Quarterly Report Q2/09

August 12, 2009

Dear Shareholder:

Birchcliff is pleased to report its second quarter financial and operating results for the three and six month periods ended June 30, 2009.

During the quarter, Birchcliff focused on planning the execution of our capital expenditure programs for the remainder of 2009 and 2010. On July 9, 2009, we announced our expanded and refocused 2009 capital expenditure program, director's approval to construct our 100% owned Pouce Coupe South Natural Gas Plant and production guidance for 2009 and a portion of 2010. The information contained in the press release dated July 9, 2009 is discussed below as it is the foundation of our go forward strategy.

2009 SECOND QUARTER RESULTS

Production

Production for the second quarter of 2009 averaged 11,313 boe per day. This is an 18% increase from the second quarter of 2008 and ahead of our internal budget and previous guidance. Average production for the first six months of the year is 11,910 boe per day. In light of the very limited capital that we have spent in 2009, we are pleased with this production profile which exhibits a strong, long life, low decline production base.

Production will continue to grow as new Montney/Doig horizontal natural gas wells come on production.

Cash Flow and Earnings

Cash flow was $20.0 million or $0.18 per share for the second quarter of 2009, as compared to $41.7 million or $0.37 per share for the second quarter of 2008. Cash flow has increased by $5.6 million over the first quarter of 2009 notwithstanding extremely low commodity prices. This is a result of lower operating costs, lower royalties and the receipt of $4.8 million in prior period gas cost allowance credits and custom processing credits.

Birchcliff had an earnings loss of $7.1 million or $0.06 per share for the second quarter of 2009 as compared to earnings of $9.8 million or $0.09 per share for the second quarter of 2008. The earnings loss is a result of weak commodity prices during the quarter.

Capital Expenditures

Birchcliff achieved its goal of spending less than its cash flow in the first six months of the year notwithstanding the significant deterioration of commodity prices, and did so without seeing significant negative production declines.

Birchcliff intentionally spent very little money in the second quarter of 2009 in order to protect its balance sheet and reduce its debt in light of weak commodity prices. During the second quarter of 2009, capital spending aggregated $5.5 million as compared to $37.5 million for the same period in the prior year. This capital spending was less than our cash flow in the second quarter of 2009. Capital expenditures of $23.9 million for the first six months of 2009 is significantly less than our six month cash flow of $34.4 million which resulted in the reduction of Birchcliff's debt. Our production remained strong in the face of this reduced spending. During the second quarter, as a result of spring break-up, Birchcliff did not participate in or conduct any drilling operations and its projects were limited to minor capital items.

Details of our capital expenditures are set forth in the Management's Discussion and Analysis portion of the quarterly report.

Indebtedness and Equity Issue

Total indebtedness at June 30, 2009 was $179.6 million, including a working capital **surplus**, down from $253.5 million at the end of the first quarter of 2009. On June 30, 2009 Birchcliff was drawn to $219.4 million on its $305 million of available credit facilities. At June 30, 2009 the amount of bank indebtedness exceeded total indebtedness as Birchcliff was unable to apply the total proceeds of the equity financing that closed on June 30, 2009 to redeem unmatured bankers' acceptances outstanding. Accordingly, approximately $37 million of the financing proceeds were held as a cash balance to be applied in the third quarter to reduce bank indebtedness as those bankers' acceptances mature.

Birchcliff completed a bought deal financing and private placement for gross proceeds of $62 million on June 30, 2009. The equity issue consisted of 10 million common shares at a price of $6.20 per share. Proceeds of the issue were used to reduce indebtedness and to fund capital expenditures. At June 30, 2009 Birchcliff had 122,807,637 common shares outstanding.

Land

Birchcliff has continued to grow its undeveloped land base in the Peace River Arch. At June 30, 2009 it owned 394,700 gross (346,038 net) undeveloped acres, with an average working interest of 88% as compared to June 30, 2008 when it owned 342,830 gross (295,438 net) undeveloped acres with an average working interest of 86%.

Events Subsequent to the Second Quarter

On July 9, 2009, Birchcliff announced its increased 2009 capital expenditure program of $105 million and its decision to proceed immediately to construct its Pouce Coupe South natural gas plant (the "**PCS Gas Plant**"). This capital budget will allow Birchcliff to increase its strategic control of its core area in the Montney/Doig natural gas resource play, to increase its Montney/Doig production and further establish its position as a leading low cost resource finder and producer.

Birchcliff's 2009 Capital Expenditure Program can be segregated into two parts, capital expenditures of approximately $61.4 million associated with normal course oil and gas operations and capital expenditures of approximately $43.6 million related to its PCS Gas Plant and the related Montney/Doig horizontal natural gas drilling and infrastructure program. This will result in additional production to Birchcliff in 2010 when the PCS Gas Plant starts up.

2009 Capital Expenditures Relating to Normal Course Operations

On February 12, 2009 Birchcliff announced its original 2009 capital expenditure budget of $80 million. As a result of depressed natural gas prices, Birchcliff has reduced its planned 2009 normal course oil and gas operations capital expenditures to $61.4 million, which is less than currently estimated 2009 cash flow. Birchcliff has budgeted to spend approximately $40 million of this capital in the second half of 2009 which includes the drilling of 8 (7.7 net) wells. In the first half of 2009, $21.4 million of capital was spent on normal course oil and gas operations.

Birchcliff plans to continue to focus its capital spending primarily on the expansion of its Montney/Doig natural gas resource play with the majority of 2009 capital being directed to vertical and horizontal wells on lands to which no reserves were attributed in the December 31, 2008 independent engineering evaluation prepared by AJM Petroleum Consultants. This is expected to result in the addition of new low cost reserves and continued growth for Birchcliff during 2009 assuming drilling results are consistent or better than with those achieved by Birchcliff with past drilling on this resource play. During the second half of 2009, Birchcliff expects to spend approximately $18.4 million on drilling, related infrastructure and land on its Montney/Doig natural gas resource play which includes the drilling of 2 (2.0 net) Montney/Doig horizontal natural gas wells as part of its normal course oil and gas operations.

Second half budget plans for our second resource play, the Worsley light oil pool, allocates approximately $14 million to prove the further development and exploitation potential of the light oil pool and to fund a recently closed minor acquisition. This capital program includes the drilling of 1 (1.0 net) horizontal well and 3 (3.0 net) vertical wells as well as capital to support continued expansion of the waterflood program.

Pouce Coupe South Natural Gas Plant and Related Montney/Doig Natural Gas Drilling

On July 9, 2009, Birchcliff announced that the Board of Directors had approved the construction of its 100% owned PCS Gas Plant which will have an initial inlet design capacity of 30 mmcf per day. Birchcliff expects that the PCS Gas Plant will be fully operational early in the second quarter of 2010. Birchcliff expects to use a minimum of 70% of the plant capacity for its own natural gas from the Pouce Coupe area and the balance will be used for third party and/or partner gas.

Birchcliff expects to drill additional Montney/Doig horizontal natural gas wells which will commence production with the start-up of the PCS Gas Plant. Birchcliff expects that these wells will add approximately 3,400 boe per day of net production. With this additional production Birchcliff expects its production rate to increase to approximately 14,000 boe per day when the PCS Gas Plant is on stream.

The PCS Gas Plant is a significant milestone for Birchcliff as it will result in a step change in terms of production and will provide the following benefits:

1. increased production growth from the Pouce Coupe area where Birchcliff's current and future production growth is presently constrained by insufficient gathering and processing capacity;

2. reduced operating costs which will increase netbacks;
3. increased third party revenues which will reduce Birchcliff's operating costs and improve netbacks;
4. increased control over production volumes and decreased exposure to production curtailments caused by third party operated processing plants;
5. increased run times from its natural gas wells in the Pouce Coupe area;
6. increased ability to expand production in the area by expanding the processing capacity of the PCS Gas Plant to correspond with the timing of its drilling plans in the area;
7. increased strategic competitive advantage over competitors in Birchcliff's core development area; and
8. reduced construction cost of the PCS Gas Plant as a result of the currently increased availability of services and equipment necessary to complete construction and the resultant competitive pricing for plant components.

The PCS Gas Plant is being constructed in the heart of Birchcliff's Montney/ Doig natural gas resource play. Control of infrastructure is a key component to the successful development of any natural gas play but is magnified in these circumstances because of the intense competition for infrastructure and gathering and processing capacity as the development of unconventional natural gas in the Pouce Coupe area of Alberta continues to grow. Birchcliff has proven in the last several years that it can find and develop natural gas in its focus area at low costs. The PCS Gas Plant will allow Birchcliff to produce natural gas at lower operating costs than producers that rely on third party processing. This will position Birchcliff to become a dominant low cost finder and producer of natural gas in the Pouce Coupe area of Alberta.

Capital Expenditures and Drilling Associated with the Pouce Coupe South Gas Plant

The total cost of the PCS Gas Plant including the acid gas disposal well and related gathering and sales pipelines is estimated to be $47.5 million, of which $3 million was spent in 2008 on the acid gas disposal well and engineering work, $32.5 million is expected to be spent in 2009 and $12 million is expected to be spent in 2010. In 2009, $2.5 million has been spent to June 30, 2009.

Birchcliff expects to drill 7 (4.9 net) Montney/Doig horizontal natural gas wells and construct related pipelines in 2009 and 2010 at a net cost of approximately $28 million. This drilling program is expected to fully utilize the PCS Gas Plant capacity when it starts-up. Of this $28 million, during 2009, Birchcliff expects to spend $10.9 million to drill 4 (2.8 net) horizontal Montney/Doig natural gas wells. These wells will not add any production until the PCS Gas Plant commences operations. This drilling is in addition to the drilling included in the $61.4 million budgeted for 2009 normal course operations that are described above. To utilize the full capacity of the PCS Gas Plant, Birchcliff believes it will have to drill 3 to 4 more Montney/Doig horizontal natural gas wells during 2010 and 2 to 3 Montney/Doig horizontal natural gas wells during each of 2011 and 2012.

The long life low decline nature of the Montney/Doig horizontal natural gas wells builds a strong long term production profile for Birchcliff. An important feature of the Montney/Doig resource play is the limited capital that has to be spent to replace Birchcliff's base production declines and utilize the full capacity of the PCS Gas Plant.

The prolific high initial deliverability of these Montney/Doig horizontal natural gas wells returns Birchcliff's capital investment quickly, but just as importantly, Birchcliff expects that after the initial steep production declines, the wells will produce with relatively low decline rates for up to 20 years. It is this long term, low decline portion of the expected production profile that builds long term sustainable cash flow for Birchcliff and is the strategic reason why Birchcliff is moving forward with the development of the Montney/Doig natural gas resource play and the development of the PCS Gas Plant.

Pouce Coupe South Gas Plant Operating Costs

Assuming Birchcliff uses 70% of the PCS Gas Plant capacity and that the remainder of the capacity is being used by third parties, Birchcliff expects its operating costs for its Montney/Doig production in the Pouce Coupe area will fall to approximately $1 per mcf, which is a significant reduction from its current operating costs.

Alberta Royalty Incentive Programs

The recently announced extension to Alberta's New Well Royalty Reduction program and the Drilling Royalty Credit program provide material royalty incentives to Birchcliff. Each Montney/Doig horizontal natural gas well is approximately 4,200 metres in length and qualifies for a drilling incentive of $840,000 in royalty credits. Further, Birchcliff expects that the initial 0.5 bcf of natural gas produced from each new Montney/Doig horizontal natural gas well will result in additional royalty savings of approximately $350,000 assuming a natural gas price of CAD $3.25/GJ at AECO and even greater royalty savings of approximately $800,000 assuming a natural gas price of CAD $5.50/GJ at AECO.

Expansion of the Pouce Coupe South Gas Plant

As part of its future planning for the development of the Montney/Doig natural gas resource play, Birchcliff has designed into the critical components of the PCS Gas Plant, sufficient capacity to permit the expansion of its natural gas inlet design capacity to 60 mmcf per day. This is intended to permit the continued growth of Birchcliff's production from this prolific Montney/Doig play while improving processing costs. A phase 2 expansion could be operational as early as late 2010 but the decision to move forward with this phase 2 expansion will be made in the fourth quarter of 2009. That decision will be based upon, amongst other matters, Birchcliff's then current view of future natural gas prices.

2009 & 2010 Production

Birchcliff's estimated average production rate for the month of July 2009 was approximately 11,000 boe per day.

Birchcliff confirms the revised 2009 capital expenditure program is expected to result in a 2009 average production rate of approximately 11,300 boe per day. Birchcliff's 2009 exit production rate is expected to be approximately 11,700 boe per day. Birchcliff's average product mix for 2009 is expected to be 72% natural gas and 28% light oil. When the PCS Gas Plant is operational in the second quarter of 2010, Birchcliff expects its production to climb to 14,000 boe per day.

Operational Update

Since the end of the second quarter and as a result of the July 9, 2009 approval of the $105 million budget, Birchcliff is now very active operationally with drilling, completions and new facility construction. Currently, we have two drilling rigs working. The first rig recently spud a 70% working interest

Montney/Doig horizontal natural gas well. The second rig is drilling a 100% working interest Doig horizontal light oil well into a Doig light oil pool. This is our first application of horizontal drilling in this pool and this play. With success, we have a number of follow up locations. A third rig will soon be starting a multi-well light oil program at Worsley which will consist of 3 (3.0 net) vertical wells and 1 (1.0 net) horizontal well.

Year to date, Birchcliff has drilled 6 (4.8 net) wells; including 3 (2.4 net) Montney/Doig vertical exploration natural gas exploration wells, 2 (1.4 net) Montney/Doig horizontal natural gas wells, and 1 (1.0 net) dry hole. Of the wells drilled in 2009, only 1 (0.7 net) Montney/Doig horizontal natural gas well is on production. The second Montney/Doig horizontal natural gas well will be on production later this month.

Birchcliff is currently drilling its 20th operated Montney/Doig horizontal natural gas well. With each of these Montney/Doig horizontal wells we improve our technical expertise and reduce our operational risk. The results from the two Montney/Doig horizontal natural gas wells drilled cased and completed in 2009 further increase our confidence on the play.

Outlook

Based on Birchcliff's current capital structure, the royalty incentives available in Alberta, reduced service costs and the results that have been achieved to date on the Montney/Doig natural gas play, Birchcliff believes that proceeding with the business plan described above will position it to capture significant value from the Montney/Doig natural gas resource play over the coming years and expose Birchcliff to significantly more upside value potential when natural gas prices improve.

I am pleased to report that Mr. Seymour Schulich, Birchcliff's largest shareholder, purchased 2 million common shares in our equity issue on June 30, 2009 and subsequently purchased a further 1,950,000 common shares on July 29, 2009 bringing his total holdings to 28,950,000 common shares or approximately 23.6% of the outstanding Birchcliff stock. These recent share purchases demonstrate Mr. Schulich's confidence in Birchcliff's business plan and asset base. Thank you Mr. Schulich for your exceptional support and guidance.

Currently, we are on track, on schedule and on budget in executing our near term business strategy. We continue to monitor commodity prices which ultimately will determine our 2010 capital expenditure programs.

Thank you to all our staff for their hard work and to our shareholders for their continued support.

On behalf of the Executive of Birchcliff

Respectfully,

A. Jeffery Tonken

President & Chief Executive Officer

FINANCIAL AND OPERATIONAL HIGHLIGHTS

	Three months ended June 30, 2009	Three months ended June 30, 2008	**Six months ended June 30, 2009**	Six months ended June 30, 2008
OPERATING				
Daily Average Production				
Light Oil – barrels	2,844	2,728	2,998	2,778
Natural Gas – thousands of cubic feet	48,808	38,525	51,479	38,158
NGLs – barrels	335	434	332	389
Total – barrels of oil equivalent (6:1)	**11,313**	**9,583**	**11,910**	**9,526**
Average Sales Price ($ Canadian)				
Light oil – per barrel	63.84	121.39	56.25	107,82
Natural Gas – per thousand cubic feet	3.75	10.93	4.55	9.65
NGLs – per barrel	52.38	112.62	49.58	102.05
Total – barrels of oil equivalent (6:1)	**33.79**	**83.58**	**35.19**	**74.26**
Undeveloped Land				
Gross (acres)	394,700	342,830	394,700	342,830
Net (acres)	346,038	295,438	346,038	295,438
NETBACK AND COST				
($ per barrel of oil equivalent at 6:1)				
Petroleum and natural gas revenue	33.92	84.02	35.40	74.67
Royalties	2.06	(13.03)	(3.03)	(11.57)
Operating expense	(8.94)	(10.79)	(9.51)	(10.55)
Transportation and marketing expense	(2.32)	(2.69)	(2.37)	(2.78)
Netback	**24.72**	**57.51**	**20.49**	**49.77**
General and administrative expense, net	(2.85)	(2.41)	(2.33)	(2.07)
Stock-based compensation expense	-	-	-	(0.01)
Realized loss on risk management contracts	-	(4.71)	-	(4.24)
Realized loss on foreign exchange	-	(0.13)	-	(0.09)
Interest expense	(2.41)	(2.48)	(2.21)	(3.61)
Taxes	-	-	-	-
Cash Flow Netback	**19.46**	**47.78**	**15.95**	**39.75**
Depletion and depreciation expense	(21.64)	(24.52)	(21.71)	(24.62)
Accretion expense	(0.38)	(0.42)	(0.36)	(0.39)
Stock-based compensation expense	(4.80)	(1.55)	(3.10)	(1.49)
Amortization of deferred financing fees	(0.21)	-	(0.10)	-
Unrealized gain (loss) on risk management contracts	-	(6.38)	-	(2.66)
Unrealized gain (loss) on foreign exchange	-	0.11	-	0.17
Future income tax recovery (expense)	0.65	(3.82)	1.51	(2.93)
Net Earnings (Loss)	**(6.92)**	**11.20**	**(7.81)**	**7.83**
FINANCIAL				
Petroleum and Natural Gas Revenue ($000)	34,917	73,273	76,315	129,465
Cash Flow from Operations ($000)	20,026	41,676	34,380	68,940
Per share – basic ($)	0.18	0.37	0.31	0.65
Per share – diluted ($)	0.18	0.36	0.30	0.63
Net Earnings (Loss) ($000)	(7,128)	9,776	(16,829)	13,604
Per share – basic ($)	(0.06)	0.09	(0.15)	0.13
Per share – diluted ($)	(0.06)	0.08	(0.15)	0.12
Common Shares Outstanding				
End of Period – basic	122,807,637	112,375,970	122,807,637	112,375,970
End of Period – diluted	134,732,322	121,270,357	134,732,322	121,270,357
Weighted Average for Period – basic	112,887,812	112,234,676	112,673,756	105,543,511
Weighted Average for Period – diluted	113,817,095	117,074,630	113,383,175	110,062,054
Capital Expenditures ($000)	5,485	37,487	23,880	89,005
Working Capital (Deficiency) ($000)	39,712	(14,456) (1)	39,712	(14,456) (1)
Revolving Credit Facilities ($000)	219,361	148,922	219,361	148,922
Total Debt ($000)	179,649	163,378	179,649	163,378

(1) This amount excludes both the accrued liability for the unrealized loss of $11.1 million on oil price risk management contracts and the related future income tax asset of $3.3 million.

MANAGEMENT'S DISCUSSION AND ANALYSIS

This Management's Discussion and Analysis (**"MD&A"**) in respect of the three and six month periods ended June 30, 2009 (the "**Reporting Periods**") as compared to the three and six month periods ended June 30, 2008 (the "**Comparable Prior Periods**") is dated August 12, 2009.

The following discussion and analysis is management's assessment of the historical financial and operating results of Birchcliff Energy Ltd. (the "**Corporation**" or "**Birchcliff**") and should be read in conjunction with the unaudited financial statements of the Corporation for the Reporting Periods and the audited financial statements as at and for the years ended December 31, 2008 and 2007 together with the notes thereto, all of which has been prepared in accordance with Canadian Generally Accepted Accounting Principles ("**GAAP**").

Additional information relating to the Corporation is available on SEDAR at www.sedar.com. Birchcliff is listed for trading on the Toronto Stock Exchange ("**TSX**") under the symbol "**BIR**".

All dollar amounts in Canadian dollars unless otherwise stated.

NON-GAAP MEASURES

This MD&A and the Corporation's Second Quarter Report for 2009 make references to terms commonly used in the petroleum and natural gas industry, such as cash flow or cash flow netback, cash flow per share, operating netback and netback.

Cash flow, as discussed in this MD&A and in the Corporation's Annual Report for 2008, appears as a separate line on the Corporation's Statements of Cash Flows above "changes in non-cash working capital" and is reconciled to net income (loss) and comprehensive income (loss). In the Corporation's disclosure, netback and/or operating netback denotes petroleum and natural gas revenue less royalties, less operating expenses and less transportation and marketing expenses. Cash flow netback as used herein denotes net earnings plus future income tax expense (less any recovery), depletion, depreciation and accretion expense, unrealized losses from risk management contracts and foreign exchange (less unrealized gains), non-cash stock-based compensation expense and amortization of deferred financing fees.

These terms are not defined by Generally Accepted Accounting Principles and consequently, they are referred to as non-GAAP measures. The reader should be cautioned that these amounts may not be directly comparable to measures for other companies where similar terminology is used.

BOE CONVERSION

Barrel of oil equivalent ("**boe**") amounts may be misleading, particularly if used in isolation. A boe conversion ratio has been calculated using a conversion rate of six thousand cubic feet of natural gas to one barrel and is based on an energy equivalent conversion method primarily applicable at the burner tip. It does not necessarily represent an economic value equivalency at the wellhead. This conversion basis conforms to National Instrument 51-101 *Standards for Oil and Gas Activities of the Canadian Securities Administrators*.

OVERALL PERFORMANCE

Production

Production in the second quarter of 2009 averaged 11,313 boe per day, which is slightly above the previously announced guidance of 11,150 boe per day. This is a 10% decrease from the 12,513 boe per day the Corporation averaged in the first quarter of 2009 and an 18% increase from the average of 9,583 boe per day in the second quarter of 2008. The decrease from the first quarter of 2009 was mainly due to normal and flush production declines. The increase from the second quarter of 2008 is virtually all due to the Corporation's drilling and operational success on its two resource plays in 2008 and into the Reporting Periods. Birchcliff continues to add Montney/Doig horizontal wells to its production portfolio which continues to increase the longevity and reduce the decline rate of its base production profile.

For the second quarter of 2009, the Corporation's production consisted of approximately 72% natural gas and 28% crude oil and natural gas liquids.

Cash Flow and Earnings

Cash flow decreased to $20.0 million ($0.18 per share) and $34.4 million ($0.31 per share) for the three and six month Reporting Periods as compared to $41.7 million ($0.37 per share) and $68.9 million ($0.65 per share) for the Comparable Prior Periods. Birchcliff had a loss of $7.1 million ($0.06 per share) and $16.8 million ($0.15 per share) for the three and six month Reporting Periods as compared to earnings of $9.8 million ($0.09 per share) and $13.6 million ($0.13 per share) for the Comparable Prior Periods. The decrease in cash flow and net loss resulted from lower average commodity prices realized in the Reporting Periods as compared to the Comparable Prior Periods, notwithstanding increased production volumes.

The AECO daily spot averaged $3.46 per mmbtu in the three month Reporting Period as compared to $10.22 per mmbtu during the three month Comparable Prior Period, which is a 66% decrease. Canadian Edmonton Par prices averaged $65.90 per barrel in the three month Reporting Period as compared to $126.07 per barrel during the three month Comparable Prior Period, which is a 48% decrease. Both of these commodity price decreases translate into reduced cash flow available for exploration and development.

Capital Expenditures and Total Debt

Birchcliff spent $5.5 million and $23.9 million in the three and six month Reporting Periods as compared to $37.5 million and $89.0 million in the Comparable Prior Periods. Although the Corporation expected capital expenditures to equal its cash flow during the six month Reporting Period, capital expenditures were reduced in response to reduced commodity prices and as a result capital expenditures were $10.5 million less than cash flow for the six month Reporting Period. Of the $5.5 million and $23.9 million in capital spent, approximately $0.9 million and $2.5 million was spent on the construction of the Pouce Coupe South natural gas plant (the "**PCS Gas Plant**") in the three and six month Reporting Periods, respectively.

Capital expenditures for the three months ended June 30, 2009 were $5.5 million, with 31% ($1.7 million) spent on drilling and completions; 42% ($2.3 million) spent on equipment and facilities; 5% ($0.3 million) spent on land acquisitions; 4% ($0.2 million) spent on seismic and other exploration and approximately 18% ($1.0 million) spent on workovers and other, administrative assets and capitalized G&A.

The Corporation's total debt (including working capital) decreased by 28% from $249.9 million at December 31, 2008 to $179.6 million at June 30, 2009. The decrease is primarily a result of the proceeds from the June 30, 2009 equity financing described below which were partially used to pay down the Corporation's Revolving Credit Facilities and which increased cash reserves pending the maturity of bankers' acceptances after the end of the Reporting Period. The decrease in total debt is also due to capital spending for the first half of 2009 being less than cash flow for the same period.

Mergers & Acquisitions

The Corporation continues to review potential property acquisitions, joint venture opportunities and corporate mergers and acquisitions with the intention of completing such a transaction if acceptable terms can be negotiated. As a result, Birchcliff may at any time be involved in negotiations with other parties in respect of property acquisitions, joint venture opportunities and corporate merger acquisition opportunities.

MAJOR TRANSACTIONS AFFECTING FINANCIAL RESULTS

- On June 30, 2009, the Corporation completed an equity financing (the "**Equity Financing**") comprised of a bought deal equity offering (the "**Bought Deal Offering**") whereby it issued 8,000,000 common shares at a price of $6.20 per share for gross proceeds of $49.6 million and a private placement (the "**Private Placement**") with its major shareholder whereby it issued 2,000,000 common shares at a price of $6.20 per share for gross proceeds of $12.4 million, for total gross proceeds of $62 million. The net proceeds of the Equity Financing were $59.3 million.
- On May 21, 2009, the Corporation amended its credit agreement with its bank syndicate which increased its existing Revolving Credit Facilities to an aggregate limit of $255 million from $240 million and extended the conversion date of those facilities until May 21, 2010. The Revolving Credit Facilities consist of an extendible revolving term credit facility with an authorized limit of

$235 million (the “**Syndicated Credit Facility**”) and an extendible revolving working capital facility with an authorized limit of $20 million (the “**Working Capital Facility**”).

- On May 21, 2009, the Corporation established a new $50 million non-revolving one year term credit facility (the “**Term Facility**”). The Corporation’s use of the Term Facility is subject to consent of the Syndicate at the time of draw-down.
- On March 14, 2008, the Corporation completed a bought deal equity financing whereby it issued 1,522,843 flow-through common shares at a price of $9.85 per flow-through share and 14,375,000 common shares at a price of $8.00 per common share for total gross proceeds of $130 million and net proceeds of approximately $123 million. Proceeds of the offering were used to retire the $100 million syndicated non-revolving credit facility used for the Worsley Acquisition and to reduce the amount outstanding under the Corporation’s revolving credit facility.

LIQUIDITY AND BANK DEBT

Working Capital

The Corporation’s working capital increased to a surplus of $39.7 million at June 30, 2009 as compared to a $38.3 million working capital deficit at December 31, 2008. The increase in working capital is largely comprised of cash proceeds received from the Equity Financing. The increased working capital also corresponds to the decrease in operational activity during the three month Reporting Period. At June 30, 2008, the working capital deficit of $14.5 million excluded an accrued liability of $11.1 million relating to the mark-to-market unrealized loss on oil price risk management contracts and an accrued asset of $3.3 million relating to future income taxes on the unrealized loss on risk management contracts.

At June 30, 2009 the major components of Birchcliff’s current assets were proceeds from the Equity Financing (62%) and cash to be received from its marketers in respect of June 2009 production (18%) which was subsequently received in July 2009. In contrast, the current liabilities consisted of trade payables (54%) and accrued capital and operating costs (46%).

Birchcliff manages its working capital using its cash flow and advances under its Revolving Credit Facilities. The Corporation’s working capital position does not reduce the amount available under the Corporation’s Revolving Credit Facilities which have a combined limit of $255 million at June 30, 2009. The Corporation was compliant with all covenants under its Revolving Credit Facilities throughout 2008 and continues to be compliant with such covenants throughout 2009 at the date hereof. The Corporation did not have any liquidity issues with respect to the operation of its petroleum and natural gas business in the Reporting Periods.

Bank Debt

The Corporation’s Revolving Credit Facilities were drawn to $219.4 million as at June 30, 2009, with an aggregate limit of $255 million as compared to $211.6 million as at December 31, 2008, when the aggregate limit was $240 million. The level of bank indebtedness at June 30, 2009 does not reflect approximately $37 million of proceeds from the Equity Financing that closed that day which were held as cash because the proceeds could not be immediately applied to reduce bank indebtedness represented by unmatured bankers’ acceptances. This cash will be applied in the third quarter to reduce bank indebtedness when the bankers’ acceptances mature.

The level of bank debt at June 30, 2009 was decreased by cash flow during the six month Reporting Period in excess of capital spent during that period, increased by a significant reduction in outstanding payables during the six month Reporting Period, and decreased by the application of $22.3 million of the net proceeds from the Equity Financing to reduce amounts outstanding under the Corporation’s Revolving Credit Facilities. At June 30, 2008, the Corporation’s Revolving Credit Facilities were drawn to $148.9 million.

The Corporation’s Revolving Credit Facilities at June 30, 2009 consisted of a $20 million Working Capital Facility and a $235 million Syndicated Credit Facility. At the end of the six month Reporting Period, the effective interest rate applicable to the Working Capital Facility was 4.8% as compared to 5.4% at the end of the six month Comparable Prior Period. The overall effective interest rate applicable to the bankers’ acceptances under the Syndicated Credit Facility was 2.0% and 2.5% during the three and six month Reporting Periods as compared to 4.1% and 4.4% during the Comparable Prior Periods.

On May 21, 2009, the Corporation established a new $50 million one year Term Facility. The Corporation's use of this Term Facility is subject to consent of the bank syndicate at the time of draw-down. No amounts were requested to be drawn under this Term Facility during the Reporting Periods.

CASH FLOW FROM OPERATIONS

Cash flow generated by the Corporation was $20.0 million ($0.18 per share) and $34.4 million ($0.31 per share) during the three and six month Reporting Periods as compared to $41.7 million ($0.37 per share) and $68.9 million ($0.65 per share) in the Comparable Prior Periods. The 52% and 50% decreases for the three and six month periods were mainly due to higher average commodity prices realized in the prior year. However, these decreases were mitigated by higher petroleum and natural gas production as a result of the drilling success in 2008 and early 2009. Future cash flow will be dependent mainly on production levels and commodity prices.

OUTSTANDING SHARE DATA

The common shares of Birchcliff are the only class of shares outstanding. Birchcliff's common shares began trading on the TSX Exchange on July 21, 2005 under the symbol "**BIR**" and were at the same time de-listed from the TSX Venture Exchange where they were trading under the same symbol prior to such time. The following table summarizes the common shares issued from December 31, 2008 to June 30, 2009:

	Common Shares
Balance at December 31, 2008	**112,395,970**
Issue of Common Shares upon exercise of options	146,665
Balance at March 31, 2009	**112,542,635**
Issue of Common Shares upon exercise of options	265,002
Issue of Common Shares(1)	10,000,000
Balance at June 30, 2009	**122,807,637**

(1) Issued under a bought deal equity offering of 8,000,000 common shares and a private placement of 2,000,000 common shares on June 30, 2009.

RESULTS OF OPERATIONS

Petroleum and Natural Gas Revenue

Petroleum and natural gas revenues totaled $34.9 million for the three month Reporting Period and $76.3 million for the six month Reporting Period as compared to $73.3 million and $129.5 million for the Comparable Prior Periods. The decreases were primarily attributable to significantly lower average commodity prices during the Reporting Periods. The following table details Birchcliff's petroleum and natural gas revenue ("**P&NG**"), production and sales prices by category for the Reporting Periods and the Comparable Prior Periods:

	Three months ended June 30, 2009				Three months ended June 30, 2008			
	Total Revenue ($000's)	Average Daily Production	%	Average ($/unit)	Total Revenue ($000's)	Average Daily Production	%	Average ($/unit)
Natural gas (mcf)	16,672	48,808	72	3.75	38,304	38,525	67	10.93
Light oil (bbls)	16,522	2,844	25	63.84	30,141	2,728	28	121.39
Natural gas liquids (bbls)	1,595	335	3	52.38	4,443	434	5	112.62
Total P&NG sales	**34,789**	**11,313**	**100**	**33.79**	**72,888**	**9,583**	**100**	**83.58**
Royalty revenue	128			0.12	385			0.44
Total P&NG revenue	**34,917**			**33.92**	**73,273**			**84.02**

	Six months ended June 30, 2009				Six months ended June 30, 2008			
	Total Revenue ($000's)	Average Daily Production	%	Average ($/unit)	Total Revenue ($000's)	Average Daily Production	%	Average ($/unit)
Natural gas (mcf)	42,363	51,479	72	4.55	67,021	38,158	67	9.65
Light oil (bbls)	30,525	2,998	25	56.25	54,507	2,778	29	107.82
Natural gas liquids (bbls)	2,980	332	3	49.58	7,226	389	4	102.05
Total P&NG sales	**75,868**	**11,910**	**100**	**35.19**	**128,754**	**9,526**	**100**	**74.26**
Royalty revenue	447			0.21	711			0.41
Total P&NG revenue	**76,315**			**35.40**	**129,465**			**74.67**

Commodity Prices

Birchcliff sells all of its crude oil on a spot basis. Birchcliff sells virtually all of its natural gas production for prices based on the AECO daily spot price. Birchcliff receives premium pricing for its natural gas due to its high heat content. The following table details the average sales price and differential received by Birchcliff for natural gas during the Reporting Periods and Comparable Prior Periods:

	Three months ended June 30, 2009	Three months ended June 30, 2008	**Six months ended June 30, 2009**	Six months ended June 30, 2008
Average Natural Gas Sales Price ($/mcf)	3.75	10.93	4.55	9.65
Average of the AECO Daily Spot Prices ($/mmbtu) [1]	3.46	10.22	4.21	9.10
Positive Differential	**0.29**	**0.71**	**0.34**	**0.55**

[1] $1.00/mmbtu = $1.00/mcf based on a standard heat value mcf.

The price the Corporation receives for its commodity production depends on a number of factors, including AECO Canadian dollar spot market prices for natural gas, Canadian dollar Edmonton par oil prices, U.S. dollar oil prices, the U.S./Canadian dollar exchange rate, and transportation and product quality differentials. Birchcliff regularly considers managing the risks associated with fluctuating spot market prices for natural gas and U.S. dollar oil prices and the U.S./Canadian dollar exchange rate. Birchcliff currently has no fixed commodity price contracts or other hedge type contracts for its natural gas and light oil production in 2009, but entered into the following oil price risk management contracts for its 2008 light oil production for the terms noted below:

Risk Management Contracts

Term	Type	Quantity	WTI Price (USD)[2]
January 1 - March 31, 2008[1]	Put	1,000	$67.50
January 1 - March 31, 2008[1]	Call	1,000	$81.40
January 1 - December 31, 2008	Costless collar	1,000	$67.50 - $79.10

(1) Each contract was entered into separately on different dates but the two contracts essentially form a costless collar.
(2) Each contract is settled on the average of the daily NYMEX WTI US$ price.

All of the Corporation's oil price risk management contracts outstanding in 2008 were settled at December 31, 2008. The Corporation did not enter into, nor had in place, any oil price risk management contracts during the Reporting Periods. As a result of the changes in the fair value of its oil price risk management contracts during the three and six month Comparable Prior Periods, the Corporation recorded to income a realized oil price risk management loss of $4.1 million and $7.3 million and an unrealized oil price risk management loss of $5.6 million and $4.6 million, respectively.

Due to the significant time and costs required to document the effectiveness of commodity price risk management contracts as hedges, Birchcliff does not account for its risk management contracts as hedges in its financial statements. The oil price risk management contracts are instead recorded at their fair values (mark-to-market) at each period end date, and realized and unrealized gains or losses on risk management contracts are shown as a separate category in the statement of net income (loss), comprehensive income (loss) and retained earnings.

The Corporation actively monitors the market to determine whether any additional commodity price risk management contracts are warranted. The Corporation has no current intention to enter into further commodity price risk management contracts.

Royalties

Royalties are paid to various government entities and other land and mineral rights owners. The following table illustrates the Corporation's royalty expense:

	Three months ended June 30, 2009	Three months ended June 30, 2008	**Six months ended June 30, 2009**	Six months ended June 30, 2008
Oil & natural gas royalties ($000's)	(2,118)	11,361	6,526	20,061
Oil & natural gas royalties ($/boe)	(2.06)	13.03	3.03	11.57
Royalties as a percentage of sales	(6.1%)	16%	8.6%	16%

Birchcliff recorded a net royalty credit of $2.1 million ($2.06 per boe) for the three month Reporting Period and a royalty expense of $6.5 million ($3.03 per boe) for the six month Reporting Period as compared to an expense of $11.4 million ($13.03 per boe) and $20.1 million ($11.57 per boe) for the Comparable Prior Periods. The overall effective royalty rate in the three and six month Reporting Period was (6.1%) and 8.6% as compared to 16% in the Comparable Prior Periods.

For the three month Reporting Period the Corporation received a royalty credit of $4.8 million, relating to 2008 and prior periods. After adjusting for this, the effective royalty rate for the three month reporting period would be 7%, as compared to 16% in the Comparable Prior Period. The 9% decrease in the effective royalty rate is a result of lower commodity prices but is also affected by the new royalty framework for 2009 and by the gas cost allowance and custom processing credits. The majority of the $4.8 million credit relates to the annual reconciliation of actual amounts in 2008 of capital expenditures eligible for gas cost allowance and processing fees eligible for a custom processing deduction in calculating royalties, as compared to estimates of those amounts previously used on an interim basis. The estimates used were based on 2007 data and they were substantially low as compared to the capital and custom processing fees actually incurred as a result of the large amount of capital spent and the large volumes of gas brought on during 2008.

For the six month Reporting Period the Corporation received a royalty credit of $3.7 million, relating to 2008 and prior periods. After adjusting for this, the effective royalty rate for the three month reporting period is 12%, as compared to 16% in the Comparable Prior Period. The 4% decrease in effective royalty rate is a result of lower commodity prices but is also affected by the new royalty framework for 2009 and by the gas cost allowance and custom processing credits, as discussed above.

New Royalty and Drilling Incentives

On March 3, 2009 the Government of Alberta announced two new short-term royalty incentives to stimulate new and continued economic activity in Alberta. The most important aspects of these initiatives are as follows:

a) new conventional oil and natural gas wells spud after April 1, 2009 and rig released on or before March 31, 2010 will be entitled to a royalty credit of $200 per meter drilled, up to a maximum of 50% (in Birchcliff's case) of the aggregate royalties payable by Birchcliff during that period; and

b) an incentive royalty rate of 5% for the first year of production from each new oil or gas well brought on production after April 1, 2009 and before March 31, 2010 up to a maximum for such well of 50,000 barrels of oil or 500 million cubic feet of natural gas.

On June 25, 2009, the Government of Alberta announced an extension to the above royalty incentives for one additional year, up to March 31, 2011. These incentives will provide material royalty relief with respect to Birchcliff's drilling activities. As a result, during the two year term of the drilling royalty credit and the term of the incentive royalty rate, Birchcliff intends to focus its capital spending program in large part on its Montney/Doig horizontal wells.

Operating Costs

Operating costs were $9.2 million ($8.94 per boe) for the three month Reporting Period and $20.5 million ($9.51 per boe) for the six month Reporting Period as compared to $9.4 million ($10.79 per boe) and $18.3 million ($10.55 per boe) for the Comparable Prior Periods. The following table compares operating costs for the Reporting Periods and the Comparable Prior Periods:

	Three months ended June 30, 2009		Three months ended June 30, 2008	
	Total ($000's)	$/boe	Total ($000's)	$/boe
Field operating costs	10,493	10.19	8,968	10.28
Recoveries	(1,084)	(1.05)	(457)	(0.52)
Field operating costs, net of recoveries	9,409	9.14	8,511	9.76
Expensed workovers and other	(203)	(0.20)	898	1.03
Total operating costs	**9,206**	**8.94**	**9,409**	**10.79**
	Six months ended June 30, 2009		Six months ended June 30, 2008	
	Total ($000's)	$/boe	Total ($000's)	$/boe
Field operating costs	22,373	10.38	18,385	10.61
Recoveries	(2,104)	(0.97)	(1,070)	(0.62)
Field operating costs, net of recoveries	20,269	9.41	17,315	9.99
Expensed workovers and other	222	0.10	985	0.56
Total operating costs	**20,491**	**9.51**	**18,300**	**10.55**

In light of currently weak commodity prices Birchcliff is focused on a priority basis on controlling and reducing operating costs on a per boe basis.

The $1.85 per boe decrease in total operating costs during the three month Reporting Period as compared to the three month Comparable Prior Period was mainly due to higher third party recoveries ($0.53 per boe), lower costs of expensed workovers ($1.23 per boe) and generally reduced costs of supplies and services ($0.09 per boe).

The $1.04 per boe decrease in total operating costs during the six month Reporting Period as compared to the six month Comparable Prior Period was mainly due to higher third party recoveries ($0.35 per boe), lower costs of expensed workovers ($0.46 per boe) and generally reduced costs of supplies and services ($0.23 per boe). Recoveries increased on a per boe basis during the Reporting Periods mainly due to higher third party compression fees.

Transportation and Marketing Expenses

Transportation and marketing expenses were $2.4 million ($2.32 per boe) for the three month Reporting Period and $5.1 million ($2.37 per boe) for the six month Reporting Period as compared to $2.3 million ($2.69 per boe) and $4.8 million ($2.78 per boe) for the Comparable Prior Periods. These costs consist primarily of transportation costs. The unit cost per boe for the Reporting Periods were lower than in the Comparable Prior Periods due to a proportionate increase in gas production, which has much lower transportation costs than the Worsley light oil field.

General and Administrative Expense

Net general and administrative costs ("**G&A**") for the three and six month Reporting Periods were $2.9 million ($2.85 per boe) and $5.0 million ($2.33 per boe) as compared to $2.1 million ($2.41 per boe) and $3.6 million ($2.07 per boe) for the Comparable Prior Periods.

The components of G&A are as follows:

	Three months ended June 30, 2009		Three months ended June 30, 2008	
	($000's)	%	($000's)	%
Salaries, benefits and consultants	2,290	59	2,256	61
Other	1,617	41	1,424	39
G & A expense, gross	3,907	100	3,680	100
Overhead recoveries	(589)	(15)	(1,249)	(34)
Capitalized overhead	(382)	(10)	(333)	(9)
G & A expense, net	**2,936**	**75**	**2,098**	**57**
G & A expense, net per boe	**$2.85**		**$2.41**	

	Six months ended June 30, 2009		Six months ended June 30, 2008	
	($000's)	%	($000's)	%
Salaries, benefits and consultants	4,399	59	4,214	59
Other	3,059	41	2,945	41
G & A expense, gross	7,458	100	7,159	100
Overhead recoveries	(1,639)	(22)	(2,831)	(40)
Capitalized overhead	(792)	(11)	(748)	(10)
G & A expense, net	**5,027**	**67**	**3,580**	**50**
G & A expense, net per boe	**$2.33**		**$2.07**	

The net G&A per boe has increased in the Reporting Periods mainly due to lower overhead and capital recoveries which are attributable to the decreased capital spent in the Reporting Periods as compared to the Comparable Prior Periods.

The capitalization of costs in the "overhead recoveries" category reflects an industry standard charge per AFE to capitalize engineering, land, accounting and operations time spent on capital projects, whereas the "capitalized overhead" category reflects a portion of costs in relation to only Birchcliff's exploration and geology department.

Interest Expense and Deferred Financing Fees

Interest expense and amortization of deferred financing fees for the three and six month Reporting Periods was $2.7 million ($2.62 per boe) and $5.0 million ($2.31 per boe) as compared to $2.2 million ($2.48 per boe) and $6.3 million ($3.61 per boe) for the Comparable Prior Periods. Included in these amounts during the Reporting Periods was $212,365 of amortized deferred financing fees related to amounts paid by the Corporation to establish the Term Facility and to extend the conversion date of the Revolving Credit Facilities to May 21, 2010. The decrease in aggregate interest expense and interest expense per boe in the six month Reporting Period as compared to the Comparable Prior Period was primarily a result of the lower effective interest rates on the Corporation's Revolving Credit Facilities during the six month Reporting Period. The amortization of deferred financing fees is a non-cash item and therefore is not deducted in determining cash flow as defined in the MD&A.

At the end of the six month Reporting Period, the effective rate applicable to the Working Capital facility was 4.8% as compared to 5.4% at the end of the six month Comparable Prior Period. The overall effective interest rate applicable to the bankers' acceptances in the Syndicated Credit Facility was 2.0% in the three month Reporting Period and 2.5% in the six month Reporting Period as compared to 4.1% and 4.4% in the Comparable Prior Periods. The Corporation's average bank debt was approximately $224.6 million in the six month Reporting Period as compared to $191.8 million in the six month Comparable Prior Period calculated as the simple average of the month end amounts.

Depletion, Depreciation and Accretion Expense

Depletion, depreciation and accretion ("**DD&A**") expenses for the three and six month Reporting Periods were $22.7 million ($22.02 per boe) and $47.6 million ($22.07 per boe) as compared to $21.7 million ($24.94 per boe) and $43.4 million ($25.01 per boe) for the Comparable Prior Periods. The DD&A on a per boe basis is lower in the Reporting Periods as compared to the Comparable Prior Periods mainly due to the reduced cost of adding proved reserves during 2008 and into the first half of 2009.

The components of DD&A are as follows:

	Three months ended June 30, 2009		Three months ended June 30, 2008	
	Total ($000's)	$/boe	Total ($000's)	$/boe
Depletion & depreciation	22,275	21.64	21,379	24.52
Accretion for asset retirement obligations	392	0.38	369	0.42
Total DD&A	**22,667**	**22.02**	**21,748**	**24.94**

	Six months ended June 30, 2009		Six months ended June 30, 2008	
	Total ($000's)	$/boe	Total ($000's)	$/boe
Depletion & depreciation	46,803	21.71	42,695	24.62
Accretion for asset retirement obligations	776	0.36	669	0.39
Total DD&A	**47,579**	**22.07**	**43,364**	**25.01**

Depletion and depreciation expense is a function of the estimated proved reserve additions and the cost of petroleum and natural gas properties in the full cost pool attributable to those proved reserves. At June 30, 2009, the Corporation excluded from its full cost pool $41.5 million (June 30, 2008 - $37.0 million) of costs for undeveloped land acquired by Birchcliff and for unproved properties acquired relating to opportunities in the probable reserve category and the potential drilling, recompletion and workover opportunities which have not yet been assigned any reserves.

Petroleum and Natural Gas Properties Impairment Test

The Corporation follows the full cost method of accounting which requires periodic review of capitalized costs to ensure that they do not exceed the recoverable value of the petroleum and natural gas properties and the fair value of the Corporation's assets.

Birchcliff performed an impairment review at June 30, 2009 on its petroleum and natural gas assets. Based on this review, Birchcliff determined there was no impairment of its petroleum and natural gas assets.

Taxes

Birchcliff recorded a future income tax recovery of $0.7 million ($0.65 per boe) for the three month Reporting Period and $3.3 million ($1.51 per boe) for the six month Reporting Period, as compared to an expense of $3.3 million ($3.82 per boe) and $5.1 million ($2.93 per boe) for the Comparable Prior

Periods. This recovery was attributed to the net loss recorded during the Reporting Periods, mainly as a result of lower average commodity prices during those periods. Birchcliff incurred $NIL and $NIL Part XII.6 taxes in the three and six month Reporting Periods as compared to $NIL and a recovery of $6,455 in the Comparable Prior Periods.

Stock-Based Compensation

Birchcliff accounts for its stock-based compensation programs, including performance warrants and stock options, using the fair value method. Under this method, the Corporation records compensation expense related to the stock-based compensation programs in the income statement over the vesting period.

The Corporation recorded a total stock-based compensation expense of $4.9 million ($4.80 per boe) in the three month Reporting Period and $6.7 million ($3.10 per boe) in the six month Reporting Period, as compared to $1.4 million ($1.55 per boe) and $2.6 million ($1.49 per boe) during the Comparable Prior Periods.

The Corporation recorded $1.9 million and $3.6 million of stock-based compensation expense relating to stock options in the three month and six month Reporting Periods. During the three month Reporting Period, the Corporation granted options to purchase 208,000 common shares (Comparable Prior Period – 169,000) at a weighted average exercise price of $6.46 per common share ($13.15 in the Comparable Prior Period). Of these options, at June 30, 2009 there remained outstanding options to purchase 208,000 common shares as compared to 169,000 options at June 30, 2008.

During the three month Reporting Period, the Corporation issued 265,002 common shares (Comparable Prior Period – 512,881 common shares) due to the exercise of vested stock options and stock options in respect of 93,834 common shares (Comparable Prior Period – 74,334 common shares) were forfeited or expired. In addition, there were no vested stock options cancelled in the Reporting Periods, as compared to NIL and 5,000 vested stock options in the respective Comparable Prior Periods. The cancellation of these vested stock options resulted in a cash-paid stock-based compensation expense of $NIL and $20,000 during the three and six months ended June 30, 2008. The Corporation is no longer making cash payments for the cancellation of vested stock options. The cash-paid expense is included in the total stock-based compensation expense.

On May 28, 2009, the ultimate expiration date of the Corporation's outstanding performance warrants was extended from January 31, 2010 to January 31, 2015 (the "**Extension**"). The Corporation recorded a non-cash stock-based compensation expense of $3.1 million relating to the extension of the performance warrants during the three and six month Reporting Periods. This amount represents the fair value of the Extension determined by the difference between the fair value of the outstanding performance warrants with the expiration date of January 31, 2015 and the fair value of the outstanding performance warrants with the expiration date of January 31, 2010. The fair value in each case was estimated as at May 28, 2009 using the Black-Scholes option-pricing model that takes into account: exercise price, expected life, current price, expected volatility, expected dividends, and risk-free interest rates.

CAPITAL EXPENDITURES AND CAPITAL RESOURCES

Capital expenditures amounted to $5.5 million and $23.9 million during the three and six month Reporting Periods as compared to $37.5 million and $89.0 million during the Comparable Prior Periods. The decrease in expenditures was in response to declining average commodity prices in the Reporting Periods as compared to the Comparable Prior Periods.

Capital Expenditures

The following table sets forth a summary of the Corporation's capital expenditures incurred during the Reporting Periods and the Comparable Prior Periods:

Three months ended June 30, ($000's)	**2009**	2008
Land	252	6,704
Seismic	193	(44)
Workovers and other	555	1,479
Drilling and completions	1,684	10,807
Well equipment and facilities	2,316	8,407
Capitalized general and administrative expenses	382	333
Total finding and development costs (F&D)	**5,382**	**27,686**
Acquisitions, net	-	9,671
Total finding, development and acquisition costs (FD&A)	**5,382**	**37,357**
Administrative assets	103	130
Total capital expenditures	**5,485**	**37,487**

Six months ended June 30, ($000's)	**2009**	2008
Land	577	9,741
Seismic	344	817
Workovers and other	611	4,087
Drilling and completions	12,356	45,122
Well equipment and facilities	8,823	18,368
Capitalized general and administrative expenses	793	748
Total finding and development costs (F&D)	**23,504**	**78,883**
Acquisitions, net	30	9,855
Total finding, development and acquisition costs (FD&A)	**23,534**	**88,738**
Administrative assets	346	267
Total capital expenditures	**23,880**	**89,005**

The following table sets forth a summary of the Corporation's capital resources for the Reporting Periods and the Comparable Prior Periods:

Capital Resources

Three months ended June 30, ($000's)	**2009**	2008
Cash generated by operations	20,026	41,676
Changes in working capital from operations	(11,518)	(592)
Asset retirement expenditures	(22)	48
Equity issues, net of issue costs	60,147	2,001
Increase (decrease) in revolving credit facilities	(8,302)	15,887
Deferred financing fees paid	(1,975)	-
Changes in working capital from investing	(15,757)	(21,533)
Total capital resources	**42,599**	**37,487**

Six months ended June 30, ($000's)	**2009**	2008
Cash generated by operations	34,380	68,940
Changes in working capital from operations	(5,768)	(8,412)
Asset retirement expenditures	(273)	(66)
Equity issues, net of issue costs	60,755	129,670
Decrease in non-revolving credit facility	-	(98,830)
Increase (decrease) in revolving credit facilities	8,980	(6,932)
Deferred financing fees paid	(1,975)	-
Changes in working capital from investing	(35,105)	4,634
Total capital resources	**60,994**	**89,004**

SELECTED QUARTERLY INFORMATION

Quarters Ended ($000's, except share and per share amounts)	June 30, 2009	March 31, 2009	December 31, 2008	September 30, 2008
Petroleum and natural gas production (boe per day)	11,313	12,513	11,524	10,000
Petroleum and natural gas commodity price ($ per boe)	33.79	36.48	47.88	73.44
Natural gas commodity price at wellhead ($ per mcf)	3.75	5.27	7.14	8.47
Petroleum commodity price at wellhead ($ per bbl)	63.84	49.33	59.10	115.95
Total petroleum and natural gas revenue	34,917	41,398	51,034	67,942
Total royalties	2,118	(8,644)	(8,888)	(12,502)
Total interest and other revenue	-	-	-	-
Total revenues, net	37,035	32,754	42,146	55,440
Total capital expenditures	5,485	18,395	58,916	89,158
Net income (loss)	(7,128)	(9,701)	(355)	16,649
Per share basic	($0.06)	($0.09)	-	$0.15
Per share diluted	($0.06)	($0.09)	-	$0.14
Cash generated by operations	20,026	14,354	24,627	37,886
Per share basic	$0.18	$0.13	$0.22	$0.34
Per share diluted	$0.18	$0.13	$0.22	$0.33
Book value of total assets	819,142	800,959	814,823	774,794
Non-revolving credit facility	-	-	-	-
Revolving credit facilities	219,361	228,867	211,586	180,995
Total debt	179,649	253,544	249,862	214,642
Shareholders' equity	535,917	496,276	507,371	506,742
Common shares outstanding – end of period				
Basic	122,807,637	112,542,635	112,395,970	112,395,970
Diluted	134,732,322	124,618,156	121,659,923	121,451,823
Weighted average common shares outstanding				
Basic	112,887,812	112,457,321	112,395,970	112,386,829
Diluted	113,817,095	112,457,321	112,801,866	116,859,500

Quarters Ended ($000's, except share and per share amounts)	June 30, 2008	March 31, 2008	December 31, 2007	September 30, 2007
Petroleum and natural gas production (boe per day)	9,583	9,470	9,260	6,014
Petroleum and natural gas commodity price ($ per boe)	83.58	64.83	54.18	40.10
Natural gas commodity price at wellhead ($ per mcf)	10.93	8.35	6.71	5.48
Petroleum commodity price at wellhead ($ per bbl)	121.39	94.72	80.94	76.95
Total petroleum and natural gas revenue	73,273	56,192	46,398	22,467
Total royalties	(11,361)	(8,700)	(7,804)	(4,007)
Total interest and other revenue	-	2	8	-
Total revenues, net	61,912	47,494	38,602	18,460
Total capital expenditures	37,487	51,518	30,306	288,321
Net income (loss)	9,776	3,828	(6,457)	(5,707)
Per share basic	$0.09	$0.04	($0.07)	($0.09)
Per share diluted	$0.08	$0.04	($0.07)	($0.09)
Cash generated by operations	41,676	27,264	19,881	9,327
Per share basic	$0.37	$0.28	$0.21	$0.14
Per share diluted	$0.36	$0.27	$0.21	$0.14
Book value of total assets	719,292	699,567	662,252	644,876
Non-revolving credit facility	-	-	98,830	97,431
Revolving credit facilities	148,922	133,035	155,854	153,360
Total debt	163,378	169,614	272,916	262,557
Shareholders' equity	488,579	475,453	340,756	342,451
Common shares outstanding – end of period				
Basic	112,375,970	111,863,089	94,554,269	94,472,583
Diluted	121,270,357	121,175,691	103,639,748	103,046,582
Weighted average common shares outstanding				
Basic	112,234,676	98,852,346	94,486,372	65,521,290
Diluted	117,074,630	102,589,422	96,548,884	66,152,795

Discussion of Quarterly Results

Birchcliff's average quarterly production in the second quarter of 2009 was 11,313 boe per day, which is a 10% decrease from 12,513 boe per day in the first quarter of 2009 and an 18% increase from 9,583 boe per day in the second quarter of 2008. The decrease from the first quarter of 2009 was mainly due to normal and flush production declines, plant turnarounds, and reduced capital spending. The year over year production increase is the direct result of the success of the Corporation's capital spending program in 2008 and into the Reporting Periods on its two resource plays.

Since the quarter ended June 30, 2008, when wellhead commodity prices peaked at an average of $10.93 per mcf and $121.39 per barrel of oil, commodity prices have decreased significantly. For the current quarter, natural gas prices averaged $3.75 per mcf at the wellhead, which is a 66% decrease and oil prices averaged $63.84 per barrel at the wellhead, which is a 47% decrease.

Cash flow generated by the Corporation in the second quarter of 2009 was $20.0 million, which is a 39% increase from $14.4 million in the first quarter of 2009 and a 52% decrease from $41.7 million in the second quarter of 2008. The increase in cash flow from the first quarter of 2009 was due to prior period royalty credits offset by lower average production volumes and lower natural gas prices realized by the Corporation in the second quarter of 2009. The decrease in cash flow from the second quarter of 2008 was mainly due to lower average commodity prices realized by the Corporation.

Birchcliff spent $5.5 million of capital during the three month Reporting Period as compared to $37.5 million during the three month Comparable Prior Period. The decrease in capital expenditures is a direct result of the Corporation's response to the drop in commodity prices in the latter part of 2008 and first half of 2009. Birchcliff continues to invest its cash flow on existing natural gas infrastructure and its Montney/Doig resource play.

The weighted average basic common shares outstanding have not changed significantly as a result of the Equity Financing occurring on the last day of the Reporting Period. The impact of the issuance of the shares on the weighted average common shares outstanding will be reflected in future periods.

OUTLOOK

Capital Expenditures

The Corporation has revised its 2009 capital expenditure program to $105 million from its previously announced capital budget of $80 million. Birchcliff spent just under $24 million of capital in the six month Reporting Period. The Corporation expects its second half 2009 capital expenditures to be approximately $81 million with approximately $40 million budgeted for the expansion of the Corporation's existing resource plays, related infrastructure and other projects, and approximately $41 million to construct the PCS Gas Plant.

Production

Birchcliff's average production rate for the second quarter of 2009 was 11,313 boe per day as compared to the previously announced guidance for the second quarter of 11,150 boe per day. The revised capital expenditure program is expected to result in a 2009 average production rate of approximately 11,300 boe per day. Birchcliff's 2009 exit production rate is expected to be 11,700 boe per day.

Working Capital

The Corporation did not have any liquidity issues with respect to the operation of its petroleum and natural gas business in the Reporting Periods, nor does it anticipate a liquidity issue in the foreseeable future. The Corporation has recently increased the aggregate limit on its Revolving Credit Facilities to $255 million and has established a new $50 million Term Facility which will provide the Corporation with greater financial flexibility in managing its business activities without liquidity concerns.

Interest Expense

Management expects that the effective interest rates applicable to the Corporation's credit facilities will be approximately 2% higher in the future than was experienced in the second quarter as a result of the increased margins (that are used to determine Birchcliff's effective interest rates) that became applicable upon the establishment of its increased credit facilities.

Resource Plays

Birchcliff has a very strong asset base with its two main resource plays, the Montney/Doig natural gas resource play and the Worsley light oil resource play. These properties provide the Corporation with a long term and operationally reliable cash flow base, the level of which is primarily dependent on commodity prices. The construction of the 100% owned PCS Gas Plant is expected to enhance the value of the Montney/Doig resource play by increasing production growth, reducing operating costs, and increasing strategic control over its core area. The extensive portfolio of development opportunities on these properties will not expire in the near term and provides low risk long life future production additions that are readily available with the investment of additional capital. The short term commodity prices will dictate the rate at which Birchcliff invests in its resource plays and the rate at which Birchcliff can grow its production, but short term commodity prices do not affect the quality or the long term value of the Corporation's asset base.

CONTRACTUAL COMMITMENTS

The Corporation is committed under a premises lease which commenced December 1, 2007 and which expires on November 30, 2017. Birchcliff does not presently use all of the leased premises and has sublet the excess space to an arms' length party on a basis that recovers approximately 40% of the rental costs for the first five years. The Corporation is committed to the following aggregate minimum lease payments (not reduced by sublease rents receivable by the Corporation):

Year	***$000's***
2009	1,607
2010	3,214
2011	3,214
2012	3,223
2013	3,331
Thereafter	13,045

DISCLOSURE CONTROLS AND PROCEDURES

Disclosure controls and procedures have been designed by The Chief Executive Officer ("**CEO**") and the Chief Financial Officer ("**CFO**") to provide reasonable assurance that (i) material information relating to Birchcliff is made known to them by others, particularly during the period in which interim filings are being prepared; and (ii) information required to be disclosed by Birchcliff in its annual filings, interim filings or other reports filed or submitted by it under securities legislation was recorded, processed, summarized and reported within the time periods specified in securities legislation. It should be noted that while the Corporation's CEO and CFO believe that the Corporation's disclosure controls and procedures are effective to provide a reasonable level of assurance, they do not expect that the disclosure controls and procedures will prevent all errors and fraud. A control system, no matter how well conceived or operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are achieved.

INTERNAL CONTROL OVER FINANCIAL REPORTING

Internal control over financial reporting is a process designed to provide reasonable assurance that all assets are safeguarded, transactions are appropriately authorized and to facilitate the preparation of relevant, reliable and timely financial reporting. Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. There has been no change in Birchcliff's internal controls over financial reporting during the three month Reporting Period that has materially affected, or is reasonably likely to materially affect, Birchcliff's internal controls over financial reporting.

CHANGE IN ACCOUNTING POLICIES

On January 1, 2009 the Corporation prospectively adopted the following Canadian Institute of Chartered Accountant ("**CICA**") Handbook Sections:

Section 3064 *Goodwill and Intangible Assets*, which defines the criteria for the recognition of intangible assets. The adoption of this section had no impact on the Corporation's financial statements.

EIC-173 *Credit Risk and the Fair Value of Financial Assets and Financial Liabilities*, which provides guidance on how to take into account credit risk of an entity and counterparty when determining the fair value of financial assets and financial liabilities, including derivative instruments. The application of this EIC did not have a material effect on the Corporation's Financial Statements.

INTERNATIONAL FINANCIAL REPORTING STANDARDS

In February 2008, Canada's Accounting Standards Board ("**AcSB**") confirmed that International Financial Reporting Standards ("**IFRS**") will be required for publicly accountable enterprises' interim and annual financial statements effective for fiscal years beginning on or after January 1, 2011. In order to transition to IFRS, Birchcliff retained an external advisor to assist in the initial scoping of the project, and has appointed internal personnel to lead the conversion. The transition plan consists of four main phases:

- Diagnostic phase which involves an assessment of the differences between Canadian GAAP and IFRS;
- Assessment and selection phase whereby the Corporation will determine its IFRS accounting policies;
- Evaluation of information systems, business processes, procedures and controls to support the new reporting standards; and
- Training and development.

To date, the Corporation has completed its IFRS diagnostic assessment and has commenced analysis and identification of accounting policy choices, including assessing impacts on information systems and business processes. A detailed Cost Generating Unit ("**CGU"**) analysis has been prepared and presented to Birchcliff's auditors for review and comment. Birchcliff expects to finalize its determination of CGU's in the third quarter of 2009 and will determine its accounting policies, in particular those pertaining to the Corporation's property, plant and equipment under IFRS. Birchcliff has also provided an introductory training session to a wide group of staff. The Corporation intends to generate financial information in accordance with IFRS throughout 2010 in order to provide comparative information for the 2011 financial statements. As such, Birchcliff will prepare a transition balance sheet as at December 31, 2009 (to be representative of the opening January 1, 2010 balance sheet) in accordance with IFRS. Based on the high-level scoping study, the following IFRS standards are expected to have the most significant impact on Birchcliff's financial reporting:

- IFRS 1 – First-time Adoption of IFRS
- IFRS 2 – Share Based Payments
- IFRS 6 – Exploration and Evaluation of Mineral Resources
- IAS 12 – Income Taxes
- IAS 16 – Property, Plant and Equipment
- ED 9 – Joint Arrangements (replacing IAS 31 – Interests in Joint Ventures)
- IAS 36 – Impairment of Assets
- IAS 37 – Provisions, Contingent Liabilities and Contingent Assets

The transition from Canadian GAAP to IFRS is a significant undertaking that may materially affect the Corporation's reported financial position and results of operations. As Birchcliff has not yet determined its accounting policies, it is not possible to quantify the impact of adopting IFRS on its financial statements at this time. In addition, due to anticipated changes to IFRS and International Accounting Standards prior to adoption of IFRS, the Corporation's plan is subject to change based on new facts and circumstances that arise after the date of this MD&A.

FORWARD LOOKING STATEMENTS

This MD&A contains certain forward-looking statements and forward-looking information (hereinafter collectively referred to as "forward-looking statements") within the meaning of applicable Canadian securities laws. These statements relate to future events or our future performance and are based upon the Corporation's current internal expectations, estimates, projections, assumptions and beliefs. All statements other than statements of historical fact are forward-looking statements. In some cases, words such as "plan", "expect", "project", "intend", "believe", "anticipate", "estimate", "may", "will", "would", "potential", "proposed" and other similar words, or statements that certain events or conditions "may" or "will" occur, are intended to identify forward-looking statements.

Undue reliance should not be placed on these forward-looking statements, as there can be no assurance that the plans, intentions or expectations upon which they are based will occur. By their nature, forward-looking statements involve numerous assumptions and known and unknown risks and uncertainties that the predictions, forecasts, projections and other forward-looking statements will not occur. Although the Corporation believes that the expectations reflected in the forward-looking statements are reasonable, there can be no assurance that such expectations will prove to be correct. The Corporation cannot guarantee future results, levels of activity, performance or achievements. Consequently, there is no representation by the Corporation that actual results achieved will be the same in whole or in part as those set out in the forward-looking statements. Such forward-looking statements in this MD&A speak only as of the date of this.

In particular, this MD&A contains forward-looking statements pertaining to the following: drilling inventory, drilling plans and timing of drilling, re-completion and tie-in of wells; plans for facilities construction and completion of the timing and method of funding thereof; productive capacity of wells, anticipated or expected production rates and anticipated dates of commencement of production; drilling, completion and facilities costs; results of projects of the Corporation; ability to lower costs borne by the Corporation; production growth expectations; timing of development of undeveloped reserves; the tax horizon of the Corporation; the future performance and characteristics of the Corporation's oil and natural gas properties; oil and natural gas production levels; the quantity of oil and natural gas reserves; planned capital expenditure programs; supply and demand for oil and natural gas; commodity prices; the impact of Canadian federal and provincial governmental regulation on the Corporation; weighting of production between different commodities; expected levels of royalty rates and incentives, operating costs, general administrative costs, costs of services and other costs and expenses; expectations regarding the Corporation's ability to raise capital and to add to reserves through acquisitions, exploration and development; and treatment under tax laws. With respect to such forward-looking statements the key assumptions on which the Corporation relies are; that future prices for crude oil and natural gas, future currency exchange rates and interest rates and future availability of debt and equity financing will be at levels and costs that allow the Corporation to manage, operate and finance its business and develop its properties and meet its future obligations; that the regulatory framework in respect of royalties, taxes and environmental matters applicable to the Corporation will not become so onerous as to preclude the Corporation from viably managing, operating and financing its business and the development of its properties; and that the Corporation will continue to be able to identify, attract and employ qualified staff and obtain the outside expertise and specialized and other equipment it requires to manage, operate and finance its business and develop its properties.

All such forward-looking statements necessarily involve risks associated with oil and gas exploration, production and marketing which may cause actual results may differ materially from those anticipated in the forward-looking statements. Some of those risks include; general economic conditions in Canada, the United States and globally; industry conditions, including fluctuations in the price of oil and natural gas; changes in governmental regulation of the oil and gas industry, including environmental regulation; fluctuations in foreign exchange rates or interest rates; geological, technical, drilling and processing problems and other difficulties in producing reserves; unanticipated operating events which can damage *facilities or reduce production or cause production to be shut in or delayed; failure to obtain regulatory approvals in a timely manner; adverse conditions in the debt and equity markets; competition from others for scarce resources; and other factors disclosed under "Risk Factors" in this MD&A.*

Readers are cautioned that the foregoing list of factors is not exhaustive. The forward-looking statements contained in this MD&A are expressly qualified by this cautionary statement. The Corporation is not under any duty to update any of the forward-looking statements after the date of this MD&A to conform such statements to actual results or to changes in the Corporation's plans or expectations, except as otherwise required by applicable securities laws.

BIRCHCLIFF ENERGY LTD.
Balance Sheets
(Unaudited) ***($000's)***

	June 30, 2009	December 31, 2008
ASSETS		
CURRENT		
Cash	**37,179**	65
Accounts receivable	**16,731**	29,836
Prepaid and other	**5,642**	3,031
	59,552	32,932
Deferred financing fees (Note 5)	**558**	-
Petroleum and natural gas properties and equipment (Note 3)	**759,032**	781,891
	819,142	814,823
LIABILITIES		
CURRENT		
Accounts payable and accrued liabilities	**19,840**	71,208
	19,840	71,208
Revolving credit facilities (Note 6)	**219,361**	211,586
Asset retirement obligations (Note 9)	**21,790**	21,223
Future income tax liability	**3,168**	3,435
Commitments (Note 12)		
SHAREHOLDERS' EQUITY		
Share capital (Note 10)	**535,917**	477,482
Contributed surplus (Note 11)	**18,990**	12,984
Retained earnings	**76**	16,905
	554,983	507,371
	819,142	814,823

See accompanying notes to the financial statements.

APPROVED BY THE BOARD

(signed) *"Larry A. Shaw"*
Larry A. Shaw, Director

(signed) *"A. Jeffery Tonken"*
A. Jeffery Tonken, Director

BIRCHCLIFF ENERGY LTD.
Statements of Net Income (Loss), Comprehensive Income (Loss) and Retained Earnings
(Unaudited) ***($000's)***

	Three months ended June 30		Six months ended June 30	
	2009	2008	**2009**	2008
REVENUE				
Petroleum and natural gas	**34,917**	73,273	**76,315**	129,465
Royalties	**2,118**	(11,361)	**(6,526)**	(20,061)
Interest and other	**-**	-	**-**	2
	37,035	61,912	**69,789**	109,406
Loss on risk management contracts (Note 8)				
Realized	**-**	4,107	**-**	7,346
Unrealized	**-**	5,567	**-**	4,615
	37,035	52,238	**69,789**	97,445
EXPENSES				
Production	**9,206**	9,409	**20,491**	18,300
Transportation and marketing	**2,381**	2,343	**5,129**	4,813
General and administrative, net	**2,936**	2,098	**5,027**	3,580
Stock-based compensation (Note 11)	**4,946**	1,350	**6,693**	2,600
Depletion, depreciation and accretion (Notes 3 and 9)	**22,667**	21,748	**47,579**	43,364
Realized foreign exchange loss (Note 8)	**-**	114	**-**	148
Unrealized foreign exchange gain (Note 8)	**-**	(98)	**-**	(302)
Interest and amortization of deferred financing fees (Notes 4, 5 and 6)	**2,698**	2,165	**4,974**	6,266
	44,834	39,129	**89,893**	78,769
INCOME (LOSS) BEFORE TAXES	**(7,799)**	13,109	**(20,104)**	18,676
TAXES				
Other taxes (recovery)	**-**	-	**-**	(7)
Future income taxes (recovery)	**(671)**	3,333	**(3,275)**	5,079
	(671)	3,333	**(3,275)**	5,072
NET INCOME (LOSS) AND COMPREHENSIVE INCOME (LOSS)	**(7,128)**	9,776	**(16,829)**	13,604
RETAINED EARNINGS (DEFICIT), BEGINNING OF PERIOD	**7,204**	(9,165)	**16,905**	(12,993)
RETAINED EARNINGS, END OF PERIOD	**76**	611	**76**	611
Net income (loss) per common share				
basic	**$(0.06)**	$0.09	**$(0.15)**	$0.13
diluted	**$(0.06)**	$0.08	**$(0.15)**	$0.12
Weighted average common shares				
basic	**112,887,812**	112,234,676	**112,673,756**	105,543,511
diluted	**112,887,812**	117,074,630	**112,673,756**	110,062,054

See accompanying notes to the financial statements

BIRCHCLIFF ENERGY LTD.
Statements of Cash Flows
(Unaudited) ***($000's)***

	Three months ended June 30		Six months ended June 30	
	2009	2008	**2009**	2008
OPERATING				
Net income (loss)	**(7,128)**	9,776	**(16,829)**	13,604
Adjustments for items not affecting cash:				
Depletion, depreciation and accretion (Notes 3 and 9)	**22,667**	21,748	**47,579**	43,364
Stock-based compensation (Note 11)	**4,946**	1,350	**6,693**	2,580
Unrealized risk management contracts loss (Note 8)	-	5,567	**-**	4,615
Unrealized foreign exchange gain (Note 8)	**-**	(98)	**-**	(302)
Amortization of deferred financing fees (Notes 5 and 6)	**212**	-	**212**	-
Future income taxes (recovery)	**(671)**	3,333	**(3,275)**	5,079
	20,026	41,676	**34,380**	68,940
Changes in non-cash working capital (Note 13)	**(11,518)**	(592)	**(5,768)**	(8,412)
Asset retirement expenditures incurred (Note 9)	**(22)**	48	**(273)**	(66)
	8,486	41,132	**28,339**	60,462
FINANCING				
Decrease in non-revolving credit facility (Note 4)	**-**	-	**-**	(98,830)
Deferred financing fees paid (Notes 5 and 6)	**(1,975)**	-	**(1,975)**	-
Increase (decrease) in revolving credit facilities (Note 6)	**(8,302)**	15,887	**8,980**	(6,932)
Issuance of share capital (Note 10)	**62,842**	2,001	**63,450**	136,582
Share issue costs (Note 10)	**(2,695)**	-	**(2,695)**	(6,912)
	49,870	17,888	**67,760**	23,908
INVESTING				
Purchase of petroleum and natural gas properties and equipment	**-**	(9,672)	**(30)**	(9,855)
Development of petroleum and natural gas properties and equipment	**(5,485)**	(27,815)	**(23,850)**	(79,150)
Changes in non-cash investing working capital (Note 13)	**(15,757)**	(21,533)	**(35,105)**	4,634
	(21,242)	(59,020)	**(58,985)**	(84,371)
NET INCREASE (DECREASE) IN CASH	**37,114**	-	**37,114**	(1)
CASH, BEGINNING OF PERIOD	**65**	65	**65**	66
CASH, END OF PERIOD	**37,179**	65	**37,179**	65
Cash interest paid	**2,486**	2,165	**4,762**	6,266
Cash taxes paid	**-**	-	**-**	254

See accompanying notes to the financial statements

1. BASIS OF PRESENTATION

Birchcliff Energy Ltd. ("**Birchcliff**" or the "**Corporation**") is engaged in the exploration for and the development, production and acquisition of, petroleum and natural gas reserves in Western Canada. Birchcliff's financial year end is December 31.

The interim financial statements of Birchcliff Energy Ltd. have been prepared by management in accordance with accounting principles generally accepted in Canada and are unaudited. The interim financial statements have been prepared following the same accounting policies and methods of computation as the audited financial statements for the period ended December 31, 2008 except as discussed in Note 2. The disclosures which follow do not include all disclosures required for the annual financial statements. These unaudited interim financial statements should be read in conjunction with the audited financial statements and notes thereto for the year ended December 31, 2008.

2. CHANGES IN ACCOUNTING POLICIES

On January 1, 2009 the Corporation adopted the following Canadian Institute of Chartered Accountant ("**CICA**") Handbook Sections:

- Section 3064, *Goodwill and intangible assets,* replacing Section 3062*, Goodwill and other intangible assets* and Section 3450*, Research and development costs*. Various changes have been made to other sections of the CICA Handbook for consistency purposes. This Section establishes standards for the recognition, measurement, presentation and disclosure of goodwill subsequent to its initial recognition and of intangible assets by profit-oriented enterprises. Standards concerning goodwill are unchanged from the standards included in the previous Section 3062. The new Section is applicable to financial statements relating to fiscal years beginning on or after October 1, 2008. Accordingly, the Corporation adopted these new standards for its fiscal year beginning January 1, 2009. The adoption of this Section did not have an impact on the Corporation's Financial Statements.
- EIC-173, *Credit Risk and the Fair Value of Financial Assets and Financial Liabilities*. In January 2009, the CICA issued EIC-173 which provides guidance on how to take into account credit risk of an entity and counterparty when determining the fair value of financial assets and financial liabilities, including derivative instruments. This EIC is effective for the Corporation's fiscal periods ending on or after January 20, 2009 with retrospect application. The application of this EIC did not have a material effect on the Corporation's Financial Statements.

Recent Accounting Pronouncements

In February 2008, the CICA Accounting Standards Board ("**ACSB**") confirmed the changeover to International Financial Reporting Standards ("**IFRS**") from GAAP will be required for publicly accountable enterprises' interim and annual financial statements effective for fiscal years beginning on or after January 1, 2011. The Corporation has completed a high level IFRS impact study and established a preliminary timeline for the execution and completion of its conversion project. At this time, Birchcliff is evaluating the impact of these differences and assessing the need for amendments to existing accounting policies in order to comply with IFRS. Birchcliff expects to be IFRS compliant by January 1, 2011.

Future Accounting Policy Changes

In December 2008, the CICA issued Section 1582, *Business Combinations*, which will replace CICA Section 1581 of the same name. Section 1582 establishes principles and requirements of the acquisition method for business combinations and related disclosures. This 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 2011 with earlier application permitted. The Corporation is currently evaluating the impact of this changeover on its financial statements.

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

3. PETROLEUM AND NATURAL GAS PROPERTIES AND EQUIPMENT

($000's)			**June 30, 2009**
	Cost	**Accumulated Depletion and Depreciation**	**Net Book Value**
Petroleum and natural gas assets	1,019,625	(262,189)	757,436
Office furniture and equipment	3,127	(1,531)	1,596
	1,022,752	**(263,720)**	**759,032**

($000's)			December 31, 2008
	Cost	**Accumulated Depletion and Depreciation**	**Net Book Value**
Petroleum and natural gas assets	996,028	(215,719)	780,309
Office furniture and equipment	2,780	(1,198)	1,582
	998,808	**(216,917)**	**781,891**

As at June 30, 2009, the cost of petroleum and natural gas properties includes $41.5 million (December 31, 2008 – $49.7 million) relating to unproved properties which have been excluded from costs subject to depletion and depreciation.

Birchcliff capitalized general and administrative costs directly related to exploration and development activities of $382,143 and $792,509 in the three and six months ended June 30, 2009 (three and six months ended June 30, 2008 - $333,000 and $748,000).

4. NON-REVOLVING ACQUISITION FACILITY

Birchcliff entered into an Acquisition Credit Agreement (the "**Acquisition Facility**") with a syndicate of banks on September 4, 2007. The agreement allowed for Birchcliff to make a one-time draw of up to $100 million on a non-revolving credit facility for the purpose of closing the Worsley Acquisition. On September 27, 2007 the Corporation gave notice to draw the entire amount of the credit facility in bankers' acceptances. The drawn amount at December 31, 2007 was $98.8 million with the $1.2 million difference being the discounted value from the $100 million credit facility limit based on the market interest rate at that time for bankers' acceptances. On March 14, 2008 the facility was repaid in full and cancelled, following the completion of the equity financing described in Note 10(d).

5. NON-REVOLVING TERM FACILITY

On May 21, 2009, the Corporation entered into a $50 million non-revolving one year term credit facility (the "**Term Facility**"). The Term Facility is provided by a syndicate of four banks (the "**Syndicate**"). No amounts have been drawn on the Term Facility as at June 30, 2009. The Corporation paid $625,000 in financing fees to the Syndicate to establish the Term Facility. These fees have been deferred as a non current asset and are being amortized to income equally over the one year term beginning on May 21, 2009. During the three and six months ended June 30, 2009, the Corporation amortized to income $67,204 in deferred financing fees applicable to the Term Facility. As at June 30, 2009, the unamortized portion of the deferred financing fees applicable to the Term Facility was $557,796.

The Corporation's use of the Term Facility is subject to consent of the Syndicate at the time of the draw-down. The Corporation has not requested a draw-down of the Term Facility during the three and six months ended June 30, 2009. The Term Facility allows for prime rate loans, US base rate loans, bankers' acceptances, letters of credit and LIBOR loans. The interest rates applicable to the Term Facility are based on a pricing grid and will increase as a result of the increased ratio of outstanding indebtedness to earnings before interest, taxes, depreciation and amortization. The Term Facility is secured by a fixed and floating charge debenture, an instrument of pledge, and a general security agreement encompassing all of the Corporation's assets for a consideration equal to the draw-down amount.

6. REVOLVING CREDIT FACILITIES

($000's)	**June 30, 2009**	December 31, 2008
Syndicated credit facility	211,621	197,410
Working capital facility	8,945	14,176
Unamortized deferred financing fees	(1,205)	-
Revolving Credit Facilities	**219,361**	**211,586**

On May 21, 2009, Birchcliff amended its agreement with its bank syndicate which increased the Corporation's existing Revolving Credit Facilities from $240 million to an aggregate limit of $255 million. The Revolving Credit Facilities consist of an extendible revolving term credit facility with an authorized limit of $235 million (the "**Syndicated Credit Facility**") and an extendible revolving working capital facility with an authorized limit of $20 million (the "**Working Capital Facility**"). The $235 million Syndicated Credit Facility is provided by a syndicate of four banks (the "**Syndicate**"). The $20 million Working Capital Facility is provided by the lead bank in the current Syndicate. As at June 30, 2009, Birchcliff had $219.4 million outstanding on its Revolving Credit Facilities. The balance in the Revolving Credit Facilities at June 30, 2009 does not reflect approximately $37 million of proceeds from the equity financing (Note 10 (f)) held as cash because the proceeds could not be immediately applied to reduce outstanding balance in the Syndicated Credit Facility represented by unmatured bankers' acceptances at June 30, 2009.

As at June 30, 2009, the effective rate applicable to the Working Capital Facility was 4.8% (December 31, 2008 – 4.7%). The overall effective interest rate applicable to the bankers' acceptances in the Syndicated Credit Facilities were 2.0% and 2.5% for the three and six months ended June 30, 2009 (three and six months ended June 30, 2008 – 4.1% and 4.4%). Also included as a reduction of the available Working Capital Facility are letters of credit issued to various service providers in the amount of $1.6 million at June 30, 2009 (December 31, 2008 – $1.8 million).

The Corporation paid $1.35 million in financing fees to the Syndicate to extend the conversion date of the Revolving Credit Facilities to May 21, 2010. These fees have been deferred and netted against the Revolving Credit Facilities and are being amortized to income over the one year extension period. During the three and six months ended June 30, 2009, the Corporation amortized to income $145,161 in deferred financing fees applicable to the Revolving Credit Facilities. As at June 30, 2009, the unamortized portion of the deferred financing fees included in the Revolving Credit Facilities was approximately $1.2 million.

The Revolving Credit Facilities allow for prime rate loans, US base rate loans, bankers' acceptances, letters of credit and LIBOR loans. The interest rates applicable to the drawn loans are based on a pricing grid and will increase as a result of the increased ratio of outstanding indebtedness to earnings before interest, taxes, depreciation and amortization.

The Revolving Credit Facilities are subject to the Syndicate's redetermination of the borrowing base twice each year as of November 15 and the conversion date. Upon any change in or redetermination of the borrowing base limit which results in a borrowing base shortfall, Birchcliff must eliminate the borrowing base shortfall amount. The Revolving Credit Facilities are secured by a fixed and floating charge debenture, an instrument of pledge, and a general security agreement encompassing all of the Corporation's assets.

Syndicated Credit Facility

The Syndicated Credit Facility has a conversion date of May 21, 2010 and a maturity date which is two years after the conversion date. Birchcliff may request an extension of the conversion date with such an extension not exceeding 364 days, in order to maintain the revolving Syndicated Credit Facility. If the Syndicate does not grant an extension of the conversion date, then upon the expiry of the conversion date, the revolving Syndicated Credit Facility will convert to a term loan whereby all principal and interest will be required to be repaid at the maturity date.

Working Capital Facility

The Working Capital Facility has a conversion date of May 21, 2010 and a maturity date which is two years after the conversion date. Birchcliff may request an extension of the conversion date with such an extension not exceeding 364 days, in order to maintain the revolving Working Capital Facility. If the Syndicate does not grant an extension of the conversion date, then upon four months after the expiry of the conversion date, the revolving Working Capital Facility will convert to a term loan whereby all principal and interest will be required to be repaid at the maturity date.

7. CAPITAL MANAGEMENT

The Corporation's general policy is to maintain a sufficient capital base in order to manage its business in the most effective manner with the goal of increasing the value of its assets and thus its underlying share value. The Corporation's objectives when managing capital are to maintain financial flexibility in order to preserve its ability to meet financial obligations, including potential obligations arising from additional acquisitions; to maintain a capital structure that allows Birchcliff to favour the financing of its growth strategy using internally-generated cash flow and its debt capacity; and to optimize the use of its capital to provide an appropriate investment return to its shareholders.

Birchcliff strives to properly exploit its current asset base and to acquire top quality assets. To that end, the Corporation is not averse to maintaining a high ratio of debt to total capital if management determines the assets it is acquiring or the projects it is drilling are of high quality.

The capital structure of the Corporation is as follows:

($000's)	**June 30, 2009**	December 31, 2008	Change %
Total shareholders' equity[1]	554,983	507,371	9%
Total shareholders' equity as a % of total capital	76%	67%	
Working capital (deficit)[2]	39,712	(38,276)	
Revolving credit facilities	219,361	211,586	
Total debt	179,649	249,862	(28%)
Total debt as a % of total capital	24%	33%	
Total Capital	**734,632**	**757,233**	**(3%)**

(1) Shareholders' equity is defined as share capital plus contributed surplus plus retained earnings, less any deficit.
(2) Working capital is defined as current assets less current liabilities.

During the six months ended June 30, 2009, total equity increased mainly due to the issuance of common shares (Note 10(f)); exercise of options (Note 10); and recording of stock-based compensation expense (Note 11) during the period.

Total debt decreased during the six month period ended June 30, 2009 by $70.2 million. Of the net proceeds from the equity issuance described in Note 10(f)), approximately $22.3 million was used to pay down the Corporation's Revolving Credit Facilities with the remaining balance held as cash. Also during the period, $10.5 million of cash flow in excess of capital spending was used to reduce total debt.

8. FINANCIAL INSTRUMENTS & RISK MANAGEMENT CONTRACTS

Birchcliff is exposed to credit risk, liquidity risk and market risk as part of its normal course of business. This Note presents information about the Corporation's exposure to each of these risks, as well as Birchcliff's objectives, policies and processes for measuring and managing risk. Further quantitative disclosures are included throughout these financial statements.

The Board of Directors has overall responsibility for the establishment and oversight of the Corporation's financial risk management framework and periodically reviews the results of all risk management activities and all outstanding positions. Management identifies and analyzes the risks faced by the Corporation and may utilize financial instruments to mitigate these risks.

Credit Risk

A substantial portion of the Corporation's accounts receivable are with customers in the oil and natural gas industry and are subject to normal industry credit risks. The carrying amount of accounts receivable reflects management's assessment of the credit risk associated with these customers. Of the Corporation's significant individual accounts receivable at June 30, 2009, approximately 46% was due from two marketers (December 31, 2008 - 21%, one marketer). Of the Corporation's revenues during the three and six months ended June 30, 2009, approximately 66% was received from two marketers and 72% was received from three marketers. During the three and six months ended June 30, 2008, approximately 73% was received from four marketers and 70% was received from three marketers. Typically, Birchcliff's maximum credit exposure to customers is revenue from two months of commodity sales.

The following table illustrates the Corporation's receivables:

($000's)	**June 30, 2009**	December 31, 2008
Marketers	10,622	15,265
Joint venture partners	5,269	14,500
Other	840	71
Total Receivables	**16,731**	**29,836**

Receivables from marketers are normally collected on the 25th day of the month following production. Birchcliff's policy to mitigate credit risk associated with these balances is to establish marketing relationships with credit worthy purchasers, to obtain guarantees from their ultimate parent companies and to obtain letters of credit as appropriate. The Corporation historically has not experienced any material collection issues with its marketers.

Cash consists of bank balances and short term deposits maturing in less than 90 days. Historically, the Corporation has not carried short term investments. Should this change in the future, counterparties will be selected based on credit ratings and management will monitor all investments to ensure a stable return, and complex investment vehicles with higher risk will be avoided.

The carrying amounts of accounts receivable and cash represent the maximum credit exposure. As at June 30, 2009, the Corporation has a $NIL allowance for doubtful accounts (December 31, 2008 – $99,000).

The Corporation's accounts receivables are aged as follows:

($000's)	**June 30, 2009**	December 31, 2008
Current (less than 30 days)	13,807	20,175
30 to 60 days	622	3,723
61 to 90 days	1,841	4,771
Over 90 days	461	1,167
Total Receivables	**16,731**	**29,836**

Liquidity Risk

Liquidity risk is the risk that the Corporation will not be able to meet its financial obligations as they become due. Birchcliff's approach to managing liquidity is to ensure, as much as possible, that it will have sufficient liquidity to meet its short term and long term financial liabilities when due, under both normal and unusual conditions without incurring unacceptable losses or risking harm to the Corporation's reputation.

The following table lists the contractual maturities of the Corporation's financial liabilities as at June 30, 2009:

($000's)	**< 1 Year**	**1 – 2 Years**	**2 – 5 Years**	**Thereafter**
Accounts payable and accrued liabilities	19,840	-	-	-
Revolving credit facilities (1)	-	-	219,361	-
Total Financial Liabilities	**19,840**	**-**	**219,361**	**-**

(1) The Revolving Credit Facilities bear interest at a floating rate and include a $9.0 million Working Capital Facility and $211.6 million Syndicated Credit Facility, net of $1.2 million in unamortized deferred financing fees.

Birchcliff prepares annual capital expenditure budgets, which are regularly monitored and updated as considered necessary. Petroleum and natural gas production is monitored weekly and is used to provide monthly current cash flow estimates. To facilitate the capital expenditure program, the Corporation has a revolving reserves-based credit facility, as outlined in Note 6, which is reviewed at least annually by the lender. Birchcliff also attempts to match its payment cycle with collection of petroleum and natural gas revenues.

Market Risk

Market risk is the risk that changes in market conditions, such as commodity prices, exchange rates and interest rates, will affect the Corporation's net earnings or the value of its financial instruments. The objective of market risk management is to manage and control exposures within acceptable limits, while maximizing returns. These risks are consistent with prior years.

Commodity Price Risk

Commodity price risk is the risk that the fair value of future cash flows will fluctuate as a result of changes in commodity prices. Significant changes in commodity prices can materially impact the Corporation's borrowing base under its credit facility. Lower commodity prices can also reduce the Corporation's ability to raise capital. Commodity prices for crude oil are impacted by world economic events that dictate the levels of supply and demand. From time to time the Corporation may attempt to mitigate commodity price risk through the use of financial derivatives.

Birchcliff had no risk management contracts in place as at or during the three and six months ended June 30, 2009.

For the three and six months ended June 30, 2009, the realized and unrealized loss ("total loss") related to the oil price risk management contracts, recognized in net income, was $NIL and $NIL (three and six months ended June 30, 2008 - $9.7 million and $12.0 million loss). Included in the total loss for three and six months ended June 30, 2008 was a net cash outlay of $4.1 million and $7.3 million relating to the actual monthly settlements incurred during the period. An unrealized loss of approximately $5.6 million and $4.6 million for the three and six months ended June 30, 2008 was also included within the total loss, identified as "unrealized risk management contracts loss" on the statements of cash flows.

The fair value of the Corporation's risk management liabilities at June 30, 2009 was $NIL (June 30, 2008 - $11.1 million). As of June 30, 2009 if WTI crude oil prices had been $1.00 USD higher or lower, with all other variables held constant, the change in the fair value of the risk management contracts would have resulted in net income (loss) and other comprehensive income (loss) that was $NIL and $NIL (June 30, 2008 - $89,000 and $266,000) higher or lower for the three and six month periods.

Foreign Currency Risk

Foreign currency risk is the risk that the fair value of future cash flows will fluctuate as a result of changes in foreign currency exchange rates. During the three and six months ended June 30, 2009, the Corporation was not exposed to any foreign currency fluctuations with respect to its WTI oil option contracts. As at June 30, 2008 if the US dollar had depreciated 10% against the Canadian dollar with all other variables held constant, Birchcliff's net income and other comprehensive income for the three and six months ended June 30, 2008 would have been $547,000 and $1.1 million higher.

The Corporation had no forward exchange rate contracts in place as at or during the three and six months ended June 30, 2008 and 2009.

Interest Rate Risk

Interest rate risk is the risk that future cash flows will fluctuate as a result of changes in market interest rates. The Corporation is exposed to interest rate cash flow risk on floating interest rate bank debt due to fluctuations in market interest rates. The remainder of Birchcliff's financial assets and liabilities are not exposed to interest rate risk.

As at June 30, 2009, if the interest rate had changed 1% with all other variables held constant, Birchcliff's net income (loss) and other comprehensive income (loss) for the three and six months ended June 30, 2009 would have changed by $572,000 and $1,119,000 (three and six months ended June 30, 2008 - $365,000 and $944,000). A sensitivity of 1% is considered reasonable given the current level of the bank prime rate and market expectations for future movements. The Corporation considers this risk to be limited and thus does not hedge its interest rate risk.

The Corporation had no interest rate swaps or financial contracts in place as at or during the three and six months ended June 30, 2008 and 2009.

Fair Value of Financial Instruments

Birchcliff's financial instruments are classified as cash, accounts receivable, accounts payable and accrued liabilities and Revolving Credit Facilities on the balance sheet.

The carrying value and fair value of these financial instruments at June 30, 2009 is disclosed below by financial instrument category, as well as any related loss and interest expense for the period:

($000's)	**Carrying Value(1)**	**Fair Value(1)**	**Loss**	**Interest Expense(2)**
Assets Held for Trading				
Cash	37,179	37,179	-	-
Loans and Receivables				
Accounts receivable	16,731	16,731	-	-
Other Liabilities				
Accounts payable and accrued liabilities	19,840	19,840	-	-
Revolving credit facilities	219,361	219,361	-	4,974

(1) Due to the short term nature of cash accounts receivable, accounts payable and accrued liabilities, their carrying values approximate their fair values. The revolving credit facilities bear interest at a floating rate and accordingly the fair market value approximates the carrying value before the carrying value is reduced for the remaining deferred financing costs.
(2) Included in interest expense on the statements of net income (loss), comprehensive income (loss) and retained earnings are deferred financing fees of $212,365 for the six months ended June 30, 2009.

9. ASSET RETIREMENT OBLIGATIONS

The Corporation's asset retirement obligations result from net ownership interests in petroleum and natural gas properties including well sites, gathering systems and processing facilities. Birchcliff estimates the total undiscounted amount of cash flows required to settle its asset retirement obligation as at June 30, 2009 to be approximately $68.5 million (December 31, 2008 – $68.1 million) which will be incurred between 2009 and 2057. A credit-adjusted risk-free interest rate of 8% and an inflation rate of 2% were used to calculate the fair value of the asset retirement obligation.

A reconciliation of the asset retirement obligations is provided below:

($000's)	**June 30, 2009**	December 31, 2008
Balance, January 1	21,223	18,806
Obligations incurred	64	1,778
Obligations acquired	-	89
Changes in estimate	-	166
Accretion expense	776	1,466
Actual expenditures incurred	(273)	(1,082)
Ending Balance	**21,790**	**21,223**

10. SHARE CAPITAL

(a) Authorized:

Unlimited number of voting common shares
Unlimited number of non-voting preferred shares

The preferred shares may be issued in one or more series and the directors are authorized to fix the number of shares in each series and to determine the designation, rights, privileges, restrictions and conditions attached to the shares of each series.

(b) Issued:

	Number of Common Shares	Amount $
Balance, December 31, 2007	**94,554,269**	**342,818,621**
Issued upon exercise of stock options	1,133,925	6,009,537
Issued upon exercise of warrants (Note (c))	809,933	3,596,103
Issued, net of costs (Note (d))	15,897,843	123,088,169
Tax effect of share issue costs (Note (e))	-	1,970,000
Balance, December 31, 2008	**112,395,970**	**477,482,430**
Issued upon exercise of stock options	146,665	887,404
Tax effect of flow through shares (Note (d))	-	(3,750,000)
Balance, March 31, 2009	**112,542,635**	**474,619,834**
Issued upon exercise of stock options	265,002	1,249,887
Issued, net of costs (Note (f))	10,000,000	59,304,600
Tax effect of share issue costs (Note (g))	-	743,000
Balance, June 30, 2009	**122,807,637**	**535,917,321**

(c) In January 2008, 809,933 common shares were issued to a former officer in exchange for 809,933 performance warrants with an exercise price of $3.00 for gross proceeds to the Corporation of $2,429,799. In addition, $1,166,304 of non-cash costs attributable to these warrants, which was previously recorded to contributed surplus, was reclassified from contributed surplus to share capital.

(d) On March 14, 2008, Birchcliff issued 1,522,843 flow-through shares at a price of $9.85 per share and 14,375,000 common shares at a price of $8.00 per share for total net proceeds of $123,088,169. As at December 31, 2008, the commitment to spend and renounce $15 million of qualified 100% deductible tax pools with respect to the flow-through shares was fulfilled.

(e) Birchcliff recognized a future income tax benefit of $1,970,000 in respect of share issue costs of $6,911,832 incurred with respect to the issuance of 15,897,843 shares on March 14, 2008.

(f) On June 30, 2009, Birchcliff issued 10,000,000 common shares at a price of $6.20 per share for total net proceeds of $59,304,600.

(g) Birchcliff recognized a future income tax benefit of $743,000 in respect of share issue costs of $2,695,400 incurred with respect to the issuance of 10,000,000 common shares on June 30, 2009.

11. STOCK-BASED COMPENSATION

The Corporation has established a stock-based compensation plan whereby officers, employees, directors and consultants may be granted options to purchase common shares at a fixed price not less than the fair market value of the stock at the time of grant, subject to certain conditions being met. Stock options granted under this plan vest over a three year period at the rate of one-third on each anniversary date of the stock option grant. All stock options granted are for a five year term.

In order to calculate the compensation expense, the fair value of the stock options or performance warrants is estimated using the Black-Scholes option-pricing model that takes into account, as of the grant date: exercise price, expected life, current price, expected volatility, expected dividends, and risk-free interest rates.

Stock Options

For the three and six months ended June 30, 2009, the Corporation recorded $1.9 million and $3.6 million (three and six months ended June 30, 2008 - $1.4 million and $2.6 million) of non-cash stock-based compensation expense and a corresponding increase to contributed surplus related to the issuance of stock options. During the three and six months ended June 30, 2009, the Corporation also recorded a cash stock-based compensation expense of $NIL and $NIL (three and six months ended June 30, 2008 - $NIL and $20,000) related to cash paid to cancel vested stock options during the period.

Using the fair value method, the weighted average fair value of stock options granted during the three and six months ended June 30, 2009 was $3.59 and $2.78 (three and six months ended June 30, 2008 - $8.29 and $4.83) per option, respectively.

At June 30, 2009, the Corporation's Amended and Restated Stock Option Plan permitted the grant of options in respect of 12,280,764 common shares (June 30, 2008 – 11,237,597). At June 30, 2009, there remained available for issuance options in respect of 3,295,811 common shares (June 30, 2008 – 5,282,942).

A summary of the Corporation's outstanding stock options during the six months ended June 30, 2009 is presented below:

	Number	Weighted Average Exercise Price ($)
Outstanding, December 31, 2008	**6,324,221**	**5.58**
Granted	3,236,900	5.02
Exercised	(146,665)	(4.15)
Forfeited	(278,667)	(6.02)
Outstanding, March 31, 2009	**9,135,789**	**5.40**
Granted	208,000	6.46
Exercised	(265,002)	(3.18)
Forfeited	(93,834)	(4.52)
Outstanding, June 30, 2009	**8,984,953**	**5.50**

The fair value of each option was determined on the date of the grant using the Black-Scholes option-pricing model. The weighted average assumptions used in calculating the fair values are set forth below:

	June 30, 2009	December 31, 2008
Risk-free interest rate	1.9%	3.1%
Expected maturity (years)	5.0	5.0
Expected volatility	63.4%	52.0%
Dividend yield	0%	0%

A summary of the stock options outstanding and exercisable under the plan at June 30, 2009 is presented below:

Exercise Price		**Awards Outstanding**			**Awards Exercisable**		
Low	High	Quantity	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Quantity	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price
$3.00	$6.00	6,456,686	3.30	$4.49	2,267,827	1.63	$3.71
$6.01	$9.00	2,082,367	3.62	$7.16	668,399	3.33	$7.23
$9.01	$12.00	158,100	4.10	$10.68	9,033	3.70	$9.57
$12.01	$14.25	287,800	4.01	$13.24	56,333	3.94	$13.15
		8,984,953	**3.41**	**$5.50**	**3,001,592**	**2.06**	**$4.69**

Performance Warrants

On January 14, 2005, as part of the Corporation's initial restructuring to become a public entity, the Corporation issued performance warrants with an exercise price of $3.00 to members of its management team as a long term incentive. Each performance warrant entitles the holder to purchase one common share at the exercise price. At June 30, 2009, there were 2,939,732 performance warrants outstanding and exercisable (June 30, 2008 – 2,939,732). Because the performance conditions were fulfilled in 2005, resulting in the performance warrants vesting, the full related expense was recorded in the statement of net income (loss) and retained earnings in that year.

On May 28, 2009, the Corporation's outstanding performance warrants were amended to extend the ultimate expiration date from January 31, 2010 to January 31, 2015 (the "**Extension**"). The Corporation recorded a non-cash stock-based compensation expense of $3.1 million relating to the extension of the performance warrants for the three and six month periods ending June 30, 2009. This amount represents the fair value of the Extension determined by the difference between the fair value of the outstanding performance warrants with the expiration date of January 31, 2015 (the "extended term") and the fair value of the outstanding performance warrants with the expiration date of January 31, 2010 (the "original term"). The fair value in each case was estimated as at May 28, 2009 using the Black-Scholes option-pricing model that takes into account: exercise price, expected life, current price, expected volatility, expected dividends, and risk-free interest rates.

Using the Black-Scholes option-pricing model, the fair value of each extended term and original term performance warrant was $4.27 and $3.23, respectively.

The assumptions used in calculating the fair value of the extended and original term performance warrants at May 28, 2009 are set forth below:

	Extended Term Performance Warrants	**Original Term Performance Warrants**
Risk-free interest rate	2.11%	2.11%
Expected maturity (years)	5.0	0.72
Expected volatility	63.0%	63.0%
Dividend yield	0%	0%

A summary of the changes during the three and six months ended June 30, 2009 and the Corporation's outstanding performance warrants as at June 30, 2009 is presented below:

	Number	**Weighted Average Exercise Price ($)**
Outstanding, December 31, 2008	**2,939,732**	**3.00**
Issued	-	**-**
Exercised	-	-
Outstanding, March 31 and June 30, 2009	**2,939,732**	**3.00**

Contributed Surplus Continuity

	$000's
Balance, December 31, 2007	**10,930**
Stock-based compensation expense – stock options [(1)]	5,004
Exercise of stock options	(2,930)
Cancellation of stock options[(2)]	(20)
Balance, December 31, 2008	**12,984**
Stock-based compensation expense – stock options [(1)]	1,747
Exercise of stock options	(279)
Balance, March 31, 2009	**14,452**
Stock-based compensation expense – stock options[(1)]	1,886
Stock-based compensation expense – performance warrants	3,060
Exercise of stock options	(408)
Balance, June 30, 2009	**18,990**

(1) Included in the stock-based compensation expense is the non cash impact of forfeitures and cancellations during the period.
(2) Included in the cancellation of stock options is cash paid to cancel 5,000 vested stock options during 2008.

12. COMMITMENTS

The Corporation is committed under an operating lease beginning December 1, 2007 which expires on November 30, 2017. Birchcliff does not use all of the leased space and has sublet the excess space to an arms' length party on a basis that recovers approximately 40% of the rental costs for the first five years. The Corporation is committed to the following aggregate minimum lease payments (not reduced by rents receivable by the Corporation)**:**

Year	***$000's***
2009	1,607
2010	3,214
2011	3,214
2012	3,223
2013	3,331
Thereafter	13,045

The Corporation is also committed to March 29, 2011 under an operating lease for another premise that it does not use and has sublet to an arm's length party on a basis that recovers all of its rental costs.

13. SUPPLEMENTARY CASH FLOW INFORMATION

The following table details the components of non-cash working capital:

	Three months ended June 30		**Six months ended June 30**	
($000's)	**2009**	**2008**	**2009**	**2008**
Provided by (used in)				
Accounts receivable	4,591	(5,908)	13,106	(11,828)
Prepaid and other	(1,891)	(314)	(2,611)	(799)
Accounts payable and accrued liabilities	(29,975)	(15,903)	(51,368)	8,849
	(27,275)	**(22,125)**	**(40,873)**	**(3,778)**
Provided by (used in)				
Operating	(11,518)	(592)	(5,768)	(8,412)
Investing	(15,757)	(21,533)	(35,105)	4,634
	(27,275)	**(22,125)**	**(40,873)**	**(3,778)**

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