

Exall
Energy Corporation



2011 Q3
FINANCIAL STATEMENTS

MANAGEMENT'S REPORT

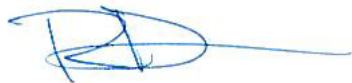
To the Shareholders of Exall Energy Corporation:

The consolidated financial statements of Exall Energy Corporation were prepared by management in accordance with appropriately selected International Financial reporting Standards ("IFRS") principles in Canada, including IAS 34 and IFRS 1. Management has used estimates and careful judgment, particularly in those circumstances where transactions affecting current periods are dependent on information not known until a future period. The financial and operational information contained in this annual report is consistent with that reported in the financial statements.

Management is responsible for the integrity of the financial and operational information contained in this report. The Company has designed and maintains internal controls to provide reasonable assurance that assets are properly safeguarded and that the financial records are well maintained and provide relevant, timely and reliable information to management. The consolidated financial statements have been prepared within reasonable limits of materiality and within the framework of the significant accounting policies summarized in the notes to the consolidated financial statements.

External auditors appointed by the shareholders have conducted an independent review of the corporate and accounting records. The Audit Committee has met with the external auditors and management in order to determine if management has fulfilled its responsibilities in the preparation of the consolidated financial statements. The Board of Directors has approved the consolidated financial statements on the recommendation of the Audit Committee.

Exall Energy Corporation



Roger N. Dueck

President and Chief Executive Officer



Warren F.E. Coles

Vice President, Finance and Chief Financial Officer

Calgary, Canada
November 08, 2011

Consolidated Statement of Financial Position (Unaudited)

As at (thousands of Canadian dollars)	September 30, 2011	December 31, 2010	January 01, 2010
Assets			
Current			
Cash	\$ 68	\$ 24	\$ 21
Accounts receivable (note 5)	8,860	5,699	2,578
Prepaid expenses	159	167	371
	9,087	5,890	2,970
Exploration and evaluation assets (note 6)	7,115	1,386	743
Property, plant and equipment (note 6)	65,209	40,983	24,397
	\$ 81,411	\$ 48,259	\$ 28,110
Liabilities			
Current			
Bank indebtedness (note 7)	\$ 19,596	\$ 13,032	\$ 7,939
Accounts payable and accrued liabilities (note 12)	13,740	7,032	3,595
	33,336	20,064	11,534
Deferred income tax liability	3,473	1,996	451
Decommissioning liabilities (note 8)	1,383	1,077	758
	38,192	23,137	12,743
Shareholders' Equity			
Share capital (note 9)	34,501	21,553	16,797
Warrants (note 9)	11	243	11
Contributed surplus (note 10)	2,444	1,757	1,167
Cumulative translation adjustment	6	-	-
Retained earnings (deficit)	6,257	1,569	(2,608)
	43,219	25,122	15,367
	\$ 81,411	\$ 48,259	\$ 28,110

The notes are an integral part of these consolidated financial statements

Commitments (note 17)

On behalf of the Board:


_____, Director
Stephen G. Roman, Executive Chairman


_____, Director

D. Allan Menzies, Audit Committee Chairman

Consolidated Statement of Earnings and Comprehensive Income

(Unaudited)

For the periods ended September 30, (thousands of Canadian dollars, except per share amounts)	Three months ended		Nine Months Ended	
	2011	2010	2011	2010
Revenue				
Oil and gas production	\$ 8,044	\$ 5,188	\$ 22,886	15,674
Royalties	(2,046)	(1,234)	(6,321)	(5,487)
	5,998	3,954	16,565	10,187
Expenses				
Oil and gas production	893	460	2,594	1,523
Depletion, depreciation and amortization (note 6)	2,009	1,077	4,981	3,192
Administration	241	387	1,243	1,320
Share based payments (note 10)	507	252	771	530
Finance costs (note 11)	156	167	375	434
Loss on assets disposition	-	-	185	-
Losses on foreign exchange translation	13	(1)	8	1
	3,819	2,342	10,157	7,000
Earnings before other income	2,179	1,612	6,408	3,187
Other income (note 16)	-	891	-	1,313
Earnings before income taxes	2,179	2,503	6,408	4,500
Deferred income tax expense	706	757	1,720	1,365
Net earnings	1,473	1,746	4,688	3,135
Other comprehensive income (loss)				
Foreign currency translation adjustment	19	-	6	(2)
Comprehensive income for the period	\$ 1,492	\$ 1,746	\$ 4,694	\$ 3,133
Net earnings per share (dollars) (note 9)				
Basic	\$ 0.02	\$ 0.03	\$ 0.08	0.06
Diluted	0.02	0.03	0.07	0.06

The notes are an integral part of these consolidated financial statements

Consolidated Statement of Changes in Equity

(Unaudited)

(thousands of Canadian dollars)	Number of common Shares (note 9)	Share capital (note 9)	Warrants (note 9)	Contributed surplus (note 10)	Cumulative translation adjustment	Retained earnings (deficit)	Total equity
Balance at December 31, 2010	53,873,707	\$ 21,553	243	\$ 1,757	-	\$ 1,569	\$ 25,122
Issue of common shares	5,750,000	11,500					11,500
Share issue costs, net of tax of \$243		(717)					(717)
Share based payments				771			771
Options exercised	530,000	321		(84)			237
Warrants exercised	2,035,147	1,844	(232)				1,612
Cumulative translation adjustment					6		6
Net earnings for the period						4,688	4,688
Balance at September 30, 2011	62,188,854	\$ 34,501	11	\$ 2,444	6	\$ 6,257	\$ 43,219
Balance at January 01, 2010	45,921,227	\$ 16,797	11	\$ 1,167	-	(2,608)	\$ 15,367
Issue of common shares	5,774,851	3,754					3,754
Share issue costs, net of tax of \$74		(225)					(225)
Share based payments				530			530
Options exercised	701,667	392		(99)			293
Issuance of warrants		(344)	344				-
Issuance of broker warrants		(60)	60				-
Exercise of warrants	50,000	49	(9)				40
Cumulative translation adjustment					(2)		(2)
Net earnings for the period						3,133	3,133
Balance at September 30, 2010	52,447,745	\$ 20,363	406	\$ 1,598	(2)	\$ 525	\$ 22,890

The notes are an integral part of these consolidated financial statements

Consolidated Statement of Cash Flow

(Unaudited)

For the periods ended September 30, (thousands of Canadian dollars)	Three months ended		Nine months ended	
	2011	2010	2011	2010
Operating activities				
Net income for the period	\$ 1,473	\$ 1,746	\$ 4,688	\$ 3,133
Adjustments for:				
Depletion and amortization	2,009	1,077	4,981	3,192
Accretion	7	6	25	20
Share based payments	507	252	771	530
Deferred income tax expense	706	757	1,720	1,365
Loss on asset disposition	-	-	185	-
Loss on foreign exchange	13	-	8	-
Changes in non-cash working capital (note 15)	(582)	(424)	(931)	(1,524)
Net cash from (used in) operating activities	4,133	3,414	11,447	6,716
Financing activities				
Increase in bank indebtedness	6,275	3,541	6,564	3,068
Proceeds from issue of share capital (note 9)	-	-	11,500	3,754
Proceeds from exercise of share options (note 9)	-	62	237	293
Proceeds from exercise of warrants (note 9)	-	40	1,612	40
Share issue costs (note 9)	-	-	(960)	(299)
Net cash from (used in) financing activities	6,275	3,643	18,953	6,856
Investing activities				
Property, plant and equipment expenditures	(16,174)	(5,636)	(34,867)	(13,956)
Proceeds on disposition	-	-	25	-
Changes in non-cash working capital (note 15)	5,782	(1,406)	4,486	402
Net cash from (used in) investing activities	(10,392)	(7,042)	(30,356)	(13,554)
Increase (decrease) in cash	16	15	44	18
Cash, beginning of the period	52	24	24	21
Cash, end of the period	\$ 68	\$ 39	\$ 68	\$ 39
Supplemental cash flow information				
Cash interest paid	\$ 149	\$ 161	\$ 350	\$ 414
Cash taxes paid	-	-	-	-

The notes are an integral part of these consolidated financial statements

Exall Energy Corporation
Notes to the Consolidated Interim Financial Statements
For the three and nine months ended September 30, 2011 and 2010
(Unaudited)

(in thousands of Canadian Dollars)

General information:

Exall Energy Corporation (“Exall Energy” or the “Company”) was incorporated under the laws of the Province of Ontario on September 15, 2006 and continued under the laws of the Province of Alberta on November 6, 2007. The Company’s shares commenced trading on the Toronto Stock Exchange (“TSX”) under the symbol “EE” on March 22, 2007. On January 31, 2007, the Company acquired 100 percent of the issued and outstanding common shares of Kingsmere Exploration Ltd. (“Kingsmere”) and amalgamated with Kingsmere on July 1, 2007, continuing operations under Exall Energy Corporation.

The consolidated financial statements of the Company as at and for the three and nine month periods ended September 30, 2011 and 2010 comprise the Company and its wholly owned subsidiaries. The Company is engaged in the exploration for and development of oil and natural gas, from its properties in Alberta, British Columbia, and Texas, and conducts many of its activities jointly with others; these financial statements reflect only the Company’s proportionate interest in such activities.

The address of the Company’s registered office is 3700, 400 – 3rd Avenue S.W., Calgary, Alberta, Canada, T2P 4H2.

2. Basis of preparation and adoption of IFRS

The Company prepares its 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, and require publicly accountable enterprises to apply such standards effective for years beginning on or after January 1, 2011. Accordingly, the Company has reported on this basis in these interim consolidated financial statements. In the financial statements, the term “Canadian 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 IAS 34 and IFRS 1. Subject to certain transition elections disclosed in note 4, the Company has consistently applied the same accounting policies in its opening IFRS statement of financial position at January 1, 2010 and throughout all periods presented, as if these policies had always been in effect. Note 4 discloses the impact of the transition to IFRS on the Company’s reported financial position, financial performance and cash flows, 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 condensed interim consolidated financial statements are based on IFRS issued and outstanding as of November 08, 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 transition adjustments recognized on change-over to IFRS.

The condensed interim consolidated financial statements should be read in conjunction with the Company’s Canadian GAAP annual financial statements for the year ended December 31, 2010.

3. Significant accounting policies, judgments and estimation uncertainty

Significant accounting policies

The significant accounting policies used in the preparation of these interim consolidated financial statements are described below.

Basis of measurement

The consolidated financial statements have been prepared under the historical cost convention, except for the revaluation of certain financial assets and financial liabilities to fair value.

Exall Energy Corporation
Notes to the Consolidated Interim Financial Statements
For the three and nine months ended September 30, 2011 and 2010
(Unaudited)

(in thousands of Canadian Dollars)

3. Significant accounting policies, judgments and estimation uncertainty (continued)

Consolidation

The financial statements of the Company consolidate the accounts of Exall Energy and its subsidiaries. All intercompany transactions, balances and unrealized gains and losses from intercompany transactions are eliminated on consolidation.

Subsidiaries are those entities which Exall Energy controls by having the power to govern the financial and operating policies. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether Exall Energy Corporation controls another entity. Subsidiaries are fully consolidated from the date on which control is obtained by Exall Energy and are de-consolidated from the date that control ceases.

Joint Arrangements

The Company conducts many of its activities through interests in jointly controlled assets and operations where the Company has a direct ownership interest in and jointly controls the assets and/or operations. The Company recognizes its proportionate share of the income, expenses, assets, and liabilities of these jointly controlled assets and/or operations in the consolidated financial statements”

Foreign currency translation

(i) Functional and presentation currency

Items included in the financial statements of each consolidated entity in the Exall Energy group are measured using the currency of the primary economic environment in which the entity operates (the “functional currency”). The consolidated financial statements are presented in Canadian dollars, which is the Company’s functional currency.

The financial statements of entities that have a functional currency different from that of Exall Energy (“foreign operations”) are translated into Canadian dollars as follows: assets and liabilities – at the closing rate at the date of the statement of financial position, and income and expenses – at the average rate of the period. All resulting changes are recognized in other comprehensive income as cumulative translation adjustments.

When an entity disposes of its entire interest in a foreign operation, or loses control, joint control, or significant influence over a foreign operation, the foreign currency gains or losses accumulated in other comprehensive income related to the foreign operation are recognized in profit or loss. If an entity disposes of part of an interest in a foreign operation which remains a subsidiary, a proportionate amount of foreign currency gains or losses accumulated in other comprehensive income related to the subsidiary is reallocated between controlling and non-controlling interests.

(ii) Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Generally, foreign exchange gains and losses resulting from the settlement of foreign currency transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in currencies other than an operation’s functional currency are recognized in the statement of comprehensive income.

Cash and cash equivalents

Cash and cash equivalents include cash on hand, deposits held with banks, and other short-term highly liquid investments with original maturities of three months or less.

Exall Energy Corporation
Notes to the Consolidated Interim Financial Statements
For the three and nine months ended September 30, 2011 and 2010
(Unaudited)

(in thousands of Canadian Dollars)

3. Significant accounting policies, judgments and estimation uncertainty (continued)

Financial instruments

The Company is required to recognize financial assets and financial liabilities, including derivatives, on the statement of financial position when the Company becomes a party to the contractual provisions of the financial instrument or non-financial derivative contract. Accordingly, all financial instruments are required to be measured at fair value upon initial recognition. Measurement in subsequent periods depends on whether the financial instrument has been classified as fair value through profit or loss, available-for sale, held-to-maturity, loans or receivables or financial liabilities at amortized cost. Financial assets and financial liabilities held for-trading are measured at fair value with changes in those fair values recognized in net earnings. Financial assets held-to-maturity, loans and receivables, and other financial liabilities are measured at amortized cost using the effective interest method of amortization. Investments in equity instruments classified as available-for-sale that do not have a quoted market price in an active market and the fair value cannot be measured reliably are measured at cost.

Cash and accounts receivable are designated as “loans or receivables”. The revolving operating loan and accounts payable and accrued liabilities are designated as “financial liabilities at amortized cost”.

For financial instruments measured at amortized cost, the Company’s applies issue costs against the carrying value of the related asset or liability.

Impairment of financial assets

At each reporting date, the Company assesses whether there is objective evidence that a financial asset is impaired. If such evidence exists, the Company recognizes an impairment loss, as follows:

- (i) Financial assets carried at amortized cost: The loss is the difference between the amortized cost of the loan or receivable and the present value of the estimated future cash flows, discounted using the instrument’s original effective interest rate. The carrying amount of the asset is reduced by this amount either directly or indirectly through the use of an allowance account.
- (ii) Available-for-sale financial assets: The impairment loss is the difference between the original cost of the asset and its fair value at the measurement date, less any impairment losses previously recognized in the statement of income. This amount represents the cumulative loss in accumulated other comprehensive income that is reclassified to net income.

Impairment losses on financial assets carried at amortized cost are reversed in subsequent periods if the amount of the loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized. Impairment losses on available-for-sale equity instruments are not reversed.

Exploration and Evaluation (“E&E”) Assets

- (i) Assets

Costs incurred after the legal right to explore an area has been obtained and before technical feasibility and commercial viability of the area have been established are capitalized as E&E assets. These costs include license acquisition, geological and geophysical, drilling, sampling, decommissioning and other directly attributable internal costs. E&E assets are not depreciated and are carried forward until technical feasibility and commercial viability of the field/area/project is determined or the assets are determined to be impaired. The Company will expense the cost of expired leases included in E&E assets, unless they relate to a viable area, in which case they will be moved to D&P asset. E&E assets will not be amortized as the Company does not have any tangible E&E assets.

Exall Energy Corporation
Notes to the Consolidated Interim Financial Statements
For the three and nine months ended September 30, 2011 and 2010
(Unaudited)

(in thousands of Canadian Dollars)

3. Significant accounting policies, judgments and estimation uncertainty (continued)

Once technical feasibility and commercial viability have been established for an area, the carrying value of the E&E assets associated with that area is tested for impairment as discussed below. The carrying value, net of any impairment loss, is then reclassified as property, plant and equipment.

If it is determined that the area is not technically feasible or commercially viable or if the Company decides not to continue the exploration and evaluation activity, then the accumulated costs are expensed to exploration expense in the period in which the event occurs.

E&E assets are assessed for impairment when facts and circumstances suggest that the carrying amount may exceed its recoverable amount. Any impairment loss is recognized in the Consolidated Statements of Earnings and Comprehensive Income as additional exploration expense and separately disclosed. E&E assets are allocated to a related cash generating unit ("CGU") containing development and production assets. The aggregate carrying amount is compared to the expected recoverable amount of the CGU generally by reference to the present value of the future cash flows from the production of reserves. Any gains or losses from the divestiture of E&E assets are recognized in net earnings.

Property, plant & equipment

(i) Development and Production Assets

Development and production assets are stated at cost less accumulated depreciation, depletion, amortization and impairment losses. Development and production assets are capitalized on an area by-area basis and include all costs associated with the development and production of the crude oil and natural gas properties as well as any E&E expenditures incurred in finding commercial reserves transferred from E&E assets. These costs include internal costs, decommissioning liabilities, and, for qualifying assets, borrowing costs, directly associated with the acquisition of, the exploration for, and the development of crude oil and natural gas reserves.

Costs accumulated within each area are depleted using the unit-of-production method based on estimated proved reserves determined using estimated future prices and costs. For purposes of this calculation, natural gas is converted to oil on an energy equivalent basis. Costs subject to depletion include estimated future costs to be incurred in developing proved reserves.

Exchanges of development and production assets are measured at fair value unless the transaction lacks commercial substance or the fair value of neither the asset received nor the asset given up can be reliably measured. When fair value is not used, the carrying amount of the asset given up is used as the cost of the asset acquired.

Repairs and maintenance are expensed when incurred.

Any gains or losses from the divestiture of development and production assets are recognized in net earnings.

Development and production assets are assessed for indicators of impairment at least annually or when facts and circumstances suggest that the carrying amount of the development and production assets may exceed its recoverable amount. Recoverable amount is determined as the greater of an asset's or CGU's value-in-use ("VIU") and fair value less costs to sell ("FVLCTS"). VIU is estimated as the discounted present value of the future cash flows expected to arise from the continuing use of a CGU or asset. In determining FVLCTS, recent market transactions are taken into account, if available. In the absence of such transactions, an appropriate valuation model is used. The impairment test is performed at the CGU level for development and production assets. Impairment losses are recognized in the Consolidated Statements of Earnings and Comprehensive Income as additional depreciation and are separately disclosed.

Exall Energy Corporation
Notes to the Consolidated Interim Financial Statements
For the three and nine months ended September 30, 2011 and 2010
(Unaudited)

(in thousands of Canadian Dollars)

3. Significant accounting policies, judgments and estimation uncertainty (continued)

Impairment losses recognized in prior periods are assessed at each reporting date for any indicators that the impairment losses may no longer exist or may have decreased. In the event that an impairment loss reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, but only to the extent that the carrying amount does not exceed the amount that would have been determined had no impairment loss been recognized on the asset in prior periods. The amount of the reversal is recognized in net earnings.

(ii) Office equipment

Office equipment is recorded at cost and amortized using the declining balance method at rates of 20% to 30% per year. Leasehold improvements are recorded at cost and depreciated on a straight-line basis over the term of the related lease.

Borrowing costs

Borrowing costs attributable to the acquisition, construction or production of qualifying assets are added to the cost of those assets, until such time as the assets are substantially ready for their intended use. All other borrowing costs are recognized as interest expense in the statement of earnings and comprehensive income in the period in which they are incurred.

Share-based payments

The Company grants stock options to certain employees. Stock options vest over eighteen months (one third every six months) and expire after five years. Each tranche in an award is considered a separate award with its own vesting period and grant date fair value. Fair value of each tranche is measured at the date of grant using the Black-Scholes option pricing model. Compensation expense is recognized over the tranche's vesting period by increasing contributed surplus based on the number of awards expected to vest. The number of awards expected to vest is reviewed at least annually, with any impact being recognized immediately.

Provisions

Provisions for restructuring costs and legal claims, where applicable, are recognized in other liabilities when the Company has a present legal or constructive obligation as a result of past events. It is more likely than not that an outflow of resources will be required to settle the obligation, and the amount can be reliably estimated. Provisions are measured at management's best estimate of the expenditure required to settle the obligation at the end of the reporting period, and are discounted to present value where the effect is material. The Company performs evaluations to identify onerous contracts and, where applicable, records provisions for such contracts.

Decommissioning liabilities

Provisions are recognized for future decommissioning liabilities associated with the company's E&E assets and property, plant and equipment. The best estimate of the decommissioning and restoration provision is recorded on a discounted basis using a risk-free interest rate. The value of the obligation is added to the carrying amount of the associated E&E or property, plant and equipment asset and amortized over the useful life of the asset. The provision is accreted at the end of each period through charges to financing costs with actual expenditures charged against the accumulated obligation. Changes in the future cash flow estimates resulting from revisions to the estimated timing or amount of undiscounted cash flows or changes in the discount rate applied are recognized as a change in the decommissioning and restoration provision and related asset.

Exall Energy Corporation
Notes to the Consolidated Interim Financial Statements
For the three and nine months ended September 30, 2011 and 2010
(Unaudited)

(in thousands of Canadian Dollars)

3. Significant accounting policies, judgments and estimation uncertainty (continued)

Income tax

Income tax comprises current and deferred tax. Income tax is recognized in the statement of earnings and comprehensive income except to the extent that it relates to items recognized directly in equity, in which case the income tax is also recognized directly in equity.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted, at the end of the reporting period, and any adjustment to tax payable in respect of previous years.

In general, deferred tax is recognized in respect of temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. Deferred income tax is determined on a non-discounted basis using tax rates and laws that have been enacted or substantively enacted at the statement of financial position date and are expected to apply when the deferred tax asset or liability is settled. Deferred tax assets are recognized to the extent that it is probable that the assets can be recovered.

Deferred income tax is provided on temporary differences arising on investments in subsidiaries and associates, except, in the case of subsidiaries, where the timing of the reversal of the temporary difference is controlled by the company and it is probable that the temporary difference will not reverse in the foreseeable future.

Deferred income tax assets and liabilities are presented as non-current.

Tax on income in interim periods accrued using the tax rate that would be applicable to expected total annual earnings.

Revenue

Revenue associated with sales of petroleum and natural gas is recognized when the risks and rewards of ownership are transferred to the buyer and collection is reasonably assured. Other revenue is recognized at the time it is earned and the Company has a contractual right to receive the revenue.

Share capital

Common shares are classified as equity. Incremental costs directly attributable to the issuance of shares are recognized as a deduction from equity.

Earnings per share

Basic earnings per share ("EPS") is calculated by dividing the net earnings (loss) for the period by the weighted average number of common shares outstanding during the period.

Diluted EPS is calculated by adjusting the weighted average number of common shares outstanding for dilutive instruments. The number of shares included with respect to options, warrants and similar instruments is computed using the treasury stock method. The Company's potentially dilutive common shares comprise stock options granted to employees, and warrants.

Accounting standards issued but not yet applied

International Financial Reporting Standard 9, Financial Instruments ("IFRS 9")

IFRS 9 as issued reflects the first phase of the IASB's work on the replacement of IAS 39 and applies to classification and measurement of financial assets and liabilities as defined in IAS 39. This is effective for annual periods beginning on or after January 1, 2013. The adoption of IFRS 9 is not expected to have a significant impact on the consolidated financial statements.

Exall Energy Corporation
Notes to the Consolidated Interim Financial Statements
For the three and nine months ended September 30, 2011 and 2010
(Unaudited)

(in thousands of Canadian Dollars)

3. Significant accounting policies, judgments and estimation uncertainty (continued)

Significant accounting judgments and estimation uncertainties

Critical accounting estimates and judgments

The Company makes estimates and assumptions concerning the future that will, by definition, seldom equal actual results. The following are the estimates and judgments applied by management that most significantly affect the Company's financial statements. These estimates and judgments have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year.

(a) Critical accounting estimates

i. Carrying Value of Property, Plant and Equipment

Development and production assets within property, plant and equipment are depreciated, depleted and amortized using the unit-of-production method based on estimated proved reserves determined using estimated future prices and costs. There are a number of inherent uncertainties associated with estimating reserves. By their nature, these estimates of reserves, including the estimates of future prices and costs, and related future cash flows are subject to measurement uncertainty, and the impact on the consolidated financial statements of future periods could be material.

ii. Exploration and Evaluation Assets

The application of the Company's accounting policy for exploration and evaluation expenditures requires judgment in determining whether it is likely that future economic benefit exists when activities have not reached a stage where technical feasibility and commercial viability can be reasonably determined and when technical feasibility and commercial viability has been reached. Estimates and assumptions may change as new information becomes available.

iii. Decommissioning liabilities

Decommissioning costs are incurred when certain of the Company's tangible long-lived assets are retired. Assumptions, based on current economic factors which Management believes are reasonable, have been made to estimate the future liability. However, the actual cost of decommissioning is uncertain and cost estimates may change in response to numerous factors including changes in legal requirements, technological advances, inflation and the timing of expected decommissioning and restoration. The impact to net earnings over the remaining economic life of the assets could be significant due to the changes in cost estimates as new information becomes available. In addition, the Company determines the appropriate risk-free discount rate at the end of each period to determine the present value of the estimated future cash outflows required to settle the obligation and may change in response to numerous market factors.

iv. Impairment of Assets

The recoverable amounts of CGU's and individual assets have been determined as the higher of the CGU's or the asset's FVLCTS and its VIU. These calculations require the use of estimates and assumptions and are subject to changes as new information becomes available including information on future commodity prices, expected production volumes, quantity of reserves, discount rates as well as future development and operating costs. Changes in assumptions used in determining the recoverable amount could affect the carrying value of the related assets and CGUs.

Exall Energy Corporation
Notes to the Consolidated Interim Financial Statements
For the three and nine months ended September 30, 2011 and 2010
(Unaudited)

(in thousands of Canadian Dollars)

3. Significant accounting policies, judgments and estimation uncertainty (continued)

(b) Critical accounting judgments

- i. Determination of CGU's

CGU's are defined as the lowest grouping of integrated assets that generate identifiable cash inflows that are largely independent of the cash inflows of other assets or groups of assets. The allocation of assets into CGU's requires significant judgment and interpretations with respect to the integration between assets, the existence of active markets, external users, shared infrastructures, and the way in which management monitors the operations.

4. Transition to IFRS

The effect of the Company's transition to IFRS, described in note 2, is summarized in this note as follows:

- (i) Transition elections
- (ii) Reconciliation of equity and comprehensive income as previously reported under Canadian GAAP to IFRS
- (iii) Adjustments to the statement of cash flows
- (iv) Additional IFRS information for the year ended December 31, 2010.

(i) Transition elections

The company has applied the following transition exceptions and exemptions to full retrospective application of IFRS:

- a) Deemed cost of property, plant and equipment - The Company has elected to measure the cost of oil and natural gas properties at the book value previously reported under Canadian GAAP (refer to note 4(ii)(g) below)
- b) Business combinations – The Company has elected not to apply IFRS 3 "Business Combinations" retrospectively to business combinations that occurred prior to transition to IFRS on January 1, 2010
- c) Foreign currency - In accordance with IFRS 1, the Company elected to transfer all foreign currency translation differences in respect of foreign operations that arose prior to January 1, 2010 to Retained Earnings (see note 4(ii)(a) below).
- d) Share-based payments - The Company has elected to apply the share-based transaction exemption to equity instruments granted after November 7, 2002 but vested prior to transition to IFRS.

Exall Energy Corporation
Notes to the Consolidated Interim Financial Statements
For the three and nine months ended September 30, 2011 and 2010
(Unaudited)

(in thousands of Canadian Dollars)

4. Transition to IFRS (continued)

(ii) Reconciliation of equity and comprehensive income as previously reported under Canadian GAAP to IFRS

As at	Note	December 31, 2010			September 30, 2010			January 01, 2010		
		Cdn GAAP (\$)	Adj (\$)	IFRS (\$)	Cdn GAAP (\$) restated	Adj (\$)	IFRS (\$)	Cdn GAAP (\$)	Adj (\$)	IFRS (\$)
Assets										
Current										
Cash		24	-	24	39	-	39	21	-	21
Accounts receivable		5,699	-	5,699	5,365	-	5,365	2,578	-	2,578
Prepaid expenses		167	-	167	89	-	89	371	-	371
		5,890	-	5,890	5,493	-	5,493	2,970	-	2,970
Exploration and evaluation assets	g	-	1,386	1,386	-	1,397	1,397	-	743	743
Property, plant and equipment	a, g	40,552	441	40,993	35,068	(342)	34,726	25,284	(887)	24,397
		46,442	1,827	48,259	40,561	1,055	41,616	28,254	(144)	28,110
Liabilities										
Current										
Bank indebtedness		13,032	-	13,032	11,007	-	11,007	7,939	-	7,939
Accounts payable and accrued liabilities		7,032	-	7,032	4,978	-	4,978	3,595	-	3,595
		20,064	-	20,064	15,985	-	15,985	11,534	-	11,534
Deferred income tax liability	f	1,602	394	1,996	1,412	330	1,742	470	(19)	451
Decommissioning liabilities	c	822	255	1,077	845	154	999	744	14	758
		22,488	649	23,137	18,242	484	18,726	12,748	(5)	12,743
Shareholders' Equity										
Share capital	h	21,680	(127)	21,553	20,488	(127)	20,361	16,924	(127)	16,797
Warrants		243	-	243	406	-	406	11	-	11
Contributed surplus	i	1,572	185	1,757	1,428	170	1,598	1,167	-	1,167
Retained earnings (deficit)		459	1,110	1,569	(3)	528	525	(2,596)	(12)	(2,608)
		23,954	1,168	25,122	22,319	571	22,890	15,506	(139)	15,367
		46,442	1,827	48,259	40,561	1,055	41,616	28,254	(144)	28,110

Exall Energy Corporation
Notes to the Consolidated Interim Financial Statements
For the three and nine months ended September 30, 2011 and 2010
(Unaudited)

(in thousands of Canadian Dollars)

4. Transition to IFRS (continued)

	Year ended December 31, 2010			Three months ended September 30, 2010			Nine months ended September 30, 2010			
	Note 4 (iii) j	Cdn GAAP (\$)	Adj (\$)	IFRS (\$)	Cdn GAAP (\$) restated	Adj (\$)	IFRS (\$)	Cdn GAAP (\$) restated	Adj (\$)	IFRS (\$)
Revenue										
Oil and gas production		22,332	-	22,332	5,188	-	5,188	15,674	-	15,674
Royalties		(7,672)	-	(7,672)	(1,234)	-	(1,234)	(5,487)	-	(5,487)
		14,660	-	14,660	3,954	-	3,954	10,187	-	10,187
Expenses										
Oil and gas production		2,084	-	2,084	460	-	460	1,523	-	1,523
Depletion and amortization	b,d,e	6,499	(1,750)	4,749	1,433	(356)	1,077	4,271	(1,079)	3,192
Administration		2,086	(4)	2,082	387	-	387	1,322	-	1,322
Share based payments	i	504	185	689	162	90	252	360	170	530
Financing costs	e	539	29	568	161	6	167	414	20	434
Gains (losses) on foreign exchange translation		-	4	4	-	(1)	(1)	-	1	1
		11,712	(1,536)	10,176	2,603	(261)	2,342	7,890	(888)	7,002
Earnings before other income		2,948	1,536	4,484	1,351	261	1,612	2,297	888	3,185
Other income		1,313	-	1,313	891	-	891	1,313	-	1,313
Earnings before income taxes		4,261	1,536	5,797	2,242	261	2,503	3,610	888	4,498
Deferred income tax expense	f	1,206	414	1,620	627	130	757	1,017	348	1,365
Net earnings for the period		3,055	1,122	4,177	1,615	131	1,746	2,593	540	3,133
Deficit, beginning of year		(2,596)	(12)	(2,608)	(1,618)	397	(1,221)	(2,596)	(12)	(2,608)
Retained earnings (deficit), end of year		459	1,110	1,569	(3)	528	525	(3)	528	525

Explanatory notes

- (a) Under Canadian GAAP, the Company's U.S subsidiary was accounted for as an integrated foreign operation. Therefore, monetary items were translated at period end rates and non-monetary items were translated at historical rates with all foreign currency gains and losses recognized in profit or loss. Under IFRS, it was determined that the functional currency of the U.S. subsidiary is U.S. dollars. Accordingly, all assets and liabilities will be translated at the foreign exchange rates applicable at the statement of financial position date. As at January 1, 2010, translation of the U.S. subsidiary based on current exchange rates resulted in a decrease in property, plant & equipment of \$65. In accordance with the available IFRS 1 optional exemption, the Company elected to transfer the cumulative foreign currency translation balance, recognized as a separate component of equity, directly to retained earnings as at January 1, 2010.

Exall Energy Corporation
Notes to the Consolidated Interim Financial Statements
For the three and nine months ended September 30, 2011 and 2010
(Unaudited)

(in thousands of Canadian Dollars)

4. Transition to IFRS (continued)

- (b) An impairment loss of \$79 relating to certain of the Company's United States development and production assets was recognized in retained earnings at January 1, 2010 for development and production assets for which an impairment indicator existed at December 31, 2009. An impairment loss of \$82 relating to certain of the Company's United States development and production assets was recognized in depletion for the twelve months ended December 31, 2010 for development and production assets for which an impairment indicator existed at December 31, 2010 (see note 6). This impairment was not recognized under Canadian GAAP. These adjustments arose because under IFRS the recoverable amount used in recognizing and measuring impairment is the higher of the asset's fair value less costs to sell and its value in use. Under Canadian GAAP, the recoverable amount used to determine whether recognition of an impairment loss is required is the undiscounted future cash flows expected from its use and eventual disposition.
- (c) In accordance with IFRS transitional provisions, the Company revalued by \$14 certain of its asset retirement liabilities to their present value of \$758 as at January 1, 2010 (September 30, 2010 - \$154; December 31, 2010 - \$255). This adjustment arose because under IFRS the decommissioning liability is calculated using a risk free rate and risk adjusted cash flows. Under Canadian GAAP, the decommissioning liability is calculated using a credit adjusted risk free rate and risk adjusted cash flows.
- (d) Under IFRS, the Company recognizes depletion using proved plus probable reserves calculated using forecast pricing. Costs being depleted under IFRS include the future development costs associated with the depletable base. Under Canadian GAAP, the Company recognized depletion using proved reserves calculated using forecast pricing. Costs being depleted under Canadian GAAP include the future development costs associated with the depletable base. The depletion expense has decreased by \$356 and \$1,079 for the three and nine months ended September 30, 2010 and by \$1,750 for the twelve months ended December 31, 2010.
- (e) In accordance with IFRS transitional provisions, the Company elected to revalue by \$14 certain of its decommissioning liabilities to their fair value of \$758 as at January 1, 2010. This adjustment resulted in adjustments to the accretion base. Under IFRS, the Company calculated accretion using the risk free rate used to calculate the decommissioning liability. Under Canadian GAAP, the Company calculated accretion using the credit adjusted risk free rate used to calculate the decommissioning liability. As a result, the accretion expense has been decreased by \$6 and \$20 for the three and nine months ended September 30, 2010 and by \$29 for the twelve months ended December 31, 2010.
- (f) The carrying values of certain assets and liabilities were adjusted as noted in notes (a) – (e) above. These adjustments resulted in changes to the temporary differences that were recorded under Canadian GAAP. The adjustments as at January 1, 2010 resulted in a decrease to the deferred tax liability of \$19. The adjustments during 2010 resulted in an increase in deferred tax expense of \$130 and \$348 for the three and nine months ended September 30, 2010 and \$414 for the year ended December 31, 2010 with offsetting amounts recorded as increases to deferred tax liabilities.
- (g) Under IFRS, the Company chose to apply the IFRS 1 exemption in relation to oil and gas full cost accounting, allocation carrying costs to development and production ("D&P") assets based upon the proved plus probable reserve volumes before royalties. The Company has chosen to capitalize \$743 of exploration and evaluation ("E&E") costs under IFRS 6. Included in the E&E costs are the costs related to undeveloped land. As required under IFRS 6, properties in the E&E phase are presented separately from property, plant and equipment. This resulted in \$743 of expenditures previously classified as property, plant and equipment to be reclassified as E&E assets as at January 1, 2010 (\$1,397 at September 30, 2010 and \$1,386 as at December 31, 2010).
- (h) Prior to December 31, 2009, the Company issued flow-through shares. Under Canadian GAAP, a deferred tax liability was recorded when tax attributes were renounced with an offsetting debit to share capital. Under IFRS, flow-through shares are accounted for differently. On issuance, the premium on the flow-through share as compared to the price of a common share is recognized as a liability. The liability is reduced as the expenditures are incurred and tax attributes are renounced. The difference between the initial liability and the deferred tax liability created is recorded as a deferred tax expense. As a result of this difference, the Company recorded an adjustment as at January 1, 2010 to decrease share capital by \$127 with an offsetting increase in retained earnings.

Exall Energy Corporation
Notes to the Consolidated Interim Financial Statements
For the three and nine months ended September 30, 2011 and 2010
(Unaudited)

(in thousands of Canadian Dollars)

4. Transition to IFRS (continued)

- (i) Under Canadian GAAP, the Company recognized stock-based compensation expense on a straight line basis. Under IFRS, share based payments are required to be recognized based on a graded vesting schedule. There was no significant impact on the Company's statement of financial position as at January 1, 2010. For the three and nine month periods ended September 30, 2010, share based payments increased by \$90 and \$170 respectively. Share based payments for the year ended December 31, 2010 was increased by \$185, as a result of these differences, with an offset to contributed surplus.
- (j) Under Canadian GAAP, the Company previously filed its interim statements for the three and nine months ended September 30, 2010 reporting net purchased drilling royalty credits as a decrease to property, plant and equipment as opposed to recognizing it as other income on the statement of operations. The Canadian GAAP statements above as at and for the periods ended September 30, 2010 have been restated for the differences as follows. For the three and nine month periods ended September 30, 2010, other income increased by \$891 and \$1,313, depletion and amortization increased by \$46 and \$75 respectively, with an offsetting increase to property plant and equipment as of September 30, 2010 of \$1,238. Deferred tax expense increased by \$197 and \$281 for the three and nine month periods then ended, with an offsetting increase to deferred tax liability of \$281 as of September 30, 2010.

(iii) Adjustments to the statement of cash flows

The transition from Canadian GAAP to IFRS had no significant impact on cash flows generated by the Company.

(iv) Additional IFRS information for the year ended December 31, 2010

- (i) Compensation of key management

Key management includes the company's directors, members of the Executive Committee and the Head of Internal Audit. Compensation awarded to key management included:

	Year ended December 31, 2010
	\$
Salaries and short-term benefits	853
Share based payments	467
	<u>1,320</u>

- (ii) Employee benefits

	Year ended December 31, 2010
	\$
Salaries and short-term benefits	448
Share based payments	141
	<u>589</u>

Exall Energy Corporation
Notes to the Consolidated Interim Financial Statements
For the three and nine months ended September 30, 2011 and 2010
(Unaudited)

(in thousands of Canadian Dollars)

4. Transition to IFRS (continued)

(iii) Earnings per share

(a) Basic

Basic earnings per share are calculated by dividing the net income by the weighted average number of ordinary shares in issue during the year.

	Year ended December 31, 2010
Net earnings for the year (in thousands of Canadian Dollars)	4,177
Weighted average number of ordinary shares in issue	51,136,020
	<u>\$ 0.08</u>

(b) Diluted

Diluted earnings per share is calculated by adjusting the weighted average number of ordinary shares outstanding to assume conversion of all dilutive potential ordinary shares. The company has two categories of dilutive potential ordinary shares: warrants and stock options. For both, a calculation is done to determine the number of shares that could have been acquired at fair value (determined as the average market share price of the company's outstanding shares for the period), based on the monetary value of the subscription rights attached to the warrants and stock options. The number of shares calculated above is compared with the number of shares that would have been issued assuming exercise of the warrants and stock options.

	Year ended December 31, 2010
Net income for the year (in thousands of Canadian Dollars)	4,177
Weighted average number of ordinary shares in issue	51,136,020
Warrants	4,639,587
Stock Options	2,526,734
Weighted average number of ordinary shares for diluted earnings per share	<u>58,302,341</u>
	<u>\$0.07</u>

5. Accounts receivable

The Company's accounts receivable consist of the following:

	September 30, 2011	December 31, 2010	January 01, 2010
Joint venture operating and other receivables	\$ 4,398	\$ 3,087	\$ 1,308
Cash calls receivable	4,462	2,612	1,270
	<u>\$ 8,860</u>	<u>\$ 5,699</u>	<u>2,578</u>

Exall Energy Corporation
Notes to the Consolidated Interim Financial Statements
For the three and nine months ended September 30, 2011 and 2010
(Unaudited)

(in thousands of Canadian Dollars)

6. Property, plant and equipment

	Exploration and evaluation	Property, plant and equipment	Total
At January 01, 2010:			
Cost	\$ 743	\$ 24,397	\$ 25,140
Accumulated depletion, amortization	-	-	-
Net book value	<u>\$ 743</u>	<u>\$ 24,397</u>	<u>\$ 25,140</u>
Year ended December 31, 2010			
Opening net book value	\$ 743	\$ 24,397	\$ 25,140
Additions	679	21,291	21,970
Depletion, amortization for the period	(36)	(4,623)	(4,659)
Impairment	-	(82)	(82)
Closing net book value	<u>\$ 1,386</u>	<u>\$ 40,983</u>	<u>\$ 42,369</u>
Nine months ended September 30, 2011			
Opening net book value	\$ 1,386	\$ 40,983	\$ 42,369
Additions	6,339	28,808	35,147
Dispositions	(211)	-	(211)
Transfers	(399)	399	-
Depletion, depreciation and amortization	-	(4,981)	(4,981)
Impairment	-	-	-
Closing net book value	<u>\$ 7,115</u>	<u>\$ 65,209</u>	<u>\$ 72,324</u>

Costs excluded from depletion as of September 30, 2011 totaled \$7,115 (December 31, 2010 - \$1,422) as these costs are for unproved projects at period-end. As of September 30, 2011, future development costs of \$2,168 (December 31, 2010 - \$9,231) are included in the depletion calculation. General and administrative expenses of \$nil (December 31, 2010 - \$67) have been capitalized during the year.

As at September 30, 2011, there were no indicators of impairment. The Company's impairment tests, performed at December 31, 2010, resulted in \$82 additional depletion recorded. The future prices used by the Company in estimating cash flows were based on forecasts by an independent reserves evaluator, adjusted for the Company's quality and transportation differentials.

7. Bank indebtedness

As at September 30, 2011, the Company has a \$27,000 (December 31, 2010 - \$17,000) revolving demand credit facility with a Canadian chartered bank. The Company has drawn \$19,596 (December 31, 2010 - \$13,032) on the facility. The facility bears interest at the lender's base prime rate plus 1.50% (December 31, 2010 - 1.50%). The limit of the credit facility is subject to adjustments from time to time to reflect changes in the Company's asset base. There are no principal repayments required on the loan. The facility requires the Company to maintain certain financial ratios and other covenants and is collateralized by a general security agreement providing security interest over all present and after acquired personal property and a floating charge on all lands of the Company. At September 30, 2011, the Company was in compliance with all covenants on this facility.

On September 8, 2009, the Company arranged for a non-revolving bridge loan facility with an arm's length lender. The facility had a maturity of December 31, 2010, bear interest at 12.5% per annum with a credit limit of \$2,000. The facility, which was subordinate to the Company's bank debt, required the Company to maintain certain financial ratios and other covenants and was collateralized by a \$2 million fixed and floating debenture over all the assets of the Company. On September 2, 2010, the balance was fully repaid and discharged.

Exall Energy Corporation
Notes to the Consolidated Interim Financial Statements
For the three and nine months ended September 30, 2011 and 2010
(Unaudited)

(in thousands of Canadian Dollars)

8. Decommissioning liabilities

The following table presents the reconciliation of the beginning and ending aggregate carrying amounts of the obligations associated with the retirement of oil and gas properties:

	September 30, 2011	December 31, 2010
Balance, beginning of year	\$ 1,077	\$ 758
Liabilities incurred	165	290
Revisions to previously recorded liabilities	116	-
Accretion expense	25	29
Balance, end of period	\$ 1,383	\$ 1,077

Total estimated undiscounted asset retirement obligations amounted to \$1,467 at September 30, 2011 (December 31, 2010 - \$1,158). The total estimated asset retirement obligations have been discounted using a risk-free rate of 1.39% to 2.46% (December 31, 2010 – 3.56% to 4.20%), and an inflation rate of 2.0% (December 31, 2010 – 2.0%).

9. Share capital

Authorized:

Unlimited number of:
Common voting shares
Preferred non-voting shares

Issued:

As at, Common shares	September 30, 2011		December 31, 2010	
	Shares	Amount	Shares	Amount
Balance, beginning of year	53,873,707	\$ 21,553	45,921,227	\$ 16,797
Exercise of options	530,000	237	881,667	345
Fair value transfer for options exercised	-	84	-	99
Issuance of common shares (i)	5,750,000	11,500	5,774,851	3,754
Value assigned to warrants	-	-	-	(344)
Exercise of warrants	2,035,147	1,612	1,295,962	1,016
Fair value transfer for warrants exercised	-	232	-	172
Share issuance costs	-	(960)	-	(360)
Future income tax on share issue costs	-	243	-	74
Balance, end of period	62,188,854	\$ 34,501	53,873,707	\$ 21,553

Warrants

Balance, beginning of year	2,085,151	\$ 243	50,000	\$ 11
Issuance of warrants (i)	-	-	2,887,426	344
Issuance of broker warrants (i)	-	-	443,687	60
Exercise of warrants	(2,035,151)	(232)	(1,295,962)	(172)
Balance, end of period	50,000	\$ 11	2,085,151	\$ 243

Exall Energy Corporation
Notes to the Consolidated Interim Financial Statements
For the three and nine months ended September 30, 2011 and 2010
(Unaudited)

(in thousands of Canadian Dollars)

9. Share capital (continued)

- (i) In February 2011, the Company closed a private placement of 5,750,000 common shares at \$2.00 per common share for gross proceeds of \$11,500. Share issue costs incurred with respect to the private placement were \$960.

In March 2010, the Company closed a private placement of 5,774,851 units at \$0.65 per unit for gross proceeds of \$3,754, with each unit consisting of one common share and one-half of one share purchase warrant. Each whole share purchase warrant may be exercised to acquire one common share at a price of \$0.80 for one year. The value assigned to the warrants issued was \$344 which was valued using the following assumptions of volatility (77.6%), interest rate (1.19%), dividend yield (nil), expected life (9.5 months) with the fair value of warrants granted of \$0.15.

Share issue costs incurred with respect to the transaction was \$360 which included a non-cash component of \$60 being the value assigned to 295,791 units issued to the broker which are exercisable at \$0.675 for a period of twelve months. Each unit consists of one common share and one-half of one share purchase warrant, each whole share purchase warrant may be exercised to acquire one common share at a price of \$0.80 for one year.

Stock options

For the period ended September 30, 2011 the Company has granted 1,542,000 options at an exercise price of \$2.20 for a period of five years with options vesting 1/3 six months from the date of grant, 1/3 one year from the date of grant, and 1/3 eighteen months from the date of grant.

In 2010, the Company granted 250,000 options at an exercise price of \$0.63 for a period of five years with options vesting 1/3 six months from the date of grant, 1/3 one year from the date of grant, and 1/3 eighteen months from the date of grant. The Company also granted 692,500 options at an exercise price of \$1.25 for a period of five years with options vesting 1/3 every six months commencing six months after the date of grant.

As at September 30, 2011, the following options were outstanding:

	September 30, 2011		December 31, 2010	
	Stock options	Weighted average exercise price (\$)	Stock options	Weighted average exercise price (\$)
Outstanding, beginning of year	4,547,500	0.61	4,486,667	0.47
Granted	1,542,000	2.20	942,500	1.09
Exercised	(530,000)	0.45	(881,667)	0.39
Expired	-	-	-	-
Outstanding, end of period	5,559,500	1.07	4,547,500	0.61
Exercisable, end of period	3,694,998	0.59	3,910,832	0.53

Exall Energy Corporation
Notes to the Consolidated Interim Financial Statements
For the three and nine months ended September 30, 2011 and 2010
(Unaudited)

(in thousands of Canadian Dollars)

9. Share capital (continued)

Exercise price range	Options outstanding	Weighted average option price	Weighted average remaining contractual life (years)	Number of options currently exercisable	Weighted average price of options currently exercisable
0.00 – 0.45	1,985,000	0.40	1.57	1,985,000	0.40
0.46 – 0.90	1,340,000	0.65	2.00	1,340,000	0.65
0.91 – 1.35	692,500	1.25	3.59	461,665	1.25
1.36 – 1.80	0	0.00	0.00	0	0.00
1.81 – 2.25	1,542,000	2.20	4.70	0	0.00
	5,559,500	1.07	2.79	3,786,665	0.59

The compensation expense for options granted was determined based on the fair value of the stock options at the grant date estimated using the Black-Scholes option valuation model with the following weighted average assumptions:

	2011	2010
Volatility rate - %	95.8	106.3
Risk-free interest rate - %	2.10	2.48
Dividend yield rate - %	-	-
Expected life – years	4.0	4.0
Fair value of option granted - \$	0.99	0.78

Weighted average number of shares outstanding	Three months ended Sept 30,		Nine months ended Sept 30,	
	2011	2010	2011	2010
Basic	62,188,854	52,378,020	60,835,824	50,448,495
Diluted	64,430,341	55,277,348	63,077,311	52,903,719

For the periods ended September 30, 2011, nil (2010 – nil) options to purchase common shares that were outstanding during the respective periods were not included in the calculations of the weighted average number of shares outstanding as they were anti-dilutive.

10. Contributed surplus

A summary of contributed surplus as at September 30, 2011 and December 31, 2010 and the changes during the periods then ended are presented below:

	September 30, 2011	December 31, 2010
Balance, beginning of year	\$ 1,757	\$ 1,167
Fair value assigned to stock options granted (note 9)	771	689
Transfer to share capital for stock options exercised	(84)	(99)
Balance, end of period	\$ 2,444	\$ 1,757

Exall Energy Corporation
Notes to the Consolidated Interim Financial Statements
For the three and nine months ended September 30, 2011 and 2010
(Unaudited)

(in thousands of Canadian Dollars)

11. Financing costs

Financing costs are comprised of the interest payments made on debts outstanding and the accretion associated with the decommissioning liabilities;

	Three months ended Sept 30,		Nine months ended Sept 30,	
	2011	2010	2011	2010
Interest paid	\$ 149	\$ 161	\$ 350	\$ 414
Accretion	7	6	25	20
	\$ 156	\$ 167	\$ 375	\$ 434

12. Related party transactions

The Company had the following related party transactions that have been recorded at the exchange amounts for the three and nine months ended September 30, 2011 and 2010:

- A corporation owned by the President and Chief Executive Officer of the Company received gross overriding royalties for a well drilled in 2003. The royalties incurred for the three and nine months ended September 30, 2011 was \$1 and \$3 (2010 - \$1 and \$3), of which \$0.2 (December 31, 2010 - \$0.3) is included in accounts payable and accrued liabilities at period-end.
- A director of the Company is a partner in a partnership that provides engineering consulting services to the Company. In the three and nine months ended September 30, 2011, the Company incurred \$213 and \$508 (2010 - \$169 and \$364) for consulting services, of which \$85 (December 31, 2010 - \$28) is included in accounts payable and accrued liabilities at period-end.
- A director of the Company is a partner in a partnership that provides legal services to the Company. The legal fees incurred for the three and nine months ended September 30, 2011 was \$12 and \$202 (2010 - \$18 and \$115) of which \$2 (December 31, 2010 - \$13) is included in accounts payable and accrued liabilities at period-end.

13. Segmented disclosure

Industry information

Operating segments are defined as components of an enterprise about which separate financial information is available, that is evaluated regularly by management in deciding how to allocate resources and in assessing performance. All of the Company's operations are in the resource sector. The Company's oil and gas operations are centralized whereby management of the Company is responsible for business results and the everyday decision making. The Company's operations are therefore segmented on a geographic basis.

The segments' accounting policies are the same as those described in the summary of significant accounting policies except that general and administrative expenses, stock based compensation, interest expense, and other items are not allocated to the individual operating segments when determining profit or loss, but are rather attributed to the corporate head office.

Exall Energy Corporation
Notes to the Consolidated Interim Financial Statements
For the three and nine months ended September 30, 2011 and 2010
(Unaudited)

(in thousands of Canadian Dollars)

13. Segmented disclosure (continued)

Geographic information

As at	Canada		United States		Consolidated	
	Sept 30, 2011	Dec 31, 2010	Sept 30, 2011	Dec 31, 2010	Sept 30, 2011	Dec 31, 2010
Total assets	\$ 81,247	\$ 48,134	\$ 164	\$ 126	\$ 81,411	\$ 48,260
Exploration and evaluation assets	7,115	1,386	-	-	7,115	1,386
Development and production assets	65,130	40,883	79	100	65,209	40,983
For the nine months ended Sept 30,	2011	2010	2011	2010	2011	2010
Capital expenditures	34,867	13,955	-	-	34,867	13,955
Oil and gas production sales	22,812	15,591	74	83	22,886	15,674
Depletion and amortization	4,962	3,153	19	39	4,981	3,192
Deferred income tax expense	1,720	1,365	-	-	1,720	1,365

14. Financial risk management

The Company is exposed to financial risks due to the nature of its business and the financial assets and liabilities it holds. The following discussion reviews material financial risks, quantifies the associated exposures, and explains how these risks, and the Company's capital, are managed.

The Company's financial instruments include cash, accounts receivable, bank indebtedness and accounts payable and accrued liabilities. The carrying amounts of these financial instruments, reported on the Company's consolidated statements of financial position, approximate their fair values due to their short-term nature.

a) Market risk

Changes in commodity prices, interest rates and foreign currency exchange rates can have an impact on the Company's earnings and value of financial assets and liabilities.

Commodity prices – The Company is exposed to commodity price risk due to the nature of its business. Oil and natural gas prices are impacted by global supply and demand, as well as political and other forces. Prices continue to be volatile and can undergo significant changes in relatively short time periods. The Company may enter into derivative commodity price contracts in order to manage its commodity price risk but has not done so to date.

The Company has never entered into forward commodity price contracts.

Interest rates – The Company is exposed to interest rate risk on its floating rate bank debt (refer to note 7 for bank indebtedness details). The Company may enter into derivative interest rate swap contracts in order to manage interest rate risk, but has not done so to date.

Foreign currency exchange rates – The reporting currency of the Company is Canadian dollars. A small portion of the Company's operations are in the United States and as a result, the Company is exposed to foreign currency exchange rate risk on some of its activities. A small percentage of the Company's oil, natural gas and liquids revenues are denominated in U.S. dollars. Similarly, a small percentage of operating and capital expenditures are incurred in U.S. dollars. Bank debt is denominated in Canadian dollars.

The Company may enter into derivative foreign currency contracts in order to manage foreign currency exchange rate risk, but has not done so to date as the risk is nominal.

Exall Energy Corporation
Notes to the Consolidated Interim Financial Statements
For the three and nine months ended September 30, 2011 and 2010
(Unaudited)

(in thousands of Canadian Dollars)

14. Financial risk management (continued)

b) Liquidity risk

The Company manages its risk of not meeting its financial obligations through management of its capital structure, annual budgeting of its revenues, expenditures and cash flows, and maintaining unused credit facilities where possible. The Company expects its 2011 operating cash flow to exceed budgeted non-discretionary expenditures, providing added liquidity. As at September 30, 2011, the Company's credit facilities had undrawn capacity of \$7,404 (December 31, 2010 - \$3,968).

Accounts payable arise in the normal course of business, and all amounts are due within three months or less of the statement of financial position date. Bank indebtedness is repayable on demand however the bank is not expected to demand payment on the facility other than monthly interest payments as further disclosed in note 7 and is subject to an annual review on May 31 of each year with interim reviews as required.

The Company believes it has adequate cash flows in conjunction with financings conducted in 2011 to discharge certain financial obligations.

c) Credit risk

The Company is exposed to credit risk in respect to its cash and cash equivalents, and accounts receivable.

Cash and cash equivalents are held in operating accounts with a highly rated Canadian bank and therefore the Company considers these assets to have negligible credit risk.

The Company's accounts receivable are primarily with joint venture partners and purchasers of its production. Production is sold to a small number of highly rated oil and gas companies. It is the Company's policy to transact with only credit worthy counterparties. The Company has not experienced any collection problems with its counterparties and does not have any overdue receivable amounts as at September 30, 2011. Of significant individual accounts receivable as at September 30, 2011, approximately 87 percent was owed from the top five customers (December 31, 2010 - 90 percent was owed from the top five customers).

The carrying amount of cash and cash equivalents and accounts receivable represents the Company's maximum credit exposure. The Company does not have an allowance for doubtful accounts, and did not write-off any receivables in the period ended September 30, 2011.

d) Capital management

The Company defines its capital as shareholder's equity and bank debt. The Company's objective is to maintain a strong capital position in order to execute its business plan and maximize value to shareholders. The Company actively manages its credit facilities to ensure the available amounts are adequate for business requirements and the rates charged are competitive. Availability of capital is a key to future success and as such, the Company strives to maintain strong relationships with the capital investment community. Methods employed to adjust the Company's capital structure could include any, all, or a combination of the following activities:

- Issue new shares through a public offering or private placement;
- Issue equity linked or convertible debt;
- Raise fixed or floating rate debt; and
- Refinance existing bank debt facilities to change amounts or terms.

The Company is subject to certain bank covenants as discussed in note 7 of which the Company is in compliance with all covenants on its loan facility as at September 30, 2011. The Company is also restricted from declaring any dividends. In addition, no changes in the approach to capital management have occurred in the period ended September 30, 2011.

Exall Energy Corporation
Notes to the Consolidated Interim Financial Statements
For the three and nine months ended September 30, 2011 and 2010
(Unaudited)

(in thousands of Canadian Dollars)

15. Supplemental cash flow information

Changes in non-cash working capital:

	Three month period ended September 30,		Nine month period ended September 30,	
	2011	2010	2011	2010
Accounts receivable	\$ (4,255)	\$ (1,923)	\$ (3,161)	\$ (2,787)
Prepaid expenses	32	7	8	282
Accounts payable and accrued liabilities	9,423	86	6,708	1,383
Changes in non-cash working capital	\$ 5,200	\$ (1,830)	\$ 3,555	\$ (1,122)
Relating to:				
Operating activities	\$ (582)	\$ (424)	\$ (931)	\$ (1,524)
Investing activities	5,782	(1,406)	4,486	402

16. Other income

During Fiscal 2010 the Company acquired royalty credits from third parties. The difference between the value of those credits and the amount paid is included in Other Income.

17. Commitments

The Company is committed to a lease agreement for office premises terminating on August 31, 2013. The estimated obligations for the term of the lease including operating costs are summarized in the following table:

2011	\$	48
2012		190
2013		126
Total	\$	364

CORPORATE INFORMATION

Corporate Office

Suite 400, 715 – 5th Avenue SW
Calgary, Alberta
T2P 2X6
Telephone: (403) 237-7820
Fax: (403) 262-4723

Officers

Stephen G. Roman, B.A.
Executive Chairman

Frank S. Rebeyka, P.Geol., B.SC. Adv.
Vice Chairman

Roger N. Dueck, B. Eng., P.Geol.
President & CEO

Warren F.E. Coles, MBA
Vice President Finance & CFO

Glen Kerr, B.Eng., P.Eng.
Vice President Operations

Board of Directors

Stephen G. Roman, Chairman ⁽¹⁾

Frank S. Rebeyka, Vice-Chairman ^{(3) (4)}

Roger N. Dueck ^{(3) (4)}

Wayne Egan ⁽¹⁾

Bernard A. Lang ^{(1) (2) (4)}

D. Allan Menzies ^{(2) (3)}

Roderick Phipps ^{(1) (2) (3) (4)}

(1) Compensation Committee

(2) Audit Committee

(3) Reserves Committee

(4) Health, Safety & Environmental Committee

Website:

www.exall.com

Stock Exchange: Trading Symbol

TSX: EE

Auditors

PricewaterhouseCoopers LLP
3100, 111 – 5th Avenue SW
Calgary, Alberta
T2P 5L3

Bank

Alberta Treasury Branch
600, 444 – 7th Avenue SW
Calgary, Alberta
T2P 0X8

Evaluation Engineers

AJM Petroleum Consultants
600, 425 – 1 Street SW
Calgary, Alberta
T2P 3L8

Legal Counsel

WeirFoulds LLP
1600, 130 King Street West
Toronto, Ontario
M5X 1J5

MacLeod Dixon LLP
3700, 400 – 3rd Avenue SW
Calgary, Alberta
T2P 4H2

Transfer Agent

Equity Financial Trust Company
200, University Avenue, Suite 400
Toronto, Ontario
M5H 4H1

Issued and Outstanding Common Shares

62,188,854

ABBREVIATIONS

Oil and Natural Gas Liquids

BBL	barrel
BBLs	barrels
MBBLS	thousand barrels
MMBLS	million barrels
MSTB	thousand stock tank barrels
BPD	barrels per day
NGLs	natural gas liquids
STB	standard tank barrels

Natural Gas

MCF	thousand cubic feet
MMCF	million cubic feet
MCFD	thousand cubic feet per day
MMCFD	million cubic feet per day
MMBTU	million British Thermal Units
BCF	billion cubic feet
GJ	gigajoule
MM	million

Other

AECO	Refers to the AECO Hub, a natural gas storage facility located in Suffield and Countess, Alberta.
AECO-C	Spot gas prices for Alberta natural gas, one of North America's price setting benchmarks.
API	American Petroleum institute
°API	An indication of the specific gravity of crude oil measured on the API gravity scale.
ARP	Alberta reference price for natural gas in Alberta is a monthly weighted average field price of all Alberta gas sales as determined by the Alberta Department of Energy, and is used for Royalty purposes.
BOE	Barrel of oil equivalent of natural gas and crude oil on the basis of 1 BOE for 6 MCF of natural gas (this conversion factor is an industry accepted norm and is not based on either energy content or current prices).
Edmonton Par	Edmonton par is used for the basis price for 40 degree API gravity light sweet crude at Edmonton, Alberta.
BOED	barrel of oil equivalent per day
GCA	gas cost allowance
m ³	cubic meters
MBOE	thousand barrels of oil equivalent
MMBOE	million barrels of oil equivalent
NYMEX	The New York Mercantile Exchange. The NYMEX natural gas futures contract is widely used as an international benchmark price, including in Canada. The delivery point is at the Henry Hub in Louisiana.
\$000s	thousands of dollars
WTI	West Texas Intermediate. The WTI, also known as Texas Light Sweet, is a type of crude oil used as a benchmark in oil pricing with its hub at Cushing, Texas

Company Definition

Exall Energy Corporation is referred to as "Exall", or the "Company" throughout the MD&A

Volume Reporting

Barrel of oil equivalent (BOE) figures for the periods presented throughout this document are expressed using a conversion rate of six thousand cubic feet of natural gas to one barrel of crude oil (6:1). BOEs may be misleading, particularly if used in isolation. The forgoing conversion ratio is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead.