs and CNOOC has the right to participate in up to 51% of any commercial development by paying its pro rata share of the development and operating costs required for production of any oil or gas. The Contractor has the right to recover exploration costs from future production.

Primeline and CNOOC are implementing a rolling development strategy in the Lishui Basin. Primeline is working with CNOOC on the development of the LS 36-1 natural gas discovery (“LS 36-1 gas field”) in Block 25/34 on a stand-alone basis. The LS 36-1 gas field was discovered by Primeline and has two wells with DSTs which tested flow rates of 9.9 and 12.6 MMcf/d of natural gas and has probable recoverable gas reserves of 119 bcf (Company net of 44 bcf).

There are several related prospects in the vicinity of the LS 36-1 gas field (generally referred to as the “Lishui Gas Play”) which have been seismically delineated and Primeline has discovered gas in one of these prospects through its well LS 35-3-1 drilled in April to June 2010. Furthermore, Primeline believes that there is hydrocarbon potential, in addition to the Lishui Gas Play, in the remainder of Block 25/34.

The development of LS 36-1 may not by itself yield significant income in the near term but it would confirm the market for gas to be produced from Block 25/34 and establish a production facility for the Lishui Gas Play. The confirmation of the market and the creation of the production facility would significantly enhance the potential value of any additional resources which may be discovered, not only in the LS 36-1 gas field itself in the probable and possible category resources but, also, in the Lishui Gas Play and elsewhere within Block 25/34.

ANNUAL PROGRESS REVIEW

During the year under review, Primeline has continued to pursue its dual strategy of working towards a stand-alone development of the LS 36-1 discovery, based on the currently confirmed resources, whilst at the same time continuing its efforts to explore the nearby prospects to expand the current resource base. Primeline has made significant progress in both aspects of the strategy.

Accordingly, Primeline’s development and exploration activities during the year under review have consisted of:

Development

- completion of the compilation of the ODP for the development of the LS 36-1 discovery and preparation for the submission of the ODP for central government approval;
- continued negotiation, in conjunction with CNOOC, of the further detailed terms on which the gas will be sold to Zhejiang Provincial Natural Gas Grid for incorporation into a Framework Agreement with Zhejiang Gas which has been signed, in July 2010, subsequent to the year end;
- negotiation and execution of CO₂ sales agreements with three regional CO₂ distributors;
- continued negotiation of the terms of the land acquisition for the landing site for offshore pipeline and gas processing terminal at the identified site in Wenzhou;

- commencement and completion of the negotiations for the Supplemental Development Agreement (“SDA”) and related agreements with CNOOC governing the development and production operations relating to the LS 36-1 gas field and required for finalisation of the ODP;
- commencement and continued discussions with financial institutions relating to the financing of Primeline’s share of the development project funding.

Exploration

As part of the overall rolling development strategy, Primeline has been actively planning the step out drilling into the nearby prospects in the Lishui Gas Play, including:

- completion of the well design and other preparation work;
- execution of a turnkey drilling contract with China Oilfield Services Ltd. (COSL) and, subsequent to the year end, drilling of an exploration well LS35-3-1 resulting in a hydrocarbon discovery.

Primeline is currently conducting the post well evaluation and a re-assessment of the remainder of the Block incorporating the information collected from the new well.

DEVELOPMENT OF LS 36-1 GAS FIELD

Development Work Overview

Primeline’s existing gas discovery, LS 36-1, has only relatively small reserves defined by the two successful wells and was previously regarded as sub-commercial. In 2007, Primeline and CNOOC obtained reserve approval from the Chinese State Reserve Commission and completed a feasibility study of the stand-alone development of LS 36-1. Based on the results of the formal feasibility study, CNOOC signed, with Zhejiang Natural Gas Development Co. Ltd. (“Zhejiang Gas”), the Agreement in Principle for the Sale and Purchase of Natural Gas from LS 36-1 (“Agreement in Principle”) in October 2008. In 2009, Primeline and CNOOC commenced and completed the preparation of the ODP for LS 36-1 and confirmed the commerciality of the gas field. Primeline and CNOOC then entered into the SDA and various other agreements related to the Development in March 2010. Primeline and CNOOC are currently preparing for the submission for government approval of the development whilst carrying out necessary development preparation work including terminal land acquisition.

Overall Development Program (“ODP”)

The ODP is required to be approved by the Chinese government before Development can officially commence. It comprises a formal development engineering plan, backed up by survey results and environmental studies, together with a full economic analysis of the Development.

Following the execution of the Agreement in Principle in October 2008 and the optimisation of the previous feasibility study between November 2008 and January 2009, Primeline contracted CNOOC Research Beijing to compile the ODP in February 2009.

CNOOC Research took overall responsibility for the compilation and technical approval of the ODP, including technical design, analytical work and management of the various surveys and third party services. The two environmental surveys, the costs of which were included in the overall budget, were previously commissioned and paid for by Primeline in May 2008 and October 2008 with the work being closely monitored by CNOOC Research. The

important surveys in 2009 were the pipeline route survey and platform site survey, which were both contracted to COSL. Other survey work included environmental surveys for the platform, pipeline, terminal and jetty, the site survey for the terminal and the fishery resources survey. Specific studies included a study of potential hazards for the terminal, pipeline and platform, an earthquake risk assessment, occupational health studies, CO₂ utilisation market research and a number of specific studies on reservoir, drilling and engineering. CNOOC Research is responsible for obtaining technical approval of the ODP from all of the appropriate Chinese State Authorities.

The technical work, supported by completed surveys and additional study results, was largely completed in July 2009. Primeline and CNOOC Shanghai held a joint review meeting in late July 2009 in Shanghai to review the initial results. Following that initial review, additional work was carried out and the final review by CNOOC Head office was held on August 27, 2009 in Wenzhou, the major city on the coast where the proposed offshore pipeline will land directly from the LS 36-1 gas field. At the final technical review, the ODP was approved and accepted by CNOOC and Primeline and it was agreed that the parties would proceed to seek internal approval from CNOOC Investment Committee and Primeline's Board before submission of the ODP for central government approval. Primeline and CNOOC confirmed the development proposals at a Joint Management Committee ("JMC") meeting held on March 31, 2010 in Shanghai.

The ODP was finalised in December 2009 after which Primeline and CNOOC prepared the supporting documentation for the ODP for submission to the relevant government departments for approval which includes an occupational hazard assessment, a safety assessment report and an environment impact assessment ("EIA"). All three reports need to be reviewed and approved by a government designated expert panel and submitted to and approved by the relevant government ministries and commissions before the ODP can be formally submitted for approval. Primeline and CNOOC aim to have approvals in place and to submit the full ODP to the National Development and Reform Commission in the third or fourth calendar quarter of 2010. The ODP was completed within its budget of RMB36 million (US\$5.5 million) (Company's share C\$4.3 million).

Development Agreements

During the majority of the financial year under review, Primeline and CNOOC were negotiating the terms of the SDA, a Joint Operating Agreement ("JOA"), an agreement relating to the implementation of the development and procurement and cost control principles ("Implementation Agreement") and a letter agreement amending a previous agreement relating to the terms of the Petroleum Contract ("Amendment Agreement"). These agreements ("Development Agreements"), which will govern the development and production operations relating to the LS 36-1 gas field, were signed on March 17, 2010 in Beijing at a ceremony attended by senior management from CNOOC and Primeline. The main terms of the Development Agreements are summarised below.

Transfer of Operatorship for the Development

One of the principal purposes of the Development Agreements was to transfer the operatorship for the development and production operations for the LS 36-1 gas field from PEOIL to CNOOC China Ltd Lishui Operating Company ("CCLOC"), to be established as a wholly owned subsidiary of CNOOC China Limited, a subsidiary of CNOOC Ltd. (the listed

subsidiary of CNOOC). Various benefits are expected from this transfer of operatorship. Firstly, CNOOC Ltd. has an established project management team which has considerable relevant experience and which would be mobilised with minimum delay. Secondly, as a subsidiary of CNOOC Ltd., CCLOC is able to procure the services and equipment required for the development of the gas field on the basis of existing CNOOC long term procurement contracts with various contractors which, together with other operational efficiencies, should result in cost savings for the Development. CCLOC will act only as operator in respect of the development and production operations for the LS 36-1 gas field; PEOIL will continue to act as operator under the Petroleum Contract in respect of all continuing exploration operations.

SDA, JOA and Implementation Agreement

Under the SDA, CNOOC formally confirmed the exercise of its right under the Petroleum Contract to take its full participating interest of 51% in the LS 36-1 gas field, such that the respective participating interests in the development of and production from the gas field are 51% CNOOC, 36.75% PECL and 12.25% PPC. The development and operating costs will be borne by the parties in accordance with their respective participating interests.

The SDA also confirmed that:

- a development area of circa 85 km² surrounding the LS 36-1 gas field will be carved out of Block 25/34;
- the production period for the LS 36-1 gas field will be for a minimum of 15 years from the commencement of commercial production and will be extended in the event that additional gas resources are discovered within Block 25/34 which can be tied into the production facilities established for LS 36-1; and
- the production facilities will be owned by the parties jointly in the proportions of their participating interests until full cost recovery and the parties shall have the continuing right, until the end of the production period, to use the production facility assets in respect of any additional resources which may be discovered within Block 25/34 and which can be tied into the production facility assets.

The SDA was subsequently ratified by the Ministry of Commerce of the People's Republic of China and became effective on June 13, 2010.

The JOA, which was entered into by CNOOC China Ltd., PECL and PPC, sets out the basis on which CCLOC shall establish a project management team in Shanghai and carry out the development and production operations. In particular, it provides that Primeline may appoint certain key members to the project management team who will be involved in all procurement and operational decisions and granted Primeline a significant degree of control over how those operations are carried out with all major decisions being by unanimous decisions of the Parties. The JOA is supplemental to the SDA and accordingly also became effective on June 13, 2010.

In the Implementation Agreement, Primeline and CNOOC agreed that the development preparation work should be implemented immediately in order that the Development could be completed in time to deliver first gas to Zhejiang Gas in accordance with the agreed target date of mid 2012 and it was agreed that CNOOC would be responsible for such initial preparation work in order to maintain the target. The Implementation Agreement also set out the agreed principle that as much of the procurement of the development as possible should be contracted using long term procurement contracts established by CNOOC in order to

achieve cost savings so that the development can be delivered as economically and efficiently as possible.

Pursuant to a previous amendment agreement in February 2008, CNOOC and Primeline had agreed that the first exploration period under the Petroleum Contract would be extended by one year and that one of the two subsequent two-year exploration periods would be reduced by a corresponding period of one year, unless otherwise agreed. It was agreed, pursuant to the Amendment Agreement, that the two remaining exploration periods under the Petroleum Contract would be for two years each. Thus, the second exploration period, which commenced on May 1, 2009, will end on April 30, 2011 and the third exploration period will commence on May 1, 2011 and end on April 30, 2013.

The signing of the Development Agreements marked the commencement of the development project with Primeline and CNOOC working in close co-operation, playing to their respective strengths for the common goal of a successful rolling development. It is intended that the agreed principles will lead to cost saving and streamlined management and scheduling which are both vitally important to the development of the LS 36-1 gas field. In addition, the clear division of responsibilities enables Primeline to focus on the step out exploration programme for which Primeline continues to be the operator.

Gas Sale Agreement

The Agreement In Principle signed between CNOOC (on behalf of themselves and Primeline) and Zhejiang Gas defined the general terms on which Zhejiang Gas agreed to purchase the future production of natural gas from the LS 36-1 gas field, including the quality of the gas, take-or-pay principles, base price, annual quantity and delivery schedule. The principles set out in the Agreement In Principle govern the further negotiation of the Framework Agreement, and, subsequently, the final gas sale contract, the terms of which can only be finalised during the development of the production facility. During the year under review, Primeline, CNOOC and Zhejiang Gas have continued their negotiation of the detailed terms of the gas sale, for incorporation into a more formal agreement relating to the gas sale, referred to as the Framework Agreement.

Subsequent to the year under review, CNOOC and Zhejiang Gas signed the Framework Agreement for the sale and purchase of gas from LS 36-1 Gas Field which was dated on July 7, 2010. The Framework Agreement replaced the Agreement in Principle. The commercial terms are substantially the same as the Agreement in Principle but the Framework Agreement contains various detailed terms, including the delivery point, delivery planning and schedule, determination of final delivery gas price and payment terms, which had not previously been confirmed in the Agreement in Principle. The Framework Agreement is sufficient to satisfy the requirement for the government approval and project financing of the development.

During the development of the production facility, when further supply and production details are confirmed, CNOOC and Primeline will negotiate further details of the gas sale and it is anticipated that the Framework Agreement will in due course be replaced by a final gas sale contract.

In signing the Framework Agreement, CNOOC acted on its own behalf and on behalf of the Company and PPC. CNOOC has previously entered into a separate agreement with the Company and PPC confirming that the Company's and PPC's share of the gas (being 36.75%

and 12.25% respectively) from the LS 36-1 gas field will be sold through CNOOC on the same terms as the Framework Agreement.

CO₂ Market Research and Sale

The raw gas in LS 36-1 contains CO₂ which must be extracted as part of the process of production of natural gas for sale into the Zhejiang provincial gas grid. Under the ODP for the LS 36-1 gas field it is planned that the CO₂ should be extracted and then liquefied to create food grade liquid CO₂ which can be sold into the local market. Primeline commissioned a detailed market research report to assess the market for liquid CO₂, which report confirmed that there is a rapidly growing market for CO₂ products in the East China region with applications including metal processing, fabrication (particularly in the ship building industry) and numerous uses in the food industry.

Primeline and CNOOC concluded initial negotiations with the three largest CO₂ distribution companies in Zhejiang and Fujian Provinces which resulted in Framework Distribution Agreements (“CO₂ Agreements”) being signed between CNOOC and each of the three distribution companies in December 2009. In entering into the CO₂ Agreements, CNOOC acted on its own behalf and on behalf of the Company and PPC. A separate agreement was entered into between CNOOC, the Company and PPC outlining the terms of authorisation for CNOOC to sell the CO₂ on behalf of the Company and PPC pursuant to the CO₂ Agreements.

Under the CO₂ Agreements the distribution companies agreed to take or pay for an aggregate amount of liquid CO₂ representing the initial proposed production from the LS 36-1 gas field. The CO₂ Agreements define the general terms on which the distribution companies will buy and distribute the liquid CO₂ to be produced by Primeline and CNOOC. These three companies will sell the liquid CO₂ into the East China market, each being granted an exclusive distribution area. The ODP contains plans for a dock facility adjacent to the gas processing terminal which is intended to be used to facilitate the transportation of the liquid CO₂ by sea.

On the basis of the price agreed for the sale of the liquid CO₂ it is anticipated that the full cost of the creation and operation of the liquefied CO₂ production facilities will be covered with a small profit.

Development Finance

Following commencement of the preparation of the ODP, Primeline entered into initial discussions with various financial institutions with the intention of securing project finance for its share of the development costs. During the year under review, Primeline continued these discussions with a number of Chinese financial institutions and made significant progress in such discussions. The intention is to arrange finance in Chinese Renminbi, since the income from sale of the gas and CO₂ and most of the development cost will be in that currency. Any such financing arrangements will of course be subject to the Central Government’s approval of the ODP.

Primeline is also exploring various options for funding the equity portion of the development cost and the cost of further exploration drilling.

RESERVE UPGRADE

Following the finalisation of the ODP by Primeline and CNOOC, Primeline appointed McDaniel and Associates Consultants Limited (“McDaniel”) of Calgary to conduct a full independent evaluation of the LS 36-1 project. McDaniel is one of the world's leading petroleum consulting firms specializing in geological studies, reserves evaluations, resource assessments, economic evaluations and petroleum engineering studies. They reviewed the full ODP report and the Agreement in Principle relating to LS 36-1 and upgraded their evaluation of the natural gas and natural gas liquid located on LS 36-1 from Contingent and Prospective Resources to Probable and Possible Reserves in accordance with the standards set out in Canadian National Instrument 51-101 and the Canadian Oil and Gas Evaluation Handbook (COGEH). McDaniel's evaluation estimates that the LS 36-1 gas field has a total project recoverable Probable Reserves of 119 bcf of natural gas and 4.91 MMbbl of natural gas liquid and light oil, which translates to Company net Probable Reserves of 44 bcf of gas and 1.8 MMbbl of natural gas liquid and light oil; and project Possible Reserves of 93 bcf of gas and 3.8 MMbbl of natural gas liquid and light oil, which translates to Company net Possible Reserves of 34 bcf of gas and 1.40 MMbbl of natural gas liquid and light oil.

Under oil industry definition, there is a 50% probability that the quantities actually recovered will equal or exceed the Probable Reserves. Possible Reserves are those additional reserves that are less certain to be recovered than Probable Reserves. There is a 10% probability that the quantities actually recovered will equal or exceed the Possible Reserves. McDaniel stated that “proved reserves have not been assigned as the ODP has not yet been approved by CNOOC and the government, and the Framework Agreement relating to the gas sale has not yet been executed.” The effective date of McDaniel's estimate is March 31, 2010.

Based on the Agreement in Principle and their view of the full product price, McDaniel estimates a net present value for the LS 36-1 project's Probable Reserves, net to Primeline, of US\$93 million at a discount rate of 5% and US\$255 million, again net to Primeline, when the Possible Reserves in LS 36-1 are included. It should be noted that these estimated values are not an estimate of fair market value.

SUMMARY OF OIL AND GAS RESERVES
AND NET PRESENT VALUES OF FUTURE NET REVENUE
as at March 31, 2010
FORECAST PRICES AND COSTS

RESERVES CATEGORY	RESERVES ⁽¹⁾⁽²⁾								
	LIGHT AND MEDIUM OIL				NATURAL GAS		NATURAL LIQUIDS		GAS
	Gross (Mbbl)	Net (Mbbl)	Gross (Mbbl)	Net (Mbbl)	Gross (MMcf)	Net (MMcf)	Gross (Mbbl)	Net (Mbbl)	
CHINA									
PROVED									
Developed Producing	-	-	-	-	-	-	-	-	-
Developed Non-Producing	-	-	-	-	-	-	-	-	-
Undeveloped	-	-	-	-	-	-	-	-	-
TOTAL PROVED	-	-	-	-	-	-	-	-	-
PROBABLE	671	688	-	-	43,871	44,435	1,133	1,148	
TOTAL PROVED PLUS PROBABLE	671	688	-	-	43,871	44,435	1,133	1,148	
POSSIBLE	496	499	-	-	34,107	34,066	881	880	
TOTAL PROVED PLUS PROBABLE PLUS POSSIBLE	1,167	1,187	-	-	77,978	78,500	2,014	2,027	

RESERVES CATEGORY	NET PRESENT VALUES OF FUTURE NET REVENUE ^{(3) (4)(5)(6)}									
	BEFORE INCOME TAXES DISCOUNTED AT (%/year)					AFTER INCOME TAXES DISCOUNTED AT (%/year)				
	0 (\$M US)	5 (\$M US)	10 (\$M US)	15 (\$M US)	20 (\$M US)	0 (\$M US)	5 (\$M US)	10 (\$M US)	15 (\$M US)	20 (\$M US)
CHINA										
PROVED										
Developed Producing	-	-	-	-	-	-	-	-	-	-
Developed Non-Producing	-	-	-	-	-	-	-	-	-	-
Undeveloped	-	-	-	-	-	-	-	-	-	-
TOTAL PROVED	-	-	-	-	-	-	-	-	-	-
PROBABLE	276,653	133,197	50,959	1,686	(28,854)	208,305	93,250	26,535	(13,839)	(39,060)
TOTAL PROVED PLUS PROBABLE	276,653	133,197	50,959	1,686	(28,854)	208,305	93,250	26,535	(13,839)	(39,060)
POSSIBLE	410,645	215,902	122,879	74,828	48,227	307,880	161,591	91,783	55,763	35,846
TOTAL PROVED PLUS PROBABLE PLUS POSSIBLE	687,298	349,099	173,838	76,514	19,373	516,185	254,841	118,318	41,925	(3,214)

Notes:

- (1) Company Gross reserves are based on a 36.75 percent working interest share of the property gross resources, on the basis that CNOOC has exercised their right to back-in and take a 51 percent interest. See "Oil and Gas Property and License Status".
- (2) Company Net reserves are based on Company share of Cost Oil and Profit Oil and due to repayment of past costs are greater than Company Gross.
- (3) Based on forecast prices and costs at March 31, 2010.
- (4) Interest expenses and corporate overhead etc. were not included.
- (5) The net present values may not necessarily represent the fair market value of the reserves.
- (6) Company Share of Net Present Values are after the deduction of Chinese Corporation Tax.

In the report McDaniel also commented that "the development of the LS36-1 field will provide an infrastructure hub in the area which may be utilized in any development of the nearby prospects. It is envisaged that development of these prospects will be by subsea wells or a well head platform with all processing at the infrastructure hub. Incremental development costs will therefore be low and the economics for any additional resources which may be discovered within LS36-1 field itself or in the nearby identified prospects would be significantly enhanced."

A summary of the McDaniel's report is available on Primeline's website: <http://www.pehi.com>.

EXPLORATION ACTIVITIES

Lishui Gas Play and 3D Seismic Data

Through the careful evaluation of the 737 sq km of 3D seismic data, covering the LS 36-1 discovery and nearby prospects, Primeline confirmed the existence of channel and canyon systems and several sizeable prospects in this new play concept area, referred to as the Lishui Gas Play. Tertiary channel sands are a proven play type in other areas including Western Africa and the Gulf of Mexico. These nearby prospects and leads could provide significant resource additions for Primeline.

As McDaniel has previously evaluated and reported, in the area covered by 737 sq km of 3D seismic around the LS 36-1 gas field, Primeline has mapped out six additional prospects with similar characteristics to LS 36-1. Two of the top prospects in this 3D area have been surveyed, one has been subsequently drilled with the second ready to drill.

PROSPECTIVE RESOURCES

The Company's prospective resources have been evaluated by McDaniel & Associates Consultants Ltd. and are set out below.

	Prospective Resources at March 31, 2010 ⁽²⁾⁽³⁾				
	Unrisked Low Estimate ⁽⁶⁾	Unrisked Best Estimate ⁽⁷⁾	Unrisked High Estimate ⁽⁸⁾	Unrisked Mean	Risked Mean
Total Company ⁽⁴⁾					
Natural Gas Resources, MMcf	96,323	234,636	576,769	290,940	102,579
Condensate Resources, Mbbl	2,661	6,462	15,822	7,998	2,815
BOE Resources, Mbbl	18,715	45,568	111,951	56,488	19,911

Notes

- (1) Prospective resources were calculated probabilistically, but based on an arithmetic aggregation of the individual prospects.
- (2) Each prospect has its own probability of geological success.
- (3) There is no certainty that any portion of the resources will be discovered. If discovered, there is no certainty that it will be economically viable or technically feasible to produce any portion of the resources.
- (4) Company Gross resources are based on a 36.75 percent working interest share of the property gross resources, on the basis that CNOOC has exercised their right to back-in and take a 51 percent interest. See "Oil and Gas Property and License Status".
- (5) Low, best and high estimates follow the COGE Handbook Section 5 resources definitions and guidelines for prospective resources. The resource range presented above is "unrisked" meaning that it is valid in the event of successfully finding hydrocarbons in each and every prospect. In this case, the possible range of recoverable resources would likely lie in the range between the low estimate and the high estimate.
- (6) The low estimate reported is the arithmetic sum of the individual prospect P90 quantities derived from probabilistic analysis. This is considered to be a conservative estimate of the quantity that will actually be recovered from the accumulation.
- (7) The best estimate is based upon the expected value, based upon the outcome of the probabilistic analysis. This is considered to be the best estimate of the quantity that will actually be recovered from the accumulation.

- (8) The high estimate is the arithmetic sum of the individual P10 quantities derived from probabilistic analysis. This is considered to be an optimistic estimate of the quantity that will actually be recovered from the accumulation.
- (9) "Risky Mean" resources are calculated based on the probability of geological success applied to the unriskey mean shown above.

The prospective resource estimates are for 6 prospects in the vicinity of the existing discovery in an area covered by 3-D seismic. Further seismic acquisition and studies over the remainder of the block (approximately 85 percent by area) could lead to the identification of additional prospects. Therefore the prospective resources detailed above do not necessarily represent the full exploration potential of Block 25/34.

LS 35-3-1 Drilling

Through several rounds of negotiation, Primeline secured a rig with COSL and on March 5, 2010, signed the turnkey drilling contract. Under the turnkey drilling contract, COSL agreed to drill the LS35-3-1 well in Block 25/34 using a jack-up rig, COSL 942. COSL also agreed to supply all necessary equipment, services and personnel for the drilling.

The LS35-3 prospect is approximately 14.5 km from the existing LS36-1 discovery and is one of four main channel system prospects Primeline identified in the area adjacent to the LS36-1 Gas Field. Any resources discovered at LS35-3 could be easily tied into the proposed production facility at the LS 36-1 gas field.

Rig 942 arrived at Primeline's location on April 9, 2010 and, the LS 35-3-1 well was spudded on April 12, 2010. On May 4, 2010, the well reached the planned total depth (TD) of 2,886m, and Primeline decided to deepen it to the TD of 2,908m which was reached on the same day. Gas shows and weak oil shows were encountered during drilling.

LS 35-3-1 Testing Results

Primeline implemented a programme of electric logging and conducted a formation evaluation logging programme including Vertical Seismic Profiling (VSP), Reservoir Characterisation Instrument (RCI -RFT) and side wall coring. The interpretation of the log data resulted in the following initial conclusions:

- Target Zone 1: 53m of continuous sandstone with porosities ranging 13-22% but no indications of hydrocarbons;
- Target Zone 2: 65m of sandstone with mudstone interbeds with porosities ranging 0-16% but with limited indications of hydrocarbons;
- Target Zone 3: gross 60m section of sandstone and mudstone interbeds with over 20m aggregate of potential hydrocarbon gas pay in two zones with porosities ranging 5-16%.

Based on these results, Primeline instructed COSL to conduct drill stem testing (DST) of the two intervals in target 3. On May 16, 2010, Primeline commenced a DST programme to test these zones under a turnkey arrangement with COSL.

DST 1 was conducted over the depth range 2,836-2,852m measured depth (MD). This was conducted conventionally using diesel in the wellbore. There was no flow of hydrocarbons to surface.

DST 2 was conducted over the depth range 2,794-2,802m MD. In contrast to DST 1, nitrogen was used in the wellbore to optimise the pressure drawdown and gas flowed naturally to the surface and was flared continuously and steadily for over 7 hours. A second flow period was attempted after an 18 hour shut-in but was unsuccessful because the test valve was blocked by formation sand. There was then a second shut-in period of 15 hours. Data from the downhole pressure gauges showed that the two pressure build-ups during the shut-in periods were consistent. The surface gas flow during the first flow period was at a low pressure which steadily rose over the 7 hour flow period but did not reach the pressure necessary to operate the separator or the flow meters. The flow potential of the well was thus not measured. Gas samples were collected at the wellhead and fluid samples were collected from the wellbore which will be analysed in laboratory conditions. It was therefore decided that sufficient data had been collected to enable the estimation of the production pressure and flow rates and the composition of the hydrocarbons in due course. The test programme ended on May 29 and the LS 35-3-1 well was declared as a gas discovery. The COSL rig was released on June 7 after the completion of end-of-well operations.

This discovery is significant in that it confirms that hydrocarbons have migrated to and are trapped in the west flank of the West Lishui Basin, the majority of which is inside Block 25/34. Three channel systems have been mapped and delineated in Primeline's 3D area, with others recognised to the north of that area which is covered by 2D seismic data. Primeline is now carrying out a careful post well evaluation over the next 4 to 6 months to assess the volume and nature of the resources discovered in LS 35-3, refine the petroleum system model and high-grade and further define prospects for further exploration drilling.

This discovery is also the first surface flow of natural gas from a low permeability reservoir in the southern East China Sea. This is significant, not only for further exploration in Block 25/34, but also for upside in the LS 36-1 Development. The LS 36-1 gas field has over 200 metres of gas-bearing low-permeability reservoirs which are directly below the gas zone being developed. With the new data from LS 35-3-1, Primeline will assess the potential for modern fracing, horizontal and multi-lateral drilling technology to enhance the low permeability reservoirs' production rates.

The total drilling cost was US\$16.5m and testing costs was US\$11.8m, which is in line with the budget.

CORPORATE DEVELOPMENT

Rights Offering

In order to fund the cost of the turnkey drilling contract for LS35-3-1 Primeline effected an offering to shareholders of rights to subscribe for 47,020,623 Shares at \$0.50 per Share ("Offering").

The Company's largest shareholder, Primeline International (Holdings) Inc. ("Primeline International"), agreed to provide a standby commitment (the "Standby Guarantee") under which Primeline International would purchase from the Company at the Subscription Price any Shares (the "Standby Shares") that were not otherwise subscribed for under the Offering prior to the expiry time, including pursuant to the Additional Subscription Privilege. Primeline International is owned by Mr. Victor Hwang, the Company's chairman.

The Company engaged Jennings Capital Inc. (“Jennings Capital”) as managing dealer for the Offering and entered into a managing dealer agreement dated March 24, 2010. Jennings Capital was entitled to a fee equal to the greater of (i) 2% of the gross proceeds from the exercise of Rights by holders of Shares, other than Mr. Hwang, his family members and affiliates (including Primeline International) and the directors and officers of the Company, and (ii) CAD\$75,000.

The Offering was closed on May 6, 2010. Under the Offering, shareholders subscribed for and purchased 39,640,833 Shares resulting in gross proceeds of \$19,820,416. Under a Standby Guarantee Agreement with the Company, Primeline International purchased the balance of 7,379,790 Shares available under the Offering, for gross proceeds of \$3,689,895. Aggregate gross proceeds of \$23,510,311 were received by Primeline. Net proceeds were \$23,056,752 after deducting the fee to Jennings Capital and professional fees and other expenses of the Offering of \$453,559. The net proceeds of the Offering were used to pay for the Company’s share of the costs of drilling and testing of the LS35-3-1 exploration well, amounting to US\$28m (the Company’s share US\$21m) plus associated supervision and evaluation costs, with the balance remaining being retained for working capital purposes. This compares with the estimate in the short form prospectus relating to the Offering as follows:

	Prospectus		Actual
	High	Low	
Drilling Costs	\$20,930,032	\$12,568,050	\$21,225,000
Working Capital	\$1,985,211	\$10,347,193	\$1,831,752
	\$22,915,243	\$22,915,243	\$23,056,752

The variance in drilling costs from those set forth in the prospectus is due to the fact that Primeline discovered gas and conducted two DSTs, as reported in the previous sections. Also, expenses of the offering were at \$453,559 were slightly higher than the \$400,000 estimated in the prospectus. The variances will have no impact on Primeline’s ability to achieve its business objectives.

PETROLEUM CONTRACT

The Petroleum Contract provides for an initial exploration period with a development period and a production period for each commercial development. The exploration period was originally for seven years commencing on May 1, 2005, split into three phases lasting 3, 2 and 2 years respectively.

In 2007 the Company and CNOOC agreed on a rolling development strategy, which entails developing the existing gas resources in the LS 36-1 Gas Field whilst at the same time continuing exploration of nearby prospects. As a result, in April 2009, in view of the work programme being undertaken in relation to the ODP and the difficulty then being experienced in locating a suitable rig, CNOOC agreed that Primeline could carry forward the unfulfilled one well commitment from the first phase into the second phase of the exploration period.

Primeline elected to enter into the second phase of the exploration period for Block 25/34 which is for two years and commenced on May 1, 2009, with a commitment for two exploration wells each with a minimum depth of 2,500m, including the one unfulfilled well commitment carried over from the first phase. Of those two commitment wells, one well,

LS35-3-1, was completed in June 2010, leaving an additional well to be drilled by April 30, 2011. Pursuant to the Petroleum Contract, the Contractors were required to relinquish 25% of the exploration area when they elected to proceed to the second phase and, as a result, the total concession area for Block 25/34 during the second phase of the exploration period was reduced to 5,221 km².

Pursuant to a previous amendment agreement in February 2008, CNOOC and Primeline agreed that the first exploration period under the Petroleum Contract would be extended by one year and that one of the two subsequent two-year exploration periods would be reduced by a corresponding period of one year, unless otherwise agreed. It was agreed on March 17, 2010, pursuant to the Amendment Agreement, that the two remaining exploration periods under the Petroleum Contract would be for two years each. Thus, the second exploration period, which commenced on May 1, 2009, will end on April 30, 2011, and the third exploration period will commence on May 1, 2011 and end on April 30, 2013.

GENERAL FINANCIAL OUTLOOK

As at the year-end (March 31, 2010), the Company held cash resources of C\$30.3 million, subsequently the Company drilled the LS 35-3-1 well and hence, at the current date, the Company has cash resources of approximately C\$6.1 million and the final payment under the drilling contract is estimated at around C\$1.7 million. The costs of running the Company's general operations are estimated at approximately C\$2.5 million per annum. Accordingly, the Company has sufficient funds in hand to continue its general operations during the coming year. However, additional financing would be required to fund the Company's obligations regarding the Development, or if the Company was to enter into any future exploration drilling contracts. There may be various alternative financing options available to the Company in the event that the Development proceeds but it is likely that the Company will be required to raise additional equity capital in order to finance any further exploration drilling contracts. The Company is exploring all possible fund-raising possibilities for both its share of development costs and for the planned exploration drilling programme.

The audited financial statements of the year ended March 31, 2010 have been prepared on the basis of accounting principles applicable to a going concern, which assumes that the Company will be able to continue in operation for the foreseeable future and will be able to realize its assets and discharge its liabilities in the normal course of business.

Several adverse conditions cast significant doubt upon the validity of this assumption. Consistent with other entities in the exploration stage, the Company has incurred operating losses since inception, has no source of revenue, is unable to self-finance operations, and has significant cash requirements to meet its overhead and continue its exploration activities. Specifically, in order to remain in good standing under its petroleum contract and to maintain the rights to its property, the Company must complete the drilling of two exploration wells on the property, at an estimated cost, including testing, of US\$45 million by April 30, 2011. One of the wells was started and completed subsequent to year end. See note 11 to the audited financial statements.

The Company's ability to continue as a going concern is dependent upon management's ability to secure the additional financing required to fund the drilling of the second exploration well and also to raise additional funding of approximately US\$22.5 million

required for the drilling of the third exploration well prior to April 30, 2013 should the Company decide to proceed with exploration phase 3. While management has been successful in obtaining funding in the past, there can be no assurance that it will be able to do so in the future. Management is investigating funding options, as normal course of business, to address financial shortfall.

If the going concern assumption were not appropriate for the audited financial statements of the Company then adjustments would be necessary to the carrying value of assets and liabilities, the reported expenses and the balance sheet classifications used, and such adjustments would be material.

FINANCIAL INFORMATION

Results of Operation

The Company's results for the financial year ended March 31, 2010 were a loss of \$1,448,046, compared to an income of \$417,602 for the previous year. The turnaround in the result of \$1,865,648 was mainly due to foreign exchange loss of \$625,444 this year vis-à-vis an exchange gain of \$1,044,532 last year. The US\$/C\$ exchange rate fell from 1.263 to 1.015 during the year. Loss per share was \$0.03 (2009 – Earnings per share \$0.01).

Liquidity and Capital Resources

As at March 31, 2010, net current assets of the Company amounted to \$25,452,075, whereas net current assets of \$8,284,794 were recorded in the prior year. The increase in net current assets of \$17,167,281 was mainly due to the increase in cash of \$21,630,647, which was mainly due to the guarantee deposit of \$23,510,311 in respect of the Rights Offering received.

During the year, exploration expenditures of \$4,900,806 (2009 - \$2,664,993) were incurred, and financed mainly from equity. As at March 31, 2010, the total amount of petroleum exploration expenses incurred and capitalized amounted to \$39,312,933 (2009 - \$34,412,127) and may be broken down as follows:

	<u>2010</u>	<u>2009</u>
	\$	\$
Exploration Drilling Related Services		
Drilling services	5,634,766	5,634,766
Drilling technical supervision and evaluation	337,001	318,394
Exploration Geological & Geophysical Surveys & Work		
Geological & geophysical survey acquisition & processing	9,787,442	9,787,442
Technical evaluations & management	4,887,397	4,403,802
Pre-development study	4,902,689	1,610,661
Interests on funding of deferred exploration expenditures	3,548,686	3,549,580
Deferred costs acquired from Primeline Petroleum Corporation	1,394,307	1,394,307
Project administration	2,969,484	2,639,946
Salaries and benefits	4,158,177	3,695,522
Travel and accommodation	1,974,154	1,658,877
Contract signing fee	539,917	539,917
Foreign exchange (gain) loss	(821,087)	(821,087)
	<u>39,312,933</u>	<u>34,412,127</u>

The increase of \$3,292,028 in pre-development study reflected the costs of the ODP undertaken in 2009/10. Technical evaluation and management increased by \$483,595 from the \$4,403,802 recorded in 2009 due to the consultancy work undertaken in relation to the ongoing exploration programme.

Project administration costs may be further broken down as follows:

	<u>2010</u>	<u>2009</u>
	\$	\$
Bank charges	14,215	12,977
Office rental	1,606,944	1,476,026
Office supplies	114,958	91,749
Sundries expenses	372,857	338,997
Postage	31,682	31,086
Professional fees	441,979	349,901
Telecommunications	85,097	75,444
Transportations	271,087	241,251
Utilities	30,665	22,515
	<u>2,969,484</u>	<u>2,639,946</u>

The Company had total assets of \$69,729,437 (2009 - \$43,137,623) which were financed by net shareholders' equity of \$40,829,146 (2009 - \$42,271,804), current liabilities of \$4,964,429 (2009 - \$440,702) and rights issue deposit of \$23,510,311 (2009 - \$nil).

The Private Placement and debt conversion on April 4, 2006 was intended to provide the Company with sufficient funds to complete its minimum commitments under Phase 1 of its exploration program and support its general and administration activities for the year. During 2010, expenditures on petroleum exploration costs of \$2,839,036 were financed from the proceeds of the Private Placement. Compared to 2009, this was \$219,209 lower.

As at March 31, 2010, the Company had net current assets of \$25,452,075 (2009 - \$8,284,794) and had a deficit of \$10,808,230 (2009 - \$9,360,184). The Company has sufficient funds to meet its commitment to drill the first well under the 2nd exploration phase (subsequently drilled in April - June 2010) and to pay for its general and administration activities for the next year. However, additional financing would be required if the Development proceeds or if the Company was to enter into future exploration drilling contracts to fulfil the 2nd well commitment in the 2nd exploration phase and any future drilling plan. Management is investigating funding options to address financial shortfalls.

Financial Instruments

The Company's financial instruments consist of cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities. The fair value of these financial instruments approximates their carrying value due to their short-term maturity or capacity of prompt liquidation.

The Company's financial instruments are exposed to certain financial risks, including currency risk, credit risk, liquidity risk, interest rate risk and price risk.

a) Currency risk

The Company holds US\$135,031 in term deposits which mature in 7 days and cash balances of US\$226,603 and RMB1,983,820.

Based on the above net exposures as at March 31, 2010, and assuming that all other variables remain constant, a 10% depreciation or appreciation of the Canadian dollar against the US dollar and Renminbi would result in an increase/decrease of approximately \$36,706 and \$29,599 respectively in the company's net loss.

b) Credit risk

Credit risk is the risk of an unexpected loss if a customer or third party to a financial instrument fails to meet its contractual obligations.

The Company's cash and cash equivalents are held at a large international financial institution in interest bearing accounts. Minimal cash balances are held in Chinese financial institutions. The company has no investments in asset-backed commercial paper.

c) Liquidity risk

Liquidity risk is the risk that the company will not be able to meet its financial obligations as they fall due.

The Company manages liquidity risk through its capital management as outlined below under the heading "Capital Management". Accounts payable relating to petroleum exploration costs and other accounts payable and accrued liabilities are due within the current operating period.

d) Interest rate risk

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The risk that the Company will realize a loss as a result of a decline in the fair value of the short-term investments included in cash and cash equivalents is minimal because these investments roll over in a very short period (seven days to one month).

e) Price risk

The Company closely monitors commodity prices to determine the appropriate course of action to be taken by the Company.

Capital Management

The Company's objectives when managing capital are to safeguard the Company's ability to continue as a going concern in order to pursue the exploration and development of its petroleum interest, acquire additional petroleum property interests and to maintain a flexible capital structure which optimizes the costs of capital at an acceptable risk. In the management of capital, the Company includes its cash and cash equivalent balances and components of shareholders' equity.

The Company manages the capital structure and makes adjustments to it in light of changes in economic conditions and the risk characteristics of the underlying assets. To maintain or adjust the capital structure, the Company may attempt to issue new shares, issue debt, acquire or dispose of assets or adjust the amount of cash and cash equivalents and investments.

In order to facilitate the management of its capital requirements, the Company prepares annual expenditure budgets that are updated as necessary depending on various factors, including successful capital deployment and general industry conditions. The annual and updated budgets are approved by the Board of Directors.

At this stage of the Company's development, in order to maximize ongoing development efforts, the Company does not pay out dividends.

The Company's investment policy is to invest its cash in highly liquid short-term interest-bearing R1-High investment rated (DBRS) investments with maturities 90 days or less from the original date of acquisition.

The Company currently is not subject to externally imposed capital requirements.

Transactions with Related Parties and Directors

During the year ended March 31, 2010, the Company paid or accrued the following:

- a) London office rent of \$66,335 (2009 - \$72,879) to a company under common control. The shareholder of that company Mr. Victor Hwang, is also the majority shareholder of the Company.
- b) fees and expenses of \$26,062 (2009 - \$27,098) to a company controlled by Mr. Peter Kelty, a director for advisory services relating to investor relations, securities and exchange matters and other administrative services.
- c) cash call of \$2,383,991 received from (2009 – \$238,927 utilized for) a company under common control of which the shareholder of that company is also the shareholder of the Company's ultimate holding company PIHI.

These transactions, which occur in the normal course of operations, are measured at the exchange amount, which is the amount of the consideration established and agreed by the related parties.

Adoption of Recent Canadian Accounting Pronouncements

Financial instruments – Disclosures

During 2009, CICA Handbook Section 3862, Financial Instruments – Disclosures (“Section 3862”) was amended to require disclosures about the inputs to fair value measurements, including their classification within a hierarchy that prioritizes the inputs to fair value measurement. The three levels of the fair value hierarchy are:

- Level 1 – Unadjusted quoted prices in active markets for identical assets or liabilities;

- Level 2 – Inputs other than quoted prices that are observable for the asset or liability either directly or indirectly; and
- Level 3 – Inputs that are not based on observable market data

The Company adopted this amended standard for the year ended March 31, 2010 and required disclosures are included in Note 8 of consolidated financial statements.

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

In January 2009, the CICA issued EIC – 173, *Credit Risk and the Fair Value of Financial Assets and Financial Liabilities*. The guidance requires that an entity’s own credit risk and the credit risk of the counterparty should be taken into account in determining the fair value of financial assets and financial liabilities, including derivative instruments. This guidance is applicable to fiscal periods ending on or after January 20, 2009. Adoption of this section has had no impact on the consolidated financial statements

Goodwill and Intangible Assets

In February 2008, the CICA issued CICA Handbook Section 3064, *Goodwill and Intangible Assets*, which replaces Section 3062, *Goodwill and Other Intangible Assets* and Section 3450, *Research and Development Costs*. Various changes have been made to other sections of the CICA Handbook for consistency purposes. Section 3064 establishes standards for the recognition, measurement, presentation and disclosure of goodwill subsequent to its initial recognition and of intangible assets by profit-oriented enterprises. The new Section was applicable to the Company’s consolidated financial statements for its fiscal year beginning April 1, 2009. There was no material impact of the Company’s consolidated financial statements as a result of adopting this standard.

Future accounting pronouncements

Business Combinations

In January 2009, the CICA issued Section 1582, *Business Combinations*, which replaces former guidance on business combinations. Section 1582 establishes principles and requirements of the acquisition method for business combinations and related disclosures. In addition, the CICA issued Sections 1601, *Consolidated Financial Statements*, and 1602, *Non-Controlling Interests*, which replace the existing guidance. Section 1601 establishes standards for the preparation of consolidated financial statements, while section 1602 provides guidance on accounting for a non-controlling interest in a subsidiary in consolidated financial statements subsequent to a business combination.

These statements apply prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after January 1, 2011 with earlier application permitted. The Company is currently evaluating the new sections to determine the potential impact on its consolidated financial statements.

International Financial Reporting Standards (“IFRS”)

The Company expects to adopt IFRS effective April 1, 2011. In 2011, the Company will have to present 2010 comparative figures restated using IFRS for each comparative period

after the transition date. As a result, the Company began to execute its IFRS implementation plan in 2009.

During 2009, the Company compared its current accounting policies under Canadian Generally Accepted Accounting Principles (“GAAP”) to IFRS and identified differences between the two standards. Based on its review of historical transactions and its current and expected business activities, the Company identified the treatment of Exploration and Evaluation (“E&E”) costs, and asset impairment as areas with the greatest potential to create significant differences in the Company’s financial statements as a result of adopting IFRS.

The Company performed a comprehensive analysis of these areas to determine the potential impact that adopting IFRS will have on the Company’s financial statements.

The International Accounting Standards Board (“IASB”) has still not made a definitive determination as to whether E&E costs should be capitalized or expensed. IFRS 6 allows companies to choose a policy that capitalizes these costs. The policy must be disclosed in the notes to the financial statements. The Company expects to continue capitalizing its E&E costs in a manner consistent with its current accounting policy.

Under Canadian GAAP, Mineral evaluation and exploration costs impairment testing is performed using a two-step test. The first step is to determine if there is an impairment loss by using an undiscounted cash flow analysis. If that analysis identifies an impairment loss, the loss is measured as the amount by which carrying value exceeds fair value. The fair value is often based on discounted cash flows. Under IFRS, assets are tested for impairment using a one-step process based on discounted cash flows. IFRS also allows the reversal of impairment charges from previous years if the fair value exceeds the carrying value of long-lived assets.

Other IFRS that apply to the Company’s operations, but that are not expected to have a significant effect on 2010 financial results based on the Company’s current and expected activities are functional currency, business combinations, share based payments, and decommissioning and retirement obligations.

The Company is still considering the impact that the adoption of IFRS will have on its financial statements.

The Company has performed its review of IFRS based on standards applicable as of the date of this report. The IASB is still developing IFRS and may propose changes to the standards between the date of this report and the date of the Company adopts IFRS. The Company’s assessment of differences between Canadian GAAP and IFRS is based on its historical, current, and expected business activities. Changes in business activities could also lead to unexpected differences to the Company’s financial statements, notes, and other disclosures as reported under Canadian GAAP and IFRS. Changes to business activities or transactions and/or IFRS could have material effects on the Company’s analysis discussed above.

The Company will track the difference between Canadian GAAP and IFRS on individual transactions throughout 2010. It will also analyze the effect of changes in IFRS as they occur. At the end of 2010, the Company will prepare two sets of financial statements. One set will comply Canadian GAAP for reporting purposes. The other set will comply with IFRS for use as comparative figures once the Company adopts IFRS on April 2011.

Subsequent Events

On March 5, 2010, the Company entered into a turnkey drilling contract with China Oilfield Services Ltd. (“COSL”) under which COSL agreed to drill LS35-3-1 well in Block 25/34 at a cost approximately US\$28 million depending on the level of testing required. The drilling started on April 12, 2010 and the COSL rig was released on June 7, 2010 after completion of end-of-well operations. The actual cost incurred by the Company, testing included is US\$21 million.

On March 25, 2010, the Company filed a preliminary short form prospectus in the provinces of British Columbia, Alberta, Ontario and Quebec relating to a rights offering (the “Offering”) to raise gross proceeds of C\$23,510,311. According to the Offering, each holder of the Company’s common shares (“Shares”) would be entitled to receive one right (a “Right”) for each Share held. One Right would entitle the holder to acquire one Share at a price of \$0.50 per share (the “Subscription Price”). The Company’s largest shareholder, Primeline International (Holdings) Inc. (“Primeline International”), had agreed to provide a standby commitment (the Standby Guarantee”) under which Primeline International would purchase from the Company at the Subscription Price any Shares (the “Standby Shares”) that are not otherwise subscribed for under the Offering. Accordingly, Primeline International deposited C\$23,510,311 into the Company’s bank account on March 26, 2010 as deposit for the Standby Guarantee.

The rights were issued to holders of common shares of record on April 15, 2010 and expired on May 6, 2010. Under the Offering, shareholders subscribed for and purchased 39,640,833 common shares resulting in gross proceeds of C\$19,820,416.50. Under the Standby Guarantee Agreement with the Company, Primeline International purchased the balance of 7,379,790 common shares available under Offering for gross proceeds of C\$3,689,895. Aggregate gross proceeds of C\$23,510,311.50 were received by the Company.

The SDA signed between CNOOC, the Company and PPC was ratified by Ministry of Commerce of PRC and became effective on June 13, 2010. All other related Development Agreements became effective the same date. CNOOC, on behalf of itself, the Company and PPC signed a Framework Agreement for Gas Sale and Purchase from LS 36-1 gas field on July 7, 2010, replacing the previous binding Gas Sale Agreement in principle.

Outstanding Share Data

On April 4, 2006, the Company granted 4,500,000 options at an exercise price of \$1.50 per share to directors, officers, employees and consultants, of which 4,300,000 options are outstanding and will expire on April 4, 2011.

On December 1, 2006, the Company awarded options to its non-executive directors, management and consultants to purchase up to 1,200,000 common shares at an exercise price of \$1.60 per share of which 217,000 options have been cancelled by agreement with the option holders, 433,000 options expired on May 31, 2008 and the balance of 550,000 options will expire on November 30, 2011.

On November 1, 2007, the Company awarded options to purchase a total of 875,000 common shares at an exercise price of \$2.00 per share, of which 250,000 options were awarded to CHF Investor Relations, the Company’s investor relations counsel, and 625,000 options were

awarded to certain of its executive directors, management and consultants. All such options will expire on October 31, 2012.

As at July 22, 2010, there are 94,041,246 common shares and 5,725,000 stock options outstanding.

Quarter ended March 31, 2010

The Company realized a loss of \$469,400 for the quarter ended March 31, 2010 compared to a loss of \$3,639 for the same period last year. The increase of \$465,761 in loss can be attributed mainly to an increase of \$343,143 in foreign exchange loss and an increase of \$104,183 in legal and professional fees.

During the quarter exploration expenditure of \$2,073,341 were incurred, comprising mainly of technical evaluation and management of \$167,668, pre-development feasibility study expenses of \$1,685,759 and salaries and benefits of \$123,005. These amounts were capitalized as petroleum exploration expenses.

Selected Annual Information

The following information were extracted from the Company's consolidated audited financial statements:

Years Ended March 31,	2010 \$	2009 \$	2008 \$
Net (loss) income	(1,448,046)	417,602	(1,956,299)
Per basic share	(0.03)	0.01	(0.040)
Per diluted share	(0.03)	0.01	(0.040)
Total assets	69,729,437	43,137,623	43,153,082
Total long-term financial liabilities	23,935,862	425,117	404,428

The increase in loss of \$1,865,648 between 2010 and 2009 was mainly due to foreign exchange loss of \$625,444 this year vis-à-vis an exchange gain of \$1,044,532 last year.

Summary of Quarterly Results (Unaudited)

Quarter Ended	2010 Mar 31 \$	2009 Dec 31 \$	2009 Sep 30 \$	2009 Jun 30 \$
Net (loss) income	(469,400)	(270,558)	(326,125)	(381,963)
Per basic share	(0.010)	(0.005)	(0.007)	(0.008)
Per diluted share	(0.010)	(0.005)	(0.007)	(0.008)

Quarter Ended	2009 Mar 31 \$	2008 Dec 31 \$	2008 Sep 30 \$	2008 Jun 30 \$
Net income (loss)	(3,639)	581,285	130,847	(290,891)
Per basic share	0.000	0.012	0.003	(0.006)
Per diluted share	0.000	0.012	0.003	(0.006)

The loss for the quarter ended March 31, 2010 of \$469,400 was mainly attributable to office expenses of \$46,283, professional fees of \$236,092 and foreign exchange loss of \$154,553.

The loss for the quarter ended March 31, 2009 of \$3,639 was mainly attributable to office expenses of \$29,819, professional fees of \$131,909 and business promotion of \$30,000, offset by foreign exchange gain of \$188,590.

The profit for the quarter ended December 31, 2008 of \$581,285 was mainly due to exchange gain of \$749,770, partially offset by office expenses of \$82,174 and professional fees of \$70,844.

PEHI has an investor relations counsel, CHF Investor Relations (www.chfir.com) which handles the Company's corporate communications in Canada. Phone: +1 416.868.1079; Fax: +1 416.868.6198. PEHI has a website at www.primelineenergy.com or www.pehi.com. The site features information on PEHI, new releases, background information and a technical summary of the project.