

MANAGEMENT DISCUSSION AND ANALYSIS (“MD&A”)

The following MD&A of Pyramid Petroleum Inc (“Pyramid” or the “Company”), of the financial condition and the results of operations for the three and nine months ended September 30, 2007 has been prepared using information that is current to November 29, 2007 and should be read in conjunction with the following:

- The unaudited interim consolidated financial statements and accompanying notes for the three and nine months ended September 30, 2007;
- The audited consolidated financial statements and accompanying notes for the year ended December 31, 2006; and
- The MD&A for the year ended December 31, 2006.

The financial information presented herein has been prepared on the basis of Canadian generally accepted accounting principles (“GAAP”). Throughout this discussion, percentage changes are calculated using numbers rounded to the decimal to which they appear.

This MD&A and the accompanying unaudited interim consolidated financial statements for the three months and nine months ended September 30, 2007, have been approved by the Board of Directors of the Company.

NON-GAAP MEASURES

Within this MD&A references are made to terms commonly used in the oil and gas industry. Cash flow from operations, cash flow per share, net oil and gas revenue and field netback are terms not defined by Canadian GAAP and are referred to as non-GAAP measures. Cash flow from operations represents net income (loss) for the period adjusted for non-cash items in the Consolidated Statements of Operations as detailed on the Consolidated Statements of Cash Flows. Cash flow per share is calculated based on the weighted average number of common shares outstanding consistent with the calculation of net income (loss) per share. Net oil and gas revenue and field netbacks both represent revenue less royalties and operating expenses. Management believes that field netback is a useful supplemental measure as it provides an indication of the Company’s operating performance, leverage and liquidity.

In conformity with National Instrument 51-101, Standards of Disclosure for Oil and Gas Activities, natural gas volumes have been converted to barrels of oil equivalent (“boe”) using a conversion ratio of six thousand cubic feet (“mcf”) of natural gas to one barrel of oil (“bbl”). This ratio is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead. Readers are cautioned that boe’s may be misleading, particularly if used in isolation.

FORWARD-LOOKING INFORMATION

Certain statements herein may constitute forward-looking information, which can generally be identified as such because of the context of the statements including words such as believes, anticipates, expects, plans, estimates, or words of a similar nature. The forward-looking statements are based on current expectations and are subject to known and unknown risks, uncertainties, and other factors that may cause the actual results, performance or achievements of the Company to be materially different from any future results.

All such forward-looking information is based on certain assumptions and analyses made by Pyramid in light of the Company’s experience and perception of historical trends, current conditions and expected

future developments, as well as other factors Pyramid believes are appropriate in the circumstances. The risks, uncertainties, and assumptions are difficult to predict and may affect operations, including, without limitation: the risks of foreign operations; foreign exchange fluctuations; commodity prices; equipment and labor shortages; inflationary costs; general economic conditions; industry conditions; changes in applicable environmental, taxation and other laws and regulations as well as how such laws and regulations are interpreted and enforced; the ability of oil and natural gas companies to raise capital; the effect of weather conditions on operations and facilities; the existence of operating risks; volatility of oil and natural gas prices; oil and natural gas product supply and demand; uncertainties associated with estimating reserves; incorrect assessments of the value of acquisitions; geological, technical, drilling and processing problems; risks inherent in the ability to generate sufficient cash flow from operations to meet current and future obligations; increased competition; stock market volatility; opportunities available to or pursued by Pyramid; and other factors, many of which are beyond the Company's control. The foregoing factors are not exhaustive.

FUNCTIONAL AND REPORTING CURRENCY

Effective April 1, 2007, the Company changed its functional currency from the Canadian dollar to the U.S. dollar. This change was made as a result of the acquisition of MC Offshore Petroleum, LLC (see Description of Business) with its activities of capital expenditures and expenses denominated in U.S. dollars becoming the predominant currency for the Company's expenditures. Following the change of functional currency to the U.S. dollar, the Company also changed its reporting currency to the U.S. dollar effective April 1, 2007. Financial statements for all periods presented have been translated into U.S. dollars (the functional and reporting currency). All comparative financial information being presented has been restated to reflect the Company's financial statements as if they have been historically reported in U.S. dollars.

All references to dollar amounts herein are in U.S. dollars.

DESCRIPTION OF BUSINESS

Pyramid was incorporated pursuant to the provisions of the Business Corporations Act (Alberta) on March 11, 2005 as a Capital Pool Company as defined in Policy 2.4 of the TSX Venture Exchange. The Company closed its Initial Public Offering (IPO) on October 19, 2005. The Company completed its Qualifying Transaction (the "Qualifying Transaction") on May 4, 2006 and started trading as a non Capital Pool Company on May 12, 2006. The Qualifying Transaction constituted acquisition of certain oil and gas assets (the "Assets") from a founding shareholder of the Company. The Assets are located in Alberta, Canada and Montana, United States. On October 3, 2006, the Company purchased the remaining working interest owned by its Officer and Director in certain oil and gas properties where the Company had earlier purchased working interest as part of the Qualifying Transaction.

On August 31, 2006, the Company completed the acquisition of a varying working interest, ranging from 1.25% to 5%, in certain oil and gas properties in the Gulf of Mexico from an arms-length party.

On April 1 2007 the Company closed its purchase of a 20% membership shares interest in a Limited Liability Company ("LLC"). One May 17, 2007, the Company increased its share ownership in the LLC to 50%. The LLC was organized for the purpose of acquiring an interest in certain oil and gas properties from an arms length party, consisting of varying non-operated working interests, ranging from 25% to 100%, in 46 producing and 16 non producing oil and gas wells in the Gulf of Mexico.

As the LLC is controlled and operated jointly by the members, the acquisition is considered to be the acquisition of an interest in a joint venture whereby only the Company's proportionate interest in the LLC is consolidated. The purchase price of the 50% membership share interest in the LLC was \$1,000,000 cash which was allocated to the Company's share of net assets acquired.

The assets acquired in August 2006 and those though the LLC are referred as GOM Assets in this MD&A.

On September 19, 2007 the Company signed a Purchase and Sale Agreement (“PSA”) to acquire AMCO Energy, Inc. (“AMCO”), a wholly owned subsidiary of Capco Energy, Inc., a corporation controlled by an Officer and Director of the Company. The purchase price is \$11,000,000 and is subject to adjustments for working capital and credit of net operating income from January 1, 2007 to the closing date. The estimated net purchase price is \$7,200,000. Upon signing of the PSA, the Company paid a cash deposit of \$200,000. The balance of the payment will be made at closing, which is expected on or before December 31, 2007. The Company is working on multiple lending options to finance this acquisition. The transaction is subject to all customary regulatory approvals. With this acquisition, Pyramid’s interest in certain of its Gulf of Mexico (“GOM”) properties will increase from the original 5% acquired in August 2006 to 29%. AMCO has a staff of qualified professionals and will continue to manage its operations in the GOM as well as Pyramid's other assets in the GOM.

Pyramid is a reporting issuer in British Columbia, Alberta and Ontario and trades on the TSX Venture Exchange (“TSXV”) under the symbol PYR.

CONSOLIDATED RESULTS HIGHLIGHTS

The following is the summary of financial results for the Company for the three months and nine months ended September 30, 2006 and 2007. Note that the results of operations for the comparative three and nine months ended September 30, 2006 consist of oil and natural gas production results from May 4, 2006, following the completion of the Qualifying Transaction.

| | Three months ended September 30 | | Nine months ended September 30 | |
|--|------------------------------------|------------|-----------------------------------|------------|
| | 2007 | 2006 | 2007 | 2006 |
| Total sales volumes (boe 6:1), net of royalties | 119,672 | 14,347 | 212,338 | 20,987 |
| Daily sales volumes (boe 6:1) - net of royalties | 1,301 | 156 | 778 | 77 |
| Statement of Operations and Deficit | | | | |
| Oil and gas sales (\$), net of royalties | 6,387,949 | 594,732 | 10,193,749 | 802,869 |
| Oil and gas sales per boe (\$) | 53.38 | 41.45 | 48.01 | 38.26 |
| Net oil and gas revenue (\$) | 3,752,702 | 443,388 | 6,484,431 | 526,245 |
| Net oil and gas revenue per boe (\$) | 31.36 | 30.90 | 30.54 | 25.07 |
| (Loss) income for the period (\$) | 397,234 | 29,204 | 956,355 | (75,106) |
| (Loss) income per share – basic and diluted (\$) | 0.01 | - | 0.03 | - |
| Statement of Cash Flows | | | | |
| Cash flow from operations (\$) | 2,118,455 | 330,950 | 3,577,893 | 435,633 |
| Cash flow from operations per share (\$) | 0.06 | 0.01 | 0.10 | 0.02 |
| Weighted average number of shares – basic | 37,123,845 | 36,595,720 | 36,784,033 | 25,651,044 |

RESULTS OF OPERATIONS

Revenues, net of royalties, for the three months and nine months ended September 30, 2007 were \$6,388,107 and \$10,247,207 respectively. The operating costs for the same periods were \$2,635,247 and \$3,709,318 respectively. The general and administrative expenses for the three months and nine months ended September 30, 2007 were \$127,445 and \$400,448 respectively. The depreciation, depletion, and accretion expense for these periods were \$1,707,711 and \$2,577,096 respectively.

The net income for the three months and nine months ended September 30, 2007 was \$397,234 and \$956,355 respectively. Cash flow from operations for the three months and nine months ended September 30, 2007 were \$2,118,455 and \$3,577,893 respectively.

A summary of the results of operations is as follows:

| (\$) | Three months ended September 30 | | Nine months ended September 30 | |
|--|------------------------------------|-----------|-----------------------------------|-----------|
| | 2007 | 2006 | 2007 | 2006 |
| Oil and gas revenue | 6,387,949 | 594,732 | 10,193,749 | 802,869 |
| Operating expenses | (2,635,247) | (151,344) | (3,709,318) | (276,624) |
| Field netbacks | 3,752,702 | 443,388 | 6,484,431 | 526,245 |
| Interest revenue and commodity contracts | 158 | 14,449 | 53,458 | 23,651 |
| General and administrative | (127,445) | (46,174) | (400,448) | (91,041) |
| Interest expense | (578,510) | (77,717) | (1,077,822) | (85,917) |
| Foreign exchange gain (loss) | (429,355) | (2,996) | (677,301) | 62,695 |
| Current income tax provision | (499,095) | - | (804,425) | - |
| Cash flow from operations | 2,118,455 | 330,950 | 3,577,893 | 435,633 |
| Depletion, depreciation, and accretion | (1,707,711) | (301,746) | (2,577,096) | (373,804) |
| Accretion of equity in debentures | (3,889) | - | (8,866) | - |
| Accretion of equity component | (9,621) | - | (35,576) | - |
| Stock-based compensation | - | - | - | (136,935) |
| Net income (loss) | 397,234 | 29,204 | 956,355 | (75,106) |
| Per share, basic and diluted | 0.01 | - | 0.03 | - |

PRODUCTION VOLUMES

The Company's production volumes, net of royalties, for each of the last four quarters are as follows.

| | Q3-07 | | | Q2-07 | | | Q1-07 | | | Q4-06 | | |
|-------------------|--------------|--------------------|----------------|--------------|--------------------|----------------|--------------|--------------------|----------------|--------------|--------------------|----------------|
| | Gas Mcf/d | Oil&NGLs bbls/d | Total Boe/d | Gas mcf/d | Oil&NGLs bbls/d | Total Boe/d | Gas mcf/d | Oil&NGLs bbls/d | Total boe/d | Gas mcf/d | Oil&NGLs bbls/d | Total boe/d |
| Montana | 656 | 9 | 119 | 653 | 10 | 119 | 655 | 11 | 120 | 691 | 10 | 125 |
| Alberta | 36 | 0 | 6 | 41 | 0 | 7 | 39 | 0 | 7 | 41 | 0 | 7 |
| Gulf of Mexico | 3,309 | 625 | 1,176 | 1,919 | 385 | 705 | 357 | 5 | 65 | 594 | 9 | 108 |
| Total | 4,001 | 634 | 1,301 | 2,613 | 395 | 831 | 1,051 | 16 | 191 | 1,326 | 20 | 241 |

Note: All production numbers are net of royalties.

CAPITAL EXPENDITURES

Capital expenditures totaled \$2,428,737 in the three months and \$3,821,673 for the nine months ended September 30, 2007. The breakdown of these expenses is as follows:

| (\$) | Three months ended September 30 | | Nine months ended September 30 | |
|-----------------------------------|------------------------------------|---------|-----------------------------------|---------|
| | 2007 | 2006 | 2007 | 2006 |
| Geological and geophysical | - | - | 51,577 | - |
| Drilling, completions and tie-ins | 2,428,737 | 270,065 | 3,770,096 | 424,328 |
| Total | 2,428,737 | 270,065 | 3,821,673 | 424,328 |

The capital expenditures include drilling and tie-in cost during the nine months ended September 30, 2007 for 50% of the LLC's share of cost in the amount of \$2,880,237. The work included sidetracking of 2 wells, work over of 7 wells and pipeline cost to 1 well in the Gulf of Mexico. The net gain to Pyramid is an increase in gross production, based on average rates, is 2,250 mcf/d and 85 bopd.

Also, included in the capital expenses are expenses related to the drilling of a well in Hays, Alberta. The well is cased and is expected to put on production with initial production rate of 130 mcf/d. Pyramid owns 90% working interest in this well and the capital expenses to the Company's share to date amount to \$360,345.

DEBT AND WORKING CAPITAL

As of September 30, 2007 the Company had current assets of \$3,529,157 and current liabilities of \$16,373,640. Included in the current liabilities are current portions of loans payable in the amount of \$6,934,566 for which debt service payments are required from approximately 80% of net operating revenues from the properties that are collateralized to the various lenders. Also, included in the current liabilities is the bank's revolving line of credit in the amount of \$3,995,670, deferred payments for purchase price in the amount of \$1,250,000, which is due in March 2008, and related party amounts payable to an Officer and Director of the Company in the amount of \$1,363,378. After adjusting for these items, the working capital results in a surplus of \$699,131.

The Company is planning to consolidate its debt that is collateralized by its US assets into one credit agreement. Management believes that this consolidation will help reduce the interest payments and also provide more free cash flow to the Company for its future development programs.

The following table summarizes the cash flow from operating, investing and financing activities for the three months and nine months ended September 30, 2007 and 2006.

| (\$) | Three months ended September 30 | | Nine months ended September 30 | |
|------------------------------------|------------------------------------|-----------|-----------------------------------|-------------|
| | 2007 | 2006 | 2007 | 2006 |
| Cash flow from operations | 2,118,455 | 330,950 | 3,577,893 | 435,633 |
| Change in non-cash working capital | (349,423) | (62,868) | (1,284,456) | (159,995) |
| Cash from (used in) | | | | |
| operating activities | 1,769,032 | 268,082 | 2,293,437 | 275,638 |
| Cash from (used in) | | | | |
| investing activities | (1,517,694) | (818,610) | (3,453,097) | (1,390,254) |
| Cash from (used in) | | | | |
| financing activities | 113,984 | (143,155) | 1,601,135 | (350,445) |

Details of various debts added during the nine months ended on September 30, 2007 are provided below:

On April 18, 2007, The Company closed a revolving demand loan facility from a Canadian bank to a maximum of Can\$4,000,000, collateralized by a charge over the Company's Montana and Alberta assets. The Company used the facility to repay the loan due to the operator of the Montana and Alberta properties and to repay the note due to the Officer and Director of the Company for the purchase in October 2007 of a working interest in the Montanan and Alberta properties. The Company is obligated to make payments of interest only, subject to availability, review and bank's right of demand. The interest on the loan is calculated at bank's prime plus 0.5%. The current prime rate is set at 6.25%.

On April 27, 2007, the Company closed a private placement of convertible debentures for a total amount of \$828,100. The net proceeds to the Company, after paying of agent's commission and legal costs,

amounted to \$720,914. The proceeds of the private placement were utilized to fund the purchase of membership shares in LLC, as discussed in “Business Description” above.

The debentures have a two year term and bear an interest rate of 12% per annum, which interest is to be paid quarterly. The holders of these debentures have an option to convert them to common shares of the company at an exercise price of \$0.45/share at any time during the term of the debenture. The Company has an option to call the debentures at any time after first anniversary from closing date if the common shares of the Company trade at over \$0.675/share for a period of 30 days.

In conjunction with the acquisition of the 50% membership share interest in the LLC, the Company assumed a term note (the “Note”) in the amount of \$12,649,982 comprised of \$12,559,898 principal plus \$90,084 of interest accrued to the dates of acquisition. The Note bears annual interest at 10% rate and is collateralized by the petroleum and natural gas assets held by the LLC and for which the LLC members have pledged their member share certificates to the lender. Principal and accrued interest on the Note are repayable in consecutive principal installments of 80% of the monthly net proceeds (revenue less royalties, net profits interests and direct operating expenses) from the related Gulf of Mexico properties to be not less than \$500,000 in principal per month plus accrued interest commencing on May 31, 2007 or at the discretion of the lender. As at September 30, 2007, the lender had only drawn two such payments, with a total of \$1,000,000 in principal payment. The loan balance as of September 30, 2007 was \$11,559,898, of which \$6,000,000 is reported as current portion, based on the minimum principal requirement.

OUTSTANDING SHARE DATA

Common shares

The Company commenced 2007 with 36,605,095 common shares outstanding. During the year, 687,500 shares were issued on the exercise of broker warrants. As of September 30, 2007, and the date of this MD&A the Company had a total of 37,292,595 common shares outstanding. Of these, a total of 17,457,432 common shares remained in escrow. The following table outlines the future releases of those shares from escrow.

| Release Date | November 11, 2007 | May 11, 2008 | November 11, 2008 | May 11, 2009 |
|---------------------|--------------------------|---------------------|--------------------------|---------------------|
| Number of shares | 4,364,358 | 4,364,358 | 4,364,358 | 4,364,358 |

Broker Warrants

As at December 31, 2006, the Company had 740,625 broker warrants outstanding. During 2007, 687,500 warrants were exercised and an additional 65,644 warrants were issued resulting in 118,769 broker warrants outstanding as at September 30, 2007 and the date of this MD&A.

Stock Options

As at December 31, 2006 and September 30, 2007, the Company had 900,000 stock options outstanding. There has been no change in the number of options outstanding as of the date of this MD&A

RELATED PARTY TRANSACTIONS

During the three months and nine months ended September 30, 2007 the Company paid a total of \$37,520 and \$68,959 respectively in interest to a related company for the loan due to the related company. Also, during the three months and nine months ended September 30, 2007 the Company paid a total of \$21,278 and \$67,547 respectively in interest to an Officer and Director of the Company for the two promissory

notes, of which one promissory note was paid in full on April 18, 2007. The discussion of relevant notes is provided in note 10 of the financial statements.

COMMODITY CONTRACTS

The Company has participated, through the operator, in financial swaps for the gas production from the Gulf of Mexico properties. The contracts have various settlement dates up to December 31, 2007. As of September 30, 2007 the mark-to-market balances for the Company's share of these swap contracts resulted in an unrealized loss of \$73,936. During the nine months ended September 30, 2007, the Company recognized \$83,346 in realized gain on these instruments.

At September 30, 2007 the Company have entered into the following financial forward arrangements:

| | <u>Quantity</u> <u>(MMBTU)/</u> <u>(BBL)</u> | <u>Price</u> <u>(US\$/MMBTU)/</u> <u>(US\$/BBL)</u> | <u>Termination Date</u> |
|-------------------------|--|---|-------------------------|
| Sales contracts: | | | |
| Gas | | | |
| 23274 | 23,115 | 7.075 | December 31, 2007 |
| 23720 | 23,115 | 7.525 | December 31, 2007 |
| 23793 | 16,080 | 8.100 | December 31, 2007 |
| Oil | | | |
| 23888 | 100,000 | 64.030 | December 31, 2007 |

The Company accounts for these contracts on a fair value basis on the balance sheet. The estimated fair value of these financial instruments is based on their quoted prices, or in their absence, third party market indicators and forecasts. The changes in the fair value associated with the above financial instruments are recorded as unrealized gain or loss on financial instruments on the statement of operations. Gain or loss arising from monthly settlements with counterparties is recognized as realized gain or loss in the statement of operations.

COMMITMENTS

A bond collateral in the amount of \$4,985,412 as at September 30, 2007 relates to the Company's share of cash collateral for performance bonds (the "Bonds") provided by the LLC to certain regulatory authorities and to the Seller of the Gulf of Mexico properties as a guarantee for plugging and abandonment liabilities. The LLC obtained the Bonds through a surety company which required the LLC to put up cash collateral. The Bonds will be released once the subject properties are abandoned at which time all cash collateral will be returned to the LLC. Further, the partner in the LLC had provided a corporate guarantee of \$1,500,000 to the bonding company as additional security for the Bonds and is charging 10% interest on the guarantee amount as a fee to the Company.

In addition to the Bonds, the Company is required to contribute 20% of the monthly net profits from the properties owned through the LLC towards an abandonment fund (the "Fund") established by the Seller as an additional guarantee against the plugging and abandonment liabilities associated with the properties. Net profits is defined in the Fund agreement as: the monies and revenues payable from gross production of the properties less (i) costs and expenses incurred attributed to the properties with respect to all existing wells located on the properties, including but not limited to the costs and expenses of operating the wells and for producing, treating and storing production from the wells; (ii) capital expenditures related to the properties; (iii) certain taxes assessed against production relating to the property; and (iv) all royalty burdens and other lease burdens affecting the properties. Where the net profit for a particular month is determined to be negative (a net loss), no contribution to the Fund is required for the related month.

Contributions to the Fund commence in April 2008. The Company's maximum amount of contribution to the Fund is \$5,000,000. Upon satisfactory performance of plugging and abandonment obligations, the Company may request a release of the Bond collateral amount and funds may be withdrawn from the Fund to maximum of the Fund balance.

CORPORATE OUTLOOK

The assets acquired as part of the Qualifying Transaction have long-term oil and gas reserves and are expected to provide a strong foundation for the Company. Also, the undeveloped lands included in these assets provide upside for future development. The GOM Assets have added reserves to the Company's asset base and have increased the overall operating cash flow. The cash flow, net of debt payment, will be utilized for further development and exploration projects.

The Company had acquired more assets during the nine months ended September 30, 2007 in the Gulf of Mexico area, as detailed in 'Description of Business'. With this acquisition the Company had established Gulf of Mexico as a core area for growth and intends to pursue further acquisitions in that area.. The Company is focusing on developing the unproved categories of reserves acquired during the above acquisitions, while continuing to acquire more oil and properties in the Gulf of Mexico, utilizing the experience of the management team.

The Company will strive to create sustainable growth in reserves, production, and cash flow through focusing on the creation of a diversified portfolio of development and exploration properties. This process requires careful selection of good quality projects and the current management team has the required experience to do this. The Company understands that it is at an early stage of operations and that it would be prudent to apply risk management techniques, adopting a 'portfolio' approach toward capital expenditures.

Selected Historical Financial Information

| Three Months ended (\$) | 2005 | 2006 | 2006 | 2006 | 2006 | 2007 | 2007 | 2007 |
|-----------------------------|------|-------|-----------|---------|-------------------|---------|-----------|-----------|
| | | Q1 | Q2 | Q3 | Q4 ⁽¹⁾ | Q1 | Q2 | Q3 |
| Net oil and gas revenue | - | - | 90,720 | 443,388 | 555,509 | 575,643 | 2,240,355 | 3,752,702 |
| Net income (loss) | - | 1,546 | (113,508) | 29,204 | (1,710,704) | 176,055 | 549,051 | 397,234 |
| Net income (loss) per share | - | - | - | - | (0.04) | - | 0.01 | 0.01 |
| Cash flow from operations | - | 1,546 | 92,841 | 330,950 | 322,655 | 417,751 | 1,223,255 | 2,118,455 |
| Net capital expenditures | - | - | 102,879 | 270,065 | 19,325 | 172,451 | 1,120,144 | 2,428,737 |

⁽¹⁾ The net loss in fourth quarter of 2006 includes impairment cost of \$1,862,790

CHANGES IN ACCOUNTING POLICIES

On January 1, 2007, the Company adopted the new or revised Canadian accounting standards for accounting changes, comprehensive income, financial instruments—recognition and measurement and financial instruments—presentation and disclosures. The impact of the adoption of the new standards is disclosed in note 3 to the June 30, 2007 unaudited interim consolidated financial statements. Additional disclosure requirements for financial instruments have been approved by the Canadian Institute of Chartered Accountants and will be required disclosure beginning January 1, 2008.

DISCLOSURE CONTROLS AND PROCEDURES

Disclosure controls and procedures are designed to provide reasonable assurance that information required to be disclosed is recorded, processed, summarized and reported with the time periods specified by securities regulations and that information required to be disclosed is accumulated and communicated to management.

The Chief Executive Officer and Chief Financial Officer have evaluated the effectiveness of Corporation's disclosure controls and procedures as of September 30, 2007 and have concluded that they are adequate and effective to provide reasonable assurance that material information related to the Company is made known. It should be noted that while the Company's Chief Executive Officer and Chief Financial Officer believe that the Company's disclosure controls and procedures provide a reasonable level of assurance that they are effective, they do not expect that the disclosure controls and procedures will prevent all errors and fraud. A control system, no matter how well conceived or operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met.

INTERNAL CONTROLS AND FINANCIAL REPORTING

The Chief Executive Officer and Chief Financial Officer of the Company are responsible for designing internal control over financial reporting 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. We have assessed the design of our internal control over financial reporting and during this process we identified certain weaknesses in internal controls over financial reporting. Due to the limited number of staff at the Company, it is not feasible to achieve complete segregation of incompatible duties. The CEO and CFO have been with the Company since its inception and have extensive industry experience. They are very aware of and are actively involved in the Company's on-going activities. As such, the capabilities and involvement of the CEO and CFO serve to mitigate the structural weakness of internal controls. Their efforts, together with the active involvement of the board of directors, are directed to minimize the risk of a material misstatement in financial reporting. However, there can be no assurance that this risk can be reduced to less than a remote likelihood of a material misstatement.

CRITICAL ACCOUNTING ESTIMATES

The Company's financial statements are prepared in accordance with Canadian generally accepted accounting principles. A comprehensive discussion of the Company's significant accounting policies is contained in note 2 to the audited consolidated financial statements for the year ended December 31, 2006. The Company's significant accounting policies are subject to estimates and key judgments about future events, many of which are beyond management's control. A detailed discussion of the critical accounting estimates of the Company is provided in the December 31, 2006 MD&A.

BUSINESS RISKS AND UNCERTAINTIES

The Company was recently incorporated and began operations in May 2006 after the completion of the Qualifying Transaction. It has a short history of earnings and has never paid any dividends. The Company expects to have increased earnings from assets acquired and additional acquisitions that the Company is pursuing, although there is no plan to pay any dividends now or in future; instead these earnings will be employed by the Company for future growth plans.

The Company is exposed to several operational risks inherent in exploring, developing, producing and marketing crude oil and natural gas. These inherent risks include: economic risk of finding and producing reserves at a reasonable cost; financial risk of marketing reserves at an acceptable price given current market conditions; cost of capital risk associated with securing the needed capital to carry out the Company's operations; risk of environment impact and credit risk of non-payment for sales contracts and joint venture partners.

The Company attempts to control operating risks by maintaining a disciplined approach to implementation of its exploration and development programs. Exploration risks are managed by hiring experienced technical professionals and by concentrating the exploration activity on specific core regions that have multi-zone potential where the Company has experience and expertise. The Company also generates internal prospects and participates in projects where ownership interest is considered sufficient to minimize risk. Operational control allows the Company to manage costs, timing and sales of production and to ensure new production is brought on-stream in a timely manner.

The Company maintains a comprehensive insurance program to reduce risk to an acceptable level and to protect it against significant losses. The Company's risk in regards to financial instruments is detailed in note 12 to the audited consolidated financial statements for the year ended December 31, 2006.

CORPORATE INFORMATION

| | |
|--------------------------------------|--|
| Head Office: | Suite 780, 910 – 7 Avenue SW Calgary, Alberta, Canada Tel: (403) 234-9000 Fax: (403) 770-8370 |
| Officers: | Chairman and CEO – Ilyas M. Chaudhary President and CFO – Mansoor A. Anjum |
| Directors: | Ilyas M. Chaudhary William E. Richards John F. Frey Mansoor A. Anjum |
| Independent Engineers: | Haas Petroleum Engineering Services, Inc. |
| Auditors: | BDO Dunwoody LLP |
| Solicitor: | Macleod Dixon LLP |
| Listing: | The TSX Venture Exchange Trading symbol: PYR |
| Transfer Agent and Registrar: | Valiant Trust Company |
| Website: | www.pyramidpetroleum.com |

Pyramid Petroleum Inc.
Interim Consolidated Financial Statements

Three and nine months ended
September 30, 2007

(Unaudited - Prepared by Management)

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NOTICE TO THE READER:

The accompanying unaudited interim consolidated financial statements of Pyramid Petroleum, Inc. for the three and nine months ended September 30, 2007 and 2006 have been prepared by management and approved by the Board of Directors of the Company. These statements have not been reviewed by the Company's external auditors.

On behalf of the Board:

Signed _____ Director
Ilyas M. Chaudhary

Signed _____ Director
Mansoor A. Anjum

Pyramid Petroleum, Inc.
Interim Consolidated Balance Sheets
(unaudited)

| Stated in U.S dollars (note 2) | September 30 2007 | December 31 2006 |
|--|----------------------|---------------------|
| Assets | | |
| Current | | |
| Cash and cash equivalents | \$ 553,495 | \$ 112,020 |
| Prepaid expenses | 164,169 | 83,775 |
| Accounts receivable | 2,811,493 | 89,404 |
| | <u>3,529,157</u> | <u>285,199</u> |
| Deferred charges (note 3) | – | 21,965 |
| Property and equipment (note 5) | 29,047,202 | 11,316,398 |
| Bond collateral (note 6) | 4,985,412 | – |
| Acquisition deposit (note 7) | 200,000 | – |
| | <u>37,761,771</u> | <u>11,623,562</u> |
| | \$ | \$ |
| Liabilities and Shareholders' Equity | | |
| Current Liabilities | | |
| Accounts payable and accrued liabilities | \$ 2,734,979 | \$ 178,002 |
| Deferred payment (note 4) | 1,250,000 | – |
| Demand loan (note 8) | 3,995,670 | – |
| Current portion of loans payable (note 9) | 6,000,000 | 668,117 |
| Due to related parties (note 10) | 2,297,944 | 1,174,149 |
| Current portion of asset retirement obligation (note 12) | 95,047 | 95,047 |
| | <u>16,373,640</u> | <u>2,115,315</u> |
| Loans payable (note 9) | 5,559,898 | 1,613,956 |
| Due to related parties (note 10) | – | 1,124,774 |
| Convertible debentures (note 11) | 847,488 | – |
| Asset retirement obligation (note 12) | 7,484,366 | 383,083 |
| | <u>30,265,392</u> | <u>5,237,128</u> |
| Shareholders' Equity | | |
| Equity instruments (note 14) | 8,125,253 | 7,956,809 |
| Contributed surplus (note 15) | 157,458 | 183,323 |
| Equity component of convertible debentures (note 11) | 32,976 | – |
| Deficit | (819,308) | (1,753,698) |
| | <u>7,496,379</u> | <u>6,386,434</u> |
| | \$ 37,761,771 | \$ 11,623,562 |

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

Pyramid Petroleum, Inc.
Interim Consolidated Statements of Operations and Deficit
(unaudited)

| Stated in U.S. Dollars (note 2) | Three months ended September 30 | | Nine months ended September 30 | |
|---|------------------------------------|--------------------|-----------------------------------|--------------------|
| | 2007 | 2006 | 2007 | 2006 |
| Revenue | | | | |
| Petroleum and natural gas, net of royalties | \$ 6,387,949 | \$ 594,732 | \$ 10,193,749 | \$ 802,869 |
| Interest revenue | 46,077 | 14,449 | 46,077 | 23,651 |
| Commodity contracts (note 16) | (45,919) | — | 7,381 | — |
| | <u>6,388,107</u> | <u>609,181</u> | <u>10,247,207</u> | <u>826,520</u> |
| Expenses | | | | |
| Operating expenses | 2,635,247 | 151,344 | 3,709,318 | 276,624 |
| General and administrative | 127,445 | 46,174 | 400,448 | 91,041 |
| Interest and financing costs | 588,131 | 77,717 | 1,113,398 | 85,917 |
| Depreciation, depletion and accretion | 1,707,711 | 301,746 | 2,577,096 | 373,804 |
| Accretion of equity component | 3,889 | — | 8,866 | — |
| Stock-based compensation | — | — | — | 136,935 |
| Foreign exchange (gain) loss | 429,355 | 2,996 | 677,301 | (62,695) |
| | <u>5,491,778</u> | <u>579,977</u> | <u>8,486,427</u> | <u>901,626</u> |
| Income (loss) before income taxes | 896,329 | 29,204 | 1,760,780 | (75,106) |
| Income tax provision | 499,095 | — | 804,425 | — |
| Net income (loss) for the period | 397,234 | 29,204 | 956,355 | (75,106) |
| Retained earning (deficit), beginning of period | (1,216,542) | (72,198) | (1,753,698) | 32,112 |
| Changes in accounting policies (note 3) | — | — | (21,965) | — |
| Deficit, ending of period | \$ (819,308) | \$ (42,994) | \$ (819,308) | \$ (42,994) |
| Income (loss) per share: | | | | |
| Basic and diluted | \$ 0.01 | \$ — | \$ 0.03 | \$ — |
| Weighted average number of shares: | | | | |
| Basic | 37,123,845 | 36,595,720 | 36,784,033 | 25,651,144 |
| Diluted | 37,342,225 | 36,772,000 | 36,971,927 | 25,890,011 |

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

Pyramid Petroleum, Inc.
Interim Consolidated Statements of Cash Flows
(unaudited)

| Stated in U.S dollars (note 2) | Three months ended September 30 | | Nine months ended September 30 | |
|---|------------------------------------|------------------|-----------------------------------|--------------------|
| | 2007 | 2006 | 2007 | 2006 |
| Cash provided by (used in) | | | | |
| Operating Activities | | | | |
| Net income (loss) for the period | \$ 397,234 | \$ 29,204 | \$ 956,355 | \$ (75,106) |
| Add: Non-cash items | | | | |
| Stock-based compensation | – | – | – | 136,935 |
| Accretion of equity component (note 11) | 3,889 | – | 8,866 | – |
| Financing costs | 9,621 | – | 35,576 | – |
| Depreciation, depletion and accretion | 1,707,711 | 301,746 | 2,577,096 | 373,804 |
| | <u>2,118,455</u> | <u>330,950</u> | <u>3,577,893</u> | <u>435,633</u> |
| Change in non-cash working capital (note 18) | <u>(349,423)</u> | <u>(62,868)</u> | <u>(1,284,456)</u> | <u>(159,995)</u> |
| | <u>1,769,032</u> | <u>268,082</u> | <u>2,293,437</u> | <u>275,638</u> |
| Financing activities | | | | |
| Proceeds from demand loan | 241,270 | – | 3,995,670 | – |
| Proceeds from convertible debentures | 112,348 | – | 940,370 | – |
| Financing costs | – | – | (93,360) | – |
| Repayment of loans payable | (1,090,084) | (92,338) | (3,372,157) | (394,716) |
| Repayment of related party debt | 951,409 | (116,322) | (979) | (21,234) |
| Proceeds on issue of common shares, net of issue costs | 110,504 | (18,522) | 131,591 | (18,522) |
| Deferred charges | – | 84,027 | – | 84,027 |
| Change in non-cash working capital (note 18) | <u>(211,463)</u> | <u>–</u> | <u>–</u> | <u>–</u> |
| | <u>113,984</u> | <u>(143,155)</u> | <u>1,601,135</u> | <u>(350,445)</u> |
| Investing activities | | | | |
| Expenditures on property and equipment | (2,428,737) | (270,065) | (3,821,673) | (424,328) |
| Acquisition of property and equipment, net of cash acquired (note 4) | – | (548,545) | (542,467) | (965,926) |
| Deposit on acquisition | (200,000) | – | (200,000) | – |
| Change in non-cash working capital (note 18) | <u>1,111,043</u> | <u>–</u> | <u>1,111,043</u> | <u>–</u> |
| | <u>(1,517,694)</u> | <u>(818,610)</u> | <u>(3,453,097)</u> | <u>(1,390,254)</u> |
| Increase (decrease) in cash | 365,322 | (693,683) | 441,475 | (1,465,061) |
| Cash and cash equivalents, beginning of period | <u>188,173</u> | <u>726,554</u> | <u>112,020</u> | <u>1,497,932</u> |
| Cash and cash equivalents, end of period | \$ 553,495 | \$ 32,871 | \$ 553,495 | \$ 32,871 |
| Supplemental cash flow information | | | | |
| Interest paid | \$ 614,312 | \$ – | \$ 1,113,624 | \$ – |
| Taxes paid | \$ – | \$ – | \$ – | \$ – |

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

Pyramid Petroleum, Inc.
Notes to Interim Consolidated Financial Statements
September 30, 2007
(unaudited)

Stated in U.S. Dollars

1. Basis of Presentation

Pyramid Petroleum Inc. ("Pyramid" or the "Company") is involved in exploration, development and production of petroleum and natural gas in Canada and the United States. These unaudited interim consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries. All inter-company balances and transactions have been eliminated upon consolidation.

The unaudited interim financial statements of the Company have been prepared by management following the same accounting policies and methods of computation as the audited consolidated financial statements of the Company for the year ended December 31, 2006, except that certain disclosures have been condensed or omitted. In this regard, these interim financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto for the year ended December 31, 2006.

These unaudited interim financial statements are stated in United States dollars and have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP"). The preparation of interim financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the period. Actual results could differ from these estimates. The financial statements have, in management's opinion, been properly prepared using careful judgment within reasonable limits of materiality and within the framework of the significant accounting policies.

The operating results for the three and nine months ended September 30, 2007 may not be indicative of the results for the year ended December 31, 2007.

2. Functional and Reporting Currency

Effective April 1, 2007, the Company changed its functional currency from the Canadian dollar to the U.S. dollar. This change was made as a result of the acquisition of MC Offshore Petroleum, LLC (see note 4) with its activities of capital expenditures, revenues and expenses denominated in U.S. dollars becoming the predominant currency for the Company's cash flows. Following the change of functional currency to the U.S. dollar, the Company also changed its reporting currency to the U.S. dollar effective April 1, 2007. Financial statements for all periods presented have been translated into U.S. dollars (the functional and reporting currency). All comparative financial information being presented has been restated to reflect the Company's financial statements as if they have been historically reported in U.S. dollars. As all necessary historical information was readily available, the Company has used the temporal method to effect the change in the reporting currency. The Company continues to use the temporal method for the calculation of foreign currency translation related to activities denominated in a foreign currency, which is now the Canadian dollar. Under the temporal method, monetary items are translated at the rate of exchange at the balance sheet date; non-monetary items are translated at historical exchange rates and income and expense items are translated at the rate in effect on the transaction date. The related translation gains and losses are reflected in the consolidated statement of loss for the period.

Pyramid Petroleum, Inc.
Notes to Interim Consolidated Financial Statements
September 30, 2007
(unaudited)

Stated in U.S. Dollars

3. Changes in Accounting Policies

On January 1, 2007, the Company adopted the new or revised Canadian accounting standards for accounting changes, comprehensive income, financial instruments—recognition and measurement and financial instruments—presentation and disclosures. Prior periods have not been restated. Additional disclosure requirements for financial instruments have been approved by the Canadian Institute of Chartered Accountants and will be required disclosure beginning January 1, 2008.

At January 1, 2007, the following adjustments were made to the balance sheet to adopt the new standards:

| | | January 1 2007 |
|------------------------------------|----|-------------------|
| Deficit – increase | \$ | 21,965 |
| Deferred financing fees – decrease | | 21,965 |

(a) Accounting changes

Voluntary changes in accounting policies are permitted only if they result in financial statements which provide more reliable and relevant information. Accounting policy changes are applied retrospectively unless it is impracticable to determine the period or cumulative impact of the change. Corrections of prior period errors are applied retrospectively and change in accounting estimates are applied prospectively by including the effect of the change in earnings.

(b) Financial instruments—recognition and measurement

This new standard requires all financial instruments within its scope, including all derivatives, to be recognized on the balance sheet initially at fair value. Subsequent measurement of all financial assets and liabilities except those held-for-trading and available for sale are measured at amortized cost determined using the effective interest rate method. Held-for-trading financial assets and liabilities are measured at fair value with changes in fair value recognized in earnings. Loans and receivable financial assets and other financial liabilities are measured at cost or amortized cost if interest-bearing. Available-for-sale financial assets are measured at fair value with changes in fair value recognized in comprehensive income and reclassified to earnings when derecognized or impaired. Changes to the measurement of existing financial assets and liabilities at the date of adoption were adjusted to either opening deficit or opening accumulated other comprehensive income as noted above.

The Company has classified its financial assets and liabilities as follows:

| <u>Held-for-trading</u> | <u>Loans and receivables</u> | <u>Other liabilities</u> |
|---------------------------|------------------------------|--|
| Cash and cash equivalents | Accounts receivable | Accounts payable and accrued liabilities |
| | Bond collateral | Deferred payment |
| | Acquisition deposit | Demand loan |
| | | Loans payable |
| | | Due to related parties |
| | | Convertible debentures |

(c) Comprehensive income

Comprehensive income is the change in shareholders' equity during a period from transactions and other events and circumstances from non-owner sources and includes unrealized gains and losses on financial assets classified as held available-for-sale. When related amounts are recorded in accordance with this new standard, the Company will report a consolidated statement of comprehensive income combined with the consolidated statement of operations and a new category, accumulated other comprehensive income, in the shareholders' equity section of the consolidated balance sheet.

Stated in U.S. Dollars

3. Changes in Accounting Policies (continued)

(d) Derivative instruments

The Company may use various types of derivative financial instruments to manage risks associated with crude oil and natural gas price fluctuations. These instruments are not used for trading or speculative purposes. Proceeds and costs realized from holding the related contracts are recognized in petroleum and natural gas revenues at the time that each transaction under a contract is settled. For the unrealized portion of such contracts, the Company utilizes the fair value method of accounting.

The fair value is based on an estimate of the amounts that would have been paid to or received from counterparts to settle these instruments given future market prices and other relevant factors. The method requires the fair value of the derivative financial instruments to be recorded at each balance sheet date with the unrealized gains or losses on these contracts recorded through the consolidated statement of operations.

The Company has elected to account for its commodity sales and other non-financial contracts, which were entered into and continue to be held for the purpose of receipt or delivery of non-financial items in accordance with its expected purchase, sale or usage requirements as executory contracts on an accrual basis rather than as non-financial derivatives. Prior to adoption of the new standards, physical receipt and delivery contracts did not fall within the scope of the definition of a financial instrument and were also accounted for as executory contracts.

(e) Transaction costs

Transaction costs attributable to financial instruments classified as other than held-for-trading are expensed in the consolidated statement of loss as incurred. Prior to January 1, 2007, transaction costs were recorded as a deferred charge and recognized in the consolidated statement of operations on a straight-line basis over the term of the financial instrument. On adoption, previously deferred transaction costs were recognized as if they had been expensed in the year incurred through an adjustment to the Company's opening deficit.

(f) Effective interest rate method

Financing fees and transaction costs attributable to financial instruments classified as other than held-for-trading such as convertible debentures are included in the recognized amount of the related financial instrument and recognized over the term of the financial instrument. Prior to January 1, 2007, financing fees and transaction costs were recorded as a deferred charge and recognized in the consolidated statement of operations on a straight-line basis over the life of the financial instrument. On adoption, financing fees and transaction costs are recognized as if the effective interest rate method had always been applied whereby the amount recognized varies over the life of the financial instrument based on the principal outstanding.

4. Acquisition

On April 1, 2007, the Company acquired a 20% membership share interest in a Limited Liability Corporation (the "LLC") for \$400,000 and an additional 30% membership share interest for \$600,000 on May 17, 2007. The LLC was organized for the purpose of acquiring an interest in certain petroleum and natural gas properties located in the Gulf of Mexico (the "Gulf of Mexico properties") from an arms length party (the "Seller"). A company controlled by an Officer and Director of the Company acted as an agent in the organization of the LLC and the acquisition of properties and has retained an option to buy up to 3.5% of the LLC's membership shares at the Company's cost. This option expires on May 17, 2008.

Pyramid Petroleum, Inc.
Notes to Interim Consolidated Financial Statements
September 30, 2007
(unaudited)

Stated in U.S. Dollars

4. Acquisition (continued)

The acquisition of the 50% membership interest in the LLC is an arms-length acquisition accounted for by the purchase method with the Company deemed the acquirer and measured at the exchange amount based on the total \$1,000,000 cash consideration. As the LLC is controlled and operated jointly by the members, the acquisition is considered to be the acquisition of an interest in a joint venture whereby only the Company's proportionate interest in the LLC is consolidated.

The allocation of the purchase price based on the fair values of the Company's 50% share of the assets acquired and liabilities assumed is as follows:

| | | |
|-----------------------------|----|--------------------|
| Cash | \$ | 457,533 |
| Other current assets | | 408,368 |
| Property and equipment | | 16,222,072 |
| Bond collateral (note 6) | | 4,985,412 |
| Loan payable | | (12,649,982) |
| Current liabilities | | (1,586,275) |
| Asset retirement obligation | | <u>(6,837,128)</u> |
| Net assets acquired | \$ | <u>1,000,000</u> |
| | | |
| <u>Purchase price</u> | | |
| Cash | \$ | <u>1,000,000</u> |

Included in the current liabilities assumed pursuant to the acquisition is a deferred payment of \$1,250,000 related to the LLC's purchase of the Gulf of Mexico properties and payable on March 31, 2008.

The interim consolidated statements of operations and deficit and cash flows include the results of the LLC from the dates of acquisition.

Management is still completing its review of the net assets acquired and therefore the purchase equation is subject to change based on the final determination of assets acquired and liabilities assumed. Final exchange acceptance of this transaction is pending until the Company can provide an engineering reserve report that complies with National Instrument 51-101.

5. Property and Equipment

| September 30, 2007 | Cost | Accumulated depletion, depreciation and impairment | Net book value |
|--------------------------------------|----------------------|---|----------------------|
| Petroleum and natural gas properties | | | |
| Producing | \$ 33,612,632 | \$ 4,704,766 | \$ 28,907,866 |
| Undeveloped | <u>139,336</u> | <u>—</u> | <u>139,336</u> |
| | <u>\$ 33,751,968</u> | <u>\$ 4,704,766</u> | <u>\$ 29,047,202</u> |

Pyramid Petroleum, Inc.
Notes to Interim Consolidated Financial Statements
September 30, 2007
(unaudited)

Stated in U.S. Dollars

5. Property and Equipment (continued)

| December 31, 2006 | Cost | Accumulated depletion, depreciation and impairment | Net book value |
|--------------------------------------|----------------------|---|----------------------|
| Petroleum and natural gas properties | | | |
| Producing | \$ 13,621,161 | \$ 2,391,825 | \$ 11,229,336 |
| Undeveloped | 87,062 | — | 87,062 |
| | <u>\$ 13,708,223</u> | <u>\$ 2,391,825</u> | <u>\$ 11,316,398</u> |

Acquisitions in the Gulf of Mexico (note 4) in the amount of \$16,222,072 were added during the nine months ended September 30, 2007. No general and administrative costs were capitalized to the Company's petroleum and natural gas properties during the first nine months of 2007. The calculation of 2007 depletion and depreciation included an estimated \$6,717,930 for future development capital costs associated with proved undeveloped reserves and excluded the cost of unproved properties of \$139,336 and discounted salvage value of \$2,106,808.

6. Bond Collateral

Bond collateral in the amount of \$4,985,412 as at September 30, 2007 relates to the Company's share of cash collateral for performance bonds (the "Bonds") provided by the LLC to certain regulatory authorities and to the Seller of the Gulf of Mexico properties as a guarantee for plugging and abandonment liabilities. The LLC obtained the Bonds through a surety company which required the LLC to put up cash collateral. The Bonds will be released once the subject properties are abandoned at which time all cash collateral will be returned to the LLC. The fair value of this amount has not been disclosed as the cash flow stream is not determinable.

The Company's partner in the LLC has provided a corporate guarantee of \$1,500,000 to the surety company as additional security of the Bonds and is charging the Company a fee of 10% on the guarantee amount.

7. Acquisition Deposit

On September 19, 2007 the Company signed a Purchase and Sale Agreement to acquire AMCO Energy, Inc. ("AMCO"), a wholly owned subsidiary of Capco Energy, Inc., a corporation controlled by an Officer and Director of the Company. The purchase price is \$11,000,000 and is subject to adjustments for working capital and credit of net operating income from January 1, 2007 to the closing date. Upon signing, the Company paid a cash deposit of \$200,000. The balance of the purchase price will be made at closing, which is expected on or before December 31, 2007. The transaction is subject to all customary regulatory approvals.

Pyramid Petroleum, Inc.
Notes to Interim Consolidated Financial Statements
September 30, 2007
(unaudited)

Stated in U.S. Dollars

8. Demand Loan

On April 18, 2007, the Company obtained a revolving one year demand loan facility from a Canadian bank to a maximum of Can\$4,000,000. The Company used the facility to repay the loan due to the operator of the Montana and Alberta properties, as described in note 9(a), and to repay the amount due to an Officer and Director of the Company for the purchase on October 2006 of a working interest in the Montana and Alberta properties, as described in note 9(b). The interest on the loan is calculated at the bank's prime rate plus 0.5%. The current prime rate is set at 6.25%. The loan is collateralized by a charge over the Company's Montana and Alberta assets. As at September 30, 2007, the Company had drawn \$3,995,670 (Cdn\$3,975,000) on the facility.

9. Loans Payable

- (a) At December 31, 2006, the Company owed \$2,282,073 to a lender, who is also the operator of the Company's assets in Montana and Alberta that were acquired as part of the Company's Qualifying Transaction. Under the terms of a trust agreement, the operator held title to the petroleum and natural gas properties as collateral for the obligations assumed on acquisition. In April 2007, the Company repaid the loan at which time the legal title to the properties was transferred to the Company.
- (b) In conjunction with the acquisition described in note 4, the Company assumed a term note (the "Note") in the amount of \$12,649,982 comprised of \$12,559,898 principal plus \$90,084 of interest accrued to the dates of acquisition.

The Note bears annual interest at 10% rate and is collateralized by the petroleum and natural gas assets in the Gulf of Mexico held by the LLC and for which the LLC members have pledged their member share certificates to the lender. Principal and accrued interest on the Note are repayable by the LLC in consecutive principal installments of 80% of the monthly net proceeds (revenue less royalties, net profits interests and direct operating expenses) from the related Gulf of Mexico properties to be not less than \$1,000,000 in principal per month plus accrued interest commencing on May 31, 2007 or at the discretion of the lender.

The \$11,559,898 balance of the Note at September 30, 2007 is comprised of the original principal amount of \$12,559,898 less \$1,000,000 of principal installments made during the period. In addition to the principal installments, the Company paid \$647,117 of interest due and payable up to September 30, 2007. The current portion of the loan payable is has been reported at \$6,000,000 based on the Company's 50% share of the minimum principal requirement.

10. Due to Related Parties

- (a) Due to a related company

As at September 30, 2007, the Company owed \$838,604 to a company controlled by an Officer and Director of the Company related to amounts incurred by the related company on behalf of the Company. The amount is unsecured and non-interest bearing with no fixed terms of repayment. The liability has been classified as current as the Company expects to repay the amount within one year from September 30, 2007.

Pyramid Petroleum, Inc.
Notes to Interim Consolidated Financial Statements
September 30, 2007
(unaudited)

Stated in U.S. Dollars

10. Due to Related Parties (continued)

(b) Due to a related company

At September 30, 2007, the Company owed \$934,566 to the operator of the Gulf of Mexico properties, who is a related party controlled by an Officer and Director of the Company. The loan was incurred as a result of the prorated allocation of the debt from the operator's bank at the time of certain assets acquired in the year 2006. The Company is not a party to the credit agreement between the operator and the bank. Under the terms of the agreement with the operator, the operator holds title to the subject properties as collateral for the obligations assumed. This entire obligation is estimated to be current, as full payment is expected within one year from September 30, 2007, based on the current estimates of production and net operating revenue.

(c) Due to an Officer and Director of the Company

The Company owed a note payable to an Officer and Director of the Company for the payment made by the Officer and Director in relation to the Gulf of Mexico properties acquired in 2006. The amount of the note payable is \$524,774. The amount is due in full on March 31, 2008 and bears a fixed interest rate of 8% per annum. The Company has not provided any collateral related to this note. Further, the Company owed a second note payable to an Officer and Director of the Company with regards to acquisition of certain petroleum and natural gas properties in Montana and Alberta. The amount of the note payable was \$600,000. The note was paid in full in April 2007 along with the other loan payable associated with those properties (note 7).

11. Convertible Debentures

In February and April 2007, the Company completed the private placement of convertible debentures (the "Debentures") for a total gross proceeds of \$828,022 (Cdn \$952,000). The Debentures have a two year term and bear an interest rate of 12% per annum, payable quarterly. Debenture holders have the option to convert the debentures to common shares of the Company on the basis of one common share for each \$0.453 (Cdn \$0.45) of principal at any time during the term of the Debentures. The Company has an option to call the Debentures at any time after the first anniversary of the closing date if the Company's shares trade at over \$0.678 (Cdn \$0.675) per share for a period of 30 days. 2,115,556 common shares are issuable in the event that the total amount of principal is converted at maturity.

At the private placement dates, the total liability component of the Debentures was been estimated at \$795,046 (Cdn \$914,140) based on the present value of principal and interest with the residual amount of \$32,976 (Cdn \$37,860) ascribed to the equity component.

In conjunction with the Debenture private placement, the Company issued 65,644 broker warrants exercisable at \$0.453 (Can \$0.45) per share for a term of two years. The fair value of the warrants has been estimated at \$17,681 (Cdn \$20,300) using the Black-Scholes pricing model based on 182% expected volatility, 3.9% risk-free rate, nil dividend yield, a two year life. In addition, the Company incurred \$93,360 (Can \$107,186) of agent's commission, legal and other closing costs. Of these costs, \$6,693 (Can \$7,684) has been classified as share issue costs and \$104,348 (Can \$119,802) as transaction costs. Transaction costs are netted against the liability component of the Debenture and are amortized to interest expense in the consolidated statement of operations using the effective interest rate method.

Pyramid Petroleum, Inc.
Notes to Interim Consolidated Financial Statements
September 30, 2007
(unaudited)

Stated in U.S. Dollars

11. Convertible Debentures (continued)

The total \$847,488 (Can \$844,445) debt amount at September 30, 2007 is comprised of the following:

| | | |
|-------------------------------|----|----------------|
| Liability component | \$ | 795,046 |
| Unamortized transaction costs | | (68,772) |
| Accretion of equity component | | 8,866 |
| Foreign exchange | | 112,348 |
| | \$ | <u>847,488</u> |

12. Asset Retirement Obligation

A reconciliation of the Company's asset retirement obligation as at September 30, 2007 is provided below:

| | | |
|-------------------------------|----|------------------|
| Balance – December 31, 2006 | \$ | 478,130 |
| Liabilities incurred | | – |
| Liabilities acquired (note 4) | | 6,837,128 |
| Accretion | | 264,155 |
| | | <u>7,579,413</u> |
| Current portion | | <u>95,047</u> |
| Balance – September 30, 2007 | \$ | <u>7,484,366</u> |

The Company's asset retirement obligation results from net ownership interests in petroleum and natural gas assets including, platforms, well sites and gathering systems. The Company estimates the total undiscounted amount of cash flows required to settle its asset retirement obligation to be approximately \$16,266,538 which will be incurred over the next 40 years, with the majority of the costs incurred between 2010 and 2020. A credit-adjusted risk-free rate of 8% percent and an inflation rate of 2% was used to estimate the fair value of the asset retirement obligation. See notes 6 and 16 with respect to bond collateral and an abandonment fund related to abandonment liabilities for the Gulf of Mexico properties.

13. Related Party Transactions

- (a) During the three and nine months ended September 30, 2007, the Company paid a total of \$37,520 and \$68,959, respectively, in interest to a related company for the loan due to the related company as in note 10.
- (b) During the three and nine months ended September 30, 2007, the Company paid a total of \$21,278 and \$67,547, respectively, in interest to an Officer and Director of the Company for the two promissory notes discussed in note 10.

Pyramid Petroleum, Inc.
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14. Equity Instruments

(a) Common shares issued

| | Number | | Amount |
|------------------------------|------------|----|-----------|
| Balance – December 31, 2006 | 36,605,095 | \$ | 7,956,809 |
| Exercise of broker warrants | 687,500 | | 175,137 |
| Share issue costs (note 10) | – | | (6,693) |
| Balance – September 30, 2007 | 37,292,595 | \$ | 8,125,253 |

During the nine months ended, 687,500 common shares were issued on the exercise of the same number of warrants for cash proceeds of \$131,591 (Cdn \$137,500) plus \$43,546 for the pro-rata allocation of the warrants' fair value.

(b) Shares held in escrow

The initial 5,000,000 common shares issued to the Company's founders and the 24,095,720 common shares issued with regard to the Qualifying Transaction are subject to certain escrow requirements restricting release of the shares over a 36 month period subsequent to the completion of the Qualifying Transaction. To date a total of 11,638,288 shares have been released from the escrow. At September 30, 2007 a total of 17,457,432 common shares remained in escrow. The following table outlines the future releases.

| Release Date | November 11, 2007 | May 11, 2008 | November 11, 2008 | May 11, 2009 |
|------------------|----------------------|-----------------|----------------------|-----------------|
| Number of shares | 4,364,358 | 4,364,358 | 4,364,358 | 4,364,358 |

(c) Broker warrants

| | Number of warrants | Weighted average exercise price | | Weighted average life remaining (years) |
|------------------------------|-----------------------|------------------------------------|---------|--|
| | | US \$ | Cdn \$ | |
| Balance – December 31, 2006 | 740,625 | \$ 0.20 | \$ 0.20 | 0.05 |
| Issued (note 9) | 65,644 | 0.45 | 0.45 | 1.42 |
| Exercised | (687,500) | 0.20 | 0.20 | 0.05 |
| Balance – September 30, 2007 | 118,769 | \$ 0.34 | \$ 0.34 | 1.24 |

(d) Stock options

As at December 31, 2006 and September 30, 2007, the Company had 900,000 stock options outstanding and exercisable an exercise price of \$0.30 (Cdn \$0.30) per share, expiring on May 4, 2011.

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15. Contributed Surplus

| | | |
|--|----|-----------------|
| Balance – December 31, 2006 | \$ | 183,323 |
| Broker warrants (note 9) | | 17,681 |
| Exercise of broker warrants (note 13(a)) | | <u>(43,546)</u> |
| Balance – September 30, 2007 | \$ | <u>157,458</u> |

16. Commodity Contracts

The Company has participated, through the operator, in financial swaps for the gas production from the Gulf of Mexico with December 31, 2007 settlement dates. The Company has accounted for these contracts based on their mark-to-market on the balance sheet date which is based on quoted prices, or in their absence, third party market indicators and forecasts. At September 30, 2007, the Company has entered into the following financial forward arrangements:

| | Quantity (MMBTU) | Price (\$/MMBTU) | Mark-to-market value |
|------------------|---------------------|---------------------|-------------------------|
| Sales contracts: | | | |
| Gas | 23,115 | 7.075 | \$ 2,211 |
| Gas | 23,115 | 7.525 | 12,560 |
| Gas | 16,080 | 8.100 | 18,067 |
| Oil | 100,000 | 64.030 | <u>(106,773)</u> |
| | | | <u>\$ (73,936)</u> |

The changes in the fair value associated with the above financial instruments result in an unrealized gain or loss on the commodity contracts. Monthly settlements with counterparties result in realized gains or losses. These amounts are recognized together as commodity contracts revenue in the consolidated statement of operations.

As of September 30, 2007 the mark-to-market balances for the Company's share of these swap contracts resulted in an unrealized loss of \$73,936 which is included in accounts payable (December 31, 2006 – \$75,965 unrealized gain included in accounts receivable). During the three and nine months ended September 30, 2007, the Company recognized a realized gain of \$8,237 and \$83,346, respectively (three and nine months ended September 30, 2006 – nil as no contracts in place) on these instruments.

17. Commitment

The Company is required to contribute 20% of the monthly net profits from the properties owned through the LLC towards an abandonment fund (the "Fund") established by the Seller as an additional guarantee against the plugging and abandonment liabilities associated with the properties.

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17. Commitment (continued)

Net profits is defined in the Fund agreement as: the monies and revenues payable from gross production of the properties less (i) costs and expenses incurred attributed to the properties with respect to all existing wells located on the properties, including but not limited to the costs and expenses of operating the wells and for producing, treating and storing production from the wells; (ii) capital expenditures related to the properties; (iii) certain taxes assessed against production relating to the property; and (iv) all royalty burdens and other lease burdens affecting the properties. Where the net profit for a particular month is determined to be negative (a net loss), no contribution to the Fund is required for the related month.

Contributions to the Fund commence in March 2008. The Company's maximum amount of contribution to the Fund is \$5,000,000. Upon satisfactory performance of plugging and abandonment obligations, the Company may request a release of the bonding amount (note 6) and funds may be withdrawn from the Fund to maximum of the Fund balance.

18. Change in Non-cash Working Capital

| | Three months ended September 30 | | Nine months ended September 30 | |
|--|---------------------------------|--------------------|--------------------------------|---------------------|
| | 2007 | 2006 | 2007 | 2006 |
| Accounts receivable | \$ (230,942) | \$ - | \$ (2,313,721) | \$ - |
| Prepaid expenses | (161,668) | (14,525) | (80,394) | (125,663) |
| Accounts payable and accrued liabilities | 942,767 | (48,343) | 2,220,702 | (34,332) |
| | <u>\$ 550,157</u> | <u>\$ (62,868)</u> | <u>\$ (173,413)</u> | <u>\$ (159,995)</u> |

The change in non-cash working capital has been allocated to the following activities:

| | Three months ended September 30 | | Nine months ended September 30 | |
|-----------|---------------------------------|--------------------|--------------------------------|---------------------|
| | 2007 | 2006 | 2007 | 2006 |
| Operating | \$ (349,423) | \$ (62,868) | \$ (1,284,456) | \$ (159,995) |
| Financing | (211,463) | - | - | - |
| Investing | 1,111,043 | - | 1,111,043 | - |
| | <u>\$ 550,157</u> | <u>\$ (62,868)</u> | <u>\$ (173,413)</u> | <u>\$ (159,995)</u> |

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19. Segmented Information

The Company's only industry segment is the exploration for and development and production of oil and natural gas. The Company undertakes exploration and development of petroleum and natural gas properties in Canada and the United States. The following tables set forth the geographical segments of the Company's operations between Canada and the United States.

| | Three months ended September 30, 2007 | | | Nine months ended September 30, 2007 | | |
|---|--|------------------|------------|---|------------------|------------|
| | Canada | United States | Total | Canada | United States | Total |
| | \$ | \$ | \$ | \$ | \$ | \$ |
| Revenues, net of royalties | 17,139 | 6,370,810 | 6,387,949 | 62,406 | 10,131,343 | 10,193,749 |
| Net income (loss) | (170,097) | 567,331 | 397,234 | (820,012) | 1,776,637 | 956,355 |
| Per share | | | | | | |
| - Basic and diluted | - | 0.01 | 0.01 | (0.02) | 0.05 | 0.03 |
| Total assets | 662,518 | 37,099,253 | 37,761,771 | 662,518 | 37,099,253 | 37,761,771 |
| Property and equipment | 629,679 | 28,417,523 | 29,047,202 | 629,679 | 28,417,523 | 29,047,202 |
| Expenditures on property and equipment | 412,619 | 2,016,118 | 2,428,737 | 412,619 | 3,409,504 | 3,821,673 |
| | | | | | | |
| | Three months ended September 30, 2006 | | | Nine months ended September 30, 2006 | | |
| | Canada | United States | Total | Canada | United States | Total |
| | \$ | \$ | \$ | \$ | \$ | \$ |
| Revenues, net of royalties | - | 594,732 | 594,732 | 3,465 | 799,404 | 802,869 |
| Net income (loss) | (62,109) | 88,569 | 26,460 | (141,630) | 66,524 | (75,106) |
| Per share | | | | | | |
| - Basic and diluted | - | - | - | - | - | - |
| Total assets | 122,819 | 12,735,631 | 12,858,450 | 122,819 | 12,735,631 | 12,858,450 |
| Property and equipment | 86,157 | 12,613,759 | 12,699,916 | 86,157 | 12,613,759 | 12,699,916 |
| Expenditures on property and equipment | 84,449 | 185,616 | 270,065 | 86,157 | 338,171 | 424,328 |