TERRACE ENERGY CORP
(formerly Terrace Resources Inc.)

CONDENSED INTERIM FINANCIAL STATEMENTS
(unaudited – prepared by management)

THREE MONTHS ENDED APRIL 30, 2011 AND 2010

TERRACE ENERGY CORP
(formerly Terrace Resources Inc.)
CONDENSED INTERIM BALANCE SHEETS
(unaudited – prepared by management)

	April 30 2011	January 31 2011	February 1 2010
ASSETS			
Current			
Cash	$ 95,869	$ 219,701	$ 290,796
Deposit	998	-	-
HST receivable	10,400	1,232	-
	107,267	220,933	290,796
Long Term			
Restricted cash (Note 6)	2,529,566	2,523,771	2,502,262
	$ 2,636,833	$ 2,744,704	$ 2,793,058

	April 30 2011	January 31 2011	February 1 2010
LIABILITIES AND SHAREHOLDERS' EQUITY			
Current			
Accounts payable and accrued liabilities	$ 56,169	$ 18,953	$ 6,098
Shareholders' Equity			
Capital Stock (Note 5)	2,880,589	2,880,589	2,880,589
Contributed Surplus (Note 5)	87,950	87,950	87,950
Deficit	(387,875)	(242,788)	(181,579)
	2,580,664	2,725,751	2,786,960
	$ 2,636,833	$ 2,744,704	$ 2,793,058

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

TERRACE ENERGY CORP
(formerly Terrace Resources Inc.)
CONDENSED INTERIM STATEMENTS OF OPERATIONS AND COMPRHENSIVE LOSS
(unaudited – prepared by management)
FOR THE THREE MONTHS ENDED APRIL 30

	2011	2010
EXPENSES		
Bank charges	$ 140	$ 77
Professional fees	103,024	15,866
Transfer and filing fees	20,710	7,927
Business investigation costs	26,810	1,889
Loss before other items	(150,684)	(25,759)
OTHER ITEMS		
Interest income	5,795	999
Foreign exchange loss	(198)	-
Net loss and comprehensive loss for the period	$ (145,087)	$ (24,760)
Basic earnings per share (excluding escrow shares)	$ (0.00)	$ (0.00)

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

TERRACE ENERGY CORP
(formerly Terrace Resources Inc.)
CONDENSED INTERIM STATEMENTS OF CHANGES IN EQUITY
(unaudited – prepared by management)

	Capital Stock				
	Shares	Amount	Contributed Surplus	Deficit	Total Shareholders' Equity
Balance, February 1, 2010	30,881,821	$ 2,880,589	$ 87,950	(181,579)	$ 2,786,960
Loss and comprehensive loss	-	-	-	(61,209)	(61,209)
Balance, January 31, 2011	30,881,821	2,880,589	87,950	(242,788)	$ 2,727,751
Loss and comprehensive loss	-	-	-	(145,087)	(145,071)
Balance April 30, 2011	30,881,821	$ 2,880,589	$ 87,950	$ (387,875)	$ 2,580,664

TERRACE ENERGY CORP
(formerly Terrace Resources Inc.)
CONDENSED INTERIM STATEMENTS OF CASH FLOWS
(unaudited – prepared by management)
FOR THE THREE MONTHS ENDED APRIL 30

	2011	2010
CASH FLOW FROM OPERTAING ACTIVITIES		
Net loss for the period	$ (145,087)	$ (24,760)
Changes in non-cash working capital items:		
Increase in HST receivable	(9,168)	(1,346)
Increase in deposit	(999)	-
Increase (decrease) in accounts payable and accrued liabilities	37,217	(2,072)
Net cash used in operating activities	(118,037)	(28,178)
CASH FLOWS FROM INVESTING ACTIVITIES		
Restricted cash	(5,795)	(999)
Change in cash for the period	(123,832)	(29,177)
Cash, beginning of period	219,701	290,796
Cash, end of period	$ 95,869	$ 261,619
Cash paid during the period for interest	$ -	$ -
Cash paid during the period for taxes	$ -	$ -

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

1. NATURE AND CONTINUANCE OF OPERATIONS

Terrace Resources Inc. (the "Company") was incorporated under the Business Corporations Act (British Columbia) on July 6, 2006. The principal business of the Company is to identify, evaluate and then acquire an interest in a business or assets. The Company is classified as a capital pool corporation ("CPC") as defined in TSX Venture Exchange (the "Exchange") Policy 2.4.

On June 2, 2009, the Company completed a transaction whereby four other CPCs purchased common shares of the Company and distributed them to their respective shareholders upon dissolution (the "CPC Combination"). The terms of the transaction, as approved by the Exchange, provided, among other things, that the Company be given 24 months to complete a "Qualifying Transaction" ("QT"), as that term is defined by the Exchange.

The Company entered into a letter agreement dated January 31, 2011 with Eagle Development pursuant to which a newly formed subsidiary of the Company, Terrace Operating, LLC, ("TOL") and Eagle Development subsequently entered into a Farmout Agreement. Eagle Development is at arm's length to the Company, and none of the directors or officers of the Company are directors, officers or 10% shareholders of Eagle Development. Under the Farmout Agreement, TOL is entitled to acquire up to an 87.5% working interest and a 65.1875% net revenue interest in the Leases and Farmout Lands from Eagle Development by funding all costs associated with and acting as operator on the re-entry and fracture stimulation and completion of a existing well or a substitute well. (See Note 6 - "Subsequent Events")

The Company reported a net loss of $147,087 (2010 - $24,760) for the three months ended April 30, 2011 and has an accumulated deficit of $ (2010 - $242,788) as at April 30, 2011. As at April 30, 2011, the Company had working capital of $56,098 (2010 - $201,980) available to meet its liabilities as they become due.

2. SIGNIFICANT ACCOUNTING POLICIES

Basis of presentation

These are the Company's first IFRS condensed interim financial statements for the first quarter of the period covered by the first IFRS annual financial statements to be presented in accordance with IFRS for the year ending January 31, 2011 and IFRS 1 First-Time Adoption of IFRS has been applied. The impact of the transition from Canadian Generally Accepted Accounting Principles (GAAP) to IFRS is explained in Note 5.

These condensed interim financial statements have been prepared on a historical cost basis using the accrual basis of accounting, except for cash flow information.

These condensed interim financial statements were prepared in accordance with International Accounting Standard *34 Interim Financial Reporting*. They do not include all of the information required for full annual financial statements.

The accounting policies set out below have been applied consistently to all the periods presented in preparing the opening balance sheet at February 1, 2010 (note 5) for purposes of transition to IFRS.

2. SIGNIFICANT ACCOUNTING POLICIES (Continued)

Use of judgments and estimates

The preparation of financial statements requires management to make estimates that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the condensed financial statements and the reported amounts of revenues ad expenses during the reported period.

Financial instruments

All financial instruments are classified as one of the following: held-to-maturity, loans and receivables, held-for-trading, available-for-sale or other financial liabilities. Financial assets and liabilities held-for-trading are measured at fair value with gains and losses recognized in net income. Financial assets held-to-maturity, loans and receivables, and other financial liabilities are measured at amortized cost using the effective interest method. Available-for-sale instruments are measured at fair value with unrealized gains and losses recognized in other comprehensive income (loss) and reported in shareholders' equity. Any financial instruments may be designated as held-for-trading upon initial recognition.

Transaction costs that are directly attributable to the acquisition or issue of financial instruments that are classified as other than held-for-trading, which are expensed as incurred, are included in the initial carrying value of such instruments.

Comprehensive income

Comprehensive income is the overall change in the net assets of the Company for a period, other than changes attributable to transactions with shareholders. It is made up of net income and other comprehensive income. Other comprehensive income includes gains or losses that Canadian generally accepted accounting principles requires to be recognized in the period but are excluded from net income for that period.

The Company has no items of comprehensive income (loss) in any period presented, accordingly, net loss equals comprehensive loss.

Stock-based compensation

The Company accounts for stock-based compensation using a fair value based method with respect to all stock-based payments to directors, employees and non-employees. For directors and employees, the fair value of the options is measured at the date of grant. For non-employees, the fair value of the options is measured on the earlier of the date at which the counterparty performance is completed or the date the performance commitment is reached or the date at which the equity instruments are granted if they are fully vested and non-forfeitable. The fair value of the options is accrued and charged to operations, with the offset credit to contributed surplus. For directors and employees the options are recognized over the vesting period, and for non-employees the options are recognized over the related service period. If and when the stock options are ultimately exercised, the applicable amounts of contributed surplus are transferred to capital stock.

Income taxes

The Company uses the asset and liability method for accounting for income taxes. Under this method of tax allocation, future income tax assets and liabilities are determined based on differences between the financial statement carrying values and their respective income tax basis (temporary differences). Future income tax assets and liabilities are measured using the tax rates expected to be in effect when the temporary differences are likely to reverse. The effect on future income tax assets and liabilities of a change in tax rates is included

2. SIGNIFICANT ACCOUNTING POLICIES (Continued)

in operations in the period in which the change is enacted or substantially assured. The amount of future income tax assets recognized is limited to the amount of the benefit that is more likely than not to be realized.

Basic and diluted loss per share

Basic loss per share is calculated using the weighted average number of common shares outstanding during the year. The Company uses the treasury stock method to compute the dilutive effect of options, warrants and similar instruments. Under this method the dilutive effect on loss per share is calculated presuming the exercise of outstanding options, warrants and similar instruments.

It assumes that the proceeds of such exercise would be used to repurchase common shares at the average market price during the year. However, the calculation of diluted loss per share excludes the effects of various conversions and exercise of options and warrants that would be anti-dilutive.

Shares held in escrow, other than where their release is subject to the passage of time, are not included in the calculation of the weighted average number of common shares outstanding.

Revenue recognition

Interest income is recognized as earned at the stated interest rate in the instrument.

3. CAPITAL STOCK

On April 30, 2011, the Company had unlimited authorized common shares, without par value and 30,881,821 shares outstanding.

Escrow shares

Of the common shares issued, 18,604,103 are subject to an escrow agreement and may not be transferred without the consent of the Exchange. The escrow agreement provides, among other things, that 10% of such shares will be released from escrow upon the completion of a QT, as defined in Exchange Policy 2.4, and that 15% of such shares will be released every six months thereafter. These shares have been excluded from the weighted average number of shares outstanding, as they are contingently returnable if the Company does not complete a QT.

4. FINANCIAL INSTRUMENTS

The Company has classified its financial instruments as follows:

- Cash and restricted cash - as held-for-trading; and
- Accounts payable and accrued liabilities - as other financial liabilities.

The Company's risk exposure and the impact on the Company's financial instruments are summarized below:

4. FINANCIAL INSTRUMENTS (Continued)

Fair value
The carrying values of cash, restricted cash, and accounts payable and accrued liabilities approximate their fair values because of the short-term maturity of these financial instruments.

Credit risk
Credit risk is the risk of potential loss to the Company if the counterparty to a financial instrument fails to meet its contractual obligations.

The Company's credit risk is primarily attributable to its cash and cash equivalents, deposit and receivables. The Company manages exposure to credit risk on liquid financial assets through maintaining its cash with major Canadian financial institutions, for which management believes the risk of loss to be minimal.

Market risk
Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in the market prices. Market risk is comprised of three types of risk: interest rate risk, foreign currency risk and other price risk..

(i) Interest rate risk

The Company's cash and restricted cash consist of cash held in a bank account that earns interest at variable interest rates. Due to the short-term nature of these financial instruments, fluctuations in interest rates will not have a significant impact on the fair value of the cash and restricted cash of the Company.

(ii) Foreign currency risk

The Company is not exposed to foreign currency fluctuations, as all expenditures incurred are denominated in Canadian dollars.

(iii) Other price risk

Other price risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in the market prices, other than those arising from interest rate risk or foreign currency risk. The Company is not exposed to significant other price risk.

Liquidity risk

Liquidity risk is the risk that the Company will encounter difficulty in satisfying financial obligations as they become due. The Company manages liquidity risk through maintaining sufficient cash on hand to meet its obligations as they become due. As at April 30, 2011, the Company was had cash of $95,869 and working capital of $51,098. The Company held restricted cash of $2,529,566 which could not be used prior to the completion of a QT without Exchange approval. (see Note 6 – "Subsequent Events")

At April 30, 2011, the Company had accrued liabilities of $56,169 (2010 - $18,953) due within three months of the period-end.

5. TRANSITION TO IFRS

As stated in Note 2, these are the Company's first condensed interim financial statements for the period covered by the first annual financial statements prepared in accordance with IFRS. There are no differences between Canadian GAAP and IFRS that are applicable to the measurement of the Company's assets and liabilities (i) at the transition date of February 1, 2010; (ii) at January 31, 2011; and (iii) at April 30, 2011. There is no impact on net loss and comprehensive loss for any period presented. Further, there has been no application of any of the exceptions available under IFRS 1 - First Time Adoption of IFRS.

The accounting policies set out in Note 2 have been applied in preparing the financial statements for the period ended April 30, 2011, the comparative information presented in these financial statements for the period ended April 30, 2011, and in the preparation of an opening IFRS balance sheet as February 1, 2010.

6. SUBSEQUENT EVENTS

On June 13, 2011 the Company announced that all conditions under the Farm out Agreement by and between the Company's wholly-owned subsidiary, Terrace Operating, LLC and Eagle Energy Development Company had been removed or waived and work over operations on the "Patos Gas Unit #1" well were expected to commence within 60 days. Terrace is entitled to earn up to an 87.5% working interest and 65.1875% net revenue interest in certain oil gas leases referred to as the "Los Patos Gas Unit" in the Tailfeathers Yegua field in Wharton County Texas, by successfully fracture-stimulating an existing well.

The transaction constituted the Company's QT. The Company is now a Tier 2 Oil and Gas issuer and it's shares have re-commenced trading under the symbol "TZR".

The previously announced private placement of 10 million units at $0.09 per unit and proposed name change from Terrace Resources Inc. to Terrace Energy Corp. have been completed.

The shares, warrants and any shares issued upon exercise of the warrants are subject to a hold period and may not be traded until October 23, 2011 except as permitted by applicable securities legislation and the rules and policies of the TSX Venture Exchange ("Exchange"). In addition to hold periods under applicable securities legislation and the policies of the Exchange, the Terrace securities issued to principals of Terrace (as that term is defined in the policies of the Exchange) under the private placement and any shares issued upon exercise of the warrants held by them are subject to a Tier 2 Value Escrow Security Agreement, pursuant to which 10% of the securities are eligible for release upon completion of the Qualifying Transaction and 15% every six months thereafter. Non-principals who purchased securities in the private placement have agreed to resale restrictions on those securities similar to the release provisions of the escrowed securities.

The proceeds of the private placement will be used together with the Company's existing working capital and previously restricted cash (see below) to fund the development of the Los Patos Gas Unit and for general working capital purposes.

In connection with the CPC Combination described in Note 1, the Company placed $2.5 million into a segregated account, which could not be accessed without Exchange approval. The Exchange approved the release of these funds upon completion of the QT. They are now available for general working capital purposes.