Diaz Resources Ltd.

2009 Annual Report

Annual Meeting

The Annual Meeting of the Shareholders of Diaz Resources Ltd. will be held at 3:00 p.m. on Wednesday, June 23, 2010 in the Cardium Room of the Calgary Petroleum Club, 319 – 5 Avenue S.W., Calgary, Alberta.

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Corporate Profile

Diaz Resources Ltd. is an oil and gas exploration and development company with land holdings and production in Canada and the United States. The Company's principal business is the exploration for oil and natural gas, with the majority of the Company's revenue being generated from gas production in Alberta and Texas. Diaz's current focus is on oil development in Alberta and Saskatchewan.

Corporate Summary

(Thousands, except per share amounts)	Years Ended December 31	
	2009	**2008**
Financial		
Revenue	**$ 6,973**	$ 15,099
Cash flow from operations	**1,881**	7,737
per share, diluted	**0.03**	0.12
Loss for the period	**(14,355)**	(4,087)
per share, diluted	**(0.21)**	(0.06)
Capital additions	**4,415**	7,778
Dispositions	**4,407**	74
Net capital additions	**8**	7,704
Net current debt	**5,844**	8,449
Convertible debentures*	**6,377**	6,094
Total assets	**36,657**	56,761
Total shares outstanding at period end	**76,576,752**	67,177,752
Operations		
Production		
Gas (MMcfd)	**3.3**	4.5
Oil (Bopd)	**97**	140
BOEd (6 Mcf = 1 Bbl)	**642**	886
Product Prices		
Gas ($/Mcf)	**$4.72**	$8.32
Oil ($/Bbl)	**$54.51**	$86.08
Reserves (proved plus probable, future costs and prices)		
Gas (Bcf)	**16.7**	20.2
Oil (MBbl)	**1,058.0**	227.0
BOE (Millions)	**3.8**	3.7
Net present value of future net revenue, before tax discounted at 10% **	**$ 52.4**	$ 59.4
Undeveloped land holdings (net acres)		
Canada	**54,409**	50,108
United States	**446**	4,321
Total net acreage	**54,855**	54,429

* Convertible debentures have a face value of $7.1 million and mature on March 26, 2012. See Note 7, "Convertible Debentures", in the notes to the financial statements for the year ended December 31, 2009.

** Net present value of future net revenue may not represent fair market value of reserves.

Message to Shareholders

2009 was a difficult year for Diaz and gas-weighted junior oil and gas companies generally. The North American economy moved into recession during the second half of 2008 and 2009 and had two significant effects on the Company. They were:

- A drop in natural gas consumption, particularly in the US, leading to an over supply and downward pressure on natural gas prices, and
- A tightening of capital markets available to the Company to raise additional investment funds.

In addition, a number of the Company's US natural gas wells declined, at higher than anticipated rates.

As a result, Diaz revenues were significantly reduced and operating cash flows available for reinvestment were greatly reduced compared with prior years.

Diaz anticipated that 2009 would be a challenging year and the management worked to ensure that the Company came through the year successfully. Hence, Diaz focused on the reduction of balance sheet leverage, put in place fixed gas price contracts for half of the Company's 2009 gas production, and refocused the Company's exploration and development activities on heavy oil projects.

The results of these efforts were:

- Asset dispositions - $4.4 million was raised from the sale of properties in Canada and in the United States,
- Financing – the Company closed a financing, raising $926,000 at the end of 2009,
- 2009 Fixed Gas Price Contracts – Diaz received approximately $925,000 in additional revenue from fixed gas price contracts during 2009,
- Oil Development – Diaz commenced a heavy oil development program in the Lloydminster area, participating in the successful drilling of three wells during Q4 2009
- Heavy Oil Exploration – the Company acquired prospective acreage on a number of oil development projects in Alberta and Saskatchewan.

As a result of the above actions, Diaz reduced its net current bank debt from $8.5 million in January 2009 to approximately $5.8 million at the end of the year. The Company plans to continue to rationalize non-core assets with the sale of its remaining U.S. producing assets, which, being principally natural gas, will be marketed when natural gas prices recover to what management regards as an acceptable level.

With the improvement in the financial condition of the Company, available capital was redirected into its heavy oil exploration and development activity in East Central Alberta and West Central Saskatchewan.

Financial

Revenue for 2009 decreased to $7.0 million compared with $15.1 million for the prior year. Cash flow from operations for 2009 decreased to $1.9 million or $0.03 per share compared with $7.7 million or $0.12 per share for the prior year. Diaz reported a loss for 2009 of $14.3 million or ($0.21) per share versus a loss of $4.1 million or ($0.06) per share in the prior year, as it took an impairment write down against its oil and gas assets of $11.4 million during Q1 2009.

Capital expenditures for 2009, totalled $4.4 million compared with $7.8 million in the prior year. Capital expenditures and debt retirement were financed from cash flow from operations and the sale of two oil and gas properties.

At December 31, 2009, Diaz had net current debt of $5.8 million versus $8.5 million at the beginning of the year. Diaz also had convertible debentures outstanding of $7.1 million (face value) that mature on March 26, 2012.

Production

The Company's total production for the year ended December 31, 2009, decreased 28% to 642 BOEd compared with the prior year average of 886 BOEd. For the fourth quarter, total production declined 39% to 532 BOEd compared with 871 BOEd in Q4 2008.

In Canada, production for the year decreased 21% as a result of the sale of production from the Carmangay (Q1) and Parkman (Q4) fields and a significant drop in production from the Leahurst and Big Bend fields. In the U.S., production rates for the year fell by 45% as mature well production declines combined with the abandonment of the Black Owl field.

Reserves and Reserves Values

The independent engineering evaluation of Diaz's properties assigned proved reserves, before royalties, of 1.6 million BOE and total reserves, before royalties, of 3.8 million BOE at December 31, 2009. These reserve estimates result in a before tax present value of estimated future net revenues, discounted at 10%, of $52.4 million.

Exploration and Development

Due to the drop in natural gas prices during the fall of 2008, Diaz changed its exploration focus exclusively to oil prospects. During 2009, Diaz acquired 18,707 acres (14,048 net acres) in Alberta and Saskatchewan resulting in a substantial portfolio of development projects on the Lloydminster oil play in Alberta as well as the Shaunavan, Bird Bear, and Viking oil plays in Saskatchewan.

During Q4 2009, Diaz drilled three Lloydminster heavy oil horizontal wells which are now on production. Subsequent to year end Diaz participated in drilling three additional horizontal wells on the same prospect at Lloydminster, Alberta and anticipates placing them on production early in the second quarter of 2010.

Business Outlook

The Company anticipates steady growth in the North American economy during 2010.

As a result oil prices should continue to firm as industrial activity recovers. Due to current high natural gas storage levels and significant volumes of gas being developed on North American shale gas projects there is still considerable uncertainty as to when natural gas prices will recover to satisfactory levels. To mitigate the uncertainty in natural gas prices, Diaz has put in place fixed gas price contracts for approximately half of the Company's anticipated 2010 gas production, at prices in excess of $5.75 per Mcf. Diaz has also closed an equity financing raising approximately $1,263,500 net of commissions to fund its ongoing Lloydminster heavy oil development drilling program.

Due to this potential ongoing weakness in the gas sector Diaz will continue to direct its efforts towards heavy oil development during 2010. The Company will continue to focus on its Lloydminster heavy oil development program and if results are successful Diaz would exit 2010 with almost half of its production derived from oil sales.

On behalf of the Board,

Donald K Clark

R.W. Lamond, Chairman

D.K. Clark, Chief Operating Officer

March 30, 2010

Operations Review

In the following description of Diaz's principal oil and natural gas properties, reserve and production amounts stated are gross reserves based on forecast costs and prices, as evaluated by AJM Petroleum Consultants. The estimates of reserves and future net revenue for the individual properties may not reflect the same confidence level as estimates and reserves in future net revenue for all properties due to the effects of aggregation.

Canadian Drilling Program

In Canada, during the year ended December 31, 2009, 4 wells were drilled (net 1.60) resulting in 4 oil wells (net 1.6).

Lloydminster, Alberta – Working Interest 50%

Diaz has a 50% working interest in 4 producing heavy oil wells (2.0 net wells). The Lloydminster field is the primary development focus of the Company. Three additional wells were drilled during Q1 2010 and are expected to be on production early in Q2 1010.

Lloydminster	Heavy Oil	
Reserves		
Proved developed producing	46	MBbl
Proved developed non-producing	27	MBbl
Proved undeveloped	200	MBbl
Probable	617	MBbl
Total proved plus probable	890	MBbl
Q4 2009 average production	43	Bopd

Lloydminster Proved plus Probable reserves totalled 890 MBOE, (23.2% of Total Company Reserves)

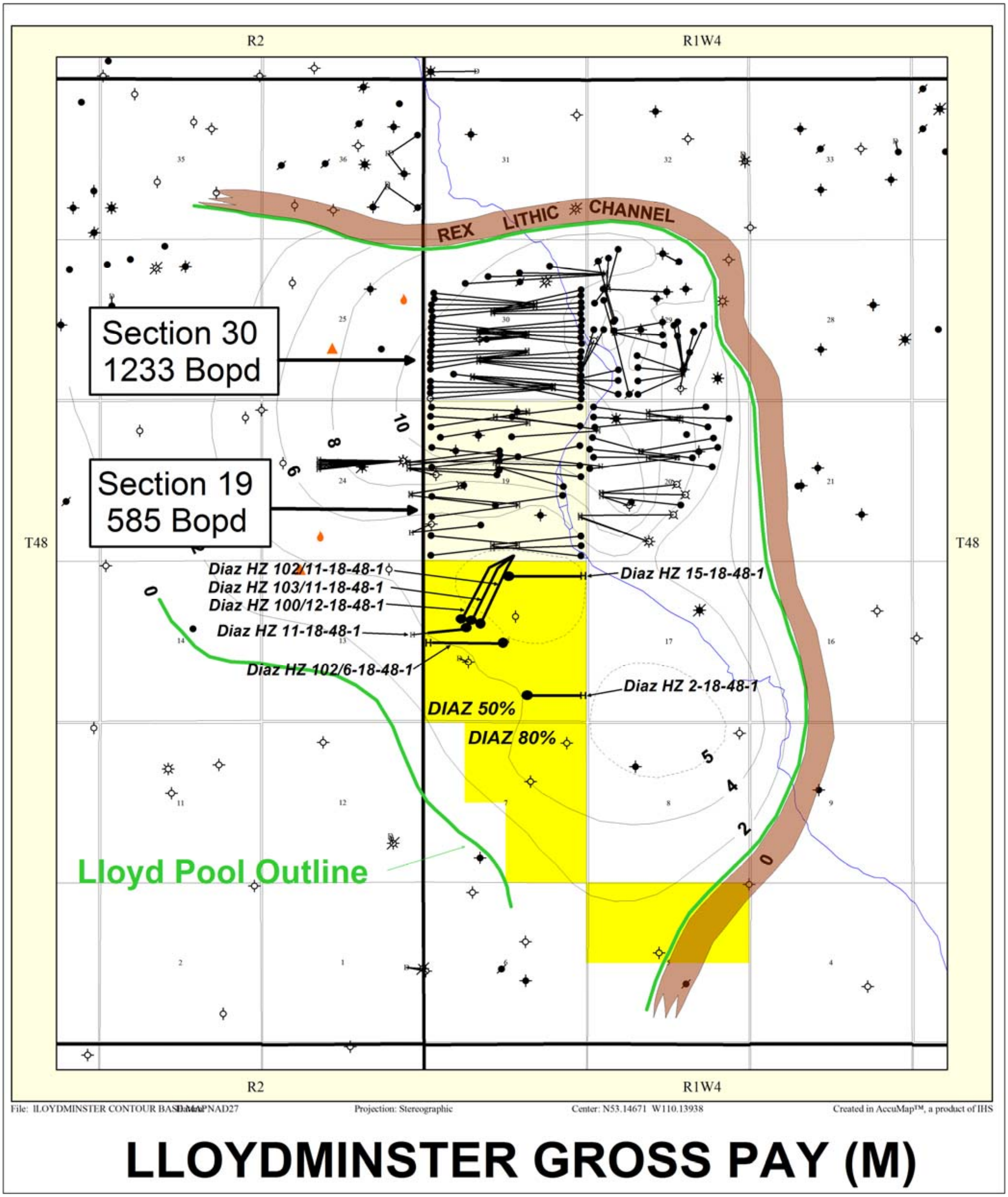
Diaz believes the Lloydminster heavy oil play may support up to 35 wells on one section, with initial production rates of approximately 60 Bopd per well. The AJM Report outlined in the "Oil and Gas Reserves" section, later in this report, assigns 60,000 barrels of proved plus probable reserves to 24 undrilled wells on this field. On the next page, is a gross pay map of the Lloydminster pool, showing Diaz's four producing wells and three horizontal wells drilled during Q1 2010 which are anticipated to be on production during Q2 2010. Diaz believes the project has very attractive economics with oil prices in the range of $80 per barrel, the drilling royalty credit and a 5% royalty for the first year of production.

Diaz currently plans to continue development drilling at the Lloydminster field starting in the summer of 2010.

Lloydminster field development economic assumptions include:

- Average gross well cost $750,000 drilled plus $200,000 for completion and production facilities.
- New well initial production - 60 bopd with a 20% annual decline.
- Revenue based on $65 per barrel.
- Operating costs - $15 per barrel.
- Alberta royalty rate of 5% for the first year of production
- Alberta drilling credits - $200 per meter drilled prior to March 31, 2011.

The following Lloydminster gross pay map includes average production for January 2010 for Sections 30 and 19.



Retlaw, Alberta

Diaz has interests in 43 producing gas wells (15.1 net wells), 1 shut-in gas well (0.5 net wells) and 1 oil well (0.5 net) in the Retlaw area located 90 miles southeast of Calgary, Alberta.

The Company's production at Retlaw, throughout 2009, averaged 741 Mcfd compared with 1,021 Mcfd for 2008. Q4 2009 production decreased to 519 Mcfd compared with 1,424 Mcfd in Q4 2008.

Retlaw	Oil and NGLs		Natural Gas	
Reserves				
Proved developed producing	3	MBbl	669	MMcf
Proved undeveloped	4	MBbl	1,061	MMcf
Probable	3	MBbl	924	MMcf
Total proved plus probable	10	MBbl	2,654	MMcf
Q4 2009 average production			519	Mcfd

Retlaw Proved plus Probable reserves totalled 452 MBOE, (11.8% of Total Company Reserves)

Enchant South – Hays, Alberta

In the Enchant South – Hays area, located 110 miles southeast of Calgary, Diaz has an interest in 39 producing gas wells (22.5 net wells) and 3 producing oil wells (2.1 net wells).

Enchant South	Natural Gas	
Reserves		
Proved developed producing	530	MMcf
Proved undeveloped	170	MMcf
Probable	1,501	MMcf
Total proved plus probable	2,201	MMcf
Q4 2009 average production	469	Mcfd

Enchant South Proved plus Probable reserves totalled 367 MBOE, (9.6% of Total Company Reserves)

Provost, including Leahurst – Alberta

Diaz holds an 80% working interest in the Leahurst field located in the Provost area. The well was drilled during October 2007 and began first production during June 2008 at over 600 Mcfd (net 480 Mcfd). The well has produced continuously since then with a natural gas production rate for the well in December 2009, of 193 Mcfd (net 155 Mcfd).

Provost, including Leahurst	Natural Gas	
Reserves		
Proved developed producing	169	MMcf
Proved developed non-producing	643	MMcf
Probable	232	MMcf
Total proved plus probable	1,044	MMcf
Q4 2009 average production	168	Mcfd

Provost, including Leahurst Proved plus Probable reserves totalled 174 MBOE, (4.5% of Total Company Reserves)

Big Bend – North-central Alberta

Diaz has an 80% working interest in the Big Bend field, located in north-central Alberta. The well was shut-in during the second half of the year awaiting workover operations which were completed in February 2010. March 2010 production rates have been in excess of 500 Mcfd.(400 Mcfd net).

Big Bend	Natural Gas	
Reserves		
Proved developed producing	407	MMcf
Proved undeveloped	228	MMcf
Probable	249	MMcf
Total proved plus probable	884	MMcf
Q4 2009 average production (shut-in)	-	Mcfd

Big Bend Proved plus Probable reserves totalled 147 MBOE, (3.8% of Total Company Reserves)

United States Drilling Program

Diaz's United States drilling program has been in the Wilcox deep gas trend concentrated in an area 100 miles South West of Houston, Texas. During the year ended December 31, 2009, 1 well was drilled (net 0.05) resulting in 1 gas well (0.05).

Provident City, Lavaca County, Texas – Working Interest 13%

The Company owns a 13% working interest in two natural gas wells producing from zones in the Wilcox formation in the Provident City field, Lavaca County.

The Provident City #1 well was producing at an average rate of approximately 1.6 MMcfd (207 Mcfd net) during the month of December 2009. Also, during the month of December, the Provident City #2 well averaged a production rate of 714 Mcfd (91 Mcfd net).

Provident City	Oil and NGLs	Natural Gas
Reserves		
Proved developed producing	4 MBbl	392 MMcf
Probable	13 MBbl	1,251 MMcf
Total proved plus probable	17 MBbl	1,643 MMcf
Q4 2009 average production	2 Bopd	295 Mcfd

Provident City Proved plus Probable reserves totalled 291 MBOE, (7.6% of Total Company Reserves)

Hound Dog, Lavaca County, Texas – Working Interest 28.1% and 25.3%

Diaz has a 28.1% working interest in the R. Dickson #1 well, a 25.3% working interest in the R. Dickson #2 well and a 25.3% working interest in the balance of the 1,635 acres of land.

The R. Dickson #1 well was producing 70 Mcfd (net 19 Mcfd) at the end of December 2009. The R. Dickson #2 well was producing 330 MMcfd (net 83 Mcfd) at year end.

Hound Dog	Natural Gas
Reserves	
Proved developed producing	58 MMcf
Probable	2,247 MMcf
Total proved plus probable	2,305 MMcf
Q4 2009 average production	91 Mcfd

Hound Dog Proved plus Probable reserves totalled 384 MBOE, (10.0% of Total Company Reserves)

N.W. Speaks Robertson #1 Well, Lavaca County, Texas – Working Interest 21.6 %

The N.W. Speaks Robertson #1 well was producing at 256 Mcfd (net 54 Mcfd) during December 2009.

NW Speaks	Natural Gas
Reserves	
Proved developed producing	46 MMcf
Proved developed non-producing	157 MMcf
Probable	880 MMcf
Total proved plus probable	1,083 MMcf
Q4 2009 average production	38 Mcfd

NW Speaks Proved plus Probable reserves totalled 181 MBOE, (4.7% of Total Company Reserves)

Oil and Gas Reserves

An independent evaluation of the Company's oil and gas reserves, conducted by AJM Petroleum Consultants, dated March 15, 2010, has assigned proved and probable reserves of 3.8 million BOE to the Company's properties, having an estimated net present value, before income tax of $52.4 million, at a 10% discount rate. There is no assurance that this represents the fair value of the assets.

Summary of Oil and Gas Reserves and Net Present Values of Future Net Revenue

Diaz's proved reserves were 18% lower than in the prior year while proved plus probable reserves increased by 4.5%. Proved reserve additions from the Lloydminster heavy oil field partially offset negative technical revisions and the sale of several properties during 2009. The significant increase in probable reserves came mostly from the Lloydminster heavy oil field.

Company Total	Light and Medium Oil		Heavy Oil		Natural Gas		Natural Gas Liquids		Total BOE	
	Gross	Net	Gross	Net	Gross	Net	Gross	Net	Gross	Net
Reserves Category	(MBbl)	(MBbl)	(MMcf)	(MMcf)	(MMcf)	(MMcf)	(MBbl)	(MBbl)	(MBOE)	(MBOE)
Proved										
Developed Producing	33	25	46	49	3,173	2,701	22	14	630	538
Developed Non-producing	7	6	27	22	1,425	1,175	6	5	278	229
Undeveloped	-	-	200	185	2,505	2,199	32	21	650	573
Total Proved	40	31	273	256	7,103	6,075	60	40	1,558	1,340
Probable	37	29	617	535	9,594	7,623	31	20	2,284	1,855
Total Proved Plus Probable	77	60	890	791	16,697	13,698	91	60	3,842	3,195

Company Tool	Before Income Taxes Discounted At (% Per Year)					After Income Taxes Discounted At (% Per Year)				
	0	5	10	15	20	0	5	10	15	20
Reserves Category	(MM$)	(MM$)	(MM$)	(MM$)	(MM$)	(MM$)	(MM$)	(MM$)	(MM$)	(MM$)
Proved										
Developed Producing	13.5	11.8	10.5	9.6	8.8	13.2	11.5	10.3	9.4	8.7
Developed Non-producing	6.8	5.1	4.1	3.3	2.7	6.6	5.0	4.0	3.2	2.6
Undeveloped	14.6	10.4	7.8	6.0	4.7	13.9	10.1	7.6	5.9	4.6
Total Proved	34.9	27.3	22.4	18.9	16.2	33.7	26.6	21.9	18.5	15.9
Probable	60.5	41.8	30.0	22.1	16.7	44.7	30.8	22.0	16.2	12.2
Total Proved Plus Probable	95.4	69.1	52.4	41.0	32.9	78.4	57.4	43.9	34.7	28.1

More detailed information with respect to the reserves reports, including cost and pricing assumptions and reserve classifications can be found in the Company's Annual Information Form. There is no assurance that the above amounts represent the fair value of the assets.

The following sets forth the benchmark reference prices, as at December 31, 2009, reflected in the Reserves Data. These price assumptions were provided to the Corporation by AJM, the Corporation's independent qualified evaluator.

			Oil		Natural Gas		NGLs		
			WTI Cushing Oklahoma	Edmonton Par Price 40^0 API	AECO Gas Price	NYMEX Gas Price	Edmonton Par Price		
Year	Inflation Rate	Exchange Rate	($US/bbl)	($Cdn/bbl)	($Cdn/Mcf)	($US/Mcf)	Propane ($Cdn/bbl)	Butane ($Cdn/bbl)	Condensate ($Cdn/bbl)
2010	0.0%	0.950	75.00	77.55	5.80	5.75	42.65	62.05	81.45
2011	2.0%	0.950	81.60	84.45	6.70	6.65	46.45	67.55	88.65
2012	2.0%	0.950	85.85	88.90	7.05	7.00	48.90	71.10	93.35
2013	2.0%	0.950	90.20	93.45	7.45	7.30	51.40	74.75	98.15
2014	2.0%	0.950	97.40	101.05	7.55	7.60	55.60	80.85	106.10
2015	2.0%	0.950	104.90	108.85	7.75	7.95	59.85	87.10	114.30
2016	2.0%	0.950	112.60	116.95	7.90	8.45	64.30	93.55	122.80
2017	2.0%	0.950	114.85	119.30	8.25	8.80	65.60	95.45	125.25
2018	2.0%	0.950	117.15	121.70	8.55	9.15	66.95	97.35	127.80
2019	2.0%	0.950	119.50	124.10	8.85	9.45	68.25	99.30	130.30
2020	2.0%	0.950	121.90	126.60	9.15	9.75	69.65	101.30	132.95
2021	2.0%	0.950	124.35	129.15	9.35	9.95	71.05	103.30	135.60
2022	2.0%	0.950	126.80	131.70	9.50	10.15	72.45	105.35	138.30
2023	2.0%	0.950	129.35	134.35	9.70	10.35	73.90	107.50	141.05
2024	2.0%	0.950	131.95	137.05	9.90	10.55	75.40	109.65	143.90
2025	2.0%	0.950	134.60	139.80	10.10	10.75	76.90	111.85	146.80
2026	2.0%	0.950	137.30	142.55	10.30	11.00	78.40	114.05	149.70
2027	2.0%	0.950	140.00	145.40	10.50	11.20	79.95	116.30	152.65
2028	2.0%	0.950	142.80	148.35	10.70	11.45	81.60	118.70	155.75
2029	2.0%	0.950	145.70	151.30	10.95	11.65	83.20	121.05	158.85
2029+	2.0%	0.950	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%

Management's Discussion and Analysis ("MD&A")

March 30, 2010

The following discussion and analysis is management's assessment of Diaz's historical, financial and operating results. This review should be read in conjunction with the audited financial statements at December 31, 2009. The reader should be aware that historical results are not necessarily indicative of future performance.

The three months ended December 31, 2009, have not been audited by the Company's auditor.

Basis of Presentation

The financial data presented herein has been prepared in accordance with accounting principles generally accepted in Canada. All dollar amounts are in Canadian dollars unless otherwise indicated.

Non-GAAP Measurements – The Management's Discussion and Analysis contains the term "cash flow from operations", which should not be considered an alternative to, or more meaningful as an indicator of the Company's performance than, "cash flow from operating activities", as determined in accordance with accounting principles generally accepted in Canada. Diaz's determination of "cash flow from operations" may not be particularly comparable to that reported by other companies especially those in other industries. Management uses "cash flow from operations" as a measure of operating performance as the measure is not exposed to non-cash working capital movements, which for a small company, could be material and misleading. The reconciliation of "cash flow from operating activities" and "cash flow from operations" is as follows:

($ Thousands, Three Months Unaudited)	Three Months Ended December 31		Year Ended December 31	
	2009	**2008**	**2009**	**2008**
Cash provided by (used for) Operating Activities:	**$ 400**	$ 573	**$ 2,778**	$ 7,761
Adjusted for:				
Abandonments	**87**	$ (128)	**$ 120**	$ 115
Change in non-cash working capital	**(128)**	701	**(1,017)**	(139)
Cash flow from operations	**$ 359**	$ 1,146	**$ 1,881**	$ 7,737

The Company also presents "annualized cash flow from operations" which equals four times the quarterly "cash flow from operations". "Cash flow from operations" per share is calculated using the weighted average shares outstanding consistent with the calculation of earnings per share. In addition, the Company presents "Net current debt", which is calculated as the aggregate of current assets and current liabilities.

BOE Presentation – The term barrels of oil equivalent (BOE) may be misleading, particularly if used in isolation. A BOE conversion ratio of 6 Mcf: 1 Bbl is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead. All BOE conversions in this report are derived by converting gas to oil in the ratio of six Mcf of gas to one Bbl of oil.

Forward-looking Statements – Certain of the statements contained herein including, without limitation, financial and business prospects and financial outlook, reserve and production estimates, drilling and re-completion plans, timing of drilling, completion and tie-in of wells and capital expenditures and the timing thereof may be forward-looking statements. Words such as "may", "will", "should", "could", "anticipate", "believe", "expect", "intend", "plan", "potential", "continue" and similar expressions may be used to identify these forward-looking statements. These statements reflect management's beliefs at the date of the report and are based on information available to management at that time. Forward-looking statements involve significant risk and uncertainties.

A number of factors could cause actual results to differ materially from the results discussed in the forward-looking statements including, but not limited to, risks associated with oil and gas exploration, development, exploitation, production, marketing and transportation, loss of markets, volatility of commodity prices, currency fluctuations, imprecision of reserve estimates, environmental risks, competition from other producers, inability to retain drilling rigs and other services, incorrect assessment of the value of acquisitions, failure to realize the anticipated benefits of acquisitions, delays resulting from or inability to obtain required regulatory approvals and ability to access sufficient capital from internal and external sources and the risk factors outlined under "Risk Factors" in the Company's Annual Information Form and elsewhere herein. The recovery and reserve estimates of Diaz's reserves provided herein are estimates only and there is no guarantee that the estimated reserves will be recovered. As a consequence, actual results may differ materially from those anticipated in the forward-looking statements. Readers are cautioned that the foregoing list of factors is not exhaustive. Additional information on these and other factors that could effect Diaz's operations and financial results are included in reports on file with Canadian securities regulatory authorities and may be accessed through the SEDAR website (www.sedar.com) or at Diaz's website (www.diazresources.com). Although the forward-looking statements contained herein are based upon what management believes to be reasonable assumptions, including but not limited to assumptions as to the price of oil and natural gas, interest rates, exchange rates and the regulatory and legal environment in which Diaz operates, the producibility of Diaz's reserves, the capital expenditures program and future operations and other matters, management cannot assure that actual results will be consistent with these forward-looking statements. Investors should not place undue reliance on forward-looking statements. These forward-looking statements are made as of the date hereof and the Company assumes no obligation to update or review them to reflect new events or circumstances except as required by applicable securities laws.

Forward-looking statements and other information contained herein concerning the oil and gas industry and the Company's general expectations concerning this industry is based on estimates prepared by management using data from publicly available industry sources as well as from reserve reports, market research and industry analysis and on assumptions based on data and knowledge of this industry which the Company believes to be reasonable. However, this data is inherently imprecise, although generally indicative of relative market positions, market shares and performance characteristics. While the Company is not aware of any misstatements regarding any industry data presented herein, the industry involves risks and uncertainties and is subject to change based on various factors.

Summary of Results

The following table provides financial data derived from the Company's financial statements for the past three years:

($ Thousands, except per BOE, BOEd and per share amounts)		**2009**		2008		**Years Ended December 31** 2007
Total revenue	**$**	**6,973**	$	15,099	$	12,082
Cash flow from operations	**$**	**1,881**	$	7,737	$	5,429
per share, basic and diluted	**$**	**0.03**	$	0.12	$	0.08
Earnings (loss) for the period	**$**	**(14,355)**	$	(4,087)	$	(1,605)
per share, basic and diluted	**$**	**(0.21)**	$	(0.06)	$	(0.02)
Property, plant & equipment impairment	**$**	**(11,408)**	$	(2,744)	$	-
Total assets	**$**	**36,657**	$	56,761	$	60,794
Net current debt	**$**	**5,844**	$	8,449	$	8,542
Convertible debentures	**$**	**6,377**	$	6,094	$	5,832
Production (BOEd)		**642**		886		865
Price ($ per BOE)	**$**	**32.22**	$	55.64	$	45.73

During 2009, weak commodity prices combined with reduced production levels resulting in decreased revenues and cash flows from operations compared with the prior two years. The loss for 2009 was higher than the prior year as a loss of $2.9 million for the year combined with an $11.4 million impairment of oil and gas assets during the first quarter of 2009. The asset impairment in Q1 2009 resulted from a sharp drop in oil and natural gas prices that reduced the present value of future cashflows below the carrying value of those assets.

Diaz was able to reduce its net current debt in 2009 by selling several of its producing oil assets and by completing a financing in October 2009.

Operations

Diaz is primarily a natural gas producer with 85% of its production for the year ended December 31, 2009, coming from natural gas wells. Diaz owns interests in producing properties in Alberta and Saskatchewan in Canada, and in Texas in the United States. Where meaningful, the following production information has been segmented for each of the Company's geographic areas of operations.

Oil & Gas Production	Three Months Ended December 31 2009	2008	Years Ended December 31 2009	2008
Gas - Canada				
Retlaw	**519**	1,424	**741**	1,021
Enchant	**469**	444	**441**	467
Leahurst	**168**	383	**260**	250
Big Bend	**-**	113	**128**	207
Therien	**148**	155	**150**	167
Jaslan	**58**	143	**99**	142
Carmangay	**78**	119	**89**	137
Other	**479**	516	**575**	648
Gas - Canada (Mcfd)	**1,919**	3,297	**2,483**	3,039
Oil & Liquids - Canada				
Lloydminster	**43**	22	**28**	17
Parkman *	**-**	27	**20**	36
Red Earth	**5**	11	**8**	8
Harmattan	**4**	9	**6**	6
Carmangay *	**-**	17	**2**	15
Hays	**1**	2	**1**	7
Other	**28**	32	**25**	39
Oil & Liquids - Canada (Bopd)	**81**	120	**90**	128
BOEd - Canada (6 Mcf = 1 Bbl)	**401**	670	**504**	635
Gas - U.S.				
Provident City	**295**	369	**345**	497
Hound Dog	**91**	177	**128**	288
Black Owl	**-**	346	**71**	347
Allen Ranch	**58**	66	**69**	118
Other	**267**	186	**170**	183
Gas - U.S. (Mcfd)	**711**	1,144	**783**	1,433
Oil & Liquids - U.S.				
Provident City	**2**	4	**3**	5
Black Owl	**-**	6	**1**	6
Other	**10**	-	**3**	1
Oil & Liquids - U.S. (Bopd)	**12**	10	**7**	12
BOEd - U.S. (6 Mcf = 1 Bbl)	**131**	201	**138**	251
Gas - Company (Mcfd)	**2,630**	4,441	**3,266**	4,472
Oil and Liquids - Company (Bopd)	**93**	130	**97**	140
BOEd - Company	**532**	871	**642**	886

* The Carmangay oil property was sold in Q1 2009. The Parkman oil property was sold in Q4 2009.

The Company's total production for the year ended December 31, 2009, decreased 28% to 642 BOEd compared with the prior year average of 886 BOEd. For the fourth quarter, total production declined 39% to 532 BOEd compared with 871 BOEd in Q4 2008.

In the U.S., production rates for the year fell by 45% as mature well production declines combined with the abandonment of the Black Owl field. In Canada, production for the year decreased 21% as the sale of production from the Carmangay (Q2) and Parkman (Q4) fields combined with declining production from mature wells and a significant drop in production from the Leahurst and Big Bend fields during the second half of the year. Big Bend was shutin because of excessive water production and can only be accessed during the winter. A workover at the Big Bend field was completed in February 2010. The well is back on production with rates in excess of 500 Mcfd (400 Mcfd net).

Product Prices	**Three Months Ended December 31**		**Years Ended December 31**	
	2009	**2008**	**2009**	**2008**
Canada				
Gas ($/Mcf)	**$ 5.27**	$ 7.66	**$ 4.88**	$ 7.99
Oil & Liquids ($/Bbl)	**$ 62.78**	$ 60.58	**$ 55.13**	$ 84.12
$/BOE	**$ 37.91**	$ 48.61	**$ 33.84**	$ 55.21
U.S.				
Gas ($/Mcf)	**$ 4.13**	$ 7.40	**$ 4.20**	$ 9.04
Oil & Liquids ($/Bbl)	**$ 33.19**	$ 82.56	**$ 46.25**	$ 107.33
$/BOE	**$ 25.59**	$ 46.24	**$ 26.26**	$ 56.73
$/BOE - Company	**$ 34.87**	$ 48.06	**$ 32.22**	$ 55.64

In Canada and in the U.S., average BOE prices for the fourth quarter and for the year were approximately 27% and 42% lower respectively than realized in the comparative prior year periods.

Canada Natural Gas Prices Adjusted For Fixed Gas Contracts	**Three Months Ended December 31**		**Years Ended December 31**	
	2009	**2008**	**2009**	**2008**
Canada				
Gas price without contracts $/Mcf	**$ 4.53**	$ 6.98	**$ 3.86**	$ 8.00
Fixed gas contract benefit (cost) $/Mcf	**$ 0.74**	$ 0.68	**$ 1.02**	$ (0.01)
Gas price with contracts $/Mcf	**$ 5.27**	$ 7.66	**$ 4.88**	$ 7.99
Fixed gas contract benefit (cost) $ '000	**$ 129**	$ 205	**$ 925**	$ (12)

The Canadian natural gas price includes the effect of fixed gas contracts in the current year and prior year periods.

As detailed above, Diaz added $925,000 to its revenue for the year ended December 31, 2009, compared with a a negative impact of $12,000 in the prior year period as a result of committing to fixed gas contracts. For the fourth quarter, Diaz added $129,000 to its revenue compared with $205,000 in Q4 2009.

Revenue from Oil and Gas Production *($ Thousands)*	**Three Months Ended December 31**		**Years Ended December 31**	
	2009	**2008**	**2009**	**2008**
Canada				
Natural gas	**$ 920**	$ 2,326	**$ 4,421**	$ 8,887
Oil and natural gas liquids	**461**	672	**1,792**	3,935
Total - Canada	**1,381**	2,998	**6,213**	12,822
U.S.				
Natural gas	**268**	778	**1,200**	4,738
Oil and natural gas liquids	**37**	74	**114**	464
Total - U.S.	**305**	852	**1,314**	5,202
Total Production Revenue - Company	**$ 1,686**	$ 3,850	**$ 7,527**	$ 18,024

For the year ended December 31, 2009, the approximate 40% - 50% reduction in average natural gas and oil prices combined with declines in production resulting in a drop of revenues of 56% in the fourth quarter and a reduction of revenues of 58% for the 2009 year compared with the prior year periods.

Production and price declines in the U.S. were larger than in Canada during the fourth quarter during the year resulting in a sharper drop in U.S. revenues compared with the prior year periods than was realized in Canada.

Royalties *($ Thousands, except per BOE and percentage amounts)*	Three Months Ended December 31 2009	Three Months Ended December 31 2008	Years Ended December 31 2009	Years Ended December 31 2008
Canada				
Crown	**$ 56**	$ 46	**$ 148**	$ 1,070
Freehold	**48**	273	**318**	778
Royalties	**$ 104**	$ 319	**$ 466**	$ 1,848
per BOE	**$ 2.84**	$ 5.19	**$ 2.54**	$ 7.96
Royalties as a percentage of revenue	**7.2%**	10.3%	**7.3%**	14.0%
U.S.				
Royalties	**$ 74**	$ 256	**$ 264**	$ 1,477
per BOE	**$ 6.20**	$ 13.85	**$ 5.27**	$ 16.11
Royalties as a percentage of revenue	**23.4%**	29.5%	**19.9%**	28.3%
Total Royalties - Company	**$ 178**	$ 575	**$ 730**	$ 3,325
per BOE	**$ 3.67**	$ 7.19	**$ 3.12**	$ 10.27

In Canada, royalty expense decreased overall as a result of weak natural gas and oil prices which in Alberta also results in a reduced royalty rate. During the second quarter of 2009, the annual gas cost allowance adjustment resulted in a credit to Diaz of $42,000 further reducing crown royalties. Diaz anticipates royalty rates should average approximately 10% to 14% of Canadian revenue for 2010 as natural gas prices are expected to be in the $4.50 - $5.50 per Mcf range. Resulting from the Lloydminster Q4 2009 three well drilling program, Diaz has earned Alberta Royalty Drilling Credits totaling $151,300 which can be used to offset up to 50% of Diaz's Alberta Crown Royalty during 2010. Diaz has also earned but has not yet assigned an additional $272,000 in royalty drilling credits.

In the United States, royalties decreased in the second quarter resulting from the receipt of a refund from the Texas Railroad Commission of $87,000 for royalty paid on a deep gas well that qualified for a temporary exemption. This has resulted in a lower than expected royalty rate for the year. Royalties are generally fixed rates in the U.S. and Diaz expects royalty rates to average 28% to 31% of U.S. revenue during 2010.

Operating and Transportation Expense *($ Thousands, except per BOE amount)*	Three Months Ended December 31 2009	Three Months Ended December 31 2008	Years Ended December 31 2009	Years Ended December 31 2008
Canada	**$ 671**	$ 1,275	**$ 2,919**	$ 3,927
per BOE	**18.45**	20.64	**15.90**	16.91
U.S.	**6**	121	**177**	440
per BOE	**0.49**	6.58	**3.55**	4.80
Total Expense - Company	**677**	1,396	**3,096**	4,367
per BOE	**$ 14.03**	$ 17.40	**$ 13.25**	$ 13.48

In Canada and in the U.S., the three and twelve month period operating costs per BOE were lower than the comparable prior year periods. In Canada, operating cost reductions were realized from the correction of a facility fee at its Parkman property, yielding a one time lump sum recovery from partners – the property was sold during October. In the U.S., operating cost savings have resulted from a reduction in the Company's estimate for property taxes which are based on natural gas revenues.

In total, operating costs for Q4 2009 decreased by 51% to $677,000 compared with $1.4 million in Q4 2008. Operating costs for 2009 reduced by 29% to $3.1 million compared with $4.4 million in the prior year.

Overhead & Stock Based Compensation *($ Thousands, except per BOE amounts)*	**Three Months Ended December 31 2009**	**2008**	**Years Ended December 31 2009**	**2008**
Cash compensation costs	**$ 279**	$ 355	**$ 1,246**	$ 1,351
Cash compensation recovered	**(53)**	$ (48)	**$ (200)**	$ (210)
Net cash compensation	**226**	$ 307	**$ 1,046**	$ 1,141
Other overhead costs	**407**	455	**1,466**	1,466
Other overhead recovered	**(57)**	(62)	**(238)**	(228)
Net other overhead	**350**	393	**1,228**	1,238
Total cash overhead	**576**	700	**2,274**	2,379
Stock based compensation costs	**90**	(66)	**169**	129
Recovered from third parties	**(204)**	(91)	**(1,051)**	(395)
Capitalized	**(59)**	(42)	**(214)**	(190)
Net overhead	**403**	501	**1,178**	1,923
per BOE	**$ 8.32**	$ 6.26	**$ 5.04**	$ 5.94

Cash compensation and other overhead costs of $576,000 for Q4 2009 and $2.3 million for 2009 were slightly less than the prior year periods. However, net overhead costs for 2009 were significantly reduced compared with the prior year as Diaz's recoveries from third parties of $1.1 million were much higher than the comparable prior year periods. The increased recovery included a one-time adjustment to Management fees charged to a related third party in Q2 2009 of $389,000 combined with additional Management fees charged to other related third parties.

Interest Expense *($ Thousands, except per BOE and percentage amounts)*	**Three Months Ended December 31 2009**	**2008**	**Years Ended December 31 2009**	**2008**
Interest expense	**$ 222**	$ 293	**$ 958**	$ 1,169
Debenture accretion and issue costs	**73**	67	**282**	262
Interest expense	**295**	360	**1,240**	1,431
per BOE	**6.10**	4.50	**5.31**	4.42
Average interest rate on bank debt	**4.5%**	4.9%	**4.2%**	5.6%
Average bank debt	**6,768**	7,832	**6,616**	8,682
Interest rate on convertible debentures	**8.75%**	8.75%	**8.75%**	8.75%
Convertible debentures - face value	**$ 7,085**	$ 7,085	**$ 7,085**	$ 7,085

Total interest expense for the fourth quarter was reduced compared with the prior year period. For 2009, interest expense decreased to $1.2 million compared with $1.4 million for the prior year. The decreases for the quarterly and year to date comparatives resulted from lower average interest rates and lower average bank debt in the current year.

Income Taxes *($ Thousands)*	Three Months Ended December 31 2009	2008	Years Ended December 31 2009	2008
Canada				
Current tax expense	**$ -**	$ 11	**$ 17**	$ 17
Future tax expense (recovery)	**1,729**	(1,034)	**(2,355)**	(1,126)
Total - Canada	**1,729**	(1,023)	**(2,338)**	(1,109)
U.S.				
Current tax expense	**(4)**	(22)	**12**	15
Future tax expense (recovery)	**(152)**	(62)	**(725)**	172
Total - U.S.	**(156)**	(84)	**(713)**	187
Total - Company	**$ 1,573**	$ (1,107)	**$ (3,051)**	$ (922)

Current taxes paid in Canada consist of capital tax and Saskatchewan provincial tax, which are based on the Company's balance sheet and gross revenue in the province. In Canada, the Company has estimated income tax pools that, together with its planned exploration and development expenditures, should be sufficient to allow Diaz to defer current taxes payable during 2010. Future tax recoveries in Canada result from reduced tax rates anticipated in future years plus the impact of the impairment of assets charged to income in 2009.

At year end, Diaz had the following tax pools available to defer current income tax:

Tax Pools *($ Thousands)*	Years Ended December 31 2009	2008
Canadian exploration expense	**$ 14,107**	$ 12,090
Canadian development expense	**6,059**	4,549
Undepreciated capital cost	**8,096**	8,096
Canadian oil and gas property expense	**2,335**	4,803
	30,597	29,538
U.S. tax pools	**1,594**	3,128
Total	**$ 32,191**	$ 32,666

In the United States, the Company was cash taxable in 2006 but due to increased capital spending during 2007 to 2009 did not have any current Federal tax. Diaz may be taxable in 2010 as the remaining tax pools are almost depleted and the Company is not planning to invest in the U.S. during 2010.

Depletion, Depreciation & Accretion *($ Thousands, except per BOE Amounts)*	Three Months Ended December 31 2009	2008	Years Ended December 31 2009	2008
Canada				
Depletion and depreciation	**$ 803**	$ 1,836	**$ 4,350**	$ 6,359
ARO accretion	**65**	68	**280**	263
Total - Canada	**868**	1,904	**4,630**	6,622
per BOE	**23.81**	30.89	**25.22**	28.52
U.S.				
Depletion and depreciation	**662**	981	**2,819**	2,717
ARO accretion	**2**	(3)	**5**	1
Total - U.S.	**664**	978	**2,824**	2,718
per BOE	**55.77**	53.04	**56.46**	29.64
Total - Company	**1,532**	2,882	**7,454**	9,340
per BOE	**$ 31.68**	$ 35.99	**$ 31.91**	$ 28.83

In Q4 2009, the Company's depletion, depreciation and accretion costs have decreased to $31.68 per BOE compared with $35.99 per BOE for Q4 2008. For 2009, the rate increased to $31.91 per BOE from $28.83 BOE for the prior year. Depletion expense is calculated based on the Company's proved reserves.

In Canada, the Company took an impairment write down on its assets of $11.4 million in Q1 2009 which resulted in a 24% reduction in the depletion rate per BOE for the fourth quarter compared with Q4 2008. For 2009, the impairment write down resulted in a 12% reduction in the depletion rate compared with the prior year.

In the U.S., Diaz's substantial probable reserves value (which is used to determine asset impairment) results in a high carrying value of its oil and gas assets when compared with the associated proved reserves.

Exploration and Development Costs

During 2009, Diaz incurred $3.9 million in additions to its oil and gas asset base.

A summary of the capital expenditures and the respective increase or decrease in estimated future capital required to produce the Company's proved and probable reserves are summarized below for the past three years.

Fixed Asset Additions *($ Thousands)*	**Years Ended December 31** **2009**	2008	2007	Three Year Total
Canada				
Land	**$ 811**	$ 590	$ 732	$ 2,133
Geological & geophysical	**446**	611	811	1,868
Drilling	**2,198**	2,072	4,039	8,309
Facilities	**571**	1,400	720	2,691
Cost incurred	**4,026**	4,673	6,302	15,001
Increase (decrease) in future costs required to produce:				
Proved reserves	**1,615**	402	(880)	1,137
Probable reserves	**10,371**	(1,222)	(1,283)	7,866
Increase (decrease) in future costs	**11,986**	(820)	(2,163)	9,003
Total Finding Costs - Canada	**$ 16,012**	$ 3,853	$ 4,139	$ 24,004
U.S.				
Land	**$ 53**	$ 823	$ 439	$ 1,315
Geological & geophysical	**-**	-	(6)	(6)
Drilling	**88**	2,136	3,530	5,754
Facilities	**6**	182	504	692
Cost incurred	**147**	3,141	4,467	7,755
Increase (decrease) in future costs required to produce:				
Proved reserves	**(17)**	(146)	(267)	(430)
Probable reserves	**(564)**	(941)	(536)	(2,041)
Increase (decrease) in future costs	**(581)**	(1,087)	(803)	(2,471)
Total Finding Costs - U.S.	**$ (434)**	$ 2,054	$ 3,664	$ 5,284
Corporate				
Total Finding Costs - Proved	**$ 5,771**	$ 8,070	$ 9,622	$ 23,463
Total Finding Costs - P+P	**$ 15,578**	$ 5,907	$ 7,803	$ 29,288

Finding and development costs are calculated by dividing the total cost in exploration and development for the period, plus the increase or decrease in estimated future costs required to produce the reserves, excluding the cost of reserve acquisitions and dispositions, by the total reserves added during the period, excluding reserves acquired and disposed of. Over the last three years, technical revisions to proved and proved plus probable additional reserves have been larger than new additions to those categories resulting in a negative reserves movement and a corresponding negative finding cost total. Diaz's finding and on-stream cost in 2009 averaged $28.32 per BOE of proved and probable reserves.

BOE's may be misleading, particularly if used in isolation. A BOE conversion factor of 6 Mcf to 1 Bbl is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead.

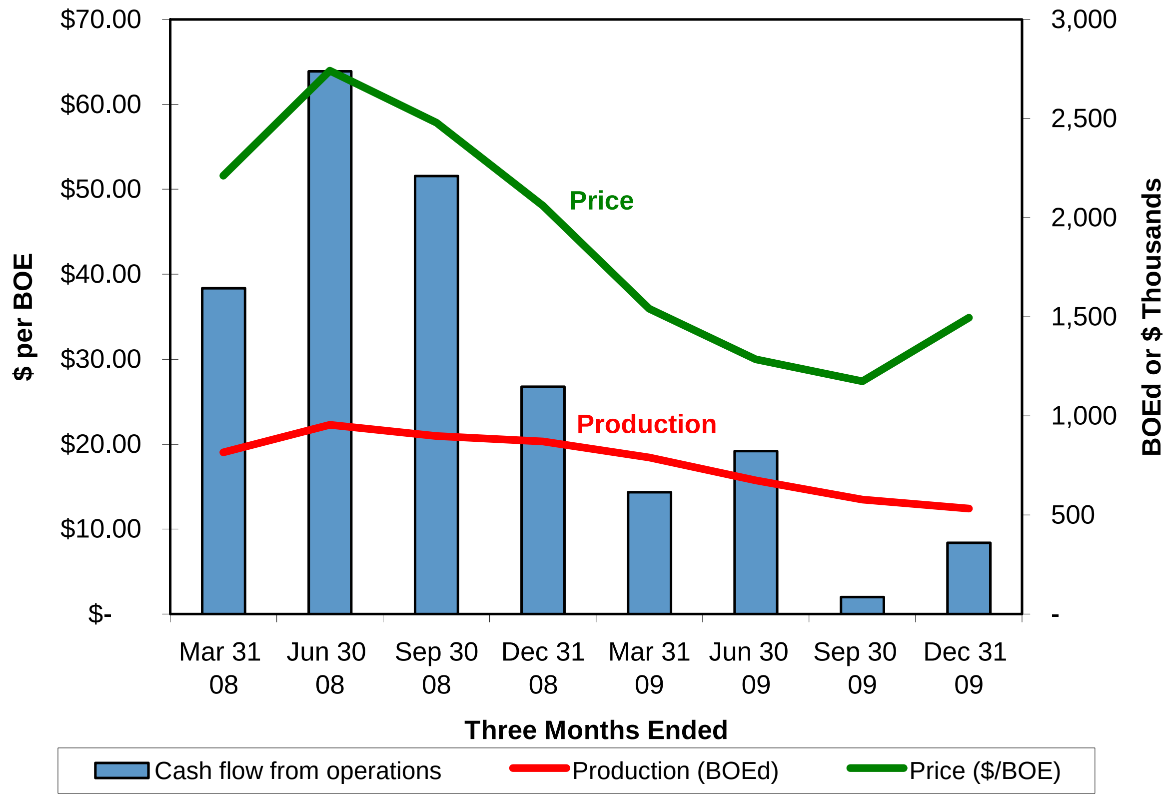
Quarterly Financial Information

($ Thousands, except production and per share amounts)	Three Months Ended							
	2009				2008			
	Dec 31	Sep 30	Jun 30	Mar 31	Dec 31	Sep 30	Jun 30	Mar 31
Production (BOEd)	**532**	578	675	791	871	899	955	816
Price ($/BOE)	**$ 34.87**	$ 27.40	$ 29.98	$ 35.93	$ 48.06	$ 57.84	$ 63.99	$ 51.59
Total revenue	**1,568**	1,225	1,932	2,248	3,389	3,964	4,576	3,170
Cash flow from operations	**359**	86	822	614	1,146	2,209	2,739	1,643
per share (basic and diluted)	**0.00**	0.00	0.01	0.01	0.02	0.03	0.04	0.02
Cash provided by operating activities	**400**	(432)	1,007	1,816	573	3,408	2,090	1,778
per share (basic and diluted)	**0.00**	0.00	0.01	0.03	0.01	0.05	0.04	0.03
Earnings (loss)	**(2,912)**	(1,070)	(619)	(9,754)	(3,561)	(277)	132	(381)
per share (basic and diluted)	**(0.04)**	(0.02)	(0.01)	(0.15)	(0.05)	0.00	0.00	(0.01)
Overhead	**313**	304	(55)	447	567	442	398	387
Net capital additions (dispositions)	**(187)**	(451)	(190)	836	2,074	1,504	1,735	2,479
Property, plant & equip. impairment	**-**	-	-	11,400	2,744	-	-	-
Total assets	**36,657**	37,725	39,826	43,264	56,761	62,927	61,114	61,221
Convertible debentures*	**6,377**	6,304	6,233	6,163	6,094	6,027	5,961	5,896
Net current debt	**5,844**	7,218	7,695	8,657	8,449	7,891	8,481	9,404

* Convertible debentures have a face value of $7.1 million and mature on March 26, 2012. See Note 7, "Convertible Debentures", in the notes to the financial statements for the twelve months ended December 31, 2009.

Diaz's production rate peaked at 955 BOEd in Q2 2008 and has declined during the last six quarters. Q2 2008 also had the highest average price per BOE. Since Q2 2008, prices have dropped by over 50% resulting in a significant reduction in cashflow. As demonstrated by the following graph, the relative change in price per BOE has had a greater impact on cashflow than the change in production rates.

Cashflow, Production and Price - Eight Quarters



Liquidity and Capital Resources

Diaz completed the year ended December 31, 2009, with a net current debt of $5.8 million compared with $8.5 million at the beginning of the year.

In May 2009, Diaz completed the sale of its interest in a non-operated oil property in the Carmangay, Alberta area for $1.0 million. In September, Diaz sold a 43.75% working interest in its Eagle Ford shale property in Texas for $810,000 while retaining a 6.25% working interest with the next gross $4.3 million of work expenditures to be paid by the purchaser. In October, Diaz completed the sale of its Parkman, Saskatchewan, oil property for $2.5 million.

A total of $4.4 million has been received for all property disposals for the year. The proceeds from the sales were used to reduce Diaz's bank debt. Also, in early October, Diaz completed a $920,000 equity private placement, net of expenses. On December 31, 2009, the Company had an $6.35 million secured loan with a Canadian financial institution which was draw to $4.4 million (2008 - $8.1 million).

As of March 31, 2010 Diaz had 86,001,252 common shares issued and outstanding.

Normal Course Issuer Bid ("NCIB")

During the year ended December 31, 2009, Diaz did not repurchase any of its Common Shares (2008 – 60,800).

Diaz is authorized to repurchase up to 760,000 Common Shares through the facilities of the Toronto Stock Exchange pursuant to a normal course issuer bid, which expires on November 30, 2010. Shares repurchased pursuant to the bid are cancelled.

Business Risk

The Company is engaged in the exploration, development, production and acquisition of crude oil and natural gas. Diaz's business is inherently risky and there is no assurance that hydrocarbon reserves will be discovered and economically produced.

Financial risks associated with the petroleum industry include fluctuations in commodity prices, interest rates and currency exchange rates. Operational risks include competition, environmental factors, reservoir performance uncertainties, a complex regulatory environment and safety concerns.

The Company minimizes its business risks by focusing on a select group of properties. This enables Diaz to have more control over the timing, direction and costs related to exploration and development opportunities. The geological focus is on areas in which the prospects are well understood by management. Technological tools are regularly used to reduce risk and increase the probability of success. The Company closely follows all government regulations and has an up-to-date emergency response plan that has been communicated to all field operations by management. Diaz also carries insurance coverage to protect itself against potential losses.

Employing a highly motivated and experienced staff of petroleum and natural gas professionals further minimizes the business risk.

The Company is exposed to commodity price and market risk for its principal products of petroleum and natural gas. Commodity prices are influenced by a wide variety of factors of which most are beyond the control of Diaz. To manage this risk, the Company has entered into a number of fixed price sales contracts in relation to natural gas prices in Canada.

Contractual Obligations and Commitment

In the normal course of business, Diaz is obligated to make future payments. These obligations represent contracts and other commitments that are known and non-cancelable. Diaz has an obligation with respect to an office lease for a minimum payment of $180,000 in 2010.

The Company also has asset retirement obligations with respect to the abandonment and reclamation of wells and facilities owned by the Company. Diaz includes the present value of the estimated liabilities for such costs on its balance sheet. The total estimated undiscounted cost of these liabilities at December 31, 2009, was $4.6 million (2008 – $5.0 million).

Off Balance Sheet Arrangements

Diaz does not currently utilize any off balance sheet arrangements with unconsolidated entities to enhance liquidity and capital resource positions or for any other purpose.

Related Party Transactions

Diaz and Sharon Energy Ltd. ("Sharon") and Tuscany Energy Ltd. ("Tuscany") and Paris Energy Inc. ("Paris") and Humboldt Capital Corporation ("Humboldt") have certain common officers and directors. In addition, at March 5, 2010, Humboldt and its directors and officers owned approximately:

- 37% of Diaz common shares,
- 25% of Paris common shares,
- 27% of Sharon common shares, and
- 44% of Tuscany common shares.

At December 31, 2009, Diaz owed Sharon $84,000 (2008 – $365,000) through the normal course of business.

For the years ended December 31, 2009 and 2008, Diaz recovered the following amounts related to certain overhead services from:

	December 31, 2009	December 31, 2008
Sharon	$671,000	$113,000
Humboldt	$288,000	$288,000
Tuscany	$104,000	Nil
Paris	$14,000	Nil

Diaz paid Sharon an overhead charge of $449,000 (2008 – $238,000) relating to U.S. operations. This relationship was discontinued in 2009.

Application of Critical Accounting Estimates

Diaz's financial statements have been prepared in accordance with generally accepted accounting principles in Canada. The significant accounting policies used by Diaz are disclosed in Note 2 to the Consolidated Financial Statements. Certain accounting policies require that management make appropriate decisions with respect to the formulation of estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses. The following discusses such accounting policies and is included in Management's Discussion and Analysis to aid the reader in assessing the critical accounting policies and practices of the Company and the likelihood of materially different results being reported.

Diaz's management reviews its estimates regularly. The emergence of new information and changed circumstances may result in actual results or changes to estimated amounts that differ materially from current estimates.

The following assessment of significant accounting policies is not meant to be exhaustive. The Company might realize different results from the application of new accounting standards promulgated, from time to time, by various rule-making bodies.

Proved Oil and Gas Reserves

Proved reserves are those reserves that can be estimated with a high degree of certainty to be recoverable. It is likely that the actual remaining quantities recovered will exceed the estimated proved reserves.

The estimated quantities of proved crude oil, natural gas liquids including condensate and natural gas that geological and engineering data demonstrate with reasonable certainty can be recovered in future years from known reservoirs under existing economic and operating conditions, i.e. prices and costs as of the date the estimate is made.

Reserves are considered proved if they can be produced economically as demonstrated by either actual production or conclusive formation tests.

The oil and gas reserve estimates are made using all available geological and reservoir data as well as historical production data. Estimates are reviewed and revised as appropriate. Revisions occur as a result of changes in prices, costs, fiscal regimes, reservoir performance or a change in the Company's plans. The effect of changes in proved oil and gas reserves on the financial results and position of the Company is described under the heading "Full Cost Accounting for Oil and Gas Activities."

Full Cost Accounting for Oil and Gas Activities

Depletion Expense

The Company uses the full cost method of accounting for exploration and development activities. In accordance with this method of accounting, all costs associated with exploration and development are capitalized whether successful or not. The aggregate of net capitalized costs and estimated future development costs less estimated salvage values is amortized using the unit of production method based on estimated proved oil and gas reserves.

An increase in estimated proved oil and gas reserves would result in a corresponding reduction in depletion expense. A decrease in estimated future development costs would result in a corresponding reduction in depletion expense.

Withheld Costs

Certain costs related to unproved properties and major development projects may be excluded from costs subject to depletion until proved reserves have been determined or their value is impaired. These properties are reviewed quarterly and any impairment is transferred to the costs being depleted.

Impairment of Long-Lived Assets

The Company is required to review the carrying value of all property, plant and equipment, including the carrying value of oil and gas assets, for potential impairment. Impairment is indicated if the carrying value of the long-lived asset or oil and gas cost center is not recoverable by the future undiscounted cash flows of proved reserves. If impairment is indicated, the amount by which the carrying value exceeds the estimated fair value of the long-lived asset is charged to earnings. Fair value is the aggregate of cash flows from proved plus probable reserves discounted at 5% per year.

Asset Retirement Obligations

The Company is required to provide for future removal and site restoration costs. The Company must estimate these costs in accordance with existing laws, contracts or other policies. These estimated costs are charged to earnings and the appropriate liability account over the expected service life of the asset.

When the future removal and site restoration costs cannot be reasonably determined, a contingent liability may exist. Contingent liabilities are charged to earnings when management is able to determine the amount and the likelihood of the future obligation.

Legal, Environmental Remediation and Other Contingent Matters

The Company is required to both determine whether a loss is probable based on judgment and interpretation of laws and regulations and determine that the loss can reasonably be estimated. When the loss is determined it is charged to earnings.

The Company's management must continually monitor known and potential contingent matters and make appropriate provisions by charges to earnings when warranted by circumstance.

Income Tax Accounting

The determination of the Company's income and other tax liabilities requires interpretation of complex laws and regulations often involving multiple jurisdictions. All tax filings are subject to audit and potential reassessment after the lapse of considerable time. Accordingly, the actual income tax liability may differ significantly from that estimated and recorded by management.

International Financial Reporting Standards (IFRS) Conversion

During 2009, the CICA Accounting Standards Board ("ACSB") confirmed the changeover to IFRS from Canadian 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 changeover to IFRS represents a change due to new accounting standards. The transition from current Canadian GAAP to IFRS is a significant undertaking that may materially affect the Company's reported financial position and operations.

In July 2009, the International Accounting Standards Board issued Additional Exemptions for First-time Adopters

(Amendments to IFRS-1) which gives the option to companies using the full cost method of accounting to carry forward the amount determined under Canadian GAAP as the deemed cost under IFRS. This exemption will significantly reduce property, plant and equipment adjustments which would have resulted from the retroactive adoption of IFRS.

To date, the CFO, the primary sponsor for the project, has prepared a summary level changeover plan for IFRS conversion that has been presented to the Audit Committee of the Board of Directors. Hallmarks of the changeover plan include, initial definition of the tasks required for conversion, a timeline for the completion of the tasks, an estimate of the effort and duration associated with the conversion, prioritization of tasks, and the assignment of key personnel within the organization.

The conversion plan has been divided into three distinct phases and management is currently in phase two as described below.

Phase One:

Identification of a project work plan that outlines potential conversion issues unique to our industry. This phase assigns ownership responsibility for each of those issues, estimates the time, duration and costs associated with each major deliverable within the plan, and presents an overall project timeline and in- progress reporting from key deliverable owners and assigned employees.

Phase Two:

Identification of the significant accounting policies that relate to each of the major conversion items within the firm. This phase identifies the changes to the accounting policies that will be required with IFRS, and adjusts the plan identified in Phase One accordingly.

Phase Three:

Management of dual reporting under Canadian GAAP and IFRS as required. This phase determines the mapping between the different accounts identified in our chart of accounts and applies this mapping to generate the IFRS reporting. Dual reporting capability is required as of January 1, 2010, so that the Company can prepare comparative information for IFRS reporting which will begin the first quarter of 2011.

Financial Instruments

All financial instruments are required to be measured at fair value on initial recognition of the instrument, except for certain related party transactions. Measurement in subsequent periods depends on whether the financial instrument has been classified as “held-for-trading,” “available-for-sale,” “held-to-maturity,” “loans and receivables” or “other financial liabilities” as defined by the standard.

Cash and cash equivalents are designated as “held-for-trading” and are measured at carrying value, which approximates fair value due to the short-term nature of these instruments. Accounts receivable are designated as “loans and receivables” and are carried at cost. Accounts payable are designated as “other financial liabilities” and are carried at cost. Long-term debt, which includes the convertible debenture, is designated as “other financial liabilities” and carried at amortized cost using the effective interest method. The financing costs associated with the Company’s $7.085 million private placement of unsecured convertible debentures on March 26, 2007, are included in the amortized cost of the debt. These costs are charged to interest expense using the effective interest rate method over the term of the debt, which matures on March 26, 2012.

The Company’s financial instruments that are included in the balance sheet are comprised of cash, accounts receivable, current liabilities and the convertible debentures.

Fair values of financial assets and liabilities

The fair values of financial instruments that are included in the balance sheet approximate their carrying amount due to the short-term maturity of those instruments.

Credit risk

Credit risk is the risk that the counterparty to a financial asset will default, resulting in the Company incurring a financial loss. The Company is exposed to credit risk on its accounts receivable and GST receivable, to a maximum of the carrying value of the aforementioned items at the end of the period. A substantial portion of the Company’s accounts receivable are with customers in the oil and gas industry and are subject to normal industry credit risks. The maximum exposure to credit risk is approximately $695,000 which represents accounts receivable balances in excess of 90 days. Management has reviewed the items comprising the accounts receivable balance and determined that all accounts are collectible; accordingly there has been no allowance for doubtful accounts recorded.

Interest rate risk

The Company is exposed to risks from interest rate fluctuation on its bank loan which is based on Prime rates. Interest rate risk is specific to the interest expense charged to income on the Company's bank debt. The Company believes a 25% volatility is a reasonable measure when assessing the potential impact of a change in interest rate. Variations in interest rates on the Company's bank debt could have resulted in gains (losses) impacting net earnings as at December 31, 2009, as follows:

($ Thousands)	Favourable 25% Change	Unfavourable 25% Change
Interest expense	$ (240)	$ 240

Liquidity risk

The Company is exposed to liquidity risk from the possibility that it will encounter difficulty meeting its financial obligations. The Company manages this risk by forecasting cash flows in an effort to match operating cash flow to future expenditures and to arrange financing, if necessary. It may take many years and substantial cash expenditures to pursue exploration and development activities on all of the Company's existing undeveloped properties. Accordingly, the Company may need to raise additional funds from outside sources in order to explore and develop its properties. There is no assurance that adequate funds from debt and equity markets will be available to the Company in a timely manner. The timing of cash outflows relating to financial liabilities are outlined in the table below:

($ Thousands)	< 1 year	2-3 years	> 3 years
Accounts payable and accrued liabilities	4,508	-	-
Bank loan	4,398	-	-
Convertible debentures plus interest	620	7,875	-

At December 31, 2009 the Company has met all the obligations associated with its financial liabilities. The majority of the Company's accounts payable are current. The bank loan is a demand loan and is classified as a current liability of less than one year. Convertible debentures are payable on March 26, 2012.

Foreign currency exchange risk

The Company is exposed to fluctuations in foreign currency exchange rates as the Company has a U.S. subsidiary with a functional currency of United States dollars while the functional currency of the Company is Canadian dollars. As a result, fluctuations in the United States dollar against the Canadian dollar could result in unanticipated fluctuations in the Company's financial results which are denominated in Canadian dollars.

The Company's exposure to foreign currency exchange risk at December 31, 2009, can be summarized as follows:

	Balance Sheet	Canada	USA
($ Thousands)	**Total**	Cdn $ Equivalent	
Cash and cash equivalents	**104**	-	104
Accounts receivable	**2,400**	2,300	100
Accounts payable	**(4,508)**	(4,276)	(232)
Total	**(2,004)**	(1,976)	(28)

Commodity price risk

Inherent to the Company's business of producing petroleum and natural gas is the commodity price risk where fluctuations in the market price of petroleum and natural gas could significantly impact the Company's ability to generate cash flow from operating activities. The Company believes a 10% volatility is a reasonable measure when assessing the potential impact of commodity price changes on natural gas and oil prices. Variations in commodity prices could have resulted in gains (losses) impacting net earnings as at December 31, 2009, as follows:

($ Thousands)	Favourable 10% Change		Unfavourable 10% Change	
Natural gas price	$	562	$	(562)
Crude oil price	$	191	$	(191)

Internal Controls over Financial Reporting (ICFR)

The Chief Executive Officer and Chief Financial Officer of Diaz (the "Certifying Officers") have designed internal controls over financial reporting or caused them to be designed under their supervision in order to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with Canadian GAAP. The Certifying Officers have assessed the design and effectiveness of the Company's ICFR at December 31, 2009.

As at December 31, 2009, there were no changes to the controls over financial reporting that occurred during the issuer's most recent interim period that has materially affected, or is reasonably likely to materially affect, the issuer's internal control over financial reporting.

The Certifying Officers have evaluated the internal controls over financial reporting and have determined that the ICFR is effective.

Disclosure Controls and Procedures (DC&P)

The Chief Executive Officer and Chief Financial Officer of Diaz (the "Certifying Officers") have designed disclosure controls and procedures or caused them to be designed under our supervision, to provide reasonable assurance that:

(i) material information relating to the issuer is made known to the Certifying Officers by others, particularly during the period in which the annual filings are being prepared; and

(ii) information required to be disclosed by the issuer in its annual filings, interim filings or other reports filed or submitted by it under securities legislation is recorded, processed, summarized and reported within the time periods specified in securities legislation.

The Certifying Officers have evaluated the disclosure controls and procedures and have determined that the DC&P are effective as at December 31, 2009.

Outlook

The Company anticipates steady growth in the North American economy during 2010.

As a result oil prices should continue to firm as industrial activity recovers. Due to current high natural gas storage levels and significant volumes of gas being developed on North American shale gas projects there is still considerable uncertainty as to when natural gas prices will recover to satisfactory levels. To mitigate the uncertainty in natural gas prices, Diaz has put in place fixed gas price contracts for approximately half of the Company's anticipated 2010 gas production, at prices in excess of $5.75 per Mcf. Diaz has also closed an equity financing raising approximately $1,263,500 net of commissions to fund its ongoing Lloydminster heavy oil development drilling program.

Due to this potential ongoing weakness in the gas sector Diaz will continue to direct its efforts towards heavy oil development during 2010. The Company will continue to focus on its Lloydminster heavy oil development program and if results are successful Diaz would exit 2010 with almost half of its production derived from oil sales.

Management's Report

The accompanying financial statements of Diaz Resources Ltd. have been prepared by management in accordance with generally accepted and consistently applied accounting principles. The Company's accounting procedures and related systems of internal controls are designed to provide reasonable assurance that its assets are safeguarded and its financial records are reliable. In recognizing that the Company is responsible for both the integrity and objectivity of the financial statements, management is satisfied that these financial statements have been prepared accordingly and within reasonable limits of materiality. Further, management is satisfied that the financial information throughout the balance of this annual report is consistent with the information presented in the financial statements.

PricewaterhouseCoopers LLP have been appointed by the shareholders of Diaz Resources Ltd. and serve as the Company's independent auditors. The Audit Committee has reviewed these statements with management and the auditors, and has reported to the Board of Directors. The Board has approved the financial statements of Diaz Resources Ltd., which are contained in this annual report.

Robert W. Lamond
President and Chairman of the Board
March 30, 2010

Brad R. Perry
Chief Financial Officer

Auditors' Report

To the Shareholders of Diaz Resources Ltd.

We have audited the consolidated balance sheets of Diaz Resources Ltd. as at December 31, 2009 and 2008 and the consolidated statements of operations and retained earnings (deficit), comprehensive loss and and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

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

PricewaterhouseCoopers LLP
Chartered Accountants
Calgary, Alberta
March 30, 2010

Consolidated Financial Statements

Consolidated Balance Sheet

As at *($ Thousands)*		**December 31** **2009**		**December 31** **2008**
ASSETS				
Current Assets				
Cash	**$**	**104**	$	544
Accounts receivable		**2,400**		2,750
Income tax receivable		**329**		359
Prepaid expense		**229**		378
		3,062		4,031
Property, plant and equipment (Note 4)		**103,907**		106,425
Accumulated depletion and depreciation		**(70,312)**		(53,695)
		33,595		52,730
Total Assets	**$**	**36,657**	$	56,761
LIABILITIES				
Current Liabilities				
Accounts payable and accrued liabilities	**$**	**4,508**	$	4,337
Bank debt (Note 3)		**4,398**		8,143
		8,906		12,480
Other Liabilities				
Convertible debentures (Note 7)		**6,377**		6,094
Future income tax liability (Note 8)		**1,942**		5,379
Asset retirement obligation (Note 9)		**3,381**		3,323
Total Other Liabilities		**11,700**		14,796
		20,606		27,276
SHAREHOLDERS' EQUITY				
Share capital (Note 5)		**20,614**		19,702
Other equity (Note 7)		**847**		848
Contributed surplus (note 5)		**1,759**		1,442
Accumulated other comprehensive income (loss)		**(307)**		-
Retained earnings (deficit)		**(6,862)**		7,493
		16,051		29,485
Total Liabilities and Shareholders' Equity	**$**	**36,657**	$	56,761

See Note 10, Commitments and Note 12, Subsequent Events.

Approved by the Board:

(Signed) *"R.W. Lamond"* Director   (Signed) *"C.A. Teare"* Director

Consolidated Statement of Operations & Retained Earnings (Deficit)

($ Thousands, except per share amounts)				Years Ended December 31
		2009		**2008**
Revenue				
Production	**$**	**7,527**	$	18,024
Royalties		**(730)**		(3,325)
Interest and other income		**176**		400
		6,973		15,099
Expenses				
Operating and transportation		**3,096**		4,367
Overhead		**1,009**		1,794
Stock based compensation		**169**		129
Interest expense		**1,240**		1,431
Foreign exchange loss (gain)		**3**		303
Depletion, depreciation and accretion		**7,454**		9,340
Property, plant & equipment impairment (Note 4)		**11,408**		2,744
		24,379		20,108
Earnings (loss) before income tax		**(17,406)**		(5,009)
Income tax				
Current tax expense (Note 8)		**30**		32
Future tax recovery (Note 8)		**(3,081)**		(954)
Total income tax		**(3,051)**		(922)
Net loss		**(14,355)**		(4,087)
Retained earnings, beginning of period		**7,493**		11,580
Retained earnings (deficit), end of period	**$**	**(6,862)**	$	7,493
Loss per share, basic and diluted	**$**	**(0.21)**	**$**	**(0.06)**

Consolidated Statements of Comprehensive Loss and Accumulated Other Comprehensive Loss

($ Thousands, except per share amounts)		Years Ended December 31 2009		2008
Net loss	$	(14,355)	$	(4,087)
Other comprehensive income (loss)				
Unrealized loss on translation of consolidated financial statements into reporting currency		(307)		-
Comprehensive loss	$	(14,662)	$	(4,087)
Accumulated other comprehensive income (loss)				
Beginning of period	$	-	$	-
Other comprehensive loss		(307)		-
Accumulated other comprehensive loss	$	(307)	$	-

Consolidated Statement of Cash Flows

($ Thousands)		Years Ended December 31 2009		2008
Cash provided by (used for):				
Operating Activities				
Loss for the period	**$**	**(14,355)**	$	(4,087)
Non-cash items:				
Interest - amortization of debenture issue costs		**283**		262
Depreciation, depletion and accretion		**7,454**		9,340
Property, plant & equipment impairment		**11,408**		2,744
Stock based compensation		**169**		129
Future tax recovery (Note 8)		**(3,081)**		(954)
Foreign exchange gain		**3**		303
		1,881		7,737
Abandonments		**(120)**		(115)
Change in non-cash working capital		**1,017**		139
		2,778		7,761
Investing Activities				
Property, plant & equipment - additions		**(4,415)**		(7,778)
Property, plant & equipment - dispositions		**4,407**		74
Change in non-cash working capital		**(316)**		(144)
		(324)		(7,848)
Financing Activities				
Increase (decrease) in bank debt		**(3,745)**		91
Common Shares				
Issued for cash		**940**		-
Share issue costs		**(28)**		(6)
Repurchased for cancellation		**-**		(12)
		(2,833)		73
Increase (decrease) in cash		**(379)**		**(14)**
Net effect of foreign exchange translations on cash flows		**(61)**		-
Cash, beginning of period		**544**		558
Cash, end of period	**$**	**104**	$	544
Supplementary information regarding cash payments:				
Interest paid during the period	**$**	**958**	$	1,169
Taxes paid during the period	**$**	**30**	$	59

Notes to the Consolidated Financial Statements

For the year ended December 31, 2009

1. ***Accounting Policies***

The consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries, Diaz Resources, Inc. and Orbit Oil & Gas Inc.

The Corporation's principal business activity is the exploration, development and operation of oil and natural gas properties in Canada and in the United States. These financial statements have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP") on a going concern basis, which contemplates the realization of assets and the payment of liabilities in the ordinary course of business.

Management has made the necessary estimates and assumptions regarding certain types of assets, liabilities, revenues and expenses in the preparation of the financial statements. Accordingly, actual results may differ from estimated amounts but management does not believe such differences will materially affect Diaz's financial position or results of operations.

Property, Plant and Equipment

The Company follows the full cost method of accounting for petroleum and natural gas operations. Under this method, all costs of exploration for and development of petroleum and natural gas reserves are capitalized by cost centre. A separate cost centre is established for each country in which the Company operates, presently Canada and the United States. Costs include lease acquisition costs, geological and geophysical expense, carrying charges on non-producing properties, costs of drilling both productive and non-productive wells and overhead charges directly related to exploration activities.

Proceeds on disposal of properties are normally applied as a reduction of the capitalized costs without recognition of a gain or loss, except where such a disposal would alter the depletion and depreciation rate by 20% or more.

Depletion and depreciation of capitalized costs are provided by using the unit of production method based on the Company's total estimated gross proved reserves, as determined by independent engineers. Natural gas reserves and production are converted to equivalent barrels of oil based on the relevant energy content. In determining the depletion base, the Company includes future costs to be incurred in developing proved reserves and excludes the costs of unproved land.

Depreciation is provided on furniture and fixtures at annual rates of 20%, on a declining balance basis.

An impairment loss is recognized in net earnings when the carrying amount of a cost centre is not recoverable and the carrying amount of the cost centre exceeds its fair value. The carrying amount of the cost centre is not recoverable if the carrying amount exceeds the sum of the undiscounted cash flows from proved reserves. If the sum of the cash flows is less than carrying amount, the impairment loss is limited to the amount by which the carrying amount exceeds the sum of:

- the fair value of proved and probable reserves; and
- the costs of unproved properties that have been subject to a separate impairment test and contain no probable reserves.

In determining the depletion and depreciation provisions for crude oil and natural gas assets, the Company includes any excess of the net book value of those crude oil and natural gas assets over the fair value.

Asset Retirement Obligation

The Company recognizes the fair value of an Asset Retirement Obligation ("ARO") as a liability in the period in which it is incurred if a reasonable estimate of fair value can be made. The present value of the estimated ARO is capitalized as part of the net capitalized asset base and the depletion of the capitalized asset retirement cost is determined on a basis consistent with depletion of the Company's other assets. With time, accretion will increase the carrying amount of the obligation. Accretion is expensed.

Cash and Cash Equivalents

Cash includes cash and cash-like short-term investments that can be liquidated into cash on less than 90-days notice.

Joint Ventures

A significant portion of the Company's activities are conducted jointly with others. These financial statements reflect the Company's proportionate interest in such activities.

Share Based Compensation Plan

The Company has a stock based compensation plan, which is described in Note 5. The Company has adopted the fair value method for accounting for stock based compensation whereby the fair value of the option granted is extimated on the date of the grant using the Black-Scholes option pricing model. Using the fair value method, compensation costs of stock based compensation are estimated and charged to earnings over the vesting period of the options.

Foreign Currency Translation

Foreign currency balances, including those of self sustaining foreign subsidiaries, are expressed in Canadian dollars on the following basis:

- Monetary assets and liabilities – at the year end rate of exchange;
- Other assets and liabilities – at the year end rate of exchange; and
- Revenues and expenses – at average rates of exchange for the period.

Flow-Through Shares

Share capital is reduced by the future tax effect of renouncing income tax cost to the purchaser of flow-through shares when the tax pools are renounced. The tax effect is calculated using the expected rate of tax.

Revenue Recognition

Revenue associated with the sale of crude oil, natural gas and natural gas liquids owned by the Company is recognized when title passes from the Company to its customers and collectability is reasonably assured.

Income Tax

Income taxes are recorded using the liability method of accounting. Future income tax assets and liabilities are recognized for temporary differences between the income tax and accounting basis of assets and liabilities and measured using the substantively enacted tax rates expected to be in effect when the timing differences are estimated to reverse. Changes in income tax rates that are substantively enacted are reflected in the accumulated future income tax balances in the period the change occurs.

Use of Accounting Estimates

The amounts recorded for depletion, depreciation and amortization of petroleum and natural gas properties and equipment and the provision for asset retirement obligation are based on estimates. The ceiling test is based on estimates of proved reserves, production rates, oil and gas prices, future costs and other relevant assumptions. The Black-Scholes option pricing model is used to estimate stock option values based on estimates of the current risk free interest rate, expected life of the options and expected volatility of the underlying common share price. By their nature, these estimates are subject to measurement uncertainty and the effect on the financial statements of changes in such estimates in future periods could be significant.

The determination of the Company's income and other tax liabilities requires interpretation of complex laws and regulations often involving multiple jurisdictions. All tax filings are subject to audit and potential reassessment after the lapse of considerable time. Accordingly, the actual income tax liability may differ significantly from that estimated and recorded by management.

Financial Instruments

All financial instruments are required to be measured at fair value on initial recognition of the instrument, except for certain related party transactions. Measurement in subsequent periods depends on whether the financial instrument has been classified as "held-for-trading," "available-for-sale," "held-to-maturity," "loans and receivables" or "other financial liabilities" as defined by the standard.

Earnings per share

The treasury stock method is used to determine the dilutive effect of stock options, warrants and other dilutive instruments. Under the treasury stock method, only "in the money" dilutive instruments impact the dilution calculations.

Basic earnings (loss) per share are calculated by dividing the weighted average number of the aggregate outstanding shares during the period into net earnings (loss) attributable to the shareholders.

Diluted earnings per share are calculated by dividing the diluted weighted average number of aggregate outstanding shares during the period in the net earnings for the period. Diluted loss per share is calculated by dividing the basic weighted average aggregate outstanding shares into the loss for the period as using the diluted weighted average shares would be anti-dilutive.

2. Change in Accounting Policies

Foreign Currency Translation

During the first quarter of 2009, the Company reclassified its U.S. subsidiaries from integrated to self-sustaining foreign operations because the subsidiaries have demonstrated that they are no longer wholly dependent on their Canadian parent for capital requirements. Accordingly, the subsidiaries now use the US$ as their functional currency. The Company has prospectively adopted the current rate method of foreign currency translation in accordance with section 1651 of the CICA handbook. Under this method, revenues and expenses are translated using average exchange rates for the applicable period, assets and liabilities are translated using the exchange rates in effect on the balance sheet dates, and shareholders' equity is translated using historical rates in effect at the date of each transaction. Resulting exchange differences are reported as a separate component of other comprehensive income.

Financial Instrument Disclosures

Effective December 31, 2009, the Corporation adopted disclosure requirements that the CICA added to Handbook Section 3862 "Financial Instruments – Disclosures." The additional requirements augmented disclosure requirements with respect to fair values and liquidity risk associated with financial instruments. Fair values are now required to be determined following a three level hierarchy:

Level 1: quoted prices in active markets for identical assets or liabilities;

Level 2: inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly; and

Level 3: inputs for the asset or liability that are not based on observable market data.

This amendment did not impact the Company as the Company does not have any financial instruments in which it uses fair values, other than cash and cash equivalents, which is considered to be level 2.

Business Combinations

In January 2009, the CICA issued Handbook Sections 1582 – Business Combinations, 1601-Consolidated Financial Statements, and 1602 – Non Controlling Interests. Section 1582 replaces Section 1581 – Business Combinations and establishes standards for the accounting for business combinations that is equivalent to the business combination accounting standard under IFRS. Sections 1601 and 1602 replace 1600 – Consolidated Financial Statements. Section 1601 provides revised guidance on the preparation of consolidated financial statements and Section 1602 addresses accounting for non controlling interests in consolidated financial statements subsequent to a business combination. These standards are effective April 1, 2011. Early adoption of the Section is permitted. If the Company chooses to early adopt any one of these Sections, the other two sections must also be adopted at the same time. The Company did not adopt this standard early.

Emerging Issues Committee ("EIC") EIC 173

The Emerging Issues Committee ("EIC") issued EIC 173 – Credit risk and the fair value of financial assets and financial liabilities on January 20, 2009. This abstract provides further guidance on the determination of the fair value of financial assets and financial liabilities under Section 3855. EIC 173 concluded that when determining the fair value of financial assets and financial liabilities, the entity should consider its own credit risk as well as the credit risk of the counterparty. This abstract should be applied retrospectively, without restatement of prior periods, to all financial assets and liabilities measured at fair value in interim and annual financial statements for the periods ending on or after January 20, 2009. Adoption of this abstract did not have a material impact.

3. ***Bank Debt***

All credit facilities that are revolving in nature must be disclosed as liabilities. Diaz utilizes a secured revolving production loan that is payable on demand and is subject to an annual review and, therefore, is considered "current" for disclosure purposes and has been disclosed under current liabilities as bank debt.

At December 31, 2009, the Company had an $6.35 million revolving production loan with a Canadian financial institution. At December 31, 2009, $4,398,000 of the loan was outstanding (December 31, 2008 - $8,143,000). The next review of the loan is scheduled to be completed prior to April 30, 2010. The loan continues is in two distinct parts as follows:

Part 1, revolving:	$5.60 million,	prime plus 2.00%;
Part 2, revolving:	$0.75 million,	prime plus 3.50%.

4. ***Property, Plant and Equipment***

($ Thousands)	**Dec. 31 2009**	Additions	Adjustment Items	Disposals	F/X Effect on prior year balance	Dec. 31 2008
Land	**$ 12,302**	$ 870	$ -	$ (3,657)	$ (286)	$ 15,375
Drilling	**56,494**	1,789	149	-	(1,680)	56,236
Facilities	**22,805**	558	-	(750)	(382)	23,379
Other	**11,146**	1,155	(120)	-	(205)	10,316
Total	**102,747**	4,372	29	(4,407)	(2,553)	105,306
Accumulated Depletion	**(69,474)**	(19,255)	-	-	2,718	(52,937)
	33,273	(14,883)	29	(4,407)	165	52,369
Furniture & Fixtures	**1,160**	43	-	-	(2)	1,119
Accumulated Depreciation	**(838)**	(80)	-	-	-	(758)
	322	(37)	-	-	(2)	361
Property, Plant and Equipment	**$ 33,595**	$ (14,920)	$ 29	$ (4,407)	$ 163	$ 52,730

In the U.S., the Company sold working interests in various properties including a significant interest in the Eagle Ford shale prospect area for $1.0 million. In Canada, the Company sold two producing oil properties, Carmangay and Parkman, for $3.4 million. Proceeds on the disposal of all properties were applied as a reduction of the capitalized costs without recognition of a gain or loss, as none of the disposals altered the depletion and depreciation rate by 20% or more.

At December 31, 2009, unproved property costs of $580,000 were excluded from the depletable cost base (2008 - $1,311,000). Unproved property costs are tested for impairment separately from those costs subject to depletion whereby the carrying value of the property must be less than or equal to the current market value.

For 2009, administrative expenses and stock options of $1,276,000 related to exploration and development activities were capitalized as part of property, plant and equipment (2008 - $920,000).

Adjustment items are shown in the table above to allow one to reconcile property, plant and equipment additions and disposals to investing activities in the Consolidated Statement of Cashflows. Capitalized stock option expense of $149,000 is a non-cash item and an abandonment charge of $120,000 is reversed as it is shown separately in the Statement.

For the calculation of depletion expense, estimated future costs to develop the proved reserves were added to property, plant and equipment. At December 31, 2009, future costs were $6,536,000 (2008 - $6,551,000).

The Company based its estimates on the future price quotes for U.S. gas at Nymex, adjusted for heat content and basis differential and for Canadian gas at the AECO price to the end of 2012 and held constant thereafter. Oil prices used were WTI for U.S. properties and Edmonton Light for Canadian properties, both adjusted for quality differentials.

Price Estimates Used for Ceiling Test				
	Nymex ($U.S./Mcf)	AECO ($Cdn/Mcf)	Edmonton Light ($Cdn/Bbl)	WTI ($U.S./Bbl)
2010	6.11	5.71	84.28	82.30
2011	6.69	6.22	88.28	86.10
2012	6.89	6.37	90.28	88.00
2013	6.89	6.37	90.28	88.00
2014	6.69	6.37	90.28	88.00

Prices are held constant therafter

The Company reviewed the carrying value of the Canadian and U.S. oil and gas properties for potential impairment. Impairment is indicated if the carrying value of the long-lived asset or oil and gas cost center is not recoverable from the future undiscounted cash flows. If impairment is indicated, the amount by which the carrying value exceeds the estimated fair value of the long-lived asset is charged to earnings. An impairment of $11.4 million was required in Q1 2009 (Q4 2008 - $2.7 million). No further impairment was required at year end.

5. Share Capital

Authorized

Unlimited number of Common Shares, no stated par value.

Voting rights

Common shares carry voting rights of one vote per share.

Issued

	Number of Shares		Amount (thousands)
Common Shares			
Balance, December 31, 2007	67,238,552	$	19,986
Tax effect of flow-through shares	-		(266)
Share issue costs (net of tax)			(6)
Repurchased for cancellation	(60,800)		(12)
Balance, December 31, 2008	67,177,752	$	19,702
Share issue costs (net of tax)			(28)
Issued for cash	9,399,000		940
Balance, December 31, 2009	76,576,752	$	20,614

		Amount (thousands)
Contributed Surplus		
Balance, December 31, 2007	$	1,313
Option compensation for the period		129
Balance, December 31, 2008	$	1,442
Option compensation for the period		228
Option compensation relating to prior period		89
Balance, December 31, 2009	$	1,759

On October 16, 2009, the Company raised $939,900 by way of a non-brokered private placement of 9,399,000 common shares at $0.10 per share.

Normal Course Issuer Bid ("NCIB")

During the year ended December 31, 2009, Diaz did not repurchase any of its Common Shares (2008 – 60,800).

Diaz is authorized to repurchase up to 760,000 Common Shares through the facilities of the Toronto Stock Exchange pursuant to a normal course issuer bid, which expires on November 30, 2010. Shares repurchased pursuant to the bid are cancelled.

Earnings per share

The treasury stock method is used to determine the dilutive effect of stock options, warrants and other dilutive instruments. Under the treasury stock method, only "in the money" dilutive instruments impact the dilution calculations. The diluted weighted average shares outstanding for December 31, 2009, does not include the conversion of the Convertible Debentures into 7,872,222 common shares as the conversion would be anti-dilutive. The anti-dilutive effect is caused because the increase in after tax earnings from the reduced interest payments on the Debentures is higher on a per share basis than the basic earnings (loss) per share.

Basic earnings (loss) per share are calculated by dividing the weighted average number of the aggregate outstanding shares during the period into net earnings (loss) attributable to the shareholders.

Diluted earnings per share are calculated by dividing the diluted weighted average number of aggregate outstanding shares during the period into the net earnings for the period. Diluted loss per share is calculated by dividing the basic weighted average aggregate outstanding shares into the loss for the period as using the diluted weighted average shares would be anti-dilutive. Stock options are not shown to be dilutive in the 2009 three and twelve month periods as they were all out-of-the-money compared with the average stock prices during those periods.

Shares Outstanding	Three Months Ended December 31		Years Ended December 31	
	2009	2008	2009	2008
Weighted average shares outstanding	75,044,306	67,183,205	69,160,555	67,212,967
Dilutive effect of stock options	-	-	-	-
Diluted weighted average shares outstanding	75,044,306	67,183,205	69,160,555	67,212,967

Stock Option Plan

The Corporation's Stock Option Plan permits the granting of options to purchase Common Shares to officers, directors, employees and other persons who provide ongoing management or consulting services to the Corporation and its subsidiaries. The Stock Option Plan currently limits the number of Common Shares that may be issued on exercise of Options to 10% of the number of outstanding Common Shares from time to time. Any increase in the issued and outstanding Common Shares will result in an increase in the available number of Common Shares issuable under the Stock Option Plan. Additionally, any exercise of options will make new grants available under the Stock Option Plan.

Options granted pursuant to the Stock Option Plan have a term not to exceed five years and vest as follows:

1/3 on grant date
1/3 on first anniversary of grant date
1/3 on second anniversary of grant date

As at December 31, 2009, there are a total of 7,635,000 options granted and outstanding under the stock option plan with a weighted average exercise price of $0.3260 per share. A total of 4,825,802 options with a weighted average exercise price of $0.3958 are exercisable at December 31, 2009.

Fixed Options	Shares	2009 Weighted Average Exercise Price	Shares	2008 Weighted Average Exercise Price
Outstanding, beginning of period	4,857,500	$ 0.4146	3,575,000	$ 0.6450
Granted	3,077,500	$ 0.1900	2,497,500	$ 0.2500
Exercised	-	$ -	-	$ -
Expired	-	$ -	(1,075,000)	$ 0.3100
Cancelled	(300,000)	$ 0.3650	(140,000)	$ 0.7079
Outstanding, end of period	7,635,000	$ 0.3260	4,857,500	$ 0.4146
Options exercisable, end of period	4,825,802	$ 0.3958	3,175,817	$ 0.5017

The following summarizes information about fixed stock options outstanding at December 31, 2009:

Exercise Price	Outstanding December 31, 2009	Weighted Average Remaining Life (years)	Exercisable December 31, 2009
$0.00 - $0.24	3,077,500	4.9589	1,025,812
$0.25 - $0.49	2,982,500	2.9433	2,224,990
$0.50 - $0.74	1,375,000	0.2943	1,375,000
$0.75 - $0.99	200,000	1.6192	200,000
	7,635,000	3.2447	4,825,802

The Company accounts for its stock based compensation plan using the fair value method whereby compensation costs have been recognized in the financial statements for share options granted to employees and directors. The impact on compensation costs of using the fair value method increased compensation costs for 2009 by $169,000 (2008 - $129,000).

The fair value of each option granted is estimated on the date of grant using the Black-Scholes option-pricing model with assumptions as follows:

	Risk Free Interest Rate (%)	**Expected Life (Years)**	**Expected Volatility**	**Weighted Average Future Value Per Option**
2006	4.24	4.0	0.43	0.5212
2007	4.28	4.0	0.61	0.2027
2008	3.40	4.5	0.53	0.1182
2009	2.12	4.5	0.70	0.1072

On December 15, 2009, the Company issued 3,077,500 new stock options to officers, directors, employees and consultants, with an exercise price of $0.19 per share.

6. Capital Disclosures

Diaz uses the term cash flow from operations, annualized cashflow and net debt in its analysis below. Cash flow from operations should not be considered an alternative to, or more meaningful as an indicator of the Company's performance than, cash flow from operating activities, as determined in accordance with accounting principles generally accepted in Canada. Diaz's determination of cash flow from operations may not be particularly comparable to that reported by other companies especially those in other industries. Management uses cash flow from operations as a measure of operating performance as the measure is not exposed to non-cash working capital movements, which for a small company, could be material and misleading. The reconciliation of cash flow from operating activities and cash flow from operations is as follows:

($ Thousands, Three Months Unaudited)	**Three Months Ended December 31**		**Year Ended December 31**	
	2009	**2008**	**2009**	**2008**
Cash provided by (used for) Operating Activities:	**$ 400**	$ 573	**$ 2,778**	$ 7,761
Adjusted for:				
Abandonments	**87**	$ (128)	**$ 120**	$ 115
Change in non-cash working capital	**(128)**	701	**(1,017)**	(139)
Cash flow from operations	**$ 359**	$ 1,146	**$ 1,881**	$ 7,737

The Company also uses annualized cash flow from operations which equals four times the quarterly cash flow from operations. In addition, the Company presents "Net current debt", which is calculated as the aggregate of current assets and current liabilities.

Diaz's objectives when managing capital are:

- To safeguard the Company's ability to continue as a going concern, so that it can continue to provide returns for shareholders and benefits for other stakeholders, and

- To provide an adequate return to shareholders by investing in oil and gas activities commensurate with the level of risk management deems acceptable.

Diaz sets the level of capital in proportion to its risk of achieving sufficient annualized operating cashflows to maintain its net current debt repayability ratio to less than twenty-four months repayability. The Company makes adjustments to capital in light of changes in economic conditions and risk characteristics of the underlying assets. In order to maintain or adjust the capital structure Diaz may issue new shares, sell assets or increase its debt.

The ratio of net current debt to annualized cashflow from operations is the primary ratio of capital that Diaz uses. Net current debt repayability is a calculation to determine the number of months required to repay net current debt from current cashflow from operations. The ratio is calculated as follows:

Net Current Debt Repayability *(Thousands, except for months)*	**2009**	**Years Ended December 31** 2008
Current liabilities	**$ 8,906**	$ 12,480
Less Current assets	**3,062**	$ 4,031
Net current debt	**5,844**	8,449
Convertible Debentures	**6,377**	6,094
Net debt	**12,221**	14,543
Annualized Cashflow from Operations	**1,436**	8,788
Months estimated to repay net current debt	**48.84**	11.54
Months estimated to repay net debt	**102.13**	19.86

The increase in net current debt repayability for the year ended December 31, 2009, compared with 2008 resulted from the sharp decline in realized oil and natural gas prices during the period. The resulting 2009 ratio is unacceptably high and management has taken and is taking steps to reduce the debt side of the equation.

7. *Convertible Debentures*

In March 2007, the Company issued unsecured subordinated convertible debentures for gross proceeds of $7,085,000. The debentures are compound financial instruments and as such have been recorded as a liability and as equity. The residual valuation method was used to determine the equity portion of the debentures. Under this approach, the liability component was valued first, and the difference between the proceeds of the debentures and the fair value of the liability was assigned to the equity component. The present value of the liability was calculated using a discount rate of 12% which approximated the interest rate that would have been applicable to non-convertible debt of the Company at the time the debentures were issued.

($ Thousands)	**2009**	**Years Ended December 31** 2008
Liability component of debenture before adjustments	**6,094**	5,832
Adjustments - expensed to interest		
Accretion of liability	**166**	147
Issue costs	**117**	115
Liability component of debenture	**$ 6,377**	$ 6,094

As of December 31, 2009, debenture issue costs of $590,000 were charged against the liability component of the debenture. These costs will be charged to interest expense over the five year life of the debenture using the effective interest rate method. Also, the liability component of the debenture will be accreted to the face value of the debenture over the five year term with a resulting charge to interest expense.

The debentures will mature on March 26, 2012, unless earlier redeemed or converted. The debentures earn interest at 8.75% per year, paid semi-annually. The principal amount of each debenture is convertible into common shares of Diaz at the option of the holder at any time prior to maturity at a conversion price of $0.90 per share. The Corporation may, at its option, elect to satisfy its obligation to pay all or any portion of the principal amount by issuing and delivering to holders on the maturity date that number of Common Shares obtained by dividing the $0.90 per share redemption price by 95% of the current trading price of a Common Share.

8. Income Taxes

The provision for income taxes in the consolidated statement of operations & retained earnings (deficit) varies from the amount that would be computed by applying the expected tax rate to earnings before income taxes. The expected tax rates used were those in effect for the periods. Calculation of the Company's Canadian future income tax results in a future tax asset; however, the Company can not be certain it will realize the value of this asset and has assigned it a fair value of nil. This adjustment is shown in the following table as a valuation allowance of $1.9 million in the tax calculation. The principal reasons for differences between "expected" income tax expense and the amount actually recorded are as follows:

			2009			2008
	Canada	**U.S.**	**Total**	Canada	U.S.	Total
Earnings (loss) before income tax	**$ (15,264)**	**$ (2,142)**	**$ (17,406)**	$ (5,034)	$ 559	$ (4,475)
Canadian / U.S. Federal tax rate	**29.08%**	**34.00%**		29.70%	34.70%	
Computed expected income tax expense (recovery)	**$ (4,439)**	**$ (728)**	**$ (5,167)**	$ (1,495)	$ 194	$ (1,301)
Increase (decrease) in income taxes resulting from:						
Valuation allowance	**1,869**	**-**	**1,869**	-	-	-
Non-deductible expenses	**23**	**-**	**23**	47	-	47
Capital and other tax	**17**	**12**	**29**	17	15	32
Other	**(12)**	**(24)**	**(36)**	(1)	(23)	(24)
Change in tax rate	**409**	**-**	**409**	138	-	138
Adjusted tax pools	**(205)**	**27**	**(178)**	186	-	186
Actual income tax expense (recovery)	**$ (2,338)**	**$ (713)**	**$ (3,051)**	$ (1,108)	$ 186	$ (922)

Future income tax liability is comprised of temporary differences between the book value of the assets of the Company and the future income tax reductions at the expected future tax rates. In Canada, the temporary differences result in a future tax asset, however, the Company has taken a valuation allowance against this asset as the expected timing and ultimate recovery are uncertain. The future tax liabilities are as follows:

Future Tax Liability - Canada

($ Thousands)	**2009**	2008
Net book value of assets under (over) associated tax base	**$ (1,026)**	$ 3,222
Asset retirement obligation	**(828)**	(868)
Attributed Canadian royalty income	**-**	(13)
Share issue costs	**(15)**	(29)
Valuation allowance	**1,869**	-
Future tax liability (asset)	**$ -**	$ 2,312

Future Tax Liability - U.S.

($ Thousands)	**2009**	2008
Net book value of assets over associated tax base	**$ 1,942**	$ 3,067
Future tax liability	**$ 1,942**	$ 3,067

Future Tax Liability - Total

($ Thousands)	**2009**	2008
Net book value of assets over associated tax base	**$ 916**	$ 6,289
Asset retirement obligation	**(828)**	(868)
Attributed Canadian royalty income	**-**	(13)
Share issue costs	**(15)**	(29)
Valuation Allowance	**1,869**	-
Future tax liability	**$ 1,942**	$ 5,379

At December 31, 2009, the Company had the following tax deductions available to reduce future taxable income:

Tax Pools	**Years Ended December 31**	
($ Thousands)	**2009**	2008
Canadian exploration expense	**$ 14,107**	$ 12,090
Canadian development expense	**6,059**	4,549
Undepreciated capital cost	**8,096**	8,096
Canadian oil and gas property expense	**2,335**	4,803
	30,597	29,538
U.S. tax pools	**1,594**	3,128
Total	**$ 32,191**	$ 32,666

Substantially all of the tax pools have no expiry date.

9. *Asset Retirement Obligation*

The Company recognizes the fair value of an Asset Retirement Obligation ("ARO") as a liability in the period in which it is incurred if a reasonable estimate of fair value can be made. The present value of the estimated ARO is capitalized as part of the net capitalized asset base and the depletion of the capitalized asset retirement cost is determined on a basis consistent with depletion of the Company's other assets. With time, accretion will increase the carrying amount of the obligation. Accretion is expensed.

The following table presents the reconciliation of the beginning and ending aggregate carrying amount of the obligation associated with the retirement of oil and gas properties:

		Years Ended December 31
($ Thousands)	**2009**	2008
Asset Retirement Obligation, beginning of period	**$ 3,323**	$ 3,069
Liabilities incurred	**35**	26
Liabilities settled	**(43)**	(51)
ARO reduction for property sales	**(209)**	-
Accretion expense	**285**	264
Foreign exchange difference	**(10)**	15
Asset Retirement Obligation, end of period	**$ 3,381**	$ 3,323

$209,000 (2008 - nil) of the Company's asset retirement obligation was reduced by selling various properties during 2009. The total undiscounted amount of estimated cash flows required to settle the obligation is $4,649,000 which has been discounted using an average credit-adjusted risk free rate of 9 percent. Most of these obligations are expected to be paid between 2011 and 2016.

10. Commitments

The Company has committed to future minimum payments under an operating base lease covering office facilities as follows:

Year ended December 31,		Amount (Thousands)
2010		180
	$	180

The Company has the following gas price contracts in place for future periods:

Fixed Price Volume		Fixed Price ($/Mcf)	Time Period for Contract
950	Mcfd	6.36	Jan 1, 2010 - Mar 31, 2010
950	Mcfd	5.70	Apr 1, 2010 - Oct 31, 2010
950	Mcfd	6.63	Nov 1, 2010 - Mar 31, 2011

11. Financial Instruments

Financial instruments are measured at fair value on initial recognition of the instrument, into one of the following five categories: held-for-trading, loans and receivables, held-to-maturity investments, available-for-sale financial assets or other financial liabilities.

Subsequent measurement of financial instruments is based on their initial classification. Held-for-trading financial assets are measured at fair value and changes in fair value are recognized in net income. Available-for-sale financial instruments are measured at fair value with changes in fair value recorded in other comprehensive income until the instrument is derecognized or impaired. The remaining categories of financial instruments are recognized at amortized cost using the effective interest rate method.

Cash is classified as held-for-trading and is measured at fair value which equals the carrying value. Accounts receivable are classified as loans and receivables, which are measured at amortized cost. Accounts payable and accrued liabilities and bank debt are classified as other financial liabilities, which are measured at amortized cost.

The convertible debentures are classified as other financial liabilities. Upon issuance, the convertible debentures were classified into equity and financial liability components on the balance sheet at their fair value. The financial liability, net of issuance costs, is accreted, which is included within interest expense over the maturity of the debentures using the effective interest rate method.

The transaction costs that are directly attributable to the acquisition or issue of a financial asset or financial liability are expensed immediately.

The estimated fair values of the financial instruments have been determined based on the Company's assessment of available market information. These estimates may not necessarily be indicative of the amounts that could be realized or settled in a market transaction. The fair values of financial instruments, other than convertible debentures, are equal to their book amounts due to the short-term maturity of these instruments.

The fair value of the bank loan approximates its book value as it is at a market rate of interest. The fair value of the convertible debentures has been calculated based on the lower of trading value and the present value of future cash flows plus the conversion option associated with the convertible debentures.

Credit risk

Credit risk is the risk that the counterparty to a financial asset will default, resulting in the Company incurring a financial loss. The Company is exposed to credit risk on its accounts receivable and GST receivable, to a maximum of the carrying value of the aforementioned items at the end of the period. A substantial portion of the Company's accounts receivable are with customers in the oil and gas industry and are subject to normal industry credit risks. The maximum exposure to credit risk is approximately $597,000 which represents accounts receivable balances in excess of 90 days. Management has reviewed the items comprising the accounts receivable balance and determined that all accounts are collectible; accordingly there has been no allowance for doubtful accounts recorded.

Interest rate risk

The Company is exposed to risks from interest rate fluctuation on its bank loan which is based on Prime rates. Interest rate risk is specific to the interest expense charged to income on the Company's bank debt. The Company believes a 25% volatility is a reasonable measure when assessing the potential impact of a change in interest rate. Variations in interest rates on the Company's bank debt could have resulted in gains (losses) impacting net earnings as at December 31, 2009, as follows:

($ Thousands)	Favourable 25% Change	Unfavourable 25% Change
Interest expense	$ (240)	$ 240

Liquidity risk

The Company is exposed to liquidity risk from the possibility that it will encounter difficulty meeting its financial obligations. The Company manages this risk by forecasting cash flows in an effort to match operating cash flow to future expenditures and to arrange financing, if necessary. It may take many years and substantial cash expenditures to pursue exploration and development activities on all of the Company's existing undeveloped properties. Accordingly, the Company may need to raise additional funds from outside sources in order to explore and develop its properties. There is no assurance that adequate funds from debt and equity markets will be available to the Company in a timely manner. The timing of cash outflows relating to financial liabilities are outlined in the table below:

($ Thousands)	< 1 year	2-3 years	> 3 years
Accounts payable and accrued liabilities	4,508	-	-
Bank loan	4,398	-	-
Convertible debentures plus interest	620	7,875	-

At December 31, 2009 the Company has met all the obligations associated with its financial liabilities. The majority of the Company's accounts payable are current. The bank loan is a revolving production loan and is classified as a current liability. Convertible debentures are payable on March 26, 2012.

Foreign currency exchange risk

The Company is exposed to fluctuations in foreign currency exchange rates as the Company has a U.S. subsidiary with a functional currency of United States dollars while the functional currency of the Company is Canadian dollars. As a result, fluctuations in the United States dollar against the Canadian dollar could result in unanticipated fluctuations in the Company's financial results which are denominated in Canadian dollars.

The Company's exposure to foreign currency exchange risk at December 31, 2009, can be summarized as follows:

	Balance Sheet	Canada	USA
($ Thousands)	**Total**	Cdn $ Equivalent	
Cash and cash equivalents	**104**	-	104
Accounts receivable	**2,400**	2,300	100
Accounts payable	**(4,508)**	(4,276)	(232)
Total	**(2,004)**	(1,976)	(28)

Commodity price risk

Inherent to the Company's business of producing petroleum and natural gas is the commodity price risk where fluctuations in the market price of petroleum and natural gas could significantly impact the Company's ability to generate cash flow from operating activities. The Company believes a 10% volatility is a reasonable measure when assessing the potential impact of commodity price changes on natural gas and oil prices. Variations in commodity prices could have resulted in gains (losses) impacting net earnings as at December 31, 2009, as follows:

($ Thousands)	Favourable 10% Change	Unfavourable 10% Change
Natural gas price	$ 562	$ (562)
Crude oil price	$ 191	$ (191)

12. Subsequent Events

On March 15th and 31st, 2010, the Company closed two tranches of a financing. Diaz issued 8,039,500 units and 1,400,000 respectively at a price of $0.15 per unit for net proceeds of approximately $1,263,500. Each unit consists of one common share and one-half of a common share purchase warrant. Each whole warrant entitles the holder thereof to purchase one common share at a price of $0.20, at any time until March 12, 2012. The common shares, warrants and common shares issuable upon exercise of the warrants are subject to a four month hold period expiring July 13, 2010 or August 1, 2010 respectively. Diaz also granted the lead agent and the sub-agents options to acquire an aggregate of 723,160 common shares of Diaz at any time until March 12, 2012 at a price of $0.156 per share.

13. Related Party Transactions

Diaz and Sharon Energy Ltd. ("Sharon") and Tuscany Energy Ltd. ("Tuscany") and Paris Energy Inc. ("Paris") and Humboldt Capital Corporation ("Humboldt") have certain common officers and directors. In addition, at March 5, 2010, Humboldt and its directors and officers owned approximately:

- 27% of Sharon common shares,
- 37% of Diaz common shares,
- 44% of Tuscany common shares, and
- 25% of Paris common shares.

At December 31, 2009, Sharon owed Diaz $111,000 (2008 – Diaz owed Sharon $365,000) through the normal course of business.

For the year ended December 31, 2009, Diaz recovered the following amounts related to certain overhead services from:

	December 31, 2009	December 31, 2008
Sharon	$671,000	$113,000
Humboldt	$288,000	$288,000
Tuscany	$104,000	Nil
Paris	$14,000	Nil

Diaz paid Sharon an overhead charge of $449,000 (2008 – $238,000) relating to U.S. operations. This relationship was discontinued in 2009.

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

14. Segmented Information

The Company's only industry segment is the exploration for and development and production of oil and natural gas. The following table sets forth the geographical segments of the Company's operations between Canada and the United States.

($ Thousands, Three Months Unaudited)	Three Months Ended December 31 2009	Three Months Ended December 31 2008	Years Ended December 31 2009	Years Ended December 31 2008
Revenue (net)				
Canada	**$ 1,328**	$ 2,778	**5,913**	$ 11,359
United States	**240**	611	**1,060**	3,740
	$ 1,568	$ 3,389	**$ 6,973**	$ 15,099
Overhead (net)				
Canada	**$ 246**	$ 485	**$ 778**	$ 1,541
United States	**67**	82	**231**	253
	$ 313	$ 567	**$ 1,009**	$ 1,794
Interest Expense				
Canada	**$ 295**	$ 360	**$ 1,240**	$ 1,431
United States	**-**	-	**-**	-
	$ 295	$ 360	**$ 1,240**	$ 1,431
Current Taxes				
Canada	**$ -**	$ 11	**$ 17**	$ 17
United States	**(3)**	(23)	**13**	15
	$ (3)	$ (12)	**$ 30**	$ 32
Cash Flow from Operations				
Canada	**$ 187**	$ 717	**$ 1,211**	$ 4,706
United States	**172**	429	**670**	3,031
	$ 359	$ 1,146	**$ 1,881**	$ 7,737
Depletion, Depreciation & Accretion				
Canada	**$ 868**	$ 1,904	**$ 4,630**	$ 6,622
United States	**664**	978	**2,824**	2,718
	$ 1,532	$ 2,882	**$ 7,454**	$ 9,340
Net Income (Loss)				
Canada	**$ (2,573)**	$ (2,901)	**$ (12,927)**	$ (3,926)
United States	**(339)**	(660)	**(1,428)**	(161)
	$ (2,912)	$ (3,561)	**$ (14,355)**	$ (4,087)
Additions to Property, Plant & Equipment				
Canada	**$ 2,214**	$ 1,324	**$ 3,793**	$ 4,705
United States	**62**	805	**622**	3,073
	$ 2,276	$ 2,129	**$ 4,415**	$ 7,778
Dispositions of Property, Plant & Equipment				
Canada	**$ 2,406**	$ 54	**$ 3,406**	$ 55
United States	**57**	1	**1,001**	19
	$ 2,463	$ 55	**$ 4,407**	$ 74
Property, Plant & Equipment Impairment				
Canada	**$ -**	$ 2,744	**$ 11,408**	$ 2,744
United States	**-**	-	**-**	-
	$ -	$ 2,744	**$ 11,408**	$ 2,744
Identifiable Assets, Net				
Canada	**$ 28,778**	$ 43,870	**$ 28,778**	$ 43,870
United States	**7,879**	12,891	**7,879**	12,891
	$ 36,657	$ 56,761	**$ 36,657**	$ 56,761

CORPORATE INFORMATION

Directors

Robert W. Lamond
Calgary, Alberta

Charles A. Teare
Calgary, Alberta

Donald K. Clark
Calgary, Alberta

Clive M. Stockdale (1)(2)
Vancouver, British Columbia

Raj Agrawal (1)
Calgary, Alberta

John G.F. McLeod (2)
Okotoks, Alberta

Robert L. McPherson (3)
Calgary, Alberta

Roger Hume (1)
Calgary, Alberta

(1) Member of the Audit Committee
(2) Member of the Compensation Committee
(3) Member of the Corporate Governance Committee

Legal Counsel

Burnet, Duckworth & Palmer LLP
Calgary, Alberta

Registrar and Transfer Agent

Computershare Trust Company of Canada
Calgary, Alberta
Toronto, Ontario

Officers

R.W. Lamond
President, Chairman of the Board & CEO

D.K. Clark
Vice President, Operations & COO

B.R. Perry
Chief Financial Officer

C.A. Teare
Executive Vice President

C.S. Cohen
Corporate Secretary

R.D. Arsenault
Controller

Subsidiaries

Diaz Resources, Inc.
Orbit Oil & Gas Inc.

Auditors

PricewaterhouseCoopers LLP
Calgary, Alberta

Stock Exchange Listing

Toronto Stock Exchange
Trading Symbol: DZR

Diaz Resources Ltd.

Suite 1800, 633 – 6 Avenue SW
Calgary, Alberta T2P 2Y5
Telephone : (403) 269-9889
Fax : (403) 269-9890
Website : www.diazresources.com

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1800, 633-6 Ave SW
Calgary, Alberta T2P 2Y5