FALCON OIL & GAS LTD.

Interim Consolidated Financial Statements

Three and Nine Months Ended September 30, 2010 and 2009

(Presented in U.S. Dollars)

FALCON OIL & GAS LTD.
INTERIM CONSOLIDATED BALANCE SHEETS
(U.S. Dollars, in thousands)
(Unaudited)

ASSETS	September 30, 2010	December 31, 2009
Current assets		
Cash and cash equivalents	$ 8,413	$ 11,804
Restricted cash	51	1,184
Amounts receivable (Note 4)	1,362	2,955
Prepaids and other	376	720
Inventory available for sale	2,571	4,196
Total current assets	12,773	20,859
Property and equipment		
Petroleum and natural gas properties, net (Note 3)	175,514	207,889
Pipeline and facilities	3,888	3,888
Furniture and equipment, net	1,814	2,086
Total property and equipment	181,216	213,863
Other assets	758	8,277
Total assets	$ 194,747	$ 242,999

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

FALCON OIL & GAS LTD.
INTERIM CONSOLIDATED BALANCE SHEETS (CONTINUED)
(U.S. Dollars, in thousands)
(Unaudited)

LIABILITIES AND SHAREHOLDERS' EQUITY	September 30, 2010	December 31, 2009
Current liabilities		
Accounts payable and accrued expenses	$ 7,062	$ 2,683
Long-term liabilities		
Convertible debentures (Note 5)	5,186	4,031
Asset retirement obligations (Note 6)	6,441	6,106
Total long-term liabilities	11,627	10,137
Total liabilities	18,689	12,820
Shareholders' equity (Note 7)		
Share capital	331,215	331,215
Contributed surplus	35,649	31,829
Equity component of convertible debentures (Note 5)	5,057	5,057
Deficit	(206,920)	(137,922)
	165,001	230,179
Non-controlling interest	11,057	-
Total shareholders' equity	176,058	230,179
Total liabilities and shareholders' equity	$ 194,747	$ 242,999

Going concern (Note 1)

Commitments and contingencies (Notes 1 & 12)

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

FALCON OIL & GAS LTD.
(A Development Stage Company)
INTERIM CONSOLIDATED STATEMENTS OF OPERATIONS, COMPREHENSIVE LOSS AND DEFICIT
(U.S. Dollars, in thousands, except share and per share amounts)
(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	**2009**	**2010**	**2009**
Petroleum revenue	$ 12	$ 7	$ 24	$ 27
Costs and expenses				
Production costs	5	11	14	30
General and administrative	2,259	3,226	8,861	9,649
Stock-based compensation	633	1,611	3,819	4,573
Impairment of petroleum and natural gas properties (Note 3)	51,000	-	51,000	45
Depreciation, depletion and accretion	205	214	636	627
Writedown of inventory available for sale	967	-	967	-
Write off of receivable (Note 3)	4,345	-	4,345	-
	59,414	5,062	69,642	14,924
Other income (expense)				
Interest expense	(372)	(331)	(1,707)	(331)
Interest income	8	40	39	307
Gain (loss) on foreign exchange	(525)	518	(683)	2,501
Other income (expense)	(334)	59	(446)	169
	(1,223)	286	(2,797)	2,646
Net loss and comprehensive loss	$ (60,625)	$ (4,769)	$ (72,415)	$ (12,251)
Net loss and comprehensive loss attributable to:				
Owners of the Company	$ (60,533)	$ (4,769)	$ (71,949)	$ (12,251)
Non-controlling interest	(92)	-	(466)	-
Net loss and comprehensive loss	$ (60,625)	$ (4,769)	$ (72,415)	$ (12,251)
Deficit, beginning of period	$(146,387)	$ (81,476)	$(137,922)	$ (73,994)
Net loss and comprehensive loss	(60,533)	(4,769)	(71,949)	(12,251)
Non-controlling interest dilution gain	-	-	2,951	-
Deficit, end of period	$(206,920)	$ (86,245)	$(206,920)	$ (86,245)
Net loss per common share – basic and diluted	$ (0.101)	$ (0.008)	$ (0.119)	$ (0.021)
Weighted average number of common shares outstanding – basic and diluted	602,216,801	598,963,758	602,216,801	596,865,711

The accompany notes are an integral part of these consolidated financial statements.

FALCON OIL & GAS LTD.
INTERIM CONSOLIDATED STATEMENTS OF CASH FLOWS
(U.S. Dollars, in thousands)
(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2010	**2009**	**2010**	**2009**
Cash flows from operating activities				
Net loss inclusive of non-controlling interest	$ (60,625)	$ (4,769)	$ (72,415)	$ (12,251)
Items not involving cash:				
Stock-based compensation	633	1,611	3,819	4,573
Depreciation, depletion and accretion	205	212	636	625
Impairment of petroleum and natural gas properties	51,000	-	51,000	45
Write off of receivable	4,345	-	4,345	-
(Gain) loss on foreign exchange	525	(518)	683	(2,501)
Accretion on convertible debentures	90	316	722	316
Amortization of deferred financing costs	27	93	212	93
Other	-	-	3	-
Changes in non-cash working capital accounts				
Amounts receivable	478	(300)	1,517	8,196
Prepaids and other	(99)	31	367	409
Writedown of inventory available for sale	967	-	967	-
Inventory available for sale	200	-	658	147
Other assets	387	-	830	-
Accounts payable and accrued expenses	320	(2,780)	61	(10,471)
Net cash provided by (used in) operating activities	(1,547)	(6,104)	(6,595)	(10,819)
Cash flows from investing activities				
Petroleum and natural gas properties	(458)	(4,203)	(2,651)	(6,760)
Furniture and equipment	(23)	(11)	(46)	(179)
Other assets	-	40	-	(183)
Net cash provided by (used in) investing activities	(481)	(4,174)	(2,697)	(7,122)
Cash flows from financing activities				
Restricted cash	-	(1,895)	1,132	(2,915)
Proceeds from unit offering, net	-	-	-	10,302
Proceeds from unit offering by subsidiary, net	(9)	-	4,438	-
Proceeds from exercise of warrants and stock options	-	1,275	-	1,275
Offering costs	-	(54)	-	(1,385)
Net cash provided by (used in) financing activities	(9)	(674)	5,570	7,277
Effect of exchange rates on cash	294	749	331	789
Cash and cash equivalents				
Net increase (decrease)	(1,743)	(10,203)	(3,391)	(9,875)
Beginning of period	10,156	25,875	11,804	25,547
End of period	$ 8,413	$ 15,672	$ 8,413	$ 15,672

The accompany notes are an integral part of these consolidated financial statements.

FALCON OIL & GAS LTD.
INTERIM CONSOLIDATED STATEMENTS OF CASH FLOWS
(U.S. Dollars, in thousands)
(Unaudited)

	Three Months Ended September 30, 2010	Three Months Ended September 30, 2009	Nine Months Ended September 30, 2010	Nine Months Ended September 30, 2009
Supplemental schedule of cash flow information:				
Cash paid for interest	$ -	$ -	$ 510	$ -
Supplemental disclosures of non-cash investing and financing activities				
Acquisition of 25% working interest in Beetaloo Basin:				
Issuance of stock in Falcon Oil & Gas Australia Limited	$ -	$ -	$ 10,000	$ -
JIB receivable (Note 3)	-	-	1,725	-
	$ -	$ -	$ 11,725	$ -
Services exchanged for stock in Falcon Oil & Gas Australia Limited	$ -	$ -	$ 170	$ -
Acquisition of 25% working interest in Beetaloo Basin:				
Note receivable	$ -	$ -	$ -	$ 5,000
Other assets	-	-	-	405
Asset retirement obligation	-	-	-	(98)
	$ -	$ -	$ -	$ 5,307
Agent warrants issued in Unit offering reflected in other assets and share capital	$ -	$ -	$ -	$ 263
Inventory available for sale reclassified to petroleum and natural gas properties	$ -	$ -	$ -	$ 600

The accompany notes are an integral part of these consolidated financial statements.

NOTE 1 – ORGANIZATION AND GOING CONCERN

Falcon Oil & Gas Ltd. ("Falcon"), incorporated under the laws of British Columbia on January 18, 1980, is considered a development stage company as defined by Canadian Institute of Chartered Accountants (CICA) Accounting Guideline No. 11.

As of September 30, 2010, the Company has producing petroleum and natural gas properties in Alberta, Canada and exploration projects in Hungary and Australia. The Company's exploration projects in Hungary and Australia continue to be evaluated, and management believes that the carrying costs of these projects are recoverable. Should the Company be unsuccessful in these exploration activities, the carrying cost of these prospects may be charged to operations.

The Company is in the business of acquiring, exploring and developing petroleum and natural gas properties which, by its nature, involves a high degree of risk, and there can be no assurance that current exploration programs will result in profitable operations. The recoverability of the carrying value of the petroleum and natural gas properties and the Company's continued existence is dependent upon the preservation of its interests in the underlying properties, the discovery of economically recoverable reserves, the achievement of profitable operations, or the ability of the Company to obtain financing or, alternatively, upon the Company's ability to economically dispose of its interests. Certain of the Company's petroleum and natural gas properties are subject to the risks associated with foreign investment, including increases in taxes and royalties, renegotiation of contracts, currency exchange fluctuations and political uncertainty.

GOING CONCERN

For the nine months ended September 30, 2010, the Company incurred a net loss attributable to the owners of the Company of $71,949 and, as at September 30, 2010, had a deficit of $206,920 and working capital of $5,711. The Company has focused on securing equity financing and a joint venture partner for its operations in the Beetaloo Basin located in the Northern Territory, Australia, and a joint venture partner for its operations in the Makó Trough located in Hungary.

In the near term, the Company's ability to continue as a going concern is dependent upon its ability to raise additional capital to fund its operations. Additional capital may be sought from existing shareholders and/or from the sale of additional common shares or other debt or equity instruments and/or direct financing of its' subsidiaries (See Note 7 below). There is no assurance such additional capital will be available to the Company on acceptable terms or at all. On November 24, 2010, Falcon entered into an agreement to raise up to CDN$63,000 in the form of units (See Note 13). Upon successful completion of the transaction, which is subject to all necessary corporate, regulatory and governmental approvals, including TSX Venture Exchange ("TSX-V") acceptance of the filing, the Company should have sufficient funds to mitigate its current liquidity weakness, including being able to fund its planned exploration activities in Australia, Hungary and South Africa.

In the longer term, the recoverability of the carrying value of the Company's long-lived assets is dependent upon the Company's ability to preserve its interest in the underlying petroleum and natural gas properties, the discovery of economically recoverable reserves, the achievement of profitable operations, and the ability of the Company to obtain financing to support its acquisition, exploration, development and production activities, and ongoing operations.

These consolidated financial statements are prepared in accordance with Canadian generally accepted accounting principles ("Canadian GAAP") appropriate for a going concern. The going concern basis of accounting assumes the Company will continue to realize the value of its assets and discharge its liabilities and other obligations in the ordinary course of business. Should the Company be required to realize the value of its assets in other than the ordinary course of business, the net realizable value of its assets may be materially less than the amounts shown in the consolidated financial statements. These consolidated financial statements do not include any adjustments to the amounts and classifications of assets, liabilities and expenses that may be necessary should the Company be unable to realize its assets, repay its liabilities and meet its other obligations in the ordinary course of business or continue operations.

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

BASIS OF PRESENTATION

The accompanying consolidated financial statements include Falcon and its wholly owned subsidiaries: Mako Energy Corporation ("Mako"), a Delaware company, TXM Oil and Gas Exploration Kft., a Hungarian limited liability company doing business as TXM Energy, LLC ("TXM"), TXM Marketing Trading & Service, LLC ("TXM Marketing"), a Hungarian limited liability company, FOG-TXM Kft. ("FOG-TXM"), a Hungarian limited liability company; and its majority owned subsidiary, Falcon Oil & Gas Australia Limited ("Falcon Australia"), (collectively "the Company"). All significant intercompany transactions and balances have been eliminated on consolidation.

The interim consolidated financial statements of the Company have been prepared by management in accordance with accounting principles generally accepted in Canada. The interim consolidated financial statements have been prepared following the same accounting policies and methods of computation as the consolidated financial statements for the year ended December 31, 2009. The disclosures which follow are incremental to the disclosures included in the December 31, 2009 consolidated financial statements. These interim consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto for the year ended December 31, 2009.

COMPARATIVE FIGURES

Certain comparative figures have been reclassified, where applicable, to conform to the current period's presentation. Such reclassifications had no effect on the Company's net loss in any of the periods presented.

BUSINESS COMBINATIONS, CONSOLIDATED FINANCIAL STATEMENTS AND NON-CONTROLLING INTERESTS

The CICA issued three new accounting standards in January 2009: Section 1582, Business Combinations ("Section 1582"), Section 1601, Consolidated Financial Statements ("Section 1601"), and Section 1602, Non-controlling Interests ("Section 1602"). These new standards will be effective for fiscal years beginning on or after January 1, 2011.

Section 1582 replaces Section 1581, Business Combinations, and establishes standards for the accounting for a business combination. It provides the Canadian equivalent to International Financial Reporting Standard IFRS 3 – Business Combinations. The section applies 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.

Sections 1601 and 1602 together replace Section 1600, Consolidated Financial Statements. Section 1601 establishes standards for the preparation of consolidated financial statements. Section 1601 applies to interim and annual consolidated financial statements relating to fiscal years beginning on or after January 1, 2011. Section 1602 establishes standards for accounting for a non-controlling interest in a subsidiary in consolidated financial statements subsequent to a business combination. It is equivalent to the corresponding provisions of International Financial Reporting Standard IAS 27 – Consolidated and Separate Financial Statements and applies to interim and annual consolidated financial statements relating to fiscal years beginning on or after January 1, 2011.

In August 2009, the CICA issued certain amendments to Section 3251, Equity. The amendments apply to entities that have adopted Section 1602, Non-controlling interests ("Section 1602"). The amendments require separate presentation on the consolidated statements of operations and comprehensive loss of loss attributable to owners of the Company and those attributable to non-controlling interests. The amendments also require that non-controlling interests be presented separately as a component of equity.

Although not mandatory until the year beginning January 1, 2011, the Company has adopted Sections 1582, 1601 and 1602, and reflected the impact of Section 1602 in the accompanying consolidated financial statements. There was no impact as a result of the adoption of Sections 1582 and 1601.

(U.S. Dollars, in thousands, except share and per share amounts)

NOTE 3 – PETROLEUM AND NATURAL GAS PROPERTIES

Interests in petroleum and natural gas proven and unproven properties include the following acquisition, exploration and development costs:

	Hungary	Canada	Australia	South Africa	Total
December 31, 2009	**$ 168,528**	**$ 47**	**$ 39,314**	**$ -**	**$ 207,889**
Acquisition costs	-	-	11,725	16	11,741
Exploration costs (Note 12)	5,588	-	950	329	6,867
Development costs	-	-	-	-	-
Asset retirement obligation	-	-	18	-	18
Impairment	(51,000)	-	-	-	(51,000)
Depletion and depreciation	-	(1)	-	-	(1)
September 30, 2010	**$ 123,116**	**$ 46**	**$ 52,007**	**$ 345**	**$ 175,514**

Capitalized interest totaled $348 for the three and nine months ended September 30, 2009. There was no capitalized interest during 2010.

The Company's Canadian properties are all proven and are subject to a ceiling test; the Company's properties in Hungary and Australia are unproven.

Impairment

As of September 30, 2010, the Company determined that the carrying value of the Hungarian petroleum and natural gas properties exceeded its estimated recoverable amount. Consequently, during the third quarter of 2010, the Company reflected an impairment of petroleum and natural gas properties of $51,000 in its consolidated statement of operations, with a corresponding reduction to petroleum and natural gas properties in the consolidated balance sheet as of September 30, 2010.

Associated with its property in Hungary, the Company has reflected as a charge to the consolidated statement of operations costs of $4,345 resulting from the Production Development Agreement, with a corresponding reduction to other assets in the consolidated balance sheet as of September 30, 2010.

HUNGARY

TXM holds a long-term Mining Plot (the "Production License") granted by the Hungarian Mining Authority. The lands within the Production License were formerly part of TXM's two petroleum and natural gas exploration licenses – the Tisza License and the Makó License (collectively, the "Exploration Licenses"). The Production License, covering approximately 245,700 acres, gives TXM the exclusive right to explore for and appraise petroleum and natural gas on properties located in south central Hungary near the town of Szolnok. The Production License further gives TXM the exclusive right to commercially develop petroleum and natural gas within the area covered by that license.

NOTE 3 – PETROLEUM AND NATURAL GAS PROPERTIES (CONTINUED)

The Exploration Licenses expired on December 31, 2009 and are not eligible for extension. However, under Hungarian laws applicable to oil and gas exploration licenses, the licensee has the first priority in obtaining a mining plot covering all or part of the area, but is not guaranteed that it will receive a mining plot. The Company has filed the required closing report within six months from the expiration of the license, and is considering the filing of an application for the mining plot by year end.

In October 2009, the Hungarian Mining Authority granted the Company's application to expand the depths under the Production License. When originally issued in May 2007, the upper depth of the Production License was defined as 9,186 feet (2,800 meters) from the surface, and extended to the basement of the Basin Centered Gas Accumulation (the "BCGA"). As a result of additional technical analysis, including extensive review of 3D seismic and the data obtained from the wells previously drilled within the Production License, the amended Production License now incorporates depths beginning at 7,546 feet (2,300 meters) throughout the entire Production License. This revision makes the Production License depth consistent with other mining plots in the immediate area.

AUSTRALIA

On April 23, 2010, Falcon Australia received notice (the "Notice") from the Department of Resources, Northern Territory Government, that it became the registered owner of the final 25% working interest in four exploration permits ("the Permits"), comprising 7,000,000 acres in the Beetaloo Basin, Northern Territories, Australia, of which it had a 75% working interest in. The final transfer of ownership was pursuant to Binding Heads of Agreement (the "Agreement") entered into on December 7, 2009, between Falcon and Falcon Australia, and PetroHunter Energy Corporation and Sweetpea Petroleum Pty Ltd ("Sweetpea"), PetroHunter's wholly owned subsidiary, (collectively "PetroHunter related entities, as the largest single shareholder of PetroHunter at the time of the transaction is also the President and CEO of the Company. Under the Agreement, Falcon Australia issued to Sweetpea 50 million common shares of Falcon Australia (valued at $10 million) and Sweetpea settled a $1,725 obligation to Falcon Australia, for its share of joint interest billings to re-enter the Shenandoah-1 well, as additional consideration for the transfer of Sweetpea's undivided 25% working interest in the Permits. Falcon has been issued 150 million shares of Falcon Australia for conversion of a portion ($30,000) of Falcon Australia's debt payable to Falcon, which approximates Falcon's initial acquisition cost previously paid to Sweetpea for the 75% working interest in the Permits held by Falcon Australia as of the date of the Agreement. Falcon Australia now owns 100% of the Permits.

Under a revised work program approved by the Northern Territory of Australia Government, Department of Resources in June 2010, the Company's required minimum work program obligations, in order to continue to hold the underlying Permits in the Beetaloo Basin, is to expend $10,100 and $5,000 during the years ending December 31, 2011 and 2012, respectively.

SOUTH AFRICA

On October 27, 2009, Falcon secured a Technical Cooperation Permit (the "TCP") to evaluate the Karoo Basin in central South Africa. Falcon had up to one year to conduct a technical appraisal of the area covered by the TCP, which did not include any well or seismic work obligations. At or before the end of the one year period, Falcon had the exclusive option to apply for an exploration permit covering all or a portion of the TCP. Falcon submitted its application which was accepted on September 7, 2010. Upon receipt of an approved exploration permit, the Company will be required to make a minimum payment of approximately $400, and obtain an approved work program. The TCP covers approximately 7.5 million acres and is located approximately 120 miles northeast of Cape Town, South Africa.

(U.S. Dollars, in thousands, except share and per share amounts)

NOTE 4 – AMOUNTS RECEIVABLE

Amounts receivable at September 30, 2010 and December 31, 2009 is comprised of the following:

	2010	2009
Joint interest owners	$ 205	$ 856
VAT and GST	935	1,131
Sale of inventory	-	350
Other	222	618
	$ 1,362	$ 2,955

NOTE 5 – CONVERTIBLE DEBENTURES

Convertible debentures at September 30, 2010 and December 31, 2009 are comprised of the following:

	2010	2009
Face amount	$ 9,272	$ 9,272
Discount – equity component of convertible debentures	(5,057)	(5,057)
Accretion on convertible debentures and amortization of offering costs	1,751	817
Foreign exchange adjustment	714	493
Offering costs attributable to convertible debentures	(1,494)	(1,494)
	$ 5,186	$ 4,031

The discount and the offering costs are being accreted and amortized to interest expense over the term of the convertible debentures.

NOTE 6 – ASSET RETIREMENT OBLIGATIONS

At September 30, 2010, the estimated total undiscounted amount required to settle the asset retirement obligations was $9,135. Costs for asset retirement have been calculated assuming an inflation rate ranging from 3.0% to 5.0%. These obligations will be settled based on the estimated useful lives of the underlying assets, which extend up to 20 years into the future. Obligations have been discounted using a credit-adjusted risk-free interest rate ranging from 6.5% to 18.0%. Changes to asset retirement obligations for the nine months ended September 30, 2010 and the year ended December 31, 2009 were as follows:

	2010	2009
Asset retirement obligations – beginning of period	$ 6,106	$ 5,285
Liabilities incurred	19	583
Revisions to estimates	-	-
Liabilities settled	-	-
Liabilities conveyed	-	(97)
Accretion	316	335
Asset retirement obligations – end of period	$ 6,441	$ 6,106

(U.S. Dollars, in thousands, except share and per share amounts)

NOTE 7 – SHAREHOLDERS' EQUITY

AUTHORIZED

The Company has authorized an unlimited number of common shares, without par value.

WARRANTS

A summary of the number of common shares reserved pursuant to the Company's outstanding share purchase warrants for the nine months ended September 30, 2010 and the year ended December 31, 2009 is as follows:

	2010	2009
Balance, beginning of period	1,250,550	4,288,750
Agent warrants	-	1,250,550
Warrants exercised	-	(3,440,000)
Warrants expired	-	(848,750)
Balance, end of period	1,250,550	1,250,550

Common shares reserved for share purchase warrants outstanding as of September 30, 2010 are as follows:

Number of Shares	Exercise Price	Expiry Date
1,250,550	$0.52 (CDN$0.60)	June 30, 2011

STOCK BASED COMPENSATION

The Company, in accordance with the policies of the TSX-V, may grant options to directors, officers, employees and consultants, to acquire up to 10% of the Company's issued and outstanding common stock. The exercise price of each option is based on the market price of the Company's stock at the date of grant, which may be less a discount in accordance with TSX-V policies. The exercise price of all options granted has been based on the market price of the Company's stock at the date of grant, and no options have been granted at a discount to the market price. The options can be granted for a maximum term of five years. The Company records compensation expense over the vesting period based on the fair value of options granted. These amounts are recorded as contributed surplus. Any consideration paid on the exercise of these options is recorded as share capital together with the related contributed surplus associated with the exercised options. Of the 4,725,000 options granted during the nine months ended September 30, 2010, 33⅓% vested at the date of grant and 33⅓% will vest on the next two anniversary dates thereafter, with a term of five years. There were no options granted during the nine months ended September 30, 2009.

(U.S. Dollars, in thousands, except share and per share amounts)

NOTE 7 – SHAREHOLDERS' EQUITY (CONTINUED)

A summary of the Company's stock option plan as of September 30, 2010 and December 31, 2009, and changes during the nine months and the year then ended, is presented below:

	2010		2009	
	Options	**Weighted-Average Exercise Price**	**Options**	**Weighted-Average Exercise Price**
Outstanding at beginning of period	41,975,000	$1.48	46,950,000	$1.90
Granted	4,725,000	$0.16	-	-
Exercised	-	-	-	-
Expired	(20,156,667)	$0.77	(3,195,000)	$3.11
Forfeited	(823,333)	$1.54	(1,780,000)	$2.07
Outstanding at end of period	25,720,000	$1.80	41,975,000	$1.48
Options exercisable at end of period	17,821,133	$2.20	32,576,000	$1.40

The following summarizes information about stock options outstanding and exercisable at September 30, 2010:

Options Outstanding	Options Exercisable	Exercise price	Weighted average remaining contractual life	Expiry date
1,450,000	1,450,000	$0.50	0.05 years	October 21, 2010
5,999,000	5,999,000	$3.98	0.60 years	May 7, 2011
3,241,000	2,592,800	$2.83	1.19 years	December 9, 2011
600,000	360,000	$0.54	1.88 years	August 17, 2012
1,000,000	600,000	$0.98	2.60 years	May 6, 2013
8,785,000	5,271,000	$1.19	2.68 years	June 5, 2013
4,645,000	1,548,333	$0.16	4.92 years	August 30, 2015
25,720,000	17,821,133			

At September 30, 2010, the weighted average remaining contractual life of stock options outstanding was 2.24 years.

The Company measures compensation costs using the fair value-based method for employee and non-employee stock options. Compensation costs have been determined based on the fair value of the options at the grant date, for employees, and at the balance sheet date for non-employees using the Black-Scholes option-pricing model.

Option-pricing models require the use of estimates and assumptions including the expected volatility of the Company's share price, the expected life of the option and the risk free interest rate. Changes in the underlying assumptions can materially affect the fair value estimates.

(U.S. Dollars, in thousands, except share and per share amounts)

NOTE 7 – SHAREHOLDERS' EQUITY (CONTINUED)

The following assumptions were used to calculate the fair value of stock options granted during the nine months ended September 30, 2010:

	2010
Expected life of options	3.25 to 5.00 years
Risk-free interest rate	2.06%
Annualized volatility	112%
Dividend rate	nil
Estimated forfeiture rate	nil

FALCON AUSTRALIA OFFERING

In January 2010, Falcon Australia commenced the private placement sale of up 50 million shares of its common stock ("FA Share") to sophisticated or professional investors within the meaning of sections 708(8) and 708(11) of the Corporations Act 2001 (Australia) pursuant to an Offer Memorandum (the "Offer"), at a price of $1.00 per FA Share with an attached option. Each option entitles the holder to acquire one additional FA Share in respect of each FA Share sold, exercisable at $1.25 for a period of three years from date of issue. The acting broker to the Offer received as a brokerage fee 6.5% of the funds raised in the Offer together with Options (on the same terms as issued to investors), calculated at 6.5% of the number of shares issued in the Offer. The July 31, 2010 closing date has been extended to September 30, 2010.

In June 2010, Falcon Australia closed on initial gross proceeds from the Offer of $4,896, before costs of the offering of $591. The proceeds from the Offer are to be utilized for operations in Australia.

As of September 30, 2010, an additional $1,218 of gross proceeds from the Offer has been received, and is being held in escrow by the acting broker, pending release after final regulatory approval.

NON-CONTROLLING INTEREST

At September 30, 2010, non-controlling interest in Falcon Australia is comprised of the following:

	Shares	**Amount**
Issuance of shares to Sweetpea for 25% working interest	50,000,000	$ 10,984
Issuance of shares for services	250,000	55
Sale of shares pursuant to offer memorandum	4,895,659	1,075
Costs of offer memorandum	-	(591)
Net loss attributable to non-controlling interest	-	(466)
	55,145,659	$ 11,057

Deficit has been credited $2,951 for the dilution gain attributable to the change in ownership of Falcon Australia.

(U.S. Dollars, in thousands, except share and per share amounts)

NOTE 7 – SHAREHOLDERS' EQUITY (CONTINUED)

SUBSEQUENT EVENTS

On August 3, 2010 and November 10, 2010, the Company agreed to issue 1,000,000 and 4,000,000 shares of common stock, respectively, to two past officers; those shares have yet to be issued.

NOTE 8 – RELATED PARTY TRANSACTIONS

Unless otherwise stated, transactions between related parties are measured at the exchange amount, being the amount of consideration agreed to between the parties.

During the nine months ended September 30, 2010, the Company incurred $100 (2009-$226) to a current director (2009 – two directors) for advisory and consulting services rendered.

During the nine months ended September 30, 2010, the Company acquired the final 25% working interest in the Beetaloo Basin Permits from PetroHunter (See Note 3).

NOTE 9 – SEGMENT INFORMATION

All of the Company's operations are in the petroleum and natural gas industry with its principal business activity being in the acquisition, exploration and development of petroleum and natural gas properties. The Company has producing petroleum and natural gas properties located in Canada and considers the results from its operations to relate to the petroleum and natural gas properties. The Company has unevaluated petroleum and natural gas properties in Hungary and Australia. An analysis of the Company's geographic areas is as follows:

	Hungary	Canada	Australia	United States	South Africa	Total
Nine Months ended September 30, 2010						
Revenue	$ 4	$ 20	$ -	$ -	$ -	$ 24
Net income (loss)	(60,241)	(6,863)	(2,407)	(2,438)	-	(71,949)
As of September 30, 2010						
Capital assets	128,431	46	52,007	387	345	181,216

	Hungary	Canada	Australia	United States	Romania	Total
Nine Months ended September 30, 2009						
Revenue	$ -	$ 27	$ -	$ -	$ -	$ 27
Net income (loss)	(1,792)	(5,124)	(163)	(5,127)	(45)	(12,251)
As of September 30, 2009						
Capital assets	217,819	51	37,971	562	-	256,403

(U.S. Dollars, in thousands, except share and per share amounts)

NOTE 10 –FINANCIAL INSTRUMENTS

(a) Fair value

The fair value of financial instruments at September 30, 2010 and December 31, 2009 is summarized in the following table. Fair value estimates are made at the balance sheet date, based on relevant quoted market and other information about the financial instruments.

	September 30, 2010		December 31, 2009	
	Carrying Value	**Fair Value**	**Carrying Value**	**Fair Value**
Financial assets:				
Held for trading				
Cash and cash equivalents and restricted cash	$ 8,464	$ 8,464	$ 12,988	$ 12,988
Loans and receivables				
Amounts receivable	1,362	1,362	2,955	2,955
Financial liabilities:				
Other financial liabilities				
Accounts payable and accrued liabilities	7,062	7,062	2,683	2,683
Convertible debentures (face value - $9,272)	5,186	9,800	4,031	10,217

(b) Financial risk disclosures

The Company thoroughly examines the various financial instrument risks to which it is exposed and assesses the impact and likelihood of those risks. These risks may include credit risk, liquidity risk, currency risk and interest rate risk. Where material, these risks are reviewed and monitored by the Board of Directors.

Credit Risk

The Company's credit risk is limited to cash and receivables. The Company maintains cash accounts at four financial institutions. The Company periodically evaluates the credit worthiness of financial institutions, and maintains cash accounts only in large high quality financial institutions, thereby reducing exposure for deposits in excess of federally insured amounts. On occasion, the Company may have cash in banks in excess of federally insured amounts. The Company believes that credit risk associated with cash is minimal. Receivables are not significant to the Company. The Company's credit risk has not changed significantly since year end.

Liquidity Risk

The Company has in place a planning and budgeting process to help determine the funds required to support the Company's normal operating requirements on an ongoing basis and its planned capital expenditures. The Company's overall liquidity risk has not changed significantly since year end.

NOTE 10 –FINANCIAL INSTRUMENTS (CONTINUED)

Currency Risk

Financial instruments that impact the Company's net income (loss) and comprehensive income (loss) due to currency fluctuations include Canadian dollar, Hungarian forint, Euro and Australian dollar denominated cash and cash equivalents, accounts receivable, reclamation deposits, accounts payable, and capital commitments for Hungarian and Australian operations.

The Company has a CDN$5.3 million convertible debenture, which exposes Falcon to fluctuations in exchange rates between Canadian and U.S. dollars. Such an exposure does also arise as a result of revenue being realized in and expense items, including certain general and administrative and production costs and interest expense on the convertible debt, being incurred in Canadian dollars. A one cent strengthening/weakening of the Canadian dollar against the U.S. dollar would decrease/increase total shareholders' equity and income/loss by less than $100.

The Company's exposure to other currencies, including the Hungarian forint, Euro and Australian dollar does not result in a significant change to total shareholders' equity and income when the respective currencies strengthen or weaken by one cent against the U.S. dollar.

Interest Rate Risk

The Company is not exposed to interest rate risk as it has no outstanding market-rate borrowings or investments.

Fair Value Estimation

The carrying value less impairment provision, if necessary, of trade receivables and payables approximate their fair values.

NOTE 11 – MANAGEMENT OF CAPITAL

The Company's objectives when managing capital are to safeguard its ability to continue as a going concern in order to explore and develop its petroleum and natural gas properties. The Company manages the components of shareholders' equity and its cash as capital, and makes adjustments to these components in response to the Company's business objectives and the economic climate. To maintain or adjust its capital structure, the Company may issue new common shares or debt instruments, or borrow money or acquire or convey interests in other assets. The Company does not anticipate the payment of dividends in the foreseeable future.

The Company's investment policy is to hold excess cash in highly-liquid, short-term instruments, such as bankers' acceptances and guaranteed investment certificates issued by major Canadian chartered banks or United States financial institutions, with initial maturity terms of less than three months from the original date of acquisition, selected with regard to the Company's anticipated liquidity requirements.

The Company does not expect its current capital resources will be sufficient to meet future acquisition, exploration, development and production plans, operating requirements and convertible debenture obligations, and is dependent upon future debt and equity, or joint venture arrangements, to meet the obligations. See Note 1.

NOTE 12 – COMMITMENTS AND CONTINGENCIES

(a) ENVIRONMENTAL

Petroleum and natural gas producing activities are subject to extensive environmental laws and regulations. These laws, which are constantly changing, regulate the discharge of materials into the environment and may require the Company to remove or mitigate the environmental effects of the disposal or release of petroleum or chemical substances at various sites. Environmental expenditures are expensed or capitalized depending on their future economic benefit. Expenditures that relate to an existing condition caused by past operations and that have no future economic benefit are expensed. Liabilities for expenditures of a non-capital nature are recorded when environmental assessment and/or remediation is probable, and the costs can be reasonably estimated.

(b) CONTINGENCIES

The Company may, from time to time, be involved in various claims, lawsuits, and disputes with third parties, or breach of contract incidental to the operations of its business. Except for the following-described dispute, the Company is not currently involved in any claims, disputes, litigation or other actions with third parties which it believes could have a material adverse effect on its financial condition or results of operations.

On November 10, 2009, the Company was served with a Complaint by a former vendor of TXM (the "Vendor"), claiming that the Company owes the Vendor approximately $3.2 million, plus interest, arising out of a dispute related to TXM's alleged failure to pay for certain oilfield equipment. Falcon and TXM intend to vigorously defend against the claim as well as make any appropriate counter claims against the Vendor.

On October 15, 2010, the High Court of Justice, Queen's Bench Division, Commercial Court in the United Kingdom ruled that jurisdiction for this matter is to be in the United Kingdom ("UK"), and not Hungary, as claimed by TXM. TXM will file an appeal to have the lower court order reversed and, if upheld, this would stop all proceedings in the UK. The Company intends to file for arbitration in Hungary, even as the lower court order is being appealed. There is no assurance that the Company will prevail in the appeal process or that arbitration in Hungary will be granted.

Although the Company is of the opinion that it has a meritorious defense to the claim by the vendor, management has determined that an appropriate estimate of the potential liability should be recorded should the Company not prevail in the matter. Accordingly, the accompanying September 30, 2010 financial statements include an obligation of $4,741, including interest and fees, related to this claim that is reflected as a charge to petroleum and natural gas properties (see Note 3) with a corresponding increase to accounts payable and accrued expenses.

(c) COMMITMENTS

Under a revised work program approved by the Northern Territory of Australia Government, Department of Resources in June 2010, the Company's required minimum work program obligations, in order to continue to hold the underlying Permits in the Beetaloo Basin, is to expend $10,100 and $5,000 during the years ending December 31, 2011 and 2012, respectively.

NOTE 13 – SUBSEQUENT EVENT

On November 24, 2010, the Falcon entered into an agreement to raise up to CDN$63,000 in the form of units ("Units") priced at CDN$0.15 per Unit (the "Offering Price") by way of a private placement (the "Offering") with two new investors, as well as certain existing shareholders of Falcon. The Offering Price represents an 18% premium to the last month's average trading price. Each Unit will consist of one common share in the capital of Falcon (each a "Common Share") and three quarters (3/4) of one common share purchase warrant (a "Warrant"). Each whole Warrant will entitle the holder thereof to acquire one additional Common Share at an exercise price of CDN$0.18, representing a 20% premium to the Offering Price, for a period of three years from the Offering's closing date (the "Closing Date"). The proceeds from the Offering will be used to fund Falcon's ongoing capital program and for general corporate purposes.

NOTE 13 – SUBSEQUENT EVENT (CONTINUED)

The Offering is subject to all necessary corporate, regulatory and governmental approvals, and is subject to TSX-V acceptance for filing. All securities issued will be subject to a four-month hold period from the Closing Date.