

## MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A") was prepared on August 11, 2008. This MD&A is provided by Management of Questerre Energy Corporation ("Questerre" or the "Company") to review second quarter 2008 activities and results as compared to the same period in the prior year. This MD&A should be read in conjunction with the unaudited interim consolidated financial statements for the six months ended June 30, 2008 and the audited consolidated financial statements for the year ended December 31, 2007.

Questerre is a junior oil & gas company involved in the exploration and development of scalable high-impact projects. To mitigate the risks associated with these projects, the Company has secured partners to assist in their development. To further diversify risk, the Company continues to develop a portfolio of conventional exploration and production assets.

The Company's common shares are listed on the Toronto Stock Exchange and Oslo Stock Exchange under the symbol "QEC".

### Forward Looking Statements

This MD&A contains forward-looking statements. Management's assessment of future plans and operations, production estimates, drilling inventory and wells to be drilled, timing of drilling and tie in of wells, productive capacity of new wells, capital expenditures and the timing thereof, may constitute forward-looking statements under applicable securities laws and necessarily involve risks including, without limitation, 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, the timing and length of plant turnarounds and the impact of such turnarounds and the timing thereof, delays resulting from or inability to obtain required regulatory approvals and ability to access sufficient capital from internal and external sources. As a consequence, the Company's actual results could differ materially from those expressed in, or implied by, the forward-looking statements. Readers are cautioned that the foregoing list of factors is not exhaustive. The forward-looking statements contained in this MD&A are made as at the date of this MD&A and the Company does not undertake any obligation to update publicly or to revise any of the included forward looking statements, whether as a result of new information, future events or otherwise, except as may be required by applicable securities laws.

### Non-GAAP Terms

This document contains the terms "cash flow from operations", "netbacks", "working capital" and "average sales price" which are non-GAAP terms. The Company uses these measures to help evaluate its performance. The Company considers netbacks a key measure as it demonstrates its profitability relative to current commodity prices and its ability to generate cash flow to fund future growth through capital investment and repay any debt outstanding. As an indicator of Questerre's performance, cash flow from operations should not be considered as an alternative to, or more meaningful than, cash flow from operating activities as determined in accordance with Canadian GAAP. Questerre's determination of cash flow generated from operations may not be comparable to that reported by other companies.

### BOE Conversions

Barrel of oil equivalent ("boe") amounts may be misleading, particularly if used in isolation. A boe conversion ratio has been calculated using a conversion rate of six thousand cubic feet of natural gas to one barrel of oil and is based on an energy equivalent conversion method application at the burner tip and does not necessarily represent an economic value equivalency at the wellhead.

## SELECT INFORMATION

As at/for the period ended	Three Months Ended		Six Months Ended	
	2008	2007	2008	2007
<b>Financial (\$)</b>				
Petroleum and Natural Gas Sales	<b>9,037,355</b>	6,555,860	<b>16,269,184</b>	14,058,298
Cash Flow from Operations	<b>5,138,828</b>	3,183,088	<b>9,077,952</b>	6,229,817
Per share – basic and diluted	<b>0.03</b>	0.02	<b>0.05</b>	0.04
Net Earnings (Loss)	<b>(2,670,086)</b>	980,543	<b>(2,017,885)</b>	1,774,445
Per share – basic and diluted	<b>(0.01)</b>	0.01	<b>(0.01)</b>	0.01
Capital Expenditures, net of dispositions	<b>2,952,768</b>	(5,110,576)	<b>20,817,018</b>	2,332,262
Working Capital Surplus	<b>68,450,058</b>	29,911,344	<b>68,450,058</b>	29,911,344
Total Assets	<b>160,395,379</b>	80,758,475	<b>160,395,379</b>	80,758,475
Shareholders' Equity	<b>143,603,481</b>	62,412,933	<b>143,603,481</b>	62,412,933
Common Shares Outstanding	<b>196,650,213</b>	155,207,583	<b>196,650,213</b>	155,207,583
Weighted average – basic	<b>181,275,421</b>	155,198,536	<b>175,504,676</b>	155,194,720
Weighted average – diluted	<b>181,275,421</b>	161,897,966	<b>175,504,676</b>	162,174,451
<b>Operations (units as noted)</b>				
Average Production				
Crude Oil and Natural Gas Liquids (bbl/d)	<b>310</b>	168	<b>307</b>	189
Natural Gas (mcf/d)	<b>5,590</b>	7,650	<b>5,708</b>	8,297
Total (boe/d)	<b>1,241</b>	1,443	<b>1,258</b>	1,572
Average Sales Price				
Crude Oil and Natural Gas Liquids (\$/bbl)	<b>122.92</b>	65.69	<b>109.33</b>	64.99
Natural Gas (\$/mcf)	<b>10.94</b>	7.96	<b>9.77</b>	7.86
Total (\$/boe)	<b>80.01</b>	49.91	<b>71.07</b>	49.41
Netback (\$/boe)				
Total Revenue	<b>80.01</b>	49.91	<b>71.07</b>	49.41
Royalties	<b>13.22</b>	10.61	<b>12.09</b>	12.11
Percentage	<b>16.52</b>	21.26	<b>17.01</b>	24.51
Field Operating Expense	<b>15.72</b>	11.19	<b>14.00</b>	11.09
Operating Netback	<b>51.07</b>	28.11	<b>44.98</b>	26.21
Net Cash G&A	<b>5.55</b>	4.52	<b>5.08</b>	4.97
Cash Netback	<b>45.52</b>	23.59	<b>39.90</b>	21.24
Wells Drilled				
Gross	<b>3.00</b>	2.00	<b>8.00</b>	10.00
Net	<b>1.50</b>	0.98	<b>4.50</b>	6.49

## HIGHLIGHTS

- Cash flow from operations for the quarter increased over 60% to \$5.14 million from \$3.18 million in 2007
- Significant pilot programs well underway in St. Lawrence Lowlands, Quebec
- Commenced full development in Antler, Saskatchewan after successful pilot program
- Tested 1,000 boe/d light oil well in Vulcan, southern Alberta using selective fracture stimulation
- Increased working interest in the Lowlands and acquired a seismic database through purchase of Terrenex
- Completed \$75 million equity offering

## SECOND QUARTER 2008 ACTIVITIES

### St. Lawrence Lowlands, Quebec

During the quarter, Questerre's partners, Forest Oil Corporation ("Forest") and Talisman Energy Canada ("Talisman"), announced major programs to appraise the commerciality of the shale horizons in the Lowlands.

Forest's program will primarily target the Utica shale on the Yamaska permits. The pilot program includes two horizontal wells with a four-stage fracture stimulation per well. Contingent upon final well results, Forest plans to commence full scale drilling in 2010. This follows the stimulation and testing of the St. Francois du Lac well in the first quarter. This well was one of two drilled by Questerre's partner, Gastem Inc., in 2007 targeting the Utica shale.

In addition to the Utica, Talisman's program will also target the shallower Lorraine horizon. The proposed program will include six vertical wells, ten horizontal wells and the recompletion of the Gentilly #1 well for shale gas production. Questerre expects the majority of the wells to be drilled on its acreage. Three of these vertical wells will test the deeper Trenton Black-River formation and complete Talisman's earning obligations under its farm-in agreement with the Company.

Both programs began in the third quarter of 2008 and initial results are expected prior to year-end.

### Northeast British Columbia

#### Greater Sierra

Processing and interpretation of the recently acquired 3-D seismic survey at Greater Sierra continued in the second quarter. The 46 square mile survey was designed to identify prospects in the primary Jean Marie formation as well as deeper horizons including the Keg River and Slave Point. Based on an early interpretation, the operator, EnCana Corporation, has started planning for a proposed 8 to 12 well program this winter.

#### Beaver River Field

Following the completion of the A-8 operation last quarter, work at the Beaver River Field ("Beaver River") focused on the refurbishment of infrastructure and the installation of a compressor at the A-2 wellsite. The compressor was certified operational in the third quarter. Well production increased initially from 360 boe/d to 600 boe/d with current rates of approximately 500 boe/d.

In light of recent shale gas developments, Questerre is evaluating potential recompletion candidates for the shales at Beaver River. The timing and extent of the program is dependent on equipment availability, logistics and partner participation.

## **Antler, Saskatchewan**

The summer work program at Antler in southeast Saskatchewan includes drilling four infill horizontal wells and the selective fracture stimulation of these wells and four existing wells. In the second quarter, Questerre participated in drilling three (1.5 net) infill wells.

The production profile for two horizontal wells selectively fracture stimulated this past winter continues to meet expectations with rates two to four times the unstimulated rates. Two new wells and one existing well were stimulated early in the third quarter and the results are consistent. Questerre continues to assess this stimulation technique throughout its acreage to maximize recovery of the oil in place.

Based on the 3-D seismic survey and these stimulation results, Questerre plans to expand this program to include up to eleven new wells and the stimulation of two existing horizontal wells.

## **Southern and Central Alberta**

Towards the end of the quarter, Questerre tested the first horizontal well in the oil pool at Vulcan, southern Alberta. Questerre has a 50% interest in the pool and this well.

The well was stimulated with a four-stage selective frac and initially flowed oil to surface at rates over 1,000 boe/d. On further testing with capacity constraints, the well flowed at rates of 750 bbl/d with associated gas and less than a 10% water cut. Tie-in was finalized early in the third quarter and the well placed on production at a regulatory restricted rate of 300 boe/d.

Two additional infill locations were been identified and drilling on the first location is scheduled for late in the third quarter. With receipt of Good Production Practice ("GPP") status in July, the operator is currently optimizing production from the oil pool.

## **Drilling Activities**

During the quarter, Questerre participated in the drilling of three (1.5 net) oil wells that were all cased and completed as oil wells.

## **Corporate**

### **Equity Offering**

To finance its share of the work programs in the Lowlands and Greater Sierra over the next 12 to 18 months, Questerre completed a \$75 million equity offering at \$4.70 per common share. The offering consisted of the issuance of 7.5 million common shares on a private placement basis in Norway and 8.625 million common shares through a short-form prospectus in Canada.

### **Acquisition**

Questerre completed the acquisition of Terrenex Ltd. ("Terrenex"), a related party with common directors and officers on April 28, 2008. Terrenex's principal assets were a working interest in sixteen exploration licenses and a seismic database in the St. Lawrence Lowlands and 10,698,785 common shares of Questerre.

Consideration for transaction was 18,910,403 common shares and \$500,000 in cash. Net of the pending cancellation of 10,698,785 Questerre common shares held by Terrenex, a total of 8,211,618 common shares were issued for the acquisition.

### **Restructuring**

On June 18, 2008, a wholly owned subsidiary recently acquired by Questerre, Magnus Energy Inc. ("Magnus") and its subsidiary, Magnus One Energy Corp. ("Magnus One"), sought protection under the Bankruptcy and Insolvency Act. The filing was precipitated by unsecured creditors rejecting an informal settlement proposal that was made prior to Questerre acquiring Magnus. Magnus and Magnus One expect to file formal proposals in the third quarter to settle amounts outstanding on a similar basis to the informal proposal previously made.

## PRODUCTION

Questerre's daily production averaged 1,241 boe/d during the second quarter of 2008 and 1,258 boe/d for the first six months of the year. Production levels remained relatively constant throughout the first six months of the year, decreasing marginally from first quarter production of 1,274 boe/d. By comparison to the prior year, production in the second quarter of 2007 of 1,443 boe/d and for the first six months of 1,572 boe/d was 14% and 20% higher respectively than the same periods in 2008.

The Antler assets increased Questerre's oil weighting from 11% in the first half of 2007 to approximately 25% in the first half of 2008. With the recent disposition of its medium crude oil production in Grand Forks, central Alberta, Questerre's oil production is entirely light sweet oil and natural gas liquids from Antler and Vulcan. The Company expects gas will represent approximately 70% of its product mix as oil production in these areas grows over the remainder of this year.

The development of new core areas in Antler and Greater Sierra and the profile of the Vulcan gas pool saw production from Alberta account for 642 boe/d, or just under 52% of the Company's production in the quarter. By contrast, for the second quarter of 2007, Alberta represented over 81% or 1,176 boe/d of Questerre's daily production. Vulcan remains the largest component of Alberta production at 75% or 483 boe/d in this quarter and 78% or 917 boe/d for the same period in 2007.

Second quarter 2008 production also reflects the disposition of approximately 45 boe/d from the Hector and Grand Forks areas of Alberta. As part of its planned disposition of non-core assets, Questerre expects to sell an additional 100 boe/d of Alberta production. The development of the Vulcan oil pool and receipt of GPP status for this pool are expected to mitigate these dispositions.

Production from British Columbia of 396 boe/d was nearly 32% of production in the quarter and 267 boe/d or approximately 20% of production for the second quarter of 2007. In 2008, the first two wells drilled by the Company in the Greater Sierra area contributed 141 boe/d and the A-2 and A-7 wells at Beaver River contributed the remainder or 255 boe/d.

Questerre expects production from Greater Sierra to approximate 70 boe/d as the wells stabilize. Production during the quarter at Beaver River was affected by fluctuating line pressure. Boost and wellhead compression are being optimized to minimize these disruptions in the future.

Questerre's new core area in Antler contributed 203 boe/d of light sweet oil during the second quarter and 176 boe/d in the first quarter of this year. Higher volumes in the second quarter were due to the flush production from two wells fracture stimulated in the first quarter. Questerre expects production volumes from this area to increase further as new horizontal wells are drilled and stimulated.

## SECOND QUARTER 2008 FINANCIAL RESULTS

### Revenue

For the three months ended June 30, 2008, Questerre reported petroleum and natural gas revenue of \$9.04 million. This compares to revenue of \$6.55 million for the same period in 2007 and \$7.23 million in the preceding period this year. With production levels and product mix relatively unchanged from the first quarter, the increased revenue in the second quarter was mainly due to improved commodity prices.

Natural gas prices were buoyed by improved fundamentals and higher oil prices in the quarter. The benchmark AECO daily index price in Alberta averaged \$10.22/mcf or 28% higher than the first quarter average of \$7.97/mcf. Realized prices were 8% higher than the average at \$10.94/mcf, largely due to higher quality gas from Vulcan. A narrower spread between the AECO price and the Station 2 price for Questerre's B.C. production also contributed to the improved realized price.

With increased demand from emerging economies and geopolitical issues, oil prices saw significant appreciation in the second quarter. The reference Edmonton Light price averaged \$126.06/bbl up from \$97.50/bbl in the first quarter, an increase of 29%. Questerre's net price increased proportionately from \$95.50/bbl to \$122.92/bbl. Realized prices in the quarter also included revenue from test production of the recently completed Vulcan horizontal well. This test production was sold at an approximate 30% discount to market prices due to treating and transportation costs. This production accounted for less than 7% of total volumes over the quarter.

Revenue was offset by losses on risk management activities during the quarter. Questerre realized a loss of \$0.22 million and recorded an unrealized loss of \$0.50 million during the period (2007: nil). The losses relate to a single derivative contract for 2,000 gj of daily production at \$8.45/gj from April 1 to October 31, 2008.

## **Royalties**

Royalty expense for the quarter was \$1.49 million (2007:\$1.39 million) and \$2.77 million for the first six months of the year (2007:\$3.45 million). As a percentage of revenue, royalties were 16.53% in the second quarter down 6% from 17.62% in the first quarter. On a year-over-year basis, royalties decreased by 22% from 21.26% in the second quarter of 2007.

The lower effective rate in the second quarter over the first quarter primarily reflects a one-time gas cost allowance credit for crown royalties on Alberta production. In comparison to the prior year, lower royalties in 2008 reflect the low-rate Antler production in Saskatchewan and the reduced rate on Alberta production countered by a higher royalty rate on production from British Columbia.

Royalties on production from British Columbia increased over the prior year from 18.5% to 22.81% primarily due to the new A-7 well at Beaver River and the two Greater Sierra wells that attract a royalty rate of 27% based on current prices. These wells meet the criteria for the crown ultra marginal gas well royalty program that would reduce these rates by approximately 50%. Subject to 12 months of consecutive production from these wells, Questerre expects to receive a credit for this amount next year.

The combined crown and royalty rate on production from Antler is the lowest for Questerre's core areas at nearly 6%. This rate for the year will vary between 5-10% based on the percentage of new production from crown and freehold lands which typically incur royalty rates of approximately 3% and 16% respectively.

## **Operating Expenses**

Operating expenses, including gathering and processing charges, were \$1.78 million for the quarter (2007: \$1.47 million) and \$3.21 million for the first half of the year (2007: \$3.16 million). On a boe basis, operating costs averaged \$15.72 for the quarter (2007: \$11.19) and \$14.00 for the year to date (2007: \$11.09).

In comparison to first quarter operating costs of \$1.43 million in the first quarter, second quarter costs were higher by \$0.35 million. The variance is mainly due to higher than expected costs in Alberta and Saskatchewan. Questerre expects these costs will decrease on a boe basis over the remainder of the year as additional production is brought on in these areas.

While production volumes were 14% lower in the second quarter of 2008 as compared to the same period in 2007, the higher costs on a boe basis reflect the general increase in operating costs in 2008.

## **General and Administrative Expenses**

Questerre recorded general and administrative expenses ("G&A") of \$0.63 million, net of capitalized overhead and recoveries for the quarter (2007: \$0.59 million) and \$1.16 million for the year to date (2007: \$1.42 million).

Gross expenses increased by 34% from \$1.70 million in the prior year to \$2.28 million in the current year and relatively unchanged at \$1.14 million for the second quarter from \$1.15 million in the first quarter. The higher costs in current year primarily reflect salary and rent increases to support the additional exploration and development activity.

Questerre capitalizes G&A representing 5% of capital expenditures incurred up to a maximum of 50% of gross G&A incurred in the period. Based on its capital expenditures in the first half of the year, Questerre capitalized G&A of \$1.04 million and recorded overhead recoveries of \$0.08 million for capital projects where it was operator. Capitalization in the prior year was significantly lower reflecting the lower capital expenditures incurred by the Company.

The lower production levels in the quarter as compared to the preceding quarter and the same period in the prior year translated into a increase on a boe basis to \$5.55 from \$4.52 in the second quarter of 2007 and \$5.37 in the first quarter of 2008.

Six months ended (\$ thousands)	2008	2007
General and administrative expenses	2,284	1,702
Bad debt expense	–	200
Capitalized expenses and overhead recoveries	(1,122)	(487)
General and administrative expenses, net	1,162	1,415

### Stock-Based Compensation

Stock-based compensation expense was \$0.53 million for the quarter ended June 30, 2008 (2007: \$0.36 million) and \$0.86 million (2007: \$0.69 million) for the first half of 2008.

Approximately 60% of the expense in the second quarter relates to two option grants made during the first half of the year. In the first quarter, 5.75 million options were granted at an exercise price of \$0.45 and in the second quarter, 2.59 million options granted at an exercise price of \$4.70 with a fair value of \$0.24 and \$3.46 per option respectively. The remainder relates to options granted in prior years. In aggregate, 8.39 million options were granted in the first half of 2008 with an average exercise price of \$1.78 and a weighted average fair value of \$3.44 per option.

### Other Income and Expense

Questerre reported interest income in the second quarter of 2008 of \$0.31 million (2007: \$0.09 million) and \$0.39 million for the year to date (2007: \$0.19 million). The income was earned on the net proceeds of the \$75 million equity offering completed by the Company in the quarter.

Interest expense of \$0.08 million was incurred by the Company under its term credit facility. The outstanding balance was paid down during the quarter from the proceeds of the equity offering. As at June 30, 2008, Questerre did not have any amounts outstanding under this facility and does not expect to for the remainder of this year.

### Depletion, Depreciation and Accretion Expense

Questerre recognized \$4.35 million in depletion, depreciation and accretion expense (“DD&A”) for the three months ended June 30, 2008 and \$8.55 million for the first six months of 2008 (2007: \$5.92 million).

For the second quarter of this year, DD&A per boe increased to \$38.51 from \$36.64 in the first quarter and from \$19.23 in second quarter of 2007. The higher amount in 2008 reflects the significant increase to the depletion base at the end of 2007 for the unsuccessful Beaver River wells. This was substantially offset by the reserve additions in Antler through the acquisition of Magnus and the successful drilling program in the first quarter of this year.

Quarter over quarter, the increase reflects the decrease in reserves associated with disposition of the assets in Alberta and no additional reserves for the Vulcan horizontal well. Questerre expects to see a positive revision to the Vulcan oil pool reserves at year-end based on the results of its drilling program.

Questerre excludes costs of \$18.24 million (2007: \$11.90 million) relating to unproved properties in the calculation of depletion.

The Company estimates its total undiscounted future asset retirement obligations to be approximately \$6.43 million with a present value at June 30, 2008 of \$4.48 million.

## Taxes

Consistent with the prior year, Questerre had sufficient tax pool deductions to offset taxable income in the second quarter of 2008 resulting in no income taxes payable for the quarter. For the six months ended June 30, 2008, Questerre recorded a future tax loss of \$0.35 million.

## Net Earnings and Cash Flow

Questerre reported a net loss of \$2.67 million for the quarter ended June 30, 2008 as compared to net earnings of \$0.98 million in the second quarter of 2007 and \$0.65 million for the first quarter of 2008. The loss in the second quarter over earnings in the first quarter is due to the future income tax loss of \$2.43 million in the second quarter. By contrast in 2007, Questerre's net income was largely due to the gain of \$1.5 million on the disposition of a portion of its working interest at Beaver River to its partner.

Cash flow from operations for the period increased to \$5.14 million from \$3.94 million in the preceding period and \$3.18 million for the same period in the prior year. Higher commodity prices in the quarter and improved operating netbacks were responsible for the increase in cash flow in spite of the decrease in production.

## Capital Expenditures

Capital expenditures, prior to acquisitions and dispositions, in the first half of 2008 were \$21.20 million as compared to \$10.46 million in 2007.

The majority of these expenditures, or \$17.69 million, were incurred in the first quarter primarily at Greater Sierra and Beaver River. In the second quarter, capital expenditures were \$3.50 million. Approximately \$1.44 million was incurred completing and tying-in wells in Vulcan, \$2.25 million was spent drilling and stimulating wells in Antler and the remainder in Quebec.

In 2007, Questerre incurred \$5.11 million in British Columbia, primarily drilling at Beaver River, and \$4.68 million spent in Alberta with the remainder in Quebec.

For the six months ended (\$ thousands)	2008	2007
Capital Expenditures		
Alberta	\$ 1,896	\$ 4,675
British Columbia	13,980	5,113
Saskatchewan	5,289	–
Quebec	30	672
Petroleum & Natural Gas Expenditures	21,195	10,460
Dispositions	(943)	(8,499)
Acquisitions	764	–
Asset Retirement Obligation	(199)	371
Total	20,817	2,332

## Capitalization and Financial Resources

Questerre reported a working capital surplus of \$68.45 million at June 30, 2008 as compared to a surplus of \$10.00 million at December 31, 2007.

The Company's current assets consist of cash and equivalents of \$67.86 million, \$2.32 million in deposits and accounts receivable of \$10.29 million. Current liabilities include \$11.46 million in accounts payable and accrued liabilities and \$0.85 million in risk management liability. The Company funded its capital expenditures of \$21.19 million for the year to date through its cash flow, credit facility and working capital.

Questerre's capital budget for the remainder of this year is expected to be approximately \$10 million. This budget will be funded through cash flow, existing cash on hand and dispositions of non-core assets.

## Share Capital

The following table provides a summary of the outstanding common shares and options as at the date of the MD&A and the preceding year-end:

	August 11 2008	June 30 2008	December 31 2007
Common Shares	197,284,170	196,650,213	168,930,470
Stock Options	17,302,088	17,936,045	13,064,170
Weighted average common shares			
Basic		175,504,676	157,078,211
Diluted		175,504,676	163,260,612

The increase in common shares outstanding from June 30, 2008 to August 11, 2008 was the exercise of 633,957 stock options.

## Contractual Obligations

Pursuant to a flow-through share private placement entered into on December 13, 2007, the Company was obligated to incur \$1.0 million in qualifying Canadian Exploration Expenses by December 31, 2008. As at June 30, 2008, the Company has a commitment remaining of \$0.5 million.

The Company is obligated to make total payments under an operating lease of \$57,906 in 2008, \$115,812 in 2009 and 2010. Questerre has commitments under a lease for office space of \$161,259 in 2008 and \$322,519 in 2009 and 2010.

## Off-Balance Sheet Arrangements

There were no off-balance sheet transactions entered into during the period, nor were there any outstanding as of the date of this MD&A.

## Business Environment and Risk

Except as detailed below, there were no changes to Questerre's risk management policies during the period from those detailed in the MD&A for the year ended December 31, 2007.

### Environmental Regulation and Risk

All phases of the oil and natural gas business present environmental risks and hazards and are subject to environmental regulation pursuant to a variety of federal, provincial and local laws and regulations. Compliance with such legislation can require significant expenditures and a breach may result in the imposition of fines and penalties, some of which may be material. Environmental legislation is evolving in a manner expected to result in stricter standards and enforcement, larger fines and liability and potentially increased capital expenditures and operating costs. In 2002, the Government of Canada ratified the Kyoto Protocol (the "Protocol"), which calls for Canada to reduce its greenhouse gas emissions to specified levels. There has been much public debate with respect to Canada's ability to meet these targets and the Government's strategy or alternative strategies with respect to climate change and the control of greenhouse gases. Implementation of strategies for reducing greenhouse gases whether to meet the limits required by the Protocol or as otherwise determined could have a material impact on the nature of oil and natural gas operations, including those of the Company.

The Federal Government released on April 26, 2007, its Action Plan to Reduce Greenhouse Gases and Air Pollution (the "Action Plan"), also known as ecoACTION and which includes the Regulatory Framework for Air Emissions. This Action Plan covers not only large industry, but regulates the fuel efficiency of vehicles and the strengthening of energy standards for a number of energy-using products. Regarding large industry and industry related projects the Government's Action Plan intends to achieve the following: (i) an absolute reduction of 150 megatonnes in greenhouse gas emissions by 2020 by imposing mandatory targets; and (ii) air pollution from industry is to be cut in half by 2015 by setting certain targets. New facilities using cleaner fuels and technologies will have a grace period of three years. In order to facilitate the companies' compliance of the Action Plan's requirements, while at the same time allowing them to be cost-effective, innovative and adopt cleaner technologies, certain options are provided. These are: (i) in-house reductions; (ii) contributions to technology funds; (iii) trading of emissions with below-target emission companies; (iv) offsets; and (v) access to Kyoto's Clean Development Mechanism.

On March 8, 2007, the Alberta Government introduced Bill 3, the Climate Change and Emissions Management Amendment Act, which intends to reduce greenhouse gas emission intensity from large industries. Bill 3 states that facilities emitting more than 100,000 tonnes of greenhouse gases a year must reduce their emissions intensity by 12% starting July 1, 2008; if such reduction is not initially possible the companies owning the large emitting facilities will be required to pay \$15 per tonne for every tonne above the 12% target. These payments will be deposited into an Alberta-based technology fund that will be used to develop infrastructure to reduce emissions or to support research into innovative climate change solutions. As an alternate option, large emitters can invest in projects outside of their operations that reduce or offset emissions on their behalf, provided that these projects are based in Alberta. Prior to investing, the offset reductions, offered by a prospective operation, must be verified by a third party to ensure that the emission reductions are real.

Given the evolving nature of the debate related to climate change and the control of greenhouse gases and resulting requirements, it is not possible to predict the impact of those requirements on the Company and its operations and financial condition.

### Review of Alberta Royalty and Tax Regime

The government has previously stated its intention to consult with industry and potentially revise the New Royalty Framework ("NRF") for unintended consequences. This consultation has now been concluded and on April 10, 2008 the government released its clarifications as well as a new "deep resource program". Highlights of this release are as follows:

#### *Deep oil wells*

- A five-year oil program for exploration wells over 2,000 meters will provide royalty adjustments to offset higher drilling costs and provide a greater incentive for producers to continue to pursue new, deeper oil plays.
- Wells deeper than 2,000 meters represented 20 per cent of oil wells drilled and 26 per cent of new conventional oil production between 2002 and 2007.
- Wells will qualify for up to \$1 million or 12 months of royalty offsets, whichever comes first.

#### *Deep natural gas*

- To encourage continued deep gas exploration, the government will replace the existing Royalty Adjustment Program with the Natural Gas Deep Drilling Program for wells deeper than 2,500 meters.
- Wells over 2,500 meters represented five per cent of natural gas wells drilled and 27 per cent of natural gas production between 2002 and 2007.
- The Natural Gas Deep Drilling Program will provide greater benefits to deeper wells, creating a sliding scale of royalty credit according to depth, up to \$3,750 per meter.

*Other clarifications as a result of the unintended consequences analysis*

- Under the New Royalty Framework, four par prices instead of two will be used to calculate royalties on oil, allowing royalties to be charged at a price closer to that received by the producer.
- Natural gas royalty will be calculated based on the sum of vertical drill depth and all laterals, encouraging greater development of coalbed methane. Greater use of laterals may significantly lessen land use and the environmental footprint of CBM development

Questerre has reviewed the new program as well as the “clarifications” and it has determined that they do not materially alter the impact of the NRF as disclosed in the Company’s 2007 annual report.

## **Critical Accounting Estimates**

Management is required to make judgments, assumptions and estimates in the application of generally accepted accounting principles that have a significant impact on the financial results of the Company. There were no changes to Questerre’s critical accounting estimates in the period from those used in the audited financial statements from 2007. Please refer to the MD&A for the year ended December 31, 2007.

## **Changes in Accounting Policies**

### **Accounting Standard Changes**

As of January 1, 2008 Questerre adopted the new CICA standards, Section 3862 “Financial Instruments – Disclosures” and Section 3863 “Financial Instruments – Presentation”, which will replace Section 3861 “Financial Instruments – Disclosure and Presentation”. The new disclosure standard increases the emphasis on the risks associated with both recognized and unrecognized financial instruments and how those risks are managed. The new presentation standard carries forward the former presentation requirements.

Also effective January 1, 2008, the Company adopted CICA 1535 “Capital Disclosures”, which will require additional disclosures of objectives, policies and processes for managing capital. In addition, disclosures will include whether companies have complied with externally imposed capital requirements.

### **Future Accounting Pronouncements**

In January 2006, the CICA Accounting Standards Board (“AcSB”) adopted a strategic plan for the direction of accounting standards in Canada. As part of the plan, accounting standards in Canada for public companies are expected to converge with International Financial Reporting Standards (“IFRS”) by the first quarter of 2011. The Company continues to monitor and assess the impact of the convergence of Canadian GAAP and IFRS.

In February 2008, the AcSB issued Handbook Section 3064, Goodwill and Intangible Assets and amended Section 1000, Financial Statement Concepts clarifying the criteria for the recognition of assets, intangible assets and internally developed intangible assets. Items that no longer meet the definition of an asset are no longer recognized with assets. The standard is effective for fiscal years beginning on or after October 1, 2008 and early adoption is permitted. Questerre is currently evaluating the impact this section will have on its results of operations and financial position.

## **Disclosure Controls and Procedures**

Disclosure controls and procedures have been designed to ensure that information required to be disclosed by the Company is accumulated and communicated to Questerre's management as appropriate to allow timely decisions regarding required disclosure. Questerre's Chief Executive Officer and Chief Financial Officer have concluded, based on their evaluation as of the end of the period covered by the annual filings, that the Company's disclosure controls and procedures as of the end of such period are effective to provide reasonable assurance that material information related to the Company, including its consolidated subsidiaries, is made known to them by others within those entities, particularly during the period in which the interim filings are being prepared.

Internal controls have been designed to provide reasonable assurance regarding the reliability of the Company's financial reporting and the preparation of financial statements together with the other financial information for external purposes in accordance with Canadian GAAP. The Company's Chief Executive Officer and Chief Financial Officer have designed or caused to be designed under their supervision internal controls over financial reporting related to the Company, including its consolidated subsidiaries.

The Company's Chief Executive Officer and Chief Financial Officer are required to cause the Company to disclose herein any change in the Company's internal control over financial reporting that occurred during the Company's most recent interim period that materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting. There were no material changes in the Company's internal controls over financial reporting during the quarter ended June 30, 2008.

It should be noted that a control system, including the Company's disclosure and internal controls and procedures, no matter how well conceived can provide only reasonable, but not absolute, assurance that the objectives of the control system will be met and it should not be expected that the disclosure and internal controls and procedures will prevent all errors or fraud.