Q2 2012

PETROBANK

Second Quarter Results

PETROBANK REPORTS Q2 2012 FINANCIAL RESULTS AND OPERATIONAL UPDATE

In this report, quarterly comparisons are second quarter 2012 compared to second quarter 2011 unless otherwise noted. All financial figures are unaudited and in Canadian dollars ($) unless otherwise noted.

SUMMARY OF FINANCIAL AND OPERATING RESULTS

	Three months ended June 30,			Six months ended June 30,		
	2012	2011	% Change	**2012**	2011	% Change
Financial						
($000s, except where noted)						
Oil and natural gas sales	**240,205**	274,952	(13)	**570,566**	556,249	3
Funds flow from operations [1]	**118,890**	148,440	(20)	**300,180**	316,824	(5)
Per share – basic ($)	**1.14**	1.40	(19)	**2.85**	2.98	(4)
– diluted ($)	**1.13**	1.38	(18)	**2.82**	2.93	(4)
Adjusted net income attributable to Petrobank shareholders [1]	**31,999**	30,659	4	**114,306**	30,638	273
Per share – basic ($)	**0.31**	0.29	7	**1.09**	0.29	276
– diluted ($)	**0.31**	0.28	11	**1.07**	0.28	282
Capital expenditures [1]						
PetroBakken	**109,756**	113,010	(3)	**316,177**	420,491	(25)
Heavy Oil Business Unit ("HBU")	**4,525**	55,641	(92)	**22,403**	109,896	(80)
Total capital expenditures	**114,281**	168,651	(32)	**338,580**	530,387	(36)
Total assets	**6,290,114**	6,571,119	(4)	**6,290,114**	6,571,119	(4)
Common shares outstanding, end of period (000s)						
Basic	**100,875**	106,303	(5)	**100,875**	106,303	(5)
Diluted [2]	**104,867**	110,155	(5)	**104,867**	110,155	(5)
Operations						
PetroBakken operating netback ($/boe) [1] [3]						
Oil, NGL and natural gas revenue [4]	**67.89**	85.02	(20)	**73.07**	79.34	(8)
Royalties	**9.44**	13.15	(28)	**10.80**	12.45	(13)
Production expenses	**13.37**	15.24	(12)	**12.95**	12.52	3
Operating netback [1] [3] [5]	**45.08**	56.63	(20)	**49.32**	54.37	(9)
Average daily production [3]						
PetroBakken – oil and NGL (bbls)	**32,236**	29,676	9	**36,286**	32,890	10
PetroBakken – natural gas (Mcf)	**38,874**	33,746	15	**38,597**	33,143	16
Total conventional (boe) [3][6]	**38,715**	35,300	10	**42,719**	38,414	11

(1) Non-GAAP measure. See "Non-GAAP Measures" section.

(2) Consists of common shares, stock options, directors deferred common shares, deferred common shares, and incentive shares as at the period end date.

(3) Six Mcf of natural gas is equivalent to one barrel of oil equivalent ("boe").

(4) Net of transportation expenses.

(5) Excludes hedging activities.

(6) HBU heavy oil volumes are excluded from average daily production as HBU operations are considered to be in the exploration and evaluation phase and accordingly are capitalized.

HIGHLIGHTS

Q2 2012 Financial and Operating Highlights

- Funds flow from operations decreased 20 percent from the second quarter of 2011 to $118.9 million, or $1.13 per diluted share, primarily as a result of lower commodity prices and increased differentials to WTI leading to lower gross operating netbacks at PetroBakken, partially offset by higher production.
- PetroBakken's second quarter production, after dispositions, averaged 38,715 barrels of oil equivalent per day ("**boepd**") (83% light oil and liquids weighted), a 10% increase over the second quarter of 2011.
- Capital expenditures before dispositions totalled $114.3 million in the second quarter with PetroBakken drilling 9 net wells.
- Production from Petrobank's Kerrobert project averaged 236 barrels of upgraded THAI® oil per day ("**bopd**") in Q2 2012, an increase from 193 bopd in Q1 2012. Production in July 2012 averaged 280 bopd and field estimates for August production to date averaged approximately 400 bopd.
- In mid-July, we completed our Normal Course Issuer Bid ("**NCIB**") and have repurchased and cancelled our approved limit of 7,273,401 Petrobank shares at a cost of approximately $88 million.
- Through our Automatic Share Repurchase and PetroBakken Share Sale Plan, we sold 5.5 million PetroBakken shares for proceeds of $67 million to fund a portion of the Petrobank share repurchases. The sale of one PetroBakken share for each Petrobank share repurchased under this plan resulted in net cash proceeds to Petrobank of $4.6 million.
- We increased the number of PetroBakken shares owned per Petrobank share outstanding to approximately 1.08 from 1.03 at December 31, 2011 through our participation in PetroBakken's dividend reinvestment plan, the repurchase of our shares under our NCIB and the sale of PetroBakken shares.

OPERATIONAL UPDATE

Kerrobert THAI® Project

THAI® production continues to increase. Full field production in the second quarter of 2012 averaged 236 bopd compared to 193 bopd in the first quarter of 2012. These production volumes represent actual sale volumes for each period reported. Production in July 2012 averaged 280 bopd and field estimates for August production to date averaged approximately 400 bopd. Our operating philosophy remains unchanged with a focus on increasing the air injection into the wells across the field and gradually increasing production and reducing operating costs. We are currently injecting air at approximately eight percent of full field design capacity and intend to continue to increase air injection to build out the THAI® combustion front.

Dawson THAI® Project

We received regulatory approval in early August to start the cold production phase on the two-well demonstration project. We expect to cold produce the wells for a period of time in order to condition the reservoir prior to initiating THAI® operations. With this approval we expect to commence cold production in Q3 2012.

Saskatchewan Conventional Cold Heavy Oil Production

As previously reported, we identified multiple opportunities to re-enter certain wells on our Saskatchewan lands for conventional cold heavy oil production. We have recently re-completed and placed on production five wells, which are expected to stabilize and produce oil in the fourth quarter.

LIQUIDITY AND CAPITAL RESOURCES

In mid-July, we completed our NCIB and have repurchased and cancelled our approved limit of 7,273,401 Petrobank shares at a cost of approximately $88 million. Through our Automatic Share Repurchase and PetroBakken Share Sale Plan, we sold 5.5 million PetroBakken shares for proceeds of $67 million to fund a portion of the Petrobank share repurchases. The sale of one PetroBakken share for each Petrobank share repurchased under this plan resulted in net cash proceeds to Petrobank of $4.6 million. We expect to renew our NCIB and PetroBakken share sale plan as soon as permitted under securities regulations, which is anticipated to be in mid-September.

Petrobank and PetroBakken manage their capital structure independently, generate their own cash flows and have the ability to fund their operations through the issuance of secured and unsecured debt as well as equity financing. Petrobank's capital resources are focused on funding corporate and Heavy Oil Business Unit expenditures. At June 30, 2012, on a standalone basis independent of PetroBakken, Petrobank's HBU and Corporate operating segment had cash and cash equivalents of $103.6 million and a net working capital surplus (including cash) of $95.1 million.

Based on Petrobank's current ownership and PetroBakken's current annual dividend of $0.96 per PetroBakken share, Petrobank expects to receive approximately $103 million of dividends annually from PetroBakken, paid monthly. PetroBakken instituted a DRIP in early 2012, which allows shareholders to reinvest monthly cash dividends in new shares at a five percent discount to the then current market price. Due to Petrobank's significant positive working capital balance, we elected to participate at a 100% level in PetroBakken's DRIP starting with the March dividend. We believe that receiving additional shares in PetroBakken is an attractive investment at this time. Petrobank may change our participation level in the future.

Petrobank currently expects to fund our future working capital requirements and HBU capital expenditure program with available cash and cash from operations.

MANAGEMENT'S DISCUSSION AND ANALYSIS

The following MD&A is dated August 13, 2012 and should be read in conjunction with the unaudited condensed interim consolidated financial statements and accompanying notes of Petrobank Energy and Resources Ltd. ("Petrobank", "we", "our" or the "Company") as at and for the three and six months ended June 30, 2012 ("interim Consolidated Financial Statements"), as well as the audited consolidated financial statements as at and for the year ended December 31, 2011 (the "Consolidated Financial Statements") and MD&A for the year ended December 31, 2011. The disclosures throughout the MD&A agree to Note 2 - Segmented Information in the interim Consolidated Financial Statements.

Management is responsible for preparing the MD&A. The Audit Committee of the Petrobank Board of Directors (the "Board") reviewed the MD&A and recommended its approval by the Board. The Board approved the MD&A.

This MD&A and the interim Consolidated Financial Statements and comparative information have been prepared in accordance with International Financial Reporting Standards ("IFRS") applicable to the preparation of interim financial statements, including IAS 34, *Interim Financial Reporting*, which are also generally accepted accounting principles ("GAAP") for publicly accountable enterprises in Canada. For all periods up to and including the year ended December 31, 2010, we prepared our consolidated financial statements in accordance with Canadian generally accepted accounting principles as set out in the Handbook of the Canadian Institute of Chartered Accountants Part V *Pre-changeover Accounting Standards* ("previous Canadian GAAP"). In accordance with the standard related to the first time adoption of IFRS, our transition date to IFRS was January 1, 2010 and therefore the comparative information for 2010 has been prepared in accordance with IFRS.

All amounts are presented in Canadian dollars, unless otherwise stated and all tabular amounts are in thousands of Canadian dollars, except share amounts or as otherwise noted. The energy content of natural gas has been measured in gigajoules ("GJ"). Natural gas volumes have been converted to barrels of oil equivalent ("boe"). Six thousand cubic feet ("Mcf") of natural gas is equal to one barrel ("bbl") based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead. Boes may be misleading, especially if used in isolation.

Additional information for the Company, including the Annual Information Form ("AIF"), can be found on SEDAR at www.sedar.com or at www.petrobank.com.

Forward-Looking Statements

In addition to historical information, the MD&A contains forward-looking statements that are generally identifiable as any statements that express, or involve discussions as to, expectations, beliefs, plans, objectives, assumptions or future events of performance. Specifically, this MD&A contains forward-looking statements relating to future capital plans and projects, future production levels, sources of funding and future dividend rates. Forward-looking statements are necessarily based upon assumptions and judgments with respect to the future including, but not limited to, the outlook for commodity markets and capital markets, success of future evaluation and development activities, the successful application of technology, prevailing commodity prices, the performance of producing wells and reservoirs, well development and operating performance, general economic and business conditions, weather, and the regulatory and legal environment. These statements are not historical facts and may be forward-looking and may involve estimates, assumptions and uncertainties which could cause actual results or outcomes to differ materially from those expressed in such forward-looking statements. The reader is cautioned that assumptions used in the preparation of such information, although considered reasonable at the time of preparation, may prove to be incorrect. Actual results achieved during the forecast period will vary from the information provided herein as a result of numerous known and unknown risks and uncertainties and other factors. Such factors include, but are not limited to: general economic, market and business conditions; fluctuations in oil and gas prices; the results of exploration and development of drilling and related activities; costs and availability of services; fluctuation in foreign currency exchange rates; the uncertainty of reserve estimates; changes in environmental and other regulations; risks associated with oil and gas operations; the ability to economically test, develop and utilize the Company's patented technologies, the feasibility of the technologies; and other factors, many of which are beyond the control of the Company. Accordingly, there is no representation by Petrobank that actual results achieved during the forecast period will be the same in whole or in part as those forecasts. Except to the extent required by law, Petrobank assumes no obligation to publicly update or revise any forward-looking statements made in this MD&A or otherwise, whether as a result of new information, future events or otherwise.

Non-GAAP Measures

This report contains certain financial measures, such as funds flow from operations, funds flow per share, adjusted net income, adjusted net income per share, capital expenditures and operating netback, which are not standardized measures recognized under GAAP and do not have a standardized meaning prescribed by GAAP. These measures are commonly utilized in the oil and gas industry and are considered informative for management and shareholders.

Funds flow from operations reflects cash generated from operating activities before changes in non-cash working capital. Funds flow per share is calculated as funds flow from operations divided by the weighted average number of shares outstanding for the period.

The following table reconciles cash flow from operating activities to funds flow from operations:

	Three months ended June 30,		Six months ended June 30,	
	2012	2011	**2012**	2011
Cash flow from operating activities	**147,107**	184,973	**358,896**	315,634
Adjustments:				
Changes in non-cash working capital	**(28,217)**	(36,533)	**(58,716)**	1,190
Funds flow from operations	**118,890**	148,440	**300,180**	316,824

Adjusted net income is determined by adding back to net income any losses or deducting any gains on the derivative financial liability, adding back any losses or deducting any gains on settlement of convertible debentures, and adding back impairments. Adjusted net income per share is calculated as adjusted net income divided by the weighted average number of shares outstanding for the period.

The following table reconciles net income (loss) to adjusted net income:

	Three months ended June 30,		Six months ended June 30,	
	2012	2011	**2012**	2011
Net (loss) income attributable to Petrobank shareholders	**(15,220)**	58,291	**3,267**	78,876
Adjustments:				
(Gain) loss on derivative financial liability	**(13,781)**	(32,778)	**6,030**	(61,048)
Loss on settlement of convertible debentures	**-**	-	**44,009**	-
Impairment	**61,000**	5,146	**61,000**	12,810
Adjusted net income attributable to Petrobank shareholders	**31,999**	30,659	**114,306**	30,638

Management considers funds flow from operations, funds flow per share, adjusted net income and adjusted net income per share important as they help evaluate performance and demonstrate the Company's ability to generate sufficient cash to fund future growth opportunities and repay debt.

Capital expenditures represent expenditures on property, plant and equipment, exploration and evaluation expenditures and other intangible asset expenditures.

Operating netback reflects revenues less royalties, transportation costs, and production expenses divided by production for the period. Operating netback demonstrates profitability relative to commodity prices per unit of production.

Funds flow from operations, funds flow per share, adjusted net income, adjusted net income per share, operating netback, and capital expenditures do not have standardized meanings and therefore may not be comparable to those reported by other companies, nor should they be viewed as an alternative to cash flow from operations or other measures of financial performance calculated in accordance with GAAP.

Petrobank's Operating Segments

During the three and six months ended June 30, 2012, the Company comprised of two operating segments: the Heavy Oil Business Unit ("HBU") and PetroBakken Energy Ltd. ("PetroBakken"). Where segmented information is provided throughout this MD&A, the HBU is combined with activities performed at the Petrobank parent company corporate level ("Corporate") and is referred to as "Petrobank Standalone".

The HBU operates our heavy oil projects using Petrobank's patented THAI® heavy oil recovery process in the field. THAI® (Toe to Heel Air Injection), is an evolutionary in-situ combustion technology for the recovery of heavy oil and bitumen. The HBU projects are in the exploration and evaluation phase and accordingly all expenses, net of revenues, are capitalized. Therefore, it is important to note that throughout this MD&A, results relating to the HBU are not included in operational results such as average daily production, revenue, royalties, production expenses, netbacks, or depletion and depreciation expense.

PetroBakken, 58 percent owned by Petrobank as at June 30, 2012, owns conventional oil and gas operations throughout western Canada with a primary focus on light oil developments from the Bakken formation in southeast Saskatchewan and in the Cardium play in Alberta. Petrobank results include 100 percent of PetroBakken's results; the 42 percent minority interest share, which Petrobank does not own, is recorded as income attributable to non-controlling interest ("NCI") on the consolidated statements of operations and comprehensive income and as paid-in capital and NCI on the consolidated statements of financial position.

Comparatives

Comparisons presented in this MD&A are the three and six months ended June 30, 2012 compared to the three and six months ended June 30, 2011, unless otherwise noted.

FINANCIAL AND OPERATIONAL REVIEW

PETROBANK STANDALONE

Significant Transactions

- We sold the May River oil sands property on February 28, 2012, including the Conklin demonstration project, for cash proceeds of approximately $225 million, net of closing adjustments, and concurrently cancelled our credit facility and withdrew our May River regulatory application.
- Through to June 30, 2012, we repurchased 6,357,000 Petrobank common shares through our Normal Course Issuer Bid for a total cost of $78.0 million. To help fund a portion of the Petrobank share repurchases, we sold 4,574,800 PetroBakken common shares for proceeds of $55.5 million.

As previously described, the HBU operations are in the exploration and evaluation phase and accordingly operating costs and royalties, net of any revenues received, are charged to exploration assets as opposed to being recognized in net income.

The following table includes Petrobank Standalone results only.

	Three months ended June 30,			Six months ended June 30,		
	2012	2011	Change	**2012**	2011	Change
General and administrative	**2,870**	3,877	(26%)	**6,847**	6,998	(2%)
Share-based compensation	**327**	2,532	(87%)	**(467)**	4,574	-
Finance and other	**(273)**	681	-	**823**	1,275	(35%)
Impairment	**-**	5,146	(100%)	**-**	12,810	(100%)
Foreign exchange (gain) loss	**(72)**	1	-	**(102)**	27	-
Depletion and depreciation expense	**225**	203	11%	**449**	391	15%
Deferred income tax recovery	**-**	(2,149)	(100%)	**-**	(5,060)	(100%)
Net loss for operating segment	**3,077**	10,291	(70%)	**7,550**	21,015	(64%)

General and Administrative

Total general and administrative costs decreased in the three months ended June 30, 2012 primarily due to fewer personnel related costs as a result of a decrease in the number of employees associated with the sale of our May River oil sands property.

Share-Based Compensation

Share-based compensation expenses relate to stock options, deferred common shares, directors deferred common shares and incentive shares (collectively, "Share-Based Awards") granted. The calculation of this non-cash expense is based on the fair value of the Share-Based Awards granted, amortized over the vesting period of the option or incentive share using the graded vesting method, or immediately upon grant of the deferred common shares and directors deferred common shares.

The decrease in share-based compensation in the three and six months ended June 30, 2012 is due primarily to the forfeiture of Share-Based Awards as a result of a decrease in the number of employees associated with the sale of our May River oil sands property. The expense incurred related to unvested Share-Based Awards is reversed upon forfeiture.

Finance and Other

Finance and other expenses includes accretion on decommissioning liabilities, amortization of deferred financing costs, and cash interest expense, offset by interest income. Cash interest expense includes interest on bank debt and standby fees.

The Petrobank Standalone segment capitalizes interest on bank debt in accordance with our accounting policy. The decrease in finance and other costs during the three and six months ended June 30, 2012 is a result of the cancellation of the credit facility at the end of February 2012. The excess cash held by the Company resulting from the sale of our May River oil sands property has been invested in short term bankers' acceptances and is earning interest income.

Impairment

The impairment expense during the three and six months ended June 30, 2011 of $5.1 million and $12.8 million, respectively, related to capitalized operating costs at our HBU's Conklin cash generating unit ("CGU"). Conklin was our oil sands demonstration project operating near Conklin, Alberta. By the end of the third quarter of 2011 we had completed all of our near-term testing operations scheduled for Conklin and we suspended the facility in the fourth quarter of 2011. Our May River oil sands property, which included the Conklin demonstration project, was sold on February 28, 2012 for cash proceeds of approximately $225 million, net of closing adjustments. As such, there is no related impairment in 2012.

Foreign Exchange (Gain) Loss

There is an immaterial foreign exchange impact in the first half of 2012 and 2011 as most of the Petrobank Standalone transactions are in Canadian dollars.

Depletion and Depreciation Expense

Petrobank Standalone depletion and depreciation expense includes only depreciation on other fixed assets and other intangible assets.

Deferred Income Tax Recovery

The calculated deferred income tax recovery has not been recorded to date in 2012 as it is not probable that future taxable profit will be available against which the deferred tax asset can be utilized. The calculated deferred income tax recovery for the three and six months ended June 30, 2012 was consistent with income earned adjusted for non-deductible tax items.

Capital Expenditures	Three months ended June 30,			Six months ended June 30,		
	2012	2011	Change	**2012**	2011	Change
Property, plant and equipment	**(69)**	272	-	**70**	376	(81%)
Exploration and evaluation	**4,448**	55,062	(92%)	**21,954**	108,975	(80%)
Other intangible assets	**146**	307	(52%)	**379**	545	(30%)
Total capital expenditures	**4,525**	55,641	(92%)	**22,403**	109,896	(80%)

Capital Expenditures By Type	Three months ended June 30,			Six months ended June 30,		
	2012	2011	Change	**2012**	2011	Change
Drilling, completions and workovers	**739**	34,700	(98%)	**1,326**	60,833	(98%)
Facilities	**496**	15,470	(97%)	**3,737**	36,673	(90%)
Land, seismic and exploration	**260**	890	(71%)	**3,457**	3,073	12%
Other [(1)]	**3,030**	4,581	(34%)	**13,883**	9,317	49%
Total capital expenditures	**4,525**	55,641	(92%)	**22,403**	109,896	(80%)

(1) Includes health, safety and environmental, capitalized salaries and benefits for qualifying employees, office furniture and fixtures and computer equipment, capitalized interest expense and operating costs, net of revenue, for projects in the exploration and evaluation phase, and expenditures on other intangible assets.

Exploration and Evaluation Expenditures by CGU – Three months ended June 30, 2012

	Drilling, Completions, and Workovers	Facilities	Land, Seismic and Exploration	Other [1]	Total
Kerrobert	468	451	30	2,693	3,642
Dawson	-	-	24	166	190
Plover	271	45	192	30	538
Other	-	-	14	64	78
Total	**739**	**496**	**260**	**2,953**	**4,448**

[1] Includes health, safety and environmental, capitalized salaries and benefits for qualifying employees, and capitalized interest and operating costs, net of revenue, for projects in the exploration and evaluation phase.

Exploration and Evaluation Expenditures by CGU – Six months ended June 30, 2012

	Drilling, Completions, and Workovers	Facilities	Land, Seismic and Exploration	Other [1]	Total
Kerrobert	468	790	247	8,732	10,237
Conklin and May River	-	1,140	39	3,495	4,674
Dawson	587	1,762	30	864	3,243
Plover	271	45	3,071	211	3,598
Other	-	-	70	132	202
Total	**1,326**	**3,737**	**3,457**	**13,434**	**21,954**

[1] Includes health, safety and environmental, capitalized salaries and benefits for qualifying employees, and capitalized interest and operating costs, net of revenue, for projects in the exploration and evaluation phase.

The majority of HBU expenditures in the three and six months ended June 30, 2012 related to drilling three stratigraphic wells at our Plover property, capitalized operating costs, net of revenue, incurred at Kerrobert, and facility commitments related to our May River and Dawson projects.

The HBU operates two significant projects which have not commenced generating significant revenue:

Kerrobert:

Production continued its upward trend in the second quarter averaging 236 barrels of oil per day ("bopd"), compared to 193 bopd in the first quarter of 2012. Subsequent to quarter end, production has further increased to 280 bopd in July. These production volumes represent actual sale volumes for each period reported. Oil production continues to average 13 to 14 degrees API, providing more evidence that upgraded THAI® oil is being produced.

Since the full Kerrobert field was placed on production in September 2011, we have maintained a consistent and patient operating philosophy to rateably increase sustained production of upgraded THAI® oil. This philosophy includes managing air injection rates in order to gradually build out the combustion front and optimizing the type, configuration and placement of the production pumps to extend their useful life and reduce downtime and maintenance costs. Our optimization strategy also includes reducing downtime of our surface facilities. Based on our experience with the two pilot wells, as the initial cold native oil production transitions to hot upgraded THAI® oil production, we expect production rates to greatly improve. However, our operating approach may extend the time frame for achieving project design production rates.

Our operational plan at Kerrobert is to continue to increase air injection rates, build out the combustion front as mentioned, increase production of upgraded THAI® oil, and reduce per barrel costs with the focus on reaching commercial production levels and beyond in 2012.

Dawson:

Our Dawson demonstration project was initially planned to consist of two THAI® well-pairs. The project is located in the Peace River, Alberta area, situated on a large Bluesky formation of heavy oil/oil sands fairway. In the second half of 2011 we drilled two THAI® well-pairs that are waiting for completion. The surface facilities are on location and are ready to be installed. Completion of this project was deferred in late 2011 to save costs associated with winter start-up of a THAI® project. Since that time, we have continued to review the Dawson reservoir and project plans. Based on this analysis, we have determined that the Dawson reservoir would benefit from being pre-conditioned for THAI® operations by producing conventional cold heavy oil from our current horizontal production wells. We may drill additional horizontal conventional production wells near the demonstration project area during this period to further pre-condition the reservoir for THAI® operations. We expect to begin the two-well THAI® demonstration project in 2013 and the full field THAI® development application is expected to be filed after the THAI® demonstration project is on production.

Commitments

The following is a summary of the estimated costs required to fulfill Petrobank Standalone's remaining contractual commitments as at June 30, 2012:

Type of Commitment	< 1 Year	1-3 Years	4-5 Years	Thereafter	Total
Office operating leases [1]	$ 1,229	$ 1,247	$ 386	$ 431	$ 3,293
Finance leases	295	1,059	97	-	1,451
Total Commitments	**$ 1,524**	**$ 2,306**	**$ 483**	**$ 431**	**$ 4,744**

(1) Minimum lease payments are net of sub-lease payments received by Petrobank, which reduces rent expense included in general and administrative expenses on the consolidated statement of operations.

Liquidity and Capital Resources

Petrobank Standalone and PetroBakken manage their capital structure independently and generate their own cash flows, and have the ability to fund their operations through the issuance of secured and unsecured debt as well as equity financing. Petrobank may also sell a portion of our ownership in PetroBakken to fund operations. The table below outlines the composition of Petrobank Standalone's capital structure and liquidity as at June 30, 2012:

	Petrobank Standalone
Working capital surplus [1]	**$ 95,052**
Bank debt – principal	**$ -**
Common share capital	**$ 1,490,870**
Credit facility	**$ -**
Committed credit capacity	**$ -**

(1) Working capital surplus is calculated as the operating segment's current assets less current liabilities.

At June 30, 2012, Petrobank Standalone had a working capital surplus of $95.1 million, including $103.6 million in cash and cash equivalents.

Petrobank manages our capital structure and makes adjustments to it in light of changes in economic conditions and the risk characteristics of the underlying assets. Petrobank considers our capital structure to include common share capital and working capital. In order to maintain or adjust the capital structure, from time to time Petrobank may issue common shares or other securities, sell a portion of our ownership in PetroBakken or other corporate assets or adjust our capital spending to manage current and projected cash levels.

Petrobank received cash proceeds of approximately $225.0 million, net of closing adjustments, on February 28, 2012 from the sale of our May River property. Proceeds from this transaction were used to repay outstanding bank debt and resulted in Petrobank having a significant positive cash and working capital balance. We cancelled our credit facility concurrent with the closing of the sale due to our cash availability and to save on standby fees.

Based on Petrobank's current ownership and PetroBakken's current annual dividend of $0.96 per PetroBakken share, Petrobank expects to receive approximately $103 million of dividends annually from PetroBakken, paid monthly. PetroBakken instituted a dividend re-investment plan ("DRIP") in 2012, which allows shareholders to reinvest monthly cash dividends in new shares at a five percent discount to the then current market price. During the six months ended June 30, 2012, Petrobank received dividends totalling approximately $8.8 million in cash and 3,393,068 PetroBakken common shares from the DRIP. Due to Petrobank's significant positive working capital balance, we elected to participate at a 100 percent level in PetroBakken's DRIP, starting with the March dividend. Petrobank may change its participation level in the future.

In April 2012, Petrobank entered into an Automatic Share Repurchase and PetroBakken Share Sale Plan (the "Plan") pursuant to which our designated broker was instructed to automatically sell one PetroBakken share for each Petrobank share purchased under the Plan, subject to certain trading parameters set forth in the Plan and to daily and aggregate trading limits imposed by the rules and policies of the Toronto Stock Exchange. Under the Plan, during the three and six months ended June 30, 2012, the broker repurchased 4,574,800 Petrobank shares and sold 4,574,800 PetroBakken shares for net proceeds to Petrobank of approximately $3.6 million. Petrobank repurchased an additional 1,782,200 shares during the six months ended June 30, 2012 under our Normal Course Issuer Bid ("NCIB") for $26.0 million. As of July 16, 2012, we completed the Plan and our NCIB. In total, we repurchased our approved limit of 7,273,401 Petrobank shares at a cost of $88.0 million and sold 5,491,201 PetroBakken shares for proceeds of $66.5 million to fund a portion of the Petrobank share repurchases. The transactions under the Plan resulted in net cash proceeds to Petrobank of $4.6 million. Upon completion of the Plan and our NCIB, the number of PetroBakken shares owned per Petrobank share outstanding increased to approximately 1.08 from 1.03 at December 31, 2011.

Petrobank currently expects to fund our working capital requirements and HBU capital expenditure program with available cash and cash from operations.

Capital Plan

HBU activity in the remainder of 2012 will focus on increasing Kerrobert production and bringing the project to commerciality. We are also anticipating capital expenditures at Dawson in 2012 in order to convert the horizontal THAI® production wells into conventional production wells and initiate conventional production. We have commenced converting or reactivating some of the existing wells on our Saskatchewan lands to cold conventional heavy oil production. We will also continue to invest in other development areas and plan to drill several stratigraphic wells at Plover and Luseland, near our Kerrobert project, and acquire seismic to further delineate these assets for future development. In addition, we are undertaking research and development activities at Archon Technologies Ltd., our wholly owned technology subsidiary, to improve and protect our intellectual property.

Dividends

The Petrobank legal entity has not paid or declared any dividends since the date of incorporation.

PETROBAKKEN

Significant Transactions

- On January 30, 2012, PetroBakken closed a private placement of senior unsecured notes (the "Notes") with a principal amount of US$900 million. The Notes bear interest at a rate of 8.625 percent per annum and mature February 1, 2020.
- On January 31, 2012, PetroBakken completed the repurchase of US$450 million of convertible debentures at a price of US$99,000 per US$100,000 of principal amount.
- In the first six months of the year, PetroBakken closed non-core asset dispositions for gross proceeds $637.6 million, which included the disposal of primarily non-operated southeast Saskatchewan Bakken assets for gross proceeds of $427.0 million on March 16, 2012, the disposal of a 2.2 percent interest in the Weyburn unit for gross proceeds of $105.0 million on February 24, 2012, the disposal of other minor non-core assets and the disposition of undeveloped land. Total production disposed of in the first six months of 2012 was 3,650 barrels of oil equivalent per day ("boepd").

Average Daily Production

	Three months ended June 30,			Six months ended June 30,		
	2012	2011	Change	**2012**	2011	Change
Oil and natural gas liquids ("NGL") (bbls)	**32,236**	29,676	9%	**36,286**	32,890	10%
Natural gas (Mcf)	**38,874**	33,746	15%	**38,597**	33,143	16%
Total PetroBakken (boe)	**38,715**	35,300	10%	**42,719**	38,414	11%

Production increased by 10 and 11 percent, respectively, for the three and six months ended June 30, 2012 primarily due to the increase in oil production resulting from the execution of PetroBakken's new well program, both in the first quarter of 2012 and the second half of 2011. The increase in gas production was primarily the result of gas associated with PetroBakken's light-oil properties and investment in gas conservation infrastructure. During the three months ended June 30, 2012, PetroBakken's capital program was limited as a result of spring-break-up, resulting in a decline in production and limited drilling activity. In the second quarter of 2012, PetroBakken drilled 9 net wells and brought 16 net wells on production. In the first six months of 2012, PetroBakken drilled 56 net wells and brought 52 net wells on production.

Beginning in late 2011 and continuing through the first half of 2012, PetroBakken executed divestitures of non-core assets that resulted in 4,100 boepd of production being sold for gross proceeds of $653.6 million. The proceeds were initially used to reduce PetroBakken's overall debt and a portion is expected to be used for reinvestment in core assets.

In southeast Saskatchewan, the Bakken business unit averaged 14,819 boepd of production, a decrease of 29 percent over the first quarter. A significant portion of the production decrease from the first quarter was the result of the 2,900 boepd non-core Bakken disposition which occurred near the end of the first quarter. In addition, spring break-up resulted in moderation of field activity and shut-in production due to limited access to wells. Activity increased towards the end of the second quarter as production was restored and there were 6 net wells drilled and 4 net wells brought on production. At June 30, 2012, there were 8 net wells waiting to go on production.

In Alberta, year over year PetroBakken continued to execute and grow production in the Cardium business unit, which averaged 15,912 boepd in the three months ended June 30, 2012, an increase of 71 percent over the same period in the prior year. Production declined slightly by four percent over the first quarter of 2012 due to plant and battery turnarounds, as well as downtime caused by spring break-up related road bans limiting lease access to service wells and transport oil. However, PetroBakken was still able to bring 11 net wells on production in the quarter, leaving 6 net wells waiting to be completed and/or brought on production at June 30, 2012. This is lower than a normal inventory level as drilling activity was limited by break-up. At the beginning of August, PetroBakken had 13 net wells waiting to be completed and/or brought on production as field activity has resumed.

Field estimates for July production are approximately 38,250 boepd, which did not materially increase from June as activity was ramping up throughout the month. At the beginning of August, PetroBakken had 27 net wells waiting to be completed or brought on production. Production is also being restored due to lower down-time as road bans were lifted and personnel were able to access sites that required service.

Average Benchmark and Realized Prices

	Three months ended June 30,			Six months ended June 30,		
	2012	2011	Change	**2012**	2011	Change
WTI (US$/bbl)	**93.49**	102.56	(9%)	**98.21**	98.33	-
WTI ($/bbl)	**94.31**	99.20	(5%)	**98.18**	95.98	2%
Edmonton Par ($/bbl)	**83.95**	103.07	(19%)	**88.09**	95.52	(8%)
Differential % of WTI	**(11%)**	4%	-	**(10%)**	-	-
AECO natural gas ($/Mcf)	**1.90**	3.88	(51%)	**2.02**	3.81	(47%)
US$ per C$1	**1.01**	0.97	4%	**1.01**	0.98	3%
Oil and NGL						
Realized price per bbl ($/bbl)	**79.35**	97.05	(18%)	**83.95**	89.25	(6%)
Differential % of Edmonton Par	**(5%)**	(6%)	(17%)	**(5%)**	(7%)	(29%)
Natural gas						
Realized price per Mcf ($/Mcf)	**2.10**	4.19	(50%)	**2.30**	4.16	(45%)

In the second quarter of 2012, realized oil and NGL prices decreased due to lower oil prices and continued wide price differentials to Canadian WTI. In the first six months of 2012, realized oil and NGL prices decreased due to wider differentials to Canadian WTI. The widening differential was the result of a persistent weakness of Edmonton par and other Canadian prices relative to WTI, which reflected decreased demand for Canadian sourced crude, in part caused by refinery turnarounds, short-term pipeline issues, and an increase in U.S. based supply. Oil differentials have been volatile in the first six months of the year, ranging from a historically normal five percent discount to as high as a 20 percent discount to WTI. More recently, differentials have been trending narrower, but PetroBakken does expect them to be volatile with wider than historical norms due to the lack of spare capacity in the pipeline and refining infrastructure, particularly in the mid-west U.S.

Revenue

	Three months ended June 30,			Six months ended June 30,		
	2012	2011	Change	**2012**	2011	Change
Oil and natural gas sales	**240,205**	274,952	(13%)	**570,566**	556,249	3%
Royalties	**(33,265)**	(42,240)	(21%)	**(83,948)**	(86,538)	(3%)
Total PetroBakken revenue	**206,940**	232,712	(11%)	**486,618**	469,711	4%

The change in second quarter sales is due to lower commodity prices partially offset by higher volumes. The change in year to date sales is due to increased oil volumes partially offset by lower pricing. The table below summarizes these changes:

Reconciliation of Changes in Oil and Natural Gas Sales

	Three months ended	Six months ended
June 30, 2011	274,952	556,249
Sales volume	21,188	60,906
Realized prices	(55,935)	(46,589)
June 30, 2012	**240,205**	**570,566**
$ change in oil and natural gas sales	(34,747)	14,317
% change in oil and natural gas sales	(13%)	3%

Net Realized Prices

	Three months ended June 30,			Six months ended June 30,		
	2012	2011	Change	**2012**	2011	Change
Oil and natural gas sales	**240,205**	274,952	(13%)	**570,566**	556,249	3%
Transportation expense	**1,027**	1,820	(44%)	**2,462**	4,575	(46%)
Total sales, net of transportation expense	**239,178**	273,132	(12%)	**568,104**	551,674	3%
Gross sales ($/boe)	**68.18**	85.59	(20%)	**73.39**	80.00	(8%)
Transportation costs ($/boe)	**0.29**	0.57	(49%)	**0.32**	0.66	(52%)
Realized price, net of transportation expense ($/boe)	**67.89**	85.02	(20%)	**73.07**	79.34	(8%)

Net realized price for the three months ended June 30, 2012 decreased mainly due to lower oil prices and wider differentials. Net realized price decreased for the first six months of 2012 mainly due to wider differentials. On a unit of production and total basis, transportation expense decreased in the second quarter and the first six months of 2012 primarily due to infrastructure investments made in southeast Saskatchewan resulting in single well batteries being tied-in to this infrastructure, which led to a reduction in trucking costs.

Royalties

	Three months ended June 30,			Six months ended June 30,		
	2012	2011	Change	**2012**	2011	Change
Royalties [(1)]	**33,265**	42,240	(21%)	**83,948**	86,538	(3%)
$ per boe	**9.44**	13.15	(28%)	**10.80**	12.45	(13%)
Royalties as a % of realized price, net of transportation costs	**14%**	15%	(7%)	**15%**	16%	(6%)

(1) PetroBakken royalties include the Saskatchewan Resource Surcharge determined as a percentage of sales from PetroBakken's Saskatchewan Crown lands.

Royalties decreased in the three months ended June 30, 2012 on a total and unit of production basis commensurate with the decrease in revenues and a slightly lower royalty rate. The decrease in royalty rate also led to the decrease in royalties and royalties per boe in the first six months of 2012. As a percentage of revenue, royalties decreased due to new production receiving a royalty holiday. On Crown lands in Saskatchewan, the first 37,740 boe of production from horizontal wells receive a royalty incentive but incur Saskatchewan Resource Surcharge of 1.7 percent. On Crown lands in Alberta, horizontal oil wells are subject to a maximum five percent royalty rate for 18 to 48 months or 50,000 to 100,000 boe of production, whichever comes first, depending on well length.

Gain (Loss) on Risk Management Contracts

	Three months ended June 30,			Six months ended June 30,		
	2012	2011	Change	**2012**	2011	Change
Realized gain (loss):						
Crude oil derivative contracts	**2,300**	(3,578)	-	**1,164**	(4,674)	-
Natural gas derivative contracts	**-**	435	-	**-**	1,176	-
Interest rate swap contracts	**(59)**	(212)	(72%)	**(158)**	(446)	(65%)
Foreign exchange contracts	**(75)**	-	-	**(75)**	-	-
	2,166	(3,355)	-	**931**	(3,944)	-
Unrealized gain (loss):						
Crude oil derivative contracts	**46,702**	37,626	24%	**28,856**	683	4,125%
Natural gas derivative contracts	**-**	(404)	-	**-**	(1,173)	-
Interest rate swap contracts	**56**	(135)	-	**188**	(185)	-
Foreign exchange contracts	**(37)**	-	-	**(37)**	-	-
	46,721	37,087	26%	**29,007**	(675)	-
Gain (loss) on risk management contracts	**48,887**	33,732	45%	**29,938**	(4,619)	-

PetroBakken enters into commodity price derivative contracts to limit exposure to declining commodity prices, thereby protecting project economics and providing increased stability of cash flows, dividends and capital expenditure programs. Commodity prices fluctuate for a number of reasons including changes in economic conditions, political events, weather conditions, disruptions in supply, and changes in demand. PetroBakken's risk management activities are conducted pursuant to risk management policies that have been approved by PetroBakken's Board of Directors.

PetroBakken enters into foreign exchange contracts to limit exposure to variability in exchange rates on U.S. dollar interest payments on the senior unsecured notes and convertible debentures, thereby providing increased stability of cash flows. At June 30, 2012, PetroBakken recorded a $0.1 million liability related to foreign exchange contracts. All foreign exchange contracts have been realized subsequent to June 30 2012.

PetroBakken's financial commodity derivative contracts are option-based contracts and as such their fair value at a particular point in time is affected by underlying commodity prices, expected commodity price volatility and the duration of the contract. The fair value of fixed price derivative contracts at a particular point in time is determined by the expected future settlements of the underlying commodity or interest rate. At June 30, 2012, the fair value of financial derivative contracts was an asset of $28.0 million (December 31, 2011 - liability of $1.0 million). The fair value of this asset represents the estimated amount that would be received for settling PetroBakken's outstanding contracts on June 30, 2012 and will be different than what will eventually be realized.

The gain or loss on risk management contracts is made up of two components; the realized component reflects actual settlements that occurred during the period, and the unrealized component represents the change in the fair value of contracts during the period. The unrealized gain on risk management contracts in the second quarter and the first six months of 2012 was primarily the result of the fluctuations in expected future WTI prices.

Production Expenses

	Three months ended June 30,			Six months ended June 30,		
	2012	2011	Change	**2012**	2011	Change
Production expenses	**47,086**	48,947	(4%)	**100,721**	87,084	16%
$ per boe	**13.37**	15.24	(12%)	**12.95**	12.52	3%

Production expenses decreased on a total and unit of production basis in the three months ended June 30, 2012 as the prior year had unusually high operating costs due to a severe spring break-up. On a total basis, production expenses increased in the first six months of 2012 as a result of higher production. On a unit of production basis, costs increased in the first six months of 2012 primarily due to cost inflation in the first quarter in the Bakken and Cardium due to increased demand for services. In particular, trucking costs increased in the Cardium due to increased wait times. Costs increased by six percent or $0.76 per boe in the second quarter of 2012 from $12.61 per boe in the first quarter of 2012, primarily due to lower volumes but consistent fixed costs leading to an increased cost per boe. Costs are expected to decrease during the year as PetroBakken restores and grows production, and completes infrastructure in the third and fourth quarters to reduce trucking activities.

Netbacks ($/boe)

	Three months ended June 30,			Six months ended June 30,		
	2012	2011	Change	**2012**	2011	Change
Oil, NGL and natural gas sales [1]	**67.89**	85.02	(20%)	**73.07**	79.34	(8%)
Royalties	**9.44**	13.15	(28%)	**10.80**	12.45	(13%)
Production expenses	**13.37**	15.24	(12%)	**12.95**	12.52	3%
Operating netback [2]	**45.08**	56.63	(20%)	**49.32**	54.37	(9%)

(1) Net of transportation expenses.
(2) Non-GAAP measure. See "Non-GAAP Measures" section within the MD&A.

The decrease in PetroBakken's netbacks for the three and six months ended June 30, 2012 was primarily due to the decrease in realized oil prices.

General and Administrative Expenses

	Three months ended June 30,			Six months ended June 30,		
	2012	2011	Change	**2012**	2011	Change
General and administrative expenses	**12,525**	9,594	31%	**24,502**	18,404	33%
$ per boe	**3.56**	2.99	19%	**3.15**	2.65	19%

General and administrative costs increased in the three and six months ended June 30, 2012 on an absolute and per boe basis due primarily to additional personnel and office costs as a result of expanding operations.

Share-Based Compensation Expenses

	Three months ended June 30,			Six months ended June 30,		
	2012	2011	Change	**2012**	2011	Change
Share-based compensation expense	**3,832**	3,704	3%	**10,038**	9,148	10%

Share-based compensation expense relates to stock options, deferred common shares and incentive shares granted. The calculation of this non-cash expense is based on the fair value of stock options, deferred common shares and incentive shares granted, amortized over the vesting period of the option and incentive share or immediately upon grant of the deferred common share. The increase in share-based compensation is primarily due to new grants.

Gain (Loss) on Derivative Financial Liability

	Three months ended June 30,			Six months ended June 30,		
	2012	2011	Change	**2012**	2011	Change
Gain (loss) on derivative financial liability	**13,781**	32,778	(58%)	**(6,030)**	61,048	-

The gain (loss) on the derivative liability represents the change in the fair value of derivative financial liability on the convertible debentures between the beginning and the end of the period. The fair value is determined using the Black-Scholes valuation model; refer to Note 9 in the interim Consolidated Financial Statements for further details.

The gain in the second quarter of 2012 is primarily due to a lower share price at June 30, 2012 compared to March 31, 2012. Although there was a slightly lower share price at June 30, 2012 compared to December 31, 2011, there is a loss in the first six months of 2012 as the gain on the remaining US$300 million outstanding convertible debentures does not fully offset the loss incurred in January 2012 on the then outstanding US$700 million of convertible debentures (prior to the US$450 million repurchase of convertible debentures on February 1, 2012 as the share price at January 31, 2012 was higher than the share price at December 31, 2011).

Finance and Other Expenses

	Three months ended June 30,			Six months ended June 30,		
	2012	2011	Change	**2012**	2011	Change
Interest on credit facility and other	**4,226**	9,650	(56%)	**13,498**	17,510	(23%)
Interest expense on convertible debentures	**2,354**	5,655	(58%)	**5,984**	11,384	(47%)
Accretion of the convertible debentures	**2,604**	5,785	(55%)	**6,435**	11,505	(44%)
Interest expense on senior unsecured notes	**19,496**	-	-	**32,160**	-	-
Accretion of senior unsecured notes	**553**	-	-	**905**	-	-
Amortization of deferred financing costs	**477**	1,061	(55%)	**973**	2,402	(59%)
Accretion of decommissioning liability	**1,347**	1,346	-	**2,688**	2,690	-
Finance and other expense	**31,057**	23,497	32%	**62,643**	45,491	38%

Interest expense on the credit facility includes interest on bank debt, stand-by fees, and fees on letters of credit. Interest on the credit facility decreased in the three and six months ended June 30, 2012 primarily due to lower bank debt outstanding during the period. A portion of the bank debt was repaid at the end of January 2012 when the senior unsecured notes were issued, and the amount outstanding continued to decrease in February and March commensurate with disposition activity. The balance began to increase in April 2012 as a result of capital spending. On average, bank debt outstanding in the second quarter of 2012 was $274 million as compared to $1,040 million in the second quarter of 2011, and $511 million for the first six months of 2012 as compared to $815 million in the first six months of 2011.

Accretion and interest expense on the convertible debentures decreased due to the repurchase of US$450 million of the US$750 million principal amount outstanding in the first quarter of 2012.

Interest and accretion on senior unsecured notes are due to the issuance of US$900 million of senior unsecured notes on January 30, 2012. Accretion on the senior unsecured notes relates to the amortization of the issuance fees and the issuance discount over the life of the senior unsecured notes.

(Loss) Gain on Dispositions

	Three months ended June 30,			Six months ended June 30,		
	2012	2011	Change	**2012**	2011	Change
(Loss) gain on dispositions	**(6,256)**	15,440	-	**122,699**	15,192	708%

The loss on dispositions in the second quarter of 2012 relates to the disposal of a minor property for net proceeds of $11.3 million. The gain on dispositions in the first six months for 2012 relates to the disposal of non-core properties for net proceeds of $627.8 million ($637.6 million gross), representing approximately 3,650 boepd of production sold. The gain in the three and six months ended June 30, 2011 relates to the disposition of minor properties for net proceeds of $21.3 million and $22.6 million respectively.

Loss on Settlement of Convertible Debentures

The loss on convertible debentures of $44.0 million in the first six months of 2012 relates to the repurchase of US$450 million principal amount of the convertible debentures and consists of acceleration of the accretion on the retired portion of the convertible debenture liability of $72.1 million, partially offset by a gain on the derivative liability of $28.1 million.

Impairment

	Three months ended June 30,			Six months ended June 30,		
	2012	2011	Change	**2012**	2011	Change
Impairment	**61,000**	-	-	**61,000**	-	-

The impairment recognized in the three and six months ended June 30, 2012 is related to PetroBakken's gas weighted BC CGU, and is the result of a decline in the fair value less costs to sell of the undeveloped land, land expiries and PetroBakken's intention not to actively develop these assets at this time. Of the impairment, $31.1 million is related to exploration assets, and $29.9 million is related to property, plant and equipment.

Foreign Exchange Loss (Gain)

	Three months ended June 30,			Six months ended June 30,		
	2012	2011	Change	**2012**	2011	Change
Foreign exchange loss (gain)	**22,443**	(4,584)	-	**8,324**	(18,759)	-

PetroBakken recognizes foreign exchange gains and losses primarily due to the appreciation or depreciation of the Canadian dollar relative to the U.S. dollar. PetroBakken's convertible debentures and senior unsecured notes are denominated in U.S. dollars and, as a result, the vast majority of unrealized foreign exchange gains or losses relate to the change in the foreign exchange rate compared to the rate at the end of the previous period. A weaker Canadian dollar at June 30, 2012 compared to March 31, 2012 and December 31, 2012 resulted in a foreign exchange loss in the second quarter and the first six months of 2012.

Depletion and Depreciation Expense

	Three months ended June 30,			Six months ended June 30,		
	2012	2011	Change	**2012**	2011	Change
Depletion and depreciation expense	**101,504**	83,348	22%	**220,149**	183,368	20%
$ per boe	**28.81**	25.95	11%	**28.32**	26.37	7%

On an absolute basis, depletion and depreciation expense increased in the second quarter and the first six months of 2012 primarily due to higher production. On a unit of production basis, the rate increased as positive reserve additions were offset by an increase in future development costs related to undeveloped reserves.

Income Tax Expense

	Three months ended June 30,			Six months ended June 30,		
	2012	2011	Change	**2012**	2011	Change
Income tax expense	**4,388**	31,396	(86%)	**82,098**	41,706	97%

The income tax expense in the second quarter of 2012 is consistent with the net loss adjusted for non-deductible items. The increased income tax expense in the first six months of 2012 was due primarily to non-deductible differences of $30.2 million on disposed properties related to goodwill associated with the assets, $11.4 million related to the loss on the settlement of convertible debentures and $1.6 million related to the change in the derivative liability valuation. Excluding these items, income tax expense for the first six months of 2012 is consistent with income earned adjusted for other non-deductible tax items generating an effective tax rate of 31 percent. Income tax expense for the first six months of 2012 also includes $1.0 million in current tax expense related to the U.S. asset disposition for proceeds of $7.8 million.

Net (Loss) Income Attributable to Non-Controlling Interest

	Three months ended June 30,			Six months ended June 30,		
	2012	2011	Change	**2012**	2011	Change
Net (loss) income attributable to NCI	**(9,367)**	48,358	-	**6,462**	70,424	(91%)

The net (loss) income attributable to NCI represents the minority interest share, which Petrobank does not own. The non-controlling interest share in PetroBakken averaged approximately 41 percent in both the three and six months ended June 30, 2012 and 2011.

Capital Expenditures

	Three months ended June 30,			Six months ended June 30,		
	2012	2011	Change	**2012**	2011	Change
Property, plant and equipment	**104,093**	86,358	21%	**306,377**	391,227	(22%)
Exploration and evaluation	**5,663**	26,652	(79%)	**9,800**	29,264	(67%)
Total capital expenditures	**109,756**	113,010	(3%)	**316,177**	420,491	(25%)

Capital Expenditures by Type

	Three months ended June 30,			Six months ended June 30,		
	2012	2011	Change	**2012**	2011	Change
Drilling, completions, equipping and recompletions	**64,264**	55,616	16%	**241,927**	323,534	(25%)
Facilities	**30,598**	20,014	53%	**49,515**	44,896	10%
Land	**6,688**	24,250	(72%)	**11,274**	26,638	(58%)
Seismic	**2,140**	960	123%	**2,756**	1,806	53%
Other [1]	**5,871**	9,556	(39%)	**10,295**	20,162	(49%)
Capital expenditures before acquisitions	**109,561**	110,396	(1%)	**315,767**	417,036	(24%)
Asset acquisitions	**195**	2,614	(93%)	**410**	3,455	(88%)
Total capital expenditures	**109,756**	113,010	(3%)	**316,177**	420,491	(25%)
Proceeds from dispositions	**(11,313)**	(21,305)	(47%)	**(627,820)**	(22,589)	2,679%
Net capital expenditures	**98,443**	91,705	7%	**(311,643)**	397,902	-

(1) Includes health, safety and environmental, capitalized salaries and benefits for qualifying employees, office furniture and fixtures and leasehold improvements.

Drilling Activity (Net), for the three months ended June 30, 2012 and 2011

	Net wells drilled		Net wells pending completion and/or tie-in		Dry and abandoned wells		Success Rate	
Business Unit	**2012**	2011	**2012**	2011	**2012**	2011	**2012**	2011
Bakken	**6** [1]	-	**8**	8	**-**	-	**100%**	100%
Conventional	**1**	-	**1**	2	**-**	-	**100%**	100%
Cardium	**2**	4	**6**	13	**-**	-	**100%**	100%
BC/Other AB	**-**	-	**-**	1	**-**	-	**100%**	100%
Total	**9**	**4**	**15**	**24**			**100%**	**100%**

(1) Includes 4 net bilateral wells (2011 - nil).

Drilling Activity (Net), for the six months ended June 30, 2012 and 2011

Business Unit	Net wells drilled		Net wells pending completion and/or tie-in		Dry and abandoned wells		Success Rate	
	2012	2011	**2012**	2011	**2012**	2011	**2012**	2011
Bakken	**29** [(1)]	33 [(1)]	**8**	8	**-**	-	**100%**	100%
Conventional	**8**	4	**1**	2	**2**	-	**75%**	100%
Cardium	**19**	42	**6**	13	**-**	1	**100%**	98%
BC/Other AB	**-**	2	**-**	1	**-**	-	**100%**	100%
Total	**56**	**81**	**15**	**24**	**2**	1	**96%**	**99%**

(1) Includes 20 net bilateral wells (2011 – 21.2 net).

The majority of PetroBakken's capital expenditures in the second quarter and first six months of 2012 were focused on drilling, completions, equipping, recompletions, and facilities. Spending in the second quarter of 2012 was lower than in the first quarter of 2012 as a result of spring break-up curtailing the drilling program. As compared to prior year, reduced crown land spending in the second quarter of 2012 was offset by an increase in facilities spending as PetroBakken constructed batteries and expanded gathering systems in the Cardium in central Alberta. The initial capital plan for 2012 contemplated reduced spending and, as a result, capital expenditures in the first six months of 2012 were lower than the prior year as fewer wells were drilled in the Cardium and in the Bakken in southeast Saskatchewan. Activity is expected to increase in the second half of the year as $175 million of the proceeds from dispositions is re-invested, primarily in the Cardium business unit. PetroBakken's revised 2012 capital program is expected to be $875 million. Facilities spending in the first six months related to expansion of gathering systems at five major facilities in southeast Saskatchewan, and construction of batteries and expansion of gathering systems at facilities in the Cardium. Activity in the Cardium and the other Alberta business units resulted in the majority of land, property, and seismic acquisitions in 2012.

Goodwill

Goodwill decreased by $3.1 million in the second quarter of 2012 due to goodwill being allocated to the non-core assets held for sale at June 30, 2012. Goodwill decreased by $94.1 million in the first six months of 2012 due to the goodwill attributed to the assets held for sale and $91.0 million of goodwill being attributed to the assets disposed of in the Bakken business unit. Goodwill as at June 30, 2012 was $1,371.1 million (December 31, 2011 - $1,465.3 million).

Decommissioning Liabilities

PetroBakken's decommissioning liabilities decreased by $0.8 million in the second quarter of 2012 due to liabilities being transferred to liabilities held for sale, partially offset by accretion expense. PetroBakken's decommissioning liabilities decreased by $8.4 million in the six months ended June 30, 2012, primarily as a result of the asset disposals partially offset by new wells drilled and accretion expense. The discount rate as at June 30, 2012 was 2.5 percent (December 31, 2011 – 2.5 percent). As at June 30, 2012, PetroBakken's decommissioning liabilities were $206.8 million (December 31, 2011 - $215.1 million).

Commitments

The following is a summary of the estimated costs required to fulfill PetroBakken's remaining contractual commitments at June 30, 2012:

Type of Commitment	< 1 Year	1-3 Years	4-5 Years	Thereafter	Total
PetroBakken					
Office operating leases [1]	5,319	12,736	12,919	24,896	55,870
Drilling and completion rigs	17,208	22,444	2,488	-	42,140
Other	1,500	1,360	239	-	3,099
Total Commitments	**$ 24,027**	**$ 36,540**	**$ 15,646**	**$ 24,896**	**$ 101,109**

(1) Minimum lease payments are net of sub-lease payments received by PetroBakken, which reduces rent expense included in general and administrative expenses on the consolidated statement of operations and comprehensive income.

Liquidity and Capital Resources

The table below outlines the composition of PetroBakken's capital structure and liquidity as at June 30, 2012:

	PetroBakken
Working capital deficit [1]	**$ 126,937**
Bank debt – principal	**$ 311,310**
Convertible debentures – principal amount (US$)	**$ 300,000**
Senior unsecured notes – principal amount (US$)	**$ 900,000**
Common share capital [2]	**$ 3,147,284**
Credit facility – borrowing base	**$ 1,400,000**
Available credit capacity	**$ 1,088,690**

(1) Working capital deficit is calculated as PetroBakken's accounts payable and accrued liabilities less PetroBakken's accounts receivable and prepaid expenses.

(2) The common share capital of PetroBakken eliminates upon consolidation of the interim Consolidated Financial Statements.

PetroBakken's strategy is to provide a reasonable dividend payout to shareholders combined with an accretive long-term growth-oriented business plan. PetroBakken is focused on securing appropriate levels of capitalization to support this business strategy. As commodity prices fluctuate, PetroBakken has the ability to alter the capital program and/or dividend payments in order to maintain acceptable debt levels. PetroBakken will continue to monitor plans and forecasts and make adjustments required to maintain acceptable levels of capitalization.

As at June 30, 2012, PetroBakken had $311.3 million of bank debt drawn on its $1.4 billion credit facility. The borrowing limit on the credit facility was increased from $1.35 billion to $1.5 billion on January 31, 2012 through an exercise of the accordion feature, and was subsequently reduced to $1.4 billion in April 2012 to reflect the issuance of senior unsecured notes and disposed reserves during the first quarter of 2012. PetroBakken's credit facility is with a syndicate of banks and has a maturity date of June 2, 2015, which was extended from June 2, 2014 in the second quarter, and generally is not subject to periodic reviews unless a significant asset disposition occurs. The credit facility has an accordion feature providing that at any time during the term, on participation of any existing or additional lenders, PetroBakken can increase the facility by $100 million to $1.5 billion.

On January 30, 2012, PetroBakken closed a private placement of senior unsecured notes ("Notes") with a principal amount of US$900 million. The Notes bear interest at a rate of 8.625 percent per annum and mature February 1, 2020. The Notes contain covenants that could limit PetroBakken's ability to issue additional debt, pay dividends, and repurchase stock, among other restrictions. PetroBakken is in compliance with all of these covenants.

As at June 30, 2012, PetroBakken had convertible debentures outstanding of US$300 million with an annual coupon of 3.125 percent. This is a US$450 million decrease from December 31, 2011 as a portion of the proceeds from the Notes issuance was used to repurchase debentures. The convertible debentures have a financial covenant that limits the amount of security and encumbrances to 35 percent of PetroBakken's total assets. PetroBakken is in compliance with this covenant. The debentures have a one-time, one-day early put option on February 8, 2013 that allows those holders that elect to exercise the option to request payment in full for their debentures. In the event that holders request payment, PetroBakken has the option to repay in cash or through the issuance of PetroBakken shares based on the lower of the then current share price and conversion price.

In the first six months of 2012, PetroBakken received $637.6 million of gross proceeds from dispositions, the majority of which were from two non-core producing assets in southeast Saskatchewan. The proceeds from these transactions were initially used to pay down the revolving credit facility.

Due to the reduction in debt and alteration in structure, PetroBakken increased available liquidity at June 30, 2012 to $1.1 billion from $0.2 billion at December 31, 2011.

In addition to the financial resources noted above, other possible sources of funds available to PetroBakken include the following:

- Funds flow from operations;
- Increases under the existing $1.4 billion credit facility;
- Issuance of common shares of PetroBakken;
- Dividend reduction;
- Issuance of additional subordinated or convertible debt;
- Renegotiating the terms of the existing convertible debentures;
- Adjustments to capital program;
- Sale of producing or non-producing assets. Cash generated from a sale may be reduced by any required debt repayments; and
- Monetization of risk management assets.

PetroBakken expects to satisfy ongoing working capital requirements with funds flow from operations, cash and available credit.

Capital Plan

PetroBakken's capital plan is focused on the development of Cardium light oil properties in central Alberta, development of Bakken and conventional Mississippian light oil properties in southeast Saskatchewan, and leveraging the significant undeveloped land base into new resource opportunities. PetroBakken's capital plan is expected to be financed through funds flow from operations and available financial resources.

Dividends

PetroBakken currently pays a monthly dividend of $0.08 per share or the equivalent of $0.96 per share per annum. The dividend represented 37 percent of PetroBakken's funds flow from operations in the three months ended June 30, 2012 before DRIP participation is considered, with the cash dividend representing 14 percent of second quarter funds flow from operations. The dividend is expected to remain the same for the remainder of 2012 and to be funded from operations and the shareholders participation in the DRIP. In the second quarter, approximately $28.6 million of the $45.2 million of dividends were paid in shares. In the first six months of 2012 approximately $48.4 million of the $90.7 million of dividends were paid in shares.

SUMMARY OF QUARTERLY RESULTS [1]

	2012		2011				2010	
	Q2	**Q1**	Q4	Q3	Q2	Q1	Q4	Q3
Financial ($000s except where noted)								
Oil and natural gas sales from continuing operations	**240,205**	**330,361**	366,881	272,346	274,952	281,297	258,359	228,537
Funds flow from continuing operations [2]	**118,890**	**181,290**	226,273	147,452	148,440	168,384	155,344	139,325
Per share – basic ($)	**1.14**	**1.70**	2.13	1.39	1.40	1.58	1.46	1.31
– diluted ($)	**1.13**	**1.69**	2.10	1.37	1.38	1.57	1.45	1.31
Adjusted net income (loss) from continuing operations [2]	**31,999**	**82,307**	26,712	7,517	30,659	(21)	17,543	30,556
Per share – basic ($)	**0.31**	**0.77**	0.25	0.07	0.29	0.00	0.17	0.29
– diluted ($)	**0.31**	**0.76**	0.25	0.07	0.28	0.00	0.16	0.29
Adjusted net income (loss) attributable to Petrobank shareholders [2] [3]	**31,999**	**82,307**	26,712	7,517	30,659	(21)	1,974,118	83,161
Per share – basic ($)	**0.31**	**0.77**	0.25	0.07	0.29	0.00	18.61	0.78
– diluted ($)	**0.31**	**0.76**	0.25	0.07	0.28	0.00	18.55	0.77
Capital expenditures [2]								
PetroBakken	**109,756**	**206,421**	274,815	271,861	113,010	307,481	262,758	241,309
HBU	**4,525**	**17,878**	28,235	30,772	55,641	54,255	37,521	49,385
Total from continuing operations	**114,281**	**224,299**	303,050	302,633	168,651	361,736	300,279	290,694
PetroBakken Operations								
Oil equivalent sales price ($/boe) [4] [5]	**67.89**	**77.36**	82.69	75.37	85.02	74.46	67.00	60.63
Royalties	**9.44**	**11.92**	12.51	12.20	13.15	11.84	9.84	8.64
Production expenses	**13.37**	**12.61**	10.97	13.13	15.24	10.20	8.97	8.38
Operating netback [2] [5] [6]	**45.08**	**52.83**	59.21	50.04	56.63	52.42	48.19	43.61
Average daily production [5]								
Crude oil and NGL (bbls)	**32,236**	**40,336**	41,660	33,112	29,676	36,140	34,754	33,230
Natural gas (Mcf)	**38,874**	**38,320**	38,083	35,776	33,746	32,534	39,474	41,193
Total (boe) [5] [7]	**38,715**	**46,722**	48,007	39,074	35,300	41,562	41,333	40,095

(1) Petrominerales Ltd. ("Petrominerales") has been presented as discontinued operations in the comparative period as this business unit was distributed to Petrobank shareholders at December 31, 2010.

(2) Non-GAAP measure. See "Non-GAAP Measures" section within this MD&A.

(3) The comparative balances prior to 2011 include the operating results of Petrominerales, a $1.9 billion non-cash gain recorded on the disposal and $23.5 million accumulated other comprehensive loss resulting from the historic translations of Petrominerales U.S. dollar amounts. Petrominerales was distributed to Petrobank shareholders on December 31, 2010.

(4) Net of transportation expenses.

(5) Six Mcf of natural gas is equivalent to one boe.

(6) Excludes hedging activities.

(7) HBU bitumen and heavy oil volumes are excluded from average daily production as HBU operations are considered to be in the exploration and evaluation phase and accordingly are capitalized.

Significant factors influencing quarterly results were:

- PetroBakken's production profile follows a typical pattern of falling in the second quarter as the onset of spring break-up conditions results in higher down-time and reduced capital activity. In addition, the second quarter of 2012 has the full effect of 4,100 boepd of non-core asset dispositions completed since the latter part of 2011. In the second half of the year, PetroBakken's capital activity usually offsets natural declines and production begins to grow with the majority of the growth in the fourth quarter. Similar to 2011, PetroBakken expects strong production increases in the second half of 2012 as 75 percent of the planned drilling program remains to be completed.
- Capital expenditures have varied quarter by quarter due to the timing of development activities. The occurrence of spring break-up in the second quarter results in road bans and lease accessibility issues resulting in reduced capital expenditures during the second quarter over the prior period. Over 85 percent of PetroBakken's capital plan in any given year is usually spent in the remaining three quarters of the year and generates the production profile described above.
- Funds flow from operations is primarily impacted by oil price variability, production levels and production expenses. The oil price PetroBakken receives has been influenced during this period through fluctuations in the typical reference price (WTI) and Canadian pricing differentials to WTI. Compared to 2011, 2012 pricing differentials have been more volatile and generally wider than historic levels, which has reduced funds flow from operations. Price differentials have been negatively impacted by refinery turnarounds, short term pipeline interruptions and the growth of North American supply creating infrastructure bottlenecks. Production levels are most impacted by PetroBakken's capital spending profile, with first half 2012 capital expenditures lower than the previous six months. Production expenses are influenced by production levels due to the high percentage of fixed costs representative of total production expenses and by general cost inflation associated with industry activity throughout this period.
- Adjusted net income fluctuations during the period have been caused by changes in funds flow from operations, unrealized gains and losses on commodity risk management contracts, unrealized foreign exchange gains and losses on converting U.S. dollar denominated debt to Canadian dollars and gains and losses on asset dispositions.

Outstanding Share Data

The number of Petrobank shares outstanding at the date of this MD&A is 99,599,432, a decrease of 1,275,256 shares from June 30, 2012, which relates the repurchase and cancellation of shares (1,312,401), partially offset by the exercise of stock options and incentive shares (37,145).

Risks and Uncertainties

There have been no significant changes in the three or six months ended June 30, 2012 to the risk and uncertainties identified in the MD&A for the year ended December 31, 2011.

Sensitivities

The Company's earnings and cash flow are sensitive to changes in crude oil and natural gas prices, exchange rates and interest rates.

The following factors demonstrate the expected impact on annualized before tax funds flow from operations excluding the effect of hedging for 2012:

Change of:		(millions)
PetroBakken		
Crude oil	US$1.00/bbl WTI reference price (assuming 32,000 bopd)	**$8.9**
	1,000 bopd of production @ US$90.00/bbl WTI	**$24.0**
Natural gas	$1.00/Mcf AECO reference price (assuming 39 MMcf /d)	**$12.1**
	10.0 MMcf per day of production @ $2.00/Mcf AECO	**$5.8**
Currency	US$0.01 in exchange rate	**$8.9**
Interest rate	1% change in interest rate	**$5.1**

Accounting Policies and Estimates

There have been no changes to the Company's critical accounting policies and estimates for the three or six months ended June 30, 2012.

Regulatory Policies

Certification of Disclosures in Interim Filings

In accordance with National Instrument 52-109 of the Canadian Securities Administrators, the Company quarterly issues a Certification of Interim Filings ("Certification"). The Certification requires certifying officers to state that they are responsible for establishing and maintaining disclosure controls and procedures ("DC&P") and internal control over financial reporting ("ICFR").

The Certification requires certifying officers to state that they designed DC&P, or caused it to be designed under their supervision, to provide reasonable assurance that: (i) material information relating to Petrobank is made known to the certifying officers by others; (ii) information required to be disclosed by Petrobank in reports filed with, or submitted to, securities regulatory authorities is recorded, processed, summarized and reported within the time periods specified under Canadian securities legislation. In addition, the Certification requires certifying officers to state that they have designed ICFR, or caused it to be designed under their supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes.

During the three and six months ended June 30, 2012, there has been no change to the Company's ICFR that has materially affected, or is reasonably likely to materially affect, the Company's ICFR. The Company has procedures in place relating to DC&P and ICFR and will continue to monitor such procedures as the Company's business evolves.

Outlook

In addition to the plans discussed in this MD&A, please see the Company's and PetroBakken's recent news releases, corporate presentations and Annual Information Forms.

CONDENSED INTERIM CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME

(Unaudited, thousands of Canadian dollars, except per share amounts)

		Three months ended June 30,		Six months ended June 30,	
		2012	2011	**2012**	2011
	Note				
Revenues					
Oil and natural gas sales		**$ 240,205**	$ 274,952	**$ 570,566**	$ 556,249
Royalties		**(33,265)**	(42,240)	**(83,948)**	(86,538)
Oil and natural gas revenues		**206,940**	232,712	**486,618**	469,711
Gain (loss) on risk management contracts	17	**48,887**	33,732	**29,938**	(4,619)
		255,827	266,444	**516,556**	465,092
Expenses					
Production		**47,086**	48,947	**100,721**	87,084
Transportation		**1,027**	1,820	**2,462**	4,575
General and administrative		**15,395**	13,471	**31,349**	25,402
Share-based compensation		**4,159**	6,236	**9,571**	13,722
(Gain) loss on derivative financial liabilities	9	**(13,781)**	(32,778)	**6,030**	(61,048)
Finance and other	12	**30,784**	24,178	**63,466**	46,766
Loss (gain) on dispositions	7	**6,256**	(15,440)	**(122,699)**	(15,192)
Loss on settlement of convertible debentures	9	**-**	-	**44,009**	-
Impairment	4, 5	**61,000**	5,146	**61,000**	12,810
Foreign exchange loss (gain)		**22,371**	(4,583)	**8,222**	(18,732)
Depletion and depreciation expense	5, 6	**101,729**	83,551	**220,598**	183,759
		276,026	130,548	**424,729**	279,146
(Loss) income before taxes and non-controlling interest ("NCI")		**(20,199)**	135,896	**91,827**	185,946
Income tax expense		**4,388**	29,247	**82,098**	36,646
(Loss) income before NCI		**(24,587)**	106,649	**9,729**	149,300
Net (loss) income attributable to NCI	15	**(9,367)**	48,358	**6,462**	70,424
Net and comprehensive (loss) income attributable to Petrobank shareholders		**$ (15,220)**	$ 58,291	**$ 3,267**	$ 78,876
Earnings per share					
Basic (loss) earnings per share	14	**$ (0.15)**	$ 0.55	**$ 0.03**	$ 0.74
Diluted (loss) earnings per share	14	**$ (0.15)**	$ 0.54	**$ 0.03**	$ 0.72

See accompanying notes to these condensed interim consolidated financial statements.

CONDENSED INTERIM CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

(Unaudited, thousands of Canadian dollars)

As at	Note	June 30, 2012	December 31, 2011
Assets			
Current assets			
Cash and cash equivalents		**$ 103,628**	$ -
Accounts receivable		**126,980**	194,296
Prepaid expenses		**12,142**	10,608
Risk management assets	17	**14,283**	3,677
Assets held for sale	3	**10,205**	315,908
		267,238	524,489
Risk management assets	17	**13,781**	4,317
Exploration assets	4	**923,767**	1,009,906
Property, plant and equipment	5	**3,707,523**	3,907,550
Other intangible assets	6	**6,660**	6,167
Goodwill	7	**1,371,145**	1,465,287
Total assets		**$ 6,290,114**	$ 6,917,716
Liabilities and shareholders' equity			
Current liabilities			
Accounts payable and accrued liabilities		**$ 274,047**	$ 410,650
Current portion of finance lease obligations		**588**	588
Risk management liabilities	17	**37**	6,414
Convertible debentures	9	**261,336**	-
Derivative financial liability	9	**10,987**	-
Liabilities held for sale	3	**1,305**	11,874
		548,300	429,526
Bank debt	8	**306,013**	1,262,003
Senior unsecured notes	10	**892,411**	-
Convertible debentures	9	**-**	639,014
Derivative financial liability	9	**-**	33,038
Finance lease obligations		**1,151**	1,401
Other long-term liabilities		**10,913**	11,938
Decommissioning liabilities	11	**210,748**	218,921
Risk management liabilities	17	**50**	2,610
Deferred tax liabilities		**642,510**	561,408
Total liabilities		**2,612,096**	3,159,859
Shareholders' equity			
Common shares	13	**1,490,870**	1,577,351
Contributed surplus		**61,985**	50,449
Paid-in capital		**841,126**	860,200
Deficit		**(172,680)**	(174,422)
Total Petrobank shareholders' equity		**2,221,301**	2,313,578
Non-controlling interest	15	**1,456,717**	1,444,279
Total equity		**3,678,018**	3,757,857
Total liabilities and equity		**$ 6,290,114**	$ 6,917,716

Commitments (Note 19)

Subsequent events (Notes 13, 16 and 17)

See accompanying notes to these condensed interim consolidated financial statements.

CONDENSED INTERIM CONSOLIDATED STATEMENTS OF CHANGE IN EQUITY

(Unaudited, thousands of Canadian dollars)

	Note	Common Shares	Contributed Surplus	Paid-in Capital	Deficit	Total
January 1, 2011		$ 1,575,448	$ 42,741	$ 840,772	$ (166,793)	$2,292,168
Total net and comprehensive income attributable to Petrobank shareholders		-	-	-	78,876	78,876
Issued under employee incentive plans		183	-	-	-	183
Share-based settlements		792	(792)	-	-	-
Share-based compensation		-	4,574	-	-	4,574
Change in paid-in capital		-	-	17,368	-	17,368
June 30, 2011		**$ 1,576,423**	**$ 46,523**	**$ 858,140**	**$ (87,917)**	**$2,393,169**
January 1, 2012		$ 1,577,351	$ 50,449	$ 860,200	$ (174,422)	$ 2,313,578
Total net and comprehensive income attributable to Petrobank shareholders		-	-	-	3,267	3,267
Share repurchases	13	(93,874)	17,446	-	(1,525)	(77,953)
Issued upon asset acquisition	13	739	-	-	-	739
Issued under employee incentive plans	13	1,211	-	-	-	1,211
Share-based settlements	13	5,443	(5,443)	-	-	-
Share-based compensation		-	(467)	-	-	(467)
Change in paid-in capital		-	-	(19,074)	-	(19,074)
June 30, 2012		**$ 1,490,870**	**$ 61,985**	**$ 841,126**	**$ (172,680)**	**$ 2,221,301**

See accompanying notes to these condensed interim consolidated financial statements.

CONDENSED INTERIM CONSOLIDATED STATEMENTS OF CASH FLOW

(Unaudited, thousands of Canadian dollars)

		Three months ended June 30,		Six months ended June 30,	
		2012	2011	**2012**	2011
Operating Activities	Note				
Net (loss) income attributable to Petrobank shareholders		**$ (15,220)**	$ 58,291	**$ 3,267**	$ 78,876
Net (loss) income attributable to NCI	15	**(9,367)**	48,358	**6,462**	70,424
Unrealized (gain) loss on risk management contracts	17	**(46,721)**	(37,087)	**(29,007)**	675
Share-based compensation		**4,159**	6,236	**9,571**	13,722
(Gain) loss on derivative financial liabilities	9	**(13,781)**	(32,778)	**6,030**	(61,048)
Non-cash finance and other	12	**5,005**	8,539	**12,032**	17,272
Loss (gain) on dispositions	7	**6,256**	(15,440)	**(122,699)**	(15,192)
Loss on settlement of convertible debentures	9	**-**	-	**44,009**	-
Impairment	4, 5	**61,000**	5,146	**61,000**	12,810
Unrealized foreign exchange loss (gain)		**22,609**	(4,592)	**10,060**	(18,448)
Depletion and depreciation expense	5, 6	**101,729**	83,551	**220,598**	183,759
Income tax expense		**4,388**	29,247	**82,098**	36,646
Decommissioning liabilities settled	11	**(1,167)**	(1,031)	**(3,241)**	(2,672)
		118,890	148,440	**300,180**	316,824
Changes in non-cash working capital	18	**28,217**	36,533	**58,716**	(1,190)
Net cash provided by operating activities		**147,107**	184,973	**358,896**	315,634
Investing Activities					
Expenditures on property, plant and equipment		**(104,024)**	(86,630)	**(306,447)**	(391,603)
Exploration and evaluation expenditures		**(10,111)**	(81,714)	**(31,754)**	(138,239)
Other intangible asset expenditures		**(146)**	(307)	**(379)**	(545)
Proceeds from dispositions – net of costs		**11,313**	21,305	**847,803**	22,589
Cash dividends received by Petrobank	15	**45**	26,352	**8,841**	52,704
Capital lease obligations		**(137)**	(202)	**(250)**	(399)
Current tax on dispositions		**-**	-	**(996)**	-
Changes in non-cash working capital	18	**(100,149)**	(234,307)	**(122,021)**	(140,670)
Net cash (used in) provided by investing activities		**(203,209)**	(355,503)	**394,797**	(596,163)
Financing Activities					
Issuance (repayment) of bank debt		**93,780**	218,605	**(956,354)**	358,505
Financing costs relating to bank debt		**(1,414)**	(3,062)	**(1,794)**	(4,904)
(Repurchase) issuance of Petrobank common shares	13	**(57,351)**	135	**(76,742)**	183
Sale of PetroBakken common shares by Petrobank	15	**55,495**	-	**55,495**	-
Repurchase of PetroBakken convertible debentures – net costs	9	**-**	-	**(452,340)**	-
Issuance of PetroBakken senior unsecured notes – net of costs	10	**-**	-	**877,583**	-
Equity (issued) repurchased by PetroBakken	15	**(30,844)**	1	**(45,195)**	4
Cash dividends paid by PetroBakken	15	**(16,554)**	(44,947)	**(42,277)**	(89,812)
Amortization of obligations under gas sale contract		**(205)**	(206)	**(411)**	(410)
Changes in non-cash working capital	18	**17**	4	**(8,030)**	(505)
Net cash provided by (used in) financing activities		**42,924**	170,530	**(650,065)**	263,061
Net change in cash and cash equivalents		**(13,178)**	-	**103,628**	(17,468)
Cash and cash equivalents, beginning of period		**116,806**	-	**-**	17,468
Cash and cash equivalents, end of period		**$ 103,628**	$ -	**$ 103,628**	$ -
Cash and cash equivalents consist of:					
Cash		**$ 9,558**	$ -	**$ 9,558**	$ -
Cash equivalents		**$ 94,070**	$ -	**$ 94,070**	$ -
Other cash flow information:					
Cash interest paid		**$ 26,103**	$ 16,027	**$ 52,755**	$ 29,679
Cash interest received		**$ 280**	$ 6	**$ 368**	$ 102

See accompanying notes to these condensed interim consolidated financial statements.

Note 1 – Corporate Information and Basis of Presentation

Corporate Information

Petrobank Energy and Resources Ltd. ("Petrobank", "we", "our" or the "Company") is a Canadian corporation with shares listed on the Toronto Stock Exchange ("TSX"). The records office and principal address is located at 3000, 525 – 8th Avenue S.W., Calgary, Alberta, T2P 1G1.

The Company is principally engaged in the exploration and development of oil and natural gas in western Canada. The condensed interim consolidated financial statements of the Company as at June 30, 2012 and for the three and six months ended June 30, 2012 and 2011 comprise the financial statements of the Company and our subsidiaries.

Basis of Presentation

The condensed interim consolidated financial statements for Petrobank as at June 30, 2012 and for the three and six months ended June 30, 2012 and 2011 should be read in conjunction with the audited consolidated financial statements as at and for the year ended December 31, 2011. The condensed interim consolidated financial statements are prepared using the same accounting policies and methods of computation as disclosed in the annual consolidated financial statements.

The condensed interim consolidated financials are presented in Canadian dollars and all amounts are rounded to the nearest thousand dollars ($000s), except where otherwise indicated. The condensed interim consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") applicable to the preparation of interim financial statements, including IAS 34, *Interim Financial Reporting*.

The condensed interim consolidated financial statements were approved by the Company's Board of Directors on August 13, 2012.

Note 2 – Segmented Information

For the periods ended June 30, 2012, the Company comprised of two operating segments: the Heavy Oil Business Unit ("HBU") and PetroBakken Energy Ltd. ("PetroBakken"). Where segmented information is provided throughout these condensed interim consolidated financial statements, the HBU is combined with activities performed at the Petrobank corporate level and is referred to as "Petrobank Standalone".

The HBU operates our heavy oil projects using Petrobank's patented THAI® heavy oil recovery process in the field. THAI® (Toe to Heel Air Injection), is an evolutionary in-situ combustion technology for the recovery of bitumen and heavy oil. The HBU projects are in the exploration and evaluation phase and accordingly all expenses, net of revenues, are capitalized.

PetroBakken (TSX: PBN), 58% owned by Petrobank as June 30, 2012 (December 31, 2011 and June 30, 2011 - 59%) is focused on conventional oil and gas operations throughout western Canada with a primary focus on light oil developments from the Bakken formation in southeast Saskatchewan and in the Cardium play in Alberta.

Results by operating segment for the three and six months ended June 30, 2012 and 2011 were as follows:

Three months ended June 30,	2012			2011		
	PetroBakken	**Petrobank Standalone**	**Total**	PetroBakken	Petrobank Standalone	Total
Revenues						
Oil and natural gas sales	**$ 240,205**	$ -	**$ 240,205**	$ 274,952	$ -	$ 274,952
Royalties	**(33,265)**	-	**(33,265)**	(42,240)	-	(42,240)
Oil and natural gas revenues	**206,940**	-	**206,940**	232,712	-	232,712
Gain on risk management contracts	**48,887**	-	**48,887**	33,732	-	33,732
	255,827	-	**255,827**	266,444	-	266,444
Expenses						
Production	**47,086**	-	**47,086**	48,947	-	48,947
Transportation	**1,027**	-	**1,027**	1,820	-	1,820
General and administrative	**12,525**	**2,870**	**15,395**	9,594	3,877	13,471
Share-based compensation	**3,832**	**327**	**4,159**	3,704	2,532	6,236
Gain on derivative financial liability	**(13,781)**	-	**(13,781)**	(32,778)	-	(32,778)
Finance and other	**31,057**	**(273)**	**30,784**	23,497	681	24,178
Loss (gain) on dispositions	**6,256**	-	**6,256**	(15,440)	-	(15,440)
Impairment	**61,000**	-	**61,000**	-	5,146	5,146
Foreign exchange loss (gain)	**22,443**	**(72)**	**22,371**	(4,584)	1	(4,583)
Depletion and depreciation expense	**101,504**	**225**	**101,729**	83,348	203	83,551
	272,949	**3,077**	**276,026**	118,108	12,440	130,548
(Loss) income before taxes and NCI	**(17,122)**	**(3,077)**	**(20,199)**	148,336	(12,440)	135,896
Income tax expense (recovery)	**4,388**	-	**4,388**	31,396	(2,149)	29,247
(Loss) income before NCI	**(21,510)**	**(3,077)**	**(24,587)**	116,940	(10,291)	106,649
Net (loss) income attributable to NCI	**(9,367)**	-	**(9,367)**	48,358	-	48,358
Net (loss) income attributable to Petrobank shareholders	**$ (12,143)**	**$ (3,077)**	**$ (15,220)**	$ 68,582	$ (10,291)	$ 58,291
Identifiable assets	**$ 5,952,929**	**$ 337,185**	**$ 6,290,114**	$ 6,093,444	$ 477,675	$ 6,571,119
Total liabilities	**$ 2,595,817**	**$ 16,279**	**$ 2,612,096**	$ 2,635,259	$ 85,309	$ 2,720,568
Capital expenditures	**$ 109,756**	**$ 4,525**	**$ 114,281**	$ 113,010	$ 55,641	$ 168,651
Dividends paid (received)	**$ 45,164**	**$ (26,300)**	**$ 18,864**	$ 44,947	$ (26,352)	$ 18,595

Six months ended June 30,	2012			2011		
	PetroBakken	**Petrobank Standalone**	**Total**	PetroBakken	Petrobank Standalone	Total
Revenues						
Oil and natural gas sales	**$ 570,566**	$ -	**$ 570,566**	$ 556,249	$ -	$ 556,249
Royalties	**(83,948)**	-	**(83,948)**	(86,538)	-	(86,538)
Oil and natural gas revenues	**486,618**	-	**486,618**	469,711	-	469,711
Gain (loss) on risk management contracts	**29,938**	-	**29,938**	(4,619)	-	(4,619)
	516,556	-	**516,556**	465,092	-	465,092
Expenses						
Production	**100,721**	-	**100,721**	87,084	-	87,084
Transportation	**2,462**	-	**2,462**	4,575	-	4,575
General and administrative	**24,502**	**6,847**	**31,349**	18,404	6,998	25,402
Share-based compensation	**10,038**	**(467)**	**9,571**	9,148	4,574	13,722
Loss (gain) on derivative financial liability	**6,030**	-	**6,030**	(61,048)	-	(61,048)
Finance and other	**62,643**	**823**	**63,466**	45,491	1,275	46,766
Gain on dispositions	**(122,699)**	-	**(122,699)**	(15,192)	-	(15,192)
Loss on settlement of convertible debentures	**44,009**	-	**44,009**	-	-	-
Impairment	**61,000**	-	**61,000**	-	12,810	12,810
Foreign exchange loss (gain)	**8,324**	**(102)**	**8,222**	(18,759)	27	(18,732)
Depletion and depreciation expense	**220,149**	**449**	**220,598**	183,368	391	183,759
	417,179	**7,550**	**424,729**	253,071	26,075	279,146
Income (loss) before taxes and NCI	**99,377**	**(7,550)**	**91,827**	212,021	(26,075)	185,946
Income tax expense (recovery)	**82,098**	-	**82,098**	41,706	(5,060)	36,646
Income (loss) before NCI	**17,279**	**(7,550)**	**9,729**	170,315	(21,015)	149,300
Net income attributable to NCI	**6,462**	-	**6,462**	70,424	-	70,424
Net income (loss) attributable to Petrobank shareholders	**$ 10,817**	**$ (7,550)**	**$ 3,267**	$ 99,891	$ (21,015)	$ 78,876
Capital expenditures	**$ 316,177**	**$ 22,403**	**$ 338,580**	$ 420,491	$ 109,896	$ 530,387
Dividends paid (received)	**$ 90,720**	**$ (52,724)**	**$ 37,996**	$ 89,812	$ (52,704)	$ 37,108

Any transactions between reportable segments are eliminated on consolidation of these condensed interim consolidated financial statements. With the exception of dividends received by Petrobank Standalone from PetroBakken, there are no significant transactions between the entities representing the reportable segments.

Note 3 – Assets and Liabilities Held for Sale

For the six months ended,	June 30, 2012
Assets held for sale, beginning of period	$ 315,908
Transfers from exploration assets	2,808
Transfers from property, plant, and equipment	33,655
Transfers from goodwill	3,144
Dispositions	(332,613)
Loss on assets held for sale	(12,697)
Assets held for sale, end of period	$ 10,205

For the six months ended,	June 30, 2012
Liabilities held for sale, beginning of period	$ 11,874
Transfers from decommissioning liability	3,310
Dispositions	(13,879)
Liabilities held for sale, end of period	$ 1,305

In the second quarter, PetroBakken committed to selling non-core assets located in Manitoba for gross proceeds of $8.9 million resulting in the assets being classified as held for sale. The carrying value of the assets exceeded the fair value less costs to sell resulting in a loss of $2.7 million in the three months ended June 30, 2012 (2011 - $nil).

Note 4 – Exploration Assets

Exploration assets comprise the Company's projects in the exploration and evaluation stage which are pending determination of technical and commercial feasibility. The following is a continuity schedule of the Company's exploration assets for the six month period ended June 30, 2012.

For the six months ended,	June 30, 2012
Exploration assets, beginning of period	$ 1,009,906
Additions	31,894
Dispositions	(26,152)
Transfers to assets held for sale	(2,808)
Transfers to property, plant, and equipment	(57,986)
Impairment	(31,087)
Exploration assets, end of period	$ 923,767

During the three and six months ended June 30, 2012, PetroBakken recognized an impairment of $31.1 million (2011 - $nil) related to undeveloped land in the gas weighted northeast BC cash generating unit ("CGU") as a result of land expiries, a decline in the fair value of the land and PetroBakken's intention not to actively develop these assets at this time. The impairment was calculated based on the difference between the net book value and the fair value less cost to sell based on acquisition metrics of recent transactions.

Note 5 – Property, Plant and Equipment

	Oil and natural gas assets [1]	Other	Total
Cost			
As at January 1, 2012	$ 5,287,202	$ 42,643	$ 5,329,845
Additions	310,333	789	311,122
Dispositions	(285,174)	-	(285,174)
Transfers to assets held for sale	(33,655)	-	(33,655)
Transfers from exploration assets	57,986	-	57,986
As at June 30, 2012	$ 5,336,692	$ 43,432	$ 5,380,124
Depletion, Depreciation and Impairment			
As at January 1, 2012	$ 1,403,903	$ 18,392	$ 1,422,295
Depletion and depreciation	216,625	3,768	220,393
Impairment	29,913	-	29,913
As at June 30, 2012	$ 1,650,441	$ 22,160	$ 1,672,601
Carrying amount as at June 30, 2012	**$ 3,686,251**	**$ 21,272**	**$ 3,707,523**

[1] Oil and natural gas assets relate entirely to PetroBakken at June 30, 2012.

Other fixed assets are mainly comprised of office furniture and fixtures and computer equipment.

During the three and six months ended June 30, 2012, PetroBakken recognized an impairment of $29.9 million (2011 - $nil) related to the gas weighted northeast BC CGU as a result of a decline in the value of the assets and PetroBakken's intention not to actively develop these assets at this time. The impairment was calculated based on the difference between the net book value and the value in use. The value in use of the property, plant and equipment was determined using the proved plus probable reserves discounted at 10 percent.

The key assumptions used in determining the value in use were the discount rate, commodity prices, volumes, and inventory of undrilled locations. The values assigned to the key assumptions represent PetroBakken's assessment of the future trends in the oil and natural gas industry and are based on both internal and external sources. A discount rate of 10 percent was used in the assessment of impairment for all CGUs. If the discount rate were to change by 10 percent, PetroBakken would have additional impairment of $1.3 million in the BC CGU for the three and six months ended June 30, 2012.

Note 6 – Other Intangible Assets

For the six months ended,	June 30, 2012
Other intangible assets, beginning of period	**$ 6,167**
Additions from internal development	**379**
Acquisition	**319**
Depreciation charge	**(205)**
Other intangible assets, end of period	**$ 6,660**

Other intangible assets comprise of certain patents, licenses, trademarks, agreements and other capital costs incurred to develop the Company's THAI® and related technologies. These assets have an estimated useful life of 15 years and began depreciating using the straight line method on January 1, 2011, when THAI® reserves were first assigned to the Company by our independent reserve engineers.

Note 7 – Asset Divestitures

HBU

On February 28, 2012, the Company closed the disposition of our May River property, which includes the May River and Conklin cash generating units, for cash proceeds of approximately $225.0 million, net of closing adjustments. There was no gain or loss recorded on disposition.

PetroBakken

During the three months ended June 30, 2012, PetroBakken closed non-core divestures for net proceeds of $11.3 million (2011 - $21.3 million) resulting in a loss on disposition of $6.3 million (2011 - $15.4 million gain).

During the six months ended June 30, 2012, PetroBakken closed non-core asset divestitures for net proceeds of $627.8 million (2011 - $22.6 million) resulting in a net gain of $122.7 million (2011 - $15.2 million gain), including the loss on assets held for sale. Included within the non-core divestitures was the sale of non-core land in Montana for $7.8 million which resulted in current income tax of $1.0 million.

The dispositions completed during the six months ended June 30, 2012, had the following impact on goodwill:

For the six months ended,	**June 30, 2012**
Goodwill, beginning of period	**$ 1,465,287**
Dispositions	**(90,998)**
Transfers to assets held for sale	**(3,144)**
Goodwill, end of period	**$ 1,371,145**

Note 8 – Bank Debt

Petrobank Standalone

On January 4, 2011, the Petrobank Standalone operating segment closed a $200 million secured credit facility with a syndicate of lenders. We cancelled the credit facility concurrent with the closing of the sale of our May River property on February 28, 2012 due to the cash available to the operating segment and to save on stand-by fees.

PetroBakken

PetroBakken's bank debt consists of borrowings against their covenant based credit facility. The facility is an extendible revolving facility in the amount of $1.4 billion from a syndicate of lenders and the maturity date was extended by one year to June 2, 2015 during the three months ended June 30, 2012. The maturity date may, at the request of PetroBakken and with consent of the lenders, be extended on an annual basis.

The credit facility lending limit was reduced to $1.4 billion from $1.5 billion in the three months ended June 30, 2012 to reflect the issuance of senior unsecured notes and disposed reserves on the non-core asset divestitures during the first quarter of 2012. The credit facility has an accordion feature providing that at any time during the term, on participation of any existing or additional lenders, PetroBakken can increase the facility by $100 million to $1.5 billion.

As at June 30, 2012	**Petrobank Standalone**	**PetroBakken**	**Petrobank Consolidated**
Bank debt outstanding	$ -	$ 311,310	$ 311,310
Deferred financing costs [1]	-	(5,297)	(5,297)
Bank debt	**$ -**	**$ 306,013**	**$ 306,013**

[1] Deferred financing costs are amortized straight line over the term of the credit facility.

Note 9 – Convertible Debentures

PetroBakken

On January 31, 2012, PetroBakken completed the repurchase of US$450 million of the US$750 million of convertible debentures at a price of US$99,000 per US$100,000 of principal amount. This resulted in a loss of $44.0 million, which consists of acceleration on the accretion of the convertible debentures of $72.1 million, partially offset by a gain of $28.1 million on the retirement of a portion of the derivative liability.

The remaining US$300 million of convertible debentures mature in February 2016. Individual holders have a one-time put option right of prepayment of the debentures for 100 percent of the par value plus accrued interest on February 8, 2013. A holder has a 10 day period between December 10, 2012 and December 20, 2012 to exercise their put option. PetroBakken can elect to make the repayment to any holder at either the put or maturity date in cash or common shares. If settlement in common shares is elected by PetroBakken, the share price used is based on the 20 day weighted average trading price ending five days prior to payment or the conversion price. Upon conversion, based on the adjusted conversion price of US$34.37, a minimum of 8,727,527 common shares may be issued. As the debentures can be redeemed in less than one year at the option of the holder, they have been classified as current as at June 30, 2012.

The following table summarizes the liability component of the Company's debentures at June 30, 2012:

For the six months ended,	June 30, 2012
Liability component, beginning of period	$ 639,014
Repurchase of convertible debentures – net of costs	(380,250)
Accretion	6,435
Changes in exchange rate	(3,863)
Liability component, end of period	**$ 261,336**

The following assumptions were used in determining the fair value of the derivative financial liability:

As at	June 30, 2012
Risk free interest rate	1.17%
Annual dividend per share [1]	-
Expected life (years)	3.6
Expected volatility [2]	49%
US/CDN $ FX rate	1.02
Market share price	CDN$12.29
Conversion share price	US$34.37

(1) Dividend per share is nil because the share conversion price is adjusted to reflect dividends paid.
(2) Expected volatility includes a premium for the difference between US$/CDN$ exchange rates.

The following table summarizes the derivative financial liability:

For the six months ended,	June 30, 2012
Derivative financial liability, beginning of period	$ 33,038
Repurchase of convertible debentures	(28,081)
Loss	6,030
Derivative financial liability, end of period	**$ 10,987**

Note 10 – Senior Unsecured Notes

On January 30, 2012, PetroBakken closed a private placement of senior unsecured notes (the "Notes") with a principal amount of US$900 million at 99.5 percent of face value. The Notes bear interest at a rate of 8.625 percent per annum and mature on February 1, 2020. PetroBakken has the option to redeem the Notes beginning on February 1, 2016 at the following redemption prices (expressed as a percentage of the principal amount of the debenture): 2016 - 104.313 percent; 2017 - 102.156 percent; 2018 and thereafter - 100 percent. The Notes are subordinate to PetroBakken's credit facility. The Notes have been classified as a liability and will be carried at amortized cost, net of $20.8 million in transaction costs and a $4.5 million initial discount on principal proceeds. The transaction costs and initial discount are accreted up to the principal balance at maturity using the effective interest method. The accretion and interest paid are expensed as finance and other expense in the condensed interim consolidated statement of operations and comprehensive income.

The U.S. dollar denominated Notes are translated for accounting purposes based on the Canadian dollar exchange rate on the date of issuance and at the end of the applicable reporting period.

The following table summarizes the Notes:

For the six months ended,	June 30, 2012
Notes, beginning of period	$ -
Proceeds, net of face value discount	898,366
Transaction costs	(20,783)
Accretion	905
Changes in foreign exchange rate	13,923
Notes, end of period	**$ 892,411**

Note 11 – Decommissioning Liabilities

The total future decommissioning liabilities were estimated by management based on the Company's net ownership interest in all wells, gathering lines and facilities, estimated costs to reclaim and abandon the wells, gathering lines and facilities and the estimated timing of the costs to be incurred in future periods.

Changes to decommissioning liabilities were as follows:

For the six months ended,	June 30, 2012
Decommissioning liabilities, beginning of year	$ 218,921
Obligations incurred	4,496
Obligations disposed	(8,852)
Obligations settled	(3,241)
Accretion expense	2,734
Transfers to liabilities held for sale	(3,310)
Decommissioning liabilities, end of period	$ 210,748

The decommissioning liabilities have been calculated using an inflation rate of two percent per annum and discounted using a risk free rate of two and a half percent per annum (December 31, 2011 – inflation rate of two percent and risk free rate of two and a half percent). Most of these obligations are not expected to be paid for several years, extending up to 28 years in the future for the HBU and 45 years in the future for PetroBakken, and are expected to be funded from general resources of the Company at their respective settlement dates. The total undiscounted amount of estimated cash flows required to settle the obligations at June 30, 2012 is $4.4 million (December 31, 2011 - $4.4 million) for the obligations in our HBU, and $217.7 million (December 31, 2011 - $235.2 million) for the obligations in PetroBakken.

Note 12 – Finance and Other

The finance and other balance includes the following:

Three months ended June 30,	2012			2011		
	Petrobank Standalone	**PetroBakken**	**Total**	Petrobank Standalone	PetroBakken	Total
Interest expense on credit facilities and other	**$ 3**	**$ 4,226**	**$ 4,229**	$ 626	$ 9,650	$ 10,276
Interest income and other	**(300)**	**-**	**(300)**	(6)	-	(6)
Interest expense on convertible debentures	**-**	**2,354**	**2,354**	-	5,655	5,655
Accretion of convertible debentures	**-**	**2,604**	**2,604**	-	5,785	5,785
Interest expense on senior unsecured notes	**-**	**19,496**	**19,496**	-	-	-
Accretion of senior unsecured notes	**-**	**553**	**553**	-	-	-
Borrowing costs capitalized [(1)]	**-**	**-**	**-**	(286)	-	(286)
Amortization of deferred financing costs	**-**	**477**	**477**	234	1,061	1,295
Accretion of decommissioning liabilities	**24**	**1,347**	**1,371**	113	1,346	1,459
Finance and other expenses	**$ (273)**	**$ 31,057**	**$ 30,784**	$ 681	$ 23,497	$ 24,178

Six months ended June 30,	2012			2011		
	Petrobank Standalone	**PetroBakken**	**Total**	Petrobank Standalone	PetroBakken	Total
Interest expense on credit facilities and other	**$ 794**	**$ 13,498**	**$ 14,292**	$ 988	$ 17,510	$ 18,498
Interest income and other	**(396)**	**-**	**(396)**	(102)	-	(102)
Interest expense on convertible debentures	**-**	**5,984**	**5,984**	-	11,384	11,384
Accretion of convertible debentures	**-**	**6,435**	**6,435**	-	11,505	11,505
Interest expense on senior unsecured notes	**-**	**32,160**	**32,160**	-	-	-
Accretion of senior unsecured notes	**-**	**905**	**905**	-	-	-
Borrowing costs capitalized [(1)]	**(606)**	**-**	**(606)**	(286)	-	(286)
Amortization of deferred financing costs	**985**	**973**	**1,958**	459	2,402	2,861
Accretion of decommissioning liabilities	**46**	**2,688**	**2,734**	216	2,690	2,906
Finance and other expenses	**$ 823**	**$ 62,643**	**$ 63,466**	$ 1,275	$ 45,491	$ 46,766

(1) The HBU credit facility was a general borrowing and related borrowing costs were capitalized in accordance with IAS 23, *Borrowing Costs*.

Note 13 – Share Capital

The equity account balances include only those of the Petrobank parent entity. PetroBakken's equity account balances eliminate upon consolidation of these financial statements.

Authorized

The authorized share capital of Petrobank consists of an unlimited number of common shares without nominal or par value, and an unlimited number of preferred shares, issuable in series, without nominal or par value.

Normal Course Issuer Bid ("NCIB")

Petrobank was authorized to purchase up to 7,273,401 common shares, representing approximately 10 percent of the public float of the Company's shares. On any trading day, Petrobank could not purchase more than 132,632 common shares. Petrobank was authorized to make purchases during the period from September 14, 2011 to September 13, 2012, or until such earlier time as the NCIB is completed or terminated at the option of Petrobank. All shares acquired under the NCIB were cancelled.

During the six months ended June 30, 2012, the Company repurchased 6,357,000 shares (2011 - nil) under the NCIB for a total cost of $78.0 million. The shares had an average price of $12.26 per share. Of the amount paid, $93.9 million was charged against share capital, $17.4 million was credited to contributed surplus, and $1.5 million was charged against retained earnings. 5,961,000 of the repurchased shares were cancelled prior to June 30, 2012; the remaining 396,000 shares were cancelled in early July 2012. The NCIB was completed as of July 16, 2012.

Common Shares

Changes in Common Shares	Number	Amount
Balance at December 31, 2011	106,400,220	$ 1,577,351
Repurchase of common shares under NCIB	-	(93,874)
Cancellation of common shares under NCIB	(5,961,000)	-
Exercise of stock options, incentive shares and DCS	385,468	1,211
Issued upon asset acquisition	50,000	739
Share-based settlements	-	5,443
Balance at June 30, 2012	**100,874,688**	**$ 1,490,870**

Stock Options

The following is a continuity of stock options outstanding:

	Stock Options	Weighted-Average Exercise Price
Balance at December 31, 2011	3,989,827	$ 16.55
Granted	522,115	13.96
Exercised	(326,900)	3.70
Forfeited	(870,802)	18.35
Expired	(62,402)	24.55
Balance at June 30, 2012	**3,251,838**	**$ 16.79**

Deferred Common Shares

The following is a continuity of deferred common shares ("DCS") outstanding:

	DCS
Balance at December 31, 2011	397,871
Granted	12,864
Exercised	(50,463)
Balance at June 30, 2012	**360,272**

Directors Deferred Common Shares

The following is a continuity of directors DCS deferred common shares outstanding:

	Directors DCS
Balance at December 31, 2011	43,131
Granted	20,400
Forfeited	(2,192)
Balance at June 30, 2012	**61,339**

Incentive Shares

The following is a continuity of incentive shares outstanding:

	Incentive Shares
Balance at December 31, 2011	374,999
Granted	83,490
Exercised	(8,105)
Forfeited	(131,383)
Balance at June 30, 2012	**319,001**

Note 14 – Earnings Per Share

Basic earnings per share is calculated by dividing net income attributable to Petrobank shareholders by the weighted average number of common shares outstanding during the period. Diluted earnings per share reflects the potential dilution of stock options, deferred common shares, directors deferred common shares and incentive shares (collectively, "Share-Based Awards").

The following tables provide a reconciliation of the numerators and the denominators of the basic and diluted per share computations for income or loss attributable to Petrobank shareholders.

	Three months ended June 30,		Six months ended June 30,	
	2012	2011	**2012**	2011
Net income attributable to Petrobank shareholders adjustments				
Basic (loss) earnings	**$ (15,220)**	$ 58,291	**$ 3,267**	$ 78,876
Impact of PetroBakken dilution on net income	**151**	(427)	**(137)**	(680)
Diluted (loss) earnings	**$ (15,069)**	$ 57,864	**$ 3,130**	$ 78,196
Weighted average common share adjustments				
Weighted average common shares outstanding, basic	**104,028,034**	106,273,964	**105,219,193**	106,260,999
Effect of Share-Based Awards	**1,060,519**	1,154,860	**1,042,662**	1,972,875
Weighted average common shares outstanding, diluted	**105,088,553**	107,428,824	**106,261,855**	108,233,874

In determination of the weighted average number of diluted common shares outstanding for the three and six months ended June 30, 2012, 2,671,276 and 2,144,300 stock options are excluded, respectively, because the effect would be anti-dilutive (2011 - 1,835,591 and 1,702,956).

Note 15 – Non-Controlling Interest

The components of the Company's non-controlling interest in PetroBakken are as follows:

Balance at December 31, 2011	$	1,444,279
Attributable income		6,462
Share-based compensation		10,038
Common shares repurchased		(45,195)
Changes in ownership interest [(1)]		19,074
Cash dividends paid or declared by PetroBakken		(42,277)
Cash dividends received by Petrobank		8,841
Sale of PetroBakken common shares by Petrobank		55,495
Balance at June 30, 2012	**$**	**1,456,717**

(1) Reflects the book values of the NCI share related to PetroBakken shares issued in connection with the dividend reinvestment plan and PetroBakken stock options, deferred common shares, and incentive shares exercised in the period.

Note 16 – Capital Management

The Company's policy is to maintain a strong capital base in order to provide flexibility in the future development of the business and maintain investor, creditor and market confidence. Petrobank Standalone and PetroBakken manage their capital structure independently, generate their own cash flows, and have the ability to fund their operations through the issuance of secured and unsecured debt as well as equity financing. Petrobank Standalone may also dispose of all or a portion of our ownership in PetroBakken to fund operations. The table below outlines the composition of Petrobank's consolidated capital structure:

	Petrobank Standalone	PetroBakken	**Petrobank Consolidated**
Working capital surplus (deficit) [1]	$ 95,052	$ (126,937)	**$ (31,885)**
Bank debt – principal	$ -	$ 311,310	**$ 311,310**
Convertible debentures – principal amount (US$)	$ -	$ 300,000	**$ 300,000**
Senior unsecured notes – principal amount (US$)	$ -	$ 900,000	**$ 900,000**
Common share capital [2]	$ 1,490,870	$ 3,147,284	**$ 1,490,870**
Credit facility	$ -	$ 1,400,000	
Available credit capacity	$ -	$ 1,088,690	

(1) Working capital surplus (deficit) is calculated as cash and cash equivalents, accounts receivable and prepaid expenses less accounts payable and accrued liabilities and the current portion of finance lease obligations.

(2) The common share capital of PetroBakken eliminates upon consolidation of these financial statements.

Petrobank Standalone

We manage our capital structure and make adjustments to it in light of changes in economic conditions and the risk characteristics of the underlying assets. We consider our capital structure to include common share capital and working capital. In order to maintain or adjust the capital structure, from time to time we may issue common shares or other securities, sell a portion of our ownership in PetroBakken or other corporate assets or adjust our capital spending to manage current and projected cash levels.

Petrobank received cash proceeds of approximately $225.0 million, net of closing adjustments, on February 28, 2012 from the sale of our May River property. Proceeds from this transaction were used to repay outstanding bank debt and result in Petrobank having a significant positive cash and working capital balance. We cancelled our credit facility concurrent with the closing of the sale due to our cash availability and to save on standby fees.

Based on Petrobank's current ownership and PetroBakken's current annual dividend of $0.96 per PetroBakken share, Petrobank expects to receive approximately $103 million of dividends annually from PetroBakken, paid monthly. PetroBakken instituted a dividend re-investment plan ("DRIP") in 2012, which allows shareholders to reinvest monthly cash dividends in new shares at a five percent discount to the then current market price. During the six months ended June 30, 2012, Petrobank received dividends totalling approximately $8.8 million in cash and 3,393,068 PetroBakken common shares from the DRIP. Due to Petrobank's significant positive working capital balance, we elected to participate at a 100 percent level in PetroBakken's DRIP, starting with the March dividend. Petrobank may change its participation level in the future.

In April 2012, Petrobank entered into an Automatic Share Repurchase and PetroBakken Share Sale Plan (the "Plan") pursuant to which our designated broker was instructed to automatically sell one PetroBakken share for each Petrobank share purchased under the Plan, subject to certain trading parameters set forth in the Plan and to daily and aggregate trading limits imposed by the rules and policies of the Toronto Stock Exchange. Under the Plan, during the three and six months ended June 30, 2012, the broker repurchased 4,574,800 Petrobank shares and sold 4,574,800 PetroBakken shares for net proceeds to Petrobank of approximately $3.6 million. Petrobank repurchased an additional 1,782,200 shares during the six months ended June 30, 2012 under our NCIB for $26.0 million.

As of July 16, 2012, we completed the Plan and our NCIB. In total, we repurchased our approved limit of 7,273,401 Petrobank shares at a cost of $88.0 million and sold 5,491,201 PetroBakken shares for proceeds of $66.5 million to fund a portion of the Petrobank share repurchases. The transactions under the Plan resulted in net cash proceeds to Petrobank of $4.6 million. Upon completion of the Plan and our NCIB, the number of PetroBakken shares owned per Petrobank share outstanding increased to approximately 1.08 from 1.03 at December 31, 2011.

The Petrobank legal entity has not paid or declared any dividends since the date of incorporation.

PetroBakken

PetroBakken's policy is to maintain a strong capital base in order to provide flexibility for the future development of the business.

PetroBakken manages their capital structure and makes adjustments to it in light of changes in economic conditions and the risk characteristics of the underlying assets. PetroBakken considers their capital structure to include common shares, bank debt outstanding, convertible debentures, senior unsecured notes and working capital. In order to maintain or adjust the capital structure, from time to time PetroBakken may issue common shares, debt or other securities, sell assets or adjust capital spending or dividend payments to manage current and projected debt levels.

PetroBakken monitors their leverage and adjusts the capital structure based on the ratio of non-convertible debt to annualized earnings before interest, taxes and non-cash items. At June 30, 2012, the ratio of non-convertible debt to annualized second quarter 2012 earnings before interest, taxes and non-cash items was 2.0 to 1, which is within a range acceptable to management. PetroBakken uses the ratio of non-convertible debt to annualized earnings before interest, taxes and non-cash items as a key indicator of PetroBakken's leverage and to monitor the strength of the statement of financial position. In order to facilitate the management of this ratio, PetroBakken prepares annual budgets, which are updated as necessary depending on varying factors including current and forecast commodity prices, changes in capital structure, execution of PetroBakken's business plan and general industry conditions. The annual budget is approved by the PetroBakken Board of Directors and updates are prepared and reviewed as required.

PetroBakken is in compliance with all covenants on the credit facility agreement. The credit facility has financial covenants that limit the ratio of secured debt (defined as total drawn on credit facility) to earnings before interest, taxes, depreciation and amortization ("EBITDA") to 3:1, limit the ratio of total debt (defined as total drawn on credit facility plus value of outstanding convertible debenture in Canadian dollars plus the value of the senior unsecured notes in Canadian dollars) to EBITDA on a trailing 12 month basis to 4:1, and limit secured debt to 50 percent of total liabilities plus total equity.

PetroBakken's convertible debentures are considered by management to be equity as opposed to debt for capital management purposes. PetroBakken has the option to repay the principal and interest amount in common shares or cash at the put or maturity date. PetroBakken is in compliance with the covenants on their convertible debentures. The convertible debenture agreement stipulates that the ratio of secured debt to total assets is not to exceed 35 percent.

PetroBakken is in compliance with all covenants on the Notes. The Notes contain covenants that could limit the Company's ability to issue additional debt, pay dividends, and repurchase stock among other restrictions.

PetroBakken had positive cash flow from operations for the three and six months ended June 30, 2012 and a credit facility with $1.1 billion of available capacity as at June 30, 2012 (December 31, 2011 - $0.2 billion).

Note 17 – Financial Instruments and Financial Risk Management

The Company identifies and analyzes the risks faced by the Company and may utilize financial instruments to mitigate these risks.

Commodity Contracts

PetroBakken had the following crude oil price risk management contracts outstanding at June 30, 2012:

Crude Oil Price Risk Management Contracts – WTI [1]

Term	Volume (bopd)	Average Price ($/bbl)	Benchmark
Jul. 2012 – Dec. 2012	12,000	$78.02 floor / $118.94 ceiling	US$ WTI
Jan. 2013 – Jun. 2013	11,250	$78.11 floor / $120.25 ceiling	US$ WTI
Jul. 2013 – Dec. 2013	9,250	$79.19 floor / $120.22 ceiling	US$ WTI
Jan. 2014 – Jun. 2014	4,250	$80.88 floor / $113.20 ceiling	US$ WTI
Jul. 2014 – Dec. 2014	1,750	$82.86 floor / $117.45 ceiling	US$ WTI

(1) Prices are the volume weighted average prices for the period.

The fair value of the commodity risk management contracts as at June 30, 2012 is a $28.0 million asset (December 31, 2011 - $0.8 million liability).

Foreign Exchange

PetroBakken entered into short-term foreign exchange contracts for the U.S. dollar interest payments. The following is a summary of foreign exchange contracts in place at June 30, 2012:

Foreign Exchange Risk Management Contracts

Term	Type	Amount (USD)	Rate (USD/CAD)
Jul. 2012	Collar	$10,000,000	$1.010 floor/$1.030 ceiling
Jul. 2012	Forward	$10,000,000	$1.022 [1]

(1) Weighted average rate.

The fair value of the foreign exchange contracts as at June 30, 2012 is a $0.1 million liability (December 31, 2011 - $nil).

Subsequent to June 30, 2012, PetroBakken settled foreign exchange contracts totalling US$40.0 million at a weighted average USD/CAD rate of 1.0169.

Fair Value of Financial Derivative Contracts

The following table summarizes the change in the fair value of PetroBakken's derivative contracts:

	Crude Oil	Interest	Foreign Exchange	Total
Risk management liability, as at December 31, 2011	$ (842)	$ (188)	$ -	$ (1,030)
Unrealized gain (loss)	28,856	188	(37)	29,007
Risk management asset (liability), as at June 30, 2012	**$ 28,014**	**$ -**	**$ (37)**	**$ 27,977**

The net risk management liability consists of current and non-current assets and liabilities. The table below summarizes the components of the net risk management liability as at June 30, 2012:

	Crude Oil	Foreign Exchange	June 30, 2012
Current			
Risk management asset	$ 14,283	$ -	$ 14,283
Risk management liability	-	(37)	(37)
Non-current			
Risk management asset	13,781	-	13,781
Risk management liability	(50)	-	(50)
Net risk management asset (liability)	**$ 28,014**	**$ (37)**	**$ 27,977**

The realized gain (loss) represents the risk management contracts settled in the period. The unrealized gain (loss) represents the change in fair value of the underlying risk management contracts to be settled in the future. The table below summarizes the components of the realized and unrealized risk management gains and losses for the three and six months ended June 30, 2012 and 2011:

	Three months ended June 30,		Six months ended June 30,	
	2012	2011	**2012**	2011
Realized gain (loss) on risk management contracts:				
Crude oil derivative contracts	**$ 2,300**	$ (3,578)	**$ 1,164**	$ (4,674)
Natural gas derivative contracts	**-**	435	**-**	1,176
Interest rate swap contracts	**(59)**	(212)	**(158)**	(446)
Foreign exchange derivative contracts	**(75)**	-	**(75)**	-
	2,166	(3,355)	**931**	(3,944)
Unrealized gain (loss) on risk management contracts:				
Crude oil derivative contracts	**46,702**	37,626	**28,856**	683
Natural gas derivative contracts	**-**	(404)	**-**	(1,173)
Interest rate swap contracts	**56**	(135)	**188**	(185)
Foreign exchange derivative contracts	**(37)**	-	**(37)**	-
	46,721	37,087	**29,007**	(675)
Gain (loss) on risk management contracts	**$ 48,887**	$ 33,732	**$ 29,938**	$ (4,619)

Note 18 – Changes in Non-Cash Working Capital

	Three months ended June 30,		Six months ended June 30,	
	2012	2011	**2012**	2011
Change in:				
Accounts receivable	**$ 19,911**	$ 47,819	**$ 67,316**	$ 21,578
Prepaid expenses	**43**	(793)	**(1,534)**	(4,547)
Accounts payable and accrued liabilities	**(91,662)**	(245,907)	**(136,603)**	(164,252)
Other	**(307)**	1,111	**(614)**	4,856
	(72,015)	(197,770)	**(71,435)**	(142,365)
Working capital deficiencies acquired	**100**	-	**100**	-
	$ (71,915)	$ (197,770)	**$ (71,335)**	$ (142,365)
Changes relating to:				
Attributable to operating activities	**$ 28,217**	$ 36,533	**$ 58,716**	$ (1,190)
Attributable to investing activities	**$ (100,149)**	$ (234,307)	**$ (122,021)**	$ (140,670)
Attributable to financing activities	**$ 17**	$ 4	**$ (8,030)**	$ (505)
	$ (71,915)	$ (197,770)	**$ (71,335)**	$ (142,365)

Note 19 – Commitments

The following is a summary of the estimated costs required to fulfill the Company's remaining contractual commitments at June 30, 2012:

Type of Commitment	< 1 Year	1-3 Years	4-5 Years	Thereafter	Total
Petrobank Standalone					
Office operating leases [(1)]	$ 1,229	$ 1,247	$ 386	$ 431	$ 3,293
Finance leases	295	1,059	97	-	1,451
PetroBakken					
Office leases [(1)]	5,319	12,736	12,919	24,896	55,870
Drilling and completion rigs	17,208	22,444	2,488	-	42,140
Other	1,500	1,360	239	-	3,099
Total Commitments	**$ 25,551**	**$ 38,846**	**$ 16,129**	**$ 25,327**	**$ 105,853**

(1) Minimum lease payments are net of sub-lease payments received by the Company, which reduces rent expense included in general and administrative expenses on the condensed interim consolidated statement of operations.