



Q1 2007

Three months ended
March 31, 2007

Company Definition

Throughout this interim report, Terra Energy Corp. is referred to as “Terra Energy”, the “Company” or the “Corporation”.

Volume Definition Reporting

For the purposes of calculating unit costs, natural gas has been converted to a barrel of oil equivalent (“boe”) using six thousand cubic feet equal to one barrel of oil unless otherwise stated. This conversion conforms to Canadian Securities Regulators National Instrument 51-101 – Standards of Disclosure for Oil and Gas Activities. Please note that the term, boe, may be misleading, particularly if used in isolation. A boe conversion ration of six thousand cubic feet per barrel is based on an energy equivalency method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead.

Directors

Ted S. Anderson (1)(2)

Ralph G. Evans(3)(4)

Tony Sabelli(1)(3)

Colin MacDonald(2)

Cas H. Morel(2)(3)(4)

Robert D. Penner(1)(2)

1. Member of the Audit Committee
2. Member of the Corporate Governance, Compensation and Nominating Committee
3. Member of the Engineering Reserves Committee
4. Member of the Safety and Environment Committee

Officers

Tim Beatty

Vice President, Capital Projects

John Behr

Vice President, Exploration

Timothy Blair

Vice President, Land

Jan Campbell

Corporate Secretary

Bud Love

Vice President, Finance and Chief Financial Officer

Rosa Lyngberg

Controller

Cas Morel

President and Chief Executive Officer

Terra Energy Corp.

**Management's Discussion & Analysis
for the three months ended March 31, 2007**

This Management's Discussion and Analysis ("MD&A") of financial condition and results of operations of Terra Energy Corp. ("Terra Energy Corp." or the "Corporation") is dated May 28, 2007. It should be read in conjunction with the unaudited interim consolidated financial statements and corresponding notes for the three month periods ended March 31, 2007 and March 31, 2006 and with the audited year end consolidated financial statements of the Corporation for the years ended December 31, 2006 and December 31, 2005.

Terra Energy's Board of Directors and Audit Committee have reviewed and approved the March 31, 2007 interim consolidated financial statements and related MD&A.

All references to dollar values refer to Canadian dollars unless otherwise stated.

This MD&A provides certain financial measures that do not have a standardized meaning prescribed by Canadian generally accepted accounting principles ("GAAP"). These non-GAAP financial measures may not be comparable to similar measures presented by other issuers.

This MD&A contains the terms "cash flow from operations" and "cash flow from operations per share", which should not be considered an alternative to, or more meaningful than, cash flow from operating activities as determined in accordance with Canadian generally accepted accounting principles as an indicator of the Corporation's performance. Cash flow from operations per share is calculated using the same weighted average basic and diluted number of shares outstanding used in the calculation of net income (loss) per share. All references to cash flow throughout this MD&A are based on cash flow before changes in non-cash working capital.

Petroleum and natural gas volumes are converted to an equivalent measurement basis referred to as a "barrel of oil equivalent" ("boe") using a conversion rate of six thousand cubic feet of natural gas to one barrel of oil ("6:1"). The 6:1 conversion ratio is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead. Readers are cautioned that boe figures may be misleading, particularly if used in isolation.

The continuous disclosure materials of the Corporation, including its annual MD&A and audited financial statements, Information Circular and Proxy Statement, material change reports and press releases issued by the Corporation are available through the SEDAR system at www.sedar.com.

FORWARD LOOKING ADVISORY

Statements in this document may contain forward-looking information. Such information is subject to known and unknown risks, uncertainties and other factors that could influence actual results or events, and cause actual results or events to differ materially from those stated, anticipated or implied in the forward looking information. As such, readers are cautioned not to place undue reliance on the forward-looking information, as no assurances can be provided as to future results, levels of activity or achievements. In addition, the reader is cautioned that historical results are not necessarily indicative of future performance.

DISCLOSURE CONTROLS AND PROCEDURES

Disclosure controls and procedures are designed to provide reasonable assurance that information required to be disclosed is recorded, processed, summarized and reported with the time periods specified by securities regulations and that information required to be disclosed is accumulated and communicated to management.

The Chief Executive Officer and Chief Financial Officer have evaluated the effectiveness of the Corporation's disclosure controls and procedures as of March 31, 2007 and have concluded that they are adequate and effective to ensure accurate and complete disclosure.

DESIGN OF INTERNAL CONTROLS OVER FINANCIAL REPORTING

Effective for the year end 2006, securities regulations state that the Corporation is to design and implement internal controls over financial reporting and disclose in its MD&A any material changes in the Corporation's internal control over financial reporting that occurred during the Corporation's most recent interim period. Internal controls are processes designed and implemented by management to provide reasonable assurance regarding the reliability the Corporation's financial reporting and the preparation of financial statements and other financial information for external purposes in accordance with Canadian GAAP. For the quarter ended March 31, 2007, the Chief Executive Officer and the Chief Financial Officer have designed internal controls over financial reporting, or caused them to be designed under their supervision. Management has concluded that internal controls are adequately designed in this regard, considering the employees involved and the control procedures in place, including management and Audit Committee oversight and quarterly external auditor reviews. Occasionally, the Corporation requires outside assistance and advice on taxation, new accounting pronouncements and complex accounting and reporting issues, which is common with companies of a similar size. It should be noted, that the Corporation's control system, no matter how well designed, can provide only reasonable, but not absolute, assurance of detecting, preventing and deterring errors or fraud.

CORPORATE HISTORY

Terra Energy is a publicly traded corporation, amalgamated under the Business Corporations Act of Alberta, and formed as a result of the amalgamation of Terra Energy Corp., Terrapet Energy Corp., and Rhodes Resources Corp. on January 30, 2004. This Management Discussion and Analysis along with the associated financial statements referenced above include the accounts of the Corporation and its wholly-owned subsidiary Constar Resources Ltd. and Terra Energy, a general partnership between Terra Energy Corp. and Constar Resources Ltd.

The Corporation's principal business is the exploration, development and production of petroleum and natural gas in Western Canada.

SELECTED QUARTERLY INFORMATION

Financial

<i>Three months ended March 31</i>	2007	2006	% Growth
Gross Revenue	\$10,384,124	\$11,189,502	(7.2%)
Cash Flow From Operations	\$3,449,145	\$5,068,870	(32.0%)
Earnings	(\$2,168,418)	(\$230,410)	n/a
Dividends	Nil	Nil	n/a
Weighted Average Shares – Basic	75,822,011	70,376,376	7.7%
Weighted Average Shares – Diluted	75,822,011	72,551,972	4.5%
Shares at Quarter End – Basic	75,203,284	71,433,708	5.3%

	March 31, 2007	December 31, 2006	% Growth
Total Assets	\$150,747,884	\$147,561,394	2.2%
Long-term Financing	\$47,116,795	\$35,478,837	32.8%

Operational

<i>Three months ended March 31</i>	2007	2006	% Growth
Production			
Average Daily Production (boe/d)	2,476	2,486	(0.4%)
Wells Drilled			
Gross	1.0	6.0	(83.3%)
Net	1.0	5.04	(80.2%)

RESULTS OF OPERATIONS

Production

<i>Three months ended March 31</i>	2007	2006	% Growth
	Average	Average	
Oil (bbl/d)	311	353	(11.9%)
Natural Gas (mcf/d)	10,278	10,902	(5.7%)
Liquids (bbl/d)	452	316	43.0%
Combined (boe/d)	2,476	2,486	(0.4%)

Operations

<i>Three months ended March 31</i>	2007	2006	2007	2006	% Growth
			(\$ / boe)	(\$ / boe)	(\$ / boe)
Gross Revenues	\$10,384,124	\$11,189,502	\$46.60	\$50.01	(6.8%)
Realized Gain on Financial Instrument	\$309,093	\$275,513	\$1.39	\$1.23	12.6%
Unrealized Gain (Loss) on Financial Instrument	(\$2,846,646)	\$322,535	(\$12.77)	\$1.44	n/a
Revenue Before Royalties	\$7,846,571	\$11,787,550	\$35.21	\$52.68	(33.2%)
Royalties	\$2,222,705	\$2,363,529	\$9.97	\$10.56	(5.6%)
Revenue After Royalties	\$5,623,866	\$9,424,021	\$25.24	\$42.12	(40.1%)
Production Expenses	\$3,120,330	\$3,023,642	\$14.00	\$13.51	3.6%
Operating Netback	\$2,503,536	\$6,400,379	\$11.23	\$28.61	(60.7%)
General & Administrative Expenses	\$1,249,055	\$1,129,064	\$5.61	\$5.05	11.1%
Interest Expense	\$635,376	\$418,314	\$2.85	\$1.87	52.5%
Realized Foreign Exchange (Gain)	-	(\$48,498)	-	(\$0.22)	n/a
Non-cash Expenses	\$3,803,882	\$4,448,678	\$17.07	\$19.88	(14.1%)
Income (Loss) Before Income Taxes	(\$3,184,777)	\$452,821	(\$14.29)	\$2.02	n/a
Income Tax Expense (Recovery)	(\$1,016,359)	\$683,231	(\$4.56)	\$3.05	n/a
Net Income (Loss)	(\$2,168,418)	(\$230,410)	(\$9.73)	(\$1.03)	n/a
Per Share – Basic	(\$0.03)	(\$0.00)			
Per Share - Diluted	(\$0.03)	(\$0.00)			

Revenue

<i>Three months ended March 31</i>	2007	2006	2007	2006	% Change
			(\$ / boe)	(\$ / boe)	(\$ / boe)
Gross Revenue	\$10,384,124	\$11,189,502	\$46.60	\$50.01	(6.8%)
Realized Gain on Financial Instrument	309,093	275,513	\$1.39	\$1.23	12.6%
Unrealized Gain (Loss) on Financial Instrument	(2,846,646)	322,535	(\$12.77)	\$1.44	n/a
Revenue Before Royalties	\$7,846,571	\$11,787,550	\$35.21	\$52.68	(33.2%)

Gross revenues decreased 7.2% to \$10,384,124 for the three month period ended March 31, 2007 compared to \$11,189,502 for the same period ended March 31, 2006. Terra Energy realized an all in price per unit of production for the three month period ended March 31, 2007 of \$46.60, down 6.8% compared to the realized price per unit of production of \$50.01 per boe for the same period ended March 31, 2006. A slight decrease in production (0.4%) and a decrease in the realized price for natural gas liquids resulted in the reduction in gross revenues on an aggregate and on a per unit of production basis.

Below is a breakdown of gross revenue prices realized by the Corporation for the three month period ended March 31, 2007:

Gross Revenue:

<i>Three Months Ended March 31</i>	2007	2006	% Change
Crude Oil (\$ / bbl)	\$66.38	\$65.46	1.4%
Natural Gas Liquids (\$ / bbl)	\$36.00	\$53.89	(33.2%)
Natural Gas (\$ / mcf)	\$7.62	\$7.58	0.5%

At period ends, in accordance with generally accepted accounting principles, the Corporation is required to calculate and reflect a "mark-to-market" value of its financial instruments. At December 31, 2006 this calculation resulted in a \$1,800,000 unrealized gain on financial instruments.

Further, during each period, the prior periods "unrealized gains" or losses are reversed and a new mark to market adjustment is calculated as at the period end. At March 31, 2007, as a result of rising forward commodity prices, the "mark-to-market" adjustment resulted in an unrealized loss of \$1,000,000. This current period unrealized loss coupled with the reversal of the December 31, 2006 \$1,800,000 unrealized gain results in Terra Energy recording an unrealized loss on financial instruments of \$2,846,646 for the quarter ended March 31, 2007. These unrealized losses are non cash items and as a result, do not affect Terra Energy's cash flow from operations. Subsequent to the end of the first quarter Terra Energy crystallized most of its natural gas commodity financial hedges resulting in an expected realized gain of \$300,000 in calendar 2007. See "Off- Balance Sheet Arrangements" for further details.

Further, during the first quarter of 2007 the Company recognized a realized gain of \$309,093 on financial instruments crystallized for crude oil and natural gas financial contracts for the three month period ended March 31, 2007.

Revenue before royalties (after realized and unrealized gains on financial instruments) decreased 33.4% to \$7,846,571 for the three month period ended March 31, 2007 compared to \$11,787,550 for the same period ended March 31, 2006. The reduction in net revenue was a due to a combination of realized and unrealized losses on financial instruments.

Factors affecting Terra Energy's realized prices include:

- Late in 2006 and in early 2007, Terra Energy entered into several financial natural gas transactions for approximately 50% of current production at prices averaging \$7.50 / mcf. For the period ended March 31, 2007, Terra Energy actually realized a cash gain of \$206,872 on its natural gas financial transactions.
- In 2006, Terra Energy "crystallized" several financial crude oil contracts relating to 2007 volumes. As a result of the transactions, Terra Energy realized a cash gain of \$102,221 during the quarter relating to crude oil contracts.

Royalties

Three months ended March 31	2007	2006	2007	2006	% Change
			(\$ / boe)	(\$ / boe)	(\$ / boe)
Royalties	\$2,222,705	\$2,363,529	\$9.97	\$10.56	(5.6%)

Royalties decreased 6.0% to \$2,222,705 for the three month period ended March 31, 2007 compared to \$2,363,529 for the same period ended March 31, 2006. Royalties on a per unit of production basis fell 5.6% to \$9.97 for the three month period ended March 31, 2007 compared to \$10.56 per boe for the same period ended March 31, 2006.

Royalties fell in aggregate and on a per unit of production basis as result of lower production volumes (0.4%) and a lower realized price per unit of production (6.8%). The effective royalty rate rose slightly to 21.4% for the three month period ended March 31, 2007 from 21.1% for the same period ended March 31, 2006.

Production Expenses

Three months ended March 31	2007	2006	2007	2006	% Change
			(\$ / boe)	(\$ / boe)	(\$ / boe)
Production Expenses	\$3,120,330	\$3,023,642	\$14.00	\$13.51	3.6%

Production expenses rose 3.2% to \$3,120,330 for the three month period ended March 31, 2007 compared to \$3,023,642 for the same period ended March 31, 2006. Production expenses on a per unit of production basis rose 3.6% to \$14.00 for the three month period ended March 31, 2007 compared to \$13.51 for the same period ended March 31, 2006.

Production expenses rose slightly as a result of a general increase in the cost of services and an unusually heavy snow fall in the winter of 2007. The expenses rose due to snow removal and power shortages caused by winter storms. The Sextet area of northern British Columbia experienced unusually high operating costs. The increase in production expenses on a per unit of production basis was caused by a small reduction in production (0.4%) coupled with a 3.2% increase in aggregate production expenses.

Production expenses fell 13.7% from the previous quarter and 7.5% on a per unit of production basis. As additional production volumes are added in subsequent quarters, Terra Energy estimates the trend of falling production expenses on a per unit of production basis to continue.

General and Administrative Expenses

Three months ended March 31	2007	2006	2007	2006	% Change
			(\$ / boe)	(\$ / boe)	(\$ / boe)
General & Administrative Expenses	\$1,249,055	\$1,129,064	\$5.61	\$5.05	11.1%

General & administrative expenses increased 10.6% to \$1,249,055 for the three month period ended March 31, 2007 compared to \$1,129,064 for the same period ended March 31, 2006. General & administrative expenses on a per unit of production basis rose 11.1% to \$5.61 for the three month period ended March 31, 2007 compared to \$5.05 for the same period ended March 31, 2006. General & administrative expenses increased as a result of higher legal, insurance and salaries costs during the quarter. General & administrative expenses on a per unit of production basis rose as a result of the higher expenditures and slightly lower production volumes.

Interest Expense

Three months ended March 31	2007	2006	2007	2006	% Change
			(\$ / boe)	(\$ / boe)	(\$ / boe)
Interest Expenses	\$635,376	\$418,314	\$2.85	\$1.87	52.5%

Interest expenses increased 51.9% to \$635,376 for the three month period ended March 31, 2007 compared to \$418,314 for the same period ended March 31, 2006. On a per unit of production basis interest expenses increased 52.5% to \$2.85 for the three month period ended March 31, 2007 compared to \$1.87 for the same period ended March 31, 2006.

Interest expenses increased as a result of higher indebtedness required during the quarter to finance the Corporation's capital expenditures program and an increase in interest rates payable on the Corporation's outstanding bank indebtedness.

Non Cash Expenses

Three months ended March 31	2007	2006	2007	2006	% Growth
			(\$ / boe)	(\$ / boe)	(\$ / boe)
Depletion and Amortization	\$3,375,514	\$3,174,836	\$15.15	\$14.19	6.7%
Accretion Expense	111,517	105,500	\$0.50	\$0.47	6.5%
Stock Based Compensation	316,851	1,393,309	\$1.42	\$6.23	(77.2%)
Unrealized Foreign Exchange Gain	-	(224,967)	-	(\$1.01)	n/a
Total Non Cash Items	\$3,803,882	\$4,448,678	\$17.07	\$19.88	(14.1%)

Non cash expenses fell 14.5% to \$3,803,882 for the three month period ended March 31, 2007 compared to \$4,448,678 for the same period ended March 31, 2006. On a per unit of production basis, non cash expenses decreased 14.1% to \$17.07 for the three month period ended March 31, 2007 compared to \$19.88 for the same period ended March 31, 2006.

Depletion and amortization expense increased 6.3% to \$3,375,514 as a result of the larger depletable asset base from Terra Energy's 2006 and 2007 capital expenditures programs and the readjustment of depletion and amortization based on the external engineering report prepared as at December 31, 2006.

Stock based compensation fell 77.2% as a result of the issuance of 48,000 new stock options during the three month period ended March 31, 2007 (less than 1% of issued and outstanding stock options) compared to 1,786,000 options issued during the three month period ended March 31, 2006. The majority of the stock based compensation for the three month period ended March 31, 2007 related to the repricing of 2,107,000 stock options held by employees of the Corporation during the quarter as previously disclosed by the Corporation on January 31, 2007.

Income Taxes

Three months ended March 31	2007	2006	2007	2006	% Change
			(\$ / boe)	(\$ / boe)	(\$ / boe)
Current Tax	-	\$10,574	-	\$0.04	n/a
Future Tax	(\$1,016,359)	\$672,657	(\$4.56)	\$3.01	n/a
Total Income Taxes (Recovery)	(\$1,016,359)	\$683,231	(\$4.56)	\$3.05	n/a

Income taxes fell to recovery of \$1,016,359 for the three month period ended March 31, 2007 compared to an expense of \$683,231 for the same period ended March 31, 2006. On a per unit of production basis, income taxes decreased to a recovery of \$4.56 for the three month period ended March 31, 2007 compared to an expense of \$3.05 for the same period ended March 31, 2006.

The recovery of income taxes relates to flow through expenditures the Corporation has incurred as at March 31, 2007.

With approximately \$124 million available in tax pools at March 31, 2007, the Corporation does not expect to incur any material cash taxes in 2007.

LIQUIDITY AND FINANCIAL CONDITION

	March 31, 2007	December 31, 2006
Working Capital	(\$8,298,388)	(\$10,331,676)
Oil and Gas Properties	\$143,688,867	\$138,704,967

The working capital deficit at March 31, 2007 was \$8,298,388 compared to a deficit of \$10,331,676 at December 31, 2006. Terra Energy's working capital deficit was affected by the reclassification of non-cash items, specifically the decrease in current assets by approximately \$1,841,861 and the increase in current liabilities to \$1,004,786 relating to the mark to market adjustments to financial instruments. This reclassification was due to the mark to market adjustment of outstanding commodity financial hedges during the quarter.

Terra Energy's bank credit facility is structured as a \$55.0mm 364 day revolving credit facility with a one year term-out. If the credit facility is not renewed at maturity, the Corporation has the ability to repay any amounts outstanding on the credit facility one year from maturity. As a result of this one year repayment feature, Terra Energy has classified its bank credit facility as a long-term financial obligation. As at March 31, 2007, Terra Energy was in compliance with all of its bank covenants.

Capitalized resource properties as at March 31, 2007 were \$143,688,867 net of accumulated depletion, compared to \$138,704,967 as at December 31, 2006. Oil and gas properties increased as a result of continued developments of oil and gas properties as well as the acquisition of undeveloped Crown land. For the three month period ended March 31, 2007 Terra Energy incurred \$8,702,014 in net capital expenditures broken down as:

<i>Three Months Ended March 31</i>	2007	2006
Exploration	\$2,126,157	\$2,362,482
Development	\$1,050,264	\$9,532,468
Undeveloped Land	\$185,149	\$3,053,218
Geological / Geotechnical	\$803,121	\$400,434
Facilities	\$4,140,671	\$6,748,064
Other Assets	\$131,652	\$271,323
Total Capital Expenditures	\$8,437,014	\$22,367,989
Net Property Acquisitions	-	-
Total Capital Expenditures	\$8,437,014	\$22,367,989

Terra Energy incurred net capital expenditures of \$8,437,014 for the three month period ended March 31, 2007. Terra Energy drilled 1 gross (1.0 net) wells during the period. Terra Energy commenced construction of the 17 km Tower / Septimus pipeline, connecting the Corporation's Tower field to its Wilder natural gas facility.

Terra Energy financed its capital expenditures for the period through a combination of bank debt and cash flow.

Cash Flow

For the three month period ended March 31, 2007, the Corporation generated cash flows from operations of \$3,449,145 (\$0.05 per basic / diluted share), a decrease of 32.0% compared to \$5,068,870 (\$0.07 per basic share) for the three month period ended March 31, 2006.

Cash flow from operations ("Cash Flow"), representing cash generated from operating activities before changes in non-cash working capital items, is a non-GAAP measure. Management utilizes Cash Flow as a key measure to assess the ability of the Corporation to finance operating activities and capital expenditures. Additionally, Cash Flow has been described and presented in order to provide shareholders and potential investors with information regarding the Corporation's liquidity and its ability to generate funds to finance its operations. This performance indicator may not be comparable to similar measures used by other companies.

The following table presents the non-GAAP financial measure "cash flow from operations".

<i>Three months ended March 31</i>	2007	2006
Net Income (Loss) For The Period	(\$2,168,418)	(\$230,410)
Future Income Tax Provision	(1,016,359)	672,657
Accretion Expense	111,517	105,500
Stock Based Compensation	316,851	1,393,309
Unrealized Gain On Financial Instruments	2,846,646	(322,535)
Realized Loss On Financial Instruments	-	275,513
Amortization Of Deferred Credit	(16,606)	-
Depletion And Amortization	3,375,514	3,174,836
Cash Flow From Operations	\$3,449,145	\$5,068,870

Capital Resources

The Corporation's share capital is as follows:

	March 31, 2007		<i>December 31, 2006</i>	
	No. of Shares	Amounts	<i>No. of Shares</i>	<i>Amounts</i>
Common Shares	75,203,284	\$65,866,977	76,900,833	\$72,570,457

During the three month period ended March 31, 2007 1,697,549 common shares were repurchased by the Corporation for \$1,767,071 at an average price of \$1.04 per common share. The Corporation recorded \$1,595,696 as a reduction of share capital and the excess of \$171,375 being charged to deficit. As at March 31, 2007 3,675,749 repurchased shares are held for cancellation. Shares repurchased under the NCIB are excluded from the outstanding number of shares.

COMMITMENTS AND CONTINGENCIES

The Corporation had outstanding letters of credit to various parties for a total of \$345,000 (2006- \$395,000). The amounts expire at various dates during 2007.

The Corporation is required to incur exploration and development activities by December 31, 2007 of approximately \$15,713,000 as a result of flow-through shares issued in November 2006. At March 31, 2007, the Corporation has incurred qualifying expenditures of approximately \$4,748,464 towards this obligation.

OFF-BALANCE SHEET ARRANGEMENTS

The Corporation is party to certain derivative instruments, including crude oil and natural gas contracts. The Corporation enters into these contracts to manage commodity price risk in future earnings and cash flow. These contracts reduce the Corporation's exposure to the fluctuations in petroleum and natural gas revenues by locking in fixed forward prices on a portion of the Corporation's crude oil and natural gas production.

At March 31, 2007 the Corporation had entered into commodity contracts, the terms of which are summarized as follows:

Contract Type	Floor Price	Ceiling Price	Volumes Per Day	Contract Term
Financial	Sell \$86.00 per Bbl	N/A	200 Bbls	June 1, 2006 to May 31, 2007
Financial	Buy \$80.65 per Bbl	N/A	200 Bbls	June 1, 2006 to May 31, 2007
Financial	Sell US\$77.25 per Bbl	N/A	100 Bbls	January 1, 2007 to December 31, 2007
Financial	Buy US\$76.40 per Bbl	N/A	100 Bbls	January 1, 2007 to December 31, 2007
Financial	Sell \$7.50 per GJ	N/A	1,000 GJ	November 1, 2006 to October 31, 2007
Financial	Sell \$6.50 per GJ	\$8.92 per GJ	1,000 GJ	November 1, 2006 to October 31, 2007
Financial	Sell \$7.50 per GJ	N/A	1,500 GJ	December 1, 2006 to December 31, 2007
Financial	Sell \$7.65 per GJ	N/A	1,000 GJ	December 1, 2006 to October 31, 2007
Financial	Sell \$7.75 per GJ	N/A	1,000 GJ	January 1, 2007 to December 31, 2007
Financial	Sell \$6.65 per GJ	N/A	2,000 GJ	March 1, 2007 to March 31, 2007

Contract Type	Floor Price	Ceiling Price	Volumes Per Day	Contract Term
Financial	Buy \$7.22 per Gj	N/A	5,500 Gj	April 1, 2007 to April 30, 2007
Financial	Buy \$7.05 per Gj	N/A	2,000 Gj	April 1, 2007 to April 30, 2007
Financial	Buy \$6.95 per Gj	N/A	2,000 Gj	April 1, 2007 to April 30, 2007
Financial	Buy \$7.41 per Gj	N/A	3,000 Gj	May 1, 2007 to December 31, 2007
Financial	Sell \$7.40 per Gj	N/A	2,000 Gj	March 1, 2007 to July 31, 2007
Financial	Sell \$6.53 per Gj	N/A	1,000 Gj	April 1, 2007 to October 31, 2007
Financial	Sell \$8.05 per Gj	N/A	1,000 Gj	November 1, 2007 to March 31, 2008
Financial	Sell \$7.45 per Gj	N/A	1,000 Gj	April 1, 2007 to March 31, 2008
Financial	Sell \$8.00 per Gj	\$8.60 per Gj	1,000 Gj	November 1, 2007 to March 31, 2008
Financial	Sell \$7.10 per Gj	N/A	1,000 Gj	April 1, 2007 to October 31, 2007
Financial	Sell \$8.00 per Gj	N/A	2,000 Gj	November 1, 2007 to December 31, 2007
Financial	Sell \$7.95 per Gj	N/A	1,000 Gj	April 1, 2007 to March 31, 2008
Financial	Sell \$8.05 per Gj	N/A	1,000 Gj	December 1, 2007 to December 31, 2007
Financial	Sell \$8.20 per Gj	\$9.21 per Gj	1,000 Gj	November 1, 2007 to March 31, 2008
Financial	Sell \$8.25 per Gj	\$9.40 per Gj	1,000 Gj	November 1, 2007 to March 31, 2008
Financial	Sell \$8.50 per Gj	\$9.00 per Gj	1,000 Gj	November 1, 2007 to March 31, 2008

The mark to market value of the above commodity products transactions of \$1,004,786 has been recorded as a liability as at March 31, 2007.

Below is a summary of commodity products transactions Terra Energy entered into subsequent to March 31, 2007 to offset existing financial commodity contracts resulting in the crystallization of gains on the contracts:

Contract Type	Floor Price	Ceiling Price	Volumes Per Day	Contract Term
Financial	Buy \$7.24 per Gj	N/A	1,000 Gj	May 1, 2007 to May 31, 2007
Financial	Buy \$7.23 per Gj	N/A	3,000 Gj	May 1, 2007 to May 31, 2007
Financial	Buy \$7.25 per Gj	N/A	2,000 Gj	May 1, 2007 to May 31, 2007
Financial	Buy \$7.30 per Gj	N/A	1,500 Gj	May 1, 2007 to May 31, 2007
Financial	Buy \$7.19 per Gj	N/A	2,000 Gj	June 1, 2007 to June 30, 2007
Financial	Buy \$7.14 per Gj	N/A	2,000 Gj	June 1, 2007 to June 30, 2007
Financial	Buy \$7.40 per Gj	N/A	1,500 Gj	June 1, 2007 to November 30, 2007
Financial	Buy \$7.48 per Gj	N/A	1,000 Gj	June 1, 2007 to December 30, 2007
Financial	Buy \$7.45 per Gj	N/A	1,000 Gj	June 1, 2007 to December 30, 2007
Financial	Buy \$7.35 per Gj	N/A	1,000 Gj	July 1, 2007 to November 30, 2007
Financial	Buy \$8.00 per Gj	\$8.60 per Gj	1,000 Gj	November 1, 2007 to March 31, 2008
Financial	Buy \$8.20 per Gj	\$9.21 per Gj	1,000 Gj	November 1, 2007 to March 31, 2008
Financial	Buy \$8.25 per Gj	\$9.40 per Gj	1,000 Gj	November 1, 2007 to March 31, 2008
Financial	Buy \$8.50 per Gj	\$9.00 per Gj	1,000 Gj	November 1, 2007 to March 31, 2008

RELATED PARTY TRANSACTIONS

The Corporation entered into transactions with the following related parties:
Pioneer Land Services Ltd. – a Director is an employee of Pioneer
Borden Ladner Gervais LLP – a Director is partner with the law firm
Fasken Martineau DuMoulin LLP – the Corporate Secretary is partner with the law firm

	March 31, 2007	March 31, 2006
Expenses		
Consulting - Pioneer Land Services Ltd.	\$209	\$4,859
Legal Consulting - Borden Ladner Gervais LLP	\$154,648	\$53,520
Joint Venture revenues and expenses - Rhodes Petroleum Corp., of which \$17,875 is included in accounts receivable in 2006	-	-
	\$154,857	\$58,379
Other		
Recorded as part of Oil and Gas Properties - Pioneer Land Services Ltd	\$5,685	\$22,440
Recorded as part of share issuance cost – Borden Ladner Gervais LLP	\$3,084	-
	\$8,769	\$22,440

OUTLOOK

The Corporation produced an average of 2,476 boe/d during the first quarter of 2007. On May 2, 2007 the Company announced the completion of the Tower-Septimus pipeline project. Two wells were tied-in through the pipeline increasing production by approximately 500 boe/d. An upgrading of Terra Energy's Wilder facility, expected to be completed in June, is anticipated to increase production above 3,000 boe/d.

Terra Energy is moving forward on its previously announced infrastructure projects. These projects will be instrumental in bringing Terra Energy's "behind pipe" production onstream. These projects include the Corporation's East Boudreau pipeline, Peace River crossing and its Eight Mile pipeline.

Construction of the Corporation's Tower-Septimus pipeline segment was completed on April 30, 2007. This pipeline segment is approximately 19 kilometres long and connects at its western end to the Corporation's existing Septimus – Wilder pipeline, creating one continuous 6" high pressure gas gathering line which is approximately 36 kilometres in length.

The Corporation submitted its East Boudreau pipeline project to the British Columbia Oil and Gas Commission in early March 2007. The East Boudreau pipeline is a combination of 4 inch and 6 inch diameter pipe, stretching approximately 19.5 kilometres from the Corporation's East Boudreau gas field to its Red Creek gas plant. The cost of the East Boudreau pipeline has been estimated at \$5 million. Subject to receiving the requisite approvals, construction work will commence following spring break-up. Upon completion, the Corporation anticipates incremental production of approximately 3 mmcf/d (500 boe/d).

During the quarter, an industry partner announced plans to construct the Peace River crossing to the McMahon plant, with an expected completion date late in the fourth quarter of 2007. Terra Energy has entered into an agreement with a midstream company for the transportation and processing of 10 mmcf/d of gas on a firm basis and up to 10 mmcf/d on an interruptible basis, for transportation and processing Terra Energy's natural gas reserves located south of the Peace River. Upon the completion of the Peace River Crossing, Terra Energy's remaining "behind pipe" gas reserves in the Tower gas field will be brought onstream. Terra Energy will also be in a position to almost immediately tie-in any new reserves which may prove up south of the Peace River. .

The Corporation has entered into agreements with a midstreamer, whereby the Corporation has committed a total of 3.25 mmcf/d (525 boe/d) of natural gas production from its Eight Mile field for a period of 3 years in exchange for the development by the midstreamer of a new gas processing facility and a connecting gas pipeline. Start up of the new processing plant is anticipated to occur in the third quarter of 2007, and Terra Energy is proceeding with plans to develop field gathering and compression facilities at Eight Mile in order to coincide with the facilities being developed by the midstreamer.

CHANGES IN ACCOUNTING POLICIES

On January 1, 2007, the corporation adopted the Canadian Institute of Chartered Accountants (“CICA”) Handbook Section 1530 “Comprehensive Income”, Section 3855 “Financial Instruments – Recognition and Measurement” Section 3865 “Hedges” and Section 3251 “Equity”. The Corporation has adopted these standards retrospectively and the comparatives interim financial statements have not been restated.

Comprehensive Income

The new standards introduce comprehensive income, which consists of net earnings and other comprehensive income (“OCI”). The Corporation’s Consolidated Financial Statements now include a Consolidated Statement of Loss, Comprehensive Loss and Deficit. The cumulative changes in OCI are included in accumulated other comprehensive income (“AOCI”), which is presented as a new category within shareholder’s equity in the Consolidated Balance Sheet.

Financial Instruments

The financial instruments standard establishes the recognition and measurement criteria for financial assets, financial liabilities and derivatives. All financial instruments are required to be measured at fair value on initial recognition of the instrument, except for certain related party transactions. Measurement in subsequent periods depends on whether the financial instrument has been classified as “held-for-trading”, “available-for-sale”, “held-to-maturity”, “loans and receivables”, or “other financial liabilities” as defined by the standard.

Financial assets and financial liabilities “held-for-trading” are measured at fair value with changes in those fair values recognized in net earnings. Financial assets “available-for-sale” are measured at fair value, with changes in those fair values recognized in OCI. Financial assets “held-to-maturity”, “loans and receivables” and “other financial liabilities” are measured at amortized cost using the effective interest method of amortization. The methods used by the Corporation in determining fair value of financial instruments are unchanged as a result of implementing the new standard.

Cash and cash equivalents are designated as “held-for-trading” and are measured at carrying value, which approximates fair value due to the short-term nature of these instruments. Accounts receivable is designated as “loans and receivables”. Accounts payable and accrued liabilities, bank overdraft and long-term financing are designated as “other liabilities”. Risk management assets and liabilities are derivative financial instruments classified as “held-for-trading” unless designated for hedge accounting.

Section 1506 – Accounting Changes

The Corporation also adopted Section 1506 – Accounting Changes the only impact of which is to provide disclosure of when an entity has not applied a new source of GAAP that has been issued but is not yet effective. This is the case with Section 3862 – Financial Instruments Disclosures and Section 3863 Financial Instruments Presentations which are required to be adopted for fiscal years beginning on or after October 1, 2007. This section also prescribes disclosures for voluntary changes and sets requirements for disclosures for the reasons of these changes. The Corporation will adopt these standards on January 1, 2008 and it is expected the only effect on the Corporation will be incremental disclosures regarding the significance of financial instruments for the entity’s financial position and performance; and the nature, extent and management of risks arising from financial instruments to which the entity is exposed.

CRITICAL ACCOUNTING ESTIMATES

In preparing financial statements in accordance with generally accepted accounting principles, management undertakes certain judgments and estimates. Changes in these judgments and estimates could have a material impact on the financial results and condition. The following discussion outlines accounting policies and practices that are critical to determining the Corporation's financial results.

Proved Oil and Gas Reserves

Under Canadian Securities Regulations National Instrument 51-101 "Standards of Disclosure for Oil and Gas Activities" (NI 51-101), "proved" reserves are those reserves that can be estimated with a high degree of certainty to be recoverable (it is likely that the actual remaining quantities recovered will exceed the estimated proved reserves). In accordance with this definition, the level of certainty targeted by the reporting company should result in at least a 90% probability that the quantities actually recovered will equal or exceed the estimated reserves. There was no such consideration of probability under National Policy 2B (NP 2B). In the case of "probable" reserves, which are obviously less certain to be recovered than proved reserves, NI 51-101 states that it must be equally likely that the actual remaining quantities recovered will be greater or less than the sum of the estimated proved plus probable reserves. With respect to the consideration of certainty, in order to report reserves as proved plus probable, the reporting company must believe that there is at least a 50% probability that the quantities actually recovered will equal or exceed the sum of the estimated proved plus probable reserves. The implementation of NI 51-101 has resulted in a more rigorous and uniform standardization of reserve evaluation.

The oil and gas reserve estimates are made using all available geological, reservoir and historical production data. Estimates are reviewed and revised as appropriate. Revisions may occur as a result of changes in prices, costs, fiscal regimes, reservoir performance or a change in the Corporation's plans.

Ceiling Test

Under the Canadian Institute of Chartered Accountants (CICA) full cost accounting guidelines, the Corporation calculates a ceiling test annually whereby the carrying value of petroleum and natural gas properties is compared to estimated future cash flow from the production of proved reserves. The Corporation has early adopted the requirement of CICA Accounting Guideline 16 "Oil and Gas Accounting - Full Cost" ("AcG 16"). The requirements of the guideline were to be followed for all fiscal years beginning on or after January 1, 2004. At March 31, 2007, the Corporation calculated the ceiling test using AcG 16 without any material adverse impact on the Corporation's financial position or results of operations.

Asset Retirement Obligation

CICA Handbook Section 3110 "Asset Retirement Obligations" requires accrued reclamation and abandonment obligations be recognized on the balance sheet by increasing oil and gas properties offset by a liability of an equal amount. Estimates are required to determine the future obligation. The asset and liability are initially measured at fair value, being the discounted future value of the liability, and then capitalized as part of the cost of the asset and subsequently amortized over the life of the asset. The liability then accretes until the retirement obligation is settled.

Litigation

The Corporation is involved in various claims and litigation arising from the normal course of business. While the outcome of these matters is uncertain and there can be no assurance that such matters will be resolved in the Corporation's favor, the Corporation does not currently believe that the outcome of adverse decisions in any pending or threatened proceeding related to these and other matters or any amount which it may be required to pay by reason thereof, would have a material adverse effect on its financial position or results of operations.

Depletion and Depreciation Expense

Terra Energy uses the full cost method of accounting for exploration and development activities whereby all costs associated with these activities are capitalized, whether successful or not. The aggregate of capitalized costs, net of certain costs related to unproved properties, and estimated future development costs is amortized using the unit-of-production method based on estimated proved reserves. Changes in estimated proved reserves or future development costs have a direct impact on depletion and depreciation expense. Certain costs related to unproved properties and major development projects may be excluded from costs subject to depletion until proved reserves have been assigned, at which point they would be included in the depletion calculation, or for impairment, for which any write-down would be charged to depletion and depreciation expense.

Stock Based Compensation and Share Purchase Warrants

The Corporation calculates the fair value of the options granted and share purchase warrants issued. This calculation is based on estimates which could differ significantly from actual results. This could have a significant impact on the financial statements.

Income Taxes

The determination of Terra Energy's income and other tax liabilities requires interpretation of complex laws and regulations often involving multiple jurisdictions. All tax filings are subject to audit and potential reassessment after the lapse of considerable time. Accordingly, the actual income tax liability may differ significantly from that estimated and recorded.

Financial Instruments

The Corporation's results are impacted by external market risks associated with fluctuations in commodity prices, operational and safety and environmental risks. The Corporation partially mitigates its exposure to market risks through the use of various financial instruments and physical contracts. The Corporation does not utilize derivative instruments for speculative purposes.

RISK FACTORS RELATING TO OIL AND GAS EXPLORATION, DEVELOPMENT AND PRODUCTION

Uncertain Discovery of Viable Commercial Prospects

The Corporation's future success may be dependent upon its ability to economically locate commercially viable oil or gas deposits. The Corporation can make no representations, warranties or guaranties that it will be able to consistently identify viable prospects, or that such prospects will be commercially exploitable. An inability of the Corporation to consistently identify and exploit commercially viable hydrocarbon deposits would have a material and adverse effect on the Corporation's business and financial position. Exploratory drilling is subject to numerous risks, including the risk that no commercially productive oil and gas reservoirs will be encountered. The cost of drilling, completing and operating wells is often uncertain, and drilling operations may be curtailed, delayed or canceled as a result of a variety of factors, including unexpected formation and drilling conditions, pressure or other irregularities in formations, blowouts, equipment failures or accidents, as well as weather conditions, compliance with governmental requirements and/or shortages or delays in the delivery of equipment. The inability to successfully locate and drill wells that will economically produce commercial quantities of oil and gas could have a material adverse effect on the Corporation's business and financial position. The Corporation's properties are in various stages of exploration and development. Whether the Corporation ultimately drills a property may depend on a number of factors including funding, the receipt of additional seismic data or reprocessing of existing data, material changes in oil or gas prices, the costs and availability of drilling equipment, success or failure of wells drilled in similar formations or which would use the same production facilities, changes in estimates of costs to drill or complete wells, the Corporation's ability to attract industry partners to acquire a portion of its working interest to reduce exposure to drilling and completion costs, decisions of the Corporation's joint working interest owners, and/or restrictions under provincial regulators.

Volatility of Oil and Natural Gas Contracts

The ultimate profitability, cash flow and future growth of the Corporation will be affected by changes in prevailing oil and gas prices. Oil and gas prices have been subject to wide fluctuations in recent years in response to changes in the supply and demand for oil and natural gas, market uncertainty, competition, regulatory developments and other factors which are beyond the control of the Corporation. It is impossible to predict future oil and natural gas price movements with any certainty. An extended or substantial decline in oil and gas prices would have a material adverse effect on (i) the Corporation's access to capital, and (ii) the Corporation's financial position and results of operations.

Increased Operating Costs

Higher operating costs for our underlying properties will directly decrease the amount of cash flow received by the Corporation. Electricity, chemicals, supplies, reclamation and abandonment, and labour costs are a few of the operating costs that are susceptible to material fluctuation.

Title of Assets

Although the Corporation conducts title reviews in accordance with industry practice prior to any purchase of resource assets, such reviews do not guarantee that an unforeseen defect in the chain on title will not arise and defeat our title to the purchased assets. If such a defect were to occur, our entitlement to the production from such purchased assets could be jeopardized.

Uncertainty of Estimates of Reserves and Future Events

Certain statements included in this report contain estimates of the Corporation's oil and gas reserves and the discounted future net revenues from those reserves, as prepared by independent petroleum engineers. There are numerous uncertainties inherent in such estimates including many factors beyond the control of the Corporation. The estimates are based on a number of assumptions including constant oil and gas prices, and assumptions regarding future production, revenues, taxes, operating expenses, development expenditures and quantities of recoverable oil and gas reserves. Such estimates are inherently imprecise indications of future net revenues, and actual results might vary substantially from the estimates based on these assumptions. Any significant variance in these assumptions could materially affect the estimated quantity and value of reserves. In addition, the Corporation's reserves might be subject to revisions based upon future production, results of future exploration and development, prevailing oil and gas prices and other factors. More over, estimates of the economically recoverable oil and gas reserves, classifications of such reserves and estimates of future net cash flows prepared by independent engineers at different times may vary substantially. Information about reserves constitutes forward-looking statements. Further, the future success of the Corporation depends upon its ability to find, develop and acquire oil and gas reserves that are economically recoverable. As a result, the Corporation must locate, acquire and develop new oil and gas reserves to replace those being depleted by production. Without successful funding for acquisitions and exploration and development activities, the Corporation's reserves will decline. No assurances can be made that the Corporation will be able to find and develop or acquire additional reserves at an acceptable cost.

Competition

The Corporation engages in the highly competitive industry of exploration for and production of oil and gas. The Corporation competes directly and indirectly with major and independent oil and gas companies in its exploration for and development of desirable oil and gas properties. Many companies and individuals are engaged in the business of acquiring interests in and developing oil and gas properties in Canada, and the industry is not dominated by any single competitor or a small number of competitors. Many of such competitors have substantially greater financial, technical, sales, marketing and other resources, as well as greater historical market acceptance than does the Corporation. The Corporation will compete with numerous industry participants for the acquisition of land and rights to prospects, and for the equipment and labor required to operate and develop such prospects. Competition could materially and adversely affect the Corporation's business, operating results and financial condition. Such competitive disadvantages could adversely affect the Corporation's ability to participate in projects with favorable rates of return.

Shortage of Supplies and Equipment

The Corporation's ability to conduct operations in a timely and cost effective manner is subject to the availability of natural gas and crude oil field supplies, rigs, equipment and service crews. Although none are expected currently, any shortage of certain types of supplies and equipment could result in delays in our operations as well as in higher operating and capital costs.

Interruption From Severe Weather

The Corporation's operations are conducted principally in the central region of Alberta, northeastern British Columbia and Saskatchewan. The weather in these areas can be extreme and can cause interruption or delays in our drilling and construction operations.

Dependence on Third-Party Pipelines

In fiscal 2006, substantially all of Terra Energy's sales of natural gas production were through deliveries to local third-party gathering systems to processing plants. In addition, the Corporation relies on access to interprovincial pipelines for the sale and distribution of substantially all of our gas. As a result, a curtailment of our sale of natural gas by pipelines or by third-party gathering systems, an impairment of our ability to transport natural gas on interprovincial pipelines or a material increase in the rates charged to us for the transportation of natural gas by reason of a change in federal or provincial regulations or for any other reason, could have a material adverse effect upon us. In such event, we would have to obtain other transportation arrangements. There can be no assurance that we would have economical transportation alternatives or that it would be feasible for us to construct pipelines. In the event such circumstances were to occur, our netbacks from the affected wells would be suspended until, and if, such circumstances could be resolved.

Operating Hazards and Uninsured Risks

The oil and gas business involves a variety of operating risks, including fire, explosion, pipe failure, casing collapse, abnormally pressured formations, adverse weather conditions, governmental and political actions, premature reservoir declines and environmental hazards such as oil spills, gas leaks and discharges of toxic gases. The occurrence of any of these events with respect to any property operated or owned (in whole or in part) by us could have a material adverse impact on us. The Corporation and the operators of our properties, maintain insurance in accordance with customary industry practices and in amounts that we believe to be reasonable. However, insurance coverage is not always economically feasible and is not obtained to cover all types of operational risks. The occurrence of a significant event that is not insured or insured fully could have a material adverse effect on our financial condition.

Restoration, Safety and Environmental Risks

Our operations are in Saskatchewan, Alberta and British Columbia. Certain laws and regulations exist that require companies engaged in petroleum activities to obtain necessary safety and environmental permits to operate. Such legislation may restrict or delay us from conducting operations in certain geographical areas. Further, such laws and regulations may impose liabilities on us for remedial and clean-up costs, personal injuries related to safety and environmental damages, such liabilities collectively referred to as “asset retirement obligations”.

Expiration of Licenses and Leases

The Corporation’s properties are held in the form of licenses and leases and working interests in licenses and leases. If the Corporation or the holder of the license or lease fails to meet the specific requirement of a license or lease, the license or lease may terminate or expire. There can be no assurance that any of the obligations required to maintain each license or lease will be met. The termination or expiration of the Corporation’s licenses or leases or the working interests relating to a license or lease may have a material adverse effect on the Corporation’s results of operations and business.

Canadian Government Regulation and Industry Conditions

The Kyoto protocol, ratified by the Canadian federal government in December 2002, came into force on February 16, 2005. The protocol commits Canada to reducing greenhouse gas emissions to six percent below 1990 levels over the period 2008-2012. The Canadian government released a framework outlining its Climate Change action plan on April 13, 2005. The plan contains few technical details regarding the implementation of the government’s greenhouse gas reduction strategy. The Climate Change Working Group of the Canadian Association of Petroleum Producers continues to work with the Canadian and Alberta governments to develop an approach for implementing targets and enabling greenhouse gas control legislation, which protects the industry’s competitiveness, limits the cost and administrative burden of compliance and supports continued investment in the sector. As the Canadian government has yet to release a detailed Kyoto compliance plan, the Corporation is unable to predict the impact of potential regulations upon its business; however, it is possible that the Corporation would face increases in operating costs in order to comply with the greenhouse gas emissions legislation.

Canadian Government Regulation and Environmental Matters

The oil and natural gas industry is subject to extensive controls and regulations imposed by various levels of the federal and provincial governments of Canada. It is not expected that any of these controls or regulations will affect the operations of the Corporation in a manner materially different than they would affect other oil and gas companies of similar size. All current legislation is a matter of public record and the Corporation is unable to accurately predict what additional legislation or amendments may be enacted. All of the governmental regulations noted below may be changed from time to time in response to economic or political conditions. The Corporation’s management believes that the trend of more expansive and stricter environmental laws and regulations will continue. The implementation of new or modified environmental laws or regulations could have a material adverse impact on the Corporation.

The Corporation is subject to various Canadian federal and provincial laws and regulations relating to the environment. The Corporation believes that it is currently in compliance with such laws and regulations. However, such laws and regulations may change in the future in a manner which will increase the burden and cost of compliance. In addition, the Corporation could incur significant liability under such laws for damages, clean-up costs and penalties in the event of certain discharges into the environment. In addition, environmental laws and regulations may impose liability on the Corporation for personal injuries, clean-up costs, environmental damage and property damage as well as administrative, civil and criminal penalties. The Corporation maintains limited insurance coverage for accidental environmental damages, but does not maintain insurance for the full potential liability that could be caused by such environmental damage. Accordingly, the Corporation may be subject to significant liability, or may be required to cease production in the event of the noted liabilities.

Provincial Regulation – Royalties Incentives and Land Tenures

In addition to federal regulations, each province has regulations which govern land tenure, royalties, production rates, extra-provincial export, environmental protection and other matters. The royalty regime is a significant factor in the profitability of oil and natural gas production. Royalties payable on production from lands other than Crown lands are determined by negotiations between the mineral owner and the lessee. Crown royalties are determined by government regulation and are generally calculated as a percentage of the value of the gross production. The rate of royalties payable generally depends in part on prescribed reference prices, well productivity, geographical location, field discovery date and the type or quality of the petroleum product produced. From time to time the provincial governments of Canada have established incentive programs which have included royalty rate reductions, royalty holidays and tax credits for the purpose of encouraging oil and natural gas exploration or enhanced planning projects. Crude oil and natural gas located in the western provinces is owned predominantly by the respective provincial governments. Provincial governments grant rights to explore for and produce oil and natural gas pursuant to leases, licenses and permits for varying terms from two years and on conditions set forth in provincial legislation including requirements to perform specific work or make payments. Oil and natural gas located in such provinces can also be privately owned and rights to explore for and produce such oil and natural gas are granted by lease on such terms and conditions as may be negotiated.

**Terra Energy Corp.
Consolidated Financial Statements
For the Three Months Ended March 31, 2007
(Unaudited)**

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Terra Energy Corp.
Consolidated Balance Sheets
As at
(Unaudited)

	March 31, 2007	December 31, 2006
Assets		
Current		
Accounts receivable	\$ 5,822,204	\$ 5,752,846
Financial instruments (Note 4)	-	1,841,861
Prepaid expenses	1,236,813	1,261,720
	7,059,017	8,856,427
Oil and gas properties	143,688,867	138,704,967
	\$ 150,747,884	\$ 147,561,394
Liabilities and Shareholders' Equity		
Current		
Bank overdraft (Note 3)	\$ 1,762,910	\$ 8,412,852
Accounts payable and accrued liabilities	12,589,709	10,775,251
Financial instruments (Note 4)	1,004,786	-
	15,357,405	19,188,103
Deferred credit	232,484	249,090
Long-term financing (Note 3)	47,116,795	35,478,837
Asset retirement obligation	5,067,843	5,033,926
Future income taxes	14,334,066	10,245,725
	82,108,593	70,195,681
Shareholders' Equity		
Share capital (Note 8(b))	65,866,977	73,004,715
Contributed surplus (Note 7)	8,589,711	7,838,602
Deficit	(5,817,397)	(3,477,604)
	68,639,291	77,365,713
	\$ 150,747,884	\$ 147,561,394
Commitments and contingencies (Note 9)		

Terra Energy Corp.
Consolidated Statements of Loss, Comprehensive Loss and Deficit
For the Three Months Ended
(Unaudited)

	March 31, 2007	March 31, 2006
Revenue		
Petroleum and natural gas revenues	\$ 10,384,124	\$ 11,189,502
Realized gain on financial instruments	309,093	275,513
Unrealized (loss) gain on financial instruments	<u>(2,846,646)</u>	<u>322,535</u>
	7,846,571	11,787,550
Royalties	<u>(2,222,705)</u>	<u>(2,363,529)</u>
	<u>5,623,866</u>	<u>9,424,021</u>
Expenses		
Production	3,120,330	3,023,642
General and administrative	1,249,055	1,129,064
Accretion expense	111,517	105,500
Stock-based compensation	316,851	1,393,309
Depletion, depreciation and amortization	3,375,514	3,174,836
Interest on long-term debt	635,376	418,314
Realized foreign exchange gain	-	(48,498)
Unrealized foreign exchange gain	<u>-</u>	<u>(224,967)</u>
	<u>8,808,643</u>	<u>8,971,200</u>
(Loss) income before income taxes	<u>(3,184,777)</u>	<u>452,821</u>
Income tax (recovery) expense		
Current tax	-	10,574
Future tax (recovery)	<u>(1,016,359)</u>	<u>672,657</u>
	<u>(1,016,359)</u>	<u>683,231</u>
Loss and comprehensive loss for the period	<u>(2,168,418)</u>	<u>(230,410)</u>
Deficit, beginning of period	<u>(3,477,604)</u>	<u>(1,259,194)</u>
Repurchase of common shares (Note 8(b))	<u>(171,375)</u>	<u>(604,493)</u>
Deficit, end of period	<u>\$ (5,817,397)</u>	<u>\$ (2,094,097)</u>
Loss per share - basic and diluted	\$ (0.03)	\$ -
Weighted average number of shares outstanding - basic	75,822,011	70,376,376
Weighted average number of shares outstanding - diluted	75,822,011	72,551,972

Terra Energy Corp.
Consolidated Statements of Cash Flows
For the Three Months Ended
(Unaudited)

	March 31, 2007	March 31, 2006
Cash flows from operating activities		
Loss for the period	\$ (2,168,418)	\$ (230,410)
Items not affecting cash:		
Future income tax (recovery)	(1,016,359)	672,657
Accretion of asset retirement obligations	111,517	105,500
Stock-based compensation	316,851	1,393,309
Unrealized loss (gain) on financial instruments (Note 4)	2,846,646	(322,535)
Realized loss on financial instruments	-	275,513
Amortization of deferred credit	(16,606)	-
Depletion, depreciation and amortization	3,375,514	3,174,836
	<u>3,449,145</u>	<u>5,068,870</u>
Changes in non-cash working capital from operations	(162,496)	1,339,502
Cash flows from operating activities	<u>3,286,649</u>	<u>6,408,372</u>
Cash flows from (used in) financing activities		
Proceeds from long-term financing	11,637,958	5,494,929
(Decrease) in bank overdraft	(6,649,942)	-
Issuance of common shares, net of issuance costs	(3,084)	4,918,655
Repurchase of common shares	(1,767,071)	(1,054,862)
Cash flows from financing activities	<u>3,217,861</u>	<u>9,358,722</u>
Cash flows (used in) from investing activities		
Additions to oil and gas properties	(8,437,014)	(22,367,989)
Changes in non-cash working capital from investing	1,932,504	(2,649,264)
Cash flows used in investing activities	<u>(6,504,510)</u>	<u>(25,017,253)</u>
Decrease in cash and cash equivalents	-	(9,250,159)
Cash and cash equivalents, beginning of period	-	13,127,316
Cash and cash equivalents, end of period	\$ -	\$ 3,877,157

1. NATURE OF OPERATIONS

Terra Energy Corp. (the "Corporation") was formed on January 30, 2004 as a result of the amalgamation of Rhodes Resources Corp, Terrapet Energy Corp., and Terra Energy Corp. pursuant to the Business Corporations Act of Alberta. The amalgamated Corporation operates under the name Terra Energy Corp. The Corporation's principal business is the exploration, development, and production of oil and natural gas in Western Canada.

2. CHANGES IN ACCOUNTING POLICIES AND PRACTICES

The interim consolidated financial statements of Terra Energy Corp. have been prepared by management in accordance with Canadian generally accepted accounting principles. The interim consolidated financial statements have been prepared following the same accounting policies and methods of computation as the consolidated financial statements for Terra Energy Corp. for the year ended December 31, 2006 except as noted below. Certain disclosures, which are normally required to be included in the notes to the financial statements, have been condensed or omitted. The interim consolidated financial statements should be read in conjunction with the audited consolidated financial statements of Terra Energy Corp. and the notes thereto for the year ended December 31, 2006.

On January 1, 2007, the Corporation adopted the Canadian Institute of Chartered Accountants ("CICA") Handbook Section 1530 "Comprehensive Income", Section 3855 "Financial Instruments - Recognition and Measurement", Section 3865 "Hedges" and Section 3251 "Equity". The Corporation has adopted these standards retrospectively and the comparative interim financial statements have not been restated.

Comprehensive Income

The new standards introduce comprehensive income, which consists of net earnings and other comprehensive income ("OCI"). The Corporation's consolidated financial statements now include a Consolidated Statement of Loss, Comprehensive Loss and Deficit. The cumulative changes in OCI are included in accumulated other comprehensive income ("AOCI"), which is presented as a new category within shareholder's equity in the Consolidated Balance Sheet.

Financial Instruments

The financial instruments standard establishes the recognition and measurement criteria for financial assets, financial liabilities and derivatives. All financial instruments are required to be measured at fair value on initial recognition of the instrument, except for certain related party transactions. Measurement in subsequent periods depends on whether the financial instrument has been classified as "held-for-trading", "available-for-sale", "held-to-maturity", "loans and receivables", or "other financial liabilities" as defined by the standard.

Financial assets and financial liabilities "held-for-trading" are measured at fair value with changes in those fair values recognized in net earnings. Financial assets "available-for-sale" are measured at fair value, with changes in those fair values recognized in OCI. Financial assets "held-to-maturity", "loans and receivables" and "other financial liabilities" are measured at amortized cost using the effective interest method of amortization. The methods used by the Corporation in determining fair value of financial instruments are unchanged as a result of implementing the new standard.

2. CHANGES IN ACCOUNTING POLICIES AND PRACTICES (continued)

Cash and cash equivalents are designated as “held-for-trading” and are measured at carrying value, which approximates fair value due to the short-term nature of these instruments. Accounts receivable is designated as “loans and receivables”. Accounts payable and accrued liabilities, bank overdraft and long-term financing are designated as “other liabilities”. Risk management assets and liabilities are derivative financial instruments classified as “held-for-trading” unless designated for hedge accounting.

The Corporation also adopted Section 1506 “Accounting Changes”, the only impact of which is to provide disclosure of when an entity has not applied a new source of GAAP that has been issued but is not yet effective. This is the case with Section 3862 “Financial Instruments Disclosures” and Section 3863 “Financial Instruments Presentations” which are required to be adopted for fiscal years beginning on or after October 1, 2007. This section also prescribes disclosures for voluntary changes and sets requirements for disclosures for the reasons of these changes. The Corporation will adopt these standards on January 1, 2008 and it is expected the only effect on the Corporation will be incremental disclosures regarding the significance of financial instruments for the entity’s financial position and performance; and the nature, extent and management of risks arising from financial instruments to which the entity is exposed.

3. LONG-TERM FINANCING

The Corporation has a revolving line of credit, with a syndicate of chartered banks, of up to \$55 million (December 31, 2006 - \$55 million), which bears interest at prime plus 0.25% (2006 - prime plus 0.25%). The facility is secured by a general security agreement, a floating charge debenture in the amount of \$150 million and an unlimited liability guarantee by Terra Energy Corp. and Constar Resources Ltd. At March 31, 2007, the Corporation was indebted on the revolving line of credit in the amount of \$47,116,795 (December 31, 2006 - \$35,478,837) and was in compliance with all loan covenants. The outstanding cheques issued in the amount of \$1,762,910 (December 31, 2006 - \$8,412,852) are shown as bank overdraft until they clear against the revolving line.

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4. FINANCIAL INSTRUMENTS

At March 31, 2007, the Corporation had entered into commodity contracts, the terms of which are summarized as follows:

Contract Type	Floor Price	Ceiling Price	Volumes Per Day	Contract Term
Financial	Sell \$86.00 per Bbl	N/A	200 Bbls	June 1, 2006 to May 31, 2007
Financial	Buy \$80.65 per Bbl	N/A	200 Bbls	June 1, 2006 to May 31, 2007
Financial	Sell US\$77.25 per Bbl	N/A	100 Bbls	January 1, 2007 to December 31, 2007
Financial	Buy US\$76.40 per Bbl	N/A	100 Bbls	January 1, 2007 to December 31, 2007
Financial	Sell \$7.50 per GJ	N/A	1,000 GJ	November 1, 2006 to October 31, 2007
Financial	Sell \$6.50 per GJ	\$8.92 per GJ	1,000 GJ	November 1, 2006 to October 31, 2007
Financial	Sell \$7.50 per GJ	N/A	1,500 GJ	December 1, 2006 to December 31, 2007
Financial	Sell \$7.65 per GJ	N/A	1,000 GJ	December 1, 2006 to October 31, 2007
Financial	Sell \$7.75 per GJ	N/A	1,000 GJ	January 1, 2007 to December 31, 2007
Financial	Sell \$6.65 per GJ	N/A	2,000 GJ	March 1, 2007 to March 31, 2007
Financial	Buy \$7.22 per GJ	N/A	5,500 GJ	April 1, 2007 to April 30, 2007
Financial	Buy \$7.05 per GJ	N/A	2,000 GJ	April 1, 2007 to April 30, 2007
Financial	Buy \$6.95 per GJ	N/A	2,000 GJ	April 1, 2007 to April 30, 2007
Financial	Buy \$7.41 per GJ	N/A	3,000 GJ	May 1, 2007 to December 31, 2007
Financial	Sell \$7.40 per GJ	N/A	2,000 GJ	March 1, 2007 to July 31, 2007
Financial	Sell \$6.53 per GJ	N/A	1,000 GJ	April 1, 2007 to October 31, 2007
Financial	Sell \$8.05 per GJ	N/A	1,000 GJ	November 1, 2007 to March 31, 2008
Financial	Sell \$7.45 per GJ	N/A	1,000 GJ	April 1, 2007 to March 31, 2008
Financial	Sell \$8.00 per GJ	\$8.60 per GJ	1,000 GJ	November 1, 2007 to March 31, 2008
Financial	Sell \$7.10 per GJ	N/A	1,000 GJ	April 1, 2007 to October 31, 2007
Financial	Sell \$8.00 per GJ	N/A	2,000 GJ	November 1, 2007 to December 31, 2007
Financial	Sell \$7.95 per GJ	N/A	1,000 GJ	April 1, 2007 to March 31, 2008
Financial	Sell \$8.05 per GJ	N/A	1,000 GJ	December 1, 2007 to December 31, 2007
Financial	Sell \$8.20 per GJ	\$9.21 per GJ	1,000 GJ	November 1, 2007 to March 31, 2008
Financial	Sell \$8.25 per GJ	\$9.40 per GJ	1,000 GJ	November 1, 2007 to March 31, 2008
Financial	Sell \$8.50 per GJ	\$9.00 per GJ	1,000 GJ	November 1, 2007 to March 31, 2008

The mark to market adjustment of these contracts has been recognized as liability in the amount of \$1,004,786 at March 31, 2007 (December 31, 2006 - asset of \$1,841,861). Subsequent to March 31, 2007, the Corporation entered into financial commodity contracts to offset existing contracts and crystallized gains (Note 10).

5. RELATED PARTY TRANSACTIONS

The Corporation had the following related party transactions:

	March 31, 2007	March 31, 2006
Expenses		
Consulting - Pioneer Land Services Ltd.	\$ 209	\$ 4,859
Legal consulting - Borden Ladner Gervais LLP	154,648	53,520
	\$ 154,857	\$ 58,379
Other		
Recorded as part of oil and gas properties - Pioneer Land Services Ltd	\$ 5,685	\$ 22,440
Recorded as part of share issuance cost - Borden Ladner Gervais LLP	3,084	-
	\$ 8,769	\$ 22,440

Revenue and expense transactions are in the normal course of operations and have been valued in these consolidated financial statements at the exchange amount which is the amount of consideration established and agreed to by the related parties.

6. STATEMENT OF CASH FLOWS

Other information:

	March 31, 2007	March 31, 2006
Interest paid	\$ 635,376	\$ 418,314
Taxes received	\$ -	\$ -
Taxes paid	\$ -	\$ 10,574

7. CONTRIBUTED SURPLUS

Contributed surplus consists of the fair value of both share warrants issued for various financing agreements and for the stock-based compensation on stock options.

The details of contributed surplus are as follows:

	March 31, 2007	December 31, 2006
Balance, beginning of period	\$ 7,838,602	\$ 3,809,311
Stock-based compensation	316,851	2,743,436
Warrants expired	434,258	2,300,356
Exercise of options and warrants to common shares	-	(1,014,501)
Balance, end of period	\$ 8,589,711	\$ 7,838,602

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8. SHARE CAPITAL

a) Authorized

- i) Unlimited number of common voting shares
- ii) Unlimited number of preferred shares

b) Issued and outstanding

	March 31, 2007		December 31, 2006	
	Number of Shares	Amounts	Number of Shares	Amounts
Common shares				
Balance, beginning of period	76,900,833	\$ 72,570,457	68,093,883	\$ 57,375,841
Issued on exercise of warrants	-	-	2,286,650	3,269,485
Issued on exercise of options	-	-	2,102,000	2,484,245
	76,900,833	72,570,457	72,482,533	63,129,571
Flow-through shares issued				
November 21, 2006 at \$1.90	-	-	8,270,000	15,713,000
	-	-	8,270,000	15,713,000
Tax effect of flow-through share renouncement	-	(5,106,725)	-	(4,254,388)
Transfer from contributed surplus	-	-	-	1,014,501
Carrying value of warrants exercised	-	-	-	873,757
Shares repurchased for cancellation	(1,697,549)	(1,595,696)	(3,851,700)	(3,233,222)
Cash share issue costs, net of tax of (2006 - \$329,857)	-	(1,059)	-	(672,762)
	(1,697,549)	(6,703,480)	(3,851,700)	(6,272,114)
Balance, end of period	75,203,284	\$ 65,866,977	76,900,833	\$ 72,570,457
Share purchase warrants				
Balance, beginning of period	1,093,700	\$ 434,258	7,752,277	\$ 3,608,371
Expired	(1,093,700)	(434,258)	(4,469,427)	(2,300,356)
Exercised	-	-	(2,189,150)	(873,757)
Balance, end of period	-	-	1,093,700	434,258
Total common shares and warrants	75,203,284	\$ 65,866,977	77,994,533	\$ 73,004,715

During 2005 and 2006, the Corporation obtained permission from the TSX Venture Exchange for Normal Course Issuer Bid (NCIB) to repurchase for cancellation up to 7,500,000 common shares (2.5 million and 5.0 million respectively).

During the calendar year 2006, the Corporation repurchased 3,851,700 shares for \$6,339,284 at an average price of \$1.65 per common share and recorded \$3,233,222 as a reduction of share capital and the excess of 3,106,062 was charged to deficit.

During the three-month period ended March 31, 2007, the Corporation repurchased 1,697,549 shares for \$1,767,071 at an average price of \$1.04 per common share and recorded \$1,595,696 as a reduction of share capital and the excess of \$171,375 was charged to deficit.

Of the repurchased shares 3,675,749 are being held for cancellation. Shares repurchased under the NCIB are excluded from the outstanding number of shares.

8. SHARE CAPITAL (continued)

c) Stock options

Details of all options outstanding are as follows:

	March 31, 2007	
	Number of Options	Weighted Average Exercise Price
Employee stock options		
Balance, beginning of period	5,802,000	\$ 1.58
Granted	48,000	\$ 1.38
Expired	(14,000)	\$ (1.85)
Balance, end of period	5,836,000	\$ 1.35
Agent options		
Balance, beginning of period	654,929	\$ 1.40
Expired	(654,929)	\$ (1.40)
Balance, end of period	-	\$ -
Total options, balance, end of period	5,836,000	\$ 1.35

In January 2007, the Corporation re-priced certain stock options. The exercise prices of 2,107,000 employee stock options previously granted ranging from \$1.15 to \$2.27 were re-priced to \$1.08. The options held by the directors and senior officers were excluded from the re-pricing. The differences between fair values of the repriced options issued as compared to the old options are expensed over the vesting periods of options.

For stock options granted to employees compensation expense of \$316,851 has been recorded for the period ended March 31, 2007 (2006 - \$1,393,309) with the offsetting credit to contributed surplus. The fair value of share options granted during the first quarter was \$23,941 estimated using the Black-Scholes option-pricing model with the following assumptions: Dividend yield nil (2006 - Nil); expected volatility at 50% (2006 - 66%); risk-free interest rate of 4% (2005 - 4.0%); weighted average life of 3.07 years (2006 - 2.96 years).

The weighted average price of outstanding stock options at March 31, 2007 was \$1.35 (2006 - \$1.56). The weighted average price for exercisable options was \$1.40 (2006 - \$1.60), and term for exercisable options was 2.62 years (2006 - 2.55 years).

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8. SHARE CAPITAL (continued)

d) Warrants

During 2004, the Corporation issued the following warrants:

2004 Terra Series B

These warrants were issued in conjunction with the subordinated debt issued on December 30, 2004 and are exercisable at \$1.40 per common share until June 30, 2007 at which time these warrants will expire.

Balance, December 31, 2006	Exercised	Expired	Balance, March 31, 2007
1,250,000	-	-	1,250,000

2004 Terra Series C

These warrants were issued in conjunction with the subordinated debt issued on December 30, 2004 and are exercisable at \$1.40 per common share until December 31, 2006 and at \$1.60 per common share until December 31, 2007 at which time these warrants will expire.

2,500,000	-	-	2,500,000
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Subtotal 2004 warrants

3,750,000	-	-	3,750,000
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During 2005, the Corporation issued the following warrants:

2005 Terra Series E

These warrants are exercisable at \$1.40 to purchase one common share until January 26, 2006 and at \$1.60 per one common share until January 26, 2007 at which time these warrants will expire.

1,093,700	-	1,093,700	-
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Subtotal 2005 warrants

1,093,700	-	1,093,700	-
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Total warrants

4,843,700	-	1,093,700	3,750,000
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9. COMMITMENTS AND CONTINGENCIES

- a) The Corporation had outstanding letters of credit to various parties for a total of \$345,000 (2006 - \$395,000) which expire at various dates during 2007.
- b) The Corporation is required to incur exploration and development activities by December 31, 2007 of approximately \$15,713,000 as a result of flow-through shares issued in November 2006. At March 31, 2007, the Corporation has incurred qualifying expenditures of approximately \$4,748,464 towards this obligation.

10. SUBSEQUENT EVENT

Subsequent to March 31, 2007, the Corporation entered into the following financial commodity contracts to offset existing contracts as at March 31, 2007 (Note 4) and crystallize gains:

Contract Type	Floor Price	Ceiling Price	Volumes Per Day	Contract Term
Financial	Buy \$7.24 per GJ	N/A	1,000 GJ	May 1, 2007 to May 31, 2007
Financial	Buy \$7.23 per GJ	N/A	3,000 GJ	May 1, 2007 to May 31, 2007
Financial	Buy \$7.25 per GJ	N/A	2,000 GJ	May 1, 2007 to May 31, 2007
Financial	Buy \$7.30 per GJ	N/A	1,500 GJ	May 1, 2007 to May 31, 2007
Financial	Buy \$7.19 per GJ	N/A	2,000 GJ	June 1, 2007 to June 30, 2007
Financial	Buy \$7.14 per GJ	N/A	2,000 GJ	June 1, 2007 to June 30, 2007
Financial	Buy \$7.40 per GJ	N/A	1,500 GJ	June 1, 2007 to November 30, 2007
Financial	Buy \$7.48 per GJ	N/A	1,000 GJ	June 1, 2007 to December 30, 2007
Financial	Buy \$7.45 per GJ	N/A	1,000 GJ	June 1, 2007 to December 30, 2007
Financial	Buy \$7.35 per GJ	N/A	1,000 GJ	July 1, 2007 to November 30, 2007
Financial	Buy \$8.00 per GJ	\$8.60 per GJ	1,000 GJ	November 1, 2007 to March 31, 2008
Financial	Buy \$8.20 per GJ	\$9.21 per GJ	1,000 GJ	November 1, 2007 to March 31, 2008
Financial	Buy \$8.25 per GJ	\$9.40 per GJ	1,000 GJ	November 1, 2007 to March 31, 2008
Financial	Buy \$8.50 per GJ	\$9.00 per GJ	1,000 GJ	November 1, 2007 to March 31, 2008

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Auditor

Deloitte & Touche, LLP, Calgary, Alberta

Evaluation Engineers

GLJ Petroleum Consultants Ltd.

Banker

TD Canada Trust, Calgary, Alberta
National Bank of Canada, Calgary, Alberta

Transfer Agent

Shareholders are encouraged to contact our Registrar and Transfer Agent for information regarding their securities holdings:

Computershare Trust Company
Suite 600, 530 Eighth Avenue SW
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Stock Symbol

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