

## notice to reader

The accompanying unaudited interim consolidated financial statements of Questerre Energy Corporation for the three months ended March 31, 2006 have been prepared by management and approved by the Audit Committee and the Board of Directors of the Corporation. These statements have not been reviewed by the Corporation's external auditors.



Michael Binnion  
*President and Chief Executive Officer*



Jason D'Silva  
*Vice President, Finance*

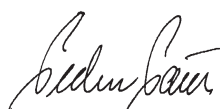
Calgary, Alberta, Canada  
*May 10, 2006*

## consolidated balance sheets

	March 31 2006 <i>(unaudited)</i>	December 31 2005
<b>Assets</b>		
Current assets		
Cash	\$ 11,322,663	\$ 9,296,160
Marketable Securities (note 4)	517,721	499,311
Accounts Receivable	2,025,909	1,533,354
Inventory	224,546	92,925
Deposits and cash calls paid	237,564	32,064
	<b>14,328,403</b>	11,453,814
Restricted cash (note 5)	100,000	100,000
Petroleum and natural gas properties – net of accumulated depletion and depreciation (note 2)	20,839,191	14,638,949
	<b>\$ 35,267,594</b>	\$ 26,192,763
<b>Liabilities</b>		
Current liabilities		
Accounts payable and accrued liabilities	\$ 3,992,318	\$ 1,597,584
Bank loan (note 5)	134,000	154,100
	<b>4,126,318</b>	1,751,684
Asset retirement obligation (note 3)	2,459,582	2,271,192
	<b>6,585,900</b>	4,022,876
<b>Shareholders' Equity</b>		
Common shares (note 7)	56,083,011	49,268,507
Contributed surplus (note 7)	1,036,925	739,640
Deficit	(28,438,242)	(27,838,260)
	<b>28,681,694</b>	22,169,887
	<b>\$ 35,267,594</b>	\$ 26,192,763

See accompanying notes to consolidated financial statements.

Approved by the Board of Directors



Director



Director

## consolidated statements of income (loss) and deficit

(unaudited)

	For the three months ended March 31	
	2006	2005
<b>Revenue</b>		
Petroleum and natural gas revenue	\$ 1,160,597	\$ 336,781
Royalties (note 6)	(406,393)	124,468
	<b>754,204</b>	<b>461,249</b>
<b>Expenses</b>		
Operating	462,444	204,700
General and administrative	212,708	253,591
Stock-based compensation (note 7 (e))	297,286	75,335
Interest expense	3,709	17,516
Interest income	(176,610)	(4,631)
Loss on sale of marketable securities	10,480	-
Foreign exchange gain	(45,894)	-
Depletion and depreciation	581,258	1,074,048
Accretion on asset retirement obligation (note 3)	8,805	-
	<b>1,354,186</b>	<b>1,620,559</b>
<b>Net loss</b>	<b>(599,982)</b>	<b>(1,159,310)</b>
Deficit, beginning of period	(27,838,260)	(24,832,698)
<b>Deficit, end of period</b>	<b>\$ (28,438,242)</b>	<b>\$ (25,992,008)</b>
<b>Net loss per share</b>		
Basic and diluted	\$ (0.01)	\$ (0.02)

See accompanying notes to consolidated financial statements.

## consolidated statements of cash flows

(unaudited)

	For the three months ended March 31	
	2006	2005
<b>Cash provided by (used in):</b>		
<b>Operating Activities</b>		
Net loss	\$ (599,982)	\$ (1,159,310)
Items not affecting cash		
Depletion and depreciation	581,258	1,074,048
Accretion on asset retirement obligation	8,805	-
Stock-based compensation expense	297,286	75,335
	<b>287,367</b>	<b>(9,927)</b>
Deferral of crown royalties	-	(142,850)
Net change in non-cash working capital	1,142,740	(110,554)
	<b>1,429,107</b>	<b>(263,331)</b>
<b>Financing Activities</b>		
Issue of common shares	7,150,000	-
Share issue costs	(335,496)	(11,468)
Repayment of bank loan	(20,100)	(20,100)
	<b>6,794,404</b>	<b>(31,568)</b>
<b>Investing Activities</b>		
Expenditures on petroleum and natural gas properties	(6,601,918)	(2,463,039)
Net change in non-cash working capital	404,910	458,674
	<b>(6,197,008)</b>	<b>(2,004,365)</b>
Increase (decrease) in cash	2,026,503	(2,299,264)
Cash, beginning of period	9,296,160	2,701,477
<b>Cash, end of period</b>	<b>\$ 11,322,663</b>	<b>\$ 402,213</b>

See accompanying notes to consolidated financial statements.

During the three months ended March 31, 2006, the Company paid \$3,709 (2005 – \$17,516) of interest and did not pay any cash taxes in 2006 and 2005.

# notes to the consolidated financial statements

For the years ended March 31, 2006 (unaudited)

The interim consolidated financial statements include the accounts of Questerre Energy Corporation and its subsidiaries ("Questerre" or "the Company") and have been prepared by management in accordance with Canadian Generally Accepted Accounting Principles. The interim consolidated financial statements are unaudited and have not been subject to review by the Company's external auditors. The interim financial statements have been prepared following the same accounting policies and methods of computation as the consolidated financial statements for the fiscal year ended December 31, 2005. Certain comparative figures have been reclassified to conform with the presentation adopted in the current year. The disclosure which follows is incremental to the disclosure included with the annual consolidated financial statements. These interim consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto in the Company's annual report for the year ended December 31, 2005.

## 1. NATURE OF OPERATIONS AND BASIS OF PRESENTATION

Questerre Energy Corporation ("Questerre" or the "Company") is primarily involved in the exploration and development of naturally fractured and hydrothermally dolomitized reservoirs. The Company has two primary projects – the Beaver River Field in British Columbia and the St. Lawrence Lowlands in Quebec. To mitigate the risks associated with these primary projects, the Company has secured partners to assist in the development of these projects.

The Company has also developed a portfolio of conventional exploration and production assets in five areas in Central and Southern Alberta – Westlock, Hector, Vulcan, Parkland and Drumheller.

## 2. CAPITAL ASSETS

	March 31 2006	December 31 2005
Petroleum and natural gas properties (net of accumulated depletion and depreciation)		
Alberta	\$ 15,271,149	\$ 9,374,442
British Columbia	3,739,935	3,458,224
Quebec	1,828,107	1,806,283
	<b>\$ 20,839,191</b>	<b>\$ 14,638,949</b>

During the three months ended March 31, 2006, the Company capitalized administrative overhead charges of \$306,869 (December 31, 2005 - \$415,957) relating to exploration and development activities.

The Company did not incur a ceiling test writedown for the three months ended March 31, 2006 (December 31, 2005 – \$1.31 million).

As at March 31, 2006, petroleum and natural gas properties included \$4.78 million (December 31, 2005 – \$6.13 million) relating to unproved properties that have been excluded from the depletion and depreciation calculation. All costs associated with the Beaver River Field, net of estimated salvage values, have been written down and included in depletion expense except \$2.95 million of seismic costs. These costs primarily relate to the 3-D seismic survey acquired over the Field in 2002 and have continuing value to the Company.

Questerre also does not include costs of \$1.83 million associated with its St. Lawrence Lowlands acreage in Quebec in the calculation of depletion or in costs subject to the ceiling test calculation. The Company's assets in Quebec remain unproved at March 31, 2006.

### 3. ASSET RETIREMENT OBLIGATION

The total future asset retirement obligation was estimated by management based on Questerre's net ownership interest in all wells and facilities, estimated costs to reclaim and abandon wells and facilities and the estimated timing of the costs to be incurred in future periods. The Company estimates its total undiscounted asset retirement obligations to be \$2,727,089 at March 31, 2006. Questerre uses a credit adjusted risk free rate of seven percent and an inflation rate of three percent over the varying lives of the assets to calculate the present value of the asset retirement obligation.

The following table provides a reconciliation of the Company's total asset retirement obligation:

	<b>March 31 2006</b>	December 31 2005
Balance, beginning of period	\$ 2,271,192	\$ 1,848,503
Increase in estimate of obligation	179,585	265,629
Accretion expense	8,805	157,060
Balance, end of period	\$ 2,459,582	\$ 2,271,192

### 4. MARKETABLE SECURITIES

As at March 31, 2006, the Company holds marketable securities with a market value of \$703,000. (December 31, 2005: \$546,120). The Company realized a loss of \$10,480 on the disposition of a portion of these securities during the first quarter of 2006.

### 5. BANK INDEBTEDNESS

In July 2002, the Company obtained a five-year, \$400,000 term loan with a Canadian bank. Under the terms of the loan, the Company must make monthly payments of \$6,700 principal plus interest until the loan is paid out. The interest rate under the loan is the bank's floating base rate plus 2.0% and the Company may lock in the rate at any time. The loan is secured by the first assignment to the bank of a \$100,000 Guaranteed Investment Certificate and by a General Security Agreement over the assets of the Company and its wholly owned subsidiary, Questerre Beaver River Inc. Financial covenants include maintaining a minimum long-term debt to tangible equity ratio of 0.8 to 1.0 and maintaining a working capital ratio of at least 1.0 to 1.0.

While Questerre currently meets this financial covenant, the Company has not been in compliance with this covenant in the past, and, therefore, the bank loan has been classified as a current liability.

### 6. DEFERRED CROWN ROYALTIES

The Company accrued Crown royalties of \$0.14 million for the year ended December 31, 2004 on production from the Beaver River Field during the second half of 2004. Payment of this royalty was contingent on the Company reaching an agreement with the Ministry of Energy and Mines in British Columbia regarding its qualification for a deep royalty credit in the amount of \$2.2 million.

In March 2005, the Company received confirmation from the Ministry of Energy and Mines in British Columbia that it qualified for a re-entry royalty credit in the amount of \$0.75 million. The Company has since recorded a recovery of the accrued Crown royalties of \$0.14 million.

## 7. SHARE CAPITAL

### a) Authorized

The Company is authorized to issue an unlimited number of Class A common voting shares. The Company is also authorized to issue an unlimited number of Class B common voting shares and an unlimited number of preferred shares, issuable in one or more series. At March 31, 2006, there were no Class B common voting shares or preferred shares outstanding.

### b) Issued and outstanding -- Class A common shares and common share warrants

	Number	Amount
<b>Common Shares</b>		
Balance, December 31, 2005	113,014,594	\$ 49,268,507
Issued for cash	11,000,000	7,150,000
Share issue costs	-	(353,496)
<b>Balance, March 31, 2006</b>	<b>124,014,594</b>	<b>\$ 56,083,011</b>

### c) Per share amounts

The following table summarizes the weighted average common shares used in calculating net income (loss) per common share:

	For the three months ended March 31 2006	2005
Basic	<b>117,536,816</b>	66,751,904
Diluted	<b>121,338,700</b>	68,520,083

The reconciling item between the basic and diluted average common shares is stock options.

### d) Stock options

The Company has a stock option plan that provides for the issuance of options to its directors, officers and employees at or above market prices. The stock options granted under the plan vest evenly over a three-year period and expire five years from the date of grant.

The following table sets forth a reconciliation of the stock option plan activity for the three months ended March 31, 2006:

	Number of Options	Weighted Avg Exercise Price
Outstanding, December 31, 2005	9,205,000	\$ 0.44
Granted	1,080,000	0.65
Cancelled	(70,000)	0.82
<b>Outstanding, March 31, 2006</b>	<b>10,215,000</b>	<b>0.46</b>
<b>Exercisable, March 31, 2006</b>	<b>2,745,833</b>	<b>\$ 0.33</b>

The outstanding options have a range of exercise prices between \$0.10 per share and \$1.00 per share, and a weighted average number of years to expiry of 4.1. The exercisable options have a range of exercise prices between \$0.10 and \$1.00 per share and have a weighted average number of years to expiry of 3.9.

*e) Stock-based compensation costs*

The Company accounts for its stock based compensation plan using the fair value method. Under this method, compensation cost attributable to share options granted to employees or directors is measured at fair value at the grant date and expensed over the expected exercise time frame with a corresponding increase to contributed surplus.

The fair value of each option granted is estimated in the date of grant using the Black-Scholes option pricing model with weighted average assumptions for grants as follows:

	For the three months ended March 31	
	2006	2005
Weighted average fair value per option	\$ 0.26	\$ 0.13
Risk free interest rate (%)	3.0	3.0
Expected life (years)	3.0	3.0
Expected volatility (%)	113.0	166.0

*f) Contributed surplus*

The following table sets forth a reconciliation of contributed surplus for the three months ended March 31, 2006:

Balance, December 31, 2005	\$ 739,640
Stock-based compensation expense	297,285
<b>Balance, March 31, 2006</b>	<b>\$ 1,036,925</b>

## 8. RELATED PARTY TRANSACTIONS

At March 31, 2006, Questerre had amounts owing to Terrenex totalling \$771 (2005 – \$89,812). All of the Directors of Terrenex serve as directors or officers of Questerre.

Questerre incurred fees of \$31,500 for the three months ended March 31, 2006 (2005 –\$31,500) to a company with common directors and officers. The transactions were in the normal course of business paid pursuant to an Office Rental Agreement for the provision of office space, office equipment and support personnel. The agreement may be terminated by either party with six months written notice.

## 9. SUBSEQUENT EVENTS

In April 2006, the Company completed the acquisition of a private exploration and production company with production and exploration acreage in the Westlock area of Central Alberta. The purchase price for the acquisition, net of any working capital adjustments was \$3 million and 7,262,742 Common Shares.