



TSX:WIS

Production Enhancement Group, Inc.
Consolidated Financial Statements
For the years ended
December 31, 2008 and 2007
(Stated in United States dollars)

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Management's Report

To the Shareholders of Production Enhancement Group, Inc. ("PEG" or the "Company")

Management of the Company ("Management") is responsible for the preparation of the financial statements in accordance with Canadian generally accepted accounting principles and for ensuring that all other financial and operating information presented in this report is consistent with those financial statements. Management maintains a system of internal control that is designed to ensure all assets are safeguarded efficiently and to facilitate the preparation of reliable and timely financial information.

The Board of Directors of the Company (the "Board") and Management have established corporate governance practices that are consistent with guidelines set out in the report issued by the Toronto Stock Exchange committee on Corporate Governance in Canada.

The Audit Committee of the Board (the "Audit Committee"), comprised of three members considered to be "outside and unrelated" directors, have reviewed the consolidated financial statements with Management and the independent auditors appointed by the shareholders of the Company (the "Auditors").

The Auditors have examined the financial statements in order to express their opinion. The Board is responsible for ensuring that Management fulfills its responsibilities for financial reporting and internal control. The Audit Committee has reviewed these financial statements with Management and the Auditors and has reported to the Board. The Board has approved the financial statements.

(signed "Joseph P. Lahey")
Joseph P. Lahey, CEO

(signed "Douglas Parker")
Douglas Parker, CFO, Corporate Secretary

March 31, 2009

Independent Auditor's Report

The Shareholders of Production Enhancement Group, Inc.

We have audited the accompanying consolidated balance sheet of **Production Enhancement Group, Inc.** (the "Company") as at December 31, 2008 and the related consolidated statements of loss, comprehensive loss and retained deficit and cash flows for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Production Enhancement Group, Inc. as at December 31, 2008 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

The accompanying consolidated financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Note 2 to the consolidated financial statements, the Company has incurred significant operating losses and negative cash flows from operations, has a working capital deficiency, and is in default on certain of its debt obligations which raises substantial doubt about the Company's ability to continue as a going concern. Management's plans with regard to this uncertainty are described in Note 23. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

The consolidated financial statements as at December 31, 2007 and for the year then ended were examined by other auditors who expressed an opinion without reservation on those financial statements in their report dated March 31, 2008.

" Pannel Kerr Forster of Texas, P.C."

Houston, Texas

March 31, 2009

Production Enhancement Group, Inc.
Consolidated Balance Sheets
(Stated in United States dollars)

December 31, 2008 December 31, 2007

ASSETS

Current

Cash	\$ 1,428,585	\$ 1,686,643
Restricted cash (Note 14 (d))	100,000	3,238,318
Accounts receivable (Note 16 (a))	6,943,818	7,571,773
Inventory (Note 6)	473,823	339,910
Prepaid expenses	1,721,292	1,322,974
Assets held for sale	-	3,808,927
	<u>10,667,518</u>	<u>17,968,545</u>

Equipment & lease deposits	471,905	444,126
Assets held for sale (Note 8)	-	240,588
Property and equipment (Note 8)	30,835,826	33,875,755
Intangible assets (Note 7)	579,262	802,204
Prepaid expense-long term portion	89,490	77,465
Investment in JV (Note 22)	216,059	-
Goodwill (Note 18 (b))	-	1,344,748
	<u>\$ 42,860,060</u>	<u>\$ 54,753,431</u>

Liabilities and Shareholders' Deficit

Current

Accounts payable and accrued liabilities	\$ 8,477,324	\$ 6,750,600
Accrued liabilities - discontinued operations	-	212,057
Dividend payable	-	39,902
Notes payable (Note 10)	695,459	812,609
Current maturities of long term debt	-	1,546,875
Debt (Note 11)	37,493,291	-
Reclassification of long-term debt	-	45,478,679
	<u>46,666,074</u>	<u>54,840,722</u>

Going concern (Note 2)

Commitments & contingencies (Note 14 & 21)

Shareholders' Deficit

Share capital (Note 12 (a))	47,550,108	22,356,051
Contributed surplus (Note 12 (b))	4,831,669	3,719,837
Deficit	(56,187,791)	(26,163,179)
	<u>(3,806,014)</u>	<u>(87,291)</u>
	<u>\$ 42,860,060</u>	<u>\$ 54,753,431</u>

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

Approved by the Board

(signed "Joseph P. Lahey")
Joseph P. Lahey, CEO

(signed "William C. Pettigrew")
William C. Pettigrew, Director

**Production Enhancement Group, Inc.
Consolidated Statements of Loss,
Comprehensive Loss and Deficit
(Stated in United States dollars)
Years Ended December 31,**

	2008	2007
Revenue	\$ 32,996,871	\$ 31,507,611
Expenses		
Cost of services	25,364,348	20,077,839
Selling, general and administrative	14,078,557	13,263,655
Interest and financing costs	12,010,203	7,248,752
Amortization of property, equipment and intangibles	5,884,494	4,954,924
Loss on disposal of assets	406,803	359,523
Impairment of long-lived assets and goodwill (Note 18 (a) & (b))	5,266,955	-
Restructuring cost (recovery) (Note 15)	(500,811)	1,430,729
	62,510,549	47,335,422
Loss before income taxes	(29,513,678)	(15,827,811)
Income tax expense, current	162,496	749,155
	(29,676,174)	(16,576,966)
Net loss from continuing operations	(29,676,174)	(16,576,966)
Discontinued Operations (Note 20), net of tax of \$0		
Loss from operations of WISE Alberta	-	(824,646)
Impairment of intangible asset (Note 18 (c))	(20,415)	-
Loss on discontinued operations of WISE Alberta	(153,841)	(2,335,017)
Net loss and comprehensive loss	(29,850,430)	(19,736,629)
Deficit, beginning of year	(26,163,179)	(6,044,556)
Dividends	(174,182)	(381,994)
Deficit, end of year	\$ (56,187,791)	\$ (26,163,179)
Loss per share from continuing operations -		
Basic and dilutive	(0.34)	(0.30)
Loss per share from discontinued operations -		
Basic and dilutive	(0.00)	(0.06)
Loss per share -		
Basic and dilutive	(0.34)	(0.36)
Weighted average number of shares outstanding -		
Basic and dilutive	86,583,018	55,827,957

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

Production Enhancement Group, Inc.
Consolidated Statements of Cash Flows
(Stated in United States dollars)
Years Ended December 31,

	2008	2007
Net loss from continuing operations	\$ (29,676,174)	\$ (16,576,966)
Cash flows from operating activities		
Non cash items		
Non cash financing costs	1,722,416	2,878,914
Amortization of property, equipment and intangibles	5,884,494	4,954,924
Impairment of long-lived assets and goodwill	5,266,955	-
Stock based compensation	791,531	433,223
Loss on disposal of asset	406,803	359,523
Restructuring costs	-	38,762
Future tax recovery	-	714,732
Prepaid Expense - long-term portion	(12,025)	(77,465)
Deposits	(28,513)	-
	<u>(15,644,513)</u>	<u>(7,274,353)</u>
Changes in non cash working capital items (Note 9 (a))	3,779,683	940,343
Cash flows from continuing operating activities	<u>(11,864,830)</u>	<u>(6,334,010)</u>
Net loss from discontinued operations (Note 20)	(174,256)	(3,159,663)
Non cash items		
Amortization of property, equipment and intangibles	-	220,037
Impairment of intangible	20,415	-
Currency conversion	2,233	-
Deposits	734	-
Loss on disposal of asset	-	1,958,143
	<u>(150,874)</u>	<u>(981,483)</u>
Changes in non-cash working capital from discontinued operations (Note 9 (b))	(164,631)	(61,726)
Cash flows from discontinued operations	<u>(315,505)</u>	<u>(1,043,209)</u>
Cash flows from financing activities		
Proceeds preferred stock offering-net of costs	-	4,540,154
Proceeds from Quest takeover-net of costs	24,148,243	-
Proceeds from employee share takeover	363,313	-
Deferred charges paid	(98,417)	(2,658,924)
Dividends paid	(103,040)	(14)
Proceeds from long-term debt	3,000,000	62,987,148
Repayment of long term debt	(15,000,000)	(28,307,691)
	<u>12,310,099</u>	<u>36,560,673</u>
Cash flows from continuing investing activities		
Restricted cash	3,138,318	(3,238,318)
Acquisition of Wireline, net of cash acquired and costs	-	(6,077,857)
Acquisition of DynaStar, net of cash acquired and costs	-	(1,857,827)
Additions property and equipment	(6,910,081)	(18,109,432)
Proceeds from disposal of assets	3,600,000	743,626
Investment in JV	(216,059)	-
Additions in intangibles	-	(22,648)
	<u>(387,822)</u>	<u>(28,562,456)</u>
Increase (decrease) in cash	(258,058)	620,998
Cash, beginning of year	1,686,643	1,065,645
Cash, end of year	<u>\$ 1,428,585</u>	<u>\$ 1,686,643</u>
Supplemental information		
Interest paid	\$ 8,994,967	\$ 2,461,056
Taxes paid	96,487	-

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

Production Enhancement Group, Inc.
Notes to the Consolidated Financial Statements
For the years ended December 31, 2008 and 2007
(Stated in United States Dollars)

1. Nature of Business

Production Enhancement Group, Inc. (the "Company" or "PEG") and its wholly owned subsidiaries, WISE Well Intervention Services, Inc., a Nevada corporation ("WWIS"), WISE Well Intervention Technologies, Inc. ("WWIT"), a Texas corporation and 1314235 Alberta Ltd, which in turn owns one hundred percent (100%) of WISE Well Intervention Services, Inc, an Alberta corporation (formerly Dyna Star Energy Services Ltd.)("WISE Alberta"), provide oil and natural gas well services. WWIS provides specialized coiled tubing, pressure pumping, nitrogen and slickline services to oil and gas producers and operators in Texas, Louisiana, Mississippi and in the inland and offshore waters of the Gulf of Mexico. WISE Alberta provided coiled tubing services to western Canada and its operations were terminated in December 2007 (Note 20). WWIS provided pumping services in Belize during 2008 but those services were discontinued in December 2008 (Note 23). WWIT was incorporated on August 9, 2007 to commercialize the Company's proprietary technology, but it has not had any significant operations to date.

2. Significant Accounting Policies

Basis of Presentation

These consolidated financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles ("Canadian GAAP"). Since the determination of many assets, liabilities, revenues and expenses is dependent upon future events, the preparation of these financial statements requires the use of estimates and assumptions. In the opinion of management, these financial statements have been prepared within reasonable limits of materiality.

The Company's consolidated financial statements for the year ended December 31, 2008 have been prepared on a going concern basis which contemplates the realization of assets and settlement of liabilities in the normal course of operations. The Company reported a significant working capital deficit due to the restructuring of its long term credit facility (Note 11) and a net loss of \$29.8 million and \$19.7 million for the years ended December 31, 2008 and 2007, respectively, and losses are expected to continue in the near term. Current liabilities exceeded current assets by \$35,998,556 and \$36,872,177 at December 31, 2008 and 2007, respectively and the accumulated deficit is \$56,187,791 and \$26,163,179 at December 31, 2008 and 2007, respectively. The Company is currently in default on certain of its debt obligations and is in discussions with the lender to amend the terms of the loan agreement. The Company has cut personnel, suspended 401k matching and lowered salaries/wages from field to top management in the first quarter of 2009. The Company has reduced fixed costs by approximately \$400,000 per month through these actions.

All amounts are stated in United States dollars, unless otherwise noted by CAD for Canadian dollars.

Certain reclassifications have been made to previous presentations to conform to the December 31, 2008 financial statements.

Consolidation

These consolidated financial statements include the accounts of Production Enhancement Group, Inc., and its wholly owned subsidiaries. All intercompany amounts and transactions have been eliminated.

Cash and Cash Equivalents

The Company considers all highly liquid investments with an original maturity of three months or less to be cash equivalents. The carrying amounts reported in the balance sheet for cash and cash equivalents are valued at cost, which approximates their fair value. The restricted cash has been presented as a current asset as it represents a certificate of deposit (CD) held with a maturity of one year.

Production Enhancement Group, Inc.
Notes to the Consolidated Financial Statements
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(Stated in United States Dollars)

Comprehensive Income and Equity

CICA Handbook Section 1530, *Comprehensive Income*, established new measurements of earnings in the financial statements. Other comprehensive income consists of changes to unrealized gains and losses on available-for-sale financial assets, changes to unrealized gains and losses on the effective portion of cash flow hedges and changes to foreign currency translation adjustments of self-sustaining foreign operations during the period. Comprehensive income measures net earnings for the period plus other comprehensive income. Amounts reported as other comprehensive income are accumulated in a separate component of shareholders' deficit as Accumulated Other Comprehensive Income.

Financial Instruments

Financial Assets

Held for trading

Financial assets that are held with the intention of generating profits in the near term and derivative contracts that are financial assets, except for a derivative that is a designated and effective hedging instrument, are classified as held for trading. In addition, any other financial assets can be designated by the Company upon initial recognition as held for trading. These instruments are subsequently re-measured at fair value with the change in the fair value recognized in net income during the period.

Held-to-maturity

Financial assets that have a fixed maturity date and which the Company has a positive intention and the ability to hold to maturity are classified as held-to-maturity, which are subsequently re-measured at amortized cost using the effective interest rate method.

Loans and receivables

Loans and receivables are non-derivative financial assets resulting from the delivery of cash or other assets in return for a promise to repay on a specified date, or on demand, usually with interest. Loans and receivables are subsequently re-measured at amortized cost using the effective interest rate method.

Available-for-sale

Available-for-sale assets are non-derivative financial assets that are either designated in this category or not classified in any of the other categories. Financial assets classified as available-for-sale are subsequently re-measured at fair value with the changes in fair value recorded in other comprehensive income.

Financial Liabilities

Held for trading

Financial liabilities that are held with the intention of generating profits in the near term and derivative contracts that are financial liabilities, except for a derivative that is a designated and effective hedging instrument, are classified as held for trading. In addition, any other financial liabilities can be designated by the Company upon initial recognition as held for trading. These instruments are subsequently re-measured at fair value with the change in the fair value recognized in net income during the period.

Production Enhancement Group, Inc.
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Other liabilities

Non-derivative financial liabilities that have not been designated as held for trading are classified as other liabilities, which are subsequently re-measured at amortized cost using the effective interest rate method.

Foreign Currency Translation

Monetary assets and liabilities denominated in foreign currencies are translated at the rate of exchange in effect at the balance sheet date. Non-monetary assets and liabilities are translated at historical exchange rates. Revenue and expenses are translated at the average rate of exchange during the year.

Financial statements of integrated foreign subsidiaries are translated using the temporal method. Under this method, monetary assets and liabilities are translated into US Dollars at the exchange rate in effect at the balance sheet date. Non-monetary assets are translated at historical exchange rates. Revenue and expenses are translated at average exchange rates for the period since acquisition, except amortization, which is translated on the same basis as the related asset. Translation gains and losses are included in net income.

Asset Retirement Obligation

The Company recognizes asset retirement obligations in the period in which they are incurred if a reasonable estimate of fair value can be determined. The associated asset retirement costs before salvage values are capitalized as part of the carrying amount of the capital asset. The liability is accreted over the estimated time period until settlement of the obligation and the asset is amortized over the estimated useful life of the asset. As at December 31, 2008 and 2007, the estimated value of any asset retirement obligation that the Company has is nominal. Accordingly, no provision has been made for any asset retirement obligations.

Future Income Taxes

The Company uses the liability method of accounting for income taxes. Under this method, future tax assets and liabilities are measured using substantially enacted tax rates and laws that will be in effect when the differences are expected to reverse. Future tax assets and unused tax losses are recognized to the extent that they are more likely than not to be realized.

Impairment of Long-lived Assets

Long-lived assets, which include property and equipment, are reviewed for impairment or when events or circumstances indicate that the carrying amount of an asset may not be recoverable. The Company's policy is to record an impairment loss when it is determined that the carrying amount of the asset exceeds the sum of the expected undiscounted future cash flows resulting from use of the asset and its eventual disposition. Impairment losses are measured as the amount by which the carrying amount of the asset exceeds its fair value and is recognized as an expense in the period of impairment. The Company has recognized an impairment loss on long-lived assets as described in Note 18 (a).

Inventory

Inventories are valued at the lower of cost or net realizable value. Cost is determined by the weighted average cost method.

Production Enhancement Group, Inc.
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(Stated in United States Dollars)

Capital Assets

Property and equipment are recorded at cost. Property and equipment that are still undergoing development and have not been placed in service are classified as assets under construction and are not amortized. Amortization, for financial statement purposes, is provided by the straight-line method over the estimated useful lives of the assets as follows:

Asset	Years
Software and equipment	2-3
Equipment	5-12
Furniture and fixtures	3-7
Vehicles	3-7
Leasehold improvements	7-39

Leases

Leases are classified at their inception as either operating or capital leases based on the economic substance of the agreement so as to reflect the risks and benefits incidental to ownership.

Transaction Costs

Transaction costs will be capitalized to the cost of financial assets and liabilities classified as other than held for trading. As a result, deferred financing costs related to the long-term debt have been reclassified against long-term debt. These transaction costs are amortized on an effective interest basis over the life of the related debt.

Goodwill

Goodwill represents the excess of cost over the fair value of net assets acquired and is not amortized. The recorded amount of goodwill is tested for impairment based on expected future cash flows to which the goodwill is attributable, at least annually at year end, or whenever events or circumstances indicate a possible impairment, to ensure that the fair value is greater than, or equal to, book value. Any impairment in the value of goodwill is charged in the period when impairment is determined. The Company has recorded a goodwill impairment for the year ended December 31, 2008 as disclosed in Note 18 (b).

Intangible Assets

Intangible assets consist of patents and the customer base from acquisitions. Intangible assets are recorded at cost less accumulated amortization. Amortization is computed on a straight-line basis over the estimated useful life of five years.

Customer base	5 years
Covenant not to compete	5 years

Intangible assets are reviewed annually with respect to their useful lives, or more frequently, if events or changes in circumstances indicate that the assets might be impaired. The Company has recorded an intangible asset impairment for the year ended December 31, 2008 as disclosed in Note 18 (c).

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Investment in Joint Venture

The Company will account for its investment in joint venture using the equity method of accounting because the investment gives it the ability to exercise significant influence, but no control, over the investee. Significant influence is generally deemed to exist where there is an ownership interest in the investee of between 20% and 50%, although other factors such as the degree of ultimate control, representation on the investee's Board of Directors or similar oversight body are considered in determining whether the equity method of accounting is appropriate. The Company will report its proportional share of the investment's net income or loss in its consolidated statements of loss, comprehensive loss.

Per Share Amounts

The loss per share is calculated using the weighted average number of common shares outstanding during the year. Diluted per share amounts reflect the potential dilution that could occur if securities or other contracts to issue common shares were exercised or converted to common shares. The treasury stock method is used to determine the dilutive effect of stock options and other dilutive instruments.

Revenue recognition

The Company's services are generally sold based upon purchase orders or contracts with the customer that include fixed or determinable prices based upon daily, hourly or job rates. Customer contract terms do not include provisions for significant post-service delivery obligations. Revenue is recognized when services are rendered and only when collectability is reasonably assured. Revenue collected in advance of rendering the service is deferred to the future period in which the service is rendered.

Stock-based compensation

The Company has a stock option plan as described in Note 12 (d). The Company follows the fair value method of accounting using the Black-Scholes option pricing model. Compensation expense for stock options is recognized using the fair value when the stock options are granted and is amortized over the option's vesting period.

Use of Estimates

The preparation of financial statements in accordance with Canadian GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenue and expenses during the reporting period. The most significant of these estimates are related to allowance for doubtful accounts, amortization of property and equipment, valuation of assets, accruals for contingent payments on long term debt (Note 11), future income tax and stock compensation. Actual results could differ significantly from these estimates. Certain items recognized in the consolidated financial statements are subject to measurement uncertainty as they are based on management's estimate using current information and judgment. The effect on the consolidated financial statements of changes in such estimates in future years could be significant.

The allowance for doubtful accounts represents the Company's best estimate of probable losses that may result from the inability of its customers to make required payments to the Company for services rendered. The Company continually monitors its accounts receivable items and uses judgment to assess the collectability of specific accounts and based on this assessment an allowance is maintained for those accounts deemed to be uncollectible.

Production Enhancement Group, Inc.
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3. Accounting Changes

Changes in accounting policies

As at January 1, 2008, the Company adopted four new Handbook sections issued by the Canadian Institute of Chartered Accountants ("CICA").

(a) Capital Disclosures

CICA Handbook Section 1535, *Capital Disclosures*, requires disclosure of an entity's objectives, policies and processes for managing capital, quantitative data about what the entity regards as capital and whether the entity has complied with any capital requirements and, if it has not complied, the consequences of such non-compliance. The Company has determined that the only impact is the disclosure contained in Note 17.

(b) Inventories

CICA Handbook Section 3031, *Inventories*, replaces the existing Section 3030 and contains requirements on measurement and disclosure of inventories to converge with International Financial Reporting Standards. This standard establishes guidance on the determination of costs and its subsequent recognition as an expense, including any write down to net realizable value and subsequent reversal of impairment to original cost. It also provides guidance on the cost formulas that are used to assign costs to inventories. The Company has determined that there is no material impact on its consolidated financial statements as the existing policies were in compliance with the revised standard.

(c) Financial Instruments Disclosures and Presentation

CICA Handbook Section 3862, *Financial Instruments – Disclosures* and CICA Handbook Section 3863, *Financial Instruments – Presentation*, increase the disclosures required that will enable users to evaluate the significance of financial instruments for an entity's financial position and performance, including disclosures about fair value. In addition, disclosure is required of qualitative and quantitative information about exposure to risks arising from financial instruments, including specified minimum disclosures about liquidity risk and market risk. The quantitative disclosures must also include a sensitivity analysis for each type of market risk to which an entity is exposed, showing how net income and other comprehensive income would have been affected by reasonably possible changes in the relevant risk variable. The only significant effect on the Company's consolidated financial statements is the incremental disclosures in Note 16.

Future accounting changes

(a) Goodwill and Intangible Assets

CICA Handbook Section 3064, *Goodwill and Intangible Assets*, will replace the existing Goodwill and Intangible Asset standard effective for years beginning on or after January 1, 2009. The new standard revises the requirement for recognition, measurement, presentation and disclosure of intangible assets. The Company does not expect that the adoption of this new standard will have a material impact on its consolidated financial statements.

(b) International Financial Reporting Standards

On February 13, 2008, the Canadian Accounting Standards Board confirmed that publicly accountable profit-oriented enterprises will be required to use International Financial Reporting Standards ("IFRS") in interim and audited financial statements for fiscal years beginning on or after January 1, 2011. Over the next three years Canadian GAAP will be modified to converge with IFRS.

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The Company's financial executives and senior accounting staff are familiarizing themselves with the new IFRS principles and requirements through formalized training and industry focus groups. An evaluation of IFRS conversion requirements that pertain to the Company will be conducted throughout 2009, which will then lead to the development of an implementation plan to transition the Company's financial reporting process, including internal controls and information systems to IFRS. During this evaluation, IFRS early adoption provisions will be investigated and the Company will evaluate whether early adoption is feasible. The evaluation will also allow the Company to be in a position to estimate the initial financial impact of the transition to IFRS so key stakeholders and users of the financial information can begin to understand the overall consequences of this process.

4. Change of Control

On April 18, 2008, Quest Energy Services (Canada) Ltd. ("Quest") offered to purchase all of the issued and outstanding common shares of the Company including common shares issuable upon the exercise of stock options and warrants and on the conversion of the preferred shares (Note 12 (c)) for CAD \$0.65 per share ("the Offer"). The Board of Directors ("Board") of PEG engaged a third party consultant to prepare a fairness opinion in relation to the Offer and unanimously recommended acceptance of the Offer based on the opinion received. On June 6, 2008, Quest, an indirect wholly owned subsidiary of Al-Qahtani Marine & Oilfield Services Co. ("Al-Qahtani") of Saudi Arabia, successfully completed its acquisition of 51,046,166 common shares of the Company. In connection with the closing of the Offer, the Company issued an additional 32,946,861 common shares to Quest at an issue price of CAD \$0.65 per share. Net proceeds were \$21 million. On July 15, 2008 Quest finalized their take-up of shares with an additional 5,705,592 shares being issued. Quest now owns 89,698,619 common shares of the Company representing approximately 83.1% of the issued and outstanding common shares of the Company. In addition, the Company's credit facility with its lender was required to be restructured upon closing of the Offer (Note 11).

The Company has recorded costs for the year ended December 31, 2008 associated with the change of control that include retention bonuses for key employees paid in December, 2008 and employment contract payouts to three former executives.

5. Acquisition

(a) On March 5, 2007, the Company purchased all of the shares of Wireline Specialists of Louisiana, Inc. ("WSL"). The Company assumed and refinanced WSL's existing debt of \$2,920,428 and paid net consideration to the selling shareholders of \$3,078,355 in cash, transaction costs of \$118,040 and an initial 1,234,739 PEG common shares subject to repricing at the first anniversary date. The acquisition was accounted for using the purchase method with the results of operations of WSL being included in the consolidated financial statements beginning March 1, 2007. The Company's common shares were valued at CAD \$1.29, such value being the volume weighted average trading day price of the Company's stock five days before and after the date of September 22, 2006.

On March 5, 2008, the number of common shares issuable pursuant to the acquisition of WSL was adjusted per the Wireline agreement. The repricing of common shares was based on the value of the volume weighted average closing price during the twenty consecutive trading days that preceded the first anniversary of the closing date of March 5, 2007. An additional 4,321,507 common shares issued in March 2008 were based on the repricing of the original 1,234,739 common shares from \$1.72 (CAD \$2.00) to \$0.3828 (CAD \$0.3828) per share.

On May 9, 2008, the Company reached a settlement with the former owners of WSL in connection with the earn-out provision of the Wireline agreement pursuant to which an additional 461,538 common shares were issued to the former owners of WSL. The shares were valued at CAD \$0.65.

Production Enhancement Group, Inc.
Notes to the Consolidated Financial Statements
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(Stated in United States Dollars)

The final purchase allocations are as follows:

Net assets acquired:		
Cash	\$	38,966 *
Non-cash working capital		1,063,125
Capital assets and deposits		4,582,696
Intangibles		765,745
Goodwill		1,226,736
Capital lease		(18,541)
Long-term debt		(2,920,428) *
	\$	<u>4,738,299</u>
Consideration:		
Common shares issued at closing, net of costs	\$	1,541,904
Cash		3,196,395 *
	\$	<u>4,738,299</u>
* Net cash effect of acquisition	\$	<u>(6,077,857)</u>

- (b) On April 27, 2007, the Company entered the western Canada oilfield services market with its purchase of all of the shares of Dyna Star Energy Services Ltd. ("Dyna Star"), a private company that provided coiled tubing and nitrogen services in Alberta. The Company assumed and refinanced Dyna Star's existing debt of CAD \$1,275,096 (USD \$1,155,083) and paid net consideration to the selling shareholders of CAD \$230,000 (USD \$208,352) cash, transaction costs of \$135,238 and 427,004 PEG common shares. The proceeds necessary to refinance the assumed indebtedness and pay the selling shareholders of Dyna Star were provided through an additional term loan from a major international financial institution. The final purchase price settlement has been finalized and the 427,004 shares were issued to the sellers in fourth quarter 2007.

The acquisition was accounted for using the purchase method with the results of operations of Dyna Star being included in the consolidated financial statements beginning May 1, 2007. The Company shares were valued at CAD \$1.26, such value being the volume weighted average trading day price of the Company's stock five days before and after the date of November 16, 2006.

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The final purchase allocations are as follows:

Net assets acquired:	
Liabilities	\$ (359,154) *
Non-cash working capital	(225,231)
Capital assets and deposits	2,435,206
Long-term debt	(1,155,083) *
	<u>\$ 695,738</u>
Consideration:	
Common shares issued at closing, net of costs	\$ 352,148
Cash	343,590 *
	<u>\$ 695,738</u>
* Net cash effect of acquisition	<u>\$ (1,857,827)</u>

6. Inventory

Inventories are valued at the lower of cost or net realizable value. Cost is determined by the weighted average cost method. Inventory is composed of coil tubing and chains, chemicals, wire and tools. The following table represents the carrying amount of inventory by classification as at December 31, 2008 and 2007.

Category	December 31, 2008	December 31, 2007
Tubing and Chains	\$ 272,808	\$ 194,240
Chemicals	191,808	145,670
Wire	9,207	-
Tools	-	-
	<u>\$ 473,823</u>	<u>\$ 339,910</u>

The following table represents the recognized expense by classification for the years ended December 31, 2008 and 2007.

Category	December 31, 2008	December 31, 2007
Tubing & Chains	\$ 784,455	\$ 766,281
Chemicals	783,139	757,892
Wire	32,194	28,610
Tools	73,851	-
	<u>\$ 1,673,639</u>	<u>\$ 1,552,783</u>

Inventories are pledged as securities for the Company's credit facility (Note 11). For the year ended December 31, 2008 there was no write down of inventories to net realizable value required.

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7. Intangible Assets

	<u>December 31, 2008</u>	<u>December 31, 2007</u>
Patent	\$ 1	\$ 22,649
Customer Base	901,469	901,469
Less: Amortization	<u>(385,541)</u>	<u>(205,247)</u>
	<u>515,929</u>	<u>718,871</u>
Covenant not to compete	100,000	100,000
Less: Amortization	<u>(36,667)</u>	<u>(16,667)</u>
	<u>63,333</u>	<u>83,333</u>
	<u>\$ 579,262</u>	<u>\$ 802,204</u>

Intangible assets are reviewed annually with respect to their useful lives, or more frequently, if events or changes in circumstances indicate that the assets might be impaired. The Company has recorded an intangible asset impairment for the year ended December 31, 2008 as disclosed in Note 18 (c).

8. Property and Equipment

	<u>December 31, 2008</u>			<u>December 31, 2007</u>		
	Cost	Accumulated Amortization	Net Book Value	Cost	Accumulated Amortization	Net Book Value
Software and equipment	\$ 1,487,861	\$ 1,330,739	\$ 157,122	\$ 1,404,121	\$ 574,156	\$ 829,965
Equipment	39,943,212	12,735,623	27,207,589	29,009,546	5,434,879	23,574,667
Furniture and fixtures	375,586	154,668	220,918	299,000	85,952	213,048
Vehicles	2,351,715	1,436,546	915,169	2,104,672	916,761	1,187,911
Leasehold improvements	148,153	39,213	108,940	85,617	15,898	69,719
Assets under construction	2,226,088	-	2,226,088	8,000,445	-	8,000,445
	<u>\$ 46,532,615</u>	<u>\$ 15,696,789</u>	<u>\$ 30,835,826</u>	<u>\$ 40,903,401</u>	<u>\$ 7,027,646</u>	<u>\$ 33,875,755</u>

Assets under construction consist of nitrogen units currently being constructed by the Company. These assets are not amortized until they become operational and are moved to the appropriate class of asset above (Note 23).

Assets held for sale related to discontinued operations have been classified as non current assets net of impairment (Note 20).

9. Changes in Non-Cash Working Capital

(a) From Operations

	<u>For the Year Ended December 31, 2008</u>	<u>For the Year Ended December 31, 2007</u>
Accounts receivable	\$ 667,059	\$ (667,883)
Inventory	(133,913)	(36,565)
Prepaid expenses	(434,878)	(425,918)
Accounts payable and accrued liabilities	3,016,655	(163,564)
Notes payable	(90,104)	312,550
Interest payable	754,864	1,921,723
	<u>\$ 3,779,683</u>	<u>\$ 940,343</u>

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(b) From Discontinued Operations

	For the Year Ended December 31, 2008	For the Year Ended December 31, 2007
Accounts receivable	\$ 75,896	\$ (33,068)
Inventory	-	54,353
Prepaid expenses and deposits	36,560	(33,776)
Accounts payable and accrued liabilities	(37,984)	(288,338)
Accrued liabilities discontinued operations	(212,057)	212,057
Notes payable	(27,046)	27,046
	<u>\$ (164,631)</u>	<u>\$ (61,726)</u>

10. Notes Payable

Notes payable represents several notes on the Company's insurance policies and the short term portion of capital leases. All of the policies required a down payment and offer monthly payments from three to ten months. Interest rates range from 6.75% to 9.25% (effective rates – 6.96% to 9.64%).

The following table represents the details of the notes payable balance at December 31, 2008 and 2007.

	December 31, 2008	December 31, 2007
All remaining US policies	\$ 677,330	\$ 416,720
Umbrella	-	29,887
Workers compensation	-	328,770
Canadian policy	-	27,046
Belize policy	8,125	-
Additional D & O	10,004	-
WL capital lease	-	1,765
A to Z capital lease	-	8,421
	<u>\$ 695,459</u>	<u>\$ 812,609</u>

11. Debt

(a) As a result of the Offer (Note 4), the Company's credit facility has been restructured. The Company has made a principal payment of \$15 million and the maturity date of the aggregate outstanding principal amount of the debt is now June 6, 2009. The Company has the option to extend the maturity date for six months with an interest rate increase of 2% and the grant by the Company of an additional 500,000 warrants at CAD \$0.65. The lender has also amended the terms to permit pre-payment of the remaining principal balance of the obligations at no penalty. The Company has incurred a \$4 million restructuring fee, with \$2 million of such being paid at the closing of the restructuring and the remaining \$2 million due and payable upon the earlier of (a) the date the obligations owing under the agreement are paid or prepaid in full, or (b) the maturity date for the remaining aggregate outstanding principal amount of the obligations under the agreement as amended, being June 6, 2009. The restructured facility is for a total of \$40 million and borrowings under the facility bear interest at 14%, with the Company having the ability to pay 3% in kind. Payment in kind will result in an increase to the principal balance due. The effective interest rate is 14.93%. The facility is secured by all assets of the Company except the Company's accounts receivable (Note 11 (c)).

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The Company had originally entered into this credit facility with a major energy lending institution (the "Lender") on August 31, 2007 to provide a senior credit facility of \$70 million. This senior facility refinanced the pre-existing senior indebtedness and provided \$40 million in expansion financing for additional capital expenditures and working capital.

As a result of the Offer (Note 4), the 8,236,436 warrants issued to the Lender in 2007 were cancelled and new warrants ("New Warrants") were issued to purchase up to 3,000,000 common shares at a fixed rate of CAD \$0.65 with a term of four years. The fair value of the New Warrants was estimated to be \$591,760 using the Black-Scholes model with the following assumptions: expected life of New Warrants four years; expected volatility of 41%; risk-free interest rate of 3.22%; and a zero dividend yield. If the Company is not publicly traded for a period of one month or more, each holder will have the option on a semi-annual basis, beginning on June 1, 2009, and continuing on each June 1 and December 1 thereafter, to put the New Warrants to the Company at a redemption price determined by (a) calculating the number of common shares for which the New Warrants are then exercisable (the "Put Shares"), which shall not include the New Warrant shares that are then outstanding, and (b) calculating an equity valuation for the Company equal to (i) the Company's trailing six months EBITDA for the period immediately ended prior to the put times twelve, minus (ii) the Company's aggregate outstanding indebtedness (net of any unrestricted cash or liquid investments) and the liquidation preference of all outstanding preferred shares of the Company, if any, and (c) calculating the redemption price for each Put Share which shall be an amount equal to the equity valuation of the Company divided by the number of all outstanding common shares of the Company, including all Put Shares and all common shares issuable upon the conversion of other outstanding securities of the Company on a fully diluted basis as if such common shares were outstanding at the time of such calculation. The unamortized value of the original warrants has been recorded as a financing cost in the current period.

The Company did not pay its principal and interest payment due December 31, 2008 until January 13, 2009 due to the negotiations in establishing an accounts receivable factoring facility (Note 11 (c)).

- (b) The Company was in breach of its debt covenants with its Lender at December 31, 2007. The Lender agreed to waive said violations for an additional interest fee of \$250,000 paid on April 18, 2008. The Company was in negotiations with the Lender to amend the terms of the loan agreement which such loan was amended May 6, 2008. The Company reclassified all such long-term debt as current until such time as the amendment was finalized.
- (c) The Company has entered into a \$7.5 million accounts receivable facility ("Facility") to be used for working capital and general business purposes with a major banking institution ("Bank"). This Facility provides working capital to meet our sales growth to ensure that the Company will have the financial flexibility to meet the needs as the business expands.

The initial funding commitment is for \$7.5 million, with the ability to expand the Facility upon the attainment of certain financial performance criteria and additional approval by the Bank. Borrowings under the Facility bear interest at prime rate plus the Bank applicable rate (approximately 10.6%), with the Company having increased interest costs should collections not be made within 90 days of the borrowing date of the accounts receivable. The Facility will advance 80% of the gross amount of eligible accounts receivable. The borrowing under the Facility will be subject to a fixed discount fee plus a variable discount fee equal to prime rate plus 1% with a minimum of 6%.

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12. Equity Instruments

(a) Share Capital

(1) Authorized:

- Unlimited number of common voting shares.
- Unlimited number of Class B common convertible voting shares, convertible to common shares upon completion of initial public offering.
- Unlimited number of Class C convertible non-voting common shares, convertible at the option of the holder, upon 75 days prior notice to the Company, on the basis of one common share for each Class C share.
- Unlimited number of non-voting preferred shares issuable in series at terms as determined by the Board, retractable by the Company.

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(2) Common shares and warrants issued and outstanding:

	<u>Number of Shares</u>	<u>Amount</u>
Common Shares		
Balance, December 31, 2006	16,357,848	\$ 15,619,467
Acquisition of Wireline, net of issuance costs	1,234,739	1,241,904
Acquisition of Dyna Star, net of issuance costs	427,004	352,148
Conversion of Preferred Stock	300,001	-
Conversion of Class C Shares	38,297,784	-
Balance, December 31, 2007	56,617,376	17,213,519
Additional shares issued pursuant to Wireline agreement (Note 5 (a))	4,321,507	-
Shares issued for Wireline earnout settlement (Note 5 (a))	461,538	300,000
Conversion of Preferred Stock	7,278,409	2,637,660
Shares issued to Quest, net of costs of \$488,445 (Note 4)	32,946,861	20,511,555
Quest share take-up	5,705,592	3,636,688
Employee share take-up	570,000	363,313
Balance, December 31, 2008	107,901,283	44,662,735
Class C Shares		
Balance, December 31, 2006	38,297,784	-
Conversion to Common Shares	(38,297,784)	-
Balance, December 31, 2007	-	-
	107,901,283	44,662,735
Preferred Stock		
Balance, December 31, 2006	-	-
Preferred share offering, net of issuance costs	6,666,667	2,184,541
Paid in kind dividends	609,134	342,077
Conversion to Common Shares	(300,001)	-
Balance, December 31, 2007	6,975,800	2,526,618
Paid in kind dividends	302,609	111,042
Conversion to Common Shares	(7,278,409)	(2,637,660)
Balance, December 31, 2008	-	-
Warrants		
Balance, December 31, 2006	6,288,433	1,559,049
Warrants issued on preferred stock (Note 12 (c))	5,436,250	2,123,938
Warrants issued to agent (Note 12 (c))	333,333	171,675
Warrants issued to lender (Note 11)	8,236,436	320,301
Expiration of warrants	(6,288,433)	(1,559,049)
Balance, December 31, 2007	14,006,019	2,615,914
Lender warrants cancelled (Note 11 (a))	(8,236,436)	(320,301)
Warrants issued to lender (Note 11 (a))	3,000,000	591,760
Balance, December 31, 2008	8,769,583	2,887,373
Total		\$ 47,550,108

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(b) Contributed Surplus

Balance, December 31, 2006	\$ 1,727,565
Employee options	274,692
Board of Director options	145,320
Advisory Board options	13,211
Expired warrants	1,559,049
Balance, December 31, 2007	3,719,837
Employee options	470,505
Board of Director options	318,430
Advisory Board options	2,596
Cancelled warrants	320,301
Balance, December 31, 2008	<u>\$ 4,831,669</u>

(c) Preferred Stock

All of the 7,278,409 preferred shares were converted to common shares during the second quarter 2008 prior to the completion of the Quest Offer (Note 4). Each preferred share was converted to one common share.

On March 5, 2007, the Company closed its offering of 6,666,667 units (each a "Unit") priced at CAD \$0.87 per Unit, for CAD \$5.8 million. Gross proceeds were \$5 million. Each Unit is comprised of one Series A preferred share and three quarters of one common share purchase warrant (each a "Warrant"). The fair value of the Warrants was estimated to be \$2,099,038 using the Black-Scholes model with the following assumptions: expected life of Warrants five years; expected volatility of 50%; risk-free interest rate of 4.0%; and a zero dividend yield. A corresponding amount of the equity raised has been allocated to Warrants.

The preferred shares paid quarterly cumulative dividends at a rate of 8% per year of the amount invested. The Company had the right to pay all or a portion of the first four quarterly dividends in kind in additional preferred shares at the equivalent common share value at the time of payment. Each preferred share was convertible at the option of the holder into one PEG common share. The dividends for the first four quarterly periods have been issued as in kind preferred shares totaling 911,743 shares with an additional cash portion totaling CAD \$17.26.

Each whole Warrant entitles the holder to purchase one common share at a price per share of CAD \$1.24 expiring March 4, 2012. The Company can accelerate the expiry of the Warrants in the event that the simple average trading price for a 30 consecutive trading day period is equal to or greater than CAD \$2.48.

The exclusive placement agent received a 7% commission and broker warrants (each a "Broker Warrant") equivalent to 5% of the number of preferred shares issued pursuant to the offering. Each Broker Warrant entitles the holder to purchase one common share at a price per share of CAD \$0.87 for a period of five years following the date of issuance. The Company can accelerate the expiration of the Broker Warrants in the event that the simple average trading price for a 30 consecutive trading day period is equal to or greater than CAD \$1.74. The fair value of the Broker Warrants of \$171,675 has been recorded as a share issue cost and they were calculated from the Black-Scholes option pricing model with the following assumptions: risk-free interest rate of 4.0 %; expected life of five years; no annual dividends paid; and expected volatility of 50%.

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On December 4, 2007, the Company announced that following negotiations with the holders of its 6,666,667 Series A preferred shares and the 5,000,000 associated Warrants for all accepting holders, the Company had amended the terms of the Warrants to include a cashless exercise option and grant one (1) additional Warrant for each ten (10) existing Warrants held. The Company granted "piggyback" registration rights to these holders in the event the Company were to file a registration statement under the US Securities Act of 1933 under certain circumstances. The cashless exercise option allows a holder of a Warrant to elect to exchange the Warrant for a number of common shares equal to the difference between the value of the common shares at the time of exercise and the original Warrant exercise price per common share (which remains at CAD \$1.24 per common share). An additional 436,250 Warrants were issued in the fourth quarter of 2007, and they have the exact same terms as the existing Warrants, including the cashless exercise option. The fair value of these warrants was estimated to be \$24,900.

There were three warrant holders who did not accept these terms, which holders represent 637,500 Warrant shares, or 12.7% of the original 5,000,000 Warrants.

(d) Stock Option Plan

On November 24, 2005, the Board approved a stock option plan (the "Plan") for the purpose of developing the interest of directors, officers, employees, and consultants in the growth of the Company. The Board amended the Plan on September 6, 2007 to include a new cashless exercise feature. The amendment was not approved by the shareholders; shareholder approval was not required as no re-pricing of options held by insiders was undertaken, and the TSX did not require shareholder approval in relation to the institution of a cashless exercise feature where there was a full deduction of the number of underlying securities from the plan reserve. Under the terms of the Plan and subsequent amendments to the Plan, the Company has reserved 10% of the issued and outstanding shares as the maximum stock options that can be granted. When granted, options have a five year term. The exercise price of the options is determined by the Board and will not be less than the market price of the common shares at the grant date. The Board will determine the vesting terms at the time of grant. In 2007 the Company also repriced the existing non-officers' and non-insiders' stock option holders with original vesting date to CAD \$0.62 from CAD \$2.00 to better reflect the market condition and pricing and to retain key employees. There were 620,000 options repriced of which 185,000 were cancelled, thus, 435,000 net stock option holders were repriced to CAD \$0.62. The impact of the repriced options resulted in an increase to stock option compensation expense of \$62,553.

The expense for the Plan for the twelve month period and the comparative period was determined using the Black-Scholes option pricing model with the following assumptions: risk-free interest rates ranging from 2.73% to 3.47%; expected life of five years; no annual dividends paid; and expected volatility of 50%.

Compensation expense for stock options is recognized using the fair value when the stock options are granted and is amortized over the options' vesting period. During the year ended December 31, 2008, \$791,531 (2007 - \$433,223) was recognized as compensation expense in the consolidated statements of loss with a corresponding increase in contributed surplus. As at December 31, 2008, 2,253,494 stock options were exercisable and the weighted average years to expiration were 3.86 years. The fair value of options granted during the year that were outstanding at December 31, 2008 was \$1,362,675 or \$0.23 per option.

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	Share Options	Option Price		Share Options	Option Price
Outstanding, December 31, 2007	4,555,000	C\$1.37	December 31, 2006	4,542,500	C\$2.00
Granted	1,315,000	C\$0.62	Granted	2,070,000	C\$0.62
Granted	5,348,000	C\$0.65	Granted	-	C\$0.65
Granted	-	C\$2.00	Granted	1,495,000	C\$2.00
Cancelled	(1,119,999)	C\$0.62	Cancelled	-	C\$0.62
Cancelled	(632,000)	C\$0.65	Cancelled	-	C\$0.65
Cancelled	(2,150,001)	C\$2.00	Cancelled	(3,552,500)	C\$2.00
Outstanding, December 31, 2008	7,316,000	C\$0.64	December 31, 2007	4,555,000	C\$1.37
Exercisable at December 31, 2008	2,142,494	C\$0.62	December 31, 2007	122,083	C\$0.62
Exercisable at December 31, 2008	111,000	C\$0.65	December 31, 2007	-	C\$0.65
Exercisable at December 31, 2008	-	C\$2.00	December 31, 2007	1,035,417	C\$2.00

The following table summarizes information about the stock options outstanding at December 31, 2008:

Options Outstanding	Option Price CAD	Wtd. Avg. Remaining Contractual Life (years)	Options Currently Exercisable	Wtd. Avg. Exercise Price of Options Currently Exercisable CAD
110,000	\$0.62	2.30	91,669	\$0.62
10,000	\$0.62	2.42	8,331	\$0.62
10,000	\$0.62	2.67	7,498	\$0.62
45,000	\$0.62	2.97	29,995	\$0.62
35,000	\$0.62	3.16	20,414	\$0.62
20,000	\$0.62	3.24	11,668	\$0.62
75,000	\$0.62	3.39	37,497	\$0.62
635,000	\$0.62	3.68	410,420	\$0.62
500,000	\$0.62	3.75	500,000	\$0.62
55,000	\$0.62	3.85	18,333	\$0.62
10,000	\$0.62	3.87	3,336	\$0.62
10,000	\$0.62	3.98	3,333	\$0.62
85,000	\$0.62	4.05	-	\$0.62
500,000	\$0.62	4.11	500,000	\$0.62
500,000	\$0.62	4.17	500,000	\$0.62
2,600,000	\$0.62	3.82	2,142,494	\$0.62
500,000	\$0.65	4.54	-	\$0.65
1,201,000	\$0.65	4.54	111,000	\$0.65
2,025,000	\$0.65	4.62	-	\$0.65
100,000	\$0.65	4.63	-	\$0.65
100,000	\$0.65	4.71	-	\$0.65
790,000	\$0.65	4.87	-	\$0.65
4,716,000	\$0.65	4.54	111,000	\$0.65
Total	7,316,000	3.86	2,253,494	

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13. Related Party Transactions

- (a) The Company reinstated the consulting agreement in which \$48,817 was recorded for consulting services to a family member of a senior executive during the year ended December 31, 2008 (2007 - \$48,000). There was an outstanding balance of consulting fees as at December 31, 2008 of \$228 (2007 – nil).
- (b) Legal fees relating to general corporate matters are charged by the law firm at which a director is a partner. For the year ended December 31, 2008 these legal fees totaled \$62,021 (2007 – nil). There were \$4,036 in outstanding legal fees as at December 31, 2008 (2007 – nil).
- (c) The Company entered into a consulting agreement with a company owned by a senior executive in the fourth quarter of 2008. Consulting services of \$70,930 were recorded for the year ended December 31, 2008 (2007 – nil) and there was a balance owing as at December 31, 2008 of \$20,886 (2007 – nil).

All of the above related party transactions are recorded at agreed to exchange amounts which reflect fair values.

14. Commitments

- (a) As at December 31, 2008, the Company has made deposits and progress payments in the amount of \$2,146,064 toward the purchase of equipment to be delivered in 2009 (Note 23). The total progress payments and balance due on delivery is estimated to be \$2,704,003 and has been funded by the credit facility with the Lender.
- (b) The Company has entered into several lease agreements with major fleet leasing companies for the lease of vehicles. The terms of the leases vary from 12 to 72 months and the monthly lease payments total \$82,181. The leases are structured as operating leases. As at December 31, 2008, the total deposits on operating leases is \$406,861. The Company has also entered into several lease agreements for the rental of real property.

The following table represents the future payments required by all of the Company's equipment and real property lease agreements as at December 31, 2008:

2009	\$ 1,472,157
2010	986,937
2011	420,701
2012	272,863
2013	121,577
	<u>\$ 3,274,235</u>

- (c) The Company has agreed to reinstate the joint venture and the WISE™ technology license agreements with Al-Qahtani for the purpose of conducting business within Saudi Arabia and in the other Gulf Cooperation countries, including Yemen, Iraq and their respective territorial waters.
- (d) The Company's corporate office lease agreement requires a \$100,000 letter of credit. The Company has secured this letter of credit with a certificate of deposit (CD). This CD is listed as restricted cash in the accompanying financial statements.

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15. Restructuring Cost Recovery

The Company has recognized a restructuring cost recovery of \$500,811. The Company was able to negotiate releases from two of its real property lease agreements that had been included in the 2007 restructuring estimate and the estimate reported for the CEO termination in October 2007 was adjusted to actual cost during the year ended December 31, 2008. In addition, the cost of moving the corporate offices and the environmental clean-up of one of our facilities were both negotiated down from our original estimates.

16. Financial Instruments and Risk Management

The Company's activities expose it to a variety of financial risks with varying degrees of significance which could affect its ability to achieve its strategic objectives for growth and shareholder return. Risk management is the responsibility of the finance function and material risks are monitored and regularly discussed with the audit committee and the Board. The main financial risks affecting the Company are credit risk, market risk and liquidity risk.

(a) Credit risk

Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its contractual obligations. The Company's credit risk arises primarily from its accounts receivables, which are typically unsecured. The objective of managing counterparty credit risk is to prevent losses relating to financial assets. This risk is generally limited due to the large base of customers and the dispersion across various geographic areas. The Company performs regular credit assessments of its customers and provides allowances for potentially uncollectible accounts receivable. The amounts disclosed in the balance sheet are net of these allowances for bad debt. Accounts receivables are considered for impairment on a case-by-case basis when they are past due or when objective evidence is received that a customer will default. Bad debt expense is recorded within selling, general and administrative expense. Three (December 2007 – two) customers accounted for 24% (December 2007 – 12%) of the outstanding receivable balance at December 31, 2008. The Company believes there is no unusual exposure associated with the collection of these receivables. No other single customer accounted for more than 10% (December 2007 - 10%) of consolidated receivables at December 31, 2008.

The following table demonstrates the outstanding customer balances for December 31, 2008 and December 31, 2007:

	December 31, 2008		December 31, 2007	
	% of Accounts receivable	Outstanding balance	% of Accounts receivable	Outstanding balance
Customer A	9%	\$ 519,130	11%	\$ 723,152
Customer B	8%	444,003	0%	-
Customer C	7%	405,595	1%	58,709
Total	24%	\$ 1,368,728	12%	\$ 781,861

For the year ended December 31, 2008 approximately 13% (2007- 14%) of the revenues were earned from one customer. No other customer accounted for more than 10% of revenue for the years ended December 31, 2008 and 2007.

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The Company's products and services are concentrated within the oil and natural gas industries. As a result of this industry focus, the Company's current and future financial performance is largely dependent upon the overall economic conditions within this industry. The Company is not able to predict with certainty the changes in the financial stability of its customers. Any material change in the financial status of any one or group of customers could have a material effect on the Company's results of operations, financial position or cash flows.

The following table represents the details of the Company's aging of its receivables and the related allowance for doubtful accounts as at December 31, 2008:

Total accounts receivable	\$ 7,817,307
Less: Allowance for doubtful accounts	(873,489)
Total accounts receivable, net	<u><u>\$ 6,943,818</u></u>
Of which:	
Not overdue; under 30 days	\$ 3,463,321
Past due for more than one day but not more than three months	1,885,638
Past due for more than three months but not more than six months	1,379,581
Past due for more than six months but not more than one year	495,001
Past due for more than one year	593,766
Less: Allowance for doubtful accounts	(873,489)
Total accounts receivable, net	<u><u>\$ 6,943,818</u></u>

The Company reviews its accounts receivable for indicators of impairment on a quarterly basis and has recorded an allowance for doubtful accounts provision of \$873,489 (2007 – \$624,671). This impairment is primarily the result of customers who have filed bankruptcy or who are experiencing financial difficulties.

At December 31, 2008, a significant portion of the Company's cash was held at one financial institution.

The carrying value of accounts receivable approximates their fair value due to the relatively short periods to maturity on these assets. The maximum exposure to credit risk is represented by the net carrying value of financial assets.

(b) Market risk

Market risk is the risk that the fair value or future cash flows of the Company's financial instruments will fluctuate due to changes in market conditions. The primary financial risks to which the Company is exposed are interest rate risk and foreign currency risk:

(i) Interest rate risk

The Company's debt bears interest at a fixed rate and its accounts receivable facility is subject to the prime rate; therefore, the Company is not exposed to significant interest rate risk.

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(ii) Foreign currency risk

The Company incurs certain administrative costs in Canadian dollars and as such the Company has exposure to foreign currency rate fluctuation risk with regard to these expenses. At December 31, 2008, the Company had a net cash position of \$1,578 denominated in Canadian dollars. In addition, the Company shares are listed on a Canadian Exchange and as such the Company's equity financing are subject to foreign currency rate fluctuations. As these risks relate to the Canadian dollar, management does not believe these risks will have a significant impact on the Company's future operations. A \$0.01 increase in the Canadian / US exchange rate would reduce the cash flow of the Company by less than \$1,000. The Company considers this risk to be limited and therefore does not hedge its foreign exchange risk.

(c) Liquidity risk

Liquidity risk includes the risk that the Company is not able to meet its financial obligations as they become due or can do so only at excessive cost. Management continuously monitors its operating cash, forecasts and capital expenditure program and adjustments are made as variables change. As these variables change, liquidity risks may require the Company to obtain additions to its credit facility or to issue additional equity instruments. The Company maintains an insurance program to minimize exposure from third party uninsured losses which also assists with reducing the Company's liquidity risk. The Company's objective in managing liquidity is to maintain sufficient and readily available reserves in order to meet its liquidity requirements at any time. Given the balances due in the next twelve months due to the restructure of the long term debt there is a risk that the Company may not be able to meet its obligations as they come due (Note 2).

17. Capital Risk Management

The Company's objective when managing its capital is to safeguard the Company's assets and its ability to continue as a going concern while at the same time maximizing the growth of its business in order to provide an adequate return for shareholders. Management defines its capital as shareholders' equity and debt, including current portion. The Company's financial strategy is formulated and adapted according to market conditions in order to maintain a flexible capital structure that is consistent with the Company's objective. In order to maintain or adjust its capital structure, the Company may refinance its existing debt, raise new debt, repurchase shares for cancellation pursuant to normal course issuer bids, issue new shares, or adjust the amounts of dividends paid in cash or in kind.

The Company monitors capital using a number of financial metrics comprised mainly of the following ratios:

- Total debt principal and interest expense payments to Earnings Before Interest, Taxes, Depreciation and Amortization and Stock Option expense (EBITDAS); and
- Working capital

EBITDAS, a non-GAAP measure which does not have a standardized meaning prescribed by GAAP and therefore may not be comparable to similar measures presented by other issuers, is calculated as the sum of net earnings, plus interest on debt and balance of purchase price, other interest or income, income taxes, amortization of fixed assets, intangibles assets and other long-lived assets and stock option expense.

Total debt principal and interest expense payments to EBITDAS reflects the ability of the Company to meet its financial obligations associated with its debt by generating sufficient operating cash flow. A ratio in excess of 1 measures the ability of the Company to generate sufficient cash to pay its debt requirements.

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Working capital is defined as current assets divided by current liabilities less any indebtedness owed to the Lender. Working capital ratio in excess of 1 measures the liquidity of the Company and the ability of the Company to meet its current obligations.

The following tables illustrate the Company's total capital and its financial ratios as at December 31, 2008 and December 31, 2007.

	Objective	December 31, 2008	December 31, 2007
Debt, including current portion		\$ 37,493,291	\$ 47,025,554
Shareholders' equity		(3,806,014)	(87,291)
Total Capital		<u>\$ 33,687,277</u>	<u>\$ 46,938,263</u>
Current Assets		\$ 10,667,518	\$ 17,968,545
Current Liabilities		46,666,074	54,840,722
Less: Exclusion of debt and debt accruals		(39,493,291)	(45,478,679)
Adjusted current liabilities		<u>\$ 7,172,783</u>	<u>\$ 9,362,043</u>
Total Working Capital	Not less than 1.0 to 1.0	<u>1.49</u>	<u>1.92</u>

	Objective	Twelve Months Ended December 31, 2008	Twelve Months Ended December 31, 2007
Net earnings (loss)		\$ (29,850,430)	\$ (19,736,629)
Plus:			
Interest expense, net of income		10,287,787	4,369,829
Income Tax		162,496	749,155
Amortization		12,894,279	7,833,839
Stock options expense		791,531	433,223
Loss on discontinued operations		153,841	3,159,663
Loss on disposal of assets		406,803	359,523
EBITDAS		<u>\$ (5,153,693)</u>	<u>\$ (2,831,397)</u>
¹ Total debt principal and interest expense payments		\$ 4,863,088	\$ 6,474,503
² Total Adjusted EBITDAS		<u>\$ (2,969,994)</u>	<u>\$ (2,831,397)</u>
Total Interest to EBITDAS	Not less than 1.0 to 1.0	<u>(1.64)</u>	<u>(2.29)</u>

¹ The Company's costs associated with the Quest Offer (Note 4) and the restructuring of the debt are excluded.

² For purposes of the Company's financial covenants, EBITDAS does not include the Company's expenses associated with the Quest Offer (Note 4) in the amount of \$2,183,699 for year ended December 31, 2008.

The Company is also subject to financial covenants within its credit facility agreement which are measured on a quarterly basis. The Company was in compliance with its financial covenants as at December 31, 2008.

As a result of the Quest Offer (Note 4) and the restructuring of the debt, the Company moved into a more liquid position. However, as a result of the hurricanes that affected the Gulf Coast area during the year, the continuing decline in the price of oil and natural gas and the financial distress in the credit markets, revenue was down significantly during the year ending 2008 and the Company has not met its objectives for the year ended December 31, 2008.

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18. Impairment

- (a) Long-lived assets – In accordance with CICA Section 3063, long-lived assets are reviewed for impairment when events or circumstances indicate that the carrying amount of a long-lived asset may not be recovered. Examples of such events or changes in circumstances related to a long-lived asset include, but are not restricted to: a significant decrease in its market price; a significant adverse change in the extent or manner in which it is being used or in its physical condition; a significant adverse change in legal factors or in the business climate that could affect its value, including an adverse action or assessment by a regulator; an accumulation of costs significantly in excess of the amount originally expected for its acquisition or construction; a current-period operating or cash flow loss combined with a history of operating or cash flow losses, or a projection or forecast that demonstrates continuing losses associated with its use; or a current expectation that, more likely than not, it will be sold or otherwise disposed of significantly before the end of its previously estimated useful life ("more likely than not" means a level of likelihood that is more than 50 percent).

Long-lived assets are considered impaired if the carrying amount of the asset exceeds the fair value. If an asset is considered to be impaired, the impairment is measured by the amount by which the carrying amount of the asset exceeds its fair value, and is charged to results of operations at the time. A physical inspection of our equipment and the unit utilization forecast has revealed equipment in unusable condition and the costs of repairs is expected to exceed the value of these assets. The Company performed impairment testing of our long-lived assets of all our reporting units and determined that an impairment charge existed on several long-lived assets in the amount of \$3,381,619. The Company has had recent discussions with manufacturers and lenders that have indicated that the re-sale price of used equipment has declined ranging from twenty to forty percent due to the current economic conditions. As such, the fair market value of the identified assets was determined by applying a discount rate in such ranges to the net book value at December 31, 2008. The long-lived assets that have been impaired consist of pickup trucks, a coil tubing unit, two pumping units and several slickline units. In addition, the Company has identified furniture and fixtures, miscellaneous equipment and computers that are in irreparable physical condition and therefore an impairment charge has been recorded. The Company has also recorded an impairment charge for its assets held for sale in the amount of \$240,588. These units were acquired in 2007 in the Dyna Star acquisition (Note 5 (b)). The Company has been unsuccessful in selling these units despite soliciting several equipment brokers both domestic and foreign.

- (b) Goodwill – The Company reviews the carrying value of goodwill for impairment on an annual basis, at year end, or when events or changes in business circumstances indicate that the carrying value may not be recoverable. The Company has recorded goodwill associated with two separate acquisitions, each of which is considered a reporting unit. We use a two-step process to test goodwill for impairment. The fair value of each reporting unit is compared with its carrying amount, including goodwill, in order to identify a potential impairment. When the carrying amount of a reporting unit exceeds its fair value, the fair value of the reporting unit's goodwill should be compared with its carrying amount to measure the amount of the impairment loss, if any. Fair value is estimated using a discounted cash flow approach. If the carrying amount of the reporting unit goodwill exceeds the fair value the goodwill may be impaired and the second step of the impairment test is performed. The second step of the test is used to measure the amount of the impairment loss, if any. The implied fair value of the reporting unit's goodwill is determined by allocating the reporting unit's fair value to all of its assets and liabilities other than goodwill in a manner similar to a purchase price allocation. The implied fair value of the goodwill that results from the application of this step is then compared to the carrying amount of the goodwill and an impairment charge would be recorded for the difference if the carrying value exceeds the implied fair value of the goodwill.

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We performed our annual impairment test at year end. The fair value of our reporting units was estimated based on a discounted projection of cash flows. The rates used in determining cash flows for each of our reporting units was a rate corresponding to our cost of capital, adjusted for risk where appropriate. In determining estimated future cash flows, current and future levels of income were considered that reflected business trends and current market conditions. As a result of a decline in service pricing, the continuing decline of oil and natural gas prices and the deterioration of the credit markets, our impairment test indicated the complete impairment in our pressure pumping services and slickline services reporting units.

We performed the second step of the goodwill impairment test and determined that an impairment of goodwill existed in both reporting units. Accordingly, we recorded a non-cash goodwill impairment charge of \$1,644,748 for the year ended December 31, 2008 reducing our goodwill balance for both the pressure pumping services and slickline services reporting units to zero.

Changes in the carrying value of goodwill from January 1, 2007 to December 31, 2008 are summarized below:

	Pumping Services	Slickline Services	Total
Balance as at January 1, 2007	\$ 418,012	\$ -	\$ 418,012
Acquisition		926,736	926,736
Balance as at December 31, 2007	418,012	926,736	1,344,748
Changes in acquisition valuation		300,000	300,000
Impairment charge	(418,012)	(1,226,736)	(1,644,748)
Balance as at December 31, 2008	\$ -	\$ -	\$ -

- (c) Intangible Assets - An intangible asset that is subject to amortization should be tested for impairment in accordance with the provisions of CICA Section 3063, Long-lived assets and an intangible asset that is not subject to amortization should be tested for impairment annually, or more frequently if events or changes in circumstances indicate that the asset might be impaired. The impairment test should consist of a comparison of the fair value of the intangible asset with its carrying amount. When the carrying amount of the intangible asset exceeds its fair value, an impairment loss should be recognized in an amount equal to the excess. The Company has recorded an impairment charge for a patent purchased in conjunction with the Dyna Star acquisition (Note 5 (b)) in the amount of \$20,415 net of currency conversion. The Company has determined that this technology is not exploitable in its current target markets and its reporting unit was discontinued in 2007 (Note 20).

19. Future Income Tax

Future income taxes reflect the net tax effects of temporary timing differences between recognition of items such as amortization, for financial reporting purposes and the deductibility for income tax purposes. As at December 31, 2008 the Company and its subsidiaries have incurred cumulative non-capital losses for income tax purposes of approximately \$41,500,000 related to US entities and \$4,600,000 related to Canadian entities, which are available to reduce taxable income in future years. If not utilized, these losses will expire between 2024 to 2027. Due to the uncertainty of utilization, only a portion of the future income tax benefit of these losses has been recognized in the financial statements.

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(a) Principal components of the future tax asset are:

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Future Income Tax Provision

	2008	2007
Accrued Liability	\$ -	\$ -
Property, plant, and equipment	(1,959,199)	(2,343,629)
Intangible Assets	547,579	376,000
Non-capital losses	17,332,382	7,924,114
Deferred financing costs	1,192,320	1,388,716
	<u>17,113,082</u>	<u>7,345,201</u>
Valuation allowance	(17,113,082)	(7,345,201)
Future tax asset	<u>\$ -</u>	<u>\$ -</u>

(b) Rate Reconciliation

The effective tax rate of income tax varies from the statutory rate as follows:

	2008	2007
Combined statutory rate	38.21%	38.21%
Loss before taxes from continuing operations	\$ (29,513,678)	\$ (15,862,234)
Computed tax (benefit)	(11,277,176)	(6,061,000)
Increase (decrease) resulting from:		
Stock based compensation	302,000	152,000
Non-deductible expenses	136,000	166,000
Current state and business taxes	162,496	-
Valuation Allowance	9,767,881	6,466,673
Other reconciling items	908,799	(8,941)
Future income tax expense (recovery)	<u>\$ -</u>	<u>\$ 714,732</u>

The future tax asset is calculated based on management's best estimates of available tax pool balances and non-capital loss balances available. In calculating the current provision, management has made certain estimates and taken certain filing positions based on current and proposed legislation. Tax provision calculations are based on substantively enacted taxation rates and projected profitability. As such, by its nature, the tax provision is subject to measurement uncertainty. Tax filings made by the Company are subject to review and confirmation by the relevant taxation authorities. Such review and reassessment may result in changes to the available tax pools. Adjustments, if any, will be reflected in the period of adjustment. At the end of the period, subject to the confirmation by taxation authorities, the Company has \$46 million of tax losses expiring at varying dates between 2024 and 2027.

20. Discontinued Operations

As a result of the Company's decision to restructure its operations and the continued depressed Canadian oil and gas market, the Board voted on November 5, 2007 to discontinue its operations in the western Canadian oilfield services market. The results of operation of the Canadian operations have been reported within discontinued operations of the accompanying financial statements. During the year ended December 31, 2008 the Company reported a \$174,256 loss (2007 – loss of \$3,159,663) from discontinued operations. The Company has recorded a liability for future costs associated with these discontinued operations of nil at December 31, 2008 (\$212,057 - 2007).

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21. Contingencies

The Company is a defendant in several lawsuits arising from the normal course of business. Defense of these suits is in the preliminary stages and while no probable outcome can be determined at this time, management believes the Company will be successful in defending the claims. Accordingly, no estimated loss provision has been made in the accompanying financial statements.

The Company is a defendant in arbitration proceedings brought by three former key employees of the Company associated with the Change of Control (Note 4) provisions in their employment agreements. The Company intends to vigorously defend each claim and has asserted, or shall assert, counterclaims that the Company has to protect the rights of the Company. The Company has made a provision based on management's estimate of the potential liability.

22. Joint Venture

The Company has funded its 40% initial capital contribution for the joint venture with Al-Qahtani Marine & Oilfield Services Co. of Saudi Arabia in the amount of \$216,059. The Joint Venture Agreement establishes a Saudi company to be named Abdul Hadi Al Qahtani WISE Co Ltd to carry out the joint venture business and the production and delivery by PEG of mobile WISE™ units to service both offshore and onshore facilities (Note 14 (c)). As at December 31, 2008 the Company's investment in the Joint Venture was not subject to impairment.

23. Subsequent Events

As at February 16, 2009, the Company ceased all operations in Belize and all equipment and personnel have been returned to the United States.

Effective February 5, 2009, Jaime B. Crawford announced his retirement as Executive Vice President of Technology from WISE Well Intervention Services, Inc. Mr. Crawford will retain his position on the Board and will provide consulting services to the Company on further technology initiatives.

On March 5, 2009, the Company advised the manufacturer of its nitrogen units that the defects being experienced in the units have not been cured. Accordingly, the Company considers the manufacturing agreement terminated and demands a full refund of all monies paid for units delivered and currently being constructed totaling \$6,201,019. The Company has advised the manufacturer that it will seek restitution legally if the demand is not satisfied.

The Company will not be able to meet the first quarter 2009 principal and interest payments due to the Lender by March 31, 2009 and will be in breach of its debt covenants. In addition, the liquidity situation of the Company is marginal. The Lender has been advised of this situation and the Company and Lender are in discussions to amend the terms of the loan agreements. The Company believes such amendment will be finalized by the end of the second quarter of 2009. However, such discussions are preliminary at this time and no agreement on terms has been reached to date.