

# Bonterra Energy Corp.



## Third Quarter 2010

### HIGHLIGHTS

(\$ 000s except \$ per share)	Three Months Ended		Nine Months Ended	
	Sept. 30, 2010	Sept. 30, 2009	Sept. 30, 2010	Sept. 30, 2009
<b>FINANCIAL</b>				
Revenue – oil and gas sales	<b>28,332</b>	20,965	<b>84,771</b>	60,766
Funds flow <sup>(1)</sup>	<b>19,622</b>	10,753	<b>58,498</b>	28,909
Per share – basic	<b>1.04</b>	0.58	<b>3.12</b>	1.62
Per share – diluted	<b>1.01</b>	0.57	<b>3.04</b>	1.62
Payout ratio <sup>(2)</sup>	<b>63%</b>	76%	<b>60%</b>	75%
Cash flow from operations	<b>17,558</b>	9,350	<b>49,275</b>	25,225
Per share – basic	<b>0.93</b>	0.50	<b>2.63</b>	1.42
Per share – diluted	<b>0.91</b>	0.50	<b>2.56</b>	1.42
Payout ratio <sup>(2)</sup>	<b>71%</b>	87%	<b>71%</b>	85%
Cash dividends per share <sup>(2)</sup>	<b>0.66</b>	0.44	<b>1.87</b>	1.20
Net earnings	<b>12,724</b>	5,790	<b>35,651</b>	16,427
Per share – basic	<b>0.68</b>	0.31	<b>1.90</b>	0.92
Per share – diluted	<b>0.66</b>	0.31	<b>1.85</b>	0.92
Capital expenditures and acquisitions net of disposals	<b>19,227</b>	17,660	<b>45,362</b>	22,616
Total assets			<b>318,493</b>	273,543
Working capital deficiency			<b>17,891</b>	14,455
Long-term debt			<b>73,901</b>	81,386
Shareholders' equity			<b>128,492</b>	74,025
<b>OPERATIONS</b>				
Oil and NGLs – barrels per day	<b>3,890</b>	3,084	<b>3,705</b>	3,126
– average price (\$ per barrel)	<b>68.79</b>	65.38	<b>71.40</b>	56.90
Natural gas – MCF per day	<b>10,674</b>	10,881	<b>10,625</b>	11,433
– average price (\$ per MCF)	<b>3.74</b>	3.13	<b>4.25</b>	3.97
Total barrels of oil equivalent per day (BOE) <sup>(3)</sup>	<b>5,669</b>	4,898	<b>5,476</b>	5,032

<sup>(1)</sup> Funds flow is not a recognized measure under GAAP. For these purposes, the Company defines funds flow as funds provided by operations before changes in non-cash operating working capital items but including gain on sale of property and investments, adjustments of investment tax credit receivable and excluding restricted cash recoveries and asset retirement expenditures.

<sup>(2)</sup> Cash payments per share are based on payments made in respect of production months within the quarter.

<sup>(3)</sup> BOE is calculated using a conversion ratio of 6 MCF to 1 barrel of oil. The conversion is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead and as such may be misleading if used in isolation.

## REPORT TO SHAREHOLDERS

Bonterra Energy Corp. (“Bonterra” or “the Company”) is pleased to announce its financial and operational results for the three months and nine months ended September 30, 2010.

### Highlights

- Produced 5,669 BOE per day, an increase of approximately 16 percent compared to the third quarter of 2009;
- Generated cash flow from operations of \$17.6 million in the third quarter of 2010 or \$0.93 per share, an increase of 88 percent per share compared to the third quarter of 2009;
- Capital expenditures for the first nine months of 2010 totaled \$51.6 million net of drilling tax credits related mainly to the drilling, completing, tie-in and equipping of 18 gross (16.0 net) operated Pembina Cardium horizontal wells with a 100 percent success rate;
- Maintained the monthly dividend at \$0.22 per share which represents a payout ratio of 60 percent of funds flow and 71 percent of cash flow;
- Debt, net of working capital, was \$91.8 million on September 30, 2010, compared to \$70.0 million on December 31, 2009. The annualized debt to funds flow ratio for 2010 is 1.18 times.

### Operations

The Company continued to execute its targeted Pembina Cardium drilling program during the third quarter. Bonterra drilled eight gross (6.9 net) operated horizontal oil wells and participated in three gross (0.45 net) non-operated horizontal wells and two gross (0.3 net) non-operated vertical oil wells in Q3 2010.

However, due to exceedingly wet weather conditions during the quarter, the Company experienced significant delays in bringing these wells on production. Bonterra was only able to place three of the operated horizontal wells and four of the non-operated wells on production for a portion of the third quarter. As of September 30, 2010, the Company had seven gross (6.18 net) horizontal wells drilled but not yet on production. During Q4 2010, Bonterra has been able to place six of these wells on production with the remaining well currently waiting on a third party tie-in.

During the quarter, a number of the Company’s natural gas wells were shut in due to overcapacity at one of the non-operated plants to which Bonterra delivers a portion of its natural gas production resulting in a loss of approximately 110 BOE per day during the quarter. As a result of these weather delays and shut ins, the Company’s production levels decreased slightly on a quarter over quarter basis, to 5,669 BOE per day compared with 5,733 BOE per day in the second quarter. Bonterra’s production volumes of 5,476 BOE per day for the first nine months of 2010 are an increase of approximately nine percent compared to the same period in 2009. The improved production levels were due mainly to the additional production associated with the Company’s horizontal Cardium drilling program.

The Company has increased its capital development budget for 2010 to approximately \$65 million to \$69 million net of drilling credits which includes the drilling of an additional five gross and net operated and two gross (0.3 net) non-operated Pembina Cardium horizontal wells in the fourth quarter of 2010.

In light of the weather related delays and postponement of capital spending and production growth into the fourth quarter, Bonterra has reduced its full year guidance to a range of 5,500 to 5,800 BOE per day. Bonterra remains highly optimistic with regard to its deep inventory of lower-risk, oil opportunities in the Pembina Cardium. The Company’s large resource position and above industry average results with its horizontal drilling program positions the Company well and Bonterra now anticipates that production levels will demonstrate exceptional levels of growth in 2011. The Board of Directors and management are currently assessing the 2011 budget and capital development plans and will release details in the fourth quarter or early 2011.

**Financial**

Oil and natural gas prices decreased quarter over quarter. The Company's average realized price for crude oil and natural gas liquids in the third quarter was \$68.79 per barrel as compared to \$71.09 per barrel in the second quarter of the year. Likewise, natural gas prices decreased to \$3.74 per MCF as compared to \$3.97 MCF in the prior quarter.

Despite the lower prices received during the quarter, revenue remained relatively stable and cash flow from operations increased 5.5 percent quarter over quarter while providing significant growth on a year over year basis. For the nine month periods, the Company recorded a 39.5 percent increase in revenue and a 95.3 percent increase in cash flow from operations in 2010 compared to the same period in 2009, mainly due to a nine percent increase in production levels and a 25.4 percent increase in crude oil prices in 2010 compared to 2009.

Subsequent to quarter end, the Company has begun to realize higher crude oil pricing while natural gas has continued to decline due mainly to the current large oversupply in North American markets. As Bonterra's production is weighted approximately 70 percent to crude oil and liquids along with a capital development program that is focused exclusively on light oil prospects, the Company expects to incur further benefits from the stronger crude oil markets.

The Board of Directors and management have maintained the monthly dividend level to shareholders at \$0.22 per share including the recently announced October dividend payable on November 30, 2010. Dividends to shareholders during the first nine months of 2010 totaled \$1.83 per share, a 53 percent increase from the 2009 level. This represents a payout ratio of 60 percent of funds flow. The Company's Board and management will continue to consider production volumes and commodity prices in determining monthly dividend amounts. There remains good potential to increase the dividend level in the near future should the current strengthened crude oil pricing environment persist coupled with the expected production level increases.

The Company continues to effectively manage its balance sheet strength and remains well positioned to fund the remaining balance of its 2010 capital program out of cash flow, proceeds from the exercising of stock options, sale of investments and the Company's line of credit. As at September 30, 2010, Bonterra had approximately \$46.1 million available under its \$120 million revolving credit facility.

**Outlook**

Bonterra remains pleased with the progress it has made on its Pembina Cardium horizontal program and will continue to pursue the aggressive development of its opportunities in the field. The Company has a 14 year drilling inventory with 435 gross locations already identified including 75 gross horizontal locations in the Halo area of the Pembina field.

It is difficult to predict when natural gas prices might recover but this low price environment may provide opportunities for the Company to further grow its asset base through acquisitions. Bonterra has historically made acquisitions counter-cyclically and this strategic approach remains significant in today's marketplace.

Bonterra will continue to execute its longterm strategy to maximize shareholder returns through prudent financial management while conservatively growing the Company with a targeted exploitation and development program. Bonterra remains well-positioned to continue paying a high dividend, maintaining the long-term sustainability of its business and providing superior value to its shareholders.



George F. Fink  
Chief Executive Officer and Director



Randy M. Jarock  
President and Chief Operating Officer

## MANAGEMENT'S DISCUSSION AND ANALYSIS

The following report dated November 10, 2010 is a review of the operations and current financial position for Bonterra Energy Corp. ("Bonterra" or "the Company") and should be read in conjunction with the unaudited financial statements for the nine months ended September 30, 2010, including the notes related thereto, and the audited financial statements for the fiscal year ended December 31, 2009, together with the notes related thereto.

### Non-GAAP Measures

Throughout this Management's Discussion and Analysis (MD&A) we use the terms "payout ratio" and "cash netback" to analyze operating performance. We calculate payout ratio by dividing cash dividends to shareholder by cash flow from operating activities both of which are measures prescribed by GAAP which appear on our consolidated statements of cash flows. We calculate cash netback by dividing various operation and deficit statement items as determined by GAAP by total production on a barrel of oil equivalent basis.

### Forward-looking Information

Certain statements contained in this MD&A include statements which contain words such as "anticipate", "could", "should", "expect", "seek", "may", "intend", "likely", "will", "believe" and similar expressions, relating to matters that are not historical facts, and such statements of our beliefs, intentions and expectations about development, results and events which will or may occur in the future, constitute "forward-looking information" within the meaning of applicable Canadian securities legislation and are based on certain assumptions and analysis made by us derived from our experience and perceptions. Forward-looking information in this MD&A includes, but is not limited to: expected cash provided by continuing operations; cash dividends; future capital expenditures, including the amount and nature thereof; oil and natural gas prices and demand; expansion and other development trends of the oil and gas industry; business strategy and outlook; expansion and growth of our business and operations; and maintenance of existing customer, supplier and partner relationships; supply channels; accounting policies; credit risks; and other such matters.

All such forward-looking information is based on certain assumptions and analyses made by us in light of our experience and perception of historical trends, current conditions and expected future developments, as well as other factors we believe are appropriate in the circumstances. The risks, uncertainties, and assumptions are difficult to predict and may affect operations, and may include, without limitation: foreign exchange fluctuations; equipment and labour shortages and inflationary costs; general economic conditions; industry conditions; changes in applicable environmental, taxation and other laws and regulations as well as how such laws and regulations are interpreted and enforced; the ability of oil and natural gas companies to raise capital; the effect of weather conditions on operations and facilities; the existence of operating risks; volatility of oil and natural gas prices; oil and gas product supply and demand; risks inherent in the ability to generate sufficient cash flow from operations to meet current and future obligations; increased competition; stock market volatility; opportunities available to or pursued by us; and other factors, many of which are beyond our control.

Actual results, performance or achievements could differ materially from those expressed in, or implied by, this forward-looking information and, accordingly, no assurance can be given that any of the events anticipated by the forward-looking information will transpire or occur, or if any of them do, what benefits will be derived there from. Except as required by law, Bonterra disclaims any intention or obligation to update or revise any forward-looking information, whether as a result of new information, future events or otherwise.

The forward-looking information contained herein is expressly qualified by this cautionary statement.

## FINANCIAL AND OPERATIONAL DISCUSSION

### Quarterly Comparisons

Financial (\$ 000s except \$ per share)	2010				2009		
	Q3	Q2	Q1	Q4	Q3	Q2	Q1
Revenue – oil and gas sales	28,332	29,191	27,248	24,946	20,965	20,501	19,300
Cash flow from operations	17,558	16,644	15,073	13,668	9,350	9,238	6,637
Per share – basic	0.93	0.89	0.81	0.76	0.50	0.52	0.38
Per share – diluted	0.91	0.86	0.79	0.75	0.50	0.52	0.38
Cash Dividends <sup>(1)</sup>	0.66	0.64	0.57	0.50	0.44	0.40	0.36
Payout Ratio <sup>(1)</sup>	71%	72%	70%	66%	87%	77%	94%
Net earnings	12,724	10,887	12,040	52,136	5,790	4,544	6,093
Per share – basic	0.68	0.58	0.64	2.88	0.32	0.26	0.35
Per share – diluted	0.66	0.56	0.63	2.85	0.32	0.26	0.35
Capital expenditures and acquisitions net of disposals	19,227	10,994	15,141	(16,976)	17,660	2,255	2,701
Total assets	318,493	307,934	305,440	293,987	273,543	258,393	260,732
Working capital deficiency	17,891	2,281	13,178	10,162	14,455	13,989	14,909
Bank debt	73,901	78,434	63,097	59,823	81,386	71,573	89,383
Shareholders' equity	128,492	126,045	125,392	118,874	74,025	72,332	56,377
Operations							
Oil and NGLs (barrels per day)	3,890	3,874	3,345	3,182	3,084	3,029	3,268
Natural gas (MCF per day)	10,674	11,157	10,038	10,193	10,881	11,551	11,877
Total BOE per day <sup>(2)</sup>	5,669	5,733	5,018	4,881	4,898	4,954	5,245

Financial (\$ 000s except \$ per share/unit)	2008			
	Q4	Q3	Q2	Q1
Revenue – realized oil and gas sales	22,613	34,226	34,398	30,493
Cash flow from operations	10,336	22,492	20,530	16,212
Per share/unit – basic	0.59	1.31	1.21	0.96
Per share/unit – diluted	0.59	1.30	1.20	0.96
Cash payments per share/unit <sup>(1)</sup>	0.62	0.96	0.84	0.70
Payout Ratio <sup>(1)</sup>	105%	73%	69%	73%
Net earnings	10,585	21,125	12,912	10,804
Per share/unit – basic	0.62	1.23	0.76	0.64
Per share/unit – diluted	0.62	1.22	0.75	0.64
Capital expenditures and acquisitions net of disposals	30,405	6,038	2,543	6,421
Total assets	265,301	150,120	153,247	150,169
Working capital deficiency	23,878	47,499	57,148	57,810
Bank debt	79,910	-	-	-
Shareholders'/unitholders' equity	56,777	57,623	46,612	48,136
Operations				
Oil and NGLs (barrels per day)	3,055	2,998	3,009	3,153
Natural gas (MCF per day)	8,817	7,233	7,272	7,139
Total BOE per day <sup>(2)</sup>	4,525	4,204	4,221	4,343

<sup>(1)</sup> Cash payments per share/unit are based on payments made in respect of production months within the quarter.

<sup>(2)</sup> BOE is calculated using a conversion ratio of 6 MCF to 1 barrel of oil. The conversion is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead and as such may be misleading if used in isolation.

## Production

	Three Months Ended			Nine Months Ended	
	Sept. 30, 2010	June 30, 2010	Sept. 30, 2009	Sept. 30, 2010	Sept. 30, 2009
Crude oil and NGLs (barrels per day)	<b>3,890</b>	3,874	3,084	<b>3,705</b>	3,126
Natural gas (MCF per day)	<b>10,674</b>	11,157	10,881	<b>10,625</b>	11,433
Average BOE per day	<b>5,669</b>	5,733	4,898	<b>5,476</b>	5,032

Barrels of oil equivalent (BOE) are calculated using a conversion ratio of 6 MCF to 1 barrel of oil. The conversion is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead and as such may be misleading if used in isolation.

Production volumes for the first nine months of 2010 were up 8.8 percent over the corresponding 2009 period. The increase was due to production increases of over 1,000 BOE per day from the Company's newly completed horizontal crude oil wells. For the month of September 2010, net production from the Company's horizontal Pembina Cardium wells was 1,569 BOE per day compared to 432 BOE per day in December 2009 and 192 BOE per day in September 2009.

Quarter over quarter saw a decline in production of 64 BOE per day. In June 2010, a non-operated natural gas plant, to which Bonterra delivers a portion of its natural gas, reached capacity and resulted in the shut in of a number of the Company's natural gas wells. The average amount of shut in natural gas during Q3 was approximately 660 MCF per day (110 BOE per day).

Effective October 1, 2010, the Company was notified of additional shut in requirements due to other owners in the plant increasing their throughput. Although Bonterra is an owner in the facility, the Company had been delivering natural gas volumes well in excess of its ownership percentage. The amount of natural gas shut in effective October 1, 2010 is approximately 1,100 MCF per day net to the Company. The Company is currently reviewing alternatives, while considering the current low natural gas prices, to either redirect this natural gas production or participate with the other owners in the plant in the expansion of the facility. A short-term solution has been presented by one of the other owners where they would redirect a portion of their natural gas to an alternative natural gas processing facility. Once this is complete, anticipated by the end of the year, Bonterra would be able to reactivate all of its currently shut in production. The Company is not too concerned about these shut in wells at the present time when natural gas prices are extremely low.

The Company drilled 18 gross (16.0 net) operated Pembina Cardium horizontal oil wells during the first nine months of 2010 (eight gross and 6.9 net in Q3 2010). The Company also participated in the drilling of three gross (0.45 net) non-operated Pembina Cardium horizontal oil wells and two gross (0.3 net) non-operated Pembina Cardium vertical oil wells during Q3 2010. Bonterra's working interest in the non-operated wells is approximately 15 percent. Unfortunately, due to the very wet third quarter, the Company was only able to place on production three gross (2.75 net) operated horizontal wells for a portion of the quarter in Q3. Four of the non-operated wells, including all three of the horizontal wells, were also only placed on production in late September. The Company expects to drill a further five operated 100 percent gross and net wells and participate in two gross (0.3 net) non-operated Pembina Cardium horizontal wells in the fourth quarter of 2010.

As of September 30, 2010 the Company had seven gross (6.18 net) horizontal wells drilled but not on production. The Company was able to place on production two 100 percent gross and net horizontal wells in October and four gross (3.43 net) horizontal wells in November. The remaining operated horizontal well (0.75 net) is currently waiting on a third party (owner of 25 percent of the well) to construct a facility on its property to allow for the Company to tie in production from this well and the rest of the wells from the Company's anticipated drilling program in this area. The original facility completion date was scheduled for

mid summer and has continuously been delayed. It is now expected to be completed prior to the end of Q4 2010. The Company is reviewing alternatives for delivering production from this area to a different facility should the completion of the currently planned facility continue to be delayed.

Due to the weather-related delays in placing on production the Company's horizontal wells and the natural gas production shut-ins, Bonterra is reducing its 2010 production guidance to a range of 5,500 to 5,800 BOE per day. Original and continuing production levels from the Company's Pembina Cardium horizontal wells are meeting if not exceeding the Company's expectations and as such the Company is anticipating a significant increase in 2011's average daily production volumes. A more detailed 2011 guidance will be provided at a later date after the Company finalizes its 2011 capital budget.

## Revenue

(\$)	Three Months Ended			Nine Months Ended	
	Sept. 30, 2010	June 30, 2010	Sept. 30, 2009	Sept. 30, 2010	Sept 30, 2009
Revenue – oil and gas sales (000s)	<b>28,332</b>	29,191	20,965	<b>84,771</b>	60,766
Average Realized Prices:					
Crude oil and NGLs (per barrel)	<b>68.79</b>	71.09	65.38	<b>71.40</b>	56.90
Natural gas (per MCF)	<b>3.74</b>	3.97	3.13	<b>4.25</b>	3.97

Revenue from petroleum and natural gas sales increased \$24,005,000, a 39.5 percent improvement in the first nine months of 2010 from the corresponding period in 2009 due to an 18.5 percent increase in crude oil production and a 25.4 percent increase in crude oil prices. Quarter over quarter saw a decrease in revenues of \$859,000 due to reduced commodity prices partly due to a larger than normal differential price between Edmonton par price and West Texas Intermediate price because of the Enbridge Inc. Lakehead pipeline rupture in the third quarter.

The Company's product split on a revenue basis is approximately 85 percent weighted towards crude oil and NGLs. This ratio will further increase as the Company develops its Pembina Cardium horizontal program.

## Royalties

(\$ 000s except \$ per BOE)	Three Months Ended			Nine Months Ended	
	Sept. 30, 2010	June 30, 2010	Sept. 30, 2009	Sept. 30, 2010	Sept. 30, 2009
Crown royalties	<b>1,907</b>	1,757	1,248	<b>5,470</b>	3,286
Freehold royalties, gross overriding royalties and net carried interests	<b>1,041</b>	1,052	697	<b>3,118</b>	1,785
Total royalty expense	<b>2,948</b>	2,809	1,945	<b>8,588</b>	5,071
% of total revenue	<b>10.4</b>	9.6	9.3	<b>10.1</b>	8.3
\$ per BOE	<b>5.65</b>	5.38	4.32	<b>5.74</b>	3.69

Royalties paid by the Company consist primarily of Crown royalties paid to the Provinces of Alberta, Saskatchewan and British Columbia. Most of the Company's wells are low productivity wells and therefore have low Crown royalty rates. The Company's average Crown royalty rate is approximately 6.4 percent (2009 – 5.4 percent) and approximately 3.7 percent (2009 – 2.9 percent) for other royalties.

Quarter over quarter saw an increase of \$139,000 in overall royalties. The increase in total royalties was due to receiving in Q2 the natural gas cost allowance credit from the Province of Alberta for 2009 in the second quarter.

#### ALBERTA GOVERNMENT COMPETITIVENESS REVIEW

On March 11, 2010, the Government of Alberta announced it will modify conventional oil and natural gas royalties effective January 2011 to increase Alberta's competitiveness in the upstream energy sector. The current five per cent front-end royalty rate on conventional oil and natural gas will become a permanent feature of the royalty system. The maximum royalty rate for conventional oil will be reduced to 40 percent from 50 percent. The maximum royalty rate for conventional and unconventional natural gas will be reduced at higher prices from 50 to 36 percent. Other royalty incentive programs will remain in effect. Management believes these changes to the royalty system should have a positive effect on the Company's future cash flow.

#### Other Revenue

(\$ 000s except \$ per BOE)	Three Months Ended			Nine Months Ended	
	Sept. 30, 2010	June 30, 2010	Sept. 30, 2009	Sept. 30, 2010	Sept. 30, 2009
Gain on sale of property	700	-	-	6,485	-
Gain on sale of investments	3,536	17	-	3,553	-
Interest and other	2	12	3	26	63
<b>Total other revenue</b>	<b>4,238</b>	29	3	<b>10,064</b>	63

In February 2010, the Company disposed of its Southeast Saskatchewan Pinto property. The proceeds of disposition were \$5,534,000 cash. At the time of disposition, the Company had a net book value of \$120,000 for the property and had an asset retirement obligation related to the property of \$371,000 that was transferred resulting in a gain on sale of property of \$5,785,000. In addition, In July 2010, the Company disposed of non-producing land for proceeds of \$700,000. The Company had no capital costs associated with this land.

Effective July 6, 2010, Comaplex Minerals Corp. (Comaplex) (a company with common directors and management with the Company) was acquired by Agnico-Eagle Mines Limited (Agnico). In exchange for Bonterra's 689,682 common shares in Comaplex, the Company received 689,682 shares in Geomark Exploration Ltd. (a company with common directors and management with the Company) and 108,693 common shares in Agnico. The common shares of Agnico trade on the Toronto Stock Exchange under the symbol AEM and the common shares of Geomark trade on the TSX Venture Exchange under the symbol GME. The value of the Agnico shares is included with Investments on the Balance Sheet.

During the first nine months of 2010, Bonterra has disposed of a portion of its investments. Gross proceeds from the sales were \$4,405,000 resulting in an accounting gain of \$3,553,000. The Company holds in excess of \$10,000,000 worth of investments as of September 30, 2010.

#### Production Costs

(\$ 000s except \$ per BOE)	Three Months Ended			Nine Months Ended	
	Sept. 30, 2010	June 30, 2010	Sept. 30, 2009	Sept. 30, 2010	Sept. 30, 2009
Production costs	8,069	6,981	6,585	21,752	20,978
\$ per BOE	15.47	13.38	14.61	14.55	15.27

Total production costs in the first nine months of 2010 have increased by \$774,000 over the first nine months of 2009. The increase is entirely due to prior year operating adjustments paid to the operator of natural gas plants in which the Company processes its natural gas. During the year the Company has expensed \$1,685,000 (\$1,177,000 in Q3) of gas processing costs related to fiscal years 2007, 2008 and 2009. These costs were all billed in 2010 and Bonterra had not previously been informed about any such costs being applicable to the Company and these costs were not previously able to be determined by Bonterra.

The impact on average production costs as a result of the above charges was an increase of \$1.13 per BOE in operating costs for the nine months and \$2.26 per BOE in Q3. Excluding these charges, production costs averaged \$13.42 for the nine months and \$13.21 for Q3. The reduction in production costs per BOE in 2010 from 2009 is primarily due to cost management practices and the Company's lower costs from its new production from higher rate horizontal wells. Average production costs in 2010 for these wells are only \$6.60 per BOE compared to approximately \$15.50 per BOE for the remainder of the Company's production.

### General and Administrative (G&A) Expense

(\$ 000s except \$ per BOE)	Three Months Ended			Nine Months Ended	
	Sept. 30, 2010	June 30, 2010	Sept. 30, 2009	Sept. 30, 2010	Sept. 30, 2009
G&A Expense	<b>1,204</b>	1,226	788	<b>3,938</b>	2,835
\$ per BOE	<b>2.31</b>	2.35	1.75	<b>2.63</b>	2.06

The increase in G&A expense year over year was primarily due to increased employee compensation resulting from accrued bonuses which increased approximately \$873,000 in the first nine months of 2010 compared to the first nine months of 2009. The Company has a bonus plan that is based on three percent of earnings before taxes. The Company firmly believes that tying employee compensation (including the use of stock options) to the performance of the Company clearly aligns the interest of the employees to that of the shareholders as the employees are not given a bonus unless the Company earns is profitable.

### Interest Expense

(\$ 000s except \$ per BOE)	Three Months Ended			Nine Months Ended	
	Sept. 30, 2010	June 30, 2010	Sept. 30, 2009	Sept. 30, 2010	Sept. 30, 2009
Interest Expense	<b>702</b>	619	815	<b>1,953</b>	2,556
\$ per BOE	<b>1.35</b>	1.19	1.81	<b>1.31</b>	1.86

Interest charges decreased in the first nine months of 2010 over the corresponding 2009 period primarily due to an approximate 0.75 percent decrease in the average interest rate charged on the Company's outstanding debt balance. The interest rate decrease is due to a reduced bank rate resulting from a better debt to cash flow ratio and to increases in loans from related parties which have a lower interest rate than bank loans.

Effective April 9, 2010, the Company renewed its bank facility under similar terms and conditions with the exception of extending the revolving period to April 27, 2012, reducing its interest and bank fees and amending one of the material covenants (see below).

The interest rate on the renewed credit facility is calculated as follows:

	Level I	Level II	Level III	Level IV	Level V
Consolidated Total Funded Debt to Consolidated Cash flow Ratio <sup>(1)</sup>	Under 1.0:1	Over 1.0:1 to 1.5:1	Over 1.5:1 to 2.0:1	Over 2.0:1 to 2.5:1	Over 2.5:1
Canadian Prime Rate Plus <sup>(2)</sup>	100	150	175	200	250
Bankers' Acceptances Rate Plus <sup>(2)</sup>	225	275	300	325	375

<sup>(1)</sup> Consolidated total funded debt excludes subordinated debt amounts but includes working capital.

<sup>(2)</sup> Numbers in table represent basis points.

Consolidated total funded debt to consolidated cash flow ratio shall be calculated each fiscal quarter and the interest rates adjusted effective as of the first day of the fiscal quarter commencing immediately after the fiscal quarter in which Bonterra files a compliance certificate containing the ratio, with each such adjustment to be effective until the next such adjustment.

As of September 30, 2010 the Company will continue to qualify for the Level I interest rates.

The following is a list of the material covenants of the Company's bank facility:

- The Company is required to not exceed \$120,000,000 in consolidated debt (includes negative working capital but excludes debt to related parties). As of September 30, 2010 the Company had consolidated total funded debt of \$59,792,000.
- Total dividends paid in the current quarter and the three previous quarters shall not exceed 80 percent of the previous four quarters' cash flow as defined under GAAP. Dividend payments totaled \$43,212,000 during the quarter and the three previous quarters while cash flow totaled \$61,379,000 during the same period for an overall payout ratio of 70 percent.

### Stock-Based Compensation

Stock-based compensation is a statistically calculated value representing the estimated expense of issuing employee stock options. The Company records a compensation expense over the vesting period based on the fair value of options granted to employees, directors and consultants. Based on currently outstanding options, the Company anticipates that a non-cash expense of approximately \$108,000 will be recorded for the balance of 2010, \$206,000 in 2011 and \$16,000 in 2012.

### Depletion, Depreciation and Accretion

The Company follows the successful efforts method of accounting for petroleum and natural gas exploration and development costs. Under this method, the costs associated with dry holes are charged to operations. For intangible capital costs that result in the addition of reserves, the Company depletes its oil and natural gas intangible assets using the unit-of-production basis by field.

For tangible assets such as well equipment, the Company now uses a 10 percent declining basis for depreciation calculation. The Company changed from the straight line basis due to the increasing reserve life index which continues to indicate a longer service life for its production assets.

Provision for depletion, depreciation and accretion was \$16,265,000 and \$14,714,000, respectively for the nine month periods ending September 30, 2010 and September 30, 2009. The increase in the depletion amount was due primarily to increased production volumes. The Company has capital costs of approximately \$6.70 (2009 - \$6.60) per proved BOE of reserves based on the December 31, 2009 independent engineering report.

## Taxes

The current tax provision relates to a resource surcharge of \$106,000 (2009 - \$211,000) payable to the Province of Saskatchewan. The resource surcharge is calculated as a flat percent of revenues generated from the sale of petroleum products produced in Saskatchewan. The resource surcharge rate is three percent in 2010. In 2009, a capital tax amount of \$269,000 payable to the Province of Quebec was incurred due to the 2008 reorganization for the conversion from a Trust to a Corporation. The capital tax payable to the Province of Quebec was a one-time charge.

The Company has the following tax pools, which may be used to reduce taxable income in future years, limited to the applicable rates of utilization:

(\$ 000s)	Rate of Utilization (%)	Amount
Undepreciated capital costs	20-100	\$ 23,688
Eligible capital expenditures	7	6,978
Share issue costs	20	1,811
Canadian oil and gas property expenditures	10	19,603
Canadian development expenditures	30	95,609
Canadian exploration expenditures	100	11,140
SR&ED expenditures	100	50,048
Income tax losses carried forward <sup>(1)</sup>	100	222,596
		<u>\$431,473</u>

<sup>(1)</sup> Income tax losses carried forward expire in the following years; 2024 - \$3,347,000, 2025 - \$7,532,000, 2026 - \$46,671,000, 2027 - \$117,189,000, 2028 - \$34,726,000, 2029 - \$13,131,000.

In addition to the above pools, the Company also has \$27,670,000 (December 31, 2009 - \$27,670,000) remaining of investment tax credits that expire in the following years; 2019 - \$3,469,000, 2020 - \$3,059,000, 2021 - \$4,667,000, 2022 - \$3,909,000, 2023 - \$3,155,000, 2024 - \$1,995,000, 2025 - \$2,257,000, 2026 - \$2,405,000, 2027 - \$2,009,000, 2028 - \$745,000.

The Company also has \$142,175,000 (December 31, 2009 - \$143,061,000) of capital loss carry forwards which can only be claimed against taxable capital gains.

The amount and timing of reversals of temporary differences will also depend on the Company's future operating results and its future acquisitions and dispositions of assets and liabilities. A significant change in any of the preceding assumptions could materially affect the Company's estimate of the future income tax asset.

## Net Earnings

(\$ 000s except \$ per share)	Three Months Ended			Nine Months Ended	
	Sept. 30, 2010	June 30, 2010	Sept. 30, 2009	Sept. 30, 2010	Sept. 30, 2009
Net Earnings	<b>12,724</b>	10,887	5,790	<b>35,651</b>	16,427
\$ per share – basic	<b>0.68</b>	0.58	0.31	<b>1.90</b>	0.92
\$ per share – fully diluted	<b>0.66</b>	0.56	0.31	<b>1.85</b>	0.92

Net earnings increased in the first nine months of 2010 by \$19,224,000 from the corresponding 2009 period. Increased revenues resulting from increased crude oil prices combined with an 18.5 percent increase in crude oil and NGL production volumes were the main reasons for the increase. The Company returned in excess of 40 percent of its gross realized revenues in net earnings. The Company's low capital costs

combined with the Company's low production decline rates continues to allow for continued positive earnings even in a lower commodity price environment.

The three months ended September 30, 2010 saw an increase of \$1,837,000 in net earnings from the three months ended June 30, 2010. The Q3 2010 increase in net earnings from Q2 2010 was due to the gain on sale of investments during the third quarter of \$3,536,000, offset by slightly lower oil and gas sales revenue and increased production costs.

### Comprehensive Income

Other comprehensive income for 2010 consists of an unrealized gain in its investments of \$5,144,000 (2009 – \$1,078,000) due to an increase in the share price of these entities. Also the Company disposed of a portion of its investments resulting in a realized gain, net of tax, of \$3,056,000.

### Cash Flow from Operations

(\$ 000s)	Three Months Ended			Nine Months Ended	
	Sept. 30, 2010	June 30, 2010	Sept. 30, 2009	Sept. 30, 2010	Sept. 30, 2009
Cash flow from operations	<b>17,558</b>	16,644	9,350	<b>49,275</b>	25,225
\$ per share – basic	<b>0.93</b>	0.89	0.50	<b>2.63</b>	1.42
\$ per share – fully diluted	<b>0.91</b>	0.86	0.50	<b>2.56</b>	1.42

The first nine month 2010 cash flow from operations increased 90.6 percent compared to first nine months of 2009 due to increased crude oil prices and increased production. Quarter over quarter cash flow decreased \$288,000.

### Cash Netback

The following table illustrates the Company's cash netback from operations for the nine month periods ended September 30:

\$ per Barrel of Oil Equivalent (BOE)	2010	2009
Production volumes (BOE)	<b>1,494,975</b>	1,373,736
Gross production revenue	<b>\$ 56.70</b>	\$ 44.23
Royalties	<b>(5.74)</b>	(3.69)
Field operating costs	<b>(14.55)</b>	(15.27)
Field netback	<b>36.41</b>	25.27
General and administrative	<b>(2.63)</b>	(2.06)
Interest and taxes	<b>(1.38)</b>	(2.21)
Cash netback	<b>\$ 32.40</b>	\$ 21.00

The following table illustrates the Company's cash netback from operations for the three month periods ended:

\$ per Barrel of Oil Equivalent (BOE)	Sept. 30, 2010	June 30, 2010
Production volumes (BOE)	521,601	521,736
Gross production revenue	\$ 55.32	\$ 55.95
Royalties	(5.65)	(5.38)
Field operating costs	(15.47)	(13.38)
Field netback	34.20	37.19
General and administrative	(2.31)	(2.35)
Interest and taxes	(1.39)	(1.25)
Cash netback	\$ 30.50	\$ 33.59

### Related Party Transactions

As a result of the acquisition of Comaplex by Agnico, the loan agreement and Bonterra common shares were transferred to Geomark. A new management agreement was entered into with the only amendment to the agreement being a reduction in the monthly management fee from \$30,000 to \$22,500.

Geomark and Comaplex combined paid a management fee to the Company of \$249,000 (2009 - \$247,500). Geomark also shares office rental costs and reimburses the Company for costs related to employee benefits and office materials. In addition, Geomark owns 204,633 (Comaplex December 31, 2009 - 204,633) common shares in the Company. Services provided by the Company included executive services (chief executive officer, president and vice president, finance duties), accounting services, oil and gas administration and office administration. All services performed were charged at estimated fair value. At September 30, 2010, Geomark owed the Company \$33,000 (Comaplex December 31, 2009 - \$105,000).

As of September 30, 2010, Geomark has loaned the Company \$20,000,000 (Comaplex December 31, 2009 - \$12,000,000). The loan is unsecured, bears interest at Canadian chartered bank prime less 5/8ths of a percent and has no set repayment terms.

The loan cannot be repaid, or demanded to be paid by Geomark, unless the Company has sufficient available borrowing limits under the Company's credit facility. Interest paid on both the Comaplex and Geomark loans during the first nine months of 2010 was \$193,000 (2009 - \$134,000). This loan results in being a substantial benefit to Bonterra and to Geomark. The interest paid to Geomark by Bonterra is substantially lower than bank interest and for Geomark, the interest earned is substantially higher than Geomark would receive by investing in bank instruments such as BA's or GIC's.

The Company also has a management agreement with Pine Cliff Energy Ltd. (Pine Cliff). Pine Cliff has common directors and management with the Company. Pine Cliff trades on the TSX Venture Exchange. Pine Cliff paid a management fee to the Company of \$67,500 (2009 - \$90,000). Services provided by the Company include executive services (CEO, president and vice president, finance duties), accounting services, oil and gas administration and office administration. All services performed are charged at estimated fair value. The Company has no share ownership in Pine Cliff. At September 30, 2010, the Company had an account receivable from Pine Cliff of \$1,000 (December 31, 2009 - \$1,000).

As of September 30, 2010, the Company's CEO and major shareholder has loaned the Company \$12,000,000 (December 31, 2009 - \$11,500,000). The loan is unsecured, bears interest at Canadian chartered bank prime less 5/8th of a percent and has no set repayment terms.

The loan cannot be repaid, or demanded to be paid by the Company's CEO, unless the Company has sufficient available borrowing limits under the Company's credit facility. Interest paid on this loan during the first nine months of 2010 was \$170,000 (2009 - \$152,000). This loan results in being a substantial benefit to Bonterra and to the CEO. The interest paid to the CEO by Bonterra is substantially lower than bank interest and for the CEO the interest earned is substantially higher than the CEO would receive by investing in bank instruments such as BA's or GIC's.

### Liquidity and Capital Resources

During the first nine months of 2010, the Company incurred capital costs of \$51,596,000 (2009 - \$22,616,000) net of drilling tax credits. The costs relate primarily to the drilling, completing, tie-in and equipping of 18 gross (16.0 net) Pembina Cardium horizontal wells as well as its proportion of the non-operated drilling costs.

The Company currently has plans to spend between \$65,000,000 and \$69,000,000 net of drilling credits on its 2010 Pembina Cardium horizontal well program and non-operated capital programs. This represents an increase of up to \$4,000,000 from its previously released budget figure. This includes the drilling of a further five gross and net operated and two gross (0.3 net) non-operated Pembina Cardium horizontal wells in the fourth quarter of 2010. Bonterra anticipates funding the balance of its 2010 capital program out of cash flow, proceeds from the exercise of employee stock options, sale of investments and the Company's line of credit. The Company has not yet finalized its 2011 capital budget. This information will be released in Q4 2010 or early 2011.

As of September 30, 2010 and December 31, 2009, the Company has a bank facility consisting of a \$100,000,000 syndicated revolving credit facility and a \$20,000,000 non-syndicated revolving credit facility. Amounts drawn under these facilities at September 30, 2010 were \$73,901,000 (December 31, 2009 - \$59,823,000). The interest rates on the outstanding debt as of September 30, 2010 were 4.0 percent and 3.3 percent on the Company's Canadian prime rate loan and Bankers' Acceptances, respectively. For information related to interest rate levels and material covenants please refer to the discussion under Interest Expense.

On October 4, 2010 the Company borrowed \$15,000,000 from a private investor. In exchange Bonterra has issued a Promissory Note for \$15,000,000. The terms of the Promissory Note are that it bears interest at three percent, is not callable by the investor prior to January 4, 2012 at which time it will be a demand note until its maturity of April 4, 2012, and can be repaid at the option of the Company at any time. Security consists of a floating demand debenture totaling \$15,000,000 over all of the Company's assets and is subordinated to any and all claims in favor of the syndicate of senior lenders providing credit facilities to the Company.

The Company is authorized to issue an unlimited number of common shares without nominal or par value.

Issued	Number	Amount (\$ 000s)
Common Shares		
Balance, January 1, 2010	18,619,641	121,955
Issued pursuant to Company share option plan	283,900	5,758
Transfer of contributed surplus to share capital	-	302
Balance, September 30, 2010	18,903,541	128,015

The Company provides an option plan for its directors, officers, employees and consultants. Under the plan, the Company may grant options for up to 1,890,354 (December 31, 2009 - 1,861,964) common shares. The exercise price of each option granted equals the market price of the common shares on the date of grant and the option's maximum term is five years.

A summary of the status of the Company's stock option plan as of September 30, 2010 and December 31, 2009, and changes during the nine month and twelve month periods ended on those dates is presented below:

	September 30, 2010		December 31, 2009	
	Options	Weighted-Average Exercise Price	Options	Weighted-Average Exercise Price
Outstanding at beginning of period	1,330,900	\$ 20.36	1,390,500	\$ 20.50
Options granted	30,000	34.66	33,000	14.90
Options exercised	(283,900)	20.28	(92,600)	20.50
Outstanding at end of period	1,077,000	\$ 20.78	1,330,900	\$ 20.36
Options exercisable at end of period	98,000	\$ 20.50	370,900	\$ 20.50

The following table summarizes information about options outstanding at September 30, 2010:

Range of Exercise Prices	Options Outstanding			Options Exercisable	
	Number Outstanding At 9/30/10	Weighted-Average Remaining Contractual Life	Weighted-Average Exercise Price	Number Exercisable at 9/30/10	Weighted-Average Exercise Price
\$14.90	22,000	2.2 years	\$14.90	-	\$ -
20.50	1,025,000	2.1 years	20.50	98,000	20.50
34.66	30,000	2.2 years	34.66	-	-
\$14.90-\$34.66	1,077,000	2.1 years	\$20.78	98,000	\$20.50

### Disclosure Controls and Procedures

Disclosure controls and procedures have been designed to ensure the information required to be disclosed by the Company is accumulated and communicated to the Company's Management, as appropriate, to allow timely decisions regarding required disclosures. The Company's Chief Executive Officer and Chief Financial Officer have concluded, based on their evaluation as of the end of the period covered by the interim filings that the Company's disclosure controls and procedures are effective to provide reasonable assurance that material information related to the issuer, is made known to them by others within the Company. It should be noted that while the Company's Chief Executive Officer and Chief Financial Officer believe that the Company's disclosure controls and procedures provide a reasonable level of assurance that they are effective, they do not expect that the disclosure controls and procedures or internal control over financial reporting will prevent all errors and fraud. A control system, no matter how well conceived or operated, can provide only reasonable, not absolute, assurance that the objective of the control system is met.

### Internal Control Update

The Company has conducted a review of its Internal Control Over Financial Reporting (ICFR), with the conclusion that as of September 30, 2010 the Company's system of ICFR as defined under NI 52-109 is adequately designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with GAAP. The control framework the Company used to design its ICFR was the Committee of Sponsoring Organizations of the Treadway Commission (COSO). In its review, the Company identified certain material weaknesses in internal controls over financial reporting:

1. due to the limited number of staff at the Company, it is not feasible to achieve the complete segregation of incompatible duties; and

2. due to the limited number of staff, the Company relies upon third parties as participants in the Company's internal controls over financial reporting.

The Company believes these weaknesses are mitigated by: the active involvement of senior management and the Board of Directors in the affairs of the Company; open lines of communication within the Company; the present levels of activities and transactions within the Company being readily transparent; the thorough review of the Company's financial statements by management, the board of directors and by the Company's auditors; and the establishment of a whistle-blower policy. However, these mitigating factors will not necessarily prevent a material misstatement occurring as a result of the aforesaid weaknesses in the Company's internal controls over financial reporting. A system of internal controls over financial reporting, no matter how well conceived or operated, can provide only reasonable, not absolute, assurance that the objectives of the internal controls over financial reporting are met. The Company has no plans for remediating the above weaknesses.

### **Financial Reporting Update**

In December 2008, the CICA issued Section 1582, "Business Combinations", which replaced former guidance on business combinations. Section 1582 establishes principles and requirements of the acquisition method for business combinations and related disclosures. This statement applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after January 1, 2011 with earlier adoption permitted.

In December 2008, the CICA issued Sections 1601, "Consolidated Financial Statements", and 1602, "Non-controlling Interests", which replaced existing Section 1600. Section 1601 establishes standards for the preparation of consolidated financial statements. Section 1602 provides guidance on accounting for a non-controlling interest in a subsidiary in consolidated financial statements subsequent to a business combination. These standards are effective on or after the beginning of the first annual reporting period beginning on or after January 2011 with earlier adoption permitted. Section 1602 currently does not impact the Company as the Company has no subsidiaries.

### **INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS)**

The Accounting Standards Board has confirmed the convergence of Canadian GAAP with IFRS will be effective January 1, 2011.

In the fourth quarter of 2009, the Company commenced phase two of the process of conversion to IFRS by engaging its external auditors to perform a detailed review of the implementation of IFRS on the Company's high impact and medium impact areas identified below:

#### **High impact areas:**

- IFRS 1 – First time adoption of IFRS
- IFRS 3 – Business combinations
- IAS 16 – Property and equipment
- IAS 36 – Impairment of assets

#### **Medium impact areas include:**

- IFRS 6 – Exploration and evaluation of mineral resources
- IFRS 2 – Share-based payments
- IAS 1 – Presentation of financial statements
- IAS 10 – Events after the balance sheet date
- IAS 12 – Income Taxes
- IAS 18 – Revenues

- IAS 23 – Borrowing costs
- IAS 39 – Financial instruments, recognition and measurement
- IAS 37 – Provisions, contingent liabilities and contingent assets

The Company is in the process of completing its review and adjustments to its opening balance sheet required in relation to its IFRS policies. The Company anticipates commencing phase three (financial statement and note compilation) during the fourth quarter of 2010. Further key information will be disclosed as it becomes available during the transition period.

The Company has implemented a new financial accounting system that provides for sufficient detail to comply with the IFRS requirements. As the Company has been using successful efforts since its inception, detail at a well level has been maintained under its past and current financial accounting systems as well as procedures are in place to capture this information at the operational level.

Implications to the Company's controls for DC&P and ICFR are being reviewed; however the Company believes that the majority of the procedures in place will apply once IFRS is implemented. Training is required and is ongoing. Individuals within the Company have been and will continue to attend courses, seminars and other training activities to ensure the Company is adequately prepared for IFRS. Use of external legal expertise will be used to ensure compliance is maintained with all contractual agreements.

Additional information relating to the Company may be found on [www.sedar.com](http://www.sedar.com) or visit our website at [www.bonterraenergy.com](http://www.bonterraenergy.com).

## **MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL STATEMENTS**

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

Management maintains a system of internal controls to provide reasonable assurance that the Company's assets are safeguarded and to facilitate the preparation of relevant and timely information.

The audit committee has reviewed these financial statements with management and has reported to the Board of Directors. The Board of Directors has approved the financial statements as presented in this interim report.

## CONSOLIDATED BALANCE SHEETS

As at September 30, 2010 and December 31, 2009

(unaudited)

(\$ 000s)	2010	2009
<b>Assets</b>		
<b>Current</b>		
Accounts receivable (Note 11)	16,975	14,713
Crude oil inventory	529	431
Prepaid expenses	2,899	3,247
Future tax asset (Note 8)	18,082	11,889
Investments	10,123	4,462
Investment in related party (Note 3)	-	4,827
	<b>48,608</b>	<b>39,569</b>
Investment in related party (Note 3)	724	-
Restricted cash (Note 4)	-	812
Investment tax credit receivable (Note 8)	27,670	27,670
Future tax asset (Note 8)	37,855	58,265
<b>Property and Equipment (Note 5)</b>		
Petroleum and natural gas properties and related equipment	307,159	255,840
Accumulated depletion and depreciation	(103,523)	(88,169)
<b>Net Property and Equipment</b>	<b>203,636</b>	<b>167,671</b>
	<b>318,493</b>	<b>293,987</b>
<b>Liabilities</b>		
<b>Current</b>		
Accounts payable and accrued liabilities	19,179	18,868
Due to related parties (Note 6)	32,000	23,500
Deferred credit (Note 8)	15,320	7,363
	<b>66,499</b>	<b>49,731</b>
Bank debt (Note 7)	73,901	59,823
Deferred credit (Note 8)	32,072	47,769
Asset retirement obligations	17,529	17,790
	<b>190,001</b>	<b>175,113</b>
<b>Shareholders' Equity (Note 9)</b>		
Share capital	128,015	121,955
Contributed surplus	3,474	3,350
	<b>131,489</b>	<b>125,305</b>
Deficit	(7,105)	(8,451)
Accumulated other comprehensive income (Note 10)	4,108	2,020
	<b>(2,997)</b>	<b>(6,431)</b>
<b>Total Shareholders' Equity</b>	<b>128,492</b>	<b>118,874</b>
	<b>318,493</b>	<b>293,987</b>

## CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

For the periods ended September 30 (unaudited) (\$ 000s)	Three Months		Nine Months	
	2010	2009	2010	2009
Shareholders' equity, beginning of period	126,045	72,332	118,874	56,777
Comprehensive income for the period	11,219	6,050	37,739	17,505
Net capital contributions (Note 9)	3,498	3,181	5,758	20,424
Stock-based compensation	142	243	426	711
Dividends declared	(12,412)	(7,781)	(34,305)	(21,392)
<b>Shareholders' Equity, End of Period</b>	<b>128,492</b>	<b>74,025</b>	<b>128,492</b>	<b>74,025</b>

## CONSOLIDATED STATEMENTS OF OPERATIONS AND DEFICIT

For the periods ended September 30 (unaudited) (\$ 000s, except \$ per Share)	Three Months		Nine Months	
	2010	2009	2010	2009
<b>Revenue</b>				
Oil and gas sales	28,332	20,965	84,771	60,766
Royalties	(2,948)	(1,945)	(8,588)	(5,071)
Gain on sale of property	700	-	6,485	-
Gain on sale of investments	3,536	-	3,553	-
Interest and other	2	3	26	63
	<b>29,622</b>	<b>19,023</b>	<b>86,247</b>	<b>55,758</b>
<b>Expenses</b>				
Production costs	8,069	6,585	21,752	20,978
General and administrative	1,204	788	3,938	2,835
Interest on bank debt	562	710	1,590	2,270
Interest on due to related parties (Note 6)	140	105	363	286
Stock-based compensation	142	243	426	711
Depletion, depreciation and accretion	6,256	5,191	16,265	14,714
	<b>16,373</b>	<b>13,622</b>	<b>44,334</b>	<b>41,794</b>
<b>Earnings Before Taxes</b>	<b>13,249</b>	<b>5,401</b>	<b>41,913</b>	<b>13,964</b>
<b>Taxes (Recovery)</b>				
Current	25	82	106	480
Future	500	(471)	6,156	(2,943)
	<b>525</b>	<b>(389)</b>	<b>6,262</b>	<b>(2,463)</b>
<b>Net Earnings for the Period</b>	<b>12,724</b>	<b>5,790</b>	<b>35,651</b>	<b>16,427</b>
Deficit, beginning of period	(7,417)	(49,689)	(8,451)	(46,715)
Dividends declared	(12,412)	(7,781)	(34,305)	(21,392)
<b>Deficit, End of Period</b>	<b>(7,105)</b>	<b>(51,680)</b>	<b>(7,105)</b>	<b>(51,680)</b>
<b>Net Earnings Per Share – Basic (Note 9)</b>	<b>0.68</b>	<b>0.31</b>	<b>1.90</b>	<b>0.92</b>
<b>Net Earnings Per Share – Diluted (Note 9)</b>	<b>0.66</b>	<b>0.31</b>	<b>1.85</b>	<b>0.92</b>

## CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

For the Periods Ended September 30 (unaudited) (\$ 000s, except \$ per Share)	Three Months		Nine Months	
	2010	2009	2010	2009
<b>Net Earnings for the Period</b>	<b>12,724</b>	5,790	<b>35,651</b>	16,427
Unrealized gains on investments (net of Income taxes; Three months ended 2010 - \$245, 2009 - \$44; Nine months ended 2010 - \$816, 2009 - \$178)	<b>1,537</b>	260	<b>5,144</b>	1,078
Realized gains on investments transferred to net earnings (net of Income taxes; Three months ended 2010 - \$494, 2009 - \$Nil; Nine months ended 2010 - \$497, 2009 - \$Nil)	<b>(3,042)</b>	-	<b>(3,056)</b>	-
<b>Other Comprehensive Income (Loss)</b>	<b>(1,505)</b>	260	<b>2,088</b>	1,078
<b>Comprehensive Income</b>	<b>11,219</b>	6,050	<b>37,739</b>	17,505
<b>Comprehensive Income Per Share – Basic (Note 9)</b>	<b>0.60</b>	0.32	<b>2.01</b>	0.98
<b>Comprehensive Income Per Share – Diluted (Note 9)</b>	<b>0.58</b>	0.32	<b>1.96</b>	0.98

## CONSOLIDATED STATEMENTS OF CASH FLOWS

For the periods ended September 30 (unaudited) (\$ 000s)	Three Months		Nine Months	
	2010	2009	2010	2009
<b>Operating Activities</b>				
Net earnings for the period	12,724	5,790	35,651	16,427
Items not affecting cash				
Stock-based compensation	142	243	426	711
Depletion, depreciation and accretion	6,256	5,191	16,265	14,714
Gain on sale of property	(700)	-	(6,485)	-
Gain on sale of investments	(3,536)	-	(3,553)	-
Future income taxes	500	(471)	6,156	(2,943)
	15,386	10,753	48,460	28,909
Change in non-cash working capital				
Accounts receivable	669	420	689	1,620
Crude oil inventory	(94)	30	(67)	329
Prepaid expenses	(216)	640	348	394
Accounts payable and accrued liabilities	2,269	(2,589)	(291)	(5,999)
Restricted cash	-	235	812	240
Asset retirement obligations settled	(456)	(139)	(676)	(268)
	2,172	(1,403)	815	(3,684)
<b>Cash Provided by Operating Activities</b>	<b>17,558</b>	<b>9,350</b>	<b>49,275</b>	<b>25,225</b>
<b>Financing Activities</b>				
Increase (decrease) in debt	(4,533)	7,612	14,078	(14,050)
Due to related parties	8,500	-	8,500	16,000
Issue of shares pursuant to private placement	-	-	-	17,996
Share issue costs	-	(35)	-	(1,046)
Stock option proceeds	3,498	-	5,758	-
Dividends	(12,412)	(7,781)	(34,305)	(21,392)
<b>Cash Used in Financing Activities</b>	<b>(4,947)</b>	<b>(204)</b>	<b>(5,969)</b>	<b>(2,492)</b>
<b>Investing Activities</b>				
Property and equipment expenditures	(19,927)	(10,501)	(51,596)	(15,457)
Proceeds on sale of property	700	-	6,234	-
Proceeds on sale of investments	4,215	-	4,405	-
Restricted term deposit	-	-	-	20
Change in non-cash working capital				
Accounts receivable	(2,011)	(1,742)	(2,951)	(1,742)
Accounts payable and accrued liabilities	4,412	3,097	602	(5,554)
<b>Cash Used in Investing Activities</b>	<b>(12,611)</b>	<b>(9,146)</b>	<b>(43,306)</b>	<b>(22,733)</b>
<b>Net Cash Inflow</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>
Cash, beginning of period	-	-	-	-
<b>Cash, End of Period</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>-</b>
<b>Cash Interest Paid</b>	<b>702</b>	<b>833</b>	<b>1,953</b>	<b>2,520</b>
<b>Cash Taxes Paid</b>	<b>45</b>	<b>349</b>	<b>132</b>	<b>541</b>

## NOTES TO THE INTERIM CONSOLIDATED FINANCIAL STATEMENTS

As at September 30, 2010 and for the three and nine month periods ended September 30, 2010 and 2009 (unaudited)

### 1. CHANGE OF ORGANIZATION

Effective January 1, 2010, Bonterra Energy Income Trust was wound up into Bonterra Oil & Gas Ltd. and Bonterra Oil & Gas Ltd. was amalgamated with Bonterra Energy Corp. The continuing entity officially changed its name to Bonterra Energy Corp. (Bonterra or the Company) subsequent to finalizing the reorganization.

### 2. SIGNIFICANT ACCOUNTING POLICIES

The accounting policies and methods of application followed in the preparation of the interim consolidated financial statements are the same as those followed in the preparation of Bonterra's 2009 annual consolidated financial statements except as described below. These interim consolidated financial statements do not include all disclosures required for annual consolidated financial statements. The interim consolidated financial statements as presented should be read in conjunction with the 2009 annual consolidated financial statements.

#### Change in Accounting Estimate

##### *Petroleum and Natural Gas Properties and Related Equipment*

On January 1, 2010, the Company prospectively began depreciating petroleum and natural gas plant and equipment using the declining balance method at 10 percent per year, a change from the straight-line method. The change of estimate was due to declining balance depreciation providing a better reflection of the estimated service life of the related assets. During the first nine months of 2010, the Company incurred \$1,535,000 (Q1 2010 - \$456,000 and cumulative Q2 2010 - \$1,056,000) less depreciation under the declining balance method, than under the straight-line method.

##### *Furniture, Equipment and Other*

On January 1, 2010, the Company prospectively began depreciating these assets using the declining balance method at rates of 10 percent to 20 percent per year, a change from the straight-line method. The change of estimate was due to declining balance depreciation providing a better reflection of the estimated service life of the related assets. During the first nine months of 2010, the Company incurred \$101,000 (Q1 2010 - \$23,000 and cumulative Q2 2010 - \$70,000) less depreciation under the declining balance method, than under the straight-line method.

#### Recent Accounting Pronouncements

In December 2008, the CICA issued Section 1582, "Business Combinations", which replaced former guidance on business combinations. Section 1582 establishes principles and requirements of the acquisition method for business combinations and related disclosures. This statement applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after January 1, 2011 with earlier adoption permitted.

In December 2008, the CICA issued Sections 1601, "Consolidated Financial Statements", and 1602, "Non-controlling Interests", which replaced existing Section 1600. Section 1601 establishes standards for the preparation of consolidated financial statements. Section 1602 provides guidance on accounting for a non-

controlling interest in a subsidiary in consolidated financial statements subsequent to a business combination. These standards are effective on or after the beginning of the first annual reporting period beginning on or after January 1, 2011 with earlier adoption permitted. Section 1602 currently does not impact the Company as it does not have any subsidiaries.

The Canadian Accounting Standards Board has confirmed that IFRS will replace Canadian GAAP effective January 1, 2011, including comparatives for 2010, for Canadian publicly accountable enterprises.

### 3. INVESTMENT IN RELATED PARTY

The investment consists of 689,682 common shares in Geomark Exploration Ltd. (Geomark) a company with common directors and management with the Company. The investment is recorded at fair market value.

Effective July 6, 2010, Comaplex Minerals Corp. (Comaplex) was acquired by Agnico-Eagle Mines Limited (Agnico). In exchange for Bonterra's 689,682 common shares in Comaplex, the Company received 689,682 shares in Geomark and 108,693 common shares in Agnico (value included in Investments on the balance sheet). The common shares of Agnico trade on the Toronto Stock Exchange under the symbol AEM and the common shares of Geomark trade on the TSX Venture Exchange under the symbol GME. The investment in Geomark represents 1.3 percent ownership in the outstanding common shares of Geomark.

### 4. RESTRICTED CASH

An escrow account was held by Silverwing Energy Inc., prior to its acquisition by the Company in 2008. The escrow account was created to support eligible expenditures related to a farm-in agreement. All necessary expenditures have been completed and the funds have been paid to the Company.

### 5. PROPERTY AND EQUIPMENT

(\$ 000s)	September 30, 2010		December 31, 2009	
	Cost	Accumulated Depletion and Depreciation	Cost	Accumulated Depletion and Depreciation
Undeveloped land	6,055	-	7,992	-
Petroleum and natural gas properties and related equipment	299,632	102,446	246,387	87,153
Furniture, equipment and other	1,472	1,077	1,461	1,016
	<b>307,159</b>	<b>103,523</b>	255,840	88,169

In February 2010, the Company disposed of its Southeast Saskatchewan Pinto property. The proceeds of disposition were \$5,534,000 cash. At the time of disposition, the Company had a net book value of \$120,000 for the property. It also had an asset retirement obligation related to the property of \$371,000 that was transferred resulting in a gain on sale of property of \$5,785,000.

In July 2010, the Company disposed of non-producing land rights for proceeds of \$700,000. The Company has never had any capital costs associated with these land rights.

### 6. DUE TO RELATED PARTIES

As of September 30, 2010, the Company's CEO and major shareholder has loaned the Company \$12,000,000 (December 31, 2009 - \$11,500,000). The loan is unsecured, bears interest at Canadian chartered bank prime less 5/8ths of a percent and has no set repayment terms but is payable on demand. Interest paid on this loan during the first nine months of 2010 was \$170,000 (2009 - \$152,000).

As a result of the acquisition by Agnico of Comaplex on July 6, 2010, the loan previously held by Comaplex was transferred to Geomark and is repayable by the Company under the same terms and conditions. As of September 30, 2010, Geomark has loaned the Company \$20,000,000.

The loan is unsecured, bears interest at Canadian chartered bank prime less 5/8ths of a percent and has no set repayment terms but is payable on demand. Interest paid on this loan during the first nine months of 2010 was \$193,000 (including interest paid to Comaplex) (Comaplex 2009 - \$134,000).

The Company's bank agreement requires that the above loans can only be repaid should the Company have sufficient available borrowing limits under the Company's credit facility. As of September 30, 2010 the Company has sufficient room to repay all balances.

Please refer to Note 11 for additional related party transactions.

## 7. BANK DEBT

As of September 30, 2010 and December 31, 2009, the Company has a bank facility consisting of a \$100,000,000 syndicated revolving credit facility and a \$20,000,000 non-syndicated revolving credit facility. Amounts drawn under the facility at September 30, 2010 were \$73,901,000 (December 31, 2009 - \$59,823,000). Interest paid on the bank loan during the first nine months of 2010 was \$1,590,000 (2009 - \$1,561,000). The interest rates on the outstanding debt as of September 30, 2010 were 4.0 percent and 3.3 percent on the Company's Canadian prime rate loan and Bankers' Acceptances, respectively. The terms of the syndicated revolving credit facility provided that the loan is revolving to April 27, 2012 and is subject to annual review. The revolving credit facility has no fixed payment requirements.

The amount available for borrowing under the credit facilities is reduced by outstanding letters of credit. Letters of credit totaling \$285,000 were issued at September 30, 2010 (December 31, 2009 - \$285,000). Security for the credit facilities consists of various fixed and floating demand debentures totaling \$200,000,000 over all of the Company's assets, and a general security agreement with first ranking over all personal and real property.

The interest rate on the new credit facility is calculated as follows:

	Level I	Level II	Level III	Level IV	Level V
Consolidated Total Funded Debt <sup>(1)</sup> to Consolidated Cash flow Ratio	Under 1.0:1	Over 1.0:1 to 1.5:1	Over 1.5:1 to 2.0:1	Over 2.0:1 to 2.5:1	Over 2.5:1
Canadian Prime Rate Plus <sup>(2)</sup>	100	150	175	200	250
Bankers' Acceptances Rate Plus <sup>(2)</sup>	225	275	300	325	375

<sup>(1)</sup> Consolidated total funded debt excludes related party amounts but includes working capital. Consolidated cash flow is calculated as cash flow according to GAAP excluding adjustments for non-cash working capital items.

<sup>(2)</sup> Numbers in table represent basis points.

Consolidated total funded debt to consolidated cash flow ratio shall be calculated each fiscal quarter and the interest rates adjusted effective as of the first day of the fiscal quarter commencing immediately after the fiscal quarter in which Bonterra files a compliance certificate containing the ratio, with each such adjustment to be effective until the next such adjustment.

The following is a list of the material covenants:

- The Company is required to not exceed \$120,000,000 in consolidated total funded debt (includes working capital but excludes subordinated debt).

- The total of the dividends paid in the current quarter and the three previous quarters shall not exceed 80 percent of the previous four quarters' cash flow as defined under GAAP excluding adjustments for non-cash working capital items.

At September 30, 2010, the Company is in compliance with all covenants.

## 8. TAXES

The Company has recorded a future tax asset related to assets and liabilities and related tax amounts:

(\$ 000s)	<b>September 30</b> <b>2010</b>	December 31 2009
Future tax liability related to investments	<b>(588)</b>	(824)
Future tax liability related to property and equipment	<b>(11,483)</b>	(5,855)
Future tax asset related to asset retirement obligations	<b>4,394</b>	4,474
Future tax asset related to finance costs	<b>499</b>	802
Future tax asset related to corporate tax losses, ITC's and SR&ED claims	<b>44,445</b>	59,668
Future tax asset related to corporate capital tax loss	<b>17,818</b>	17,883
Valuation adjustment	<b>(17,230)</b>	(17,883)
<b>Future Tax Asset – Long-term</b>	<b>37,855</b>	58,265
Current portion of future income tax asset related to corporate tax losses and SR&ED claims	<b>18,082</b>	11,889
<b>Future Tax Asset – Current</b>	<b>18,082</b>	11,889

A reconciliation of the deferred credit is as follows:

(\$ 000s)	
Amount recorded on reorganization	71,303
Amortized in 2008	(4,240)
Amortized in 2009	(12,356)
Rate adjustment 2009	425
Balance as of December 31, 2009	55,132
Amortized in first quarter of 2010	(3,567)
Amortized in second quarter of 2010	(1,461)
Amortized in third quarter of 2010	(2,282)
Rate adjustment 2010	(430)
<b>Balance as of September 30, 2010</b>	<b>47,392</b>
Current portion	15,320
Long-term portion	32,072
	<b>47,392</b>

The Company has the following tax pools, which may be used to reduce taxable income in future years, limited to the applicable rates of utilization:

(\$ 000s)	Rate of Utilization (%)	Amount
Undepreciated capital costs	20-100	23,688
Eligible capital expenditures	7	6,978
Share issue costs	20	1,811
Canadian oil and gas property expenditures	10	19,603
Canadian development expenditures	30	95,609
Canadian exploration expenditures	100	11,140
SR&ED expenditures	100	50,048
Income tax losses carried forward <sup>(1)</sup>	100	222,596
		431,473

<sup>(1)</sup> Federal income tax losses carried forward expire in the following years; 2024 - \$3,347,000, 2025 - \$7,532,000, 2026 - \$46,671,000, 2027 - \$117,189,000, 2028 - \$34,726,000, 2029 - \$13,131,000.

The Company has \$27,670,000 (December 31, 2009 - \$27,670,000) remaining of investment tax credits that expire in the following years; 2019 - \$3,469,000, 2020 - \$3,059,000, 2021 - \$4,667,000, 2022 - \$3,909,000, 2023 - \$3,155,000, 2024 - \$1,995,000, 2025 - \$2,257,000, 2026 - \$2,405,000, 2027 - \$2,009,000, 2028 - \$745,000.

The Company also has \$142,175,000 (December 31, 2009 - \$143,061,000) of capital loss carry forwards which can only be claimed against taxable capital gains.

The amount and timing of reversals of temporary differences will also depend on the Company's future operating results, and acquisitions and dispositions of assets and liabilities. A significant change in any of the preceding assumptions could materially affect the Company's estimate of the future income tax asset.

## 9. SHAREHOLDERS' EQUITY

Authorized

The Company is authorized to issue an unlimited number of common shares without nominal or par value.

Issued	Number	Amount (\$ 000s)
Common Shares		
Balance, January 1, 2010	18,619,641	121,955
Issued pursuant to Company share option plan	283,900	5,758
Transfer of contributed surplus to share capital	-	302
Balance, September 30, 2010	18,903,541	128,015

The Company is authorized to issue an unlimited number of Class "A" redeemable Preferred Shares and an unlimited number of Class "B" Preferred Shares. There are currently no outstanding Class "A" redeemable preferred shares or Class "B" preferred shares.

The number of common shares used to calculate diluted net earnings per share for the three and nine month periods ended September 30 is as follows:

	Three Months		Nine Months	
	2010	2009	2010	2009
Basic shares outstanding	<b>18,840,418</b>	18,524,851	<b>18,739,449</b>	17,821,584
Dilutive effect of share options	<b>530,549</b>	217,416	<b>534,483</b>	5,270
Diluted shares outstanding	<b>19,370,967</b>	18,742,267	<b>19,273,932</b>	17,826,854

A summary of the changes in the Company's contributed surplus is presented below:

Contributed surplus (\$ 000s)	2010	2009
Balance, beginning of period	<b>3,350</b>	2,542
Stock-based compensation expensed (non-cash)	<b>426</b>	711
Stock-based options exercised (non-cash)	<b>(302)</b>	-
Balance, end of period	<b>3,474</b>	3,253

The deficit balance is composed of the following items:

(\$ 000s)	September 30, 2010	September 30, 2009
Accumulated earnings	<b>312,395</b>	224,609
Accumulated cash dividends/distributions	<b>(319,500)</b>	(276,289)
Deficit	<b>(7,105)</b>	(51,680)

The Company provides an option plan for its directors, officers, employees and consultants. Under the plan, the Company may grant options for up to 1,890,354 common shares. The exercise price of each option granted equals the market price of the common shares on the date of grant and the option's maximum term is five years.

A summary of the status of the Company's stock option plan as of September 30, 2010 and December 31, 2009, and changes during the nine month and twelve month periods ended on those dates is presented below:

	September 30, 2010		December 31, 2009	
	Options	Weighted-Average Exercise Price	Options	Weighted-Average Exercise Price
Outstanding at beginning of period	<b>1,330,900</b>	\$ 20.36	1,390,500	\$ 20.50
Options granted	<b>30,000</b>	<b>34.66</b>	33,000	14.90
Options exercised	<b>(283,900)</b>	<b>20.28</b>	(92,600)	20.50
Outstanding at end of period	<b>1,077,000</b>	\$ 20.78	1,330,900	\$ 20.36
Options exercisable at end of period	<b>98,000</b>	\$ 20.50	370,900	\$ 20.50

The following table summarizes information about options outstanding at September 30, 2010:

Range of Exercise Prices	Options Outstanding			Options Exercisable	
	Number Outstanding At 9/30/10	Weighted-Average Remaining Contractual Life	Weighted-Average Exercise Price	Number Exercisable at 9/30/10	Weighted-Average Exercise Price
\$14.90	22,000	2.2 years	\$14.90	-	\$ -
20.50	1,025,000	2.1 years	20.50	98,000	20.50
34.66	30,000	2.2 years	34.66	-	-
\$14.90-\$34.66	1,077,000	2.1 years	\$20.78	98,000	\$20.50

The Company records compensation expense over the vesting period based on the fair value of options granted to employees, directors and consultants. In 2010, the Company granted 30,000 stock options with an estimated fair value of \$164,000 (\$5.48 per option) using the Black-Scholes option pricing model with the following key assumptions:

Weighted-average risk free interest rate (%)	1.9
Expected life (years)	3.0
Weighted-average volatility (%)	33.0
Dividend yield 2010	based on the percentage of dividends paid during the period granted

#### 10. ACCUMULATED OTHER COMPREHENSIVE INCOME

(\$ 000s)	January 1, 2010	Other Comprehensive Income	September 30, 2010
Unrealized gains on available-for-sale financial assets (net of tax of \$914)	2,020	2,088	4,108

(\$ 000s)	January 1, 2009	Other Comprehensive Income	December 31, 2009
Unrealized gains on available-for-sale financial assets (net of tax of \$347)	1,420	600	2,020

#### 11. RELATED PARTY TRANSACTIONS

The Company received a management fee from Geomark and Comaplex of \$249,000 (Comaplex 2009 - \$247,500) for management services and office administration. This fee has been included as a recovery in general and administrative expenses. At September 30, 2010, the Company had an account receivable from Geomark of \$33,000 (Comaplex December 31, 2009 - \$105,000). Effective July 6, 2010, the Company cancelled its management agreement with Comaplex due to its takeover by Agnico.

A new management agreement was entered into with Geomark effective July 6, 2010, under the same terms and conditions as those of the Comaplex agreement except that the monthly fee is \$22,500 compared to Comaplex's monthly fee of \$30,000.

The Company received a management fee from Pine Cliff Energy Ltd. (Pine Cliff) of \$67,500 (2009 - \$90,000) for management services and office administration. This fee has been included as a recovery in general and

administrative expenses. At September 30, 2010 the Company had an account receivable from Pine Cliff of \$1,000 (December 31, 2009 - \$1,000).

These transactions are in the normal course of operations and are measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties.

## **12. FINANCIAL AND CAPITAL RISK MANAGEMENT**

### Financial Risk Factors

The Company undertakes transactions in a range of financial instruments including:

- Receivables
- Restricted cash
- Payables
- Common share investments
- Due to related parties
- Bank loans

The Company's activities result in exposure to a number of financial risks including market risk (commodity price risk, interest rate risk, and foreign exchange risk), credit risk, and liquidity risk.

The Company's overall risk management program seeks to mitigate these risks and reduce the volatility on the Company's financial performance. Financial risk management is carried out by senior management under the direction of the Directors of the Company.

The Company may enter into various risk management contracts in accordance with Board approval to manage the Company's exposure to commodity price fluctuations. Currently no risk management agreements are in place. The Company does not speculatively trade in risk management contracts. The Company's risk management contracts are entered into to manage the risks relating to commodity prices from its business activities.

### Capital Risk Management

The Company's objectives when managing capital, which the Company defines to include shareholders' equity, debt and working capital balances, are to safeguard the Company's ability to continue as a going concern, so that it can continue to provide returns to its shareholders and benefits for other stakeholders and to maintain an optimal capital structure to reduce the cost of capital. In order to maintain or adjust the capital structure, the Company may adjust the amount of dividends, debt facilities or issue new shares.

The Company monitors capital on the basis of the ratio of debt to cash flow. This ratio is calculated using each quarter end net debt (total debt adjusted for working capital excluding amounts related to future taxes and deferred credits) and divided by the preceding twelve months cash flow. The Company believes that a net debt level of approximately one and a half year's cash flow is an appropriate level to allow it to take advantage in the future of either acquisition opportunities or to provide flexibility to develop its undeveloped resources by horizontal or vertical drill programs.

The following section (a) of this note provides a summary of the Company's underlying economic positions as represented by the carrying values, fair values and contractual face values of the Company's financial assets and financial liabilities. The Company's net debt to cash flow from operations is also provided.

The following section (b) addresses in more detail the key financial risk factors that arise from the Company's activities including its policies for managing these risks.

The following section (c) provides details of the Company's risk management contracts that are used for financial risk management.

a) Financial assets, financial liabilities and debt ratio

The carrying amounts, fair value and face values of the Company's financial assets and liabilities are shown in Table 1.

Table 1

(\$ 000s)	As at September 30, 2010			As at December 31, 2009		
	Carrying Value	Fair Value	Face Value	Carrying Value	Fair Value	Face Value
Financial assets						
Accounts receivable	16,975	16,975	17,044	14,713	14,713	14,873
Investments	10,123	10,123	N/A	4,462	4,462	N/A
Investment in related party	724	724	N/A	4,827	4,827	N/A
Restricted cash	-	-	-	812	812	812
Financial liabilities						
Accounts payable and accrued liabilities	19,179	19,179	19,179	18,868	18,868	18,868
Due to related parties	32,000	32,000	32,000	23,500	23,500	23,500
Bank debt	73,901	73,901	73,901	59,823	59,823	59,823

Financial instruments consisting of accounts receivable, restricted cash, accounts payable and accrued liabilities, due to related parties and long-term debt are carried on the consolidated balance sheet at amortized cost. Investments and investment in related party are carried at fair value. All of the fair value items are transacted in active markets. Bonterra classifies the fair value of these transactions according to the following hierarchy based on the amount of observable inputs used to value the instrument.

Level 1 – Quoted prices are available in active markets for identical assets or liabilities as of the reporting date. Active markets are those in which transactions occur in sufficient frequency and volume to provide pricing information on an ongoing basis.

Level 2 – Pricing inputs are other than quoted prices in active markets included in Level 1. Prices in Level 2 are either directly or indirectly observable as of the reporting date. Level 2 valuations are based on inputs, including quoted forward prices for commodities, time value and volatility factors, which can be substantially observed or corroborated in the marketplace.

Level 3 – Valuations in this level are those with inputs for the asset or liability that are not based on observable market data.

Bonterra's investments and investment in related party have been assessed on the fair value hierarchy described above and are all considered Level 1.

The net debt and cash flow figures as of September 30, 2010 are presented in Table 2.

*Table 2*  
(\$ 000s)

	<b>September 30, 2010</b>
Bank debt	<b>73,901</b>
Accounts payable and accrued liabilities	<b>19,179</b>
Due to related parties	<b>32,000</b>
Current assets <sup>(1)</sup>	<b>(30,526)</b>
<b>Net Debt</b>	<b>94,554</b>
Cash flow from operations <sup>(2)</sup>	<b>62,650</b>
<b>Net debt to cash flow from operations</b>	<b>1.51</b>

<sup>(1)</sup> Current assets include accounts receivable, crude oil inventory, prepaid expenses, and investments.

<sup>(2)</sup> Cash flow from operations includes the previous 12 months net earnings less adjustment for stock-based compensation, depletion, depreciation and accretion, gain on sale of property and investments, future income taxes, changes in non-cash working capital items, asset retirement obligations settled, restricted cash and investment tax credit receivable.

b) Risks and mitigations

Market risk is the risk that the fair value or future cash flow of the Company's financial instruments will fluctuate because of changes in market prices. Components of market risk to which the Company is exposed are discussed below.

Commodity price risk

The Company's principal operation is the production and sale of crude oil, natural gas and natural gas liquids. Fluctuations in prices of these commodities directly impact the Company's performance and ability to continue with its dividends.

The Company has used various risk management contracts to set price parameters for a portion of its production. Management, in agreement with the Board of Directors, decided that it will discontinue the use of commodity price agreements. The Company will assume full risk in respect of commodity prices.

Interest rate risk

Interest rate risk refers to the risk that the value of a financial instrument or cash flows associated with the instrument will fluctuate due to changes in market interest rates. Interest rate risk arises from interest bearing financial assets and liabilities that the Company uses. The principal exposure of the Company is on its borrowings which have a variable interest rate which gives rise to a cash flow interest rate risk.

The Company's debt facilities consists of a \$100,000,000 revolving operating line, \$20,000,000 demand operating line and \$32,000,000 due to related parties. The borrowings under these facilities are at Canadian chartered bank prime plus or minus various percentages as well as by means of bankers' acceptances (BA's) within the Company's credit facility. The Company manages its exposure to interest rate risk through entering into various term lengths on its BA's but in no circumstances do the terms exceed six months.

### *Sensitivity Analysis*

Based on historic movements and volatilities in the interest rate markets and management's current assessment of the financial markets, the Company believes that a one percent variation in the Canadian prime interest rate is reasonably possible over a 12-month period.

A one percent increase (decrease) in the Canadian prime rate would increase (decrease) annual net earnings and comprehensive income by \$762,000.

### Foreign exchange risk

The Company has no foreign operations and currently sells all of its product sales in Canadian currency. The Company is, however, exposed to currency risk in that crude oil is priced in U.S. currency then converted to Canadian currency. The Company currently has no outstanding risk management agreements. Management, in agreement with the Board of Directors, decided that at least in the near term it will discontinue the use of commodity price agreements. The Company will assume full risk in respect of foreign exchange fluctuations.

### Credit risk

Credit risk is the risk that a contracting party will not complete its obligations under a financial instrument and cause the Company to incur a financial loss. The Company is exposed to credit risk on all financial assets included on the balance sheet. To help mitigate this risk:

- The Company only enters into material agreements with credit worthy counterparties. These include major oil and gas companies or major Canadian chartered banks;
- Agreements for product sales are primarily on 30 day renewal terms; and
- Investments are generally only with companies that have common management with the Company. Investments not in related companies are reviewed continuously for value and are considered held only for short term periods.

Of the accounts receivable balance at September 30, 2010 (\$16,975,000) and December 31, 2009 (\$14,713,000) approximately 84 percent (2009 – 87 percent) relates to product sales to international oil and gas companies and drilling credits receivable from the province of Alberta.

The Company assesses quarterly, if there has been any impairment of the financial assets of the Company. The Company does have a credit risk exposure as the majority of the Company's accounts receivable are with counterparties having similar characteristics. However, payments from the Company's largest accounts receivable counterparties have consistently been received within 30 days and the sales agreements with these parties are cancellable with 30 days notice if payments are not received.

At September 30, 2010 approximately \$105,000 or approximately 0.6 percent (December 31, 2009, approximately \$244,000 or 1.6 percent) of the Company's total accounts receivable are aged over 120 days and considered past due. The majority of these accounts are due from various joint venture partners. The Company actively monitors past due accounts and takes the necessary actions to expedite collection, which can include withholding production or netting payables when the accounts are with joint venture partners. Should the Company determine that the ultimate collection of a receivable is in doubt, it will provide the necessary provision in its allowance for doubtful accounts with a corresponding charge to earnings. If the Company subsequently determines an account is uncollectable, the account is written off with a corresponding charge to the allowance account. The Company's allowance for doubtful accounts balance at September 30,

2010 is \$69,000 (December 31, 2009 - \$160,000) with the difference being included in general and administrative expenses. There were no accounts written off during the period.

The carrying value of accounts receivable approximates their fair value due to the relatively short periods to maturity on this instrument. The maximum exposure to credit risk is represented by the carrying amount on the balance sheet. There are no material financial assets that the Company considers past due.

#### Liquidity risk

Liquidity risk includes the risk that, as a result of the Company's operational liquidity requirements:

- The Company will not have sufficient funds to settle a transaction on the due date;
- The Company will not have sufficient funds to continue with its dividends;
- The Company will be forced to sell assets at a value which is less than what they are worth; or
- The Company may be unable to settle or recover a financial asset at all.

To help reduce these risks the Company:

- Maintains a portfolio of high-quality, long reserve life oil and gas assets.

The Company has the following maturity schedule for its financial liabilities:

(\$ 000s)	Recognized on Financial Statements	Payments Due by Period		
		Less than 1 year	2-3 years	4-5 years
Accounts payable and accrued liabilities	Yes - Liability	19,179	-	-
Due to related parties	Yes - Liability	32,000	-	-
Long-term bank debt	Yes - Liability	-	73,901	-
Office leases	No	1,000	1,531	89
<b>Total</b>		<b>52,179</b>	<b>75,432</b>	<b>89</b>

c) Risk management contracts

The Company has no outstanding risk management contracts.

### **13. SUBSEQUENT EVENT – DIVIDENDS**

Subsequent to September 30, 2010, the Company declared a dividend of \$0.22 per common share payable on October 29, 2010 to shareholders of record on October 15, 2010 and a dividend of \$0.22 per common share payable on November 30, 2010 to shareholders of record on November 15, 2010.

### **14. SUBSEQUENT EVENT – DEBENTURE ISSUE**

On October 4, 2010 the Company borrowed \$15,000,000 from a private investor. In exchange Bonterra has issued a Promissory Note for \$15,000,000. The terms of the Promissory Note are that it bears interest at three percent, is not callable by the investor prior to January 4, 2012 at which time it will be a demand note until its maturity of April 4, 2012, and can be repaid at the option of the Company at any time. Security consists of a floating demand debenture totaling \$15,000,000 over all of the Company's assets and is subordinated to any and all claims in favor of the syndicate of senior lenders providing credit facilities to the Company.

### **Board of Directors**

G.J. Drummond, Nassau, Bahamas  
G.F. Fink, Calgary, Alberta  
C.R. Jonsson, Vancouver, British Columbia  
F.W. Woodward, Calgary, Alberta

### **Officers**

G.F. Fink – Chief Executive Officer and Chairman of the Board  
R.M. Jarock – President and Chief Operating Officer  
G.E. Schultz – Vice President, Finance, Chief Financial Officer and Secretary

### **Registrar & Transfer Agent**

Olympia Trust Company, Calgary, Alberta

### **Auditors**

Deloitte & Touche LLP, Calgary, Alberta

### **Solicitors**

Borden Ladner Gervais LLP, Calgary, Alberta

### **Bankers**

CIBC, Calgary, Alberta  
The Royal Bank of Canada, Calgary, Alberta  
Alberta Treasury Branches, Calgary, Alberta

### **Stock Listing**

The Toronto Stock Exchange  
Trading Symbol: BNE

### **Head Office**

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### **Website**

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