FAIRBORNE ENERGY LTD.

2011 second quarter interim report

HIGHLIGHTS

	THREE MONTHS ENDED JUNE 30, 2011	2010	SIX MONTHS ENDED JUNE 30, 2011	2010
Financial ($THOUSANDS, EXCEPT PER SHARE AMOUNTS)				
Petroleum and natural gas revenue	**54,442**	59,633	**102,973**	123,015
Funds generated from operations (1)	**27,241**	32,261	**57,074**	75,017
Per share – basic	**$0.27**	$0.31	**$0.56**	$0.73
Per share – diluted	**$0.26**	$0.31	**$0.55**	$0.73
Cash flow from operations				
(including changes in working capital)	**24,102**	26,273	**49,198**	70,817
Per share – basic	**$0.24**	$0.26	**$0.48**	$0.69
Per share – diluted	**$0.23**	$0.26	**$0.47**	$0.69
Profit	**652**	2,361	**33,302**	13,446
Per share – basic	**$0.01**	$0.02	**$0.33**	$0.13
Per share – diluted	**$0.01**	$0.02	**$0.32**	$0.13
Exploration and development expenditures	**26,039**	21,492	**97,695**	88,708
Proceeds from the sale of petroleum				
and natural gas properties	**(17,920)**	–	**(141,380)**	–
Working capital (surplus) deficit				
(excluding convertible debentures)	**(21,673)**	6,487	**(21,673)**	6,487
Bank indebtedness	**152,227**	123,081	**152,227**	123,081
Convertible debentures	**98,706**	96,508	**98,706**	96,508
Operations				
Average production				
Natural gas *(Mcf per day)*	**65,171**	66,812	**64,365**	63,862
Crude oil *(bbls per day)*	**2,287**	3,110	**2,497**	3,055
Natural gas liquids *(bbls per day)*	**766**	1,149	**892**	919
Sulphur *(tonnes per day)* (2), (4)	**56**	92	**62**	73
Total *(BOE per day)*	**13,971**	15,486	**14,179**	14,690
Average sales price (3)				
Natural gas *($ per Mcf)*	**4.45**	4.91	**4.40**	5.31
Crude oil *($ per bbl)*	**94.13**	75.79	**87.47**	77.48
Natural gas liquids *($ per bbl)*	**63.75**	36.24	**58.60**	40.87
Sulphur *($ per tonne)* (4)	**127.96**	60.26	**111.94**	29.64
Netback per BOE *($ per BOE)*				
Petroleum and natural gas sales (3)	**40.50**	39.63	**39.82**	42.14
Sulphur block revenue	**–**	2.52	**–**	3.95
Royalties	**(6.30)**	(6.16)	**(4.63)**	(5.35)
Operating expenses	**(8.89)**	(9.22)	**(9.14)**	(8.95)
Transportation	**(1.05)**	(1.10)	**(1.05)**	(1.07)
Operating netback	**24.26**	25.67	**25.00**	30.72
Wells drilled *(gross)*	**3**	1	**25**	17
Undeveloped land *(net acres)*	**228,272**	232,466	**228,272**	232,466

(1) The calculation of funds generated from operations and cash flow from operations for the three months ended June 30, 2011 exclude $3.7 million (June 30, 2010 - $3.2 million) of interest expense which is classified as finance expense under IFRS. Similarly, for the six months ended June 30, 2011, $7.8 million (2010 - $6.2 million) of interest expense is classified as finance expense under IFRS.

(2) A BOE conversion ratio has been calculated using a conversion rate of one tonne of sulphur to one barrel.

(3) Excludes the change in fair value of derivatives.

(4) Excludes the sale of inventory at the West Pembina sulphur block.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following Management Discussion and Analysis of Financial Condition and Results of Operations ("MD&A") was prepared at, and is dated, August 2, 2011. This document is provided by the management of Fairborne Energy Ltd. ("Fairborne" or the "Company") to review second quarter 2011 activities and results as compared to the same period in the previous year, and should be read in conjunction with the unaudited interim consolidated financial statements including selected notes for the three and six months ended June 30, 2011 and the audited consolidated financial statements including notes for the years ended December 31, 2010 and 2009. The MD&A should be read in conjunction with the Company's MD&A for the year ended December 31, 2010, as disclosure which is unchanged from the December 31, 2010 MD&A has not been duplicated herein. Additional information relating to Fairborne, including Fairborne's annual information form, is available on SEDAR at www.sedar.com

Nature of Business: Fairborne is a growth-oriented exploration and production company. The Company maintains its head office in Calgary and is engaged in the business of exploring for, developing, acquiring and producing crude oil and natural gas in Western Canada. Fairborne follows a strategy of balancing risk and reward by focusing on opportunities by geographic area and prospect type. Within the selected areas, the Company develops a portfolio of exploration and development prospects in conjunction with an active acquisition strategy.

Forward Looking Statements: This document contains forward-looking statements. Management's assessment of future plans and operations and ability to satisfy Convertible Debentures when due may constitute forward-looking statements under applicable securities laws and necessarily involve risks including, without limitation, risks associated with oil and gas exploration, development, exploitation, production, marketing and transportation, loss of markets, volatility of commodity prices, currency fluctuations, imprecision of reserve estimates, environmental risks, competition from other producers, inability to retain drilling rigs and other services, incorrect assessment of the value of acquisitions, failure to realize the anticipated benefits of acquisitions, the inability to fully realize the benefits of the acquisitions, delays resulting from or inability to obtain required regulatory approvals and ability to access sufficient capital from internal and external sources. As a consequence, the Company's actual results may differ materially from those expressed in, or implied by, the forward looking statements. Forward looking statements or information are based on a number of factors and assumptions which have been used to develop such statements and information but which may prove to be incorrect. Although Fairborne believes that the expectations reflected in such forward-looking statements or information are reasonable, undue reliance should not be placed on forward looking statements because the Company can give no assurance that such expectations will prove to be correct. In addition to other factors and assumptions which may be identified in this document and other documents filed by the Company, assumptions have been

Interim Management's Discussion & Analysis

made regarding, among other things: the impact of increasing competition; the general stability of the economic and political environment in which Fairborne operates; the ability of the Company to obtain qualified staff, equipment and services in a timely and cost efficient manner; drilling results; the ability of the operator of the projects which the Company has an interest in to operate the field in a safe, efficient and effective manner; Fairborne's ability to obtain financing on acceptable terms; field production rates and decline rates; the ability to replace and expand oil and natural gas reserves through acquisition, development or exploration; the timing and costs of pipeline, storage and facility construction and expansion; the ability of the Company to secure adequate product transportation; future oil and natural gas prices; currency, exchange and interest rates; the regulatory framework regarding royalties, taxes and environmental matters in the jurisdictions in which the Company operates; and Fairborne's ability to successfully market its oil and natural gas products. Readers are cautioned that the foregoing list of factors is not exhaustive. Additional information on these and other factors that could affect the Company's operations and financial results are included in reports on file with Canadian securities regulatory authorities and may be accessed through the SEDAR website (www.sedar.com) or at the Company's website (www.fairborne-energy.com).

Furthermore, the forward looking statements contained in this document are made as at the date of this document and the Company does not undertake any obligation to update publicly or to revise any of the included forward looking statements, whether as a result of new information, future events or otherwise, except as may be required by applicable securities laws.

Non-IFRS Terms: This document contains the terms "funds generated from operations per share", "cash flow from operations per share", "net debt" and "netbacks" which are non-IFRS terms. The Company uses these measures to help evaluate its performance. The Company uses net debt (bank indebtedness plus negative working capital or less positive working capital, excluding convertible debentures) as an alternative measure of outstanding debt. The Company considers corporate netbacks a key measure as it demonstrates its profitability relative to current commodity prices. Netbacks which have no IFRS equivalent are calculated on a BOE basis by deducting royalties, operating costs, and transportation from petroleum and natural gas sales and sulphur block sales. Fairborne also presents funds generated from operations per share and cash flow from operations per share and such per share amounts are calculated using weighted average shares outstanding consistent with the calculation of profit per share.

BOE Conversions: Barrel of oil equivalent ("BOE") amounts may be misleading, particularly if used in isolation. A BOE conversion ratio has been calculated using a conversion rate of one tonne of sulphur to one barrel and six thousand cubic feet of natural gas to one barrel. This conversion ratio of six thousand cubic feet of natural gas to one barrel is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead.

CHANGE IN ACCOUNTING POLICIES AND RECENT ACCOUNTING PRONOUNCEMENTS

Changeover to International Financial Reporting Standards ("IFRS")

Prior to 2011, Fairborne prepared its financial statements under Canadian Generally Accepted Accounting Principles ("GAAP"). Effective January 1, 2011, Canadian public companies were required to adopt International Financial Reporting Standards ("IFRS"). The Company's interim consolidated financial statements for the three and six months ended June 30, 2011, including comparative amounts, have been prepared on an IFRS basis. Information previously reported under Canadian GAAP has been restated under IFRS with reconciliations provided in the notes to the interim consolidated financial statements as at and for the three and six months ended June 30, 2011.

SECOND QUARTER 2011 FINANCIAL RESULTS

Production

	THREE MONTHS ENDED JUNE 30,		SIX MONTHS ENDED JUNE 30,	
	2011	2010	**2011**	2010
Natural gas *(Mcf per day)*	**65,171**	66,812	**64,365**	63,862
Crude oil *(bbls per day)*	**2,287**	3,110	**2,497**	3,055
Natural gas liquids *(bbls per day)*	**766**	1,149	**892**	919
Sulphur *(tonnes per day)* [(1), (2)]	**56**	92	**62**	73
Total *(BOE per day)*	**13,971**	15,486	**14,179**	14,690
Natural gas % of production	**78%**	72%	**76%**	72%

(1) A BOE conversion ratio has been calculated using a conversion rate of one tonne of sulphur to one barrel.
(2) Excludes the sale of inventory at the West Pembina sulphur block.

Second quarter 2011 reflected the full impact of the property disposition completed late in the first quarter of 2011 which reduced production by approximately 1,800 BOE per day. In addition, production continued to be negatively impacted by a mechanical failure at a third party gas plant as well as wet weather conditions on the Company's Saskatchewan and Manitoba properties. Despite production interruptions and property sales, production increases from new wells during the second quarter resulted in average production of 13,971 BOE per day, only 3% lower than the preceding first quarter of 2011 (14,388 BOE per day), and 10% lower than the comparative second quarter of 2010 (15,486 BOE per day).

Natural gas production of 65.2 MMcf per day during the second quarter of 2011 was marginally higher than the preceding first quarter of 2011 (63.6 MMcf per day) reflecting the successful first quarter drilling program, which more than offset properties disposed during the first quarter.

Crude oil and NGL production of 3,053 bbls per day for the second quarter of 2011 was 28% lower than the second quarter of 2010 (4,259 BOE per day) and 18% lower than preceding first quarter of 2011 (3,730 BOE per day) reflecting the impact of the property disposition completed in the first quarter.

Interim Management's Discussion & Analysis

Commodity Prices & Risk Management Activities

	THREE MONTHS ENDED JUNE 30,		SIX MONTHS ENDED JUNE 30,	
	2011	2010	**2011**	2010
Average Prices [1]				
Natural gas *($ per Mcf)*	**4.45**	4.91	**4.40**	5.31
Crude oil *($ per bbl)*	**94.13**	75.79	**87.47**	77.48
Natural gas liquids *($ per bbl)*	**63.75**	36.24	**58.60**	40.87
Sulphur *($ per tonne)* [2]	**127.96**	60.26	**111.94**	29.64
BOE *($ per BOE)*	**40.20**	39.45	**39.58**	41.89
Benchmark Prices				
AECO Daily Index *(Cdn$ per Mcf)*	**3.88**	3.89	**3.83**	4.42
AECO Monthly Index *(Cdn$ per Mcf)*	**3.74**	3.86	**3.76**	4.61
Edmonton par *(Cdn$ per bbl)*	**102.65**	75.14	**95.54**	77.72
Nymex Calendar Average *(US$ per bbl)*	**102.56**	78.03	**98.33**	78.37

(1) Excludes the change in the fair value of derivatives.
(2) Excludes revenue from the sale of inventory at the West Pembina sulphur block.

Risk Management – Physical Sales Contracts

Fairborne's risk management strategy is based on the following objectives:

- protect shareholder return on investment;
- reduce risk exposure in budgeted annual funds flow projections; and
- help ensure transaction economics on acquisitions.

Natural Gas

Fairborne's average realized natural gas price in the second quarter of 2011 was 15% higher than the AECO Daily benchmark reference price due to corporate hedging activities and the higher heat content of Fairborne's production. Compared to the prior year, Fairborne's realized natural gas price for the three months ending June 30, 2011 was 9% lower due to different physical sales and derivative contracts in 2011. An average of 13,340 Mcf per day was sold under fixed price physical sales and derivative contracts during the second quarter of 2011 representing 20% of the Company's natural gas production. Risk management activities increased the Company's natural gas revenue by an estimated $1.9 million in the second quarter of 2011 which had the effect of increasing Fairborne's realized natural gas price by $0.32 per Mcf to $4.45 per Mcf.

At June 30, 2011, Fairborne had one natural gas swap that was accounted for as a derivative contract and the mark-to-market value of this contract was recorded as an asset of $1.5 million at June 30, 2011.

The following table summarizes the outstanding fixed price physical sales and derivative contracts for natural gas, including contracts outstanding at June 30, 2011 as well as contracts entered into after June 30, 2011:

	2011
Swaps	
Volume *(Mcf per day)*	**13,274**
Average price *($ per Mcf)*	**5.71**

Conversion factor: 1 Mcf = 1.13 GJ

Crude Oil

During the second quarter of 2011, Fairborne had an average of 1,000 bbls per day of crude oil under fixed price physical sales and derivative contracts representing 44% of crude oil production. Risk management activities, including option costs for puts purchased during the quarter, reduced the Company's crude oil revenue by $1.2 million ($5.77 per bbl) in the second quarter. Fairborne's realized crude oil price of $94.13 per bbl in the second quarter of 2011 was 24% higher than the same period in 2010 reflecting the overall increase in market prices.

The following table summarizes the outstanding fixed price physical sales and derivative contracts on crude oil, including contracts outstanding at June 30, 2011 as well as contracts entered into after June 30, 2011:

	2011
Collars	
Volume *(bbls per day)*	**500**
Average floor *(CDN$ per bbl)*	**$70.00**
Average ceiling *(CDN$ per bbl)*	**$101.25**
Swaps	
Volume *(bbls per day)*	**500**
Average price *(CDN$ per bbl)*	**$75.00**
Total volume *(bbls per day)*	**1,000**
Average floor price *(CDN$ per bbl)*	**$72.50**

At June 30, 2011, Fairborne had one crude oil collar and one crude oil swap that were accounted for as derivative contracts and the combined mark-to-market value of these contracts was recorded as a liability of $2.1 million at June 30, 2011. The liability was partially offset by the asset recorded on the derivative natural gas contract.

Sulphur

The Company's average realized sulphur price in the second quarter of 2011 was $127.96 per tonne, compared to $60.26 in the second quarter of 2010 reflecting the continued recovery of sulphur prices during 2011.

Interim Management's Discussion & Analysis

Petroleum and Natural Gas Revenue

	THREE MONTHS ENDED JUNE 30,			SIX MONTHS ENDED JUNE 30,	
($thousands except as noted)	**2011**	2010		**2011**	2010
		IFRS	GAAP (1)		IFRS
Petroleum and natural gas sales:					
Natural gas	**26,420**	29,847	29,847	**51,316**	61,342
Crude oil	**19,596**	21,449	21,449	**39,544**	42,846
Natural gas liquids	**4,441**	3,789	3,789	**9,459**	6,794
Sulphur	**657**	504	504	**1,248**	390
Total	**51,114**	55,589	55,589	**101,567**	111,372
Per BOE	**$40.20**	$39.45	$39.45	**$39.58**	$41.89
Other petroleum and natural gas revenue items:					
Sulphur block	**–**	3,552	3,552	**–**	10,511
Change in fair value of derivatives	**2,952**	233	233	**796**	455
Royalty income	**376**	259	259	**610**	677
Total	**3,328**	4,044	4,044	**1,406**	11,643
Total petroleum and natural gas revenue	**54,442**	59,633	59,633	**102,973**	123,015
Per BOE	**$42.82**	$42.32	$42.32	**$40.12**	$46.27

(1) As previously reported under Canadian GAAP.

The calculation of Fairborne's reported petroleum and natural gas revenue for the three months ended June 30, 2010 was unchanged upon restatement to IFRS.

Fairborne reported petroleum and natural gas sales of $51.1 million for the second quarter of 2011, representing a slight increase from the preceding first quarter of 2011 ($50.5 million) and an 8% decrease from the $55.6 million reported in the second quarter of 2010. Compared to the preceding first quarter, second quarter 2011 petroleum and natural gas sales reflected lower oil and NGL production partially offset by higher commodity prices and natural gas production. Compared to the prior year, second quarter 2011 petroleum and natural gas sales reflected lower production and natural gas prices partially offset by higher crude oil prices.

Other revenue items in the second quarter of 2010 included $3.6 million of revenue from Fairborne's contract for the sale of inventory at the West Pembina sulphur block. This contract was satisfied in June 2010 and no further revenue will be recognized. The change in fair value of derivatives represents the change in the mark-to-market value of derivative contracts. The $3.0 million increase recorded in the second quarter of 2011 (2010 – $0.2 million) reflects both the changes in the unrealized value of existing contracts as well as a reduction for amounts realized on contracts that settled during the period. Fairborne's risk management program, including derivative contracts and physical sales contracts, increased the Company's realized revenue by an estimated $0.7 million in the second quarter of 2011, compared to an increase to revenue of $4.8 million in the second quarter of 2010.

Royalties

($thousands except as noted)	THREE MONTHS ENDED JUNE 30, 2011	2010 IFRS	2010 GAAP (1)	SIX MONTHS ENDED JUNE 30, 2011	2010 IFRS
Crown	**5,767**	6,762	6,762	**7,494**	10,398
Freehold and overriding	**2,247**	1,924	1,924	**4,386**	3,822
Total	**8,014**	8,686	8,686	**11,880**	14,220
Crown *(% of P&NG sales)*	**11.3%**	12.2%	12.2%	**7.4%**	9.3%
Freehold and overriding *(% of P&NG sales)*	**4.4%**	3.5%	3.5%	**4.3%**	3.4%
Total *(% of P&NG sales)*	**15.7%**	15.6%	15.6%	**11.7%**	12.8%
Per BOE	**$6.30**	$6.16	$6.16	**$4.63**	$5.35

(1) As previously reported under Canadian GAAP.

The calculation of Fairborne's reported royalties for the three months ended June 30, 2010 was unchanged upon restatement to IFRS.

Fairborne recorded $8.0 million of royalties during the second quarter of 2011, representing a royalty rate of 15.7%, consistent with the prior year rate of 15.6%. Royalties for the second quarter of both 2011 and 2010 included royalty adjustments resulting from the Crown's annual recalculation of allowable deductions and credits. These second quarter adjustments were $3.1 million in 2011 and $3.3 million in 2010 resulting in comparable royalty rates year over year and higher reported royalties from the preceding first quarter 2011 rate of 7.6%.

Production and Operating Costs

($thousands except as noted)	THREE MONTHS ENDED JUNE 30, 2011	2010 IFRS	2010 GAAP (1)	SIX MONTHS ENDED JUNE 30, 2011	2010 IFRS
Operating costs					
Natural gas	**8,800**	9,278	10,069	**17,508**	17,224
Oil and NGLs	**2,501**	3,715	3,715	**5,949**	6,567
Transportation costs	**1,339**	1,553	1,553	**2,691**	2,844
Total	**12,640**	14,546	15,337	**26,148**	26,635
Operating costs, per BOE	**$8.89**	$9.22	$9.78	**$9.14**	$8.95
Transportation costs, per BOE	**$1.05**	$1.10	$1.10	**$1.05**	$1.07
Production and operating costs, per BOE	**$9.94**	$10.32	$10.88	**$10.19**	$10.02

(1) As previously reported under Canadian GAAP.

The calculation of Fairborne's reported production and operating costs for the three months ended June 30, 2010 was reduced by $0.8 million upon restatement to IFRS as a result of turnarounds and overhauls being capitalized under IFRS. In addition, transportation costs have been reclassified and are included in production and operating costs under IFRS.

Interim Management's Discussion & Analysis

Fairborne recorded operating costs of $11.3 million ($8.89 per BOE) during the second quarter of 2011, 5% lower than the preceding first quarter of 2011 ($9.39 per BOE) and 4% lower than the second quarter of 2010 ($9.22 per BOE). Operating cost reductions were attributed to the start up of the Company's Marlboro gas plant in May 2011 as well as the property disposition in March 2011 which included properties with a combined operating cost in excess of the corporate average.

Transportation costs of $1.3 million ($1.05 per BOE) for the second quarter of 2011 include clean oil trucking, trucking of natural gas liquids, certain third party fuel charges and transportation and fuel costs associated with the usage of natural gas pipelines. Transportation costs in the second quarter of 2011 are consistent when compared to the preceding first quarter of 2011 ($1.04 per BOE).

Operating Netbacks

($ per BOE)	THREE MONTHS ENDED JUNE 30, 2011	2010		SIX MONTHS ENDED JUNE 30, 2011	2010
		IFRS	GAAP (1)		IFRS
Petroleum and natural gas sales (2)	**40.20**	39.45	39.45	**39.58**	41.89
Sulphur block revenue	**–**	2.52	2.52	**–**	3.95
Royalty income	**0.30**	0.18	0.18	**0.24**	0.25
Royalties	**(6.30)**	(6.16)	(6.16)	**(4.63)**	(5.35)
Operating costs	**(8.89)**	(9.22)	(9.78)	**(9.14)**	(8.95)
Transportation	**(1.05)**	(1.10)	(1.10)	**(1.05)**	(1.07)
Operating netback	**24.26**	25.67	25.11	**25.00**	30.72

(1) As previously reported under Canadian GAAP.

(2) Excludes the change in fair value of derivatives

Fairborne's operating netback of $24.26 per BOE was 6% lower than the first quarter of 2011 ($25.72 per BOE) and 5% lower compared to the second quarter of 2010 ($25.67 per BOE). Compared to the first quarter of 2011, the decrease in operating netbacks reflects an increase in royalties partially offset by stronger commodity prices and reduced operating expenses. Compared to the second quarter of 2010, the decrease in operating netback is primarily due to no sulphur block revenue being received in 2011.

General and Administrative ("G&A") Expenses

($thousands except as noted)	THREE MONTHS ENDED JUNE 30, 2011	2010		SIX MONTHS ENDED JUNE 30, 2011	2010
		IFRS	GAAP (1)		IFRS
G&A expenses, net of recoveries	**3,595**	3,907	4,703	**7,075**	6,264
Compensation costs	**648**	778	1,094	**1,362**	1,130
Total G&A expenses	**4,243**	4,685	5,797	**8,437**	7,394
G&A expenses, net of recoveries, per BOE	**$2.83**	$2.77	$3.34	**$2.76**	$2.36
Compensation costs, per BOE	**$0.51**	$0.56	$0.78	**$0.53**	$0.42

(1) As previously reported under Canadian GAAP.

Fairborne's G&A expenses for the three months ended June 30, 2010 was reduced by $0.8 million and compensation costs were reduced by $0.3 million upon restatement to IFRS as a result of directly attributable general and administrative costs and associated compensation costs that were capitalized to exploration and evaluation assets and petroleum and natural gas properties and equipment under IFRS. The amount that has been capitalized under IFRS is in excess of the capitalized portion permitted under joint operating agreements.

Fairborne recorded $3.6 million ($2.83 per BOE) of G&A expenses, net of recoveries, in the second quarter of 2011, consistent when compared to the preceding first quarter of 2011 ($2.69 per BOE) and the comparative prior year ($2.77 per BOE). On a year to date basis, 2011 G&A expenses of $7.1 million are 13% higher than the prior year due to costs associated with the 2010 employee bonus program which was recorded in the first quarter of 2011.

Compensation expense of $0.6 million in the second quarter of 2011 is consistent with the preceding first quarter of 2011 ($0.7 million) and the second quarter of 2010 ($0.8 million).

Depreciation and Amortization ("D&A")

	THREE MONTHS ENDED JUNE 30,			SIX MONTHS ENDED JUNE 30,	
	2011	2010		**2011**	2010
		IFRS	GAAP (1)		IFRS
Depreciation and amortization *($thousands)*	**23,491**	25,200	35,048	**47,088**	47,927
Per BOE	**$18.48**	$17.88	$24.87	**$18.35**	$18.03

(1) As previously reported under Canadian GAAP.

Fairborne's depreciation and amortization for the three months ended June 30, 2010 was reduced by $9.8 million upon restatement to IFRS. Although IFRS requires a unit of production calculation which is consistent with Canadian GAAP, under IFRS, Fairborne has elected to base depreciation on proved plus probable reserves while Canadian GAAP was proved reserves only. D&A also increased $0.2 million as a result of the depreciation of turnarounds that are now capitalized under IFRS. In addition, ARO accretion of $0.2 million has been reclassified to finance expense under IFRS.

Fairborne recorded $23.5 million ($18.48 per BOE) in depletion and amortization in the second quarter of 2011, consistent with $23.6 million recorded in the preceding first quarter of 2011 ($18.22 per BOE).

Gain on Disposition of Capital Assets

	THREE MONTHS ENDED JUNE 30,			SIX MONTHS ENDED JUNE 30,	
($thousands except as noted)	**2011**	2010		**2011**	2010
		IFRS	GAAP (1)		IFRS
Gain on disposition of P&NG assets	**–**	–	–	**47,167**	–
Gain (loss) on recognition of non-monetary transactions	**(411)**	1,096	–	**517**	1,237
Total gain (loss) on disposition of capital assets	**(411)**	1,096	–	**47,684**	1,237
Per BOE	**$(0.32)**	$0.78	–	**$18.59**	$0.47

(1) As previously reported under Canadian GAAP.

Interim Management's Discussion & Analysis

Under the Canadian GAAP full cost accounting guideline, gains or losses were not recognized upon the disposition of P&NG assets unless the disposition resulted in a significant change in the depletion rate. Under IFRS, gains and losses are recognized in profit on the disposal of an item of P&NG assets. The amount of the gain or loss is determined by comparing the proceeds from disposal with the carrying amount of the item. This will include transactions such as sales of assets, farm-outs, asset swaps and other non-monetary transactions which typically were not recorded under Canadian GAAP. For the six months ended June 30, 2011, the gain on disposition of capital assets includes a $47.2 million gain related to the property disposition completed in the first quarter of 2011.

Finance Expense

($thousands except as noted)	THREE MONTHS ENDED JUNE 30, 2011	2010 IFRS	2010 GAAP (1)	SIX MONTHS ENDED JUNE 30, 2011	2010 IFRS
Interest expense	**3,656**	3,226	3,226	**7,827**	6,219
Accretion of convertible debentures	**571**	550	483	**1,142**	1,100
Accretion of asset retirement obligation	**233**	241	241	**458**	483
Impairment loss on trade receivable	**–**	–	–	**117**	–
Total finance expense	**4,460**	4,017	3,950	**9,544**	7,802
Per BOE	**$3.51**	$2.85	$2.80	**$3.72**	$2.93

(1) As previously reported under Canadian GAAP.

Under IFRS, finance income and finance expenses are reported separately from operating activities. The accretion of convertible debentures for the three months ended June 30, 2010 was increased by $0.1 million upon restatement to IFRS. Under IFRS, the allocation used to determine the equity and liability components of the convertible debentures was determined using the relative fair values on December 19, 2007 when Fairborne converted from a trust to a corporation as opposed to the date of issue under Canadian GAAP. In addition, under IFRS, accretion of asset retirement obligation of $0.2 million was reclassified from D&A to finance expense.

Fairborne recorded $4.5 million in finance expense in the second quarter of 2011, a 12% decrease from the preceding quarter (Q1 2011 – $5.1 million), consistent with lower debt levels in the second quarter. Finance expense increased 11% compared to the $4.0 million recorded in the second quarter of 2010, which was consistent with higher average debt levels during 2011 compared to the prior year. Also included in total interest is the amortization of financing charges associated with the issuance of the convertible debentures. The financing charges amortized in 2011 were consistent with the prior year. These costs will continue to be expensed over the term of the debentures.

Taxes

	THREE MONTHS ENDED JUNE 30, 2011	2010 IFRS	2010 GAAP (1)	SIX MONTHS ENDED JUNE 30, 2011	2010 IFRS
Deferred taxes (reduction) *($thousands)*	**531**	1,234	(1,823)	**14,258**	6,828
Per BOE	**$0.42**	$0.88	($1.29)	**$5.55**	$2.57

(1) As previously reported under Canadian GAAP.

Fairborne's deferred taxes for the three months ended June 30, 2010 increased $3.1 million upon restatement of IFRS. Conceptually, the calculation of deferred taxes remains the same under IFRS. The change in deferred taxes reflects the tax effect of other changes recorded upon restatement to IFRS.

Fairborne recorded deferred taxes of $0.5 million in the second quarter of 2011 compared to deferred taxes of $1.2 million during the second quarter of 2010, both of which reflect a provision for future tax at tax rates expected to apply when the related temporary differences reverse.

Profit and Funds Generated from Operations

	THREE MONTHS ENDED JUNE 30,			SIX MONTHS ENDED JUNE 30,	
($thousands except as noted)	**2011**	2010		**2011**	2010
		IFRS	GAAP [1]		IFRS
Funds generated from operations	**27,241**	32,261	27,448	**57,074**	75,017
Per share – basic	**$0.27**	$0.31	$0.27	**$0.56**	$0.73
Per share – diluted	**$0.26**	$0.31	$0.27	**$0.55**	$0.73
Cash flow from operations					
(including changes in working capital)	**24,102**	26,273	19,692	**49,198**	70,817
Per share – basic	**$0.24**	$0.26	$0.19	**$0.48**	$0.69
Per share – diluted	**$0.23**	$0.26	$0.19	**$0.47**	$0.69
Profit (loss)	**652**	2,361	(7,121)	**33,302**	13,446
Per share – basic	**$0.01**	$0.02	($0.07)	**$0.33**	$0.13
Per share – diluted	**$0.01**	$0.02	($0.07)	**$0.32**	$0.13

(1) As previously reported under Canadian GAAP.

BOE Analysis

	2011		2010	
THREE MONTHS ENDED JUNE 30,	**$THOUSANDS**	**$ PER BOE**	$THOUSANDS	$ PER BOE
Petroleum and natural gas revenue [1]	**54,442**	**42.82**	59,633	42.32
Royalties	**(8,014)**	**(6.30)**	(8,686)	(6.16)
Production and operating costs	**(12,640)**	**(9.94)**	(14,546)	(10.32)
Change in fair value of derivatives	**(2,952)**	**(2.32)**	(233)	(0.17)
General & administrative [2]	**(3,595)**	**(2.83)**	(3,907)	(2.77)
Funds generated from operations	**27,241**	**21.43**	32,261	22.90
Finance expense	**(4,460)**	**(3.51)**	(4,017)	(2.85)
Change in fair value of derivatives	**2,952**	**2.32**	233	0.17
Compensation expense – non-cash	**(648)**	**(0.51)**	(778)	(0.56)
Gain (loss) on disposition of capital assets	**(411)**	**(0.32)**	1,096	0.78
Depreciation and amortization	**(23,491)**	**(18.48)**	(25,200)	(17.88)
Deferred taxes	**(531)**	**(0.42)**	(1,234)	(0.88)
Profit	**652**	**0.51**	2,361	1.68

(1) Including the change in fair value of derivatives (non-cash) and revenue from the sale of inventory at the West Pembina sulphur block.
(2) Net of compensation expense (non-cash).

Interim Management's Discussion & Analysis

SIX MONTHS ENDED JUNE 30,	2011 $THOUSANDS	2011 $ PER BOE	2010 $THOUSANDS	2010 $ PER BOE
Petroleum and natural gas revenue (1)	102,973	40.12	123,015	46.27
Royalties	(11,880)	(4.63)	(14,220)	(5.35)
Operating expenses	(26,148)	(10.19)	(26,635)	(10.02)
Change in fair value of derivatives	(796)	(0.30)	(455)	(0.17)
General & administrative (2)	(7,075)	(2.76)	(6,264)	(2.36)
Compensation expense (3)	–	–	(424)	(0.16)
Funds generated from operations	57,074	22.24	75,017	28.21
Finance expense	(9,544)	(3.72)	(7,802)	(2.93)
Change in fair value of derivatives	796	0.30	455	0.17
Compensation expense – non-cash	(1,362)	(0.53)	(706)	(0.26)
Gain on disposition of capital assets	47,684	18.59	1,237	0.47
Depreciation and amortization	(47,088)	(18.35)	(47,927)	(18.03)
Deferred taxes	(14,258)	(5.55)	(6,828)	(2.57)
Profit	33,302	12.98	13,446	5.06

(1) Including the change in fair value of derivatives (non-cash) and revenue from the sale of inventory at the West Pembina sulphur block.
(2) Net of compensation expense.
(3) Cash component of compensation expense which resulted from the cash settlement of Restricted Units and Performance Units.

Fairborne reported funds generated from operations of $27.2 million ($21.43 per BOE) for the second quarter of 2011, a decrease of 16% when compared to the second quarter of 2010 ($32.3 million). The decrease in funds generated from operations reflected lower natural gas prices, lower sulphur block revenues and increased royalties in 2011.

The profit of $0.7 million for the second quarter of 2011 (Q2 2010 – $2.4 million) reflects the decrease in cash flows. The profit of $33.3 million ($12.98 per BOE) for the six months ended reflects the impact of the gain recorded on the property disposition completed late in the first quarter of 2011.

LIQUIDITY AND CAPITAL RESOURCES

Capital Expenditures

Under Canadian GAAP, all petroleum and natural gas assets were accounted for under the full cost accounting guideline. Under IFRS, P&NG assets have been divided into intangible exploration assets ("E&E assets") and petroleum and natural gas properties and equipment ("development assets").

Capital Expenditures – Petroleum and Natural Gas Properties and Equipment

($thousands)	Three months ended June 30, 2011	2010		Six months ended June 30, 2011	2010
		IFRS	GAAP (1)		IFRS
Development expenditures					
Land and property acquisitions	**4,143**	4,434	7,704	**5,131**	11,230
Geological and geophysical	**1,421**	1,258	1,183	**4,241**	4,516
Drilling and completions	**8,490**	8,733	7,809	**58,180**	52,215
Well equipment and facilities	**9,834**	3,183	3,054	**27,925**	13,689
Turnarounds and overhauls	**489**	804	–	**489**	1,031
Corporate assets	**251**	132	132	**318**	137
Total development expenditures	**24,628**	18,544	19,882	**96,284**	82,818
Dispositions					
Proceeds from sale of petroleum and natural gas properties	**(17,920)**	–	–	**(141,380)**	–

(1) *As previously reported under Canadian GAAP.*

Fairborne's development expenditures for the three months ended June 30, 2010 were reduced by $2.9 million upon restatement to IFRS as E&E expenditures are reported separately under IFRS. In addition, development expenditures increased by $0.8 million due to the capitalization of turnarounds and overhauls under IFRS and a further $0.8 million due to capitalized G&A.

During the second quarter of 2011, Fairborne's development expenditures totaled $24.6 million with capital expenditures financed through funds generated from operations. Land and property acquisitions of $4.1 million during the quarter were primarily focused in the Marlboro and Sinclair areas where $3.5 million was utilized to acquire additional acreage at provincial land sales. In the second quarter of 2011, $1.1 million of general and administrative costs were capitalized to development assets which included $0.9 million of directly attributable G&A costs and $0.2 million of related to stock based compensation costs.

Fairborne spent $8.5 million on drilling and completion activities in the second quarter of 2011 with a total of three (1.5 net) wells drilled resulting in two (0.8 net) natural gas wells on the Company's Marlboro property and one (0.7 net) oil well at Sinclair. Tangible development expenditures of $9.8 million during the three months ended June 30, 2011 included the tie-in of various wells at Sinclair and Marlboro as well as the construction of the Marlboro gas plant.

In the second quarter of 2011, Fairborne completed the disposition of a partial interest in the Marlboro 40 MMcf per day sweet natural gas processing facility. Fairborne sold a 40% working interest in the Marlboro gas plant to a third party midstream company for proceeds of $18.0 million while retaining a 42% working interest, priority access to the divested working interest capacity and operatorship of the facility. With the disposition, Fairborne has committed to a 10 year processing agreement with the midstream company. As a result of this agreement, $6.4 million of the proceeds were allocated to a deferred credit which will be amortized against operating costs on a straight line basis over the term of the processing agreement. For the six months ended June 30, 2011, proceeds from the sale of petroleum and natural gas properties also includes proceeds of $123.5 from the property disposition completed in the first quarter of 2011.

Interim Management's Discussion & Analysis

Capital Expenditures – Intangible Exploration Assets

	THREE MONTHS ENDED JUNE 30,			SIX MONTHS ENDED JUNE 30,	
($thousands)	**2011**	2010		**2011**	2010
		IFRS	GAAP (1)		IFRS
Exploration expenditures					
Land and seismic	**1,177**	2,948	–	**1,177**	5,890
Exploratory drilling and completions	**234**	–	–	**234**	–
Total	**1,411**	2,948	–	**1,411**	5,890

(1) As previously reported under Canadian GAAP.

Additions to E&E assets for the three months ended June 30, 2011 were $1.4 million (Q1 2011 – nil) with $1.2 million incurred for land and seismic and $0.2 million for drilling and completion activities. E&E assets include projects that are pending determination of technical feasibility and economic viability.

Working Capital and Bank Indebtedness

At June 30, 2011, Fairborne had drawn $152.2 million (December 31, 2010 – $206.3 million) against its credit facilities and had working capital surplus of $21.7 million (December 31, 2010 – deficit of $17.7 million), excluding convertible debentures. The working capital surplus was largely attributable to an accounts receivable for proceeds on the sale of a portion of the Company's interest in the Marlboro gas plant. This amount was received immediately after the end of the quarter. Fairborne financed its 2011 second quarter capital expenditure program of $26.0 million from funds generated from operations.

Fairborne's credit facilities at June 30, 2011 included a $310 million extendible revolving term credit facility and a $15 million demand operating credit facility for a total available facility of $325 million. The extendible revolving term facility is available on a revolving basis until May 26, 2012 and, if not renewed at this date, repayment of the amounts drawn will be required on May 26, 2013. The facilities continue to be subject to semi-annual reviews.

Convertible Debentures

At June 30, 2011, Fairborne had Convertible Unsecured Subordinated Debentures (the "Convertible Debentures") outstanding with a face value of $100 million. The Convertible Debentures bear interest at a rate of 6.5% per annum, which is payable semi-annually in arrears on December 31 and June 30 of each year and mature on December 31, 2011. If the Company does not choose to redeem the Convertible Debentures prior to the maturity date, they will be paid at their face of $100 million on December 31, 2011.

Fairborne has adequate liquidity to satisfy the Convertible Debenture obligation when it comes due in December 2011 or earlier if the Company chooses to do so. At current debt levels, the Company has sufficient credit available on its bank facilities to satisfy the payment of Convertible Debentures. In determining the appropriate method for satisfying the debenture obligation, Fairborne will consider a variety of options including: the availability of other sources of debt with different characteristics than the existing bank debt; the sale of assets; limiting the size of the investment program; and new common equity if available on favorable terms.

Shareholders' Equity

The Company is authorized to issue an unlimited number of common shares and an unlimited number of preferred shares, issuable in series.

During the second quarter of 2011, 41,364 common shares were issued on the exercise of stock options.

The following table provides a summary of outstanding common shares, convertible debentures, shares and stock options at the dates indicated:

(thousands)	JULY 31, 2011	JUNE 30, 2011	DECEMBER 31, 2010
Common shares	**102,572**	**102,572**	102,506
Convertible debentures [(1)]	**$100,000**	**$100,000**	$100,000
Stock options	**7,615**	**7,797**	7,024
Weighted average common shares [(2)]			
Basic	**n/a**	**102,538**	102,486
Diluted	**n/a**	**103,623**	103,255

(1) The Convertible Debentures are convertible into common shares at a conversion price of $13.50 per share.
(2) Weighted average common shares outstanding are for the twelve months ended December 31, 2010 and for the six months ended June 30, 2011.

CONTRACTUAL OBLIGATIONS AND COMMITMENTS

During the second quarter of 2011, Fairborne entered into a ten year processing agreement that includes a processing fee commitment of approximately $2.6 million per annum plus operating costs on the facility.

BUSINESS ENVIRONMENT AND RISK

The business risks the Company is exposed to are those inherent in the oil and gas industry as well as those governed by the individual nature of Fairborne's operations. Geological and engineering risks, the uncertainty of discovering commercial quantities of new reserves, commodity prices, interest rate and foreign exchange risks, competition and government regulations – all of these govern the businesses and influence the controls and management at the Company. Fairborne manages these risks by:

- attracting and retaining a team of highly qualified and motivated professionals who have a vested interest in the success of the Company;
- operating properties in order to maximize opportunities;
- employing risk management instruments to minimize exposure to volatility of commodity prices, interest rate and foreign exchange rates;
- maintaining a strong financial position; and
- maintaining strict environmental, safety and health practices.

Interim Management's Discussion & Analysis

CONTROLS AND PROCEDURES

Disclosure Controls and Procedures

Fairborne's Chief Executive Officer and Chief Financial Officer have designed or caused to be designed under their supervision, disclosure controls and procedures to provide reasonable assurance that (i) material information relating to the Company is made known to Fairborne's Chief Executive Officer and Chief Financial Officer by others, particularly during the period in which the annual and interim filings are being prepared; and (ii) information required to be disclosed by the Company in its annual filings, interim filings or other reports filed or submitted by it under securities legislation is recorded, processed, summarized and reported within the time period specified in securities legislation.

Internal Controls over Financial Reporting

Fairborne's Chief Executive Officer and Chief Financial Officer have designed or caused to be designed under their supervision, internal controls over financial reporting to provide reasonable assurance regarding the reliability of the Company's financial reporting and the preparation of financial statements for external purposes in accordance with IFRS.

No material changes in Fairborne's internal controls over financial reporting were identified during the three months ended June 30, 2011, that have materially affected, or are reasonably likely to materially affect, the Company's internal controls over financial reporting.

It should be noted that a control system, including Fairborne's disclosure and internal controls and procedures, no matter how well conceived, can provide only reasonable, but not absolute, assurance that the objectives of the control system will be met and it should not be expected that the disclosure and internal controls and procedures will prevent all errors or fraud.

QUARTERLY FINANCIAL INFORMATION

The following is a summary of select financial information for the quarterly periods indicated:

	2011		2010 (1)	
	Q2	Q1	Q4	Q3
Financial *($thousands, except per share amounts)*				
Petroleum and natural gas revenue	**54,442**	48,531	56,904	54,718
Funds generated from operations	**27,241**	29,833	32,642	32,533
Per share – basic	**$0.27**	$0.29	$0.32	$0.32
Per share – diluted	**$0.26**	$0.29	$0.32	$0.31
Cash flow from operations				
(including changes in working capital)	**24,102**	25,096	39,286	27,311
Per share – basic	**$0.24**	$0.24	$0.38	$0.27
Per share – diluted	**$0.23**	$0.24	$0.38	$0.26
Profit (loss)	**652**	32,650	(8,247)	3,201
Per share – basic	**$0.01**	$0.32	($0.08)	$0.03
Per share – diluted	**$0.01**	$0.31	($0.08)	$0.03
Total assets	**1,052,932**	1,039,135	1,072,064	1,071,759
Working capital deficit (surplus)				
(excluding convertible debentures)	**(21,673)**	47,175	17,743	22,622
Convertible debentures	**98,706**	98,135	97,564	97,058
Bank indebtedness	**152,227**	101,774	206,331	194,042
Operations				
Average production				
Natural gas *(Mcf per day)*	**65,171**	63,550	71,845	68,910
Crude oil *(bbls per day)*	**2,287**	2,710	2,946	2,916
Natural gas liquids *(bbls per day)*	**766**	1,020	1,028	1,036
Sulphur *(tonnes per day)* (2)	**56**	67	62	66
Total *(BOE per day)*	**13,971**	14,388	16,010	15,503

(1) Restated using IFRS.
(2) Excludes the sale of inventory at the West Pembina sulphur block.

Interim Management's Discussion & Analysis

	2010 (1)		2009 (2)	
	Q2	Q1	Q4	Q3
Financial *($thousands, except per share amounts)*				
Petroleum and natural gas revenue	59,633	63,382	58,338	55,244
Funds generated from operations	32,261	42,756	37,863	37,236
Per share – basic	$0.31	$0.42	$0.37	$0.43
Per share – diluted	$0.31	$0.41	$0.37	$0.43
Cash flow from operations (including changes in working capital)	26,273	44,544	38,750	40,048
Per share – basic	$0.26	$0.43	$0.38	$0.46
Per share – diluted	$0.26	$0.43	$0.38	$0.46
Profit (loss)	2,361	11,085	(3,124)	(497)
Per share – basic	$0.02	$0.11	$(0.02)	$(0.01)
Per share – diluted	$0.02	$0.11	$(0.02)	$(0.01)
Total assets	973,304	985,353	940,443	961,920
Working capital deficit (surplus)	6,487	34,741	6,370	(1,539)
Convertible debentures	96,508	95,958	96,510	96,027
Bank indebtedness	123,081	102,536	103,738	204,046
Operations				
Average production				
Natural gas (Mcf per day)	66,812	60,878	59,132	56,797
Crude oil (bbls per day)	3,110	3,000	3,037	3,292
Natural gas liquids (bbls per day)	1,149	686	617	563
Sulphur (tonnes per day) (3)	92	54	33	100
Total (BOE per day)	15,486	13,886	13,542	13,421

(1) *Restated using IFRS*
(2) *As previously reported under Canadian GAAP.*
(3) *Excludes the sale of inventory at the West Pembina sulphur block.*

Interim Consolidated Financial Statements

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

(unaudited)

(thousands of Canadian dollars)	**JUNE 30, 2011**	DECEMBER 31, 2010
Assets		
Current assets		
Cash and cash equivalents	**$ 478**	$ 319
Accounts receivable	**50,925**	31,825
Prepaid expenses and deposits	**5,645**	5,813
Total current assets	**57,048**	37,957
Petroleum and natural gas properties and equipment *(Note 3)*	**978,741**	1,012,015
Intangible exploration assets *(Note 4)*	**17,143**	15,732
Goodwill *(Note 5)*	**–**	6,360
Total capital assets	**995,884**	1,034,107
	$ 1,052,932	$ 1,072,064
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities	**$ 34,804**	$ 54,333
Derivative liability *(Note 14)*	**571**	1,367
Convertible debentures *(Note 7)*	**98,706**	97,564
Total current liabilities	**134,081**	153,264
Bank indebtedness *(Note 6)*	**152,227**	206,331
Provisions *(Note 8)*	**17,424**	12,730
Deferred taxes	**115,490**	101,232
Total non-current liabilities	**285,141**	320,293
Total liabilities	**419,222**	473,557
Equity		
Common shares	**537,001**	536,812
Equity portion of convertible debentures *(Note 7)*	**2,964**	2,964
Contributed surplus	**33,700**	31,988
Retained earnings	**60,045**	26,743
Total equity	**633,710**	598,507
Commitments *(Note 15)*		
	$ 1,052,932	$ 1,072,064

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

Interim Consolidated Financial Statements

CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME

(unaudited)

	FOR THE THREE MONTHS ENDED JUNE 30,		FOR THE SIX MONTHS ENDED JUNE 30,	
	2011	2010	**2011**	2010
(thousands of Canadian dollars except per share amounts)				
Revenue				
Petroleum and natural gas	**$ 54,442**	$ 59,633	**$ 102,973**	$ 123,015
Royalties	**(8,014)**	(8,686)	**(11,880)**	(14,220)
	46,428	50,947	**91,093**	108,795
Expenses				
Production and operating	**12,640**	14,546	**26,148**	26,635
General and administrative	**4,243**	4,685	**8,437**	7,394
Depreciation and amortization *(Note 3)*	**23,491**	25,200	**47,088**	47,927
Results from operating activities	**6,054**	6,516	**9,420**	26,839
Gain (loss) on disposition of capital assets	**(411)**	1,096	**47,684**	1,237
Finance expense *(Note 12)*	**(4,460)**	(4,017)	**(9,544)**	(7,802)
Profit before taxes	**1,183**	3,595	**47,560**	20,274
Deferred taxes	**531**	1,234	**14,258**	6,828
Profit and comprehensive income	**$ 652**	$ 2,361	**$ 33,302**	$ 13,446
Profit per share *(Note 9)*				
Basic	**$ 0.01**	$ 0.02	**$ 0.33**	$ 0.13
Diluted	**$ 0.01**	$ 0.02	**$ 0.32**	$ 0.13

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

Interim Consolidated Financial Statements

CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

(unaudited)

	2011		2010	
FOR THE SIX MONTHS ENDED JUNE 30,	**Number**	**Amount**	Number	Amount
(thousands of Canadian dollars)	***(thousands)***		*(thousands)*	
Common shares				
Balance, beginning of period	**102,506**	**$ 536,812**	102,462	$ 536,532
Issued on exercise of stock options	**66**	**189**	12	38
Issued on vesting of Restricted Units and Performance Units	**–**	**–**	15	140
Balance, end of period	**102,572**	**$ 537,001**	102,489	$ 536,710
Warrants				
Balance, beginning of period	**–**	**$ –**	4,406	$ 1,620
Expired	**–**	**–**	(4,406)	(1,620)
Balance, end of period	**–**	**$ –**	–	$ –
Equity portion of convertible debentures *(Note 7)*				
Balance, beginning and end of period		**$ 2,964**		$ 2,964
Contributed surplus				
Balance, beginning of period		**$ 31,988**		$ 24,827
Equity based compensation *(Note 10)*		**1,859**		3,310
Stock options exercised		**(147)**		(28)
Warrants expired		**–**		1,620
Balance, end of period		**$ 33,700**		$ 29,729
Retained earnings				
Balance, beginning of period		**$ 26,743**		$ 18,343
Profit		**33,302**		13,446
Balance, end of period		**$ 60,045**		$ 31,789
Total equity				
Balance, end of period		**$ 633,710**		$ 601,192

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

Interim Consolidated Financial Statements

CONSOLIDATED STATEMENTS OF CASH FLOWS

(unaudited)

FOR THE SIX MONTHS ENDED JUNE 30,	2011	2010
(thousands of Canadian dollars)		
Operating activities		
Profit	$ 33,302	$ 13,446
Adjustments for:		
Depreciation and amortization *(Note 3)*	47,088	47,927
Deferred taxes	14,258	6,828
Change in fair values of derivatives *(Note 14)*	(796)	(455)
Finance expense (including accretion) *(Note 12)*	9,544	7,802
Gain on disposition of capital assets	(47,684)	(1,237)
Stock based compensation *(Note 10)*	1,362	706
Funds generated from operations	57,074	75,017
Change in non-cash working capital *(Note 11)*	(7,743)	(3,794)
Asset retirement expenditures *(Note 8)*	(133)	(406)
Net cash from (used in) operating activities	49,198	70,817
Financing activities		
Bank indebtedness	(54,104)	19,343
Issuance of common shares	42	10
Interest paid	(7,582)	(5,787)
Net cash from (used in) financing activities	(61,644)	13,566
Investing activities		
Expenditures on petroleum and natural gas properties *(Note 3)*	(96,284)	(82,818)
Expenditures on exploration assets *(Note 4)*	(1,411)	(5,890)
Proceeds from sale of petroleum and natural gas properties	141,380	–
Change in non-cash working capital *(Note 11)*	(31,080)	4,434
Net cash from (used in) investing activities	12,605	(84,274)
Change in cash and cash equivalents	159	109
Cash and cash equivalents, beginning of period	319	147
Cash and cash equivalents, end of period	$ 478	$ 256

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

SELECTED NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

FOR THE SIX MONTHS ENDED JUNE 30, 2011 (UNAUDITED)

(tabular amounts are stated in thousands and thousands of Canadian dollars except per share amounts)

NATURE OF OPERATIONS

Fairborne Energy Ltd. (the "Company" or "Fairborne") is a resource-based company engaged in the exploration for and the development and production of natural gas, natural gas liquids and crude oil in Western Canada. The Company is incorporated under the laws of the Province of Alberta and is domiciled in Canada, with its principal place of business located at 3400, 450 – 1st Street SW Calgary, Alberta.

These consolidated financial statements as at and for the period ended June 30, 2011 and 2010 comprise the Company and its wholly owned subsidiaries. The Company has the following significant wholly owned subsidiaries, incorporated or formed, as applicable, in Canada: Case Sub Ltd. and Fairborne Pivotal Production Partnership.

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

1. BASIS OF PRESENTATION

These consolidated financial statements have been prepared by management in accordance with International Financial Reporting Standards ("IFRS") which was adopted in Canada on January 1, 2011. In these financial statements, the term "Canadian GAAP" refers to Canadian GAAP before the adoption of IFRS.

These interim consolidated financial statements have been prepared in accordance with IFRS applicable to the preparation of interim financial statements, including IAS 34 and IFRS 1. Subject to certain transition elections disclosed in Note 2, the Company has consistently applied the same accounting policies throughout all periods presented, as if these policies had always been in effect. These financial statements should be read in conjunction with the consolidated financial statements and notes thereto for the year ended December 31, 2010 as well as the significant accounting policies under IFRS as discussed in note 1 to the interim consolidated financial statements for the three months ended March 31, 2011. Note 2 discloses the impact of the transition to IFRS on the Company's reported financial position, financial performance and cash flows, including the nature and effect of significant changes in accounting policies from those used in the Company's consolidated financial statements for the three and six months ended June 30, 2010. Comparative figures for 2010 in these financial statements have been restated to give effect to these changes.

The policies applied in these interim consolidated financial statements are based on IFRS issued and outstanding when the Board of Directors approved the statements. Any subsequent changes to IFRS that are given effect in the Company's annual consolidated financial statements for the year ending December 31, 2011 could result in restatement of these interim consolidated financial statements, including the transition adjustments recognized on change-over to IFRS. The consolidated financial statements were authorized by the Board of Directors on August 3, 2011.

Interim Consolidated Financial Statements

2. CHANGES IN ACCOUNTING POLICIES AND PRACTICES

Initial Adoption of IFRS

Effective January 1, 2010 the Company adopted IFRS. The following tables reconcile previously reported amounts to adjusted IFRS amounts.

STATEMENT OF OPERATIONS FOR THE SIX MONTHS ENDED JUNE 30, 2010

	NOTES	CANADIAN GAAP (ADJUSTED FOR IFRS PRESENTATION)	EFFECT OF TRANSITION TO IFRS	IFRS
(thousands of Canadian dollars except per share amounts)				
Revenue				
Petroleum and natural gas		$ 123,015	–	$ 123,015
Royalties		(14,220)	–	(14,220)
		108,795	–	108,795
Expenses				
Production and operating	*h*	27,653	(1,018)	26,635
General and administrative	*b,d*	10,410	(3,016)	7,394
Depreciation and amortization	*a,e,h*	65,714	(17,787)	47,927
Results from operating activities		5,018	21,821	26,839
Gain on disposition of capital assets	*f*	–	1,237	1,237
Finance expense	*c,e*	(7,668)	(134)	(7,802)
Profit (loss) before taxes		(2,650)	22,924	20,274
Deferred taxes	*g,i*	662	6,166	6,828
Profit and comprehensive income (loss)		$ (3,312)	16,758	$ 13,446
Profit (loss) per share				
Basic		$ (0.03)	$ 0.16	$ 0.13
Diluted		$ (0.03)	$ 0.16	$ 0.13

Interim Consolidated Financial Statements

STATEMENT OF OPERATIONS FOR THE THREE MONTHS ENDED JUNE 30, 2010

(thousands of Canadian dollars except per share amounts)	NOTES	CANADIAN GAAP (ADJUSTED FOR IFRS PRESENTATION)	EFFECT OF TRANSITION TO IFRS	IFRS
Revenue				
Petroleum and natural gas		$ 59,633	–	$ 59,633
Royalties		(8,686)	–	(8,686)
		50,947	–	50,947
Expenses				
Production and operating	*h*	15,337	(791)	14,546
General and administrative	*b,d*	5,797	(1,112)	4,685
Depreciation and amortization	*a,e,h*	34,810	(9,610)	25,200
Results from operating activities		(4,997)	11,513	6,516
Gain on disposition of capital assets	*f*	–	1,096	1,096
Finance expense	*c,e*	(3,947)	(70)	(4,017)
Profit (loss) before taxes		(8,944)	12,539	3,595
Deferred taxes (reduction)	*g, i*	(1,823)	3,057	1,234
Profit and comprehensive income (loss)		$ (7,121)	9,482	$ 2,361
Profit (loss) per share				
Basic		$ (0.07)	$ 0.09	$ 0.02
Diluted		$ (0.07)	$ 0.09	$ 0.02

TOTAL EQUITY AS AT JUNE 30, 2010

(thousands of Canadian dollars)	NOTES	CANADIAN GAAP	EFFECT OF TRANSITION TO IFRS	IFRS
Common shares	*i*	531,919	4,791	536,710
Equity component of convertible debentures	*c*	5,581	(2,617)	2,964
Contributed surplus	*j*	30,830	(1,101)	29,729
		568,330	1,073	569,403
Retained earnings, opening	*b,c,g,i,j*	19,407	(1,064)	18,343
Profit and comprehensive income for the six months ended June 30, 2010		(3,312)	16,758	13,446
Retained earnings, closing		16,095	15,694	31,789
Total equity		584,425	16,767	601,192

Interim Consolidated Financial Statements

NOTES:

a) **DEPRECIATION AND AMORTIZATION –** Under Canadian GAAP, the full cost pool was depleted as one unit on a unit of production basis over proved reserves. Under IFRS, the Company depletes petroleum and natural gas interests at an individual component (i.e. area) level on a unit of production basis over proved plus probable reserves. For the six months ended June 30, 2010 the impact was a decrease of $18.2 million in depreciation and amortization expense. For the three months ended June 30, 2010, this change in policy resulted in a decrease in depreciation and amortization expense of $9.8 million.

b) **SHARE BASED PAYMENTS –** Under Canadian GAAP, share based payments accounted for on a liability basis (Restricted and Performance Units and Retention Awards) were measured at their intrinsic values. Under IFRS they are measured at their fair values. At June 30, 2010, this resulted in a decrease to opening retained earnings (January 1, 2010) of $1.1 million. For the six months ended June 30, 2010, this change in policy resulted in a decrease in general and administrative expenses of $1.2 million and had an insignificant impact for the three months ended June 30, 2010.

c) **CONVERTIBLE DEBENTURES –** Under Canadian GAAP, convertible debentures were initially allocated to equity and liability components based on the relative fair values of the components on the date of issue. Under IFRS, the convertible debentures are also allocated to equity and liability components; however, this allocation was determined using the relative fair values of the components on December 19, 2007 when Fairborne converted from a trust to a corporation. At June 30, 2010, this resulted in a decrease in the equity component of convertible debentures of $2.6 million and an increase in opening retained earnings (January 1, 2010) of $2.7 million. For the six months ended June 30, 2010, this resulted in an increase to finance expense of $0.1 million. For the three months ended June 30, 2010, this also resulted in an increase in finance expenses of $0.1 million.

d) **CAPITALIZED GENERAL AND ADMINISTRATION EXPENSE –** Under Canadian GAAP, directly attributable general and administration costs were capitalized to petroleum and natural gas properties and equipment. Under IFRS, directly attributable general and administration costs are capitalized to intangible exploration assets and petroleum and natural gas properties and equipment, however the makeup of directly attributable general and administration costs varies. For the year six months ended June 30, 2010, this change in policy resulted in decrease in general and administrative expenses of $1.8 million. For the three months ended June 30, 2010, this change in policy resulted in a decrease in general and administrative expenses of $1.1 million.

e) **ACCRETION –** Under IFRS accretion is included in finance expense where under Canadian GAAP it was included in depletion and depreciation.

f) **NON-MONETARY TRANSACTIONS –** Under Canadian GAAP, non-monetary transactions including farm-outs, pooling of interests and asset swaps did not result in the recognition of gains or losses from disposition. Under IFRS, gains and losses on the disposal of an item of petroleum and natural gas properties and equipment, including oil and natural gas interests, are determined by comparing the proceeds from disposal with the carrying amount of petroleum and natural gas properties and equipment and are recognized net in profit or loss. For the six months ended June 30, 2010, this change in policy resulted in a gain on disposition of capital assets of $1.2 million. For the three months ended June 30, 2010, this change in policy resulted in a gain on disposition of capital assets of $1.1 million.

g) **DEFERRED TAXES –** For the six months ended June 30, 2010 the tax impact of IFRS adjustments resulted in an increase in deferred tax expense of $6.2 million. For the three months ended June 30, 2010, the impact was an increase in deferred tax expense of $3.1 million. The treatment of tax rate changes also differs under Canadian GAAP and IFRS. Under Canadian GAAP, when income tax rates change the impact is recorded through tax expense. Under IFRS, if the initial taxes were recorded through equity the adjustment is also recorded through equity. At June 30, 2010, the impact is a increase of $0.3 million to opening retained earnings (January 1, 2010).

h) **TURNAROUNDS AND OVERHAULS –** Under Canadian GAAP, turnarounds and overhauls were included in operating expenses; however under IFRS these expenditures are capitalized as a separate component of petroleum and natural gas properties and equipment and are depreciated over their estimated useful lives. For the six months ended June 30, 2010, the impact of this change was a decrease in production and operating expenses of $1.0 million and an increase in depreciation and amortization of $0.4 million. For the three months ended June 30, 2010, the impact of this change is a decrease in production and operating expenses of $0.8 million and an increase in depreciation and amortization of $0.2 million.

i) **FLOW THROUGH SHARES –** Under Canadian GAAP, share capital was recorded at net proceeds less the deferred tax liability related to the renounced expenditures. Under IFRS, the increase to share capital when flow-through shares are issued is measured based on the current market price of common shares. The incremental proceeds, or “premium” is recorded as a deferred charge. When expenditures are incurred a deferred tax liability is recognized and the deferred charge is reversed. The net amount is recognized as deferred tax expense. At June 30, 2010, this resulted in an increase in share capital of $4.8 million and a $4.1 million decrease to opening retained earnings (January 1, 2010). For the three and six months ended June 30, 2010, the impact is an increase to deferred tax expense of $0.1 million and $0.4 million, respectively.

j) **WARRANTS –** Under Canadian GAAP, warrants were recorded at fair value on the date of issue. Under IFRS the warrants are recorded at fair value on the date when Fairborne converted to a corporation. The warrants expired unexercised in June 2010 and the outstanding amount was reclassified to contributed surplus. The impact of this at June 30, 2010 was a decrease to contributed surplus of $1.1 million and a corresponding increase to opening retained earnings (January 1, 2010).

Interim Consolidated Financial Statements

3. PETROLEUM AND NATURAL GAS PROPERTIES AND EQUIPMENT

Resource Properties and Equipment

	FOR THE SIX MONTHS ENDED JUNE 30, 2011	FOR THE YEAR ENDED DECEMBER 31, 2010
Cost		
Balance, beginning of period	$ 1,109,728	$ 873,586
Additions	100,955	170,092
Acquired in business combinations	–	72,677
Dispositions	(103,004)	(6,627)
Balance, end of period	$ 1,107,679	$ 1,109,728
Accumulated depreciation and impairment losses		
Balance, beginning of period	$ (99,519)	$ –
Depreciation	(46,964)	(99,665)
Disposals	15,545	146
Balance, end of period	$ (130,938)	$ (99,519)
Net book value, end of period	$ 976,741	$ 1,010,209

Corporate Assets

	FOR THE SIX MONTHS ENDED JUNE 30, 2011	FOR THE YEAR ENDED DECEMBER 31, 2010
Cost		
Balance, beginning of period	$ 4,600	$ 4,307
Additions	318	293
Balance, end of period	$ 4,918	$ 4,600
Accumulated depreciation and impairment losses		
Balance, beginning of period	$ (2,794)	$ (2,408)
Depreciation	(124)	(386)
Balance, end of period	$ (2,918)	$ (2,794)
Net book value, end of period	$ 2,000	$ 1,806

	JUNE 30, 2011	DECEMBER 31, 2010
Petroleum and natural gas properties and equipment – cost	$ 1,112,597	$ 1,114,328
Petroleum and natural gas properties and equipment – accumulated depreciation	(133,856)	(102,313)
Petroleum and natural gas properties and equipment – net book value	$ 978,741	$ 1,012,015

4. INTANGIBLE EXPLORATION ASSETS

Evaluation and Exploration Assets

	FOR THE SIX MONTHS ENDED JUNE 30, 2011	FOR THE YEAR ENDED DECEMBER 31, 2010
Cost		
Balance, beginning of period	$ 15,732	$ 5,407
Additions	1,411	10,325
Balance, end of period	$ 17,143	$ 15,732

5. GOODWILL

	FOR THE SIX MONTHS ENDED JUNE 30, 2011	FOR THE YEAR ENDED DECEMBER 31, 2010
Cost		
Balance, beginning of period	$ 6,360	$ 16,170
Disposal through property sale	(6,360)	–
Impairment loss	–	(9,810)
Balance, end of period	$ –	$ 6,360

The impairment of goodwill is recognized as amortization expense in the statement of operations and will not be reversed.

6. BANK INDEBTEDNESS

At June 30, 2011 the Company had a $310 million extendible revolving term credit facility and a $15 million demand operating credit facility available from a syndicate of Canadian chartered banks, subject to the banks' semi-annual valuation of Fairborne's petroleum and natural gas properties. The extendible revolving term facility is available on a revolving basis until May 26, 2012 (364 day facility) at which time it may be extended, at the lenders option. If the revolving period is not extended, the undrawn portion of the facility will be cancelled and the amount outstanding will convert to a 365 day non-revolving term facility. The amounts outstanding under the non-revolving term facility are required to be repaid at the end of the term facility being May 26, 2013. Interest payable on amounts drawn under the facilities is at the prevailing bankers' acceptance rates plus stamping fees, lenders' prime rate or LIBOR rates plus applicable margins, depending on the form of borrowing by the Company. The margins and stamping fees vary from 0.50% to 3.75% depending on financial statement ratios and the form of borrowing. The credit facilities are secured by a general security agreement and a first ranking floating charge on the assets of the Company. At June 30, 2011 letters of credit totaling $2.1 million were outstanding.

Interim Consolidated Financial Statements

7. CONVERTIBLE DEBENTURES

	NUMBER OF DEBENTURES	DEBT COMPONENT	EQUITY COMPONENT
Balance, January 1, 2010	100,000	$ 95,409	$ 2,964
Accretion	–	2,155	–
Balance, December 31, 2010	100,000	97,564	2,964
Accretion	–	1,142	–
Balance June 30, 2011	**100,000**	**$ 98,706**	**$ 2,964**

At June 30, 2011 the Company had 100,000 convertible unsecured subordinated debentures outstanding with a face value of $100 million that mature on December 31, 2011. The debentures bear interest at a rate of 6.5% per annum, which is payable semi-annually in arrears on December 31 and June 30 of each year. The debentures can be converted into common shares of Fairborne at any time at the option of the holders at a conversion price of $13.50 per share. The debentures are redeemable in whole or in part, prior to the maturity date, at the option of the Company at a redemption price of $1,025 plus accrued and unpaid interest.

8. PROVISIONS

A reconciliation of provisions is provided below:

	FOR THE SIX MONTHS ENDED JUNE 30, 2011	FOR THE YEAR ENDED DECEMBER 31, 2010
Asset retirement obligation, beginning of period	**$ 12,730**	$ 11,200
Acquired in business combination	**–**	1,262
Provisions made during the period	**619**	711
Provisions used during the period	**(133)**	(1,491)
Disposals	**(2,555)**	(81)
Accretion	**458**	1,129
Asset retirement obligation, end of period	**11,119**	12,730
Other provisions	**6,305**	–
Balance, end of period	**$ 17,424**	$ 12,730

9. PROFIT PER SHARE

The following table summarizes the weighted average common shares used in calculating profit per share:

	THREE MONTHS ENDED JUNE 30,		SIX MONTHS ENDED JUNE 30,	
	2011	2010	**2011**	2010
Numerator				
Profit for the period – basic & diluted	**$ 652**	$ 2,361	**$ 33,302**	$ 13,446
Denominator				
Weighted average shares – basic	**102,568**	102,483	**102,538**	102,474
Stock options	**962**	804	**1,085**	804
Denominator for diluted profit per share	**103,530**	103,287	**103,623**	103,278
Basic profit per share	**$ 0.01**	$ 0.02	**$ 0.33**	$ 0.13
Diluted profit per share	**$ 0.01**	$ 0.02	**$ 0.32**	$ 0.13

Excluded from the diluted number of shares for the six month period ended June 30, 2011 is the effect of convertible debentures (7.4 million shares) and 1.2 million stock options as their effect is anti-dilutive. Excluded from the diluted number of shares for the six month period ended June 30, 2010 is the effect of convertible debentures (7.4 million shares) and 3.5 million stock options.

10. EQUITY BASED COMPENSATION

Stock based compensation expense of $1.9 million (June 30, 2010 – $2.1 million) was recognized in the period, all of which (June 30, 2010 – $3.3 million) was related to awards accounted for as equity settled transactions. Of this amount, stock based compensation costs of $0.5 million (June 30, 2010 – $1.0 million) were capitalized during the period.

i. Stock option plan

The following table sets forth a reconciliation of the stock option plan activity:

	FOR THE SIX MONTHS ENDED JUNE 30, 2011		FOR THE YEAR ENDED DECEMBER 31, 2010	
	NUMBER OF OPTIONS	**WEIGHTED AVERAGE EXERCISE PRICE**	NUMBER OF OPTIONS	WEIGHTED AVERAGE EXERCISE PRICE
Balance, beginning of period	**7,024**	**$ 4.24**	5,235	$ 4.25
Granted	**1,066**	**5.33**	2,200	4.20
Exercised	**(138)**	**3.02**	(97)	3.49
Forfeited	**(155)**	**4.42**	(314)	4.31
Balance, end of period	**7,797**	**$ 4.07**	7,024	$ 4.24
Exercisable, end of period	**3,641**	**$ 4.34**	1,713	$ 4.59

Interim Consolidated Financial Statements

The fair value of options granted in the period was estimated using the Black-Scholes option pricing model. The weighted average assumptions used in the valuation model were as follows:

	FOR THE SIX MONTHS ENDED JUNE 30, 2011	FOR THE YEAR ENDED DECEMBER 31, 2010
Fair value at grant date	$ 2.09	$ 1.68
Share price	$ 5.33	$ 4.20
Exercise price	$ 5.33	$ 4.20
Risk free interest rate	1.9%	1.6%
Expected volatility	55%	64%
Average expected life	3 years	3 years
Dividend rate	Nil	Nil

An estimated forfeiture rate of two percent (2010 – two percent) has been applied to the compensation costs recognized. This estimate is adjusted to the actual forfeiture rate.

The weighted average share price for options exercised during the period at the date of exercise was $4.61 (December 31, 2010 – $4.41). The expected volatility was determined using historical volatility for a period commensurate with the option life.

The following table summarizes stock options outstanding at June 30, 2011:

EXERCISE PRICE	OPTIONS OUTSTANDING	REMAINING TERM (YEARS)
$ 2.00 – $ 4.99	6,649	3.37
$ 5.00 – $ 7.99	1,015	4.66
$ 8.00 – $ 10.99	58	2.25
$ 11.00 – $ 13.99	75	2.06
	7,797	3.52

ii. Retention Award Plan

The following table sets forth a reconciliation of the retention award plan activity:

	FOR THE SIX MONTHS ENDED JUNE 30, 2011		FOR THE YEAR ENDED DECEMBER 31, 2010	
	NUMBER OF AWARDS	WEIGHTED AVERAGE EXERCISE PRICE	NUMBER OF AWARDS	WEIGHTED AVERAGE EXERCISE PRICE
Balance, beginning of period	60	$ 5.52	1,390	$ 5.74
Forfeited	–	–	(870)	5.75
Cancelled	(60)	5.52	(460)	5.75
Balance, end of period	–	$ –	60	$ 5.52
Exercisable, end of period	–	$ –	40	$ 5.52

11. SUPPLEMENTAL CASH FLOW INFORMATION:

The following table sets forth the changes in non-cash working capital:

FOR THE SIX MONTHS ENDED JUNE 30,	2011	2010
Change in receivables	$ (19,100)	$ 8,371
Change prepaid expenses and deposits	168	2,189
Change in accounts payable and accrued liabilities	(19,891)	(5,635)
Change in deferred revenue	–	(4,285)
	$ (38,823)	$ 640
Operating	$ (7,743)	$ (3,794)
Investing	$ (31,080)	$ 4,434

12. FINANCE EXPENSE

	THREE MONTHS ENDED JUNE 30,		SIX MONTHS ENDED JUNE 30,	
	2011	2010	2011	2010
Interest on bank indebtedness	$ 2,031	$ 1,601	$ 4,577	$ 2,969
Interest on convertible debentures	1,625	1,625	3,250	3,250
Accretion of convertible debentures	571	550	1,142	1,100
Accretion of asset retirement obligation	233	241	458	483
Impairment loss on trade receivables	–	–	117	–
Finance expenses recognized in profit and loss	$ 4,460	$ 4,017	$ 9,544	$ 7,802

13. FINANCIAL INSTRUMENTS

The carrying value of Fairborne's financial instruments, other than bank indebtedness and convertible debentures, approximate their fair value due to their short maturity. The fair value of the bank indebtedness approximates its carrying value as it bears interest at a floating rate. The fair value of the convertible debentures at June 30, 2011 was $100.2 million (December 31, 2010 – $102.5 million).

Interim Consolidated Financial Statements

14. COMMODITY CONTRACTS

Fairborne has a risk management program whereby the Company sells forward a portion of its future production through fixed price sales contracts with customers.

a) Commodity Contracts Recorded at Fair Value:

At June 30, 2011, certain contracts have been recorded on the statement of financial position at their estimated fair value as a $0.6 million liability (December 31, 2010 – $1.4 million). The change in the fair value has been recorded in petroleum and natural gas revenue.

OIL:

	VOLUME (bbls PER DAY)	PRICE (CDN$ PER bbl)	SETTLEMENT INDEX
Collars			
July 1, 2011 – Dec 31, 2011	500	70.00 – 101.25	WTI
Swaps			
July 1, 2011 – Dec 31, 2011	500	75.00	WTI

NATURAL GAS:

	VOLUME (GJs PER DAY)	PRICE (CDN$ PER GJ)	SETTLEMENT INDEX
AECO Swap			
July 1, 2011 – Dec 31, 2011	5,000	5.16	AECO C Monthly

b) Commodity Contracts not Recorded at Fair Value:

The following contracts outstanding at June 30, 2011 have been entered into for the purpose of physical delivery of a non-financial item; therefore, the physical delivery contracts are not fair valued. Settlements on these contracts are included in petroleum and natural gas revenue as they occur.

NATURAL GAS:

	VOLUME (GJs PER DAY)	PRICE (CDN$ PER GJ)	SETTLEMENT INDEX
Swaps			
July 1, 2011 – Dec 31, 2011	5,000	5.00	AECO C Monthly
July 1, 2011 – Dec 31, 2011	5,000	5.00	AECO C Monthly

15. COMMITMENTS

During the quarter, Fairborne entered into a ten year processing agreement that includes a processing fee commitment of approximately $2.6 million per annum plus operating costs on the facility.

Corporate Information

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AUDITORS

KPMG LLP

RESERVE EVALUATORS

GLJ Petroleum Consultants Ltd.

BANKERS

Royal Bank of Canada
National Bank of Canada
Canadian Imperial Bank of Commerce
Alberta Treasury Branch
Union Bank

LEGAL COUNSEL

Burnet, Duckworth & Palmer LLP
McCarthy Tetrault LLP

STOCK EXCHANGE LISTING

The Toronto Stock Exchange

Trading Symbol: **FEL**
Convertible Debentures: **FEL.DB**

CORPORATE GOVERNANCE

A system of corporate governance for Fairborne has been established to provide the Board of Directors, management and shareholders of the Company with effective governance. A more detailed discussion of corporate governance is available in the Information Circular for the Annual Meeting of Shareholders.

DIRECTORS

Greg Bay
President and CEO
Cypress Capital Management Ltd.

Robert B. Hodgins
Investor and Corporate Director

Johannes J. Nieuwenburg
General Partner
KERN Partners Ltd.

Carl J. Tricoli
Founder and Managing Partner
Denham Capital Management LP

Steven R. VanSickle
President and CEO
Fairborne Energy Ltd.

Richard A. Walls
President and
Chief Executive Officer
C & C Energia Ltd.

Rodney D. Wimer
President
Mazama Capital Partners

GENERAL INFORMATION

Shareholders and interested investors are encouraged to visit our web site: *http://www.fairborne-energy.com* Historical public documents, corporate information, latest presentation material and press releases are all available. Filings also available at: www.sedar.com

OFFICERS

Steven R. VanSickle
President
and Chief Executive Officer

David L. Summers
Chief Operating Officer

Aaron G. Grandberg
Chief Financial Officer

Jackie M. Cugnet
Vice President
Finance

David S. Cymbalisty
Vice President
Engineering

Scott W. Hadley
Vice President
Exploration

F. Tom Park
Vice President
Marketing

Gary M. Poirier
Vice President
Production

David E.T. Pyke
Vice President
Land and Contracts