

## Consolidated Statements of Financial Position

(Unaudited)

Stated in thousand of dollars

As at	March 31, 2012	December 31, 2011
<b>Assets</b>		
Current Assets		
Accounts receivable	23,857	19,512
Prepaid expenses and deposits	3,419	4,948
	<b>27,276</b>	24,460
Exploration and evaluation assets (note 4)	57,800	47,719
Petroleum and natural gas properties (note 5)	597,334	437,854
Goodwill (note 4)	5,934	6,029
	<b>\$ 688,344</b>	\$ 516,062
<b>Liabilities</b>		
Current liabilities		
Accounts payable and accrued liabilities	\$ 64,380	\$ 49,467
Fair value of financial contracts (note 6)	\$ 1,741	2,151
	<b>66,121</b>	51,618
Fair value of financial contracts (note 6)	5,982	2,751
Bank debt (note 7)	121,665	72,197
Decommissioning obligations	39,378	37,511
Deferred income taxes	54,737	27,829
<b>Shareholders' equity</b>		
Share capital (note 8)	350,152	278,302
Contributed surplus	15,059	12,879
Performance warrants (note 8)	7,196	7,196
Accumulated other comprehensive income	623	1,005
Retained earnings	27,431	24,774
	<b>400,461</b>	324,156
Subsequent event (note 9)		
	<b>\$ 688,344</b>	\$ 516,062

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

## Consolidated Statements of Income (Loss) and Comprehensive Income (Loss)

(Unaudited)

Stated in thousands of dollars, except per share amounts

	Three months ended March 31,	
	2012	2011
<b>Revenues</b>		
Petroleum and natural gas	\$ 51,060	\$ 25,872
Royalties	(10,017)	(3,665)
Realized loss on financial contracts (note 6)	(770)	(740)
Unrealized loss on financial contracts (note 6)	(2,821)	(2,607)
	<b>37,452</b>	<b>18,860</b>
<b>Expenses</b>		
Operating	9,556	7,642
Transportation	1,458	1,162
General and administrative	2,972	2,175
Transaction costs	363	87
Stock-based compensation	966	723
Depletion and depreciation	16,890	8,303
Finance expense	1,688	709
Gain on disposal of petroleum and natural gas properties	-	(1,513)
	<b>33,893</b>	<b>19,288</b>
Income (loss) before income taxes	<b>3,559</b>	<b>(428)</b>
Deferred income taxes	<b>902</b>	<b>74</b>
<b>Net income (loss) for the year</b>	<b>\$ 2,657</b>	<b>\$ (502)</b>
<b>Other comprehensive income:</b>		
Currency translation adjustment	(382)	-
<b>Other comprehensive income for the period</b>	<b>(382)</b>	<b>-</b>
<b>Total comprehensive income (loss) for the period</b>	<b>\$ 2,275</b>	<b>\$ (502)</b>
Income (loss) per share (note 8)		
Basic	\$ 0.04	\$ (0.01)
Diluted	\$ 0.04	\$ (0.01)

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

**Consolidated Statement of Changes in Shareholders' Equity**

(Unaudited)

Stated in thousands of dollars, except share amounts

	Number of common shares	Share capital	Contributed surplus	Performance warrants	Accumulated other comprehensive income	Retained earnings	Total equity
Balance at December 31, 2010	56,094,548	\$ 220,845	\$ 4,664	\$ 7,196	\$ -	\$ 22,679	\$ 255,384
Net loss for the period	-	-	-	-	-	(502)	(502)
Stock-based compensation	-	-	1,696	-	-	-	1,696
Transfer on exercise of options	-	2	(2)	-	-	-	-
Options exercised	2,000	22	-	-	-	-	22
<b>Balance at March 31, 2011</b>	<b>56,096,548</b>	<b>\$ 220,869</b>	<b>\$ 6,358</b>	<b>\$ 7,196</b>	<b>\$ -</b>	<b>\$ 22,177</b>	<b>\$ 256,600</b>
Balance at December 31, 2011	63,040,987	278,302	12,879	7,196	1,005	24,774	\$ 324,156
Net income for the period	-	-	-	-	-	2,657	2,657
Issued pursuant to acquisition	7,919,436	71,275	-	-	-	-	71,275
Accumulated other comprehensive income	-	-	-	-	(382)	-	(382)
Share issue costs (net of tax of \$30)	-	(88)	-	-	-	-	(88)
Stock-based compensation	-	-	2,420	-	-	-	2,420
Transfer on exercise of options & warrants	-	240	(240)	-	-	-	-
Options exercised	67,999	400	-	-	-	-	400
Warrants exercised	4,545	23	-	-	-	-	23
<b>Balance at March 31, 2012</b>	<b>71,032,967</b>	<b>\$ 350,152</b>	<b>\$ 15,059</b>	<b>\$ 7,196</b>	<b>\$ 623</b>	<b>\$ 27,431</b>	<b>\$ 400,461</b>

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

## Consolidated Statements of Cash Flows

(Unaudited)

Stated in thousands of dollars

	Three months ended March 31,	
	2012	2011
Cash provided by (used in)		
<b>Operating</b>		
Net income (loss)	\$ 2,657	\$ (502)
Gain on disposal of petroleum and natural gas properties	-	(1,513)
Unrealized loss on financial contracts	2,821	2,607
Finance expense	1,688	709
Interest expense	(1,433)	(448)
Depletion and depreciation	16,890	8,303
Decommissioning expenditures	(484)	(181)
Stock-based compensation	966	723
Deferred income taxes	902	74
Change in non-cash working capital	(2,136)	(765)
Cash flow from operating activities	21,871	9,007
<b>Financing</b>		
Bank debt	34,845	32,369
Issues of common shares and performance warrants, net of issue costs	305	22
Cash flow from financing activities	35,150	32,391
<b>Investing</b>		
Petroleum and natural gas properties	(45,286)	(35,539)
Exploration and evaluation assets	(9,612)	(10,762)
Disposition of petroleum and natural gas properties	-	1,301
Acquisitions (note 3)	(18,500)	-
Change in non-cash working capital	16,377	2,165
Cash flow used in investing activities	(57,021)	(42,835)
Change in cash	-	(1,437)
Cash, beginning of period	-	1,437
<b>Cash, end of period</b>	\$ -	\$ -

Cash is defined as cash and cash equivalents.

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

## NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS

Tabular amounts are in thousands of dollars, except share and per share data

(Unaudited)

### 1. REPORTING ENTITY

Surge Energy Inc.'s (the "Corporation" or "Surge") business consists of the exploration, development and production of oil and gas from properties in western Canada and the northern United States. The interim consolidated financial statements include the accounts of the Corporation, its wholly-owned subsidiaries and partnerships.

### 2. BASIS OF PREPARATION

#### Statement of compliance

These interim consolidated financial statements have been prepared in accordance with International Accounting Standard 34, "Interim Financial Reporting" and using the accounting policies outlined by the Corporation in its annual consolidated financial statements for the year ended December 31, 2011. These interim consolidated financial statements do not include all of the information required for full annual financial statements.

The interim consolidated financial statements were authorized for issuance by the Board of Directors on May 8, 2012.

### 3. ACQUISITION

#### (a) Pradera Resources Inc.

Effective January 6, 2012, the Corporation acquired all of the issued and outstanding common shares Pradera Resources Inc. ("Pradera"), a privately held junior oil and gas exploration company, in exchange 7,919,436 common shares of Surge with an assigned value of \$71.3 million. The purpose of the acquisition was to expand the Corporation's exposure to certain light oil plays. The common shares have been ascribed a fair value of \$9.00 per common share issued, as determined based on the Corporation's closing share price at the date of closing, being January 6, 2012. In addition, Surge incurred transaction costs of \$0.4 million, which were expensed through the statement of income. The operations of Pradera have been included in the results of Surge commencing January 6, 2012. The transaction was accounted for by the purchase method. The allocation of the purchase price, based on management's estimates of fair values, is as follows:

<b>Fair value of net assets acquired:</b>	
Petroleum and natural gas properties	\$ 127,230
Exploration and evaluation assets	2,660
Current assets	5,948
Current liabilities	(3,796)
Bank debt	(14,623)
Decommissioning obligations	(1,608)
Deferred income tax liability	(26,036)
<b>Net assets acquired</b>	<b>\$ 89,775</b>
<b>Consideration:</b>	
Cash	\$ 18,500
Common shares (7,919,436 at \$9.00 per share)	71,275
<b>Total consideration paid</b>	<b>\$ 89,775</b>

Included in the 2012 interim consolidated statement of income and comprehensive income are the following amounts:

<b>Amounts since acquisition</b>	
Revenue	\$ 8,932
Income and comprehensive income	2,577

#### 4. EXPLORATION AND EVALUATION ASSETS AND GOODWILL

Exploration and evaluation (E&E) assets consist of the Corporation's exploration projects which are pending the determination of proven or probable reserves. Additions represent the Corporation's share of costs incurred on E&E assets during the period.

##### Exploration & Evaluation Assets

	Total
<b>Cost:</b>	
Balance at December 31, 2011	\$47,719
Acquisitions (note 3)	2,660
Additions	9,612
Change in foreign exchange rate	(143)
Transfer to petroleum and natural gas properties	(2,048)
<b>Balance at March 31, 2012</b>	<b>\$57,800</b>

##### Goodwill

	Total
<b>Cost</b>	
Balance at December 31, 2011	\$6,029
Change in foreign exchange rate	(95)
<b>Balance at March 31, 2012</b>	<b>\$5,934</b>

#### 5. PETROLEUM AND NATURAL GAS PROPERTIES

	Total
<b>Cost or deemed cost</b>	
Balance at December 31, 2011	\$ 504,802
Acquisitions (note 3)	127,230
Additions	45,779
Transfer from exploration and evaluation assets	2,048
Capitalized stock-based compensation	1,454
Change in foreign exchange rate	(141)
<b>Balance at March 31, 2012</b>	<b>\$ 681,172</b>

	Total
<b>Accumulated depletion and depreciation</b>	
Balance at December 31, 2011	(\$66,948)
Depletion and depreciation expense	(16,890)
<b>Balance at March 31, 2012</b>	<b>(\$83,838)</b>

	Total
<b>Carrying amounts</b>	
At December 31, 2011	437,854
<b>At March 31, 2012</b>	<b>597,334</b>

The calculation of depletion and depreciation expense for the three months ended March 31, 2012 included an estimated \$155.6 million (March 31, 2011 - \$79.4 million) for future development costs associated with proved plus probable reserves and excluded \$30.5 million (March 31, 2011 - \$27.0 million) for the estimated salvage value of production equipment and facilities.

## 6. RISK MANAGEMENT CONTRACTS

As a means of managing commodity price and interest rate volatility, the Corporation enters into various derivative financial instrument agreements and physical contracts. The fair value of forward contracts and swaps is determined by discounting the difference between the contracted prices and published forward price curves as at the statement of financial position date, using the remaining contracted oil and natural gas volumes and a risk-free interest rate (based on published government rates). The fair value of options and costless collars is based on option models that use published information with respect to volatility, prices and interest rates.

The following table outlines the realized and unrealized gains (losses) on oil and gas commodity contracts for the three months ended March 31, 2012:

Term	Type (floating to fixed)	Volume	Swap Price (Surge receives) (C\$)	Index (Surge pays) (C\$)	Three months Mar 31, 2012	
					Unrealized gains (losses) (\$000s CDN)	Realized gains (losses) (\$000s CDN)
Jan 1 to Dec 31, 2012	Swap	250 bbls/d	\$ 97.00	WTI - NYMEX	(176)	(138)
Jan 1 to Dec 31, 2012	Call	63 bbls/d	\$ 80.00	WTI - NYMEX	570	-
Jan 1 to Dec 31, 2012	Put	250 bbls/d	\$ 80.00	WTI - NYMEX	(638)	(131)
Jan 1 to Dec 31, 2012	Call	250 bbls/d	\$ 89.95	WTI - NYMEX	(258)	298
Jan 1 to Dec 31, 2012	Swap	250 bbls/d	\$ 80.00	WTI - NYMEX	207	(525)
Jan 1 to Dec 31, 2012	Put	250 bbls/d	\$ 90.00	WTI - NYMEX	(804)	(110)
Jan 1 to Dec 31, 2012	Call	93 bbls/d	\$ 90.00	WTI - NYMEX	624	-
Jan 1 to Dec 31, 2012	Put	500 bbls/d	\$ 90.00	WTI - NYMEX	(1,486)	(187)
Jan 1 to Dec 31, 2012	Call	158 bbls/d	\$ 90.00	WTI - NYMEX	1,098	-
Jan 1 to Dec 31, 2012	Call	500 bbls/d	\$ 96.00	WTI - NYMEX	(242)	321
Jan 1 to Dec 31, 2012	Swap	500 bbls/d	\$ 85.00	WTI - NYMEX	189	(822)
Jan 1 to Dec 31, 2013	Call	250 bbls/d	\$ 98.00	WTI - NYMEX	1,260	-
Jan 1 to Dec 31, 2013	Swap	250 bbls/d	\$ 85.00	WTI - NYMEX	(1,469)	-
Apr 1 to Dec 31, 2012	Swap	500bbls/d	\$ 101.50	WTI - NYMEX	(427)	-
Apr 1 to Dec 31, 2012	Swap	500bbls/d	\$ 90.00	WTI - NYMEX	(1,996)	-
Apr 1 to Dec 31, 2012	Call	500bbls/d	\$ 96.00	WTI - NYMEX	1,523	-
Jan 1 to Dec 31, 2013	Swap	250bbls/d	\$ 98.00	WTI - NYMEX	(576)	-
Jan 1 to Dec 31, 2013	Swap	250bbls/d	\$ 95.00	WTI - NYMEX	(845)	-
Jan 1 to Mar 31, 2013	Swap	250bbls/d	\$ 104.85	WTI - NYMEX	(17)	-
Jan 1 to Mar 31, 2013	Swap	500bbls/d	\$ 95.00	WTI - NYMEX	230	-
Jan 1 to Mar 31, 2013	Call	315bbls/d	\$ 95.00	WTI - NYMEX	(259)	-
Apr 1 to Jun 30, 2013	Swap	250bbls/d	\$ 105.05	WTI - NYMEX	2	-
Apr 1 to Jun 30, 2013	Swap	500bbls/d	\$ 95.00	WTI - NYMEX	(445)	-
Apr 1 to Jun 30, 2013	Call	300bbls/d	\$ 95.00	WTI - NYMEX	422	-
<b>Total</b>					<b>\$ (3,513)</b>	<b>\$ (1,294)</b>



Term	Type (floating to fixed)	Volume	Differential (Surge receives) (C\$)	Index (Surge pays) (C\$)	Three months March 31, 2012	
					Unrealized gains (losses) (\$000s CDN)	Realized gains (losses) (\$000s CDN)
Jan 1 to Mar 31, 2012	Swap	500 bbls/d	\$ 13.25	Western Canadian Select	(104)	\$373
Jan 1 to Jun 30, 2012	Swap	250 bbls/d	\$ 14.85	Western Canadian Select	303	151
<b>Total</b>					<b>\$ 199</b>	<b>\$ 524</b>

The following table outlines the realized and unrealized losses on interest rate contracts for three months ended March 31, 2012:

Term	Type (floating to fixed)	Amount (C\$)	Company Fixed Interest Rate (%) <sup>(1)</sup>	Counter party Floating Rate Index	Three months ended March 31, 2012	
					Unrealized gain (loss) (\$000s CDN)	Realized gain (loss) (\$000s CDN)
Jan 1, 2012 to Dec 31, 2014	Swap	\$ 50,000,000	2.74%	CAD-BA-CDOR	493	-

(1) The interest rate hedge is comprised of a range, beginning at 1.439% and escalating quarterly to a maximum of 3.952%.

The following table summarizes the sensitivity of the fair value of the Corporation's market risk management positions to fluctuations in interest rates, crude oil, and natural gas prices. Both such fluctuations were evaluated independently, with all other variables held constant. In assessing the potential impact of these fluctuations, the Corporation believes that the volatilities presented below are reasonable measures. Fluctuations in interest rates, crude oil and natural gas prices, which would impact the mark-to-market calculation of commodity contracts, could have had the following impact on the net earnings:

Net Earnings Impact for the Three Months ended March 31, 2012		
	Price Increase	Price Decrease
Crude Oil - Change of +/- \$1.00	\$ (881)	\$ 881
Interest rate - Change of +/- 100 points	\$ (375)	\$ 375

## 7. BANK DEBT

In connection with the closing of the Pradera Acquisition, as detailed in Note 3, the Corporation increased its revolving term credit facility from \$150 million to \$175 million. Subsequent to March 31, 2012 the Corporation further increased its credit facility from \$175 million to \$250 million. The facility had an effective interest rate of prime plus 1.25 percent as at March 31, 2012 (March 31, 2011 – prime plus 1.50 percent). The facility's next scheduled review is required before November 1, 2012.

## 8. SHARE CAPITAL.

### (a) Stock Options

Under the Corporation's stock option plan, it may grant options to its officers, directors, employees and certain consultants for up to 7,103,297 common shares of the Corporation as at March 31, 2012. The exercise price of each option equals the market price of the Corporation's common shares at the date of grant. Options granted have a term of five years to maturity and vest as to one-third on each of the first, second and third anniversaries from the date of grant.

	March 31, 2012		December 31, 2011	
	Number of Options	Weighted average exercise price	Number of Options	Weighted average exercise price
Stock options outstanding, beginning of period	4,948,999	\$ 7.54	2,683,667	\$ 6.24
Granted	154,000	\$ 9.88	2,355,500	\$ 8.92
Exercised	(67,999)	\$ 5.86	(47,168)	\$ 3.95
Forfeited	(27,500)	\$ 6.09	(43,000)	\$ 5.96
Stock options outstanding, end of period	5,007,500	\$ 7.64	4,948,999	\$ 7.54
Exercisable at period-end	976,653	\$ 6.37	899,484	\$ 6.10

The following table summarizes stock options outstanding and exercisable at March 31, 2012:

Range of exercise prices	Options Outstanding			Options Exercisable		
	Number outstanding	Weighted average exercise price	Weighted average contractual life (years)	Number exercisable	Weighted average exercise price	
\$1 to \$2.99	26,667	\$ 1.75	1.70	26,667	\$ 1.75	
\$3 to \$4.99	39,000	\$ 3.20	2.73	39,000	\$ 3.20	
\$5 to \$6.99	2,422,999	\$ 6.40	3.32	767,317	\$ 6.42	
\$7 to \$8.99	740,334	\$ 8.11	3.96	143,669	\$ 7.80	
\$9 to \$11.15	1,778,500	\$ 9.33	4.38	-	\$ -	
\$1 to \$11.15	5,007,500	\$ 7.64	3.78	976,653	\$ 6.37	

### (b) Performance warrants

The Corporation has 2,069,319 performance warrants outstanding (December 31, 2011 – 2,073,864) that expire on April 13, 2015. As at March 31, 2012, all 2,069,319 performance warrants were vested and exercisable at a price of \$5.17.

### (c) Per share amounts

The following table summarizes the shares used in calculating the income per share:

	March 31, 2012	March 31, 2011
Weighted average number of shares - basic	70,474,105	56,094,747
Effect of dilutive stock options	1,711,244	-
Weighted average number of shares - diluted	72,185,349	56,094,747

In computing diluted per share amounts at March 31, 2012, 52,099 options (March 31, 2011 – 3,081,667) and nil performance warrants (March 31, 2011 – 2,076,136) were excluded from the calculation as their effect was anti-dilutive.

## 9. SUBSEQUENT EVENT

(a) Subsequent to the first quarter, Surge entered into the following financial oil pricing contracts:

Term	Type	Volume	Price (C\$) (Surge Receives)	Index (Surge pays) (C\$)
1) Jan 1, 2013 - Jun 30, 2013	Swap	500bbls/d	90.00	WTI - NYMEX
Jan 1, 2013 - Jun 30, 2013	Call	380bbls/d	90.00	WTI - NYMEX
2) Jul 1, 2012 - Dec 31, 2012	Swap	500bbls/d	95.00	WTI - NYMEX
Jul 1, 2012 - Dec 31, 2012	Call	500bbls/d	99.80	WTI - NYMEX
3) Jan 1, 2013 - Mar 31, 2013	Swap	500bbls/d	95.00	WTI - NYMEX
Jan 1, 2013 - Mar 31, 2013	Call	500bbls/d	103.70	WTI - NYMEX
4) Jan 1, 2013 - Jun 30, 2013	Swap	1,000bbls/d	90.00	WTI - NYMEX
Jan 1, 2013 - Jun 30, 2013	Call	1,000bbls/d	96.00	WTI - NYMEX

(b) Subsequent to the first quarter, Surge entered into the following financial oil differential contracts:

Term	Type	Volume	Differential (C\$) (Surge Receives)	Index (Surge pays) (C\$)
1) Jun 1, 2012 - Sep 30, 2012	Swap	500bbls/d	20.25	Western Canadian Select
2) Jun 1, 2012 - Jun 30, 2012	Swap	750bbls/d	17.50	Western Canadian Select