Q2

2011 QUARTERLY REPORT

QUESTERRE ENERGY CORPORATION

2011

QUESTERRE ENERGY CORPORATION IS AN INDEPENDENT ENERGY COMPANY FOCUSED ON UNCONVENTIONAL OIL AND GAS PROJECTS. THE COMPANY IS DEVELOPING A PORTFOLIO OF LIGHT OIL ASSETS PRIMARILY IN SASKATCHEWAN. THE COMPANY IS ALSO LEVERAGING ITS EXPERTISE TO COMMERCIALIZE ITS UTICA SHALE GAS DISCOVERY IN THE ST. LAWRENCE LOWLANDS, QUÉBEC. QUESTERRE'S COMMON SHARES TRADE ON THE TORONTO STOCK EXCHANGE UNDER THE SYMBOL QEC.

President's Message

With the shale gas environmental assessment underway in Québec, we shifted our short term strategy to unconventional oil. Accelerating development of our Antler asset will be our first priority, both through organic growth and accretive acquisitions.

Although it will take longer than we expected, commercializing our Utica shale gas discovery remains our main long term priority. While the government assesses the potential environmental impacts and develops new regulations, we will focus on communications with stakeholders to secure our social license to operate.

Highlights

- Interim regulations for shale gas development announced by the Government of Québec
- Oil and gas exploration licenses extended during strategic environmental assessment
- Completed divestiture of interest in Beaver River Field to Transeuro Energy
- Cash flow from operations of $2.27 million and production of 586 boe/d with improved oil weighting leveraging higher prices during the quarter
- Balance sheet strength preserved with over $131 million in positive working capital and no debt

St. Lawrence Lowlands, Québec

Consistent with the BAPE recommendations, the government of Québec commissioned a strategic environmental assessment ("SEA") for shale gas development in the second quarter. A multi-stakeholder committee was appointed to conduct the SEA and new regulations were enacted to govern operations during this period.

The announcement of the SEA materially impacted our timeline for commercial development of the Utica. During this time, the government mandated limited activities while it increases its understanding of the industry and develops the appropriate regulations. We were pleased to learn that the Ministry of Natural Resources acknowledged this impact and extended the term of our exploration licenses up to three years.

Environmental assessments are common for large scale resource projects, including shale gas development in other jurisdictions. While we appreciate the importance of assessing the local impacts, we are hopeful that, rather than re-creating the proverbial wheel, the committee will leverage the growing body of research that corroborates the established industry practices to safely develop shale gas. This includes the 1,000 page preliminary Draft Supplemental Generic Environmental Impact Study recently published by the Department of Environmental Conversation in New York on the development of shale resources in the state. It confirms the safety and benefits of shale gas development, including that it is highly unlikely that groundwater contamination would occur by fluids pumped into a wellbore for hydraulic fracturing.

Dispelling the persistent myths about shale gas development such as groundwater contamination remains an important part of our public relations efforts in Québec. The reports emerging from a wide variety of sources continue to validate our position. We are optimistic that these will allow us to refocus the debate on the real issues like water handling and cementing practices that are common to all drilling operations and unrelated to hydraulic fracturing.

Antler, Saskatchewan

Accelerating activity at Antler is key to our strategy of diversifying into unconventional light oil during the environmental assessment in Québec.

Our planned development of this light oil resource will benefit from our learning curve over the last two years. Refinements to our drilling and completion programs, improved production practices and operating efficiencies have contributed to increased recoveries and lower operating costs.

Notwithstanding the excellent fiscal terms in Saskatchewan that enhance these economics, returns are challenged by weather and equipment availability.

Heavy rainfall this spring coupled with high snow pack resulted in record flooding in southern Saskatchewan that submerged well sites, access roads and highways. The province, Canada's second largest oil producer, reported that approximately 20,000 to 30,000 barrels of oil production was shut-in as a result of this flooding. We expect this will further constrain available completion equipment during a very short summer operating season.

Through a combination of geography and design, our existing production was largely unaffected by the inclement weather. The majority of our horizontal wells are pipeline connected to our main battery eliminating the trucking from well sites that were flooded. Our main battery is located on drier ground and proximate to open highways allowing trucking of the produced oil to the sales terminal.

As weather conditions improve, we are resuming field operations. Our plans for the remainder of this year are to drill up to 10 (5.0 net) wells. As equipment availability permits, we will look to a second rig to achieve this plan. With an inventory of wells to be drilled and awaiting completion, we anticipate contracting frac equipment for a definitive period. This will allow us to reduce the lag between drilling and completion from six months to four months or less. Subject to these constraints, we are targeting a corporate exit production rate of 750 boe/d for 2011.

Early in the third quarter, we expanded our presence in the area through an acquisition of producing assets and undeveloped land for $13.25 million. The acquisition of approximately 100 bbl/d of operated production added a number of infill and step out locations. We continue to look for assets that will complement our existing production at Antler.

Operational and Financial

The weather related delays and equipment shortages at Antler lowered our production volumes as we were unable to complete wells as planned. With the disposition of the Beaver River Field, we also lost 70 boe/d for the last month of the quarter. Although volumes were lower, the higher oil weighting realized higher prices and improved our results.

Cash flow from operations for the quarter was $2.27 million with average daily production of 586 boe/d and an operating netback of $58.75/boe. Our operating margins should improve over the remainder of the year with the elimination of the fixed operating costs and relatively minimal production volumes associated with the Beaver River Field.

Outlook

Over the remainder of this year and next, unconventional oil will be our main focus.

We will continue to actively develop Antler. This will include organic growth as well as accretive acquisitions. Our goal is to create a core area with a value in excess of our current market capitalization. Another goal is to create shareholder value through scalable early stage unconventional projects targeting light oil. We have the in-house expertise and balance sheet strength to capitalize on the right opportunities when they arise.

Although the timeline has been extended, we remain committed to the goal of commercializing our Utica shale discovery. We have been very encouraged by the growing body of evidence that endorses that shale gas can be developed safely. We believe communicating this and the benefits to local stakeholders will be essential to securing our social license to operate.

Michael Binnion
President and Chief Executive Officer

The Management's Discussion and Analysis ("MD&A") was prepared as of August 10, 2011. This interim MD&A should be read in conjunction with the unaudited interim consolidated financial statements of Questerre Energy Corporation ("Questerre" or the "Company") as at and for the three and six month periods ended June 30, 2011 and 2010, and the 2010 MD&A and audited annual consolidated financial statements of the Company for the year ended December 31, 2010. Additional information relating to Questerre, including Questerre's Annual Information Form for the year ended December 31, 2010 is available on SEDAR at www.sedar.com.

Questerre is an independent energy company focused on unconventional oil and gas projects. The Company is developing a portfolio of light oil assets primarily in Saskatchewan. The Company is also leveraging its expertise to commercialize its Utica shale gas discovery in the St. Lawrence Lowlands, Québec. Questerre is committed to the economic development of its resources in an environmentally conscious and socially responsible manner.

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

Basis of Presentation

Unless otherwise noted, all financial information, including comparative figures pertaining to Questerre's 2010 results, has been prepared in accordance with Canadian generally accepted accounting principles ("GAAP"), specifically International Accounting Standard ("IAS") 34 – *Interim Financial Reporting*, within Part 1 of the Canadian Institute of Chartered Accountants Handbook.

This is Questerre's first year presenting figures in the MD&A prepared using accounting policies within the framework of International Financial Reporting Standards ("IFRS"). In previous periods, the company prepared its consolidated financial statements and interim consolidated financial statements in accordance with Canadian generally accepted accounting principles in effect prior to January 1, 2011 ("previous GAAP"). Comparative figures presented in this MD&A pertaining to Questerre's 2010 results have been restated to be in accordance with IFRS. A reconciliation of comparative figures from previous GAAP to IFRS is provided in the notes to the June 30, 2011 unaudited interim consolidated financial statements. Comparative figures presented in this MD&A pertaining to Questerre's 2009 results were prepared in accordance with previous GAAP and were not required to be restated.

All financial information is reported in Canadian dollars, unless otherwise noted. Certain amounts in prior years have been reclassified to conform to the current year's presentation.

Forward Looking Statements

Certain statements contained within this MD&A, and in certain documents incorporated by reference into this document, constitute forward-looking statements. These statements relate to future events or our future performance. All statements other than statements of historical fact may be forward-looking statements. Forward-looking statements are often, but not always, identified by the use of words such as "seek", "anticipate", "budget", "plan", "continue", "estimate", "expect", "forecast", "may", "will", "project", "predict", "potential", "targeting", "intend", "could", "might", "should", "believe" and similar expressions. These statements involve known and unknown risks, uncertainties and other factors that may cause actual results or events to differ materially from those anticipated in such forward-looking statements. We believe the expectations reflected in those forward-looking statements are reasonable but no assurance can be given that these expectations will prove to be correct and such forward-looking statements included in, or incorporated by reference into, this MD&A should not be unduly relied upon. These statements speak only as of the date of this MD&A or as of the date specified in the documents incorporated by reference into this MD&A, as the case may be.

This MD&A, and the documents incorporated by reference, contain forward-looking statements pertaining to the following:

- the performance of our oil and natural gas properties;
- the size of our oil, natural gas liquids and natural gas reserves and production levels;
- estimates of future cash flow;
- projections of prices and costs;
- drilling plans and timing of drilling, recompletion and tie-in of wells by Questerre and its partners;
- weighting of production between different commodities;
- commodity prices, exchange rates and interest rates;
- expected levels of royalty rates, operating costs, general and administrative costs, costs of services and other costs and expenses;
- capital expenditure programs and other expenditures and the timing and method of financing thereof;
- supply of and demand for oil, natural gas liquids and natural gas;
- expectations regarding our ability to raise capital and to continually add to reserves through acquisitions and development;
- our ability to grow or sustain production and reserves through prudent management;
- the emergence of accretive growth opportunities and continued access to capital markets;
- our future operating and financial results;
- schedules and timing of certain projects and our strategy for future growth; and
- treatment under governmental and other regulatory regimes and tax, environmental and other laws.

In particular, this MD&A contains the following forward-looking statements pertaining to the following:

- production volumes;
- timing of drilling programs and resulting cash flows;
- future oil and gas prices;
- operating costs;
- royalty rates;
- future development, exploration and acquisition activities and related expenditures;
- the amount of future asset retirement obligations; and
- future liquidity and future financial capacity.

With respect to forward-looking statements contained in this MD&A and the documents incorporated by reference herein, we have made assumptions regarding, among other things:

- future oil and natural gas prices;
- the continued availability of capital, undeveloped lands and skilled personnel;
- the costs of expanding our property holdings;
- the ability to obtain equipment in a timely manner to carry out exploration, development and exploitation activities;
- the ability to obtain financing on acceptable terms;
- the ability to add production and reserves through exploration, development and exploitation activities; and
- the continuation of the current tax and regulatory regime.

The actual results could differ materially from those anticipated in these forward-looking statements as a result of the risk factors set forth below and elsewhere in this MD&A and the documents incorporated by reference into this document:

- volatility in market prices for oil, natural gas liquids and natural gas;
- counterparty credit risk;
- access to capital;
- changes or fluctuations in oil, natural gas liquids and natural gas production levels;
- liabilities inherent in oil and natural gas operations;
- adverse regulatory rulings, orders and decisions;
- attracting, retaining and motivating skilled personnel;
- uncertainties associated with estimating oil and natural gas reserves;
- competition for, among other things, capital, acquisitions of reserves, undeveloped lands, and services;
- incorrect assessments of the value of acquisitions and targeted exploration and development assets;
- fluctuations in foreign exchange or interest rates;
- stock market volatility, market valuations and the market value of the securities of Questerre;
- failure to realize the anticipated benefits of acquisitions;
- actions by governmental or regulatory authorities including changes in royalty structures and programs and income tax laws or changes in tax laws and incentive programs relating to the oil and gas industry;
- limitations on insurance;
- changes in environmental or other legislation applicable to our operations, and our ability to comply with current and future environmental and other laws; and
- geological, technical, drilling and processing problems and other difficulties in producing oil, natural gas liquids and natural gas reserves.

Statements relating to "reserves" or "resources" are by their nature deemed to be forward-looking statements, as they involve the implied assessment, based on certain estimates and assumptions that the resources and reserves described can be profitably produced in the future.

Readers are cautioned that the foregoing lists of factors are not exhaustive. The forward-looking statements contained in this MD&A and the documents incorporated by reference herein are expressly qualified by this cautionary statement. We do not undertake any obligation to publicly update or revise any forward-looking statements except as required by applicable securities law.

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.

Non-GAAP Terms

This document contains the terms "cash flow from operations" and "netbacks" which are non-GAAP terms. The Company uses these measures to help evaluate its performance.

As an indicator of Questerre's performance, cash flow from operations should not be considered as an alternative to, or more meaningful than, cash flows from operating activities as determined in accordance with GAAP. Questerre's determination of cash flow from operations may not be comparable to that reported by other companies. Questerre considers cash flow from operations to be a key measure as it demonstrates the Company's ability to generate the cash necessary to fund operations and support activities related to its major assets.

Cash Flow from Operations Reconciliation

	Three months ended June 30		Six months ended June 30	
	2011	2010	**2011**	2010
Cash flows from operating activities	**$ 3,247,212**	$ (484,182)	**$ 4,113,708**	$ 2,179,972
Net change in non-cash operating working capital	**(979,536)**	674,199	**(209,082)**	(1,473,564)
Cash flow from operations	**$ 2,267,676**	$ 190,017	**$ 3,904,626**	$ 706,408

The Company considers netbacks a key measure as it demonstrates its profitability relative to current commodity prices. Operating netbacks per boe equal total petroleum and natural gas sales per boe adjusted for royalties per boe and operating expenses per boe.

The Company also uses the term "working capital surplus". Working capital surplus, as presented, does not have any standardized meaning prescribed by GAAP and may not be comparable with the calculation of similar measures for other entities. Working capital surplus, as used by the Company, is calculated as current assets less current liabilities excluding the current portion of the share based compensation liability.

Select Information

As at/for the period ended June 30,	Three months ended 2011	2010	Six months ended 2011	2010
Financial ($, except common shares outstanding)				
Petroleum and Natural Gas Sales	**4,138,050**	2,813,743	**8,103,439**	5,789,096
Cash Flow from Operations	**2,267,676**	190,017	**3,904,626**	706,408
Per share - Basic	**0.01**	-	**0.02**	-
Per share - Diluted	**0.01**	-	**0.02**	-
Net Profit (Loss)	**4,938,387**	(4,535,629)	**6,172,646**	(6,269,681)
Per share - Basic	**0.02**	(0.02)	**0.03**	(0.03)
Per share - Diluted	**0.02**	(0.02)	**0.03**	(0.03)
Capital Expenditures, net of acquisitions and dispositions	**1,305,781**	3,806,236	**8,549,261**	8,883,276
Working Capital Surplus	**131,312,369**	160,932,087	**131,312,369**	160,932,087
Total Assets	**250,973,021**	258,023,289	**250,973,021**	258,023,289
Shareholders' Equity	**234,312,816**	237,989,679	**234,312,816**	237,989,679
Common Shares Outstanding	**232,115,528**	233,835,478	**232,115,528**	233,835,478
Weighted average - basic	**233,610,707**	233,809,187	**233,981,259**	220,174,636
Weighted average - diluted	**236,472,552**	240,694,908	**237,475,415**	228,789,956
Operations (units as noted)				
Average Production				
Crude Oil and Natural Gas Liquids (bbl/d)	**401**	303	**425**	299
Natural Gas (Mcf/d)	**1,111**	1,904	**1,154**	1,866
Total (boe/d)	**586**	620	**617**	610
Average Sales Price				
Crude Oil and Natural Gas Liquids ($/bbl)	**102.50**	75.25	**94.76**	77.32
Natural Gas ($/Mcf)	**3.96**	4.25	**3.89**	4.75
Total ($/boe)	**77.60**	49.87	**72.56**	52.43
Netback ($/boe)				
Petroleum and Natural Gas Sales	**77.60**	49.87	**72.56**	52.43
Royalties Expense	**(6.25)**	(12.87)	**(6.08)**	(10.21)
Percentage	**8%**	26%	**8%**	19%
Operating Expense	**(12.60)**	(15.53)	**(13.02)**	(16.55)
Operating Netback	**58.75**	21.47	**53.46**	25.67
Wells Drilled				
Gross	**1.00**	4.00	**9.00**	7.00
Net	**0.50**	1.46	**5.25**	2.96

Highlights

- Interim regulations for shale gas development announced by the Government of Québec
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Second Quarter 2011 Activities

St. Lawrence Lowlands, Québec

In June 2011, the Ministry of Sustainable Development, Environment and Parks in Québec ("MDDEP") introduced new regulations for shale gas development in the province.

The interim regulations require operators to inform and consult the public prior to commencing operations. To increase the understanding of shale gas, MDDEP may have representatives participate in observing the drilling and completion operations. Operators will also be required to provide MDDEP with technical information including drilling and completion methods and technology, water management programs, proposed completion fluid composition and volumes and sampling water wells within a one kilometer radius of the proposed operations.

These regulations are designed to implement the recommendations of the Bureau d'audiences publiques sur l'environment ("BAPE") report that were published in early March 2011 by MDDEP.

The BAPE report mandated a strategic environmental assessment of shale gas development in Québec ("SEA"). The recommendations also included provisions for controlled piloting which will include the drilling and completion of a limited number of wells while the environmental review is being conducted. Questerre anticipates these wells will be part of the pilot program to assess commerciality. The pilot program, including the completion and testing of the St. Gertrude and Fortierville wells, is scheduled to resume next spring unless equipment availability improves.

During the quarter, MDDEP also announced the mandate and membership of the committee that will oversee the SEA. The committee will have a total of 11 members and include representatives from ministries of municipal affairs, natural resources, the education and research sector, the sustainable development and environmental sector and industry. It will be chaired by MDDEP.

The committee's mandate will include delivery of a report on the SEA to address the issues identified and provide recommendations for the regulatory regime to govern shale gas development. Upon the completion of the assessment over the next two to three years, the Ministry of Natural Resources ("MNRF") has confirmed it plans to introduce new hydrocarbon legislation that is expected to facilitate commercial development.

MNRF recently introduced new legislation suspending the term of the exploration licenses for petroleum, natural gas and underground reservoirs in the province of Québec for a period of up to three years as determined by the Minister. Holders of these licenses are also exempted from performing the work required under the Mining Act for this period.

Antler, Saskatchewan

Record flooding in southeast Saskatchewan suspended the Company's planned drilling and completion operations in the second quarter of 2011.

During the quarter, Questerre entered into an agreement to acquire approximately 100 bbl/d of light oil production and 6,942 net acres of undeveloped land proximate to its existing assets. The proved and probable reserves assigned to this asset by an independent reserve engineering firm as of March 31, 2011 is 419 Mbbl representing only six percent of the oil in place. The acquisition closed in July 2011 with cash consideration of $13.25 million.

Contingent upon completion equipment availability and weather, Questerre has plans for a phased program that could include up to 10 (5.00 net) additional wells later this year including locations on the newly acquired acreage.

Northeast British Columbia

In May 2011, Questerre concluded its agreement with Transeuro Energy Corp. ("Transeuro") for Transeuro to acquire the remaining 50% interest in the Beaver River Field (the "Field").

Pursuant to the agreement, Transeuro acquired all the issued and outstanding shares of Questerre Beaver River Inc. ("QBR"), a wholly owned subsidiary of the Company that owns the other 50% interest in the Field.

In consideration, Questerre received 40 million common shares of Transeuro representing 8.7% of the outstanding common shares of the company. Questerre has also advanced Transeuro a $2.00 million loan to fund its ongoing operations. The loan will be due and payable on the earlier of 12 months or the announcement of a future financing by Transeuro. Questerre has plans to maintain its share position through a $2.00 million commitment to this future financing by Transeuro subject to final terms.

Corporate

Pursuant to the Normal Course Issuer Bid, a total of 2,783,200 common shares were purchased at a weighted average price of $1.00/share during the second quarter of 2011. 942,200 common shares were purchased through the facilities of the TSX at an average price of $1.01/share and 1,841,000 common shares were purchased through the facilities of Oslo Bors at an average price of $0.99/share.

Drilling Activities

In the second quarter of 2011, Questerre participated in the drilling of one (0.50 net) oil well in Alberta and no natural gas wells. In the second quarter of 2010, Questerre participated in the drilling of two (0.46 net) natural gas wells in Québec and two (1.00 net) oil wells in Saskatchewan.

Production

Three months ended June 30,	**2011**			2010		
	Oil and Liquids (bbl/d)	**Natural Gas (Mcf/d)**	**Equivalent (boe/d)**	Oil and Liquids (bbl/d)	Natural Gas (Mcf/d)	Equivalent (boe/d)
Saskatchewan	**343**	**-**	**343**	232	-	232
Alberta	**58**	**685**	**172**	71	1,256	280
British Columbia	**-**	**426**	**71**	-	648	108
	401	**1,111**	**586**	303	1,904	620

Six months ended June 30,	**2011**			2010		
	Oil and Liquids (bbl/d)	**Natural Gas (Mcf/d)**	**Equivalent (boe/d)**	Oil and Liquids (bbl/d)	Natural Gas (Mcf/d)	Equivalent (boe/d)
Saskatchewan	**364**	**-**	**364**	225	-	225
Alberta	**61**	**680**	**174**	74	1,248	282
British Columbia	**-**	**474**	**79**	-	618	103
	425	**1,154**	**617**	299	1,866	610

Production volumes in the second quarter of 2011 declined from the preceding quarter and the same period in the prior year. This reflects the challenging weather conditions and equipment shortages that impacted planned drilling and completion operations in Antler, Saskatchewan. While volumes were lower, the Company's focused program in this area over the last 18 months has resulted in an increased oil weighting to capitalize on higher oil prices.

Oil and liquids production averaged 401 bbl/d in the second quarter of 2011, a 32% increase from the second quarter of 2010 and an 11% decrease from the 450 bbl/d produced in the prior quarter. For the first six months of the year, these volumes have increased 42% to 425 bbl/d from 299 bbl/d in 2010 with the growth entirely from Saskatchewan. Production growth in 2011, and especially the second quarter of 2011, has been slower than expected with shut-ins and delays associated with weather and completion equipment availability in Saskatchewan. With no investment in conventional natural gas assets over the last year, oil and liquids accounted for 68% of total production improving from 49% in the second quarter of 2010 and consistent with 69% in the first quarter of 2011.

Natural gas production averaged 1,111 Mcf/d in the second quarter of 2011, a 7% decrease from the previous quarter and a 42% decrease from the corresponding period in 2010. Year to date, natural gas production has declined 38% to 1,154 Mcf/d from the prior year. Questerre's gas production is attributable to its non-operated conventional assets in Alberta and BC and its interest in the Beaver River Field. With the disposition of this interest effective May 30, 2011 coupled with natural declines in its remaining assets and no further investment planned in conventional natural gas drilling, Questerre anticipates these volumes to decrease further over the remainder of this year.

Second Quarter 2011 Financial Results

Petroleum and Natural Gas Sales

During the second quarter of 2011, revenue improved due to materially higher oil prices and an increasing oil weighting partially offset by lower overall volumes.

Petroleum and natural gas revenue for the quarter ended June 30, 2011 grew marginally to $4.14 million from $3.97 million in the prior quarter when relatively lower oil prices mitigated the benefit of higher oil production. In the second quarter of 2010, Questerre reported revenue of $2.81 million based on lower oil volumes and prices.

Geopolitical events continued to impact crude oil prices during the quarter. Prices initially included a significant premium for the potential supply disruptions in the Middle East and North Africa. Subsequently, this premium began to erode as the situation moderated and the market focused on the ongoing European debt crisis and the state of the US economy.

Questerre's oil and liquids price averaged $102.50/bbl in the quarter, a 17% increase from the prior quarter price of $87.78/bbl and a 36% increase from the second quarter 2010 price of $75.25/bbl. These realized prices tracked the change in the reference Edmonton Light price from $75.18/bbl in the second quarter of 2010 to $87.97/bbl in the first quarter of 2011 and to $103.07/bbl in the second quarter of 2011.

Sustained supply growth and limited demand growth continue to influence natural gas prices in the short term. Concerns remain regarding the increasing horizontal rig efficiency and the impact of the backlog of uncompleted wells from the dry gas shale plays despite the move towards oil and liquids rich gas plays that should temper this supply growth. While power generation demand is growing as natural gas is competitive with the price of coal, material increases in this sector and the industrial demand sector will be necessary before prices improve.

In the second quarter of 2011, the benchmark AECO price averaged $3.87/Mcf (2010: $3.89/Mcf) marginally higher than $3.79/Mcf in the first quarter. This translated into a realized price of $3.96/Mcf in the second quarter of 2011 (2010: $4.25/Mcf) as compared to $3.82/Mcf in the first quarter. On a year to date basis, the realized price is 18% lower at $3.89/Mcf from $4.75/Mcf in the prior year.

Royalties

Royalty expense for the second quarter of 2011 totaled $0.33 million compared to $0.35 million in the prior quarter and $0.73 million in the second quarter of 2010. The second quarter of 2010 included prior period amounts. Excluding the prior period amounts, the royalty rate as a percentage of revenue for the current quarter is 8%, the prior quarter is 9% and the second quarter of 2010 is 11%.

For the first six months of 2011, the royalty expense totaled $0.68 million (2010: $1.13 million). Excluding prior period amounts in 2010 the royalty rate has decreased to 8% in 2011 from 12% in 2010.

The overall reduction in the royalty rates is mainly due to the increasing proportion of revenues from the Antler area where the royalty rate is currently 6%. This includes the Saskatchewan Resource Surcharge of 1.7% of gross revenue from the province. The majority of the Company's wells are located on Crown lands where it benefits from a royalty incentive rate of up to 2.5% on the first 100,000 barrels of production. Subject to the timing of additional drilling throughout the year, Questerre expects its royalty rate to increase as additional wells are drilled on freehold lands where the royalty rate averages 17%.

Operating Costs

Total operating expenses for the second quarter were $0.67 million (2010: $0.88 million) and for the first six months of this year, operating costs totaled $1.45 million (2010: $1.83 million). In the preceding quarter of 2011, operating costs totaled $0.78 million. On a per boe basis, operating costs decreased to $12.60 in the second quarter of 2011 (2010: $15.53) from $13.37 in the prior quarter. These costs, on a boe basis, averaged $13.02 for the first six months of 2011 (2010: $16.55).

Operating costs at Antler in the second quarter of 2011 were $8.46/bbl compared to $7.88/bbl in the previous quarter and $12.06/bbl in the second quarter of 2010. Year to date operating costs have been $8.18/bbl compared to $13.47/bbl in the prior year. The significant decrease year over year is due to operating efficiencies, specifically the electrification of well sites and pipeline tie-ins that have reduced the costs associated with single well batteries. Furthermore, increased volumes cover the fixed operating costs associated with this area, lowering the unit of production costs.

Field operating expenses in Alberta averaged $11.65/boe for the quarter, significantly lower than $15.84/boe in the first quarter of 2011 and $13.07/boe in the second quarter of 2010. Despite a higher proportion of fixed costs in Vulcan, a focus on improving operating efficiencies and lowering third party gathering and processing charges was successful in the second quarter of this year.

With the disposition of the Beaver River Field at the end of May 2011, field operating costs for the quarter totaled $0.19 million (2010: $0.23 million) and $0.22 million in the prior quarter. With a high proportion of fixed operating costs, the disposition is expected to have a material positive impact on the Company's overall operating costs in the future. At Greater Sierra, largely variable operating costs of $0.03 million in the quarter were down from $0.05 million in the prior year second quarter due to the decline in production volumes.

General and Administrative Expenses

	Three months ended June 30		*Six months ended June 30*	
	2011	2010	**2011**	2010
General and administrative expenses, gross	**$ 1,901,181**	$ 1,615,504	**$ 3,510,699**	$ 3,125,690
Capitalized expenses and overhead recoveries	**(627,902)**	(164,910)	**(1,145,494)**	(465,265)
General and administrative expenses, net	**$ 1,273,279**	$ 1,450,594	**$ 2,365,205**	$ 2,660,425

Gross general and administrative expenses ("G&A") saw an increase in the second quarter of 2011 to $1.90 million (2010: $1.62 million) from $1.61 million in the prior quarter. For the first six months of 2011 the gross G&A expense was $3.51 million (2010: $3.13 million). Increases in public and government relations expenses, legal fees and higher staffing costs account for the higher expenses in 2011 over the prior year.

With the increase in the gross expense more than offset by the increase in the capitalized expenses and overhead recoveries, net G&A decreased to $2.37 million in 2011 from $2.66 million in 2010.

Other Income and Expenses

Questerre reported interest income of $0.91 million for the first six months of the year (2010: $0.54 million) and $0.45 million for the three months ended June 30, 2011 (2010: $0.43 million). The interest was earned principally on the net proceeds of the equity issuance completed by Questerre in the first quarter of 2010. The interest is higher in the first six months of 2011 with the proceeds being invested for the entire period compared to only a portion of the first six months of 2010 after the financing was closed. The cash is invested in Guaranteed Investment Certificates issued by Canadian chartered banks and credit unions.

In the second quarter of 2011, the Company finalized the sale of its wholly owned subsidiary QBR which resulted in a gain of $4.68 million.

Questerre recorded a bad debt expense of $0.35 million in the first six months of 2011 (2010: $0.99 million), $0.17 million in the second quarter of 2011 (2010: $0.99 million) and $0.17 million in the prior quarter for amounts due from the joint venture partner at the Field. Questerre was the operator of the joint property and had exercised its first charge operators' lien which mitigated a portion of the exposure. No further bad debt expense for this property will be incurred for the remainder of the year following the sale of the Field in the second quarter of 2011.

Marketable securities represent investments in shares of public companies which are designated as available for sale and are stated at fair value. Any unrealized gain or loss is recognized in other comprehensive income (loss) for the period in which they arise. For the first six months of 2011, the Company recorded an unrealized loss net of deferred tax of $1.39 million (2010: nil). At June 30, 2011, Questerre holds marketable securities with a market value of $1.20 million.

Share Based Compensation

As at January 24, 2011, the Company amended its stock option plan to include a put right. Pursuant to the put right, an optionee may request the Company to purchase all or any part of the then vested options of the optionee for an amount equal to the market price of the common shares less the option price of the option shares. Notwithstanding the foregoing, the Company may, at its sole discretion, decline to accept and, accordingly, have no obligations with respect to the exercise of a put right at any time. Once the put options are cash settled, the options are cancelled. Under the plan, fair values are determined at each reporting date using the Black-Scholes option pricing model. Periodic changes in fair value are recognized in net profit (loss) as share based compensation expense with a corresponding change to the liability. Obligations for cash payments are recorded as a share based compensation liability based on the fair value of the liability at the reporting date. The prior period numbers before the modification remain unchanged.

Share based compensation expense for the second quarter of 2011 totaled $0.10 million (2010: $2.80 million) as compared to a recovery of $0.96 million in the prior quarter. For the first half of 2011, share based compensation was a recovery of $0.85 million compared to an expense of $4.04 million in the first half of 2010. As mandated by existing accounting standards, this represents the change in the estimated fair value of stock options outstanding using the Black-Scholes pricing model.

The Black-Scholes model calculates a theoretical value of the options based on the price of the Company's shares, its volatility, risk free rate and expected life. With the significant decrease in the Company's share price in the first half of 2011, the Black-Scholes values have decreased and therefore a recovery was recorded in the period.

Depletion, Depreciation and Accretion

Gross depletion and depreciation expense for the second quarter of 2011 increased 1% to $1.59 million from $1.57 million in the prior quarter. The increase in the gross expense is due to an 11% increase in the depletion rate from $26.77/boe in the prior quarter to $29.78/boe in the current quarter. The increase in the rate was almost entirely offset by the 10% decrease in production volumes over the prior period.

The higher depletable base in the current year accounts for the 32% increase, on a unit of production basis, from $22.54/boe in the prior year. With the higher rate partially offset by a 5% decrease in production volumes, gross depletion and depreciation expense increased from $1.27 million in the second quarter of 2010 to $1.59 million in the second quarter of 2011.

Questerre recognized $0.04 million in accretion expense for the second quarter of 2011 (2010: $0.05 million) and $0.05 million in the prior quarter. Year to date, the accretion expense is $0.09 million (2010: $0.09 million). The minor decrease in the current quarter relates to the sale of QBR in May 2011 and the corresponding decrease in the accretion expense for June 2011. The estimated net present value of the total asset retirement obligation is $3.87 million as at June 30, 2011 based on a total future undiscounted liability of $6.18 million.

Deferred Taxes

In the second quarter of 2011, Questerre reported a deferred tax expense of $0.10 million compared to a $0.40 million deferred tax recovery in the second quarter of 2010. The prior quarter had a deferred tax expense of $0.14 million. For the first half of 2011 a deferred tax expense of $0.24 million was recorded compared to a $0.30 million deferred tax recovery in the same period in 2010. Consistent with the prior periods, Questerre had sufficient tax pool deductions to offset taxable income in the first half of 2011.

Total Comprehensive Income (Loss)

Questerre recorded total comprehensive income of $3.54 million for the second quarter of 2011 compared to a $4.54 million total comprehensive loss in the second quarter of 2010. The year to date total comprehensive income is $4.78 million compared to a total comprehensive loss of $6.27 million in 2010. In 2011, the adoption of the liability method of accounting for share based compensation and the decrease in the fair value of the stock options created a year to date gain of $0.85 million for share based compensation compared to a $4.04 million expense in 2010. Increasing the total comprehensive income in 2011 was the $4.68 million gain on the sale of QBR. One significant item that decreased the 2011 total comprehensive income was a $1.39 million unrealized loss, net of deferred tax, on marketable securities. These are the three significant changes from the prior year with respect to the total comprehensive income (loss). The higher sales from the increased oil and liquids production and realized pricing also helped contribute to the total comprehensive income in 2011.

Capital Expenditures

	Three months ended June 30		*Six months ended June 30*	
	2011	2010	**2011**	2010
Saskatchewan	**$ 393,871**	$ 2,005,268	**$ 6,434,561**	$ 4,291,238
Québec	**508,529**	1,937,259	**1,588,019**	4,595,059
Alberta	**356,092**	(173,407)	**349,077**	(51,159)
Manitoba	**26,096**	-	**111,465**	-
British Columbia	**17,343**	23,790	**51,691**	34,812
Corporate	**3,850**	13,326	**14,448**	13,326
	$ 1,305,781	$ 3,806,236	**$ 8,549,261**	$ 8,883,276

Questerre incurred capital expenditures of $1.31 million in the second quarter of 2011 (2010: $3.81 million) and $8.55 million for the first half of the year (2010: $8.88 million), focused primarily on its light oil assets in Saskatchewan. The Company's significant capital expenditures for the first half of 2011 consisted of the following:

- In Saskatchewan, $6.43 million was incurred primarily to drill, complete and tie-in several wells. In the first half of 2011, the Company spud a total of eight (4.75 net) wells in the Antler area of Saskatchewan.
- $1.59 million was invested in the St. Lawrence Lowlands, Québec where the Company continues to focus on the evaluation of the Utica shale.

- The significant portion of the $0.35 million of Alberta expenditures relates to the drilling of one (0.50 net) oil well in the second quarter of 2011.
- The $0.11 million incurred in Manitoba primarily relates to acquiring land rights.

The Company's significant capital expenditures for the first half of 2010 consisted of the following:

- $4.60 million was invested in the St. Lawrence Lowlands, Québec where the Company finished the drilling of Gentilly No. 2 spud in the fourth quarter of 2009, spud two wells, Fortierville No. 1 and St. Gertrude No. 1 and continued the completion and testing of St. Edouard No. 1A to assess the Utica shale.
- In Saskatchewan $4.29 million was incurred in Antler primarily to drill, complete and tie-in several wells. During the period, the Company spud five (2.50 net) wells.
- In Alberta the resolution of a joint venture audit in the second quarter of 2010 resulted in the credit balance for the quarter and year to date.

Liquidity and Capital Resources

Questerre reported a working capital surplus of $131.31 million at June 30, 2011 as compared to a surplus of $136.08 million at December 31, 2010.

The Company's current assets consist of cash and cash equivalents of $128.15 million, $1.20 million of marketable securities, $6.89 million of accounts receivable, a $2.00 million loan receivable and $0.33 million in prepaids and deposits. Current liabilities of $7.25 million represent accounts payable and accrued liabilities.

The Company believes it is sufficiently capitalized with a working capital surplus of $131.31 million at June 30, 2011, positive cash flow from operations and no debt. The majority of future planned capital spending to be incurred in Québec is contingent upon the results of the pilot program conducted by Questerre's partners, the results of the strategic environmental assessment and the introduction of new hydrocarbon legislation. Subject to these conditions, Questerre anticipates its light oil assets will provide a further source of development capital for activities in Québec. As a result of its positive working capital position, the Company has elected to suspend its existing $5 million revolving credit facility with a Canadian chartered bank.

Cash Flow from Operations and Cash Flows from Operating Activities

Cash flow from operations in the second quarter of 2011 of $2.27 million was $0.63 million or 39% higher than the preceding quarter and $2.08 million or 1093% higher than the prior year second quarter. Year to date, the cash flow from operations of $3.90 million was $3.20 million or 453% higher than the first six months of 2010. The increase in the cash flow from operations in the current quarter from the preceding quarter was primarily due to options purchased by the Company pursuant to the put right in the first quarter totaling $0.57 million. Compared to the prior year periods, the increases are primarily due to significantly higher petroleum and natural gas sales and interest income along with lower royalties, operating and G&A expenses. On a year to date basis, the petroleum and natural gas sales increase is due to a 38% increase in the realized price to $72.56/boe (2010: $52.43/boe) and a 1% production increase.

Cash flows from operating activities for the first six months of 2011 was $4.11 million compared to $2.18 million in the same period in 2010. The increased cash flows from operating activities of $1.93 million is due to the negative change in the non-cash working capital of $1.26 million offset by the increase in the cash flow from operations of $3.20 million as discussed above.

Share Capital

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

	August 10 2011	June 30 2011	December 31 2010
Common shares	232,115,528	232,115,528	234,131,728
Stock options	21,674,169	21,814,169	20,035,835
Weighted average common shares			
Basic		233,981,259	227,181,288
Diluted		237,475,415	234,326,194

In December 2010, the Company announced its intention to conduct a Normal Course Issuer Bid ("NCIB") through the facilities of the TSX and the Oslo Stock Exchange. Under the terms of the NCIB, Questerre is authorized to acquire up to an aggregate of 11,706,586 of its common shares over the next 12-month period representing approximately 5% of its issued and outstanding common shares as at December 16, 2010. All common shares purchased by Questerre under the NCIB will be returned to treasury and cancelled. The NCIB commenced on December 22, 2010 and will terminate on December 21, 2011, or the earlier of the date all common shares which are subject to the NCIB are purchased.

To date 2,783,200 common shares have been purchased under the NCIB for consideration of $2.79 million. As of June 30, 2011, 425,000 common shares were pending cancellation but have subsequently been cancelled after the quarter end.

There have been 3,405,000 options granted, 767,000 options exercised by issue of common shares, 503,000 options purchased by the Corporation pursuant to the put right and 356,666 options forfeited during the first six months of 2011.

Commitments and Contingencies

Questerre has certain contractual obligations relating to the lease of office space and data licensing as set out in the table below:

	Total	Less than 1 year	1 - 3 years	4 - 5 years	After 5 years
Office lease	$ 1,343,725	$ 304,240	$ 608,479	$ 431,006	$ -
Data licensing	400,000	100,000	200,000	100,000	-
	$ 1,743,725	$ 404,240	$ 808,479	$ 531,006	$ -

The Company is a defendant and plaintiff in a number of legal actions arising in the normal course of business. The Company believes that any liabilities that might arise pertaining to any such matters would not have a material effect on its consolidated financial position.

In the second quarter of 2011, a joint venture partner filed a statement of claim with respect to amounts formally disputed by Questerre. Questerre has filed its statement of defense and counterclaim with respect to this issue. The claim is for $3.9 million and the entire amount is accounted for in the consolidated financial statements.

Risk Management

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, 2010.

Accounting Standards Changes

Questerre has completed its adoption of IFRS for the year beginning on January 1, 2011. As a result, the Company's financial results for 2011 and comparative periods are reported under IFRS while selected historical data continues to be reported under previous GAAP.

The key areas of adjustment to the January 1, 2010 and December 31, 2010 balance sheets as a result of the transition to IFRS were as follows:

- Impairment of Property, Plant and Equipment ("PP&E") under IFRS was tested as required on initial transition to IFRS based on discounted cash flows for each Cash Generating Unit ("CGU"), which is a more granular level than required under previous GAAP. Also, under previous GAAP, a discounted cash flow analysis was not required if the undiscounted cash flows from proved reserves exceeded the carrying amount. As at January 1, 2010, the Company recorded an impairment of $18.52 million, which reduced PP&E with a corresponding charge to deficit. For the year ended December 31, 2010, additional impairment of natural gas assets of $1.36 million was recorded in net profit (loss), with a corresponding decrease to PP&E.
- Under previous GAAP, asset retirement obligations were discounted at a credit adjusted risk fee rate of 7 and 12 percent. The estimated cash flow to abandon and remediate the wells and facilities was risk adjusted under previous GAAP; therefore, the obligation is discounted at a risk free rate under IFRS. The risk free rate is based on the Government of Canada bonds rates based on the remaining life to abandon each well. At January 1, 2010 the Company used a risk free rate that ranged from 1.45 to 4.10 percent. Upon transition to IFRS this resulted in a $1.89 million increase in the asset retirement obligation with a corresponding increase in the deficit.
- Under previous GAAP, the Company followed the full cost method of accounting for oil and gas properties whereby all costs of acquisition, exploration for and development of oil and gas reserves were capitalized at the cost-centre level. Under IFRS, pre-exploration costs are expensed as incurred. After the legal right to explore is acquired, exploration costs are capitalized as exploration and evaluation assets. Once the exploration area achieves technical feasibility and commercial viability, exploration and evaluation costs are moved to PP&E. Upon transition to IFRS, the Company reclassified $23.62 million of PP&E to exploration and evaluation assets. As at December 31, 2010, the Company reclassified $49.76 million of PP&E to exploration and evaluation assets.
- Nearly all the previous GAAP to IFRS differences have an impact on deferred taxes as the adjustments change the accounting balance and the amount of the temporary or permanent differences. The impact of these changes increased the deferred tax asset by $5.69 million as at January 1, 2010 and by $3.56 million as at December 31, 2010 under IFRS.

The additional impacts of the IFRS transition on the Company's net profit (loss) are as follows:

- Upon transition to IFRS, the Company adopted a policy of depleting oil and natural gas interests on a unit of production basis over net proved plus probable reserves. The depletion policy under previous GAAP was based on units of production over proved reserves. In addition depletion was calculated at a Canadian cost-centre level under previous GAAP. IFRS requires depletion and depreciation to be calculated based on individual components. For the year ended December 31, 2010 transition differences resulted in a decrease to depletion of $7.33 million with a corresponding change to PP&E.
- Under previous GAAP, proceeds from divestitures were deducted from the full cost pool without recognition of a gain or loss unless the deduction resulted in a change to the depletion rate of 20% or greater. Under IFRS, gains or losses are recorded on divestitures and calculated as the difference between the proceeds and the net book value of the asset disposed. For the year ended December 31, 2010, the Company recognized a $0.34 million gain on divestitures in net profit (loss).
- Under previous GAAP, the Company's equity-settled stock options were measured at their fair value at the grant date. This amount was expensed to stock based compensation on the income statement over the vesting period using graded vesting. Forfeitures were accounted for as they occurred. Under IFRS, an estimate of forfeitures must be factored into the calculation of the expense at the grant date and any difference between the estimates and actual is recognized in the period when actual forfeitures are incurred. The effect on net profit (loss) for the year ended December 31, 2010 is to reduce share based compensation expense by $0.32 million with a corresponding decrease to contributed surplus.
- Future income taxes are now referred to as deferred taxes.

Refer to the notes of the interim consolidated financial statements for further details on the impacts of the transition to IFRS.

Future Accounting Pronouncements

The following standards and interpretations have not been illustrated as they will only be applied for the first time in future periods. They may result in consequential changes to the accounting policies and other note disclosures. The Company is currently evaluating the impact of adopting these standards on its consolidated financial statements.

IFRS 9 Financial Instruments

As at January 1, 2015, the Company will be required to adopt IFRS 9 *Financial Instruments*, which is the result of the first phase of the International Accounting Standards Board's ("IASB") project to release IAS 19 *Financial Instruments: Recognition and Measurement*. The new standard was issued in November 2009 and replaces the current multiple classification and measurement models for financial assets and liabilities with a single model that has only two classification categories: amortized cost and fair value. IFRS 9 also replaces the models for measuring equity instruments, and such instruments are either recognized at fair value through net profit (loss) or at fair value through other comprehensive income (loss). Where such equity instruments are measured at fair value through other comprehensive income (loss), dividends are recognized in net profit (loss) to the extent they are not clearly representing a return of investment, however, other gains and losses (including impairments) associated with such instruments remain in accumulated comprehensive income (loss) indefinitely.

Requirements for financial liabilities were added in October 2010 and they largely carried forward existing requirements in IAS 39 *Financial Instruments: Recognition and Measurement,* except that fair value changes due to credit risk for liabilities designated at fair value through net profit (loss) would generally be recorded in other comprehensive income (loss).

<u>IFRS 10 Consolidation</u>

IFRS 10 revises the definition of control and focuses on the need to have power and variable returns for control to be present. IFRS 10 provides guidance on participating and protective rights and also addresses the notion of "de facto" control. It also includes guidance related to an investor with decision making rights to determine if it is acting as a principal or agent. IFRS 10 replaces SIC-12 *Consolidation—Special Purpose Entities* and parts of IAS 27 *Consolidated and Separate Financial Statements*.

IAS 27 has been amended to conform to the changes made in IFRS 10 but retains the current guidance for separate financial statements.

<u>IFRS 11 Joint Arrangements</u>

IFRS 11 requires a venturer to classify its interest in a joint arrangement as a joint venture or joint operation. Joint ventures will be accounted for using the equity method of accounting whereas for a joint operation the venturer will recognize its share of the assets, liabilities, revenue and expenses of the joint operation. Under existing IFRS, entities have the choice to proportionately consolidate or equity account for interests in joint ventures. IFRS 11 supersedes IAS 31 *Interests in Joint Ventures* and SIC-13 *Jointly Controlled Entities—Non-monetary Contributions by Venturers*.

<u>IFRS 12 Disclosure of Interest in Other Entities</u>

IFRS 12 establishes disclosure requirements for interests in other entities, such as joint arrangements, associates, special purpose vehicles and off balance sheet vehicles. The standard carries forward existing disclosures and also introduces significant additional disclosure requirements that address the nature of, and risks associated with, an entity's interests in other entities. IFRS 12 replaces disclosure requirements previously included in IAS 27, IAS 31 and IAS 28 *Investments in Associates*.

IAS 28 has been amended to conform to the changes made in IFRS 10 and IFRS 11.

<u>IFRS 13 Fair Value Measurement</u>

IFRS 13 is a comprehensive standard for fair value measurement and disclosure requirements for use across all IFRS standards. The new standard clarifies that fair value is the price that would be received to sell an asset, or paid to transfer a liability in an orderly transaction between market participants, at the measurement date. It also establishes disclosures about fair value measurement. Under existing IFRS, guidance on measuring and disclosing fair value is dispersed among the specific standards requiring fair value measurements and in many cases does not reflect a clear measurement basis or consistent disclosures.

The above four standards are effective for annual periods beginning on or after January 1, 2013. Early adoption is permitted, providing the standards are adopted concurrently.

IAS 1 Presentation of Financial Statements

In June 2011, the IASB issued an amendment to IAS 1 *Presentation of Financial Statements* requiring companies to group items presented within other comprehensive income (loss) based on whether they may be subsequently reclassified to net profit (loss). This amendment to IAS 1 is effective for annual periods beginning on or after July 1, 2012 with full retrospective application. Early adoption is permitted.

Internal Control Over Financial Reporting

Questerre is required to comply with National Instrument 52-109 "Certification of Disclosure in Issuers' Annual and Interim Filings". The 2011 certificate requires that the Company disclose in the interim MD&A any changes in the Company's internal controls over financial reporting that occurred during the period that have materially affected, or are reasonably likely to materially affect the Company's internal control over financial reporting.

Management completed an assessment of the internal controls over financial reporting. During the process of management's assessment, it was determined that certain weaknesses existed in internal controls over financial reporting. The weaknesses are the result of the Company's size and limited number of staff and include: (i) the inability to achieve complete segregation of duties; and (ii) having insufficient staff with the required technical tax knowledge to deal with complex and non-routine matters. The Company believes that these weaknesses are mitigated by: (i) the President and Chief Executive Officer and the Chief Financial Officer overseeing all material transactions; (ii) the audit committee, comprised of independent members of the Board of Directors, reviewing the quarterly interim and annual audited financial statements with management; (iii) the Board of Directors' approval of the financial statements based on the audit committee's recommendation after its review; and (iv) the Company consulting with its third party expert advisors as needed in connection with the recording and reporting of complex and non-routine transactions.

The Company has evaluated the impact of the adoption of IFRS on its processes, controls and financial reporting systems and has made modifications to its control environment accordingly. There were no significant changes in Questerre's internal control over financial reporting during the quarter ended June 30, 2011 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

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.

Quarterly Financial Information

	June 30 2011	March 31 2011	December 31 2010	September 30 2010
Production (boe/d)	**586**	650	605	649
Average Realized Price ($/boe)	**77.60**	67.78	58.33	49.47
Petroleum and Natural Gas Sales	**4,138,050**	3,965,389	3,246,637	2,953,980
Cash Flow from Operations	**2,267,676**	1,636,950	2,599,486	1,438,666
Per share - Basic	**0.01**	0.01	0.01	0.01
Per share - Diluted	**0.01**	0.01	0.01	0.01
Net Profit (Loss)	**4,938,387**	1,234,259	(3,011,526)	(1,652,678)
Per share - Basic	**0.02**	0.01	(0.01)	(0.01)
Per share - Diluted	**0.02**	0.01	(0.01)	(0.01)
Capital Expenditures, net of acquisitions and dispositions	**1,305,781**	7,243,480	20,916,846	8,606,402
Working Capital Surplus	**131,312,369**	130,616,809	136,076,978	154,531,153
Total Assets	**250,973,021**	261,365,161	260,548,991	261,433,625
Shareholders' Equity	**234,312,816**	232,275,278	238,686,128	239,189,258
Weighted Average Common Shares Outstanding				
Basic	**233,610,707**	234,434,615	234,126,067	234,021,347
Diluted	**236,472,552**	238,509,767	238,754,183	240,363,560

Note: The 2009 periods below represent previous GAAP.

	June 30 2010	March 31 2010	December 31 2009	September 30 2009
Production (boe/d)	620	600	759	632
Average Realized Price ($/boe)	49.87	55.10	49.37	47.92
Petroleum and Natural Gas Sales	2,813,743	2,975,353	3,447,123	2,786,384
Cash Flow from Operations	190,017	516,391	595,717	502,357
Per share - Basic	-	-	-	-
Per share - Diluted	-	-	-	-
Net Loss[(1)]	(4,535,629)	(1,734,052)	(3,898,088)	(2,838,032)
Per share - Basic	(0.02)	(0.01)	(0.02)	(0.01)
Per share - Diluted	(0.02)	(0.01)	(0.02)	(0.01)
Capital Expenditures, net of acquisitions and dispositions	3,806,236	5,077,040	3,438,205	3,259,938
Working Capital Surplus	160,932,087	165,597,791	46,500,671	49,016,405
Total Assets	258,023,289	261,952,906	145,272,364	149,304,238
Shareholders' Equity	237,989,679	239,742,030	129,977,202	132,216,221
Weighted Average Common Shares Outstanding				
Basic	233,809,187	206,388,591	199,243,068	197,827,758
Diluted	240,694,908	216,789,825	208,653,009	206,723,239

(1) The net loss for the three months ended September 30, 2009 has been restated. Questerre acquired Terrenex Ltd. and its wholly owned foreign subsidiary Cabernet Holdings Ltd. ("Cabernet") on April 28, 2008. The only significant asset Cabernet owned was Questerre common shares. On July 22, 2009, Cabernet was dissolved and a taxable event was deemed to have occurred. The result was presented on the September 30, 2009 financial statements as a $1,256,314 increase to the future tax asset on the balance sheet. The offset was initially recorded to the future tax recovery line on the statements of operations and as a result the deficit line on the balance sheet. Upon subsequent review, since the recovery related to an equity item it should have been booked to common shares in the shareholders' equity section.

The general trends over the last eight quarters are as follow:

- The increased development spending in 2010 and 2011 in Antler is beginning to generate production and cash flow growth but production decreases in both Beaver River and Vulcan have generally offset the production gains to date. This was compounded with the sale of QBR in the second quarter of 2011. During the third quarter of 2009, a significant portion of the natural gas production in BC was shut-in due to the low price environment resulting in a marked decrease in volumes over the prior quarters.
- With an increasing percentage of Questerre's volumes being comprised of oil and liquids and the corresponding increase of the realized oil and liquids pricing, petroleum and natural gas sales has increased in recent quarters.
- Following the same trend as the petroleum and natural gas sales, the cash flow from operations has increased in recent quarters due to the increase in higher netback oil and liquids volumes and decreased cash costs.
- In the second quarter of 2010, the net loss increased due to additional share based compensation expense and bad debt expense. The decreased net loss in the third quarter of 2010 is primarily due to the gain on extinguishment of liabilities related to Magnus entities. In the first quarter of 2011, with the adoption of the liability method of accounting for stock options, the decrease in the fair value of the stock options at the end of the quarter created a gain for share based compensation and overall a net profit. In the second quarter of 2011, the higher profit is primarily due to the gain on the sale of the QBR subsidiary.
- The working capital surplus, total assets and shareholders' equity were all relatively consistent until the first quarter of 2010 when a financing was closed for gross proceeds of $127.91 million.

Consolidated Balance Sheets

(unaudited)

(Canadian dollars)	Note		**June 30 2011**		December 31 2010		January 1 2010
					(Note 15)		*(Note 15)*
Assets							
Current Assets							
Cash and cash equivalents		**$**	**128,147,962**	$	141,974,856	$	51,396,052
Marketable securities	5		**1,200,000**		-		204,336
Accounts receivable			**6,890,516**		7,894,381		4,509,203
Loan receivable	6		**2,000,000**		-		-
Inventory	7		**-**		344,138		301,599
Deposits and prepaid expenses			**325,540**		507,124		619,990
			138,564,018		150,720,499		57,031,180
Investments	5		**494,506**		-		-
Property, plant and equipment	8		**52,250,721**		48,249,407		42,145,349
Exploration and evaluation assets	9		**51,717,450**		49,762,437		23,621,537
Goodwill			**2,345,944**		2,467,816		2,467,816
Deferred tax assets			**5,600,382**		9,348,832		7,180,344
		$	**250,973,021**	$	260,548,991	$	132,446,226
Liabilities							
Current Liabilities							
Accounts payable and accrued liabilities		**$**	**7,251,649**	$	14,643,521	$	10,530,509
Current portion of share based compensation liability	12		**4,497,743**		-		-
			11,749,392		14,643,521		10,530,509
Asset retirement obligation	10		**3,867,536**		7,219,342		6,655,654
Share based compensation liability	12		**1,043,277**		-		-
			16,660,205		21,862,863		17,186,163
Shareholders' Equity							
Share capital	11		**309,112,753**		311,652,770		184,962,957
Contributed surplus			**12,276,394**		18,888,735		11,218,598
Accumulated other comprehensive income (loss)			**(1,393,600)**		-		-
Deficit			**(85,682,731)**		(91,855,377)		(80,921,492)
			234,312,816		238,686,128		115,260,063
		$	**250,973,021**	$	260,548,991	$	132,446,226

Commitments and contingencies (note 13).

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

Consolidated Statements of Net Profit (Loss), and Comprehensive Income (Loss)

(unaudited)

(Canadian dollars)	Note	Three months ended June 30 **2011**	Three months ended June 30 2010	Six months ended June 30 **2011**	Six months ended June 30 2010
Revenue					
Petroleum and natural gas sales		**$ 4,138,050**	$ 2,813,743	**$ 8,103,439**	$ 5,789,096
Royalties		**(333,185)**	(726,043)	**(679,114)**	(1,127,268)
Petroleum and natural gas revenue, net of royalties		**3,804,865**	2,087,700	**7,424,325**	4,661,828
Expenses					
Operating		**671,844**	876,530	**1,454,248**	1,827,162
General and administrative		**1,273,279**	1,450,594	**2,365,205**	2,660,425
Pre-exploration		**40,750**	-	**40,750**	-
(Gain) loss on marketable securities		**-**	21,875	**-**	(321,524)
Gain on sale of subsidiary	1	**(4,682,182)**	-	**(4,682,182)**	-
Bad debt expense		**174,395**	985,939	**347,834**	985,939
Depletion and depreciation	8, 9	**1,587,960**	1,272,145	**3,153,739**	2,481,734
Accretion of asset retirement obligation	10	**44,063**	45,846	**90,391**	88,422
Share based compensation (recovery)	12	**103,048**	2,804,446	**(853,727)**	4,043,978
		(786,843)	7,457,375	**1,916,258**	11,766,136
Interest income		**448,684**	430,053	**907,574**	537,391
Profit (loss) before taxes		**5,040,392**	(4,939,622)	**6,415,641**	(6,566,917)
Deferred taxes (recovery)		**102,005**	(403,993)	**242,995**	(297,236)
Net profit (loss)		**4,938,387**	(4,535,629)	**6,172,646**	(6,269,681)
Other comprehensive income (loss), net of tax					
Unrealized loss on marketable securities	5	**(1,393,600)**	-	**(1,393,600)**	-
Total comprehensive income (loss)		**$ 3,544,787**	$ (4,535,629)	**$ 4,779,046**	$ (6,269,681)
Net profit (loss) per share					
Basic and diluted	11	**$ 0.02**	$ (0.02)	**$ 0.03**	$ (0.03)

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

Consolidated Statements of Changes in Equity

(unaudited)

	Note	Share capital	Contributed surplus	AOCI *	Deficit	Total equity
Balance at January 1, 2010		$ 184,962,957	$ 11,218,598	$ -	$ (80,921,492)	$ 115,260,063
Issue of common shares	11	127,907,414	-	-	-	127,907,414
Share issue costs, net of tax of $1,682,620	11	(5,318,056)	-	-	-	(5,318,056)
Options exercised	12	3,777,314	(1,411,353)	-	-	2,365,961
Share based compensation	12	-	4,043,978	-	-	4,043,978
Net loss		-	-	-	(6,269,681)	(6,269,681)
Balance at June 30, 2010		$ 311,329,629	$ 13,851,223	$ -	$ (87,191,173)	$ 237,989,679
Balance at January 1, 2011		$ 311,652,770	$ 18,888,735	$ -	$ (91,855,377)	$ 238,686,128
Options exercised	11	995,480	-	-	-	995,480
Normal course issuer bid	11	(3,535,497)	744,330	-	-	(2,791,167)
Reclassification of share based compensation	12	-	(7,356,671)	-	-	(7,356,671)
Other comprehensive loss		-	-	(1,393,600)	-	(1,393,600)
Net profit		-	-	-	6,172,646	6,172,646
Balance at June 30, 2011		**$ 309,112,753**	**$ 12,276,394**	**$ (1,393,600)**	**$ (85,682,731)**	**$ 234,312,816**

**Accumulated other comprehensive income*

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

Consolidated Statements of Cash Flows

(unaudited)

(Canadian dollars)	Note	Three months ended June 30 **2011**	2010	Six months ended June 30 **2011**	2010
Operating Activities					
Net profit (loss)		**$ 4,938,387**	$ (4,535,629)	**$ 6,172,646**	$ (6,269,681)
Adjustments for:					
Depletion and depreciation	8, 9	**1,587,960**	1,272,145	**3,153,739**	2,481,734
Accretion of asset retirement obligation	10	**44,063**	45,846	**90,391**	88,422
Share based compensation (recovery)	12	**103,048**	2,804,446	**(853,727)**	4,043,978
(Gain) loss on marketable securities		**-**	21,875	**-**	(321,524)
Gain on sale of subsidiary		**(4,682,182)**	-	**(4,682,182)**	-
Bad debt expense		**174,395**	985,939	**347,834**	985,939
Deferred taxes (recovery)		**102,005**	(403,993)	**242,995**	(297,236)
Cash paid on exercise of stock options	12	**-**	-	**(567,070)**	-
Abandonment expenditures		**-**	(612)	**-**	(5,224)
		2,267,676	190,017	**3,904,626**	706,408
Change in non-cash working capital		**979,536**	(674,199)	**209,082**	1,473,564
Net cash from operating activities		**3,247,212**	(484,182)	**4,113,708**	2,179,972
Investing Activities					
Property, plant and equipment expenditures		**(686,947)**	(1,868,977)	**(6,478,186)**	(4,288,217)
Exploration and evaluation expenditures		**(618,834)**	(1,937,259)	**(2,071,075)**	(4,595,059)
Disposition of subsidiary		**(705,986)**	-	**(705,986)**	-
Proceeds from sale of marketable securities		**-**	346,425	**-**	525,860
Purchase of investments		**(494,506)**	-	**(494,506)**	-
Change in non-cash working capital		**(5,315,739)**	(3,806,469)	**(5,936,732)**	(2,169,105)
Net cash used in investing activities		**(7,822,012)**	(7,266,280)	**(15,686,485)**	(10,526,521)
Financing Activities					
Proceeds from issue of share capital		**217,250**	35,825	**537,050**	130,273,375
Repurchase of shares under normal course issuer bid	11	**(2,791,167)**	-	**(2,791,167)**	-
Share issuance costs		**-**	(77,496)	**-**	(7,000,676)
Net cash from financing activities		**(2,573,917)**	(41,671)	**(2,254,117)**	123,272,699
Change in cash and cash equivalents		**(7,148,717)**	(7,792,133)	**(13,826,894)**	114,926,150
Cash and cash equivalents, beginning of period		**135,296,679**	174,114,335	**141,974,856**	51,396,052
Cash and cash equivalents, end of period		**$ 128,147,962**	$ 166,322,202	**$ 128,147,962**	$ 166,322,202

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

1. Reporting Entity

Questerre Energy Corporation ("Questerre" or "the Company") is a full cycle exploration and production company. The Company targets scalable high-impact projects and has developed a portfolio of exploration and production assets. The interim consolidated financial statements of the Company as at and for the three and six months ended June 30, 2011 and 2010 comprise the Company and its wholly owned subsidiaries in those periods owned.

On June 18, 2008, Magnus Energy Inc. ("Magnus") and its wholly-owned subsidiary Magnus One Energy Corp. (collectively the "Magnus entities") applied for protection under the *Bankruptcy and Insolvency Act (Canada).* Magnus was a wholly-owned subsidiary of Questerre. In the third quarter of 2010, the Company finalized the assignment of the Magnus entities into bankruptcy. This transaction resulted in a gain on extinguishment of liabilities related to Magnus entities of $1,130,345.

In May 2011, Questerre concluded its agreement with Transeuro Energy Corp. ("Transeuro") for Transeuro to acquire the remaining 50% interest in the Beaver River Field (the "Field").

Pursuant to the agreement, Transeuro acquired all the issued and outstanding shares of Questerre Beaver River Inc. ("QBR"), a wholly owned subsidiary of the Company that owns the other 50% interest in the Field. In consideration, Questerre received 40 million common shares of Transeuro representing 8.7% of the outstanding common shares of the company, valued at $2,800,000. The sale of QBR resulted in a gain on the sale of the subsidiary of $4,804,054 and a write down of goodwill of $121,872.

Questerre has also advanced Transeuro a $2 million loan to fund its ongoing operations. The loan will be due and payable on the earlier of 12 months or the announcement of a future financing by Transeuro. Questerre has plans to maintain its share position through a $2 million commitment to this future financing by Transeuro subject to final terms.

Questerre is incorporated under the laws of the Province of Alberta and is domiciled in Canada. The address of its registered office is 1650, 801 – 6th Avenue SW, Calgary, Alberta.

2. Basis of Preparation

a) Statement of compliance

The Company prepares its consolidated financial statements in accordance with Canadian generally accepted accounting principles as set out in the Handbook of the Canadian Institute of Chartered Accountants ("CICA Handbook"). In 2010, the CICA Handbook was revised to incorporate International Financial Reporting Standards ("IFRS"), and require publicly accountable enterprises to apply such standards effective for years beginning on or after January 1, 2011. Accordingly, the Company commenced reporting on this basis in its 2011 interim consolidated financial statements. In these consolidated financial statements, the term "previous GAAP" refers to Canadian GAAP before the adoption of IFRS.

These interim consolidated financial statements have been prepared in accordance with IFRS applicable to the preparation of interim financial statements, including International Accounting Standard ("IAS") 34 *Interim Financial Reporting*, and IFRS 1 *First-Time Adoption of International Financial Reporting Standards* ("IFRS 1"). The accounting policies followed in these interim financial statements are the same as those applied in the Company's interim financial statements for the period ended March 31, 2011. The Company has consistently applied the same accounting policies throughout all periods presented, as if these policies had always been in effect. Note 15 discloses the impact of the transition to IFRS on the Company's reported equity as at June 30, 2010 and comprehensive income (loss) for the three and six months ended June 30, 2010, including the nature and effect of significant changes in accounting policies from those used in the Company's consolidated financial statements for the year ended December 31, 2010.

The policies applied in these interim consolidated financial statements are based on IFRS issued and outstanding as of August 10, 2011, the date the Board of Directors approved the statements. Any subsequent changes to IFRS that are given effect in the Company's annual consolidated financial statements for the year ending December 31, 2011 could result in restatement of these interim consolidated financial statements, including the adjustments recognized on transition to IFRS.

The condensed interim consolidated financial statements should be read in conjunction with the Company's previous GAAP annual consolidated financial statements for the year ended December 31, 2010, and the Company's interim consolidated financial statements for the quarter ended March 31, 2011 prepared in accordance with IFRS applicable to interim financial statements.

b) Basis of measurement

The interim consolidated financial statements have been prepared on the historical cost basis except for available for sale financial assets and share based payment transactions which are measured at fair value with changes in fair value recorded in other comprehensive income (loss) or net profit (loss).

c) Functional and presentation currency

These interim consolidated financial statements are presented in Canadian dollars, which is the Company's functional currency.

d) Jointly controlled assets

Many of the Company's oil and natural gas activities involve jointly controlled assets. The interim consolidated financial statements include the Company's share of these jointly controlled assets and a proportionate share of the relevant revenue and related costs.

3. Changes in Accounting Policies and Disclosures

a) New and amended standards and interpretations

Accounting standards effective for periods beginning on or after January 1, 2011 have been adopted as part of the transition to IFRS.

b) Standards issued but not yet effective

The following standards and interpretations have not been illustrated as they will only be applied for the first time in future periods. They may result in consequential changes to the accounting policies and other note disclosures. The Company is currently evaluating the impact of adopting these standards on its consolidated financial statements.

IFRS 9 Financial Instruments

As at January 1, 2015, the Company will be required to adopt IFRS 9 *Financial Instruments*, which is the result of the first phase of the International Accounting Standards Board's ("IASB") project to release IAS 19 *Financial Instruments: Recognition and Measurement*. The new standard was issued in November 2009 and replaces the current multiple classification and measurement models for financial assets and liabilities with a single model that has only two classification categories: amortized cost and fair value. IFRS 9 also replaces the models for measuring equity instruments, and such instruments are either recognized at fair value through net profit (loss) or at fair value through other comprehensive income (loss). Where such equity instruments are measured at fair value through other comprehensive income (loss), dividends are recognized in net profit (loss) to the extent they are not clearly representing a return of investment, however, other gains and losses (including impairments) associated with such instruments remain in accumulated comprehensive income (loss) indefinitely.

Requirements for financial liabilities were added in October 2010 and they largely carried forward existing requirements in IAS 39 *Financial Instruments: Recognition and Measurement,* except that fair value changes due to credit risk for liabilities designated at fair value through net profit (loss) would generally be recorded in other comprehensive income (loss).

IFRS 10 Consolidation

IFRS 10 revises the definition of control and focuses on the need to have power and variable returns for control to be present. IFRS 10 provides guidance on participating and protective rights and also addresses the notion of "de facto" control. It also includes guidance related to an investor with decision making rights to determine if it is acting as a principal or agent. IFRS 10 replaces SIC-12 *Consolidation—Special Purpose Entities* and parts of IAS 27 *Consolidated and Separate Financial Statements*.

IAS 27 has been amended to conform to the changes made in IFRS 10 but retains the current guidance for separate financial statements.

IFRS 11 Joint Arrangements

IFRS 11 requires a venturer to classify its interest in a joint arrangement as a joint venture or joint operation. Joint ventures will be accounted for using the equity method of accounting whereas for a joint operation the venturer will recognize its share of the assets, liabilities, revenue and expenses of the joint operation. Under existing IFRS, entities have the choice to proportionately consolidate or equity account for interests in joint ventures. IFRS 11 supersedes IAS 31 *Interests in Joint Ventures*, and SIC-13 *Jointly Controlled Entities—Non-monetary Contributions by Venturers*.

IFRS 12 Disclosure of Interest in Other Entities

IFRS 12 establishes disclosure requirements for interests in other entities, such as joint arrangements, associates, special purpose vehicles and off balance sheet vehicles. The standard carries forward existing disclosures and also introduces significant additional disclosure requirements that address the nature of, and risks associated with, an entity's interests in other entities. IFRS 12 replaces disclosure requirements previously included in IAS 27, IAS 31 and IAS 28 *Investments in Associates*.

IAS 28 has been amended to conform to the changes made in IFRS 10 and IFRS 11.

IFRS 13 Fair Value Measurement

IFRS 13 is a comprehensive standard for fair value measurement and disclosure requirements for use across all IFRS standards. The new standard clarifies that fair value is the price that would be received to sell an asset, or paid to transfer a liability in an orderly transaction between market participants, at the measurement date. It also establishes disclosures about fair value measurement. Under existing IFRS, guidance on measuring and disclosing fair value is dispersed among the specific standards requiring fair value measurements and in many cases does not reflect a clear measurement basis or consistent disclosures.

The above four standards are effective for annual periods beginning on or after January 1, 2013. Early adoption is permitted, providing the standards are adopted concurrently.

IAS 1 Presentation of Financial Statements

In June 2011, the IASB issued an amendment to IAS 1 *Presentation of Financial Statements* requiring companies to group items presented within other comprehensive income (loss) based on whether they may be subsequently reclassified to net profit (loss). This amendment to IAS 1 is effective for annual periods beginning on or after July 1, 2012 with full retrospective application. Early adoption is permitted.

4. Financial Risk Management

a) Overview

The Company's activities expose it to a variety of financial risks that arise as a result of its exploration, development, production, and financing activities such as credit risk, liquidity risk and market risk. The Company manages its exposure to these risks by operating in a manner that minimizes this exposure.

b) Fair value of financial instruments

The Company's financial instruments as at June 30, 2011 included cash and cash equivalents, marketable securities, investments, accounts receivable, loan receivable, accounts payable and accrued liabilities. As at June 30, 2011, all the Company's financial assets and liabilities are recorded at their carrying value as it approximates fair value.

The disclosures about the inputs to fair value measurements are required, including their classification within a hierarchy that prioritizes the inputs to fair value measurement.

Level 1 Fair Value Measurements

Level 1 fair value measurements are based on unadjusted quoted market prices.

Marketable securities – The fair value of marketable securities are determined by the closing bid price per share as at the balance sheet date multiplied by the number of shares. As the marketable securities are recorded at fair value using quoted market prices they are classified as Level 1 of the hierarchy.

Level 2 Fair Value Measurements

Level 2 fair value measurements are based on valuation models and techniques where the significant inputs are derived from quoted indices.

Level 3 Fair Value Measurements

Level 3 fair value measurements are based on unobservable information.

Investments – The fair value is determined using valuation models where significant inputs are not derived from observable market data.

As at each reporting period, the Company will assess whether a financial asset, other than those classified as held-for-trading is impaired. Any impairment loss will be included in net profit (loss) for the period.

c) Credit risk

Substantially all of the accounts receivable are with customers and joint venture partners in the oil and gas industry and are subject to normal industry credit risks. The Company generally extends unsecured credit to these customers and therefore, the collection of accounts receivable may be affected by changes in economic or other conditions. Management believes the risk is mitigated by entering into transactions with long-standing, reputable counterparties and partners. Wherever possible, the Company requires cash calls from its partners on capital projects before they commence. Accounts receivable related to the sale of the Company's petroleum and natural gas production is paid in the following month from major marketing companies and the Company has not experienced any credit loss relating to these sales.

The Company's accounts receivables are aged as follows:

		June 30 2011		December 31 2010
Current	**$**	**1,798,903**	$	4,772,869
31 - 60 days		**291,705**		1,587,619
61 - 90 days		**1,191,486**		1,048,305
>90 days		**3,702,136**		5,725,622
Allowance for doubtful accounts		**(93,714)**		(5,240,034)
	$	**6,890,516**	$	7,894,381

The Company has a $2 million loan receivable due from Transeuro. The receivable is due on the earlier of 12 months or the announcement of a future financing by Transeuro. Management believes the risk is mitigated by several commitments related to the future financing.

d) Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they become due. The Company's processes for managing liquidity risk include ensuring, to the extent possible, that it will have sufficient liquidity to meet its liabilities when they become due. The Company prepares annual capital expenditure budgets which are monitored and are updated as required. In addition, the Company requires authorizations for expenditures on projects to assist with the management of capital.

Since the Company operates in the upstream oil and gas industry, it requires sufficient cash to fund capital programs necessary to maintain or increase production, develop reserves and to potentially acquire strategic assets. The Company's capital programs are funded principally by cash obtained through equity issuances and from operating activities. During times of low oil and natural gas prices, a portion of capital programs can generally be deferred, however, due to the long cycle times and the importance to future cash flow in maintaining the Company's production, it may be necessary to utilize alternative sources of capital to continue the Company's strategic investment plan during periods of low commodity prices. As a result, the Company frequently evaluates the options available with respect to sources of long and short term capital resources. Occasionally, to the extent possible, the Company will use derivative instruments to manage cash flow in the event of commodity price declines.

e) Market risk

Market risk is the risk that changes in market prices, such as commodity prices, foreign exchange rates and interest rates will affect the Company's profit or the value of the financial instruments. The objective of the Company is to mitigate exposure to these risks while maximizing returns to the Company.

Commodity price risk

Commodity price risk is the risk that the fair value or future cash flows will fluctuate as a result of changes in commodity prices. Commodity prices for oil and natural gas are impacted by not only the relationship between the Canadian and United States dollar but also world economic events that dictate the levels of supply and demand. The Company may enter into oil and natural gas contracts to protect, to the extent possible, its cash flow on future sales. The contracts reduce the volatility in sales revenue by locking in prices with respect to future deliveries of oil and natural gas. As at June 30, 2011, the Company had no oil and natural gas risk management contracts in place.

Currency risk

Even though all of Questerre's petroleum and natural gas sales are denominated in Canadian dollars, the underlying market prices for these commodities are impacted by the exchange rate between Canada and the United States. As at June 30, 2011, the Company had no forward foreign exchange contracts in place.

Interest rate risk

Interest rate risk is the risk that future cash flows will fluctuate as a result of changes in market interest rates. The Company has had no debt outstanding, interest rate swaps or financial contracts in place at or during the period ended June 30, 2011.

f) Capital management

The Company believes it is well capitalized with positive cash flow from operations (a non-GAAP measure defined as cash flows from operating activities before changes in non-cash operating working capital), no debt and a working capital surplus (defined as current assets less current liabilities excluding the current portion of the share based compensation liability) of over $131 million consisting mainly of cash and cash equivalents.

The volatility of commodity prices have a material impact on Questerre's cash flow from operations. Questerre attempts to mitigate the effect of lower prices by shutting in production in unusually low pricing environments, reallocating capital to more profitable areas and reducing capital spending based on results and other market considerations.

The Company considers its capital structure to include shareholders' equity and any outstanding debt. The Company will adjust its capital structure to minimize its cost of capital through the issuance of shares, securing credit facilities and adjusting its capital spending. Questerre monitors its capital structure based on the current and projected cash flow from operations.

	June 30 2011	December 31 2010	January 1 2010
Shareholders' equity	$ 234,312,816	$ 238,686,128	$ 115,260,063

5. Marketable Securities & Investments

		June 30 2011		December 31 2010
Current investments:				
Marketable securities	**$**	**1,200,000**	$	-
Long-term investments:				
Other equity investment		**494,506**		-
	$	**1,694,506**	$	-

Marketable securities represent investments in shares of public companies and the other equity investment represent shares held in a private company.

Marketable securities are designated as available for sale and are stated at fair value. Any unrealized gain or loss is recognized in other comprehensive income (loss) for the period in which they arise.

The following table sets out the changes in marketable securities:

		June 30 2011		December 31 2010
Balance, beginning of period	**$**	**-**	$	204,336
Proceeds on sale of subsidiary		**2,800,000**		-
Sale of marketable securities		**-**		(525,860)
Realized gain on sale of marketable securities		**-**		241,870
Unrealized gain (loss) on marketable securities		**(1,600,000)**		79,654
	$	**1,200,000**	$	-

For the three and six months ended June 30, 2011, the unrealized loss on marketable securities of $1,600,000 was recorded net of deferred tax of $206,400 in other comprehensive income (loss).

6. Loan Receivable

On May 30, 2011, the Company also closed an agreement to advance Transeuro a $2 million loan to fund its ongoing operations. The loan will be due and payable on the earlier of 12 months or the announcement of a future financing by Transeuro.

7. Inventory

During the period, $130,275 in fuel inventory was purchased (2010: nil) and $142,656 (2010: $154,296) was recognized as an expense. At June 30, 2011, the inventory balance is nil, as it solely related to QBR, which was sold in the second quarter of 2011.

8. Property, Plant and Equipment

	Oil and Natural Gas Assets	Corporate Assets	Total
Cost or deemed cost:			
Balance at January 1, 2010	$ 60,217,761	$ 1,565,779	$ 61,783,540
Additions	13,674,217	13,326	13,687,543
Transfers from exploration and evaluation assets	43,316	-	43,316
Disposals	(1,392,046)	-	(1,392,046)
Balance at December 31, 2010	72,543,248	1,579,105	74,122,353
Additions	6,701,972	14,448	6,716,420
Transfer from exploration and evaluation assets	208,238	-	208,238
Disposals	(3,780,304)	(631,464)	(4,411,768)
Balance at June 30, 2011	**$ 75,673,154**	**$ 962,089**	**$ 76,635,243**
Depletion, depreciation and impairment losses:			
Balance at January 1, 2010	$ 18,519,949	$ 1,118,242	$ 19,638,191
Depletion and depreciation	5,486,913	266,234	5,753,147
Impairment	1,360,685	-	1,360,685
Disposals	(879,077)	-	(879,077)
Balance at December 31, 2010	24,488,470	1,384,476	25,872,946
Depletion and depreciation	2,858,451	64,893	2,923,344
Disposals	(3,780,304)	(631,464)	(4,411,768)
Balance at June 30, 2011	**$ 23,566,617**	**$ 817,905**	**$ 24,384,522**

	Oil and Natural Gas Assets	Corporate Assets	Total
Net book value:			
At December 31, 2010	$ 48,054,778	$ 194,629	$ 48,249,407
At June 30, 2011	**$ 52,106,537**	**$ 144,184**	**$ 52,250,721**

During the period ended June 30, 2011, the Company capitalized administrative overhead charges of $243,877 (December 31, 2010: $629,900) directly related to development activities. Included in the depletion calculation are future development costs of $8,735,154 (December 31, 2010: $7,857,000).

During the year ended December 31, 2010, due to declining natural gas prices, the Company tested the Midway, Kaka, Other Alberta, Vulcan and Beaver River cash generating units ("CGUs") for impairment. The recoverable amount of the CGU was estimated based on the higher of the value in use ("VIU") and the fair value less costs to sell ("FVLCTS"). The estimate of FVLCTS was determined using a discount rate of 10% and forecasted cash flows based on proved plus probable reserves, with escalating prices and future development costs obtained from the reserve report after tax. Based on the assessment, the carrying amount of the CGUs was determined to be $1,360,685 lower than its recoverable amount, and an impairment loss was recognized.

9. Exploration and Evaluation ("E&E") Assets

Reconciliation of the movements in E&E assets:

		June 30 2011		December 31 2010
Carrying amount, beginning of period	**$**	**49,762,437**	$	23,621,537
Additions		**2,393,646**		26,184,216
Transfers to property, plant and equipment		**(208,238)**		(43,316)
Impairment loss		**(230,395)**		-
Carrying amount, end of period	**$**	**51,717,450**	$	49,762,437

During the period ended June 30, 2011, the Company capitalized administrative overhead charges of $832,732 (December 31, 2010: $1,256,800) directly related to E&E activities.

The impairment of E&E assets is recognized as additional depletion and depreciation expense in net profit (loss).

E&E assets consist of the Company's exploration projects which are pending the determination of technical feasibility and commercial viability. Additions represent the Company's share of costs incurred on E&E assets during the period.

10. Asset Retirement Obligation

The Company's asset retirement and abandonment obligations result from its ownership interest in oil and natural gas assets. The total asset retirement obligation is estimated based on the Company's net ownership interest in all wells and facilities, estimated costs to reclaim and abandon these wells and facilities and the estimated timing of the costs to be incurred in future periods. The Company has estimated the net present value of the asset retirement obligation to be $3,867,536 as at June 30, 2011 (December 31, 2010: $7,219,342) based on an undiscounted total future liability of $6,178,365 (December 31, 2010: $9,661,749). These payments are expected to be made over the next 25 years. The discount factor, being the risk free rate related to the liability, is between 1.59 and 3.55 percent (2010: 1.67 and 3.52 percent). An inflation rate of three percent over the varying lives of the assets is used to calculate the present value of the asset retirement obligation.

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

		June 30 2011		December 31 2010
Balance, beginning of period	**$**	**7,219,342**	$	6,655,654
Revisions due to change in discount rate		**(211)**		273,903
Revisions due to change in estimates		**180,441**		(247,823)
Liabilities incurred		**316,999**		374,157
Sale of subsidiary		**(3,939,426)**		(6,662)
Accretion		**90,391**		170,113
Balance, end of period	**$**	**3,867,536**	$	7,219,342

11. Share Capital

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 June 30, 2011, there were no Class B common voting shares or preferred shares outstanding.

a) Issued and outstanding – Class A Common Shares

	Number		Amount
Balance, January 1, 2010	199,722,143	$	184,962,957
Issue of common shares	30,000,000		127,907,414
Issued on exercise of options	4,409,585		4,162,250
Shares issue costs, net of tax			(5,379,851)
Balance, December 31, 2010	234,131,728		311,652,770
Issued on exercise of options	767,000		995,480
Repurchased under normal course issuer bid	(2,783,200)		(3,535,497)
Balance, June 30, 2011	**232,115,528**	**$**	**309,112,753**

b) Normal course issuer bid

In December 2010, the Company announced its intention to conduct a Normal Course Issuer Bid ("NCIB") through the facilities of the TSX and the Oslo Stock Exchange. Under the terms of the NCIB, Questerre is authorized to acquire up to an aggregate of 11,706,586 of its common shares over the next 12-month period representing approximately 5% of its issued and outstanding common shares as at December 16, 2010. All common shares purchased by Questerre under the NCIB will be returned to treasury and cancelled. The NCIB commenced on December 22, 2010 and will terminate on December 21, 2011, or the earlier of the date all common shares which are subject to the NCIB are purchased.

When common shares are repurchased, the amount of consideration paid, net of the excess of the purchase price of common shares over their average carrying value, is recognized as a reduction of share capital. The excess of the average carrying value over the purchase price is recorded as contributed surplus. Repurchased shares that are not cancelled at the balance sheet date are recorded in share capital, as treasury shares, at the purchase price of the common shares. Common shares transactions are recognized on a trade date basis.

At June 30, 2011, 2,358,200 common shares have been purchased and cancelled under the NCIB with a par value of $3,140,033 and consideration of $2,395,703. During the quarter, an additional 425,000 common shares were purchased for $395,464 that had not been cancelled at June 30, 2011. These shares are considered treasury stock at the end of the quarter resulting in $395,464 included in share capital. Subsequent to quarter end, the common shares have been cancelled and returned to treasury.

c) Per share amounts

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

	Three months ended June 30		*Six months ended June 30*	
	2011	2010	**2011**	2010
Basic	**233,610,707**	233,809,187	**233,981,259**	220,174,636
Diluted	**236,472,552**	-	**237,475,415**	-

Under the current stock option plan, options can be exchanged for common shares of the Company or for cash at the Company's discretion. As a result, they are considered potentially dilutive and are included in the calculation of diluted profit per share for the period.

For the diluted amounts 2.86 million and 3.49 million common shares were added to the basic weighted average number of shares outstanding for the three and six month periods ended June 30, 2011 respectively. These share additions represent the dilutive effect of stock options according to the treasury stock method.

12. Share Based Compensation

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

As at January 24, 2011, the Company modified its stock option plan. Under the modified option plan, a put right was included that allows the optionee to settle options with cash or equity. The Corporation has the option to decline a put right exercise at any time. Under the put right, the optionee will receive the net cash proceeds that is the excess of the closing price at the day of the put notice over the exercise price. Once the options are cash settled, the options are cancelled. At the time of the plan modification, $9,231,368 of contributed surplus was transferred to the share based compensation liability on the Company's consolidated balance sheet.

The number and weighted average exercise prices of stock options are as follows:

	June 30, 2011		December 31, 2010	
	Number of Options	**Weighted Average Exercise Price**	Number of Options	Weighted Average Exercise Price
Outstanding, beginning of period	**20,035,835**	**$2.47**	18,618,753	$1.53
Forfeited	**(356,666)**	**2.32**	(136,668)	2.72
Exercised	**(1,270,000)**	**0.71**	(4,409,585)	0.59
Granted	**3,405,000**	**1.29**	5,963,335	4.03
Outstanding, end of period	**21,814,169**	**$2.39**	20,035,835	$2.47
Exercisable, end of period	**9,516,512**	**$1.68**	9,142,702	$1.32

The following table summarizes information about stock options outstanding and exercisable at June 30, 2011:

	Options Outstanding			Options Exercisable		
	Number of Options	Weighted Average Years to Expiry	Weighted Average Exercise Price	Number of Options	Weighted Average Years to Expiry	Weighted Average Exercise Price
$0.45 - $0.65	4,753,334	1.65	$0.45	4,753,334	1.65	$0.45
$0.74 - $1.14	1,650,000	3.64	0.87	490,000	0.60	0.77
$1.15 - $1.80	4,392,500	3.29	1.52	1,571,658	1.38	1.47
$2.37 - $2.78	2,650,000	4.24	2.49	562,498	3.21	2.60
$4.00 - $4.70	8,368,335	3.21	4.23	2,139,022	2.36	4.55
	21,814,169	**3.04**	**$2.39**	**9,516,512**	**1.80**	**$1.68**

The fair value of the liability was estimated at June 30, 2011 using the Black-Scholes valuation model with the weighted average assumptions as follows:

	June 30 2011
Weighted average fair value per award ($)	**0.35**
Volatility (%)	**89**
Forfeiture rate (%)	**2.15**
Expected life (years)	**2.81**
Risk free interest rate (%)	**2.88**

Note - The 2010 comparative period is not disclosed as the Company previously reported using equity accounting.

This forfeiture rate estimate is adjusted to the actual forfeiture rate. Expected volatility and expected life is based on historical information.

The modification to the option plan was accounted for prospectively. Share based compensation of $853,727 was recovered during the six months ended June 30, 2011 and $4,043,978 was expensed during the comparable period in 2010 prior to the modification. In addition, share based compensation expense of $63,576 (2010: $nil) was capitalized during the six months ended June 30, 2011.

The following table provides a reconciliation of the Company's share based compensation liability:

		June 30 2011
Balance, beginning of period	$	-
Amount transferred from contributed surplus		7,356,671
Share based compensation expense (recovery)		(853,727)
Capitalized share based compensation expense		63,576
Reclassification to share capital on exercise of stock options		(458,430)
Cash payment for options surrendered		(567,070)
Share based compensation liability	$	5,541,020
Current portion	$	4,497,743
Non-current portion		1,043,277
	$	5,541,020

The current portion represents the maximum amount of the liability payable within the next 12-month period if all vested options are surrendered for cash settlement.

13. Commitments and Contingencies

The Company has commitments under a lease for office space of $152,120 in 2011, $304,240 per year for 2012 to 2014 and $278,885 in 2015. In the first quarter of 2011, Questerre entered into a data licensing agreement. The Company has commitments under the agreement of $100,000 per year for 2012 to 2015.

In May 2011, Questerre announced its plan to maintain its share position through a $2 million commitment to a future financing by Transeuro subject to final terms.

The Company is a defendant and plaintiff in a number of legal actions arising in the normal course of business. The Company believes that any liabilities that might arise pertaining to any such matters would not have a material effect on its consolidated financial position.

In the second quarter of 2011, a joint venture partner filed a statement of claim with respect to amounts formally disputed by Questerre. Questerre has filed its statement of defense and counterclaim with respect to this issue. The claim is for $3.9 million and the entire amount is accounted for in the consolidated financial statements.

14. Subsequent Events

In July 2011, Questerre announced it has closed an asset acquisition in southeast Saskatchewan for a cash purchase price of $13.25 million. The acquisition is effective May 1, 2011 and closed on July 7, 2011.

15. Transition to IFRS

As stated in Note 2, these interim consolidated financial statements are for the period covered by the first annual consolidated financial statements prepared in accordance with IFRS as at and for the year ended December 31, 2011. Previously, the Company prepared its interim and annual consolidated financial statements in accordance with previous GAAP.

The Company adopted IFRS on January 1, 2011 with a transition date of January 1, 2010. Under IFRS 1 *First Time Adoption of International Financial Reporting Standards*, IFRS is applied retrospectively at the transition date with the offsetting adjustments to assets and liabilities generally included in the deficit.

The effect of the Company's transition to IFRS is summarized as follows:

- Transition elections
- Reconciliations as previously reported under previous GAAP to IFRS
- Adjustments to the statements of cash flows

<u>Transition elections</u>

IFRS 1 *First Time Adoption of International Financial Reporting Standards* allows first-time adopters certain exemptions from the retrospective application of certain IFRSs effective for December 2011 year-ends. The Company has applied the following exemptions:

a) Business combinations

IFRS 1 indicates that a first-time adopter may elect not to apply IFRS 3 *Business Combinations* retrospectively to business combinations that occurred prior to the date of transition to IFRS. The Company has elected to apply IFRS relating to business combinations prospectively from January 1, 2010. As such, previous GAAP balances relating to business combinations entered into before that date, including goodwill, have been carried forward without adjustment.

b) Election for full cost oil and gas entities

The Company elected an IFRS 1 exemption whereby the previous GAAP full cost pool was measured upon transition to IFRS as follows:

(i) E&E assets consist of the Company's exploration projects which are pending the determination of technical feasibility and commercial viability. Under previous GAAP these costs were grouped with the full cost pool. Upon transition to IFRS, the Company reclassified unproved properties from the full cost pool under previous GAAP to E&E assets; and

(ii) the remaining full cost pool was allocated to producing and development assets and components on a pro rata basis to the underlying assets using proved reserve volumes as at January 1, 2010.

c) Asset retirement obligation

Since the Company has elected to apply the IFRS 1 full-cost as deemed cost exemption, asset retirement obligation must be measured as at January 1, 2010 in accordance with IAS 37. The difference between that amount and the carrying amount of those liabilities at the date of transition is recognized directly in deficit.

d) Share based compensation

IFRS 1 encourages, but does not require, first-time adopters to apply IFRS 2 *Share-based payments* to equity instruments that were granted on or before November 7, 2002, or equity instruments that were granted subsequent, to November 7, 2002 and vested before the later of the date of transition to IFRS and January 1, 2005. The Company has elected not to apply IFRS 2 to awards that vested prior to January 1, 2010.

IFRS 1 also outlines specific guidelines that a first-time adopter must adhere to under certain circumstances. The Company has applied the following guidelines to its opening balance sheet dated January 1, 2010:

e) Estimates

In accordance with IFRS 1, an entity's estimates under IFRS at the date of transition to IFRS must be consistent with estimates made for the same date under previous GAAP, unless there is objective evidence that those estimates were in error. The Company's IFRS estimates as at January 1, 2010 are consistent with its previous GAAP estimates for the same date.

Restatement of equity from previous GAAP to IFRS

IFRS employs a conceptual framework that is similar to previous GAAP. However, significant differences exist in certain matters of recognition, measurement and disclosure. While adoption of IFRS has not changed the Company's actual cash flows, it has resulted in changes to the Company's reported financial position and results of operations. In order to allow the users of the consolidated financial statements to better understand these changes, the Company's previous GAAP statement of comprehensive income (loss) and balance sheets for the quarter ended June 30, 2010 and the year ended December 31, 2010 have been reconciled to IFRS, with the resulting differences explained.

Reconciliation of Equity at the date of IFRS transition – January 1, 2010

	Notes	Restated Canadian GAAP *(note h)*	Effect of transition to IFRS	IFRS
Assets				
Current assets				
Cash and cash equivalents		$ 51,396,052	$ -	$ 51,396,052
Marketable securities		204,336	-	204,336
Accounts receivable		4,509,203	-	4,509,203
Inventory		301,599	-	301,599
Deposits and prepaid expenses		619,990	-	619,990
		57,031,180	-	57,031,180
Property, plant and equipment	(a,b)	84,286,835	(42,141,486)	42,145,349
Exploration and evaluation assets	(b)	-	23,621,537	23,621,537
Goodwill		2,467,816	-	2,467,816
Deferred tax assets	(g)	1,486,533	5,693,811	7,180,344
		$ 145,272,364	$ (12,826,138)	$ 132,446,226
Liabilities and Equity				
Current liabilities				
Accounts payable and accrued liabilities		$ 10,530,509	$ -	$ 10,530,509
Asset retirement obligation	(e)	4,764,653	1,891,001	6,655,654
		15,295,162	1,891,001	17,186,163
Shareholders' Equity				
Share capital	(h)	184,962,957	-	184,962,957
Contributed surplus		11,218,598	-	11,218,598
Deficit	(a,e,g,h)	(66,204,353)	(14,717,139)	(80,921,492)
		129,977,202	(14,717,139)	115,260,063
		$ 145,272,364	$ (12,826,138)	$ 132,446,226

Reconciliation of Equity at June 30, 2010

	Notes	Restated Canadian GAAP *(note h)*	Effect of transition to IFRS	IFRS
Assets				
Current assets				
Cash and cash equivalents		$ 166,322,202	$ -	$ 166,322,202
Accounts receivable		6,283,949	-	6,283,949
Inventory		147,303	-	147,303
Deposits and prepaid expenses		1,100,985	-	1,100,985
		173,854,439	-	173,854,439
Property, plant and equipment	(a,b,d)	86,978,286	(42,688,080)	44,290,206
Exploration and evaluation assets	(b)	-	28,250,628	28,250,628
Goodwill		2,467,816	-	2,467,816
Deferred tax assets	(g)	4,825,224	4,334,976	9,160,200
		$ 268,125,765	$ (10,102,476)	$ 258,023,289
Liabilities and Equity				
Current liabilities				
Accounts payable and accrued liabilities		$ 12,922,352	$ -	$ 12,922,352
Asset retirement obligation	(e)	5,308,899	1,802,359	7,111,258
		18,231,251	1,802,359	20,033,610
Shareholders' Equity				
Share capital	(h)	311,329,629	-	311,329,629
Contributed surplus	(f)	14,061,634	(210,411)	13,851,223
Deficit	(a,d,e,f,g,h)	(75,496,749)	(11,694,424)	(87,191,173)
		249,894,514	(11,904,835)	237,989,679
		$ 268,125,765	$ (10,102,476)	$ 258,023,289

Reconciliation of Equity at the end of the last reporting year under previous GAAP – December 31, 2010

	Notes	Canadian GAAP	Effect of transition to IFRS	IFRS
Assets				
Current assets				
Cash and cash equivalents		$ 141,974,856	$ -	$ 141,974,856
Accounts receivable		7,894,381	-	7,894,381
Inventory		344,138	-	344,138
Deposits and prepaid expenses		507,124	-	507,124
		150,720,499	-	150,720,499
Property, plant and equipment	(a,b,c,d)	109,983,549	(61,734,142)	48,249,407
Exploration and evaluation assets	(b)	-	49,762,437	49,762,437
Goodwill		2,467,816	-	2,467,816
Deferred tax assets	(g)	5,784,127	3,564,705	9,348,832
		$ 268,955,991	$ (8,407,000)	$ 260,548,991
Liabilities and Equity				
Current liabilities				
Accounts payable and accrued liabilities		$ 14,643,521	$ -	$ 14,643,521
Asset retirement obligation	(e)	5,365,096	1,854,246	7,219,342
		20,008,617	1,854,246	21,862,863
Shareholders' Equity				
Share capital	(h)	311,652,770	-	311,652,770
Contributed surplus	(f)	19,208,740	(320,005)	18,888,735
Deficit	(a,c,d,e,f,g,h)	(81,914,136)	(9,941,241)	(91,855,377)
		248,947,374	(10,261,246)	238,686,128
		$ 268,955,991	$ (8,407,000)	$ 260,548,991

Reconciliation of Total Comprehensive Loss for the three months ended June 30, 2010

	Notes		Canadian GAAP		Effect of transition to IFRS		IFRS
Revenue							
Petroleum and natural gas sales		$	2,813,743	$	-	$	2,813,743
Royalties			(726,043)		-		(726,043)
Petroleum and natural gas revenue, net of royalties			2,087,700		-		2,087,700
Expenses							
Operating			876,530		-		876,530
General and administrative			1,450,594		-		1,450,594
Loss on marketable securities			21,875		-		21,875
Bad debt expense			985,939		-		985,939
Depletion and depreciation	(d)		3,297,822		(2,025,677)		1,272,145
Accretion of asset retirement obligation	(e)		93,888		(48,042)		45,846
Share based compensation	(f)		2,862,960		(58,514)		2,804,446
			9,589,608		(2,132,233)		7,457,375
Interest income			430,053		-		430,053
Loss before taxes			(7,071,855)		2,132,233		(4,939,622)
Deferred taxes (recovery)	(g)		(1,132,594)		728,601		(403,993)
Total comprehensive loss for the period		$	(5,939,261)	$	1,403,632	$	(4,535,629)

Reconciliation of Total Comprehensive Loss for the six months ended June 30, 2010

	Notes	Canadian GAAP	Effect of transition to IFRS	IFRS
Revenue				
Petroleum and natural gas sales		$ 5,789,096	$ -	$ 5,789,096
Royalties		(1,127,268)	-	(1,127,268)
Petroleum and natural gas revenue, net of royalties		4,661,828	-	4,661,828
Expenses				
Operating		1,827,162	-	1,827,162
General and administrative		2,660,425	-	2,660,425
Gain on marketable securities		(321,524)	-	(321,524)
Bad debt expense		985,939	-	985,939
Depletion and depreciation	(d)	6,522,551	(4,040,817)	2,481,734
Accretion of asset retirement obligation	(e)	218,744	(130,322)	88,422
Share based compensation	(f)	4,254,389	(210,411)	4,043,978
		16,147,686	(4,381,550)	11,766,136
Interest income		537,391	-	537,391
Loss before taxes		(10,948,467)	4,381,550	(6,566,917)
Deferred taxes (recovery)	(g)	(1,656,071)	1,358,835	(297,236)
Total comprehensive loss for the period		$ (9,292,396)	$ 3,022,715	$ (6,269,681)

Reconciliation of Total Comprehensive Loss for the year ended December 31, 2010

	Notes	Canadian GAAP	Effect of transition to IFRS	IFRS
Revenue				
Petroleum and natural gas sales		$ 11,989,713	$ -	$ 11,989,713
Royalties		(1,556,071)	-	(1,556,071)
Petroleum and natural gas revenue, net of royalties		10,433,642	-	10,433,642
Other income		192,500	-	192,500
		10,626,142	-	10,626,142
Expenses				
Operating		3,262,269	-	3,262,269
General and administrative		4,122,149	-	4,122,149
Gain on marketable securities		(321,524)	-	(321,524)
Bad debt expense		1,429,691	-	1,429,691
Depletion and depreciation	(d)	13,087,318	(7,334,172)	5,753,146
Impairment of assets	(a)	-	1,360,685	1,360,685
Gain on divestitures	(c)	(1,130,345)	(337,031)	(1,467,376)
Accretion of asset retirement obligation	(e)	444,594	(274,481)	170,113
Share based compensation	(f)	9,544,015	(320,005)	9,224,010
		30,438,167	(6,905,004)	23,533,163
Interest income		1,509,498	-	1,509,498
Loss before taxes		(18,302,527)	6,905,004	(11,397,523)
Deferred taxes (recovery)	(g)	(2,592,744)	2,129,106	(463,638)
Total comprehensive loss for the period		$ (15,709,783)	$ 4,775,898	$ (10,933,885)

Notes to the Reconciliation of Equity and Total Comprehensive Loss from previous GAPP to IFRS

a) Impairment

Under previous GAAP, the Company applied a two part impairment test (the "ceiling test") to the net carrying amount, of oil and gas assets, whereby the first step compared the net carrying value of the asset to their relative recoverable amount. The recoverable amount is calculated as the undiscounted cash flow from the properties using proved reserves and expected future prices and costs. If the carrying amount of the properties exceeds their recoverable amount, then an impairment loss, equal to the amount by which the carrying amount of the properties exceeds the discounted cash flow from those properties using proved and probable reserves and expected future prices and costs, is recognized.

Under IFRS, the recoverable amounts have been determined based on the higher of VIU and FVLCTS at the level of CGUs. If the carrying amount of the asset exceeds its recoverable amount, the asset is impaired and an impairment loss is charged to net profit (loss) to reduce the carrying amount in the balance sheet to its recoverable amount.

With the adoption of IAS 36, the Company recorded impairments on its natural gas assets in Western Canada that were grouped into CGUs based on similar geological structure. Declining long-term natural gas prices resulted in the carrying amounts for these CGUs exceeding their recoverable amounts. The recoverable amount was calculated using a FVLCTS valuation based on a 25 year cash flow projection discounted at a rate of 10%. Discounted future cash flows were based on proved plus probable reserves using forecast prices and costs. As at January 1, 2010, the Company recorded an impairment of $18,519,949 which reduced property, plant and equipment with a corresponding charge to deficit. For the year ended December 31, 2010, additional impairment of natural gas assets of $1,360,685 was recorded in net profit (loss), with a corresponding decrease to property, plant and equipment.

For the purpose of impairment testing, goodwill is allocated to all the Company's CGUs and is tested at an operating segment level. The recoverable amount, based on the higher of VIU and the FVLCTS was determined to be higher than the carrying amount of all the CGUs and an impairment loss was not recorded as at January 1, 2010 and December 31, 2010.

b) Oil and gas properties

Under previous GAAP, the Company followed the full cost method of accounting for oil and gas properties whereby all costs of acquisition, exploration for and development of oil and gas reserves were capitalized at the cost-centre level. Under IFRS, pre-exploration costs are expensed as incurred. After the legal right to explore is acquired, exploration costs are capitalized as E&E assets. Once the exploration area achieves technical feasibility and commercial viability, E&E costs are moved to property, plant and equipment. Upon transition to IFRS, the Company reclassified $23,621,537 of property, plant and equipment to E&E assets.

As at June 30, 2010 and December 31, 2010, the Company reclassified $28,250,628 and $49,762,437 of property, plant and equipment to E&E assets.

c) Divestitures

Under previous GAAP, proceeds from divestitures were deducted from the full cost pool without recognition of a gain or loss unless the deduction resulted in a change to the depletion rate of 20 percent or greater. Under IFRS, gains or losses are recorded on divestitures and calculated as the difference between the proceeds and the net book value of the asset disposed.

For the year ended December 31, 2010, the Company recognized a $337,031 gain on divestitures in net profit (loss).

d) Depletion

Upon transition to IFRS, the Company adopted a policy of depleting oil and natural gas interests on a unit of production basis over proved plus probable reserves. The depletion policy under previous GAAP was based on units of production over proved reserves. In addition depletion was calculated at a Canadian cost-centre level under previous GAAP. IFRS requires depletion and depreciation to be calculated based on individual components.

There was no impact of this difference on adoption of IFRS at January 1, 2010 as a result of the IFRS 1 election as discussed above.

For the three and six month periods ended June 30, 2010, transition differences related to impairment, asset retirement costs and component accounting resulted in a decrease to depletion of $2,025,677 and $4,040,817 with a corresponding change to property, plant and equipment.

For the year ended December 31, 2010 transition differences resulted in a decrease to depletion of $7,334,172 with a corresponding change to property, plant and equipment.

e) Asset retirement obligation

Under previous GAAP, asset retirement obligations were discounted at a credit adjusted risk fee rate of 7 and 12 percent. The estimated cash flow to abandon and remediate the wells and facilities was risk adjusted under previous GAAP; therefore, the obligation is discounted at a risk free rate under IFRS. The risk free rate is based on the government of Canada bonds rates based on the remaining life to abandon each well. At January 1, 2010, the Company used a risk free rate that ranged from 1.45 to 4.10 percent. Upon transition to IFRS this resulted in a $1,891,001 increase in the asset retirement obligation with a corresponding increase in the deficit.

As a result of the lower risk free rate under IFRS, accretion decreased by $48,042 and $130,322 for the three and six months ended June 30, 2010.

The following table provides a reconciliation of the Company's asset retirement obligation as at December 31, 2010:

	As reported December 31 2010	Adjustment upon transition to IFRS	IFRS December 31 2010
Balance, beginning of period	$ 4,764,653	$ 1,891,001	$ 6,655,654
Revisions due to change in discount rate	-	273,903	273,903
Revisions due to change in estimates	45,206	(293,029)	(247,823)
Net liabilities incurred	117,305	256,852	374,157
Liabilities settled	(6,662)	-	(6,662)
Accretion	444,594	(274,481)	170,113
Balance, end of period	$ 5,365,096	$ 1,854,246	$ 7,219,342

During 2010, there was downward movement in the risk free rate. The change in the liability is due to the decreased risk free rates, net liabilities incurred and revisions related to changes in estimates during the year. With the lower risk free rate accretion decreased by $274,481 for the year ended December 31, 2010.

f) Share based compensation

Under previous GAAP, the Company's equity-settled share based payments were measured at their fair value at the grant date. This amount was expensed to stock based compensation on the income statement over the vesting period using graded vesting. Forfeitures were accounted for as they occurred. Under IFRS, an estimate of forfeitures must be factored into the calculation of the expense at the grant date and any difference between the estimates and actuals is recognized in the period when actual forfeitures are incurred.

The effect on net profit (loss) for the three and six month periods ended June 30, 2010 is to reduce share based compensation expense by $58,514 and $210,411 with a corresponding decrease to contributed surplus.

The effect on net profit (loss) for the year ended December 31, 2010 is to reduce share based compensation expense by $320,005 with a corresponding decrease to contributed surplus.

g) Deferred taxes

Nearly all the previous GAAP to IFRS differences have an impact on deferred taxes as the adjustments change the accounting balance and the amount of the temporary or permanent differences. The tax impact of the above changes increased the deferred tax assets as follows:

	Note		As at January 1 2010		As at June 30 2010		As at December 31 2010
Property, plant and equipment	(a,c,d)	$	5,266,821	$	3,980,986	$	3,093,018
Asset retirement obligation	(e)		426,990		353,990		471,687
Balance, end of period		$	5,693,811	$	4,334,976	$	3,564,705

The impact of these changes increased the deferred tax asset by $5,693,811 as at January 1, 2010, by $4,334,976 as at June 30, 2010 and $3,564,705 as at December 31, 2010 under IFRS.

For the three and six months ended June 30, 2010, the Company decreased the deferred tax recovery by $728,601 and $1,358,835, which resulted in a deferred tax recovery of $403,993 and $297,236 which was recorded in net profit (loss).

For the year ended December 31, 2010, the Company decreased the deferred tax recovery by $2,129,106, which resulted in a deferred tax recovery of $463,638, which was recorded in net profit (loss).

h) Restatement of previous GAAP

Questerre acquired Terrenex Ltd. and its wholly owned foreign subsidiary Cabernet Holdings Ltd. ("Cabernet") on April 28, 2008. The only significant asset Cabernet owned was Questerre common shares. On July 22, 2009, Cabernet was dissolved and a taxable event was deemed to have occurred. The result was presented on the September 30, 2009 financial statements as a $1,256,314 increase to the future tax asset on the balance sheet. The offset was initially recorded to the future tax recovery line on the statements of operations and as a result the deficit line on the balance sheet. Upon subsequent review, since the recovery related to an equity item it should have been booked to common shares in the shareholders' equity section.

The previous GAAP consolidated statements of operations, comprehensive loss and deficit have been amended and restated as follows:

	Year ended December 31 2009	Adjustment	Restated Year ended December 31 2009
Future tax recovery	$ (4,192,378)	$ 1,256,314	$ (2,936,064)
Net loss and comprehensive loss	$ (13,722,888)	$ (1,256,314)	$ (14,979,202)
Net loss per share			
Basic and diluted	$ (0.07)		$ (0.08)

The previous GAAP consolidated balance sheets have been amended and restated as follows:

	Period ended June 30 2010	Year ended December 31 2009	Adjustment	Restated Period ended June 30 2010	Restated Year ended December 31 2009
Common shares	$ 310,073,315	$ 183,706,643	$ 1,256,314	$ 311,329,629	$ 184,962,957
Deficit	$ (74,240,435)	$ (64,948,039)	$ (1,256,314)	$ (75,496,749)	$ (66,204,353)

Adjustments to the statements of cash flows

The adoption of IFRS did not have a significant impact on the amounts reported as the operating, investing and financing cash flows in the consolidated statements of cash flows.

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