TERRACE ENERGY CORP.

(formerly Terrace Resources Inc.)
(the "Company")

MANAGEMENT'S DISCUSSION AND ANALYSIS OF THE COMPANY'S FINANCIAL CONDITION AND RESULTS OF OPERATIONS FOR THE THREE MONTHS ENDED APRIL 30, 2012 AND 2011

Introduction

The following Management Discussion and Analysis ("MD&A") of Terrace Energy Corp. (the "Company" or "Terrace") has been prepared by management, in accordance with the requirements of National Instrument of 51-102 as of June 27, 2012 and should be read in conjunction with the unaudited condensed consolidated interim financial statements for the three months ended April 30, 2012 and 2011 and the related notes contained therein which have been prepared under International Financial Reporting Standards ("IFRS"), the audited consolidated financial statements and the related MD&A for the year ended January 31, 2012, and all other disclosure documents of the Company. The information contained herein is not a substitute for detailed investigation or analysis on any particular issue. The information provided in this document is not intended to be a comprehensive review of all matters and developments concerning the Company. Additional information relevant to the Company's activities can be found on SEDAR at www.sedar.com and the Company's website at www.terraceenergy.net.

All financial information in this MD&A related to 2012 and 2011 have been prepared in accordance with IFRS and all dollar amounts are quoted in Canadian dollars, the reporting and functional currency of the Company, unless specifically noted.

Cautionary Statement Regarding Forward Looking Statements

This discussion and analysis and the documents referenced in this discussion and analysis contain forward-looking information which may include, but is not limited to, statements with respect to future activities of the Company, the Company's plans for its oil and gas properties, the future financial or operating performance of the Company, its subsidiaries and its projects, the timing and amount of estimated future capital required, operating and capital expenditures, costs and timing of future exploration, government regulation of oil and gas operations, environmental risks, reclamation expenses, title disputes or claims, limitations of insurance coverage, the timing and possible outcome of pending litigation and regulatory matters. These statements relate to analyses and other information that are based on forecasts of future results, estimates of amounts not yet determinable and assumptions of management. Readers are cautioned not to place undue reliance upon these forward looking statements.

Overview

Background

Terrace Energy Corp. was incorporated on July 6, 2006 under the Business Corporations Act (British Columbia) and previously named Terrace Resources Inc.

The Company was classified as a capital pool corporation ("CPC") as defined in TSX Venture Exchange (the "Exchange") Policy 2.4. In June 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. At the particular time, the Company was required to place $2,500,000 into a segregated account, which could not be accessed without Exchange approval. These funds, together with accrued interest, were made available for general working capital purposes upon completion of the Company's qualifying transaction in June 2011.

The Company is now classified as a Tier 2 Oil and Gas issuer. Its common shares trade on the Exchange under the symbol "TZR".

The Company is in the business of acquiring, exploring and developing oil and gas properties. The Company has no prior history of revenues or operating cash flows. The continuing operations of the Company are therefore dependent upon its ability to raise additional capital as required and future profitable operations, neither of which is assured.

The Company's head and principal office is located at Suite 270, 666 Burrard Street, Vancouver, British Columbia V6C 2X8. Its registered and records office is located at 10th Floor, 595 Howe Street, Vancouver, British Columbia V6C 2T5. The Company also maintains an office in Houston, Texas.

The following table lists the Company's principal operating subsidiaries, their jurisdiction of incorporation and its percentage ownership of their voting securities:

Name of subsidiary	Place of Incorporation	Percentage ownership
Terrace US Holdings LLC	USA	100%
Terrace Operating LLC	USA	100%
Terrace Cutlass LLC	USA	100%
Terrace STS LLC	USA	100%

Exploration and evaluation

The following is a brief description of the Company's principal exploration and evaluation properties:

Los Patos Gas Unit

In June, 2011, the Company's wholly-owned subsidiary, Terrace Operating, LLC, and Eagle Energy Development Company entered into a farm-out agreement which entitled the Company to earn up to an 87.5% working interest and 65.1875% net revenue interest in certain oil gas leases covering 320 acres 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 agreement constituted the Company's qualifying transaction.

Work over operations on the Patos Gas Unit #1 well were completed in October 2011. The Company incurred total expenditures of $380,242, which were approximately $49,000 more than the amount estimated in the Company's filing statement dated June 1, 2011.

By funding all costs associated with the re-fracture, stimulation and completion of an existing primarily gas well, the Company fulfilled its obligations under the agreement and earned its interests in all of the project acreage. The well was deemed not successful and since the Company has no further exploration plans at this time it has reduced the carrying value of Los Patos to the approximate current market cost of leasing comparable acreage on similar terms. The Company may choose to explore, joint venture, sell, lease or abandon Los Patos in the future.

Cutlass

In November, 2011, the Company's wholly owned subsidiary, Terrace Cutlass LLC entered into an agreement with Lightning Oil Company, of San Antonio Texas ("Lightning"), under which the Company was granted the right to earn an 18.75% net revenue interest ("NRI") in certain oil, gas and mineral leases covering 3,395 net acres in the Dimmit and LaSalle Counties, Texas for $376,508 and a commitment to participate in a two well

drilling program. In February 2012, the Company acquired an additional 5% working interest and 3.75% net revenue interest for an additional $233,254.

In order to earn the net revenue interests (22.5% in aggregate), the Company agreed to pay 33.33% of all costs, including acreage leases, prospect fees, site preparation and drilling, until the completion of two wells, and thereafter 30% of all costs relating to the lease payments, prospect fees and infrastructure costs covering 1,342 net acres (the "Dimmit County Acreage"). The Company advanced the sum of $2,133,019 in March 2012 representing the operator's estimate of the Company's share of costs to drill both vertical and horizontal extensions and complete, the first well. Drilling commenced in late April, 2012.

In addition, after the drilling and technical evaluation of the first well on the Dimmit County Acreage, the Company had the right to exercise its option to earn a 22.5% net revenue interest in the remaining 2,053 acres (the "LaSalle County Acreage") at a cost of approximately US$570,462, representing the operator's estimate of the Company's share of lease payments. The Company exercised its right under the agreement and made the payment in June 2012. The Company is now obligated to fund 33.33% of the cost of an initial well on the La Salle County acreage. In June 2012, the Company advanced the additional sum of US$1,428,600 representing the operator's estimate of the Company's share of the drilling, evaluation and casing costs of the vertical extension of the well.

Lightning is the operator of the project with technical and operational input from the Company's technical personnel.

STS Olmos

In November 2011, the Company's wholly-owned subsidiary, Terrace STS LLC, entered into an agreement with Whittier Energy Company of Houston, Texas ("Whittier") to purchase all of Whittier's leasehold interest in approximately 14,400 gross acres (3,875 net acres) in LaSalle and McMullen Counties, Texas for $1,014,100. Whittier's interests to be acquired by the Company vary slightly across the acreage, averaging a 26.88% Working Interest and a 20.16% NRI.

The Company's share of the costs to drill and complete the first well (STS 1-667) was $1,251,590, which was brought into production in February 2012. Its working and net revenue interests in this well are 16.87% and 12.65% respectively. Upon completion, the costs of the first well and a portion of the acreage acquisition costs less incidental sales were transferred from Exploration and Evaluation assets to Property and Equipment.

In May 2012, the Company advanced the additional sum of US$2,698,197 representing the operator's estimate of the Company's share of the costs to drill and complete a second well on the STS Olmos project acreage. The Company's working and net revenue interests in this well are 33.33% and 25% respectively.

Results of Operations

For the three months ended April 30, 2012 and 2011

The Company only recently engaged in the business of acquiring, exploring and developing oil and gas properties. The Company's first revenues derived from operations were earned during the three months ended April 30, 2012. The Company had no prior history of revenues.

Net income for the three months ended April 30, 2012 was $212,244, including a gain of $30,969 from foreign currency exchange, compared to a loss of $145,087, including a loss of $198 from foreign currency exchange, for the three months ended April 30, 2011. Non cash deductions for share-based payments and depletion and accretion were $81,055 in 2012, compared to $nil in 2011.

Oil and gas sales for the three months ended April 30, 2012 were $555,756 compared to $nil for the three months ended April 30, 2011. The Company had incidental revenues of approximately $8,967 from a past producing well it acquired as part of the STS Olmos acquisition and $546,789 from its first well (STS 1-667), which was completed and placed into production in February, 2012. STS 1-667 operated for 81 days in the quarter during which time it produced 38,768 barrels of oil and liquids and 46,067million cubic feet of natural gas. The Company's share of this production was approximately 4,904 barrels of oil and liquids at an average price of $109.11 per barrel and 5,827 million cubic feet of natural gas and an average price $2.17 per million cubic feet.

Direct operating expenses
Production and operating expenses for the three months ended April 30, 2012 was $31,223, compared to $nil for the three months ended April 30, 2011. Total depletion and accretion expense for the three months ended April 30, 2012 was $5,506 compared to $nil for the three months ended April 30, 2011. State royalties were $34,062 for the three months ended April 30, 2012 compared to $nil for the three months ended April 30, 2011.

Administrative expenses for the three months ended April 30, 2012 were $71,453 compared to $140 for the three months ended April 30, 2011. The increase in administrative expenses is attributable to office expenses, salaries, rent and accounting relating to the establishment of offices in Texas.

Business investigation costs for the three months ended April 30, 2012 were $nil compared to $26,810 for the three months ended April 30, 2011. These expenses were incurred prior to the Company being classifies as a Tier 2 Oil & Gas Issuer, as defined by the Exchange, and relate to its search for a qualifying transaction, which was completed in June 2011.

Consulting expenses for the three months ended April 30, 2012 were $42,820 compared to $nil for the three months ended April 30, 2011. Upon completing its qualifying transaction, the Company engaged David Gibbs to manage its operations, on a fee for services basis. Subsequent to April 30, 2012, Mr. Gibbs was appointed president of the Company.

Professional expenses for the three months ended April 30, 2012 were $41,359 compared to $103,024 for the three months ended April 30, 2011. Legal fees were the major component of professional fees for the three months ended April 30, 2012. The major component of professional fees included legal fees in Canada associated with the acquisition of the qualifying transaction for the three months ended April 30, 2011.

Project investigation costs for the three months ended April 30, 2012 were $5,082 compared to $nil for the three months ended April 30, 2011. These expenses relate to the Company's ongoing assessment of prospective projects. When a project is determined not to be suitable all costs associated with the investigations are expensed.

Travel and investor relations expenses for the three months ended April 30, 2012 were $54,845 compared to $nil for the three months ended April 30, 2011. These expenses increased due to the commencement of operations in Texas.

Transfer agent and filing fees for the three months ended April 30, 2012 were $12,852 compared to $20,710 for the three months ended April 30, 2011. Transfer agent and filing fees decreased in the current period due to the completion of a qualifying transaction and increased market activity associated with the new share issues in the period ended April 30, 2011.

Summary of Quarterly Results

The results of the Company's most recent eight quarters are set out below:

	April 30, 2012	January 31, 2012	October 31, 2011	July 31, 2011
Revenue	$ 555,756	$ -	$ -	$ -
Net income (loss)	212,244[1]	(561,886)[2]	(251,308)[3]	(251,065)[4]
Exploration and evaluation	4,075,106	2,973,526	360,959	-
Property and equipment	1,313,608	-	-	-
Total assets	9,449,160	5,592,676	3,332,630	3,425,756
Income (loss) per share – basic and diluted	0.00	(0.01)	(0.01)	(0.01)

	April 30, 2011	January 31, 2011	October 31, 2010	July 31, 2010
Revenue	$ -	$ -	$ -	$ -
Net income (loss)	(145,087)	(14,429)	4,026	(26,046)
Exploration and evaluation	-	-	-	-
Property and equipment	-	-	-	-
Total assets	2,636,833	2,744,704	2,743,031	2,736,821
Income (loss) per share – basic and diluted	(0.00)	(0.00)	0.00	(0.01)

Notes:

1) Net income during this period includes non-cash deductions of $75,549 for share–based payments and $5,506 for depletion and accretion expenses.
2) The Company's loss during this period includes non-cash deductions of $95,878 for share-based payments and $234,564 for impairment of oil and gas properties.
3) The Company's loss includes expenses incurred in connection with the Company's new business after the completion of its qualifying transaction in June 2011.
4) The Company's loss during this period includes non-cash deductions of $173,699 for share-based payments.

Fluctuations in reported earnings during the prior quarters are primarily due to changes in share-based payments, professional fees, business investigation costs and costs associated with its new business after completion of the Company's qualifying transaction in June 2011. There was no impact on quarterly results transitioning from Canadian Generally Accepted Accounting Principles to International Financial Reporting Standards ("IFRS").

Financial Condition, Liquidity and Capital Resources

As at April 30, 2012, the Company had cash of $3,512,294, accounts receivable of $521,694 and accounts payable and accrued liabilities of $125,705 due within three months of the three months ended April 30.

In May 2012, the Company completed a private placement of $10,000,000 of which $3,605,000 was received in April 2012.

The balance of proceeds from the private placement will be used, together with the Company's existing working

capital, to fund the development of the Company's oil and gas properties and for general working capital purposes.

Subsequent to April 30, 2012, the Company advanced the sum of US$2,698,197 representing the operator's estimate of the Company's share of the costs to drill and complete a second well on the STS Olmos project acreage and the additional aggregate sum of US$1,999,062 representing the operator's estimate of the Company's share of the lease payments, drilling, evaluation and casing costs of a vertical extension of a second well on the Cutlass project acreage.

As of the date of this report, the Company has no significant commitments or restrictions on its cash except as described herein (see "Background"). The Company has not pledged any of its assets as security for loans, or otherwise, and is not subject to any debt or other covenants. Management of the Company believes it has sufficient capital to meet its financial obligations over the next twelve months. However, additional financing may be required to fund the future development of its oil and gas properties. Although the Company has been successful with securing capital in the past, there is no assurance that it will secure necessary capital in the future.

Off Balance Sheet Arrangements

There are no off-balance sheet arrangements to which the Company is committed.

Key Management Personnel Compensation

During the three months ended April 30, 2012, the Company:

a) Paid or accrued $48,425 (2011 - $nil) for consulting services of which $5,605 were capitalized, $1,345 (2011 - $nil) for project investigation costs, $nil (2011 - $2,931) for business investigation costs to Dave Gibbs, an officer and director of the Company.

b) Paid or accrued $36,169 (2011 - $55,932) for legal services to a law firm of which Paul Visosky, the former corporate secretary of the Company is a principal;

c) Paid or accrued $4,500 (2011 - $nil) for accounting services to a firm where Scott Davis, an officer of the Company is a partner; and

d) Paid or accrued $nil (2011 - $3,000) for accounting services to Jennie Choboter, a former officer of the Company.

The compensation paid to key management personnel was $54,270 (2011 - $5,932).

New accounting policy

Revenue recognition

Revenue from the sale of oil and gas is recorded when title passes to an external party and is based on volumes delivered to customers at contractual delivery points, and rates and collectability are reasonably assured. Delivery is generally at the time the product enters the pipeline. The cost associated with the delivery, including operating and maintenance costs, transportation and production based royalty expenses, are recognized during the same period in which the related revenue is earned and recorded.

<u>New accounting standards and interpretation</u>

A number of new standards, amendments to standards and interpretations are effective for annual periods beginning after January 1, 2013, including IAS 1 *Presentation of Financial Statements,* IAS 19 *Employee Benefits,* IFRS 9 *Financial Instruments,* IFRS *10 Consolidated Financial Statements,* IFRS 11 *Joint Arrangements,* IFRS 12 *Disclosure of Interest of Other Entities, and* IFRS 13 *Fair Value Measurement,* and have not been applied in preparing these consolidated financial statements. None of these are expected to have a significant effect on the consolidated financial statements of the Company, except for IFRS 9 *Financial Instruments* ("IFRS 9"), which becomes mandatory for the Company's 2015 consolidated financial statements and could change the classification and measurement of financial assets. The extent of the effects of the new accounting standards on the condensed interim consolidated financial statements has not been determined.

Risk Factors

The exploration and development of oil and gas properties involves certain significant risks not within the control of management. Risks factors affecting the prospects of the Company include, but are not limited to, the following:

<u>Exploration, Development and Production Risks</u>
Oil and natural gas exploration involves a high degree of risk and there is no assurance that expenditures made on future exploration by the Company will result in new discoveries of oil or natural gas in commercial quantities. The Company, through its subsidiaries, has the right to earn working interests in various oil & gas properties described herein. To earn such interests the Company must incur certain specified expenditures to evaluate and complete a number of prospective wells capable of producing oil and gas in paying quantities. No assurance can be given that the Company will be successful in completing a well capable of producing oil and gas. The long-term commercial success of the Company depends on its ability to find, acquire, develop and commercially produce oil and natural gas reserves. Without the continual addition of new reserves, any existing reserves the Company may have at any particular time and the associated production if any therefrom will decline over time as the reserves are exploited. A future increase in the Company's reserves will depend not only on its ability to explore and develop any properties it may have from time to time, but also on its ability to select and acquire suitable producing properties or prospects. No assurance can be given that the Company will be able to continue to locate satisfactory properties for acquisition or participation. Exploration and development activities may be delayed or adversely affected by factors outside the control of the Company including adverse climatic and geographic conditions, labour disputes, compliance with governmental requirements, shortage or delays in installing and commissioning plant and equipment or import or customs delays. Drilling may involve unprofitable efforts, not only with respect to dry wells, but also with respect to wells, though yielding some oil or gas, are not sufficiently productive to justify commercial development or cover operating and other costs. Oil and natural gas exploration, development and production operations are subject to all the risks and hazards typically associated with such operations, including hazards such as fire, explosion, blowouts, cratering, sour gas releases and spills, each of which could result in substantial damage to oil and natural gas wells, production facilities, other property and the environment or in personal injury.

<u>Additional Funding Requirements</u>
Terrace has no prior history of production or profitability and its financial resources may not be sufficient to fund its ongoing activities at all times. From time to time, the Company will require additional financing to carry out its oil and gas acquisition, exploration and development activities. Failure to obtain such financing on a timely basis could cause the Company to forfeit its interest in certain properties, miss certain acquisition opportunities and reduce or terminate its operations. Any additional financing is likely to involve the issuance of securities which could be substantially dilutive.

No Assurance of Title

Title to oil and gas interests is often not capable of conclusive determination without incurring substantial expense. The nature of the oil and gas leasing and title regime in the U.S. is such that interests in tracts of acreage may be represented by many leases and other agreements affecting oil and gas rights and access and obtaining absolute confirmation of chain of title would be time consuming and expensive. While the Company will conduct a title review of a particular area prior to commencement of drilling there can be no assurance of title. Title may be subject to unregistered liens and other defects which, if affecting a core area, could have a material adverse effect on the Company, its financial condition, results of operations and prospects.

Permits and Licenses

The activities of the Company are subject to government approvals, various laws governing prospecting, development, land resumptions, production taxes, labour standards and occupational health, safety, toxic substances and other matters, including issues affecting local native populations. Although the Company believes its planned development work is in accordance with all applicable rules and regulations, no assurance can be given that new rules and regulations will not be enacted or that existing rules and regulations will not be applied in a manner which could limit or curtail production or development. Amendments to current laws and regulations governing operations and activities of exploration and quarrying, or more stringent implementation thereof, could have a material adverse impact on the business, operations and financial performance of the Company. Further, the exploration and development permits and licenses that have and may be issued in respect of each project may be subject to conditions which, if not satisfied, may lead to the revocation of such permits and licenses. In the event of revocation, the value of the Company's investments in such projects may decline.

Reserve Estimates

No current reserves have been estimated in respect of the Company's oil & gas properties.. There are numerous uncertainties inherent in estimating quantities of oil, natural gas and natural gas liquids reserves and resources and associated cash flows, including many factors beyond the Company's control. In general, estimates of economically recoverable oil and natural gas reserves and the future net cash flows from them are based upon a number of variable factors and assumptions, such as historical production from the properties, production rates, ultimate reserve recovery, timing and amount of capital expenditures, marketability of oil and natural gas, royalty rates, the assumed effects of regulation by governmental agencies and future operating costs, all of which may vary from actual results. The Company's actual production, revenues, taxes and development and operating expenditures with respect to its reserves will vary from estimates thereof and such variations could be material.

Prices and Markets for Oil and Natural Gas

Oil and natural gas are commodities whose prices are determined based on world demand, supply and other factors, all of which will be beyond the control of the Company. World prices for oil and natural gas have fluctuated widely in recent years. Any material decline in prices could result in a reduction of net production revenue. Certain wells or other projects may become uneconomic as a result of a decline in world oil prices or natural gas prices, leading to a reduction in the volume of the Company's oil and gas reserves. The Company might also elect not to produce from certain wells at lower prices. All of these factors could result in a material decrease in the Company's future net production revenue, causing a reduction in its oil and gas acquisition and development activities. Prices for oil and gas are subject to large fluctuations in response to relatively minor changes in the supply of and demand for oil and gas, market uncertainty and a variety of additional factors beyond the control of the Company. These factors include economic conditions, in the United States and Canada, the actions of OPEC, governmental regulation, political stability in the Middle East and elsewhere, the foreign supply of oil and gas, risks of supply disruption, the price of foreign imports and the availability of alternative fuel sources. Any substantial and extended decline in the price of oil and gas would have an adverse effect on the Company's carrying value of its reserves, borrowing capacity, revenues, profitability and cash flows from operations and may have a material adverse effect on the Company's business, financial condition, results of operations and prospects.

Uninsurable Risks

Lack of Adequate Insurance

In the course of exploration, development and production of mineral properties, certain risks, and in particular, unexpected or unusual geological operating conditions including rock bursts, cave-ins, fires, flooding and earthquakes may occur. It is not always possible to fully insure against such risks and the Company may decide not to take out insurance against such risks as a result of high premiums or other reasons. Should such liabilities arise, they could reduce or eliminate any future profitability and result in increasing costs and a decline in the value of the securities of the Company.

Competition

The oil and gas industry is highly competitive. The Company's competitors for the acquisition, exploration, production and development of oil and natural gas properties, and for capital to finance such activities will include companies that have greater financial and personal resources available to them than the Company.

Risks Associated with Joint Operating Agreements

The development of the Company's oil & gas properties is governed by a various joint operating agreements. The existence or occurrence of a disagreement or dispute with or among the other parties to such agreement could have a material adverse impact on the Company's profitability or the viability of its interests , which could have a material adverse impact on the Company's business prospects, results of operations and financial condition.

Environmental Risks

All phases of the oil and natural gas business present environmental risks and hazards and are subject to environmental regulation pursuant to a variety of international conventions and provincial and municipal laws and regulations. Environmental legislation provides for, among other things, restrictions and prohibitions on spills, releases or emissions of various substances produced in association with oil and gas operations. The legislation also requires that wells and facility sites be operated, maintained, abandoned and reclaimed to the satisfaction of applicable regulatory authorities. Compliance with such legislation can require significant expenditures and a breach may result in the imposition of fines and penalties, some of which may be material. Environmental legislation is evolving in a manner expected to result in stricter standards and enforcement, larger fines and liability and potentially increased capital expenditures and operating costs. There is no assurance that future changes in environmental regulation, if any, will not adversely affect the Company's operations or prevent operations all together. Government approvals and permits are currently, and may in the future be, required in connection with the Company's operations, which could potentially make operations expensive or prohibit them altogether. To the extent such future approvals are required and not obtained, the Company may be curtailed or prohibited from proceeding with planned exploration or development of the Properties or from commencing production.

Availability of Drilling Equipment and Access Restrictions

Oil and natural gas exploration and development activities are dependent on the availability of drilling and related equipment in the particular areas where such activities will be conducted. Demand for such limited equipment or access restrictions may affect the availability of such equipment to the Company and may delay exploration and development activities.

Current Global Financial Conditions

Current global financial conditions have been subject to increased volatility and numerous financial institutions have either gone into bankruptcy or have had to be rescued by governmental authorities. Access to public financing has been negatively impacted by both sub-prime mortgages and the liquidity crisis affecting the asset-backed commercial paper market. These factors may impact the ability of the Company to obtain equity or debt financing in the future and, if obtained, on terms favourable to the Company. If these increased levels of volatility and market turmoil continue, the Company's operations could be adversely impacted and the value and the price of the Company's shares could continue to be adversely affected.

Geo Political Risks

The marketability and price of oil and natural gas that may be acquired or discovered by the Company is and will continue to be affected by political events throughout the world that cause disruptions in the supply of oil. Conflicts, or conversely peaceful developments, arising in the Middle East, and other areas of the world, have a significant impact on the price of oil and natural gas. Any particular event could result in a material decline in prices and therefore result in a reduction of the Company’s net production revenue.

Transportation Costs

Disruption in or increased costs of transportation services could make oil and natural gas a less competitive source of energy or could make the Company's oil and natural gas less competitive than other sources. The industry depends on rail, trucking, ocean-going vessels, pipeline facilities, and barge transportation to deliver shipments, and transportation costs are a significant component of the total cost of supplying oil and natural gas. Disruptions of these transportation services because of weather related problems, strikes, lockouts, delays or other events could temporarily impair the ability to supply oil and natural gas to customers and may result in lost sales. In addition, increases in transportation costs, or changes in transportation costs for oil and natural gas produced by competitors, could adversely affect profitability. To the extent such increases are sustained, the Company could experience losses and may decide to discontinue certain operations forcing the Company to incur closure and/or care and maintenance costs, as the case may be. Additionally, lack of access to transportation may hinder the expansion of production at some of the Company's properties and the Company may be required to use more expensive transportation alternatives.

Pipeline Capacity

Although pipeline expansions are ongoing, the availability of sufficient pipeline capacity continues to affect the oil and natural gas industry and limit the ability to produce and to market natural gas production. In addition, the pro-rationing of capacity on the inter-state pipeline systems also continues to affect the ability to export oil and natural gas.

Reliance on Key Individuals

The Company's success depends to a certain degree upon certain key members of the management. It is expected that these individuals will be a significant factor in the Company's growth and success. The loss of the service of members of the management and certain key employees could have a material adverse effect on the Company.

Conflicts of Interest

Certain of the Company's directors are also directors, officers or shareholders of other companies that are engaged in the business of acquiring, developing and exploiting natural resource properties. Such associations may give rise to conflicts of interest from time to time. Such a conflict poses the risk that the Company may enter into a transaction on terms which place the Company in a worse position than if no conflict existed. The directors are required by law to act honestly and in good faith with a view to the best interest of the Company and to disclose any interest which they may have in any project or opportunity of the Company. However, each director has similar obligations to other companies for which such director serves as an officer or director. If a conflict of interest arises at a meeting of the board of directors, any director in a conflict is required disclose his interest and abstain from voting on such matter. In determining whether or not the Company will participate in any project or opportunity, the board of directors will primarily consider the degree of risk to which the Company may be exposed and its financial position at that time.

Financial Instruments

The Company has classified its financial instruments as follows:

- Cash - as FVTPL;
- Accounts receivable – as loans and receivables; 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:

Fair value

The carrying values of cash, restricted cash, accounts receivable, and accounts payable and accrued liabilities approximate their fair values due to 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 accounts 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. Accounts receivable is comprised from the sale of oil and gas.

Market risk

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate due to 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

To the extent that payments made or received on the Company's monetary assets and liabilities are affected by changes in prevailing market interest rates, the Company is exposed to interest rate cash flow risk.

To the extent that changes in prevailing market interest rates differ from the interest rates in the Company's monetary assets and liabilities, the Company is exposed to interest rate price risk.

The Company's exposure to interest rate risk is minimal.

(ii) Foreign currency risk

The Company's principal asset is located in the United States. As at the date of this report, the majority of the Company's cash was held in Canadian dollars and was therefore subject to fluctuation against the United States dollar. Based on the balances as at April 30, 2012, if the US dollar had weakened (strengthened) against the Canadian dollar, with all other variables held constant, by 1%, net loss would be approximately $1,000. There would be no effect on other comprehensive loss. The Company does not use derivatives or similar instruments to manage currency risk.

(iii) Other price risk

Other price risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate due to 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, 2012, the Company had cash of $3,512,294, accounts receivable from the sale of oil and gas of $521,694 and accounts payable and accrued liabilities of $125,705 due within three months of the period-end.

Shareholder's Equity and Outstanding Share Data

The authorized share capital of the Company consists of an unlimited number of common shares.

As of April 30, 2012 and June 27, 2012, the Company had 52,919,321 and 62,919,321 common shares outstanding respectively.

As of June 27, 2012, the Company had the following stock options and warrants outstanding:

- Stock options

Number of options	Number of options exercisable	Exercise price	Expiry Date
1,800,000	1,800,000	$ 0.12	June 22, 2016
250,000	62,500	$ 0.19	July 15, 2016
250,000	62,500	$ 0.21	September 16, 2016
250,000	62,500	$ 0.19	October 18, 2016
100,000	20,000	$ 0.53	November 25, 2016
250,000	25,000	$ 0.67	December 16, 2016
2,900,000	2,032,500		

- Warrants

Number of warrants	Exercise price	Expiry date
7,112,500	0.18	June 21, 2016

Internal Controls Over Financial Reporting

Changes in Internal Control over Financial Reporting ("ICFR")

In connection with National Instrument 52-109, Certification of Disclosure in Issuer's Annual and Interim Filings ("NI 52-109") adopted in December 2008 by each of the securities commissions across Canada, the Chief Executive Officer and Chief Financial Officer of the Company will file a Venture Issuer Basic Certificate with respect to financial information contained in the unaudited interim financial statements and the audited annual

financial statements and respective accompanying Management's Discussion and Analysis. The Venture Issue Basic Certification does not include representations relating to the establishment and maintenance of disclosure controls and procedures and internal control over financial reporting, as defined in NI52-109.

Proposed Transactions

There are no proposed transactions that have not otherwise been disclosed herein.

Contingencies

There are no contingent liabilities.

Management's Responsibility For Financial Statements

The information provided in this report, including the financial statements, is the responsibility of management. In the preparation of these statements, estimates are sometimes necessary to make a determination of future values for certain assets or liabilities. Management believes such estimates have been based on careful judgments and have been properly reflected in the financial statements.

Other MD&A Requirements

Additional disclosure of the Company's technical reports, material change reports, news releases and other information can be obtained on SEDAR at www.sedar.com.

Directors and Officers

Eric Boehnke	Director and CEO
David Gibbs	Director and President
Dan Carriere	Director
Murray Oliver	Director
William McCartney	Director
Ken Shannon	Director
Scott Davis	CFO
Deborah Cotter	Secretary

Contact Person

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