



To Our Shareholders

During the first quarter of 2011, Painted Pony Petroleum Ltd. continued to enjoy financial and operational success. Quarterly results include the following:

- grew daily production to average 4,027 boe per day (weighted 50% oil and liquids and 50% gas) up 73% from first quarter 2010 and 17% from fourth quarter 2010;
- generated funds flow from operations of \$12.1 million (\$0.21 per diluted share);
- raised \$80.0 million in a bought deal financing;
- exited the first quarter of 2011 with positive working capital of \$64.1 million and no debt with unutilized, increased credit facilities of \$75 million;
- realized first quarter 2011 field netbacks of \$59.08 per bbl for oil, on sales prices averaging \$87.08 per bbl; and,
- added land in both Saskatchewan and British Columbia, bringing total land holdings to over 200,000 net acres.

OPERATIONAL ACTIVITIES

The Company conducted an active capital program during the first quarter of 2011, which included the drilling of 12 (8.1 net) wells.

BRITISH COLUMBIA

Painted Pony continues to focus on developing and expanding its liquid rich Montney gas project at Blair-Cameron in northeast British Columbia. Given recent operational successes, the Company has moved the Montney gas project beyond piloting into delineation and development. Three wells (1.5 net) on a single pad were drilled for Montney, each one targeting a different layer (Upper, Middle and Lower) of the Montney. All three (1.5 net) were successfully completed and put on production in the second quarter of 2011. The Montney project in northeastern British Columbia continues to perform above expectations. With several successful wells producing from each of the three primary targets within the Montney, Painted Pony plans to move to further delineation and development of this world-class resource.

Painted Pony also continues to actively evaluate the Buckinghorse shale gas potential. The first stimulations of two (1.0 net) wells drilled in late 2010, in this 800 meter thick resource, are currently planned for early in the fourth quarter of 2011.

SASKATCHEWAN

In Saskatchewan 9 (6.6 net) wells were drilled during the first quarter of 2011 targeting light oil. The Company enjoyed drilling success at Midale (Bakken), Alameda (Mississippian), and Ingoldsby (Mississippian). Further completions of the first quarter drilled wells have been put on hold by an extended period of unusually wet weather and associated flooding. This unusually long spring breakup has persisted since mid-March. The affected area covers a wide swath of industry activity and incorporates most of the Company's working interest

oil properties. As with most operators in the area, the flooding conditions have significantly impacted Painted Pony's production operations, drilling program and work-over projects. To date, the Company estimates these adverse conditions have delayed the drilling schedule by more than 60 rig days in comparison to prior years.

Most recently, several towns in the Weyburn/Midale district experienced severe flooding and a state of emergency was declared by the province of Saskatchewan. Painted Pony continues to monitor the Saskatchewan situation, however at this time it is difficult to estimate when normal oilfield operations will resume. Accordingly, certain production volumes and new production additions may continue to be curtailed or delayed. This has been a major problem for all oil producers in the area and also for local farmers who have been unable to plant crops. The Energy Minister of Saskatchewan recently stated that this is a once in 500 years event.

PRODUCTION

Daily production grew to average 4,027 boe per day in the first quarter of 2011, up 17% over the fourth quarter of 2010, and 73% over the first quarter of 2010. Daily Saskatchewan sales in the first quarter averaged 2,082 boe per day (weighted 95% oil and liquids) and sales from British Columbia averaged 1,945 boe per day (weighted 99% gas).

Production in the second quarter has been adversely affected by flooding in Saskatchewan, and gas plant disruptions in both Saskatchewan and British Columbia have resulted in the Company's production being reduced by an estimated 500 boe/d. The Company expects to return to normal production growth in the third quarter of 2011.

LAND

At March 31, 2011, the Company held 200,521 net acres of land, consisting of 76,049 net acres (119 net sections) in Saskatchewan and 124,472 net acres (194 net sections) in British Columbia. To date during the second quarter of 2011, the Company has completed an asset acquisition and continues to participate in Crown land sales that complement existing core areas. The Company now has over 81,000 net acres (127 net sections) of Montney rights in northeastern British Columbia. A number of joint ventures have been announced in recent months in the "Northern Montney Trend" and land prices continue to escalate offsetting Painted Pony lands, despite suppressed gas prices.

FINANCIAL RESOURCES

Painted Pony's focus on conservative fiscal management continues. In February 2011, the Company issued 7,620,000 Class A shares at \$10.50 per share, raising gross proceeds of \$80.0 million. At March 31, 2011, Painted Pony had a positive working capital position of \$64.1 million and no debt. In March 2011, the demand revolving operating credit facility was increased to \$75.0 million, replacing the previous \$65.0 million demand revolving credit facility. The facility is subject to review on or before September 30, 2011.

IFRS

Painted Pony's conversion to IFRS, including the redetermination of 2010 operations under IFRS in comparison to GAAP was completed during the second quarter of 2011. The net impact on funds flow from operations was minor (March 2011: \$45,000 and March 2010: \$10,000), notwithstanding numerous differences in components of after tax net income.

EXECUTIVE TEAM

Painted Pony is pleased to welcome James D. (Jim) Reimer, P.Geol. as Vice President, Exploration. Mr. Reimer brings more than 30 years experience to Painted Pony, including 12 years in executive exploration roles.

On Behalf of the Board of Directors, we thank you for your support.

Patrick R. Ward
President and Chief Executive Officer
June 24, 2011

Financial and Operational Highlights

(unaudited)

Three months ended March 31,	2011	2010
Financial (000's except per share)		
Petroleum and natural gas revenue (before royalties)	\$ 19,315	\$ 14,146
Funds flow from operations ⁽¹⁾	\$ 12,098	\$ 9,156
Per share – basic ⁽²⁾	\$ 0.22	\$ 0.21
Per share – diluted ⁽³⁾	\$ 0.21	\$ 0.20
Cash flow from operating activities	\$ 11,555	\$ 9,221
Net income	\$ 2,144	\$ 1,546
Per share – basic ⁽²⁾	\$ 0.04	\$ 0.04
Per share – diluted ⁽³⁾	\$ 0.04	\$ 0.03
Capital expenditures ⁽⁴⁾	\$ 25,085	\$ 35,482
Net working capital	\$ 64,100	\$ 15,639
Total assets	\$ 330,156	\$ 186,881
Shares outstanding		
Class A	59,186,073	44,136,700
Class B	1,173,600	1,173,600
Operational		
Daily sales volumes		
Oil (bbls per day)	1,811	1,722
Condensate (bbls per day)	54	27
NGL's (bbls per day)	141	19
Gas (mcf per day)	12,126	3,322
Total (boe per day)	4,027	2,322
Realized prices		
Oil (per bbl)	\$ 87.08	\$ 79.58
Gas (per mcf)	\$ 3.77	\$ 5.21
Field operating netbacks		
Oil (per bbl)	\$ 59.08	\$ 58.71
Gas & associated liquids (per boe)	\$ 17.03	\$ 13.45
Company combined (per boe)	\$ 35.95	\$ 47.02

1. This table contains the term "funds flow from operations", which should not be considered an alternative to, or more meaningful than "cash flow from operating activities" as determined in accordance with International Financial Reporting Standards ("IFRS") as an indicator of the Company's performance. Funds flow from operations and funds flow from operations per share (basic and diluted) does not have any standardized meaning prescribed by IFRS and may not be comparable with the calculation of similar measures for other entities. Management uses funds flow from operations to analyze operating performance and leverage and considers funds flow from operations to be a key measure as it demonstrates the Company's ability to generate the cash necessary to fund future capital investment. The reconciliation between funds flow from operations and cash flow from operating activities can be found in "Management's Discussion and Analysis". Funds flow from operations per share is calculated using the basic and diluted weighted average number of shares for the period, and after the deemed conversion of the Class B shares to Class A shares, consistent with the calculations of earnings per share.
2. Basic per share information is calculated on the basis of the weighted average number of Class A shares outstanding in the period.
3. Diluted per share information reflects the potential dilution effect of options and the convertible Class B shares, each of which may be anti-dilutive. Net income is adjusted for the amount of finance expense applicable to the Class B shares for the period. The conversion of Class B shares into Class A shares, if dilutive, is computed by dividing \$10 by the greater of \$1.00 and the Current Trading Price, defined as the weighted average trading price of the Class A shares for the last 30 consecutive trading days.
4. Including decommissioning obligations and share-based payments.

Management's Discussion and Analysis

The following Management's Discussion and Analysis ("MD&A") of the consolidated financial results as provided by the management of Painted Pony Petroleum Ltd. ("Painted Pony" or the "Company") should be read in conjunction with the unaudited condensed interim consolidated financial statements and related notes for the three months ended March 31, 2011 and the consolidated financial statements and related notes for the year ended December 31, 2010. This commentary is dated June 24, 2011.

The condensed interim consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS"). The Company adopted IFRS on January 1, 2011. Previously Painted Pony prepared its interim consolidated financial statements in accordance with Canadian Generally Accepted Accounting Principles ("Canadian GAAP"). The financial data presented is in accordance with IFRS in Canadian dollars, except where indicated otherwise. These documents and additional information about Painted Pony, including the Annual Information Form, are available on SEDAR at www.sedar.com.

Description of Company

Painted Pony is a Calgary-based exploration and development company focused on oil in southeast Saskatchewan and natural gas in northeast British Columbia. The Class A and Class B shares of Painted Pony trade on the TSX Venture Exchange under the symbols "PPY.A" and "PPY.B", respectively.

Painted Pony commenced commercial operations on April 3, 2007 upon completion of a financial reorganization as part of an overall restructuring of the Company. On May 23, 2007, subsequent to completion of an initial public offering on May 17, 2007, the Class A shares and Class B shares of Painted Pony Petroleum Ltd. began trading on the TSX Venture Exchange. Painted Pony then commenced an active exploration program.

Non-IFRS Measures

Management's Discussion and Analysis contains the term "funds flow from operations", which should not be considered an alternative to, or more meaningful than cash flow from operating activities as determined in accordance with IFRS as an indicator of the Company's performance. Funds flow from operations and funds flow from operations per share (basic and diluted) do not have any standardized meaning prescribed by IFRS and may not be comparable with the calculation of similar measures for other entities. Management uses funds flow from operations to analyze operating performance and considers funds flow from operations to be a key measure as it demonstrates the Company's ability to generate the cash necessary to fund future capital investment and to repay debt. Funds flow from operations per share is calculated using the basic and diluted weighted average number of shares for the period, and after deemed conversion of Class B shares into Class A shares, consistent with the calculations of earnings per share. The Company reconciles funds flow from operations to cash flow from operating activities, which is the most directly comparable measure calculated in accordance with IFRS, as follows:

(000s)

Three months ended March 31,	2011	2010
Cash flow from operating activities	\$ 11,555	\$ 9,221
Changes in non-cash working capital	439	(65)
Decommissioning expenditures	104	-
Funds flow from operations	\$ 12,098	\$ 9,156

Management's Discussion and Analysis also contains other industry benchmarks and terms, such as net working capital position (calculated as current assets less current liabilities) and operating netbacks (calculated on a per unit basis as oil, gas and natural gas liquids revenues less royalties and transportation and operating costs), which are not recognized measures under IFRS. Management believes these measures are useful supplemental measures of, firstly, the total net position of current assets and current liabilities the Company has and, secondly, the profitability relative to commodity prices. Readers are cautioned, however, that these measures should not be construed as alternatives to other terms such as current and long-term debt or net income determined in accordance with IFRS as measures of performance. Painted Pony's method of calculating these measures may differ from other companies, and accordingly, may not be comparable to similar measures used by other companies.

Forward-looking Information

This MD&A contains forward-looking statements relating to future events. Forward-looking information is information that does not relate strictly to historical or current facts, and can be identified by words such as "anticipate", "continue", "estimate", "expect", "forecast", "may", "will", "project", "should", "believe", "intend", or similar expressions. These statements represent management's reasonable projections, expectations, and estimates as of the date of this document, but undue reliance should not be placed upon them as they are derived from numerous assumptions. These assumptions are subject to known and unknown risks and uncertainties, including the business risks discussed in this MD&A, which may cause actual performance and financial results to differ materially from any projections of future performance or results expressed or implied by such forward-looking statements.

The forward looking information in this document is subject to significant risks and uncertainties and is based on a number of material factors and assumptions which may prove to be incorrect; including but not limited to the following:

- volumes in 2011 will be more weighted to gas than in 2010 as success from operations targeting the Montney formation in British Columbia could add incremental volumes;
- the average oil price in 2011 will be approximately 3% less than the Edmonton par reference price and the natural gas price received will be approximately the AECO daily spot price;
- overall royalties in 2011 will approximate 13% of total revenues, assuming similar commodity prices to first quarter 2011;
- expected economic benefits from the multi-well oil battery facility and water disposal facility in the Huntoon area include reducing production disruptions caused by adverse weather, cost-effective water handling and disposal, reducing trucking costs and eliminating the capital investment of oil storage tanks at each well location;
- sales of solution gas and associated liquids from the Huntoon-Midale area are expected to increase netbacks during 2011;
- weather related issues are expected to result in incremental costs in Saskatchewan during the second and third quarters of 2011;
- net general and administrative costs will be reflective of capital expenditure levels in the balance of 2011;
- as gross Saskatchewan sales revenues fluctuate in 2011, the Saskatchewan resource surcharge is expected to vary accordingly;
- wells drilled in Saskatchewan in the first quarter of 2011 are expected to be completed by the end of the third quarter;
- certain leases that are approaching expiry in British Columbia will be continued through execution of a work program;
- available credit facilities may be utilized on a periodic basis in 2011;

- the risk of accounts receivables becoming uncollectible is mitigated by the financial position of the applicable entities; and
- the Company has sufficient financial resources with which to conduct its capital program; further, this is subject to the additional assumption that the drilling rigs, field service providers, completion and tie-in equipment will be available as required and that the costs of securing such services and equipment will not materially exceed expectations.

While we anticipate that subsequent events and developments may cause our views to change, we do not have an intention to update this forward-looking information, except as required by applicable securities laws. This forward-looking information represents our views as of the date of this document and such information should not be relied upon as representing our views as of any date subsequent to the date of this document. We have attempted to identify important factors that could cause actual results, performance or achievements to vary from those current expectations or estimates expressed or implied by the forward-looking information contained here-in. However, there may be other factors that cause results, performance or achievements not to be as expected or estimated and that could cause actual results, performance or achievements to differ materially from current expectations. Other risks and uncertainties include, but are not limited to, the following:

- normal risks common to the oil and natural gas industry, including various operational risks in the carrying out of exploration, development and production operations;
- risks and uncertainty of oil and gas geological deposits;
- revisions, amendments or changes to capital expenditure plans including exploration, development and exploitation projects;
- risks as to the availability and pricing of appropriate financing alternatives on acceptable terms;
- potential changes in income tax regulations, governmental policies, rules, practices or approval process changes, or delays, or enhancements; and
- the Company's ability to attract and retain qualified professional employees.

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

The reader is further cautioned that the preparation of consolidated financial statements in accordance with IFRS requires management to make certain judgments and estimates that affect the reported amounts of assets, liabilities, revenues and expenses. Estimating reserves is also critical to several accounting estimates and requires judgments and decisions based upon available geological, geophysical, engineering and economic data. These estimates may change, having either a negative or positive effect on net earnings as further information becomes available, and as the economic environment changes.

There can be no assurance that forward-looking information will prove to be accurate, as results and future events could differ materially from those expected or estimated in such statements. Accordingly, readers should not place undue reliance on forward-looking information. From time to time, Painted Pony's management makes estimates and forms opinions on which the forward-looking statements are based. The Company assumes no obligation to update forward-looking statements if circumstances, management's estimates, or opinions change, unless prescribed by securities laws.

BOE Presentation

Barrels of oil equivalent ("boe") may be misleading, particularly if used in isolation. A boe conversion ratio of six thousand cubic feet of gas ("mcf") to one barrel of oil ("bbl") (6 mcf:1 bbl) is used as an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead. All boe conversions in this report are derived by converting natural gas to oil in the ratio of six mcf of gas to one barrel of oil. Readers should be aware that historical results are not necessarily indicative of future performance.

Net Income and Funds Flow from Operations

Painted Pony generated funds flow from operations of \$12.1 million for the three months ended March 31, 2011, compared to \$9.2 million for the quarter ended March 31, 2010. On a basic per share basis, funds flow from operations for the quarters ended March 31, 2011 and 2010 were \$0.22 and \$0.21, respectively, and on a diluted basis, funds flow from operations was \$0.21 and \$0.20 per share, respectively, for the two quarters.

Cash flow from operating activities was \$11.6 million for the three months ended March 31, 2011, compared to \$9.2 million for the quarter ended March 31, 2010.

Painted Pony produced net income of \$2.1 million in the quarter ended March 31, 2011, compared to \$1.5 million earned during the three months ended March 31, 2010. Basic and diluted income per share are \$0.04 for the three months ended March 31, 2011, compared to basic and diluted income per share of \$0.04 and \$0.03, respectively for the three months ended March 31, 2010.

Sales Volumes

During the three months ended March 31, 2011, Painted Pony's sales volumes increased 73%, to average 4,027 boe per day compared to 2,322 boe per day for the quarter ended March 31, 2010. The increase is primarily from incremental gas sales in British Columbia. In the first quarter of 2011, 52% of total volumes were from Saskatchewan, compared to 75% in the first quarter of 2010.

Sales volumes in the first quarter of 2011 were weighted 50% towards gas compared to 24% in the comparable 2010 period, reflecting the focus of the capital program towards British Columbia gas producing assets. All of Painted Pony's light oil sales originate from Saskatchewan operations while 88% of the sales of gas, condensate and NGL's are from British Columbia.

Average Daily Sales Volumes

Three months ended March 31,	2011	2010
Oil (bbls/d)	1,811	1,722
Condensate (bbls/d)	54	27
NGL's (bbls/d)	141	19
Gas (mcf/d)	12,126	3,322
Total (boe/d)	4,027	2,322

Daily oil sales volumes in the first quarter of 2011 grew by 5% compared to the same period in 2010 and gas sales increased by 265% over the same period in 2010, reflecting the significant success of the Montney drilling program.

Saskatchewan operations and production volumes have been negatively impacted during the second quarter of 2011 due to an unusually wet and extended spring break-up. Company oil production has been temporarily shut-in due to road bans and flooding; field operations have been delayed and sales of gas and liquids from the Huntoon area have ceased due to non-operated plant scheduled and unscheduled repairs and maintenance. Normal activity has not yet resumed. In British Columbia, gas sales from the Cameron/Kobes area is expected to be temporarily shut-in for 21 days during the second quarter of 2011 for the scheduled McMahon gas processing plant turn-around. The Company anticipates sales volumes in 2011 to be increasingly weighted towards gas sales, as success from operations targeting the Montney formation in British Columbia add incremental volumes.*

**This paragraph contains forward-looking information. Please refer to "Forward-looking Information" and "Business Risks, Uncertainties and Forward-looking Information" for a discussion of the risks and uncertainties related to such information.*

Revenues

Petroleum and natural gas sales increased 37% to \$19.3 million in the quarter ending March 31, 2011, compared to \$14.1 million for the three months ended March 31, 2010. In the first quarter of 2011, oil sales revenues were 74% of total sales dollars compared to 87% in the first quarter of 2010, while oil volumes were 45% and 74% in the three months ended March 31, 2011 and 2010, respectively. In both periods, oil sales contributed disproportionately more to total sales dollars compared to volumes, reflecting the relative strength of crude oil prices compared to gas prices.

Sales by Product (000s)

Three months ended March 31,	2011	2010
Oil	\$ 14,197	\$ 12,336
Gas	4,109	1,556
Condensate	397	187
NGL's	612	67
Total	\$ 19,315	\$ 14,146

Crude oil revenue in the three months ended March 31, 2011 was \$14.2 million compared to \$12.3 million during the quarter ended March 31, 2010. Oil revenues increased 15% from the first quarter of 2010 to the first quarter of 2011. Oil prices averaged \$87.08 per bbl in the first quarter of 2011 compared to \$79.58 per bbl during the same 2010 quarter. Painted Pony received an average crude oil price approximately the same as the Edmonton light reference price in the first quarters of both 2011 and 2010. Painted Pony's light oil is a premium light crude with low sulfur content.

Revenue from gas, condensate and NGL sales totaled \$5.1 million during the three months ended March 31, 2011, compared to \$1.8 million received during the three months ended March 31, 2010. The Company received an average gas price of \$3.77 per mcf in the quarter ended March 31, 2011, a price comparable to the AECO daily spot average gas reference price of \$3.79 per mcf. In the first quarter of 2010, the Company received an average gas price of \$5.21 per mcf. Gas prices have been very weak in North America during the first quarter of 2011.

To date, Painted Pony has not undertaken any risk management contracts or commodity price contracts.

The Company generally expects in 2011 to receive an average oil price approximately 3% less than the Edmonton par reference price, reflecting the prices currently paid for crude oil in Saskatchewan, where the Company tends to deliver the bulk of its oil production. The Company expects to receive a natural gas price equivalent to the AECO daily spot price. The average prices reported for Painted Pony's sales are the weighted net price, which is reflective of month to month price and sales volume changes.*

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Average Benchmark Prices

Three months ended March 31,	2011	2010
Exchange rate (US\$/Cdn\$)	1.0146	0.9618
Oil - WTI (US\$/bbl)	94.60	78.88
- Edmonton par – light oil (\$/bbl)	88.70	80.59
Gas - AECO, daily spot (\$/mcf)	3.79	4.93

Painted Pony's Realized Prices

Three months ended March 31,	2011	2010
Oil (\$/bbl)	87.08	79.58
Gas (\$/mcf)	3.77	5.21
Condensate (\$/bbl)	82.25	77.78
NGL (\$/bbl)	48.24	38.13

Royalties

Royalties for the three months ended March 31, 2011 are lower on a percentage of sales and on a per boe basis in comparison to the three months ended March 31, 2010, reflecting lower commodity prices for natural gas and royalty incentives in British Columbia. In the quarter ended March 31, 2011, total royalties were \$2.5 million, or approximately 12.9% of total revenue. For the quarter ended March 31, 2010, total royalties were \$2.0 million, or approximately 14.4% of revenue. In the three months ended March 31, 2011, oil royalties averaged 15.4% of sales, while gas and associated product royalties averaged 6.2%.

Through the balance of 2011, the Company anticipates overall royalty rates to continue at approximately 13% of total revenues, reflecting the combined impact of newly drilled wells enjoying royalty holidays with increased royalty rates from older wells, assuming similar commodity prices.*

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Painted Pony's producing properties in British Columbia are all on crown lands and in Saskatchewan are on a combination of freehold and crown lands. Approximately 42% of the crown royalty costs during the three months ended March 31, 2011 were from sales on Saskatchewan oil properties, while sales of gas from recently drilled wells in British Columbia enjoyed provincial royalty incentives. Freehold royalties are from the sale of oil, gas and liquids within Saskatchewan. Gross overriding royalties are mainly from oil sales on lands earned through farm-ins and are mostly attributable to wells in Saskatchewan.

Royalties as a % of Revenue

Three months ended March 31,	2011	2010
Crown	1.4	2.0
Freehold	8.5	8.6
GOR	3.0	3.8
	12.9	14.4

Royalties by Type (000s)

Three months ended March 31,	2011	2010
Crown	\$ 280	\$ 284
Freehold	1,633	1,217
GOR	587	541
	\$ 2,500	\$ 2,042
Per boe (6 mcf:1 bbl)	\$ 6.90	\$ 9.77

Operating and Transportation (000s, except per unit)

Operating and transportation costs for the three months ended March 31, 2011 were \$3.8 million or \$10.45 per boe. This compares to \$2.3 million or \$10.90 per boe for the first quarter of 2010.

Three months ended March 31,	2011	2010
Oil	\$ 2,384	\$ 1,388
Gas and associated liquids	1,402	889
Net	\$ 3,786	\$ 2,277
Oil (\$/bbl)	\$ 14.62	\$ 8.96
Gas and associated liquids (\$/boe)	7.03	16.47
Operating and transportation cost - total (\$/boe)	\$ 10.45	\$ 10.90

Overall per unit operating costs decreased in the first quarter of 2011 compared to the same period of 2010, reflecting incremental sales volumes and cost-saving measures implemented by the Company.

For the Company's oil producing properties, operating costs are primarily oil transportation, emulsion and hauling, road and lease maintenance, fuel and power expenditures, equipment rentals and contract operator fees. During the first quarter of 2011, these properties required a number of minor workovers and repairs and maintenance in addition to spring break-up related issues. Weather related issues are expected to result in incremental costs in Saskatchewan during the second and third quarters of 2011.*

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Operating costs for gas and associated liquids properties are mainly compression fees, contract operating fees, fuel and power, gas transportation, processing and treating fees, and maintenance expenditures on the more mature properties. Per unit gas operating costs were lower in the first quarter of 2011 compared to the same period of 2010 primarily due to increased through-put volumes.

Operating Netbacks

For the three months ended March 31, 2011, field operating netbacks averaged \$35.95 per boe, compared to field operating netbacks of \$47.02 per boe during the quarter ended March 31, 2010.

Combined Field Operating Netback (\$/boe)

Three months ended March 31,	2011	2010
Sales	\$ 53.30	\$ 67.69
Royalties	(6.90)	(9.77)
Operating costs	(10.45)	(10.90)
Field operating netback	\$ 35.95	\$ 47.02

Netbacks by Commodity

Three months ended March 31,	2011	2010
Crude oil (\$/bbl)	\$ 59.08	\$ 58.71
Gas and associated products (\$/boe)	\$ 17.03	\$ 13.45

During the first quarter of 2011, Painted Pony's per unit netback for crude oil was 68% of the gross sales price, compared to 66% for gas and related products, or 67% overall.

Netbacks from crude oil production in Saskatchewan were \$59.08 per bbl for the quarter ended March 31, 2011, compared to \$58.71 per bbl in the three months ended March 31, 2010. The increased per bbl netback for crude oil during the first quarter of 2011, reflects higher oil prices partially offset by higher operating costs associated with minor workovers, oil transportation and road and lease maintenance costs when compared to the first quarter of 2010.

The Company monitors netbacks for gas inclusive of associated products. In the first quarter of 2011, netbacks primarily from British Columbia properties, which produce gas and associated products averaged \$17.03 per boe in the three months ended March 31, 2011, compared to \$13.45 per boe in the first quarter of 2010. Netbacks increased in British Columbia despite lower gas prices. This was the result of significantly lower royalty costs and slightly reduced operating costs which were caused by increased volumes resulting in lower per unit processing and compression costs.

The decrease in the Company's overall netbacks is primarily due to the increased gas weighting, with its lower per unit netback, in the first quarter of 2011 compared to the same 2010 period.

Other Income

Other income is primarily from processing, salt water disposal fees and compression fees. Other income during the first quarter of 2011 increased dramatically as the Company has ownership in three facilities that generate processing income. The first quarter of 2010 income was negligible as these facilities had yet to be constructed.

Other Income (000s)

Three months ended March 31,	2011	2010
Other income	\$ 196	\$ 4

General and Administrative

Net general and administrative expenses were \$0.9 million and \$0.5 million during the three months ended March 31, 2011 and 2010. On a per boe basis, net general and administrative costs were \$2.37 per boe in the first quarter of 2011, compared to \$2.22 per boe in the same period of 2010.

General and Administrative Costs

Three months ended March 31, (000s, except per boe)	2011	2010
Gross costs	\$ 1,724	\$ 1,251
Capitalized	(364)	(422)
Recoveries	(500)	(365)
Net costs	\$ 860	\$ 464
Net G&A, per boe	\$ 2.37	\$ 2.22

Gross general and administrative costs in the first quarter of 2011 were 38% greater than in the first three months of 2010, primarily due to salaries, consulting costs, and associated administrative costs for twenty-nine people compared to eighteen people in the first quarter of 2010. Bonuses of \$0.2 million were paid in the first quarter of 2010, but not paid until the second quarter in 2011. In the first quarter of both years, major general and administrative costs included office rent and parking, fees to professional service providers, costs associated with annual reporting and computer related charges.

The Company's policy of allocating and capitalizing costs associated with new capital projects was unchanged in the first quarter of 2011 compared to the same period of 2010. During the quarter ended March 31, 2011, the Company allocated \$0.4 million of administrative costs to capital projects, compared to a similar amount of \$0.4 million during the same period of 2010. The portion allocated to capital projects was in accordance with common industry practice whereby an operator calculates and allocates overhead to each working interest partner in proportion to their ownership interest, based on 100% of the capital expenditures. Decreased cost allocations in the first quarter of 2011 reflect the decreased operated capital expenditure levels compared to the first quarter of 2010. General and administrative cost recoveries in the three months ended March 31, 2011, were \$0.5 million, compared to \$0.4 million during the quarter ended March 31, 2010, directly reflecting increased exploration staff and activity.

In 2011, net general and administrative costs per boe have remained flat compared to the first quarter of 2010 reflecting the increased production base and incremental staffing, including additional exploration personnel. During the balance of 2011, variations in the capital expenditure levels will be reflected in the capitalization and recovery of general and administrative costs during the periods.*

**This paragraph contains forward-looking information. Please refer to "Forward-looking Information" and "Business Risks, Uncertainties and Forward-looking Information" for a discussion of the risks and uncertainties related to such information.*

Capital Taxes

Capital taxes, specifically the Saskatchewan resource surcharge, were \$0.3 million for the three months ended March 31, 2011 compared to \$0.2 million in the first quarter of 2010. As gross Saskatchewan sales revenues fluctuate, capital taxes are expected to vary correspondingly in 2011.*

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Share-Based Payments

Share-based payment costs were \$0.7 million in the three months ended March 31, 2011 compared to \$1.2 million in the first quarter of 2010. The Company capitalized \$0.04 million during the quarter ended March 31, 2011 and \$0.3 million during the three months ended March 31, 2010. The share-based payment expense is a non-cash calculation, utilizing the Black-Scholes model, of the estimated cost associated with options granted to purchase Class A shares. This expense does not represent actual cash compensation realized by the recipients of the options upon the eventual exercise and disposition of these options.

Depletion and Depreciation

Depletion and depreciation expense in the three months ended March 31, 2011 totaled \$8.0 million and \$5.4 million in the three months ended March 31, 2010. On a per boe basis, the charge decreased in the first quarter of 2011 compared to the first quarter of 2010, reflecting the addition of reserves at lower costs than historical levels. In the first quarter of 2011, Painted Pony excluded the exploration and evaluation assets of \$43.8 million from the depletion calculation, compared to \$17.7 million for the three months ended March 31, 2010.

Depletion and Depreciation Costs

Three months ended March 31, (000s, except per boe)	2011	2010
Depletion and depreciation	\$ 7,994	\$ 5,354
Per boe	\$ 22.06	\$ 25.62

Depletion rates reflect the all-in combined effect of the first quarter 2011 transition to IFRS combined with reduced depletion rates with the addition of gas reserves. The depletion rate utilizes proved plus probable reserves in the calculation.

Depreciation expense was recognized for office equipment, computer hardware and software and office furniture being depreciated on a 20% per annum declining balance basis.

Gain on Sale of Assets

After restating the financial statements in 2010 to reflect IFRS standards, three earnings events occurred in the first quarter resulting in a "gain on sale of assets" of \$0.1 million. This reflects the IFRS standard as outlined in the "Significant Accounting Policies" in note 3 of the interim financial statements and in this MD&A under the heading "Property, Plant and Equipment and Impairment of Assets". No comparable gains or losses were recognized in the first quarter of 2011.

Gain on sale of assets (000s)

Three months ended March 31,	2011	2010
Gain on sale of assets	\$ -	\$ 104

Net Finance Expense

Painted Pony invests cash in interest-bearing deposit accounts and short-term deposits, generating interest income. Interest income in the first quarters of 2011 and 2010 were minimal reflecting the low interest rates.

Finance charges are the result of interest on borrowings along with associated fees related to the amount of credit available to the Company. Finance charges in the three months ended March 31, 2011 totaled \$0.2 million and \$0.03 million for the three months ended March 31, 2010. Finance charges have increased as the Company has an available credit facility of \$75 million as at March 31, 2011 compared to \$43 million as at March 31, 2010.

Accretion costs from the convertible Class B shares were \$0.2 million in both the first quarters of 2011 and 2010, although the cost did increase marginally in 2011 as a result of a higher present value.

Accretion costs on decommissioning obligations increased from \$0.05 million for the three months ended March 31, 2010 compared to \$0.07 million in the same 2011 quarter, as a result of additional wells drilled and acquired, along with ownership in additional facilities.

Net Finance Expense (000s)

Three months ended March 31,	2011	2010
Interest income	\$ (115)	\$ (35)
Finance charges	159	25
Accretion of decommissioning obligations	74	48
Accretion of Class B share liability	180	168
Total	\$ 298	\$ 206

Capital Expenditures

In the first quarter of 2011, Painted Pony conducted an active drilling program with the drilling of 12 (8.1 net) wells, of which 9 (6.6 net) wells were targeting oil in Saskatchewan and 3 (1.5 net) wells were targeting Montney gas in British Columbia. Exploration and development capital expenditures, including facilities and land costs totaled \$24.5 million in the first quarter of 2011 compared to \$34.4 million incurred in the first quarter of 2010.

Capital Expenditures (000s)

Three months ended March 31,	2011	2010
Lease acquisitions and retention	\$ 184	\$ 186
Drilling and completions	19,576	11,566
Facilities and equipment	4,354	5,348
Exploration and evaluation	393	17,295
Exploration and development	24,507	34,395
Head office expenditures	51	29
	24,558	34,424
Property acquisitions	27	-
Abandonment expenditures	104	-
Share-based payments	42	332
Gain on sale of assets	-	104
Decommissioning costs	354	622
Total expenditures	\$ 25,085	\$ 35,482

In Saskatchewan, the Company drilled 7 (5.6 net) horizontal Bakken oil wells in the Huntoon, Midale, and Weyburn areas, and 1 (0.5 net) horizontal Mississippian oil well at Alameda. The Company also drilled 1 (0.5 net) vertical oil well at Alameda, for a total of 9 (6.6 net) wells in Saskatchewan during the first quarter of 2011. Of the wells drilled in Saskatchewan during the first quarter, 6 (4.6 net) wells were placed on production by the end of the quarter. Extremely wet weather and resulting road bans and flooding in Saskatchewan during the second quarter of this year has limited access to leases and hampered the ability to complete operations. The remaining 3 (2.0 net) wells are expected to be completed in the third quarter.*

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In the first quarter of 2011, Painted Pony drilled 3 (1.5 net) horizontal Montney gas wells on the d-5-K pad in the Blair area of British Columbia. The wells were completed and tied-in to existing infrastructure in the second quarter, producing gas from the lower, middle and upper Montney formations. In addition, 1 (0.5 net) vertical Montney well and 1 (0.3 net) lower Montney horizontal well were brought on-stream in May.

Painted Pony's land position continues to grow. Currently, the Company owns 76,049 net acres of land (93% undeveloped) in Saskatchewan and 124,472 net acres of land (83% undeveloped) in British Columbia. During the first quarter of 2011, the Company added lands in British Columbia through participation at provincial lands sales. Painted Pony's total land position at March 31, 2011 is 200,521 net acres, of which 87% are undeveloped. At March 31, 2010, Painted Pony had 171,237 net acres in both provinces.

The Company continues to expect certain leases that are approaching expiry to be continued through execution of work programs comprised of seismic and/or drilling operations.*

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Liquidity and Capital Resources

As at March 31, 2011, Painted Pony had current assets of \$95.8 million and current liabilities of \$31.7 million, resulting in a net working capital position of \$64.1 million. Available cash has been, and is currently, on deposit in a major Canadian financial institution or invested in term deposits. Management has received confirmation from the financial institution that these funds are available on demand.

Management anticipates that the Company will continue to have adequate liquidity to fund future working capital requirements and capital expenditures through a combination of cash flows, the availability of credit facilities and investment capital. As a result of the global economic slowdown, there exists uncertainty in the commodity, credit and capital markets, which the Company continues to monitor in conjunction with its financing alternatives. The capital program will be reviewed, and adjusted if believed necessary based on commodity prices, perceived credit and investment capital availability and share price levels to support the Company's objectives of maintaining a net debt to funds flow from operations ratio of one times or less.*

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The Company has a \$75 million demand revolving credit facility with a Canadian chartered bank. Interest for the demand revolving credit facility is payable at a floating rate determined as the lender's prime rate plus 0.5% to 2.5%, depending on the Company's debt to cash flow ratio, as defined by the lender. A standby fee is charged at 0.20% to 0.45% of the undrawn portion of the credit facility, depending on the Company's cash flow ratio, as defined by the lender. Security is provided by a first fixed and floating charge demand debenture of \$100 million on all of the Company's assets. Painted Pony has provided a negative pledge and undertaking to provide fixed charges over major petroleum and natural gas reserves in certain circumstances.

The availability under the demand revolving credit facility is subject to an interim review on or before September 30, 2011. To date in 2011, the Company has not drawn on its credit facility. There can be no assurance that the amount of the available demand credit facility will not be decreased at the next interim review.

Commitments

At March 31, 2011, the Company is committed to minimum tolls for transportation of oil through a major carrier system that began June 1, 2010 and ends in 2015. At March 31, 2011, the Company is further committed to minimum tolls for transportation of oil through a major carrier system that is estimated to begin July 1, 2011 and ends in 2016. The total minimum cost of the two commitments is estimated to be \$2.9 million.*

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At March 31, 2011, the Company was committed to future payments totaling \$2.0 million for office space rental and a proportionate share of operating costs through 2015.

Share Capital

On February 17, 2011, the Company completed a bought deal financing of 7,620,000 Class A shares at a price of \$10.50 per share for total gross proceeds of \$80.0 million. As at March 31, 2011, there were 59,186,073 Class A shares and 1,173,600 Class B shares issued and outstanding.

The Company has a Stock Option Plan (the "Plan") whereby options to purchase Class A Shares may be granted by the Board of Directors to directors, officers, and employees of, and consultants to, the Company. The Plan has reserved for issuance a number of Class A Shares equal to ten percent of the aggregate number of Class A Shares and Class B Shares issued and outstanding from time to time.

In the first quarter of 2011, a total of 549,373 options were exercised at an average price of \$3.98 per Class A share and 77,980 options were forfeited and cancelled. No new options were granted during the period January 1, 2011 to March 31, 2011. The outstanding options are exercisable over a five year period at a weighted-average price of \$4.77 per option for each Class A share with generally one-third vesting immediately, one-third vesting one year from the date of grant, and one-third vesting two years from the date of grant. As at March 31, 2011, 3,921,567 options to purchase Class A shares were issued and outstanding.

The Company is authorized to issue an unlimited number of Preferred Shares, issuable in series. As at March 31 and June 24, 2011, no Preferred Shares were issued or outstanding.

As at June 24, 2011, there were 59,532,673 Class A shares, 1,173,600 Class B shares and 5,434,867 options at an average price of \$6.86 per Class A share issued and outstanding.

Income Taxes

At the end of the first quarter of 2011, the Company had a \$1.1 million (December 31, 2010: \$1.2 million) estimated future tax liability. In the first quarter of 2011, the Company recognized a future income tax benefit of \$1.1 million for share issue costs which was partially offset by a deferred tax expense of \$1.0 million.

Dividends

The Company has not declared or paid any dividends. Any decision to pay dividends on any of its shares will be made by the Board of Directors on the basis of earnings, financial requirements and other conditions existing at such future time.

Off Balance Sheet Arrangements

No off balance sheet arrangements existed as at March 31, 2011.

Related Party Transactions

The Company utilizes the services of a law firm in which the Corporate Secretary is a Partner. During the three months ended March 31, 2011, the Company incurred \$0.07 million (2010: \$0.03 million) on legal services. All related party transactions have been measured at the agreed to terms and exchange values, being the consideration established and agreed to by the parties.

Financial Instruments and Other Instruments

The fair values of the Company's cash and cash equivalents, trade and other receivables and trade and other payables approximate their carrying amounts due to the short-term nature of these financial instruments.

The Company's trade and other receivables are primarily with industry partners and are subject to normal industry credit risks. The Company extends unsecured credit to these entities, and therefore, the collection of any receivables may be affected by changes in the economic environment or other conditions. Management believes the risk is mitigated by the financial position of the entities.*

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The Class B shares have been accorded compound instrument treatment, whereby they have been separated into their liability and equity components using the effective interest method. The liability component accretes up to the principal balance at maturity. The equity component will be reclassified to share capital upon conversion.

To date, the Company has not participated in any risk management contracts or commodity price contracts.

Performance Compared to Guidance

Readers are reminded that forward looking information in this document is subject to significant risks and uncertainties and is based on a number of material factors and assumptions which may prove to be incorrect. A comparison of performance in the first quarter of 2011 to previously announced guidance by the Company is as follows:

- The Company indicated it expected sales volumes in 2011 to be weighted approximately 50% towards gas sales. During the first quarter of 2011, gas sales averaged 50% of sales volumes, as the Company continues to drill and find gas in British Columbia at a faster rate than new oil production in Saskatchewan.
- The Company indicated it expected the average oil price in 2011 to be approximately 3% less than the reference price. In each month during the first quarter of 2011, the Company's weighted average price was between 1% and 2% less than the reference price.
- The Company indicated it expected the average natural gas price in 2011 to be at a premium to the AECO daily spot price. During the first quarter of 2011, Painted Pony received a weighted average price approximately the same as the reference price, reflecting the impact of associated gas sales from the oil properties in Saskatchewan.
- The Company indicated it expected overall royalty rates to approximate 13% of total revenues. For the first three months of 2011, royalties averaged approximately 13%.
- The Company indicated expected economic benefits from the multi-well oil battery facility and water disposal facility in the Huntoon-Midale area would include reducing production disruptions, cost-effective water handling and disposal, reduced trucking costs and eliminating the capital investment of oil storage tanks at each well location. The Company further indicated it expected reduced oil operating costs in future months from the various batteries and gathering systems. Subsequent to the multi-well oil battery and water disposal facility being put on-stream during the first quarter of 2010, but prior to spring breakup issues in 2011 and excluding workovers, minimal production disruptions occurred and operating costs declined.
- The Company indicated it expected capital taxes to correspondingly increase in 2011 as gross oil sales increased, which is consistent with first quarter 2011 costs.

Change in Accounting Policies

IFRS

The condensed interim consolidated financial statements have been prepared in accordance with IFRS. The Company mandatorily adopted IFRS on January 1, 2011. Previously, Painted Pony prepared its interim consolidated financial statements in accordance with Canadian GAAP. The Company has provided IFRS accounting policies and prepared reconciliations between Canadian GAAP and IFRS in Notes 2, 3 and 20 of its March 31, 2011 condensed interim consolidated financial statements and its 2010 comparative information. The adoption of IFRS did not have an impact on the Company's operations. The following table provides summary reconciliations of Painted Pony's 2010 net income under Canadian GAAP and IFRS to illustrate the impact on adoption.

Summary of Net Income

(0000s)	Total 2010	Q4 2010	Q3 2010	Q2 2010	Q1 2010
Net Income (loss) - GAAP	\$ 1,894	\$ 1,373	\$ (510)	\$ 350	\$ 681
Additions / (deductions):					
Other income	(134)	(48)	(34)	(17)	(35)
General and administrative	248	65	85	73	25
Share-based payments	108	29	21	25	33
Depletion and depreciation	3,194	345	643	908	1,298
Net finance charges	(1,053)	(262)	(282)	(303)	(206)
Deferred income taxes	(2,517)	(1,078)	(954)	(131)	(354)
Gain (loss) on sale of assets	7,482	4,089	3,289	-	104
Total increase to income	7,328	3,140	2,768	555	865
Net Income - IFRS	\$ 9,222	\$ 4,513	\$ 2,258	\$ 905	\$ 1,546

Accounting Policy Changes

The following discussion illustrates the significant differences between Canadian GAAP and the accounting policies applied by the Company under IFRS. IFRS 1 "First-time Adoption of International Financial Reporting Standards" allows first-time adopters certain exemptions from retrospective application of certain IFRS policies. IFRS policies have been retrospectively applied except where specific IFRS 1 optional and mandatory exemptions permitted an alternative treatment upon transition to IFRS.

IFRS 1 Exemptions

IFRS 1 contains exemptions whereby a company may choose to apply IFRS to property, plant and equipment prospectively to its full cost pool provided an impairment test under IFRS standards is conducted at the transition date. More specifically a company may choose to allocate the historical full cost pool to cash generating units ("CGUs") by utilizing either volumes or values from current reserves at the transition date. Painted Pony elected to apply this optional exemption under IFRS 1 and has allocated the historical cost pool (net book value) to CGUs based on proven plus probable reserve values.

As part of the aforementioned exemption, Painted Pony re-measured its decommissioning liabilities, previously referred to as asset retirement obligations, as at the date of transition in accordance with IFRS standards and recognized the difference from the amount recorded under Canadian GAAP directly into retained earnings. Refer to "Decommissioning Obligations" below for further details.

The Company applied the optional exemption in respect of business combinations and share-based payment transactions, both of which grant a first-time adopter relief from restatement in accordance with IFRS prior to the date of transition to IFRS.

Painted Pony determined that the total impact of the conversion to IFRS was a reduction in retained earnings on January 1, 2010 in the amount of \$4.8 million. The Company has performed impairment calculations at the transition date and did not have any transitional write-downs associated with its petroleum and natural gas properties.

Exploration and Evaluation

Exploration and evaluation ("E&E") costs are expenditures incurred for which technical feasibility and commercial viability have not yet been determined. Such expenditures include costs of acquiring licenses, seismic and exploratory drilling and completion costs and directly attributable general and administration costs. When technical feasibility and commercial viability are determined, the costs are transferred to property, plant and equipment. At the date of transition, Painted Pony determined its E&E balance was \$13.4 million, almost entirely related to undeveloped land.

E&E will be expensed if the costs do not relate to an established CGU and its technical feasibility and commercial viability cannot be established. For the year ended December 31, 2010, no E&E costs were expensed.

Exploration and evaluation assets are assessed for impairment if (i) sufficient data exists to determine technical feasibility and commercial viability, (ii) facts and circumstances suggest that the carrying amount exceeds the recoverable amount and (iii) amounts are transferred to CGU's. For purposes of impairment testing, exploration and evaluation assets are combined with cash-generating units. For the three months ended March 31, 2011 and the year ended December 31, 2010, no impairment of E&E costs was recognized.

Property, Plant and Equipment and Impairment of Assets

Property, plant and equipment ("PP&E") costs include expenditures where technical feasibility and viability have been determined. Under IFRS, Painted Pony capitalizes these costs in PP&E, within CGU's, and measures them at cost less accumulated depletion, depreciation and impairment losses. The cost of property, plant and equipment at the date of transition to IFRS, was determined by adopting the IFRS 1 exemption whereby the carrying value of property, plant and equipment assets assumes the carrying value under GAAP at the transition date. Under IFRS, Painted Pony is required to recognize and measure an impairment loss if the carrying value of PP&E exceeds the recoverable amount for any individual CGU. This recoverable amount is the higher of fair value less costs to sell and value in use. The Company's CGUs will be used for the impairment testing, while under Canadian GAAP, impairment tests were measured at the country level. There were no impairments recorded upon transition, comparative periods or at March 31, 2011.

With respect to dispositions, under Canadian GAAP there is no recognition of a gain or loss unless the sale would result in a change to the depletion rate of 20 percent or greater. Under IFRS, property, plant and equipment dispositions will generally result in recognition of a gain or loss to income regardless of the amount of the transaction, as there is no threshold for measurement.

Under Canadian GAAP full cost principles, farm-out arrangements with third parties did not result in a recognizable event for financial reporting purposes. Under IFRS standards, farm-out arrangements result in a recognizable event. On a concurrent basis, a working interest in lease rights is exchanged or "sold" (derecognized) after an earnings event within a farm-out arrangement occurs for the value of reserves "received" (purchased). This transaction will result in a "gain or loss on asset sales", being the difference between the purchase amount and the sale amount.

Depletion and Depreciation

Under IFRS, the net carrying value of property, plant and equipment assets are depleted using the unit of production method with reference to the related proven and probable reserves at a CGU level, taking into account estimated future development costs necessary to bring those reserves into production. Under Canadian GAAP, proven reserves and associated future development costs were applied at a country level and used for depletion purposes. The reserve information is determined by independent reserve engineers on an annual basis. On a quarterly basis, this information may be updated internally or by independent reserve engineers. This change has resulted in a lower depletion and depreciation charge to net income during 2010. The impact of this change is illustrated in the reconciliation of net income above.

Decommissioning Obligations

The Company's activities give rise to dismantling, decommissioning and site disturbance re-mediation activities. Provision is made for the estimated cost of site restoration and capitalized in the relevant asset category.

Under Canadian GAAP, decommissioning liabilities were measured as the estimated fair value of the retirement and decommissioning expenditures expected to be incurred. In measuring the fair value, Painted Pony used a credit-adjusted risk-free rate. Under IFRS, decommissioning obligations are measured as the best estimate of the expenditures to be incurred using a lower risk-free discount rate. As a result, Painted Pony's decommissioning obligations increased at the date of transition by \$1.9 million. During the year ended December 31, 2010, the Company's decommissioning liabilities increased by \$3.2 million, including accretion adjustments. Due to the higher fair values and the reduced discount rate, the accretion recognized in net income throughout 2010 decreased. Under IFRS, this accretion is now classified and disclosed as a finance cost in the statement of income and comprehensive income. The impact of this change is illustrated in the reconciliation of net income above.

Share-Based Payments

Under Canadian GAAP, the Company accounted for options granted to directors, officers, employees and certain consultants by measuring the fair value of the instruments issued and amortized this value over the instruments vesting periods. Fair value was measured using the Black-Scholes option pricing model using inputs that included share price on measurement date, exercise price of the instrument, expected volatility, weighted average expected life of the instruments, expected dividends and a risk-free interest rate. Under IFRS the Company must also estimate and apply a forfeiture rate on the grant date and subsequently adjust it to reflect the actual number of options that vest. Under Canadian GAAP, forfeitures were recorded at the time of expiry or cancellation. The impact of the forfeiture rate changes was nominal for the Company. A required change in treatment for options granted to consultants under IFRS compared to GAAP was the primary reason for differences recognized.

Flow-through Shares

Flow-through shares are resource expenditure deductions for income tax purposes related to development and exploratory activities funded by flow-through share arrangements which are renounced to investors in accordance with income tax legislation. Under Canadian GAAP, the accounting treatment for flow-through shares was to record the full amount of the proceeds in share capital. When expenditures are renounced, the related tax effect is recorded to share capital and the deferred income tax liability. Under IFRS, the amount initially recorded in share capital was limited to the amount of proceeds that would have been received on that date if they were not issued as flow-through shares. The difference between the actual proceeds and the amount recorded in share capital is set up as a deferred premium on the statement of financial position. When the expenditures are incurred, the deferred premium on the flow-through shares is reversed and the related tax effect is recorded to the deferred income tax liability. The impact of this change in accounting policy is incorporated in the table in note 20(c) of the "Notes to Condensed Interim Consolidated Financial Statements".

Income Tax

Income tax expense is comprised of deferred income tax expense and has been adjusted to reflect the tax effect arising from the differences between Canadian GAAP and IFRS. The impact of this change is illustrated in the reconciliation of net income above and in note 20(h) of the "Notes to Condensed Interim Consolidated Financial Statements".

Critical Accounting Estimates

The significant accounting policies used by the Company are disclosed in note 3 of the Condensed Interim Consolidated Financial Statements for the three months ended March 31, 2011 and 2010. The significant accounting policies followed by the Company under Canadian GAAP prior to conversion to IFRS are disclosed in the Company's annual audited consolidated financial statements. For a discussion on critical accounting policies and estimates under GAAP prior to conversion to IFRS, the reader is directed to the 2010 annual Management's Discussion and Analysis on SEDAR. Certain accounting policies require that management make appropriate decisions with respect to the formulation of estimates and assumptions that affect the reported amounts of assets, liabilities and expenses. The Company's management reviews its estimates regularly.

New Standards and Interpretations Not Yet Adopted

In November 2009, the IASB published IFRS 9 – “*Financial Instruments*”, which covers the classification and measurement of financial assets as part of its project to replace IAS 39 – “*Financial Instruments: Recognition and Measurement*”. In October 2010, the requirements for classifying and measuring financial liabilities were added to IFRS 9. Under this guidance, entities have the option to recognize financial liabilities at fair value through earnings. If this option is elected, entities would be required to reverse the portion of the fair value change due to credit risk out of earnings and recognize the change in other comprehensive income. IFRS 9 is effective for the Company on January 1, 2013. Early adoption is permitted and the standard is required to be applied retrospectively. There will be no significant impact to the Company upon implementation of the issued standard.

In May 2011, IFRS 10 “*Consolidated Financial Statements*” was issued which sets out the principles for the presentation and preparation of consolidated financial statements when an entity controls one or more other entities. IFRS 10 replaces SIC-12 “*Consolidation—Special Purpose Entities*” and parts of IAS 27 “*Consolidated and Separate Financial Statement*” and is effective for annual periods beginning on or after January 1, 2013. Earlier application is permitted. The Company is currently evaluating the impact of this standard on its consolidated financial statements.

In May 2011, IFRS 11 “*Joint Arrangements*” was issued to address reporting inconsistencies. This standard requires a single method to account for interests in jointly controlled entities, focusing on the rights and obligations of a joint arrangement, rather than its legal form (as is currently the case). IFRS 11 supersedes IAS 31 “*Interests in Joint Ventures*” and SIC-13 “*Jointly Controlled Entities—Non-Monetary Contributions by Venturers*”, and is effective for annual periods beginning on or after January 1, 2013. Earlier application is permitted. The Company is currently evaluating the impact of this standard on its consolidated financial statements.

In May 2011, IFRS 12 “*Disclosure of Interests in Other Entities*” was issued. This comprehensive standard applies to entities that have an interest in a subsidiary, a joint arrangement, an associate or an unconsolidated structured entity. IFRS 12 is effective for annual periods beginning on or after January 1, 2013. Earlier application is permitted. The Company is currently evaluating the impact of this standard on its consolidated financial statements.

In May 2011, IFRS 13 “*Fair Value Measurements*” was issued. This standard defines fair value, setting out a single IFRS framework for measuring fair value and required disclosures about fair value measurements. IFRS 13 is to be applied for annual periods beginning on or after January 1, 2013. Earlier application is permitted. The Company is currently evaluating the impact of this standard on its consolidated financial statements.

Business Risks, Uncertainties and Forward-looking Information*

Statements in this document may contain forward-looking information including expectations of future production, components of cash flow and earnings, expected future events and/or financial results that are forward-looking in nature and subject to substantial risks and uncertainties. The reader is cautioned that assumptions used in the preparation of such information may prove to be incorrect. The Company cautions the readers that actual performance will be affected by a number of factors, many of which may respond to changes in economic and political circumstances throughout the world. Events or circumstances may cause actual results to differ materially from those predicted, a result of numerous known and unknown risks, uncertainties, and other factors, many of which are beyond the control of the Company. These risks include, but are not limited to, the risks associated with the oil and gas industry, and changes to commodity prices and interest and foreign exchange rates. Industry related risks could include, but are not limited to, operational risks in exploration, development and production, delays or changes in plans, risks associated with the uncertainty of reserve estimates, health and safety risks and the uncertainty of estimates and projections of production, costs and expenses. The following external factors beyond the Company’s control may affect the marketability of oil and natural gas produced: industry conditions including changes in laws and regulations, changes in income tax regulations, increased competition, fluctuations in commodity prices, interest rates, and variations in the Canadian/United States dollar exchange rate. The reader is cautioned not to place undue reliance on this forward-looking information.

Painted Pony's production and exploration activities are concentrated in the Western Canadian Sedimentary Basin, where activity is highly competitive and includes a variety of different sized companies ranging from smaller junior producers to the much larger integrated petroleum companies. Painted Pony is subject to the various types of business risks and uncertainties including:

- Finding and developing oil and natural gas reserves at economic costs;
- Production of oil and natural gas in commercial quantities; and
- Marketability of oil and natural gas produced.

In order to reduce exploration risk, the Company strives to employ highly qualified and motivated professional employees with a demonstrated ability to generate quality proprietary geological and geophysical prospects. To help maximize drilling success, Painted Pony combines exploration in areas that afford multi-zone prospect potential, targeting a range of low to moderate risk prospects with some exposure to select high-risk plays with high-reward opportunities. Painted Pony also explores in areas where the Company's officers and employees have significant drilling experience.

The Company mitigates its risk related to producing hydrocarbons through the utilization of the most appropriate technology and information systems. In addition, Painted Pony seeks operational control of its projects, where feasible.

Oil and gas exploration and production can involve environmental risks such as pollution of the environment and destruction of natural habitat, as well as safety risks such as personal injury. In order to mitigate such risks, Painted Pony conducts its operations at high standards and follows safety procedures intended to reduce the potential for personal injury to employees, contractors and the public at large. The Company maintains current insurance coverage for general and comprehensive liability as well as limited pollution liability. The amount and terms of this insurance are reviewed on an ongoing basis and adjusted as necessary to reflect changing corporate requirements, as well as industry standards and government regulations. Painted Pony may periodically use financial or physical delivery hedges to reduce its exposure against the potential adverse impact of commodity price volatility, as governed by formal policies approved by senior management, subject to controls established by the Board of Directors.

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Legal, Environmental, Remediation and Other Contingent Matters

The Company reviews legal, environmental, remediation and other contingent matters to both determine whether a loss is probable based on judgment and interpretation of laws and regulations, and determine that the loss can reasonably be estimated. When the loss is determined, it is charged to earnings. The Company's management monitors known and potential contingent matters and makes appropriate provisions by charges to earnings when warranted by circumstances.

Selected Consolidated Quarterly Information

The following tables set forth selected consolidated financial information of the Company for the most recently completed quarters ending at the first quarter of 2011.

Quarter ended (unaudited) (\$000s except volumes and per share)	March 31, 2011
Gross revenues ⁽¹⁾	19,315
Funds flow from operations	12,098
Basic per share	0.22
Diluted per share	0.21
Cash flow from operating activities	11,555
Net income	2,144
Basic per share	0.04
Diluted per share	0.04
Capital expenditures, net	24,558
Capital acquisitions, net	27
Working capital	64,100
Total assets	330,156
Decommissioning obligations ⁽²⁾	7,574
Convertible Class B shares liability	10,716
Average daily sales volumes (boe/d)	4,027

(1) Petroleum and natural gas sales, before royalties and operating and transportation, excluding interest and other income.

(2) Formerly asset retirement obligations under Canadian GAAP.

Quarter ended (unaudited) (\$000s except volumes and per share)	March 31, 2010	June 30, 2010	Sept. 30, 2010	Dec. 31, 2010
Gross revenues ⁽¹⁾	14,146	12,752	14,764	16,621
Funds flow from operations	9,156	7,705	9,122	10,411
Basic, per share	0.21	0.17	0.20	0.20
Diluted, per share	0.20	0.17	0.19	0.20
Cash flow from operating activities	9,221	8,355	7,698	10,200
Net income	1,546	905	2,258	4,513
Basic, per share	0.04	0.02	0.05	0.09
Diluted, per share	0.03	0.02	0.05	0.09
Capital expenditures, net	34,424	31,853	19,655	21,357
Capital acquisitions, net	-	-	-	12,846
Working capital (deficiency)	15,639	(8,592)	22,454	(1,205)
Total assets	186,881	175,982	223,347	244,579
Decommissioning obligations ⁽²⁾	4,961	5,137	5,626	7,145
Convertible Class B shares liability	10,015	10,186	10,360	10,536
Average daily sales volumes (boe/d)	2,322	2,532	3,080	3,443

(1) Petroleum and natural gas sales, before royalties and operating and transportation, excluding interest and other income.

(2) Formerly asset retirement obligations under Canadian GAAP.

Quarter ended (unaudited) ⁽³⁾ (\$000s except volumes and per share)	June 30, 2009	Sept. 30, 2009	Dec. 31, 2009
Gross revenues ⁽¹⁾	4,889	7,834	11,612
Funds flow from operations	1,826	4,513	6,981
Basic, per share	0.06	0.12	0.17
Diluted, per share	0.06	0.12	0.16
Cash flow from operating activities	531	4,273	6,157
Net income (loss)	(1,965)	(2,046)	1,953
Basic and diluted, per share	(0.06)	(0.05)	0.05
Capital expenditures, net	4,633	12,141	16,483
Capital acquisitions, net	-	13,587	1
Working capital	22,290	1,096	40,679
Total assets	108,308	112,861	164,907
Decommissioning obligations ⁽²⁾	1,931	2,278	2,439
Average daily sales volumes (boe/d)	1,313	1,655	2,006

(1) Petroleum and natural gas sales, before royalties and operating and transportation, excluding interest and other income.

(2) Asset retirement obligations under Canadian GAAP.

(3) Painted Pony's IFRS transition date was January 1, 2010, therefore 2009 comparative information has not been restated from Canadian GAAP.

Significant factors and trends that have affected the Company's results during the above quarterly periods are as follows:

- Gross revenues are impacted by both fluctuating commodity prices and production volumes. The Company's successful capital program has generated incremental production volumes steadily over the last eight quarters, which has generally lead to higher cash flows. The sales prices realized by the Company have generally approximated the Edmonton par light oil prices and AECO daily spot gas prices throughout the above periods. The reference price fluctuations reflect changes in supply and demand by commodity, both internationally and domestically.
- Funds flow from operations have both increased and decreased over time, reflecting primarily the impact of fluctuating commodity prices on a growing production base. Per production unit operating and transportation cost variations track seasonal weather-related issues combined with fixed commitments. Throughout 2010, commodity prices were substantially stronger than during 2009, increasing funds flow from operations. Oil prices continue to improve in 2011, while natural gas prices have modestly declined. The net effect of strong oil prices will contribute to increased funds flow from operations. Royalty changes vary due to commodity prices, production levels and the status of the different provincial royalty holiday incentive programs. As the production base in Saskatchewan matures, incremental royalties occur on wells as the maximum volumes provided for under the provincial incentive programs are attained. Royalty incentive programs have continued in British Columbia and the Company should continue to enjoy lower royalty rates.
- Cash flow from operating activities has increased or decreased in concert with funds flow from operations and is further impacted by the timing of related trade and other payable and receivable settlements.
- Net income in the first quarter of 2011 continues to improve due to growth in production, improved oil prices and stable operating costs. Net income in three of the four quarters of 2010 was significantly impacted by growth in production and increased strength in oil prices. In the third quarter of 2010, the Company recorded \$2.0 million of non-cash share-based payments for share options surrendered for cancellation. Throughout the second and third quarters of 2009, net income reflected relatively weaker commodity prices, lower production volumes and higher operating costs due to trucking oil. During the final quarter of 2009 Painted Pony realized net income as a result of increased production volumes from successful drilling operations and increases in oil prices.

- Net capital expenditures fluctuations have reflected both available capital resources and intentional capital spending restraint during weaker economic periods.
- Net capital acquisitions occurred in the fourth quarter of 2010 and the third quarter of 2009 when strategic opportunities were identified and completed.
- Total assets and non-current liabilities (provisions) have generally increased quarter over quarter, reflecting the execution of the Company's capital program, somewhat offset by depletion.
- Overall daily production has steadily increased since the inception of the Company reflecting the execution of the Company's strategic plan to grow its reserve and production base.

Additional Information

Additional information regarding the Company and its business and operations is available on the Company's profile at www.sedar.com. Copies of the information can also be obtained by contacting the Company at Painted Pony Petroleum Ltd., 300, 602 – 12 Avenue SW., Calgary, Alberta T2R 1J3 (Phone 403 475-0440), by email at info@paintedpony.ca or on the Company's website at www.paintedpony.ca.

PAINTED PONY PETROLEUM LTD.
CONDENSED INTERIM CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

(Unaudited)
(000's)

As at	March 31, 2011	December 31, 2010	January 1, 2010
		<i>(note 20)</i>	<i>(note 20)</i>
ASSETS			
Current assets			
Cash and cash equivalents <i>(note 4)</i>	\$ 72,985	\$ 9,748	\$ 46,575
Trade and other receivables	22,435	17,200	5,198
Prepaid expenses and deposits	333	320	324
	95,753	27,268	52,097
Non-current assets			
Exploration and evaluation <i>(note 5)</i>	43,847	43,535	13,424
Property, plant and equipment <i>(note 6)</i>	190,556	173,776	96,301
Deferred tax asset	-	-	3,052
	\$ 330,156	\$ 244,579	\$ 164,874
LIABILITIES			
Current liabilities			
Trade and other payables	\$ 31,653	\$ 28,473	\$ 11,418
Non-current liabilities			
Decommissioning obligations <i>(note 8)</i>	7,574	7,145	4,290
Convertible Class B shares liability <i>(note 9)</i>	10,716	10,536	9,847
Deferred tax liability	1,113	1,232	-
	51,056	47,386	25,555
EQUITY			
Share capital <i>(note 10)</i>	259,235	178,772	135,731
Equity component of convertible Class B shares <i>(note 9)</i>	(2,923)	(2,923)	(2,923)
Contributed surplus <i>(note 10)</i>	15,228	15,928	10,317
Retained earnings (deficit)	7,560	5,416	(3,806)
	279,100	197,193	139,319
	\$ 330,156	\$ 244,579	\$ 164,874

Basis of presentation *(note 2)*
Commitments *(note 14)*
Subsequent events *(note 19)*

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

PAINTED PONY PETROLEUM LTD.
CONDENSED INTERIM CONSOLIDATED STATEMENTS OF INCOME AND
COMPREHENSIVE INCOME

(Unaudited)
(\$000s, except per share amounts)

Three months ended March 31,	2011	2010
		<i>(note 20)</i>
Revenue		
Petroleum and natural gas	\$ 19,315	\$ 14,146
Royalties	(2,500)	(2,042)
Other	196	4
	17,011	12,108
Expenses		
Operating and transportation	3,786	2,277
General and administrative	860	464
Capital taxes	267	211
Share-based payments <i>(note 10)</i>	683	1,162
Depletion and depreciation <i>(note 6)</i>	7,994	5,354
Gain on sale of assets	-	(104)
	13,590	9,364
Results from operating activities	3,421	2,744
Finance income	(115)	(35)
Finance expense	413	241
Net finance expense <i>(note 12)</i>	298	206
Income before income tax	3,123	2,538
Deferred income tax expense	979	992
Net Income and Comprehensive Income for the Period	\$ 2,144	\$ 1,546
Earnings per share:		
Basic <i>(note 11)</i>	\$ 0.04	\$ 0.04
Diluted <i>(note 11)</i>	\$ 0.04	\$ 0.03

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

PAINTED PONY PETROLEUM LTD.
CONDENSED INTERIM CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

(Unaudited)
(\$000s, except shares)

Periods Ended March 31, 2011 and 2010 and December 31, 2010

	Number of shares Class A	Share capital Class A	Equity component Class B	Contributed surplus	Retained earnings (deficit)	Total equity
Balance, Jan. 1, 2010 <i>(note 20)</i>	44,081,700	\$ 135,731	\$ (2,923)	\$ 10,317	\$ (3,806)	\$ 139,319
Share-based payments	-	-	-	1,494	-	1,494
Options exercised <i>(note 10)</i>	55,000	326	-	(108)	-	218
Income for the period	-	-	-	-	1,546	1,546
Balance, March 31, 2010	44,136,700	\$ 136,057	\$ (2,923)	\$ 11,703	\$ (2,260)	\$ 142,577
Issue of shares	6,800,000	44,064	-	-	-	44,064
Share issue costs, net of tax of \$653	-	(1,800)	-	-	-	(1,800)
Share-based payments	-	-	-	4,408	-	4,408
Options exercised <i>(note 10)</i>	80,000	451	-	(183)	-	268
Income for the period	-	-	-	-	7,676	7,676
Balance at Dec. 31, 2010	51,016,700	\$ 178,772	\$ (2,923)	\$ 15,928	\$ 5,416	\$ 197,193
Issue of shares	7,620,000	80,010	-	-	-	80,010
Share issue costs, net of tax of \$1,097	-	(3,158)	-	-	-	(3,158)
Share-based payments	-	-	-	725	-	725
Options exercised <i>(note 10)</i>	549,373	3,611	-	(1,425)	-	2,186
Income for the period	-	-	-	-	2,144	2,144
Balance at March 31, 2011	59,186,073	\$ 259,235	\$ (2,923)	\$ 15,228	\$ 7,560	\$ 279,100

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

PAINTED PONY PETROLEUM LTD.
CONDENSED INTERIM CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

(\$000s)

Three months ended March 31,	2011	2010
Cash flows from operating activities:		
Net income for the period	\$ 2,144	\$ 1,546
Items not affecting cash:		
Share-based payments	683	1,162
Depletion and depreciation	7,994	5,354
Net finance expense	298	206
Deferred income tax expense	979	992
Gain on sale of assets	-	(104)
Decommissioning expenditures	(104)	-
Changes in non-cash working capital <i>(note 13)</i>	(439)	65
	11,555	9,221
Cash flows from investing activities:		
Exploration and evaluation additions	(393)	(17,295)
Property, plant and equipment additions	(24,165)	(17,129)
Acquisition of property, plant & equipment	(27)	-
Changes in non-cash working capital <i>(note 13)</i>	(1,773)	15,204
	(26,358)	(19,220)
Cash flows from financing activities:		
Issue of share capital	80,010	-
Exercise of share options	2,186	218
Share issuance costs	(4,255)	-
Finance and interest costs <i>(note 12)</i>	(45)	10
Changes in non-cash working capital <i>(note 13)</i>	144	(64)
	78,040	164
Change in cash and cash equivalents	63,237	(9,835)
Cash and cash equivalents, beginning of period	9,748	46,575
Cash and cash equivalents, end of period <i>(note 4)</i>	\$ 72,985	\$ 36,740

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

PAINTED PONY PETROLEUM LTD.
NOTES TO CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
Three months ended March 31, 2011 and 2010

1. Reporting Entity

Painted Pony Petroleum Ltd.'s (the "Company") principal business activity is the exploration, development and production of petroleum and natural gas resources in western Canada. The condensed interim consolidated financial statements of the Company as at and for the three month periods ended March 31, 2011 and 2010 include the accounts of the Company and its wholly owned subsidiaries, Painted Pony Petroleum Corp. and Painted Rock Resources Ltd. The Company's head office is located at Suite 300, 602 – 12 Ave. S.W., Calgary, AB.

2. Basis of Presentation

Statement of Compliance

The condensed interim consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) International Accounting Standard (IAS) 34 "Interim Financial Reporting". These are the Company's first IFRS condensed consolidated interim financial statements for part of the period covered by the first IFRS annual financial statements, and IFRS 1 "*First-time Adoption of International Financial Reporting Standards*" has been applied (see note 20). The condensed interim consolidated financial statements were authorized for issue by the Board of Directors on June 24, 2011. The condensed interim consolidated financial statements do not include all of the information required for full annual financial statements.

Basis of Measurement

The condensed interim consolidated financial statements have been prepared primarily on the historical cost basis. The methods used to measure fair values are discussed in note 16.

Functional and Presentation Currency

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

Use of Estimates and Judgements

The preparation of financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the year in which the estimates are revised and in any future years affected.

Information about significant areas of estimation uncertainty and critical judgments in applying accounting policies that have the most significant effect on the amounts recognized in the consolidated financial statements is included in the following notes:

- Note 5 – valuation of exploration and evaluation assets
- Note 6 – valuation of property, plant and equipment
- Note 8 – provisions
- Notes 9 and 10 – measurement of share-based payments
- Note 17 – valuation of financial instruments
- Note 18 – contingencies

Reserve estimates impact a number of the areas referred to above in particular, the valuation of property, plant and equipment and the calculation of depletion and depreciation.

3. Significant Accounting Policies

The accounting policies set out below have been applied consistently to all periods presented in these condensed interim consolidated financial statements, and have been applied consistently by the Company and its subsidiaries.

Certain comparative amounts have been reclassified to conform to the current year's presentation.

Basis of Consolidation

(i) Subsidiaries

Subsidiaries are entities controlled by the Company. Control exists when the Company has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, potential voting rights that currently are exercisable are taken into account. The financial statements of subsidiaries are included in the condensed consolidated financial statements from the date that control commences until the date that control ceases.

The purchase method of accounting is used to account for acquisitions of subsidiaries and assets that meet the definition of a business under IFRS. The cost of an acquisition is measured as the fair value of the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date. The excess of the cost of acquisition over the fair value of the identifiable assets, liabilities and contingent liabilities acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognized immediately in the statement of income.

(ii) Jointly controlled operations and jointly controlled assets

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

(iii) Transactions eliminated on consolidation

Intercompany balances and transactions, and any unrealized income and expenses arising from intercompany transactions, are eliminated in preparing the condensed interim consolidated financial statements.

Financial instruments

(i) Non-derivative financial instruments

Non-derivative financial instruments comprise cash and cash equivalents, trade and other receivables, trade and other payables and the Class B shares liability. Non-derivative financial instruments are recognized initially at fair value plus, for instruments not at fair value through profit or loss, any directly attributable transaction costs. Subsequent to initial recognition non-derivative financial instruments are measured as described below.

(ii) Cash and cash equivalents

Cash and cash equivalents comprise cash on hand, term deposits held with banks, other short-term highly liquid investments with original maturities of three months or less. Bank overdrafts that are repayable on demand form part of the Company's cash management, whereby management has the ability and intent to net bank overdrafts against cash and are included as a component of cash and cash equivalents for the purpose of the statement of cash flows.

(iii) Financial assets at fair value through profit or loss

An instrument is classified at fair value through profit or loss if it is held for trading or is designated as such upon initial recognition. Financial instruments are designated at fair value through profit or loss if the Company manages such investments and makes purchase and sale decisions based on their fair value in accordance with the Company's risk management or investment strategy. Upon initial recognition, attributable transaction costs are recognized in profit or loss when incurred. Financial instruments at fair value through profit or loss are measured at fair value, and changes therein are recognized in profit or loss.

(iv) Financial liabilities at amortized cost

Financial liabilities at amortized cost include trade and other payables, amounts drawn on the demand credit facility and the convertible Class B shares liability. Trade and other payables are initially recognized at the amount required to be paid less any required discount to reduce the payables to fair value. Long-term debt is recognized initially at fair value, net of any transaction costs incurred, and subsequently at amortized cost using the effective interest method.

Financial liabilities are classified as current liabilities if payment is due within twelve months. Otherwise, they are presented as non-current liabilities.

(v) Compound instruments

Compound instruments, being the convertible Class B shares, are separated into their liability and equity components using the effective interest method. The liability component accretes up to the principal balance at maturity. The equity component will be reclassified to share capital upon conversion.

(vi) Other

Other non-derivative financial instruments, such as cash and cash equivalents and trade and other receivables, are measured at amortized cost using the effective interest method, less any impairment losses.

Share Capital

Class A shares are classified as equity. Incremental costs directly attributable to the issue of shares and share options are recognized as a deduction from equity, net of any tax effects.

Property, Plant and Equipment and Exploration and Evaluation Assets

(i) Recognition and measurement

Exploration and evaluation expenditures:

Pre-licence costs are recognized in the statement of income as incurred. Exploration and evaluation costs, including the costs of acquiring licenses, seismic, exploration drilling and directly attributable general and administrative costs, initially are capitalized as exploration and evaluation assets according to the nature of the assets acquired. The costs are accumulated in cost centers pending determination of technical feasibility and commercial viability.

The technical feasibility and commercial viability of extracting a mineral resource is considered to be determinable when proven or probable reserves are determined to exist. A review is carried out, on a quarterly basis, to ascertain whether proven or probable reserves have been discovered. Upon determination of proven or probable reserves, exploration and evaluation assets attributable to those reserves are first tested for impairment and then reclassified from exploration and evaluation assets to property, plant and equipment assets.

Development and production costs:

Items of property, plant and equipment, which include oil and gas development and production assets, are measured at cost less accumulated depletion, depreciation and accumulated impairment losses. Development and production assets are grouped into CGU's for impairment testing. The cost of property, plant and equipment at January 1, 2010, the date of transition to IFRS, was determined by adopting the IFRS 1 exemption whereby the carrying value of property, plant and equipment assets under IFRS assumes the carrying value under GAAP at transition date. When significant parts of an item of property, plant and equipment, including oil and natural gas interests, have different useful lives, they are accounted for as separate items (major components).

Gains and losses on disposal of an item of property, plant and equipment, are determined by comparing the proceeds from disposal with the carrying amount of the asset(s) and are recognized within "gain/loss on sale of assets" in profit or loss.

(ii) Subsequent costs

Costs incurred subsequent to the determination of technical feasibility and commercial viability and the costs of replacing parts of property, plant and equipment are recognized as oil and natural gas interests only when they increase the future economic benefits embodied in the specific assets to which they relate. All other expenditures are recognized in profit or loss as incurred. Such capitalized oil and natural gas interests generally represent costs incurred in developing proved and/or probable reserves and bringing on or enhancing production from such reserves. The carrying amount of any replaced or sold component is derecognized. The costs of periodic servicing of property, plant and equipment are recognized in profit or loss as incurred.

(iii) Depletion and depreciation

The net carrying value of development or production assets is depleted using the unit of production method by reference to the ratio of production in the period to the related proven and probable reserves, taking into account estimated future development costs necessary to bring those reserves into production. Future development costs are estimated taking into account the level of development required to produce the reserves. These estimates are reviewed by independent reserve engineers on an annual basis, at minimum.

Proven and probable reserves are estimated using independent reserve engineer reports in accordance with Canadian Securities Regulation National Instrument 51-101 and represent the estimated quantities of oil, natural gas and natural gas liquids which geological, geophysical and engineering data demonstrate with a specified degree of certainty to be recoverable in future years from known reservoirs and which are considered commercially producible. There should be a 50 percent statistical probability that the actual quantity of recoverable reserves will be more than the amount estimated as proven and probable and a 50 percent statistical probability that it will be less. The equivalent statistical probabilities for the proven component of proven and probable reserves are 90 percent and 10 percent, respectively.

Such reserves may be considered commercially producible if management has the intention of developing and producing them and such intention is based upon:

- a reasonable assessment of the future economics of such production;
- a reasonable expectation that there is a market for all or substantially all the expected oil and natural gas production; and
- evidence that the necessary production, transmission and transportation facilities are available or can be made available.

Reserves may only be considered proven and probable if producibility is supported by either actual production or a conclusive formation test. The area of reservoir considered proven includes (a) that portion delineated by drilling and defined by gas-oil and/or oil-water contacts, if any, or both, and (b) the immediately adjoining portions not yet drilled, but which can be reasonably judged as economically productive on the basis of available geophysical, geological and engineering data. In the absence of information on fluid contacts, the lowest known structural occurrence of oil and natural gas controls the lower proved limit of the reservoir.

Reserves which can be produced economically through application of improved recovery techniques (such as fluid injection) are only included in the proven and probable classification when successful testing by a pilot project, the operation of an installed program in the reservoir or other reasonable evidence (such as, experience of the same techniques on similar reservoirs or reservoir simulation studies) provides support for the engineering analysis on which the project or program was based.

For other assets, depreciation is recognized in profit or loss on a declining-balance rate of 20% based on their estimated useful lives. Exploration and evaluation assets are not depreciated.

Leased Assets

Payments made under operating leases are recognized in profit or loss on a straight-line basis (or as otherwise contractually defined) over the term of the lease. Lease incentives received are recognized as part of the total lease expense over the term of the lease.

Impairment

(i) Financial assets

A financial asset is assessed at each reporting date to determine whether there is any objective evidence that it is impaired. A financial asset is considered to be impaired if objective evidence indicates that one or more events have had a negative effect on the estimated future cash flows of that asset.

An impairment loss in respect of a financial asset measured at amortized cost is calculated as the difference between its carrying amount and the present value of the estimated future cash flows discounted at the original effective interest rate.

Individually significant financial assets are tested for impairment on an individual basis. The remaining financial assets are assessed collectively in groups that share similar credit risk characteristics.

All impairment losses are recognized in profit or loss.

An impairment loss is reversed if the reversal can be related objectively to an event occurring after the impairment loss was recognized. For financial assets measured at amortized cost the reversal is recognized in profit or loss.

(ii) Non-financial assets

The carrying amounts of the Company's non-financial assets, other than exploration and evaluation assets and deferred tax assets, are reviewed whenever there is an indication of impairment. If any such indication exists, the asset's recoverable amount is estimated.

For the purpose of impairment testing, assets are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups of assets (the "cash-generating unit" or "CGU"). The recoverable amount of an asset or a CGU is the greater of its value in use and its fair value less costs to sell.

In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. Value in use is generally computed by reference to the present value of the future cash flows expected to be derived from production of proven and probable reserves.

Exploration and evaluation assets are assessed for impairment if: (i) sufficient data exists to determine technical feasibility and commercial viability, (ii) facts and circumstances suggest that the carrying amount exceeds the recoverable amount and (iii) when they are reclassified to property, plant and equipment. For purposes of impairment testing, exploration and evaluation assets are combined with cash-generating units.

An impairment loss is recognized if the carrying amount of an asset or its CGU exceeds its estimated recoverable amount. Impairment losses are recognized in profit or loss.

Impairment losses recognized in prior years are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depletion and depreciation or amortization, if no impairment loss had been recognized.

Share-Based Payments

The Company has issued options to acquire shares to directors, officers, consultants and employees. The fair value of options on the date they are granted is recognized as compensation expense with a corresponding increase in contributed surplus over the vesting period. A forfeiture rate is estimated on the grant date and is adjusted to reflect the actual number of options that vest. The Company uses the Black-Scholes model to estimate fair value.

Provisions

A provision is recognized if, as a result of a past event, the Company has a present legal or constructive obligation that can be estimated reliably and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the liability. Provisions are not recognized for future operating losses.

(i) Decommissioning obligations

The Company's activities give rise to dismantling, decommissioning and site disturbance re-mediation activities. Provision is made for the estimated cost of site restoration and capitalized in the relevant asset category.

Decommissioning obligations are measured at the present value of management's best estimate of expenditure required to settle the present obligation at the Statement of Financial Position date. Subsequent to the initial measurement, the obligation is adjusted at the end of each period to reflect the passage of time and changes in the estimated future cash flows underlying the obligation. The increase in the provision due to the passage of time is recognized as a finance cost whereas increases/decreases due to changes in the estimated future cash flows are capitalized. Actual costs incurred upon settlement of the decommissioning obligations are charged against the provision to the extent the provision had been established.

Revenue Recognition

Revenue from the sale of oil and natural gas is recorded when the significant risks and rewards of ownership of the product is transferred to the buyer, which is usually when legal title passes to the external party, and when collection is reasonably assured.

Tariffs and tolls charged to other entities for use of pipelines and facilities owned by the Company are recognized as other revenue as they accrue in accordance with the terms of the service or tariff and tolling agreements.

Royalty income is recognized in petroleum and natural gas revenues as it accrues in accordance with the terms of the overriding royalty agreements.

Finance Income and Expenses

Finance expense consists of interest expense and miscellaneous fees on credit facility borrowings, accretion of the discount on provisions, accretion of the convertible Class B share liability and impairment losses recognized on financial assets.

Finance income comprises interest income and is recognized as it accrues in profit or loss, using the effective interest rate.

Income Tax

Income tax expense comprises deferred income tax expense and is recognized in profit or loss except to the extent that it relates to items recognized directly in equity, in which case it is recognized in equity. The Company currently does not recognize any current income tax expense.

Deferred tax is recognized using the balance sheet method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is not recognized on the initial recognition of assets or liabilities in a transaction that is not a business combination. Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date. Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset, and they relate to income taxes levied by the same tax authority on the same taxable entity, or on different tax entities, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realized simultaneously.

A deferred tax asset is recognized to the extent that it is probable that future taxable profits will be available against which the temporary difference can be utilized. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realized.

Earnings per Share

Basic per share information is calculated on the basis of the weighted average number of Class A shares outstanding during the period. Diluted per share information reflects the potential dilution effect of options and convertible Class B shares. The Company calculated the dilutive impact of the convertible Class B shares assuming the outstanding Class B shares are converted at the later of the beginning of the period or the date of issue. Net income is adjusted for the amount of finance expense applicable to the Class B shares for the period. The number of Class A shares issued upon the conversion of each Class B share will be equal to \$10.00 divided by the greater of \$1.00 and the weighted average trading price per share of the Class A shares for the last 30 consecutive trading days as of the statement of financial position date.

Anti-dilutive instruments are not included in the determination of diluted per share amounts.

4. Cash and Cash Equivalents

(\$000s)	Three months ended March 31, 2011	Year ended December 31, 2010
Bank balances	\$ 32,985	\$ 9,748
Term deposits	40,000	-
Cash and cash equivalents	\$ 72,985	\$ 9,748

5. Exploration and Evaluation Assets (“E&E”)

(\$000s)	
Cost:	
Balance, January 1, 2010	\$ 13,424
Additions	45,890
Acquisitions	1,800
Transfers to property, plant and equipment	(17,579)
Balance, December 31, 2010	\$ 43,535
Additions	393
Transfers to property, plant and equipment	(81)
Balance, March 31, 2011	\$ 43,847

Exploration and evaluation assets do not have any accumulated depletion and depreciation or impairments as at March 31, 2011.

Exploration and evaluation assets consist of the Company's exploration projects which are pending the determination of proven or probable reserves. Acquisitions represent exploration and evaluation assets purchased during the period. Additions represent the Company's share of costs incurred on exploration and evaluation assets during the period.

6. Property, Plant and Equipment (“PP&E”)

(\$000s)	Oil and Natural gas properties	Office furniture & equipment	Total
Cost or deemed cost:			
Balance, January 1, 2010	\$ 96,103	\$ 272	\$ 96,375
Acquisitions	11,046	-	11,046
Cash additions	61,199	200	61,399
Non-cash additions	11,451	-	11,451
Transfers from exploration and evaluation	17,579	-	17,579
Balance, December 31, 2010	197,378	472	197,850
Acquisitions	27	-	27
Cash additions	24,114	51	24,165
Non-cash additions	501	-	501
Transfers from exploration and evaluation	81	-	81
Balance, March 31, 2011	\$ 222,101	\$ 523	\$ 222,624
Depletion and depreciation:			
Balance, January 1, 2010	\$ -	\$ 74	\$ 74
Depletion and depreciation	23,939	61	24,000
Balance, December 31, 2010	23,939	135	24,074
Depletion and depreciation	7,975	19	7,994
Balance, March 31, 2011	\$ 31,914	\$ 154	\$ 32,068
Carrying amounts:			
At January 1, 2010	\$ 96,103	\$ 198	\$ 96,301
At December 31, 2010	\$ 173,439	\$ 337	\$ 173,776
At March 31, 2011	\$ 190,187	\$ 369	\$ 190,556

(a) Depreciation and Impairment Charge

The depletion, depreciation and impairment of property, plant and equipment, and any eventual reversal thereof, are recognized in depletion and depreciation in the statement of income (see also note 16).

(b) Security

Security is provided by a first fixed and floating charge debenture of \$100 million on all of the Company's assets. The Company has provided a negative pledge and undertaking to provide fixed charges over major petroleum and natural gas reserves in certain circumstances.

(c) Capitalized General and Administrative Expense and Share-based Payments

For the three months ended March 31, 2011 and 2010, the Company capitalized general and administrative expenses and share-based payments as follows:

Three months ended March 31,	2011	2010
General and administrative	\$ 364	\$ 422
Share-based payments	42	332
Total	\$ 406	\$ 754

7. Bank Debt

At March 31, 2011 the Company had a \$75 million demand revolving operating credit facility available for use. Undrawn as of March 31, 2011, this facility is subject to a review on or before September 30, 2011. There can be no assurance that the amount of the available demand credit facility will not be decreased at the next scheduled review.

Interest for the demand revolving credit facility is payable at a floating rate determined as the lender's prime rate plus 0.5% to 2.5%, depending on the Company's debt to cash flow ratio, as defined by the lender. A standby fee of 0.20% to 0.45% is charged on the undrawn portion of the credit facility, depending on the Company's cash flow ratio, as defined by the lender. Security is provided by a first fixed and floating charge debenture of \$100 million on all of the Company's assets. The Company has provided a negative pledge and undertaking to provide fixed charges over major petroleum and natural gas reserves in certain circumstances.

8. Decommissioning Obligations

(\$000s)	March 31, 2011	December 31, 2010
Balance, beginning of period	\$ 7,145	\$ 4,290
Provisions	459	2,731
Decommissioning expenditures	(104)	(100)
Accretion	74	224
Balance, end of period	\$ 7,574	\$ 7,145
Non-current	\$ 7,574	\$ 7,145
Current	-	-
	\$ 7,574	\$ 7,145

Decommissioning Obligations

The Company's decommissioning obligations result from its ownership interest in oil and natural gas assets including well sites and facilities. The total decommissioning obligation is estimated based on the Company's net ownership interest in all wells and facilities, estimated costs to reclaim and abandon these wells and facilities and the estimated timing of the costs to be incurred in future years. The Company has estimated the net present value of the decommissioning obligations to be \$7.6 million as at March 31, 2011 (December 31, 2010: \$7.1 million) based on an undiscounted total future liability of \$14.8 million (December 31, 2010 - \$14.2 million). These payments are expected to be made over the next 25 to 30 years with the majority of costs to be incurred between 2026 and 2028. The discount factor, being the risk-adjusted rate related to the liability, is 4% (2010: 4%) and the inflation rate is 2% (2010: 2%).

9. Convertible Class B Shares

On reorganization, the Company had 6,615 convertible Class B shares (the "Class B shares") outstanding. On May 17, 2007, the Company issued 1,080,000 Class B shares on a flow-through basis and 86,985 Class B shares in satisfaction of debt, which were not on a flow-through basis, bringing the total number of Class B shares to 1,173,600. An unlimited number of Class B shares are authorized for issuance. The Class B shares are convertible at the option of the Company until the close of business on June 30, 2012, into Class A shares. The number of Class A shares obtained upon conversion of each Class B share will be equal to \$10.00 divided by the greater of \$1.00 and the then current market price (as defined) of the Class A shares (the "conversion formula"). If the Company fails to exercise the conversion option by the close of business on June 30, 2012, then the Class B shares shall be convertible at the option of the shareholder, at any time after June 30, 2012, and before August 1, 2012 into Class A shares pursuant to the conversion formula described above. Any Class B shares not converted prior to close of business on August 1, 2012 will be automatically converted into Class A shares pursuant to the conversion formula. The Class B shares are listed and posted for trading on the TSX Venture Exchange under the symbol "PPY.B".

The Class B shares were determined to be compound instruments. As the Class B shares are convertible into Class A shares, based on the conversion formula above, the number of Class A shares is unknown, and therefore are presented as a liability. The Class B share liability is accreted using the effective interest rate method (7%) over the term of the Class B shares, such that the carrying amount of the financial liability will be equal to the principal balance of \$11.7 million at maturity.

The following table indicates the convertible Class B shares activities :

(\$000's)	Three months ended March 31, 2011	Year ended December 31, 2010
Balance, beginning of period	\$ 10,536	\$ 9,847
Accretion on convertible Class B share liability	180	689
Balance, end of period	\$ 10,716	\$ 10,536

At the date of transition to IFRS, the Company recognized the equity component for the convertible Class B shares as a conversion option of \$2.0 million and \$0.9 million related to the deferred income tax effect of the Class B shares.

10. Share Capital

(a) Authorized

Unlimited: Class A and B shares

Unlimited: Preferred shares, none outstanding as at March 31, 2011, December 31, 2010 and January 1, 2010

The Class A shares are voting on the basis of one vote per share. There are no dividends payable on the Class A shares. In the event of the liquidation or dissolution of the Company, the Class B shares will be converted at the conversion rate (note 9) into Class A shares and the Class A shares are entitled to receive, on a pro rata basis, all assets of the Company as are distributable to the holders of shares.

(b) Stock options

The Company has an option program that entitles officers, directors and employees to purchase shares in the Company. Options are granted at the market price of the shares at the date of grant, have a five year term and generally vest one-third immediately with the balance over two years.

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

	Weighted Average Exercise Price	Number
Balance, January 1, 2010	\$ 3.53	2,755,000
Granted	6.25	1,938,920
Exercised	3.60	(135,000)
Forfeited and cancelled	5.88	(10,000)
Balance, December 31, 2010	\$ 4.68	4,548,920
Exercised	3.98	(549,373)
Forfeited and cancelled	5.16	(77,980)
Balance, March 31, 2011	\$ 4.77	3,921,567
Exercisable at December 31, 2010	\$ 4.20	2,799,306
Exercisable at March 31, 2011	\$ 4.40	2,474,600

Number of Options Outstanding	Exercise Price	Remaining Life (yrs)	Grant Date Fair Value	Exercisable Options	Exercise Price
877,000	\$ 3.97	1.8	\$ 2.62	877,000	\$ 3.97
75,000	\$ 1.40	2.7	0.90	75,000	\$ 1.40
682,500	\$ 2.85	3.3	1.84	440,334	\$ 2.85
349,500	\$ 3.15	3.3	2.04	197,000	\$ 3.15
137,000	\$ 5.88	3.7	3.80	90,666	\$ 5.88
609,167	\$ 5.88	3.8	3.71	400,000	\$ 5.88
70,000	\$ 5.60	4.2	3.62	22,000	\$ 5.60
1,121,400	\$ 6.51	4.4	4.21	372,600	\$ 6.51
3,921,567	\$ 4.77	3.4	\$ 3.08	2,474,600	\$ 4.40

The weighted average share price at the date of exercise for share options exercised during the three months ended March 31, 2011 was \$10.36 (three months ended March 31, 2010 - \$6.57).

The Company accounts for its stock options granted to employees, consultants, officers and directors using the fair value method. In accordance with the Company's incentive stock plan, these options have an exercise price equal to the fair value of the Company's Class A shares at the date of grant using the Black-Scholes option-pricing model. The following weighted-average fair value of the options granted and the assumptions used are as follows:

Three months ended March 31,	2010
Fair value per option (weighted average)	\$ 3.71
Volatility (%)	80
Option life (years)	5
Dividends	-
Risk-free interest rate (%)	1.88

No stock options were granted during the three months ended March 31, 2011.

A forfeiture rate of 0% (2010 – 0%) is used when measuring share-based payments. Share-based payments of \$0.7 million (three months ended March 31, 2010 - \$1.2 million) were expensed and \$42,000 (three months ended March 31, 2010 - \$0.3 million) was capitalized during the three months ended March 31, 2011.

11. Earnings per Share

Basic earnings per share was calculated as follows:

(\$000s except shares)

Three months ended March 31,	2011	2010
Net income for the period	\$ 2,144	\$ 1,546
Weighted average number of shares		
Class A shares – basic	55,082,225	44,128,088
Class A shares – diluted	56,927,128	45,183,322
Net income per share – basic	\$ 0.04	\$ 0.04
Net income per share - diluted	\$ 0.04	\$ 0.03

The average market value of the Company's shares for purposes of determining the dilutive effect of converting the Class B shares to Class A shares and of outstanding share options was based on quoted market prices for the period. All of the Class B shares were excluded from the diluted earnings per share calculation as they were determined to be anti-dilutive for the quarters ended March 31, 2011 and 2010. During the three months ended March 31, 2011, nil (2010: 30,622) options were excluded from the weighted-average diluted share calculation of Class A shares.

12. Finance Income and Expense

(\$000s)

Three months ended March 31,	2011	2010
Finance income:		
Interest income	\$ (115)	\$ (35)
	(115)	(35)
Finance expense:		
Interest and financing costs	159	25
Accretion of decommissioning obligations	74	48
Accretion of convertible Class B share liability	180	168
	413	241
Net finance expense recognized in profit or loss	\$ 298	\$ 206

13. Supplemental Cash Flow Information

Changes in non-cash working capital is comprised of:

(\$000s)

Three months ended March 31,	2011	2010
Source/(use) of cash:		
Trade and other receivables	\$ (5,235)	\$ (2,746)
Prepaid expenses and deposits	(13)	41
Trade and other payables	3,180	17,910
	\$ (2,068)	\$ 15,205
Related to operating activities	\$ (439)	\$ 65
Related to investing activities	(1,773)	15,204
Related to financing activities	144	(64)
	\$ (2,068)	\$ 15,205

14. Operating Commitments

(a) At March 31, 2011, the Company is committed to two contracts, that expire in 2016, that require an estimated \$2.9 million of minimum tolls for transportation of oil through a major carrier system, and are payable as follows:

(\$000s)	Amount
2011	\$ 643
2012	826
2013	612
2014	459
2015	244
2016	67
	\$ 2,851

(b) The Company is committed to future payments for office space rental through to 2015 as follows:

(\$000s)	Amount
2011	\$ 473
2012	624
2013	443
2014	263
2015	241
	\$ 2,044

15. Related Party Transactions

The Company utilizes the services of a law firm in which the Corporate Secretary is a Partner. During the three months ended March 31, 2011, the Company incurred \$66,000 (2010: \$27,000) on services obtained from the firm, excluding disbursements. As at March 31, 2011, the Company owed this related party \$63,470 (December 31, 2010: \$15,329).

16. Determination of Fair Values

A number of the Company's accounting policies and disclosures require the determination of fair value, for both financial and non-financial assets and liabilities. Fair values have been determined for measurement and/or disclosure purposes based on the following methods. When applicable, further information about the assumptions made in determining fair values is disclosed in the notes specific to that asset or liability.

(a) *Property, Plant and Equipment and Exploration and Evaluation Assets*

The fair value of property, plant and equipment recognized in a business combination, is based on market values. The fair value of property, plant and equipment is the estimated amount for which property, plant and equipment could be exchanged on the acquisition date between a willing buyer and a willing seller in an arm's length transaction after proper marketing wherein the parties had each acted knowledgeably, prudently and without compulsion. The fair value of oil and natural gas interests (included in property, plant and equipment) and exploration and evaluation assets is estimated with reference to the discounted cash flows expected to be derived from oil and natural gas production based on externally prepared reserve reports. The risk-adjusted discount rate is specific to the asset with reference to general market conditions.

The market value of other items of property, plant and equipment is based on the quoted market prices for similar items.

(b) *Cash and Cash Equivalents, Trade and Other Receivables and Trade and Other Payables*

The fair value of cash and cash equivalents, trade and other receivables and trade and other payables are estimated as the present value of future cash flows, discounted at the market rate of interest at the reporting date. At March 31, 2011 and December 31, 2010, the fair value of these balances approximated their carrying value due to their short term to maturity.

(c) *Stock Options*

The fair value of employee stock options is measured using a Black-Scholes option pricing model. Measurement inputs include share price on measurement date, exercise price of the instrument, expected volatility, weighted average expected life of the instruments (based on historical experience and general option holder behavior), expected dividends and the risk-free interest rate.

(d) *Class B Shares*

The fair value of the convertible Class B liability at March 31, 2011 was \$10.9 million (December 31, 2010 - \$10.9 million) based on the market price of \$9.25 per Class B share (December 31, 2010 - \$9.25 per Class B share, based on the December 24, 2010 closing price being the last trade of 2010).

17. Financial Risk Management

(a) Overview:

The Company's activities expose it to a variety of financial risks that arise as a result of its exploration, development, production and financing activities such as:

- credit risk;
- liquidity risk; and
- market risk.

This note presents information about the Company's exposure to each of the above risks, the Company's objectives, policies and processes for measuring and managing risk, and the Company's management of capital. Further quantitative disclosures are included throughout these consolidated financial statements.

The Board of Directors oversees management's establishment and execution of the Company's risk management framework. Management has implemented and monitors compliance with risk management policies. The Company's risk management policies are established to identify and analyze the risks faced by the Company, to set appropriate risk limits and controls and to monitor risks and adherence to market conditions and the Company's activities.

(b) Credit risk:

Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its contractual obligations and arises principally from the Company's receivables from joint venture partners and oil and natural gas purchasers. The Company's maximum exposure to credit risk at March 31, 2011 and December 31, 2010 is as follows:

Carrying amount (\$000s)	March 31, 2011	December 31, 2010
Cash and cash equivalents	\$ 72,985	\$ 9,748
Trade and other receivables	22,435	17,200
Prepaid expenses and deposits	333	320
Total current assets	\$ 95,753	\$ 27,268

Trade and other receivables:

All of the Company's operations are conducted in Canada. The Company's exposure to credit risk is influenced mainly by the individual characteristics of each customer.

Receivables from oil and natural gas purchasers are normally collected on the 25th day of the month following production. The Company's policy to mitigate credit risk associated with these balances is to establish marketing relationships with large purchasers. The Company historically has not experienced any collection issues with its oil and natural gas purchasers. Receivables from joint venture partners are typically collected within one to three months of the joint venture bill being issued. The Company attempts to mitigate the risk from joint venture receivables by obtaining partner pre-approval. However, the receivables are from participants in the oil and natural gas sector and collection of the outstanding balances is dependent on industry factors such as commodity price fluctuations, escalating costs and the risk of unsuccessful drilling. In addition, further risk exists with joint venture partners if a disagreement were to arise, which may increase the potential for non-collection. The Company does not typically obtain collateral from oil and natural gas purchasers or joint venture partners; however, the Company does have the ability to withhold production from joint venture partners in the event of non-payment.

The Company does not anticipate any default as it transacts with creditworthy customers and management does not expect any losses from non-performance by these customers. As such, a provision for doubtful accounts has not been recorded at either March 31, 2011 or December 31, 2010.

The breakdown of trade and other receivables at the reporting date by type of customer was:

Carrying amount (\$000s)	March 31, 2011	December 31, 2010
Sales revenue	\$ 7,585	\$ 7,109
Joint interest	13,473	9,045
Other	1,377	1,046
Total trade and other receivables	\$ 22,435	\$ 17,200

The Company has two significant independent commodity purchasers. One entity purchases the majority of natural gas produced in British Columbia which accounted for \$1.5 million of trade and other receivables at March 31, 2011 (December 31, 2010: \$1.5 million). A second entity purchases the majority of oil produced in Saskatchewan which accounted for \$5.5 million of trade and other receivables at March 31, 2011 (December 31, 2010: \$5.0 million).

As at March 31, 2011 and December 31, 2010, the Company's trade and other receivables are aged as follows:

Carrying amount (\$000s)	March 31, 2011	December 31, 2010
Not past due (less than 30 days)	\$ 18,602	\$ 15,339
Past due (31 – 90 days)	3,629	1,691
Past due (more than 90 days)	204	170
Total receivables	\$ 22,435	\$ 17,200

Cash and cash equivalents:

The Company limits its exposure to credit risk by only investing in liquid securities that are guaranteed by the Province of Alberta. Given these credit ratings, management does not expect any counterparty to fail to meet its obligations.

(c) Liquidity risk:

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due. The Company's approach to managing liquidity is to ensure, to the extent possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Company's reputation.

Typically the Company ensures that it has sufficient cash on demand to meet expected operational expenses currently and in the foreseeable future, including the servicing of financial obligations; this excludes the potential impact of extreme circumstances that cannot reasonably be predicted, such as natural disasters. To achieve this objective, the Company prepares annual capital expenditure budgets, which are regularly monitored and updated as considered necessary. Further, the Company utilizes authority for expenditures on both operated and non-operated projects to further manage capital expenditures. The Company also attempts to match its payment cycle with collection of oil and natural gas revenue on the 25th of each month. In addition, the Company maintains a \$75 million credit facility to provide capital when needed, of which \$75 million was available at the end of the period.

(d) Market risk:

Market risk is the risk that changes in market prices, such as commodity prices, foreign exchange rates and interest rates, will affect the Company's income or the value of the financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimizing the return.

The Company may use both financial derivatives and physical delivery sales contracts to manage market risks. All such transactions are conducted within risk management tolerances that are reviewed by the Board of Directors. As at March 31, 2011, the Company had not entered into any derivatives to manage market risk.

Prices for oil are determined in global markets and generally denominated in United States dollars. Natural gas prices obtained by the Company are influenced by both US and Canadian demand and the corresponding North American supply, and recently, by imports of liquefied natural gas. The exchange rate effect cannot be quantified but generally an increase in the value of the Canadian dollar as compared to the U.S. dollar will reduce the prices received by the Company for its petroleum and natural gas sales. Commodity price risk is the risk that the fair value or future cash flows will fluctuate as a result of changes in commodity prices. Commodity prices for oil and natural gas are impacted by not only the relationship between the Canadian and United States dollars, but also world economic events that dictate the levels of supply and demand.

The Company's production is usually sold using "spot" or near term contracts, with prices fixed at the time of transfer of custody or on the basis of a monthly average market price. The Company, however, may give consideration in certain circumstances to the appropriateness of entering into long term, fixed price marketing contracts. To date, the Company has not undertaken any risk management contracts or commodity price contracts. The Company has contracted the majority of its oil to one purchaser on a month-to-month rolling contract. The majority of the Company's natural gas is sold monthly on a best-efforts basis to one purchaser under a one-year term contract, which runs from November 1 to October 31 of each year.

Interest rate risk is the risk that future cash flows will fluctuate as a result of changes in market interest rates. For the period ended March 31, 2011, if interest rates had been 0.5% lower than the first quarter 2011 weighted-average rate of 1.25%, with all other variables held constant, income and comprehensive income for the period would have been \$64,000 lower due to lower interest income. An equal and opposite impact would have occurred to income and comprehensive income had interest rates been 0.5% higher.

(e) Capital management:

The Company's policy is to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain future development of the business. The Company manages its capital structure and makes adjustments to it in the light of changes in economic conditions and the risk characteristics of the underlying oil and natural gas assets. The Company considers its capital structure to include shareholders' equity, loans and borrowings and working capital. In order to maintain or adjust the capital structure, the Company may issue shares and adjust its capital spending to manage current and projected debt levels.

The Company monitors capital based on the ratio of net debt to annualized cash flow. This ratio is calculated as net debt, defined as outstanding loans and borrowings plus or minus working capital, divided by cash flow from operations before changes in non-cash working capital for the most recent calendar quarter and then annualized. The Company's objective is to maintain a net debt to funds flow from operations ratio of 1:1 or less. This ratio may increase at certain times as a result of acquisitions. In order to facilitate the management of this ratio, the Company prepares annual capital expenditure budgets, which are updated as necessary depending on varying factors including current and forecast prices, successful capital deployment and general industry conditions. The annual and updated budgets are approved by the Board of Directors. As at March 31, 2011, the Company did not have a debt balance on its statement of financial position.

There were no changes in the Company's approach to capital management during the period. Neither the Company nor any of its subsidiaries are subject to externally imposed capital requirements. The credit facilities are subject to a periodic review of the borrowing base which is directly impacted by the value of the oil and natural gas reserves.

18. Contingencies

Although the Company believes it has title to its oil and natural gas properties, it cannot control or completely protect itself against the risk of title disputes or challenges. There can be no assurance that claims or challenges by third parties against the Company's properties will not be asserted at a future date.

19. Subsequent Events

On April 5, 2011, the Company closed an acquisition of light oil properties in southeast Saskatchewan from a private company for cash consideration of \$7.7 million, before closing adjustments and related costs.

On April 13, 2011, pursuant to the terms and conditions of its stock option plan, the Company granted an aggregate of 1,505,900 incentive stock options to purchase Class A shares to certain directors, officers, employees and consultants. The options are exercisable over a five year period at an exercise price of \$10.60 per share, with one-third vesting immediately, one-third in one year and the final one-third vesting in two years.

On May 30, 2011, pursuant to the terms and conditions of its stock option plan, the Company granted an aggregate of 354,000 incentive stock options to purchase Class A shares to certain officers and employees. The options are exercisable over a five year period at an exercise price of \$12.10 per share, with one-third vesting immediately, one-third in one year and the final one-third vesting in two years.

20. First time adoption of International Financial Reporting Standards

As disclosed in Note 2, these are the Company's first condensed interim consolidated financial statements for the period covered by the first annual consolidated financial statements to be prepared in accordance with IFRS. The accounting policies set out in note 3 have been applied in preparing the condensed interim consolidated financial statements for the period ended March 31, 2011, the comparative financial statements for the periods ended March 31, 2010 and December 31, 2010 and the January 1, 2010 transitional consolidated statement of financial position. IFRS 1 "First-time Adoption of IFRS" and International Accounting Standard ("IAS") 34 "Interim Financial Reporting" have been applied to these condensed interim consolidated financial statements.

As a result of applying IFRS 1, the Company is required to present comparative information with the application of IFRS accounting policies as at the January 1, 2010 transition date and comparative information for the three months ended March 31, 2010 and for the year ended December 31, 2010. IFRS 1 provides for certain mandatory and optional exemptions for first-time adopters to alleviate the retrospective application of all the accounting standards under IFRS.

An explanation of how the transition from Canadian GAAP to IFRS has affected the Company's financial position, financial performance and cash flows is set out in the following tables.

Key First –Time Adoption Exemptions Applied

IFRS 1 "First-Time Adoption of International Financial Reporting" allows first-time adopters certain exemptions from retrospective application of certain IFRS.

The following include the significant IFRS 1 exemptions taken by the Company at January 1, 2010:

- **Historical cost as deemed cost:**
The Company elected an IFRS 1 exemption whereby the Canadian GAAP full cost pool was measured upon transition to IFRS at the amount determined under Canadian GAAP as at January 1, 2010. Costs included in the full cost pool on January 1, 2010 were allocated on a pro-rata basis to the underlying assets on the basis of proved and probable reserves values as at January 1, 2010. The exploration and evaluation assets were reclassified from the full cost pool to exploration and evaluation assets at the amount that was recorded under Canadian GAAP.
- **Business combinations:**
IFRS 3 "Business Combinations" has not been applied to acquisitions of subsidiaries or interests in joint ventures that occurred before January 1, 2010.
- **Decommissioning obligations:**
The Company elected the exemption under IFRS 1 which allows for the re-measurement of decommissioning obligations on the IFRS transition date to be recorded through the deficit.
- **Share-based payment transactions:**
The Company elected the exemption under IFRS 1 and prospectively applied IFRS 2 to its awards that vest after the transition date.

**Reconciliation of Consolidated Statement of Financial Position from Canadian GAAP to IFRS
At the Date of IFRS Transition – January 1, 2010**

(Unaudited)
(\$000s)

	Canadian GAAP	Effect of transition to IFRS	IFRS
ASSETS			
Current assets			
Cash and cash equivalents	\$ 46,575	\$ -	\$ 46,575
Trade and other receivables	5,198	-	5,198
Prepaid expenses and deposits	324	-	324
	52,097	-	52,097
Non-current assets			
Exploration and evaluation <i>(note a)</i>	-	13,424	13,424
Property, plant and equipment <i>(note a)</i>	109,725	(13,424)	96,301
Deferred tax asset <i>(note h)</i>	3,085	(33)	3,052
	\$ 164,907	\$ (33)	\$ 164,874
LIABILITIES			
Current liabilities			
Trade and other payables	\$ 11,418	\$ -	\$ 11,418
Non-current liabilities			
Decommissioning obligations <i>(note b)</i>	2,439	1,851	4,290
Convertible Class B shares liability <i>(note c)</i>	-	9,847	9,847
	13,857	11,698	25,555
EQUITY			
Share capital <i>(note f)</i>	139,739	(4,008)	135,731
Equity component of convertible Class B shares	-	(2,923)	(2,923)
Contributed surplus <i>(note d)</i>	10,360	(43)	10,317
Retained earnings (deficit) <i>(notes b, c, d, f, h)</i>	951	(4,757)	(3,806)
	151,050	(11,731)	139,319
	\$ 164,907	\$ (33)	\$ 164,874

Reconciliation of Condensed Consolidated Statement of Financial Position from Canadian GAAP to IFRS

As at March 31, 2010 under Canadian GAAP to IFRS

(Unaudited)

(\$000s)

	Canadian GAAP	Effect of transition to IFRS	IFRS
ASSETS			
Current assets			
Cash and cash equivalents	\$ 36,740	\$ -	\$ 36,740
Trade and other receivables	7,944	-	7,944
Prepaid expenses and deposits	283	-	283
	44,967	-	44,967
Non-current assets			
Exploration and evaluation (note a)	-	17,707	17,707
Property, plant and equipment (note a,e)	138,371	(16,223)	122,148
Deferred tax asset (note h)	2,307	(248)	2,059
	\$ 185,645	\$ 1,236	\$ 186,881
LIABILITIES			
Current liabilities			
Trade and other payables	\$ 29,328	\$ -	\$ 29,328
Non-current liabilities			
Decommissioning obligations (note b)	2,829	2,132	4,961
Convertible Class B shares liability (note c)	-	10,015	10,015
	32,157	12,147	44,304
EQUITY			
Share capital (note f)	140,065	(4,008)	136,057
Equity component of convertible Class B shares	-	(2,923)	(2,923)
Contributed surplus (note d)	11,791	(88)	11,703
Retained earnings (deficit) (notes b, c, d, e, f, h)	1,632	(3,892)	(2,260)
	153,488	(10,911)	142,577
	\$ 185,645	\$ 1,236	\$ 186,881

Reconciliation of Condensed Consolidated Statement of Financial Position from Canadian GAAP to IFRS

At the End of the Last Reporting Year under Canadian GAAP – December 31, 2010

(Unaudited)

(\$000s)

	Canadian GAAP	Effect of transition to IFRS	IFRS
ASSETS			
Current assets			
Cash and cash equivalents	\$ 9,748	\$ -	\$ 9,748
Trade and other receivables	17,200	-	17,200
Prepaid expenses and deposits	320	-	320
	27,268	-	27,268
Non-current assets			
Exploration and evaluation <i>(note a)</i>	-	43,535	43,535
Property, plant and equipment <i>(note a, e)</i>	206,078	(32,302)	173,776
Deferred tax asset <i>(note h)</i>	851	(851)	-
	\$ 234,197	\$ 10,382	\$ 244,579
LIABILITIES			
Current liabilities			
Trade and other payables	\$ 28,473	\$ -	\$ 28,473
Non-current liabilities			
Decommissioning obligations <i>(note b)</i>	3,970	3,175	7,145
Convertible Class B shares liability <i>(note c)</i>	-	10,536	10,536
Deferred tax liability <i>(note h)</i>	-	1,232	1,232
	32,443	14,943	47,386
EQUITY			
Share capital <i>(note f)</i>	182,795	(4,023)	178,772
Equity component of convertible Class B shares	-	(2,923)	(2,923)
Contributed surplus <i>(note d)</i>	16,114	(186)	15,928
Retained earnings <i>(note b, c, d, e, f, h)</i>	2,845	2,571	5,416
	201,754	(4,561)	197,193
	\$ 234,197	\$ 10,382	\$ 244,579

**Reconciliation of Condensed Consolidated Statement of Income and Comprehensive Income
For the Three Months ended March 31, 2010 from Canadian GAAP to IFRS**

(Unaudited)

(\$000s, except per share amounts)

	Canadian GAAP	Effect of Transition to IFRS	IFRS
Revenue			
Petroleum and natural gas	\$ 14,146	\$ -	\$ 14,146
Royalties	(2,042)	-	(2,042)
Other <i>(note i)</i>	39	(35)	4
	12,143	(35)	12,108
Expenses			
Operating and transportation	2,277	-	2,277
General and administrative <i>(note i)</i>	489	(25)	464
Capital taxes	211	-	211
Share-based payments <i>(note d)</i>	1,195	(33)	1,162
Depletion and depreciation <i>(note e)</i>	6,652	(1,298)	5,354
Gain on sale of assets <i>(note g)</i>	-	(104)	(104)
	10,824	(1,460)	9,364
Results from operating activities	1,319	1,425	2,744
Finance income <i>(note i)</i>	-	(35)	(35)
Finance expense <i>(note b,i)</i>	-	241	241
Net finance expense	-	206	206
Income before income tax	1,319	1,219	2,538
Deferred income tax expense <i>(note h)</i>	638	354	992
Net income and comprehensive income for the period	\$ 681	\$ 865	\$ 1,546
Earnings per share:			
Basic	\$ 0.01		\$ 0.04
Diluted	\$ 0.01		\$ 0.03

**Reconciliation of Condensed Consolidated Statement of Income and Comprehensive Income
For the Year ended December 31, 2010 from Canadian GAAP to IFRS**

(Unaudited)

(\$000s, except per share amounts)

	Canadian GAAP	Effect of Transition to IFRS	IFRS
Revenue			
Petroleum and natural gas	\$ 58,283	\$ -	\$ 58,283
Royalties	(7,529)		(7,529)
Other (note i)	249	(134)	115
	51,003	(134)	50,869
Expenses			
Operating and transportation	11,379	-	11,379
General and administrative (note i)	2,523	(248)	2,275
Capital taxes	822	-	822
Share-based payments (note d)	4,773	(108)	4,665
Depletion and depreciation (note e)	27,194	(3,194)	24,000
Gain on sale of assets (note g)	-	(7,482)	(7,482)
	46,691	(11,032)	35,659
Results from operating activities	4,312	10,898	15,210
Finance income (note i)	-	(134)	(134)
Finance expense (note b,i)	-	1,187	1,187
	-	1,053	1,053
Income before income tax	4,312	9,845	14,157
Deferred income tax expense (note h)	2,418	2,517	4,935
Net income and comprehensive income for the period	\$ 1,894	\$ 7,328	\$ 9,222
Earnings per share:			
Basic	\$ 0.04		\$ 0.19
Diluted	\$ 0.04		\$ 0.19

The Company adopted IFRS on January 1, 2011 with a transition date of January 1, 2010. Under IFRS 1 “First time adoption of International Financial Reporting Standards”, IFRS is applied retrospectively at the transition date with the offsetting adjustments to assets and liabilities included in retained earnings.

IFRS employs a conceptual framework that is similar to Canadian GAAP. While the adoption of IFRS has not changed the actual cash flows of the Company, the adoption has resulted in significant changes to the reported financial position and results of operation of the Company and immaterial changes to the makeup of operating, investing and financing cash flows.

(a) IFRS 1 election for full cost oil and gas entities

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

- (i) exploration and evaluation assets were reclassified from the full cost pool to exploration and evaluation assets at the amount that was recorded under Canadian GAAP; and
- (ii) the remaining full cost pool was allocated to the producing/development assets pro-rata using proven plus probable pre-tax reserve values based on a discount rate of 10%.

The impact on the reclassification from the full cost pool to exploration and evaluation assets on the condensed consolidated statements of financial position for the periods ended January 1, 2010, March 31, 2010 and December 31, 2010 are as follows:

Condensed Consolidated Statement of Financial Position:

(\$000s)	January 1, 2010	March 31, 2010	December 31, 2010
Exploration and evaluation	13,424	17,707	43,535
Property, plant and equipment	(13,424)	(17,707)	(43,535)
Impact on total assets	-	-	-

(b) Decommissioning obligations:

Under Canadian GAAP asset retirement obligations were discounted at a credit adjusted risk free rate of 8%. Under IFRS the estimated cash flow to abandon and remediate the wells and facilities has been risk adjusted; therefore, the provision is discounted at a risk free rate in effect at the end of each reporting period (4% for all periods presented in these notes). Upon transition to IFRS this resulted in a \$1.9 million increase in the decommissioning obligations with a corresponding increase in the deficit. As a result of the lower discount rate, the Company recorded additional decommissioning costs to PP&E and lower related accretion expense during the 2010 periods. In addition, under Canadian GAAP accretion of the discount was included in depletion and depreciation. Under IFRS it is included in finance expense.

As a result of the change in the decommissioning obligation, the impact on the consolidated statements of financial position and consolidated statements of income and comprehensive income for the periods ended January 1, 2010, March 31, 2010 and December 31, 2010 are as follows:

Condensed Consolidated Statements of Financial Position:

(\$000s)	January 1, 2010	March 31, 2010	December 31, 2010
Property, plant and equipment	-	287	1,352
Decommissioning obligations	1,851	2,132	3,175
Impact on retained earnings (deficit)	(1,851)	(1,845)	(1,823)

Condensed Consolidated Statements of Income and Comprehensive Income:

(\$000s)	March 31, 2010	December 31, 2010
Finance expense	(6)	(28)
Impact on income and comprehensive income	6	28

(c) Convertible Class B shares:

Under Canadian GAAP, the Company's convertible Class B shares were presented as share capital. Under IFRS, the Class B shares do not qualify for equity presentation and must be presented as a liability due to the number of Class A shares issued on conversion, based on the conversion formula (note 9), being variable until the Company or shareholders exercise conversion rights. The value of the Class A shares on issuance was determined to be \$5.2 million (\$1.00 per Class A share). It was also determined that the face value of convertible Class B shares is \$11.7 million (\$9.97 per Class B share). Using a 7 percent discount rate and a term of 5.21 years, the Company calculated a present value of approximately \$8.2 million on issuance, which will accrete to the \$11.7 million face value on August 1, 2012, the expiration date of the shareholder's conversion option. A deferred tax liability of \$0.9 million was recognized on issuance relating to the difference between the face value and present value of the Class B shares. The deferred tax liability is reversed proportionately to the accretion expense on the convertible Class B share liability.

The flow-through share premium of \$1.6 million was recognized for the Class A and Class B shares issued on the initial public offering. The flow-through share premium reduced share capital, and as expenditures were incurred, the premium was recorded through income. The amount recorded for the Class B equity component relates to the conversion feature of \$2.0 million, recognizing the value of the Company's lower limit of \$1.00 per Class A share in the Class B to Class A conversion formula, along with the deferred income tax effect of the Class B shares of \$0.9 million.

The following table provides the effect of transition to IFRS for the Company's share capital transactions involving convertible Class B shares from previous GAAP to IFRS at the date of transition:

<i>(\$000s)</i>	Effect of Transition to IFRS
Class A share capital	3,916
Convertible Class B share capital	(11,704)
Convertible Class B share liability	8,247
Deferred income tax liability	899
Equity component of Class B shares	(2,923)
Retained earnings	1,565
	-

In addition to the above adjustment, the Company recorded the effect of accretion expense from May 2007 through to March 31, 2011. As a result of adopting this policy, the effect of the change to accretion expense and the Class B liability was as follows:

Consolidated Statements of Financial Position:

<i>(\$000s)</i>	January 1, 2010	March 31, 2010	December 31, 2010
Impact on Convertible Class B liability	1,600	168	689

Consolidated Statements of Income and Comprehensive Income:

<i>(\$000s)</i>	March 31, 2010	December 31, 2010
Impact on Finance expense	168	689
Impact on income and comprehensive income	(168)	(689)

(d) Share-based payments:

Under Canadian GAAP, the Company recognized an expense related to share-based payments on a graded basis over individual vesting periods, but did not incorporate a forfeiture rate. Under IFRS, the Company is required to estimate a forfeiture rate and apply this to the Black-Scholes model. Furthermore, the Company has determined that option recipients classified as consultants under Canadian GAAP would not be classified as such under IFRS. The impact of the changes to share-based payments for the periods ended January 1, 2010, March 31, 2010 and December 31, 2010 are as follows:

Consolidated Statements of Financial Position:

(\$000s)	January 1, 2010	March 31, 2010	December 31, 2010
Property, plant and equipment	-	(12)	(50)
Share capital	-	-	15
Contributed surplus	43	88	186
Impact on retained earnings (deficit)	43	76	151

Consolidated Statements of Income and Comprehensive Income:

(\$000s)	January 1, 2010	March 31, 2010	December 31, 2010
Share-based payments	-	(33)	(108)
Impact on income and comprehensive income	-	33	108

(e) Depletion policy:

Upon transition to IFRS, the Company adopted a policy of depleting oil and natural gas interests on a unit of production basis over proven plus probable reserves. The depletion policy under Canadian GAAP was based on units of production over proven reserves. In addition depletion was done on the Canadian cost centre under Canadian GAAP. IFRS requires depletion and depreciation to be calculated based on a component basis, as determined by the Company. In addition, accretion expense is reported as finance expense under IFRS.

There was no impact on property, plant and equipment of the depletion policy change on adoption of IFRS at January 1, 2010, due to the IFRS 1 election discussed above. As a result of the change in policy of depleting oil and natural gas interests on a proven plus probable basis and the reclassification of accretion expense to finance expense, the impact on the condensed consolidated statements of financial position and condensed consolidated statements of income and comprehensive income for the periods ended March 31, 2010 and December 31, 2010 are as follows:

Consolidated Statements of Financial Position:

(\$000s)	March 31, 2010	December 31, 2010
Property, plant and equipment	1,298	3,194
Impact on total assets	1,298	3,194

Consolidated Statements of Income and Comprehensive Income:

(\$000s)	March 31, 2010	December 31, 2010
Depletion and depreciation expense	(1,298)	(3,194)
Impact on income and comprehensive income	1,298	3,194

(f) Flow-through shares:

In 2007, the Company issued flow-through shares where the amount of the issue represented the “flow-through” of tax pool deductions to investors. Under Canadian GAAP, the accounting treatment for the flow-through shares is to record the full amount of the proceeds in share capital. When expenditures are renounced, the related tax effect is recorded to share capital and the future tax liability. Under IFRS, the amount initially recorded in share capital is limited to the value that would have been received for shares issued on a non-flow-through basis, and the difference between the actual proceeds and the amount recorded in share capital is set up as a deferred premium on flow-through shares. When the expenditures are incurred, the related deferred premium on flow-through shares is reversed and the related tax effect is recorded to the deferred income tax liability (see note 20 (c)).

(g) Gains and losses on disposition of assets:

Under Canadian GAAP, proceeds from asset sales were deducted from the full cost pool without recognition of a gain or loss unless the deduction resulted in a change in the depletion rate of 20 percent or greater, in which case a gain or loss was recorded. Under IFRS, gains and losses are recorded on asset sales and are calculated as the difference between the proceeds and the net book value of the asset disposed. For the periods ended March 31, 2010 and December 31, 2010, the Company recognized gains of \$0.1 million and \$7.5 million, respectively, on farm out's of certain lands held by the Company.

(h) Income taxes:

Deferred income taxes have been adjusted to reflect the tax effect arising from the differences between IFRS and Canadian GAAP. The application of the IFRS adjustments for note 20 (a) through to (g) resulted in the following impact for the periods ended January 1, 2010, March 31, 2010 and December 31, 2010 as follows:

Consolidated Statements of Financial Position:

(\$000s)	January 1, 2010	March 31, 2010	December 31, 2010
Property, plant and equipment	-	(140)	(468)
Deferred income tax asset (liability)			
Related to property, plant and equipment	-	(335)	(2,590)
Related to decommissioning obligations	478	552	820
Related to convertible Class B shares	(511)	(464)	(312)
Impact on retained earnings (deficit)	(33)	(387)	(2,550)

Consolidated Statements of Income and Comprehensive Income:

(\$000s)	March 31, 2010	December 31, 2010
Deferred income tax expense	354	2,517
Impact on income and comprehensive income	(354)	(2,517)

Corporate Information

BOARD OF DIRECTORS

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Calgary, Alberta

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Vice President, Exploration
Surge Energy Inc.
Calgary, Alberta

Allan K. Ashton
Chairman of the Board
Ashton Petroleum Consultants
Priddis, Alberta

Glenn R. Carley
Executive Chairman & Director
Galleon Energy Inc.
Calgary, Alberta

Arthur J. G. Madden
Chief Financial Officer
Crown Point Ventures Ltd.
Calgary, Alberta

Patrick R. Ward
President & Chief Executive Officer
Painted Pony Petroleum Ltd.
Calgary, Alberta

HEAD OFFICE

300, 602 – 12 Ave SW
Calgary, Alberta T2R 1J3
Phone: (403) 475-0440
Fax: (403) 238-1487
Email: info@paintedpony.ca
Toll Free Investor: 1 (866) 975-0440
Website: www.paintedpony.ca

EXCHANGE LISTING

The TSX Venture Exchange
Trading symbols:

Class A Shares: PPY.A
Class B Shares: PPY.B

OFFICERS

Patrick R. Ward
President and Chief Executive Officer

Joan E. Dunne
Vice President, Finance and Chief Financial Officer

Michael E. Belenkie
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Mary Kay Axford
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Douglas T. McCartney
Partner, Burstall Winger LLP
Corporate Secretary

LEGAL COUNSEL

Burstall Winger LLP

AUDITORS

KPMG LLP

BANKERS

National Bank of Canada

EVALUATION ENGINEERS

Sproule Associates Limited

REGISTRAR AND TRANSFER AGENT

Olympia Trust Company
Calgary, Alberta
1 800 727-4493
Enquiries: cssinquiries@olympiatrust.com