UNREALIZED**POTENTIAL**
OPPORTUNITYDRIVEN

cequence
energy ltd

HIGHLIGHTS

(000's except per share amounts)	Three months ended September 30			Nine months ended September 30		
	2010	2009	% Change	2010	2009	% Change
Financial ($)						
Production revenue, including realized hedge	$ 12,951	$ 5,962	117%	$ 32,218	$ 19,136	68%
Net loss	(3,620)	(6,994)	(48%)	(8,396)	(5,998)	40%
Per share, basic and diluted	(0.05)	(0.26)	(81%)	(0.17)	(0.39)	(56%)
Funds flow from operations (1)	3,695	(2,663)	239%	11,036	766	1,341%
Per share, basic and diluted	0.05	(0.10)	150%	0.22	0.05	340%
Production volumes						
Natural gas (Mcf/d)	23,674	6,734	252%	17,649	7,556	134%
Crude oil (bbls/d)	332	128	159%	285	124	130%
Natural gas liquids (bbls/d)	342	67	410%	202	88	130%
Total (boe/d)	4,619	1,317	251%	3,428	1,471	133%
Sales prices						
Natural gas, including realized hedges ($/Mcf)	$ 4.13	$ 7.69	(46%)	$ 4.79	$ 7.70	(38%)
Crude oil ($/bbl)	70.47	66.85	5%	72.36	61.00	19%
Natural gas liquids ($/bbl)	57.33	66.76	(14%)	63.65	49.42	29%
Total ($/boe)	$ 30.47	$ 49.20	(38%)	$ 34.42	$ 47.64	(28%)
Operating Netbacks ($/boe)						
Price	$ 30.47	$ 49.20	(38%)	$ 34.42	$ 47.64	(28%)
Royalties	(3.15)	(9.66)	(67%)	(3.37)	(5.86)	(42%)
Transportation	(2.88)	(2.55)	13%	(3.00)	(1.98)	52%
Operating costs	(10.38)	(21.53)	(52%)	(11.41)	(17.69)	(36%)
Operating Netback	$ 14.06	$ 15.46	(9%)	$ 16.64	$ 22.11	(25%)
Capital Expenditures	$ 8,309	$ 3,334	149%	$ 39,728	$ 8,310	378%
Corporate Acquisitions (4)	142,496	320	N/A	171,865	320	N/A
Property Acquisitions (net)	47,725	15,763	203%	48,004	15,763	205%
Total capital expenditures	$198,530	$ 19,416	923%	$259,597	$ 24,393	964%
Net debt and working capital (deficiency) (2)	(68,857)	23,888	(388%)	(68,857)	23,888	(388%)
Long-term debt related to investments (3)	-	(18,120)	(100%)	-	(18,120)	(100%)
Weighted average shares outstanding (basic and diluted)	69,060	26,577	160%	50,321	15,333	228%
Undeveloped land (net acres)	300,800	155,400	94%	300,800	155,400	94%

(1) Funds flow from operations is calculated as cash flow from operating activities before adjustments for asset retirement expenditures and net changes in non-cash working capital.

(2) Net debt and working capital is calculated as cash, net working capital less commodity contract asset, demand credit facilities and excluding the current portion of future income taxes.

(3) The long-term debt related to investments was a stand-alone credit facility with Cequence's lender to provide short term liquidity to the Company in light of the restructuring of the asset backed MAV II notes. During the three months ended September 30, 2010 the MAV II notes were sold and the proceeds, in addition to available cash, were used to pay down the long-term debt related to investments and close the facility.

(4) Corporate acquisitions for the nine months ended September 30, 2010 includes $29,319 related to the acquisition of Peloton Exploration Corp. ($645 cash) and $142,546 related to the acquisition of Temple Energy Inc. ($2,438 cash).

MANAGEMENT'S DISCUSSION AND ANALYSIS

This Management's Discussion and Analysis ("MD & A") of the financial and operating results of Cequence Energy Ltd. ("Cequence" or the "Company") should be read in conjunction with the Company's unaudited consolidated financial statements (the "Financial Statements") and related notes for the three and nine months ended September 30, 2010 as well as with the audited consolidated financial statements (the "Annual Financial Statements") and related notes and MD & A for the year ended December 31, 2009.

Additional information relating to the Company, including its MD & A for the prior year and the annual information form ("AIF") is available on SEDAR at www.sedar.com.

This MD & A is dated November 10, 2010.

BASIS OF PRESENTATION

The financial data presented below has been prepared in accordance with Canadian Generally Accepted Accounting Principles ("GAAP"). The financial information presented reflects the consolidated financial statements of Cequence.

The reporting and the measurement currency is the Canadian dollar. For the purpose of calculating unit costs, natural gas is converted to a barrel of oil equivalent ("boe") using six thousand cubic feet of natural gas equal to one barrel of oil unless otherwise stated. The term barrels of oil equivalents (boe) may be misleading, particularly if used in isolation. A boe conversion ratio for gas of 6 Mcf:1 boe is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead.

Unless otherwise stated and other than per unit items, all figures are presented in thousands.

NON-GAAP MEASUREMENTS

Within the MD & A references are made to terms commonly used in the oil and gas industry. Netback is not defined by GAAP in Canada and is referred to as a non-GAAP measure. Netbacks equal total revenue less royalties, operating costs and transportation costs. Management utilizes this measure to analyze operating performance.

Funds flow from operations is a non-GAAP term that represents cash flow from operating activities before adjustments for asset retirement expenditures and net changes in non-cash working capital. The Company evaluates its performance based on earnings and funds flow from operations. The Company considers funds flow from operations a key measure as it demonstrates the Company's ability to generate the cash flow necessary to fund future growth through capital investment and to repay debt. The Company's calculation of funds flow from operations may not be comparable to that reported by other companies. Funds flow from operations per share is calculated using the same weighted average number of shares outstanding used in the calculation of income (loss) per share.

Non-GAAP financial measures do not have a standardized meaning prescribed by GAAP and are therefore unlikely to be comparable to similar measures presented by other issuers.

OVERVIEW

On July 30, 2009 the shareholders of Cequence (formerly Sabretooth Energy Ltd.) approved certain reorganization transactions to recapitalize the Company with new equity, appoint new management and restructure the board of directors. Also as part of the transaction the Company changed its name to Cequence Energy Ltd. and affected a four for one share consolidation (the "reorganization transactions"). These transactions were approved by the shareholders of the Company at the annual and special meeting of shareholders held on July 29, 2009.

The reorganization transactions included a private placement to new management, employees, directors and consultants, a rights offering to existing shareholders and a subscription receipts offering. Total cash proceeds from the equity offerings totalled $65,315, a portion of which was used to eliminate the outstanding operating bank line and complete three property acquisitions in 2009.

On August 18, 2009, Cequence announced the entering into of two separate purchase and sale agreements, one with a private oil and gas company providing for the acquisition by Cequence of the minor assets ("Minor Assets") and one with a subsidiary of a major publicly traded oil and gas company providing for the acquisition by Cequence of the Peace River Arch Assets (the "PRA Assets"). The purchase price for the Minor Assets was $4,000 and the purchase price for the PRA Assets was $13,250, both subject to adjustment. The acquisition of the PRA Assets was completed on September 24, 2009 with an effective date of June 1, 2009 and the acquisition of the Minor Assets was completed in late August with an effective date of August 1, 2009. Production at the time of acquisition of the acquired assets was approximately 850 boe/d (90 percent natural gas).

On November 12, 2009, the Company acquired all of the issued and outstanding shares of HFG Holdings Inc. ("HFG") not already held by Cequence for consideration of 2,645 common voting shares. The transaction was accounted for using the purchase method. The elimination of the non-controlling interest through an acquisition at a purchase price greater than HFG's book value in the Company's consolidated financial statements had the effect of increasing property and equipment assets, and decreasing future income tax assets. The accounts of the Company include the results of HFG for the year ended December 31, 2009. The non-controlling interest presented on the statement of operations includes the non-controlling interest's share of the operations of HFG to the date of acquisition.

The cost of acquisition was satisfied by the issuance of 2,645 shares valued at $3.97 per share based on the average trading price of the Company's stock during the three days before and three days after the announcement of the transaction. Transaction costs were $380 for a total acquisition cost of $10,882.

On June 11, 2010, the Company acquired all of the issued and outstanding shares of Peloton Exploration Corp. ("Peloton"), a private oil and gas company, for consideration of 12,059 common voting shares. The shares were valued based on Cequence's five day weighted average trading price on the TSX before and after the announcement of the transaction. The transaction was accounted for using the purchase method whereby the assets acquired and liabilities assumed are recorded at their fair value. The accounts of the Company include the results of Peloton effective June 11, 2010. The purchase price allocation is as follows:

Cost of Acquisition	$(000's)
Common shares (12,059 at $2.51)	30,269
Transaction costs	645
Total	**30,914**

Fair Value of the Assets and Liabilities Acquired	$(000's)
Property and equipment	29,319
Fair value of commodity contracts	339
Bank debt	(4,984)
Working capital deficiency	(1,031)
Asset retirement obligations	(552)
Future income tax assets – non-current	7,918
Future income tax liabilities – current	(95)
Total	**30,914**

On July 27, 2010, Cequence sold certain non-producing gas weighted properties in the Sinclair region of Northwest Alberta for total cash consideration of $36,900, subject to final adjustments. No gain or loss resulted on the sale as the sale did not change the depletion rate of the Company by more than 20 percent.

On August 19, 2010 the Company completed the sale of 3,200 shares on a CEE "flow-through" private placement basis at $2.50 per share for proceeds of $8,000 as well as 870 shares on a CDE "flow-through" private placement basis at $2.30 per share for proceeds of $2,001, resulting in a total issuance of 4,070 shares for total proceeds of $10,001. Under the terms of the respective agreements, Cequence is required to renounce $8,000 of CEE expenditures and $2,001 of CDE expenditures in February 2011. The qualifying CDE and CEE expenditures must be incurred by December 31, 2011 pursuant to the terms of the related agreements. As at September 30, 2010 the Company has not any incurred any of the qualifying CEE or CDE expenditures.

On August 19, 2010 the Company completed the sale of 18,545 subscription receipts at a price of $2.10 per subscription receipt for total proceeds of $38,945. The subscription receipts were convertible to Cequence common voting shares without further consideration upon the closing of the Deep Basin Assets acquisition (see below). Upon closing of the Deep Basin Assets acquisition on September 8, 2010, the subscription receipts were converted on a one for one basis, for no additional consideration and without further action, into common voting shares of the Company. On September 17, 2010, Cequence completed the sale of 2,500 common voting shares related to an over-allotment option on the subscription receipts offering discussed above at $2.10 per share for total proceeds of $5,250.

On September 8, 2010, the Company closed the acquisition of certain gas weighted properties located in the Simonette area of Northwest Alberta (the "Deep Basin Assets"). The purchase price, subject to final adjustments, was $85,000. An asset retirement obligation of $3,683 has been recognized as part of the acquisition.

On September 10, 2010, the Company acquired all of the issued and outstanding shares of Temple Energy Inc. ("Temple"), a private oil and gas company, for consideration of 46,846 common voting shares. The acquisition was effected by way of a plan of arrangement, whereby Cequence Acquisitions Ltd., a newly formed subsidiary of the Company, was amalgamated with Temple and continued as Cequence Acquisitions Ltd. The shares were valued based on Cequence's five day weighted average trading price on the TSX before and after the announcement of the transaction. The transaction was accounted for using the purchase method whereby the assets acquired and liabilities assumed are recorded at their fair value. The accounts of the Company include the results of Temple effective September 10, 2010.

The estimated purchase price allocation is as follows:

Cost of Acquisition	$(000's)
Common shares (46,846 at $2.28)	106,809
Transaction costs	2,438
Total	109,247

Fair Value of the Assets and Liabilities Acquired	$(000's)
Property and equipment	142,546
Fair value of commodity contracts	4,201
Bank debt	(36,423)
Working capital deficiency	(3,834)
Asset retirement obligations	(5,902)
Future income tax assets – non-current	9,842
Future income tax liabilities – current	(1,183)
Total	109,247

On September 10, 2010, Cequence completed the sale of 2,950 common voting shares through a private placement to a major shareholder as well as certain management and directors of the Company at $2.10 per share for total proceeds of $6,195.

SUBSEQUENT EVENTS

On October 15, 2010, the Company completed the sale of its 2011 fixed price commodity contracts totalling 4,000 gj/day at prices ranging from $5.85 to $6.20 per gj for total proceeds of $3,386. The proceeds will be used to fund future drilling activities.

Effective October 29, 2010, the Company agreed to sell, on a private placement basis, 2,250 units at a price of $2.00 per unit for total proceeds of $4,500. Each unit entitles the holder to one common share on a CDE "flow-through" basis, one warrant to purchase one common share on a CDE "flow-through" basis at any time on or after August 1, 2011 and prior to August 15, 2011 at a price set as a 10 percent premium to the 10 day volume weighted average trading price of the Company's shares on the TSX for the period July 18, 2011 to July 29, 2011 (the "2011 Warrants") and one warrant to purchase one common share on a CDE "flow-through" basis at any time on or after August 1, 2012 and prior to August 15, 2012 at a price set as a 10 percent premium to the 10 day volume weighted average trading price of the Company's shares on the TSX for the period July 18, 2012 to July 31, 2012 (the "2012 Warrants). The purchaser has unconditionally committed to exercise the 2011 Warrants prior to August 15, 2011 and Cequence has the option to hold up to 1,500 of the shares to initially be issued in escrow until such time as the 2011 Warrants are exercised. If the 2011 Warrants are not exercised, the shares held in escrow shall be cancellable at no cost to Cequence and no redress to the shareholder. The 2012 Warrants are conditional on the exercise of the 2011 Warrants and if the 2011 Warrants are not exercised in accordance with their terms, the 2012 Warrants become null and void.

SELECTED FINANCIAL INFORMATION

Cequence recorded a loss of $3,620 for the quarter ended September 30, 2010. Net income (loss) and funds flow from operations for the period were negatively impacted by low natural gas prices.

Funds flow from operations was $3,695 for the quarter compared to negative funds flow of $2,663 for the same quarter in 2009. The increase in funds flow is due largely to an increase in revenue resulting from the expanded production base of the Company through acquisitions completed in 2010.

A reconciliation of cash flow from operating activities to funds flow from operations is as follows:

	Three months ended September 30		Nine months ended September 30	
$(000's)	2010	2009	2010	2009
Cash flow from operating activities	$ 5,600	$ (1,645)	$ 6,193	$ 2,377
Asset retirement expenditures	39	-	105	17
Net change in non-cash working capital	(1,944)	(1,018)	4,738	(1,628)
Funds flow from operations	$ 3,695	$ (2,663)	$ 11,036	$ 766

RESULTS OF OPERATIONS

Average production volumes, revenue and prices for the three and nine month periods ended September 30, 2010 and 2009 are outlined below:

	Three months ended September 30		Nine months ended September 30	
	2010	2009	2010	2009
Production				
Natural Gas (Mcf/d)	23,674	6,734	17,649	7,556
Crude Oil (bbls/d)	332	128	285	124
Natural gas liquids (bbls/d)	342	67	202	88
Total (boe/d)	4,619	1,317	3,428	1,471
Total production (boe)	424,992	121,179	935,940	401,673
$(000's)				
Revenue				
Natural gas	$ 8,432	$ 1,965	$ 20,746	$ 8,534
Realized gains on natural gas contracts	563	2,800	2,335	7,346
Total natural gas	8,995	4,765	23,081	15,880
Crude Oil	2,154	785	5,622	2,063
Natural gas liquids	1,802	412	3,515	1,193
Total production revenue	$ 12,951	$ 5,962	$ 32,218	$ 19,136
Average prices				
Natural gas ($/Mcf)	$ 3.87	$ 3.17	$ 4.31	$ 4.14
Realized natural gas hedge ($/Mcf)	0.26	4.52	0.48	3.56
Natural gas including realized hedge gains and losses ($/Mcf)	4.13	7.69	4.79	7.70
Crude Oil (per bbl)	70.47	66.85	72.36	61.00
Natural gas liquids (per bbl)	57.33	66.76	63.65	49.42
Average sales price before hedge (per boe)	$ 29.15	$ 26.10	$ 31.93	$ 29.35
Average sales price including hedge (per boe)	$ 30.47	$ 49.20	$ 34.42	$ 47.64

PRODUCTION

Production for the nine months ended September 30, 2010 averaged 3,428 boe/d compared to production of 1,471 boe/d in 2009. Production for the three months ended September 30, 2010 averaged 4,619 boe/d compared to production of 1,317 boe/d in the third quarter of 2009. The increase in production is due to property acquisitions completed in 2009, the acquisitions of Peloton and Temple completed in the second and third quarters of 2010, respectively, the acquisition of the Deep Basin Assets in the third quarter of 2010, as well as new drilling and recompletions in the first nine months of 2010. The Deep Basin Assets and Temple acquisitions were completed on September 8, 2010 and September 10, 2010, respectively. At the time of acquisition, the Deep Basin Assets were producing approximately 2,285 boe/d and Temple was producing approximately 2,680 boe/d for total acquired production of 4,965 boe/d. Since the acquisitions were completed late in the quarter, the effect was to increase production by approximately 1,165 boe/d for the quarter ended September 30, 2010. Consolidated production subsequent to the completion of the acquisitions was approximately 8,000 boe/d.

REVENUE

Total production revenue was $12,951 in the third quarter of 2010 compared to $5,962 for the comparable period in 2009. The increase in revenue is mainly attributable to the 251 percent increase in production, offset by a 38 percent decrease in realized sales prices. For the nine months ended September 30, 2010, total production revenue increased 68 percent to $32,218 from $19,136 in the prior year. The increase is the result of a 133 percent increase in production volumes, offset by a 28 percent decrease in realized sales prices.

PRICING

Cequence realized a natural gas price including hedging gain (as described below) for the three and nine month periods ended September 30, 2010 of $4.13 per Mcf and $4.79 per Mcf, respectively. The realized prices for the nine months ended September 30, 2010 are above prevailing market prices as 6,000 gj per day of the Company's natural gas production in the first quarter was sold at a price of $7.85 under a fixed price contract, which expired March 31, 2010. The Company also assumed commodity contracts on the acquisitions of Peloton and Temple for a total of 8,800 gj per day of natural gas in 2010 at prices ranging from $4.69 per gj to $5.75 per gj. Further, 2,800 Mcf/d of the Company's natural gas production in the nine months ended September 30, 2010 was sold at Chicago which was at a premium to AECO prices. Cequence's production is approximately 86 percent natural gas and consequently, fluctuations in natural gas prices have a significant impact on the Company.

Oil prices for the third quarter of 2010 were $70.47 per barrel, up 5 percent from the same time period in 2009. Oil prices for the nine months ended September 30, 2010 were $72.36, up 19 percent from the same period in 2009. Natural gas liquids prices for the third quarter of 2010 were $57.33 per barrel, down 14 percent from the same time period in 2009. Natural gas liquids prices for the nine months ended September 30, 2010 were $63.65 per barrel, up 29 percent from the same period in 2009.

Benchmark natural gas, crude oil and natural gas liquids prices were higher than the three and nine month comparative periods in 2009. The following table details the Company's benchmark indices:

	Three months ended September 30		Nine months ended September 30	
Benchmark Pricing	2010	2009	2010	2009
AECO –C Spot (CDN$/Mcf)	$ 3.53	$ 2.98	$ 4.11	$ 3.79
WTI crude oil (US$/bbl)	75.79	68.14	77.43	57.09
Edmonton par price (CDN$/bbl)	74.90	72.22	77.24	63.50
US$/CDN$ exchange rate	0.96	0.91	0.97	0.85

COMMODITY PRICE MANAGEMENT

Cequence has a commodity price risk management program which provides the Company flexibility to enter into derivative and physical commodity contracts to protect future cash flows for planned capital expenditures. The Company had a natural gas contract in place that expired in March 31, 2010 for the sale of 6,000 gj per day of natural gas for a price of $7.85 per gj. As part of the acquisition of Peloton, Cequence assumed natural gas contracts for the sale of 1,800 gj per day of natural gas at prices ranging from $4.69 per gj to $5.32 per gj. As part of the acquisition of Temple, Cequence assumed natural gas contracts for the sale of 11,000 gj per day of natural gas at prices ranging from $5.15 per gj to $6.20 per gj. The fair value of derivative commodity contracts at September 30, 2010 is $4,612 compared to $3,033 for the same quarter in 2009.

	Three months ended September 30		Nine months ended September 30	
	2010	2009	2010	2009
Realized gain on commodity contracts	$ 563	$ 2,800	$ 2,335	$ 7,346
Unrealized gain (loss) on commodity contracts	114	(2,422)	(1,348)	(1)
Total	$ 677	$ 378	$ 987	$ 7,345

ROYALTY EXPENSE

Royalty expense in the third quarter of 2010 was $1,340 or 11 percent of revenue compared to $1,170 or 37 percent of revenue in the third quarter of 2009. For the nine months ended September 30, 2010, royalties as a percentage of revenue were 11 percent compared to 20 percent in the comparative period in 2009. In the three and nine months ended September 30, 2009, there was a one-time adjustment to increase overriding royalties related to properties acquired in 2007 and adjustments reducing crown royalties related to previous periods. As a result, freehold and overriding royalties both as a percentage of revenue and on a per barrel basis are lower in the three and nine months ended September 30, 2010 than in the comparative periods in 2009. Crown royalties for the nine months ended September 30, 2010 are relatively consistent with the comparative period in 2009. Based on the nature of the Company's production and facilities, at current commodity prices Cequence reduces a significant portion of its crown royalties with gas cost allowance. Royalties as a percentage of revenue are in line with the Company's expectation of 10 percent of revenue for 2010.

	Three months ended September 30		Nine months ended September 30	
$(000's)	2010	2009	2010	2009
Crown	$ 981	$ (257)	$ 2,693	$ 831
Freehold / Overriding	359	1,427	460	1,524
	$ 1,340	$ 1,170	$ 3,153	$ 2,355
As a % of Revenue, Before Hedging Activity				
Crown	8%	(8)%	9%	7%
Freehold / Overriding	3%	45%	2%	13%
	11%	37%	11%	20%
Per Unit of Production ($/boe)				
Crown	$ 2.30	$ (2.12)	$ 2.88	$ 2.07
Freehold / Overriding	0.85	11.78	0.49	3.79
	$ 3.15	$ 9.66	$ 3.37	$ 5.86

TRANSPORTATION EXPENSE

Transportation costs for the nine months ended September 30, 2010 were $3.00 per boe, an increase of 52 percent from the comparative period in 2009 primarily due to the gas transportation contract described below. In the third quarter of 2010, transportation costs increased to $2.88 per boe from $2.55 per boe in the comparative period in 2009. Beginning in the fourth quarter of 2009, approximately 2,800 Mcf/d of natural gas is being shipped on the Alliance pipeline at a cost of $1.50 per Mcf for sale at Chicago. Cequence continues to expect that transportation will average $2.50 per boe for 2010 as costs on properties acquired through the acquisitions of Temple and the Deep Basin Assets are expected to be lower than Cequence's costs realized in the first nine months of 2010.

	Three months ended September 30		Nine months ended September 30	
$(000's)	2010	2009	2010	2009
Transportation ($)	$ 1,223	$ 309	$ 2,806	$ 794
Per Unit of Production ($/boe)	$ 2.88	$ 2.55	$ 3.00	$ 1.98

OPERATING COSTS

For the nine months ended September 30, 2010, operating costs decreased to $11.41 per boe from $17.69 in the comparative period in 2009. Operating costs during the third quarter of 2010 were $4,410 or $10.38 per boe compared to $2,609 or $21.53 per boe for the same time period in 2009. Operating costs decreased in the three and nine months ended September 30, 2010 compared to the same periods in 2009 due mainly to lower costs on new wells drilled and recompleted in the period and on wells acquired through the acquisitions of Peloton, Temple and the Deep Basin Assets. Operating costs for the nine months ended September 30, 2010 are in line with Cequence's expectation of approximately $11 to $13 per boe. Following the transactions completed in the third quarter, operating costs are expected to be $9 to $11 per boe for the fourth quarter of 2010.

	Three months ended September 30		Nine months ended September 30	
$(000's)	2010	2009	2010	2009
Operating Costs ($)	$ 4,410	$ 2,609	$ 10,677	$ 7,107
Per Unit of Production ($/boe)	$ 10.38	$ 21.53	$ 11.41	$ 17.69

OPERATING NETBACKS

Cequence's netback for the third quarter of 2010 decreased to $14.06 per boe from $15.46 per boe for the same period in 2009. For the nine months ended September 30, 2010 the netback decreased to $16.64 per boe from $22.11 per boe in the comparative period of 2009. In comparison to 2009, the decrease in the netback in the three and nine month periods is primarily due to a lower realized sales price resulting from the expiry of the Company's 6,000 gj/day commodity contract at March 31, 2010 offset by lower royalty expenses and operating costs.

Prior to hedging, Cequence's netbacks increased in both the three and nine month periods ended September 30, 2010 due to an increase in sales prices and a decrease in royalty expenses and operating costs.

	Three months ended September 30		Nine months ended September 30	
	2010	2009	2010	2009
Production revenue, including realized hedge gains (losses)	$ 30.47	$ 49.20	$ 34.42	$ 47.64
Royalty expense	(3.15)	(9.66)	(3.37)	(5.86)
Transportation Expense	(2.88)	(2.55)	(3.00)	(1.98)
Operating Costs	(10.38)	(21.53)	(11.41)	(17.69)
Netback, $/boe	$ 14.06	$ 15.46	$ 16.64	$ 22.11
Netback, excluding realized hedge gains (losses), $/boe	$ 12.74	$ (7.64)	$ 14.15	$ 3.82

GENERAL AND ADMINISTRATIVE EXPENSES

For the nine months ended September 30, 2010 general and administrative ("G&A") expenses decreased to $3,320 from $3,542 in 2009. On a per barrel basis, G&A expenses decreased for the nine months ended September 30, 2010 compared to 2009 to $3.55 per boe from $8.82 per boe, respectively, as the production base of the Company has increased and expenditures have decreased from the prior year. The reorganization of the Company in August 2009 led to a reduction in overall G&A expenses.

G&A expenses were $1,357 or $3.19 per boe for the three months ended September 30, 2010. On a per barrel basis, G&A expenses decreased 48 percent from the same period in 2009 as a result of increased sales volumes. G&A expenses for the year continue to be in line with Cequence's expectation of approximately $3.00 to $3.75 per boe in 2010.

	Three months ended September 30		Nine months ended September 30	
$(000's)	2010	2009	2010	2009
G&A Expenses ($)	$ 1,357	$ 745	$ 3,320	$ 3,542
Total G&A ($/boe)	$ 3.19	$ 6.15	$ 3.55	$ 8.82

REORGANIZATION EXPENSES

The three and nine months periods ended September 30, 2009 include all of the costs of the reorganization transaction completed on July 30, 2009. These one-time costs related primarily to the legal, investment banking and severance costs incurred to restructure the Company and totaled $3,295.

INTEREST EXPENSE

Interest expense for the three months ended September 30, 2010 was $952 compared to $474 for the comparative period in 2009. For the nine months ended September 30, 2010 interest expense was $1,240 compared to $1,237 in 2009. Included in interest expense for the three and nine months ended September 30, 2010 is $555 and $635, respectively, of transaction costs related to the establishment and renewal of the Company's credit facilities.

Interest expense net of the transaction costs described above was $397 and $605 for the three and nine month periods ended September 30, 2010, respectively, a decrease over the comparative periods in 2009. The decrease in interest expense, excluding transaction costs, in both periods is attributable to the decrease in average bank debt and lower interest rates. As part of the reorganization of Sabretooth, the Company repaid all of its outstanding current debt. The Company's debt did not increase to current levels until late in the third quarter of 2010, as debt was assumed on the acquisition of Temple and used in part to pay the cash consideration for the Deep Basin Assets. This resulted in interest expense decreasing in the first nine months of 2010 as compared to 2009.

	Three months ended September 30		Nine months ended September 30	
$(000's)	2010	2009	2010	2009
Interest Expense ($)	$ 397	$ 474	$ 605	$ 1,192
Transaction Costs ($)	555	-	635	45
Total Interest Expense ($)	$ 952	$ 474	$ 1,240	$ 1,237
Per Unit of Production ($/boe)	$ 2.24	$ 3.91	$ 1.33	$ 3.08

DEPLETION, DEPRECIATION AND AMORTIZATION ("DD&A")

DD&A expense for the three months ended September 30, 2010 was $8,428 or $19.83 per boe. For the nine months ended September 30, 2010, DD&A was $19,809 or $21.17 per boe. DD&A rates are lower than in the comparable periods in 2009 due mainly to drilling in the period and the acquisitions of Peloton, Temple and the Deep Basin Assets, which were completed at a lower cost per boe than Cequence's existing resource base.

	Three months ended September 30		Nine months ended September 30	
$(000's)	2010	2009	2010	2009
Depletion expense ($)	$ 8,428	$ 3,056	$ 19,809	$ 9,979
Per Unit of Production ($/boe)	$ 19.83	$ 25.22	$ 21.17	$ 24.84

ASSET RETIREMENT OBLIGATIONS

Total asset retirement obligations at September 30, 2010 were $14,547 compared to $4,059 at December 31, 2009. Net additions to asset retirement obligations in the first nine months of 2010 totalled $10,293 which relates to liabilities assumed on the acquisitions of Peloton, Temple and the Deep Basin Assets, liabilities sold on the sale of the Sinclair properties as well as to drilling activity, facility additions and changes in estimates. During the three and nine month periods ended September 30, 2010, the Company recorded accretion expense of $132 and $300, respectively (2009- $54 and $133, respectively).

STOCK-BASED COMPENSATION

The Company recognizes stock-based compensation expense for stock options and performance warrants. For the three months ended September 30, 2010, Cequence recorded $217 (2009 – negative $268) in stock-based compensation expense related to stock options, with a corresponding increase to contributed surplus. For the nine months ended September 30, 2010, stock-based compensation expense related to stock options was $690 compared to $60 in 2009.

The Company issued 10,483 options in the first nine months of 2010. Total stock-based compensation expense of $8,994 was determined using the Black-Scholes option pricing model and will be expensed over the four year vesting period of the options granted in the first six months of 2010 and over the three year vesting period of the options granted in the three months ended September 30, 2010.

As part of the reorganization of Sabretooth, certain officers and directors of the Company were awarded a total of 5,200 performance warrants that were exercisable into a non-voting share of Cequence at a price of $1.88. At the time the performance warrants were negotiated, the market price of the Company's shares was $1.48. The performance warrants were divided into three equal tranches with the first one-third having had a four year term and vested once the 20 day weighted average share price of Cequence exceeded $3.20. The second tranche had a 4.5 year term and vested if the 20 day weighted average share price of Cequence exceeded $4.40. The final third of the performance warrants had a five year term and vested if the 20 day weighted average share price of Cequence exceeded $5.60. The performance warrants were convertible to non-voting shares of Cequence.

During the three months ended September 30, 2010 these warrants were cancelled as part of the acquisition of Temple and any unrecognized stock based compensation expense was recognized in income. The cost to cancel the warrants of $451 was recognized as a transaction cost and capitalized as part of the acquisition of Temple.

The Company recognized $142 of stock based compensation for the performance warrants in the nine months ended September 30, 2010 (September 30, 2009 - $513).

COMMON SHARES OUTSTANDING

Issued common voting shares (000's)	Number	Stated Value
Balance, December 31, 2009	39,530	$ 267,908
Future income tax on renouncing expenditures for flow-through shares	-	(512)
Corporate acquisitions – Peloton	12,059	30,269
Flow-through share private placement	4,070	10,001
Subscription receipts	21,045	44,195
Corporate acquisition – Temple	46,846	106,809
Common share private placement	2,950	6,195
Share issue costs, net of taxes of $1,159	-	(3,344)
Balance, September 30, 2010	126,500	$ 461,521

As part of the reorganization transactions in the third quarter of 2009, the Company consolidated its common voting shares on a four for one basis. All historical amounts have been restated.

On October 26, 2009, the Company issued 500 common shares on a CDE "flow-through" basis for total proceeds of $2,025. In accordance with the terms of the agreement and pursuant to certain provisions of the Income Tax Act (Canada), the Company renounced, for income tax purposes, development expenditures of $2,025 to the holders of the flow-through common shares effective December 31, 2009. Future tax of approximately $512 associated with renouncing the expenditures was recorded on the date of renunciation in the first quarter of 2010. As at December 31, 2009, the Company had incurred all of the qualifying expenditures.

On June 11, 2010, the Company completed the acquisition of Peloton and issued 12,059 common voting shares with a deemed value of $2.51 per share for total deemed consideration of $30,269.

On August 19, 2010 the Company completed the sale of 3,200 shares on a CEE "flow-through" private placement basis at $2.50 per share for proceeds of $8,000 as well as 870 shares on a CDE "flow-through" private placement basis at $2.30 per share for proceeds of $2,001, resulting in a total issuance of 4,070 shares for total proceeds of $10,001. Under the terms of the respective agreements, Cequence is required to renounce $8,000 of CEE expenditures and $2,001 of CDE expenditures in February 2011. The qualifying CDE and CEE expenditures must be incurred by December 31, 2011 pursuant to the terms of the related agreements. As at September 30, 2010 the Company has not any incurred any of the qualifying CEE or CDE expenditures.

On August 19, 2010 the Company completed the sale of 18,545 subscription receipts at a price of $2.10 per subscription receipt for total proceeds of $38,945. The subscription receipts were convertible to Cequence common voting shares without further consideration upon the closing of the Deep Basin Assets acquisition. Upon closing of the Deep Basin Assets acquisition on September 8, 2010, the subscription receipts were converted on a one for one basis, for no additional consideration and without further action, into common voting shares of the Company. On September 17, 2010, Cequence completed the sale of 2,500 common voting shares related to an over-allotment option on the subscription receipts offering discussed above at $2.10 per share for total proceeds of $5,250.

On September 10, 2010, the Company completed the acquisition of Temple and issued 46,846 common voting shares with a deemed value of $2.28 per share for total deemed consideration of $106,809.

On September 10, 2010, Cequence completed the sale of 2,950 common voting shares through a private placement to a major shareholder as well as certain management and directors of the Company at $2.10 per share for total proceeds of $6,195.

As at September 30, 2010 there were no issued or outstanding non-voting shares (December 31, 2009 – none).

As of the date of this MD & A, Cequence had the following securities outstanding: 128,750 common voting shares, 10,831 stock options, 2,250 CDE flow-through 2011 Warrants and 2,250 CDE flow-through 2012 Warrants.

CAPITAL EXPENDITURES

	Three months ended September 30		Nine months ended September 30	
$(000's)	2010	2009	2010	2009
Property Acquisitions	$ 84,597	$ 15,763	$ 85,050	$ 15,763
Property Dispositions	(36,872)	-	(37,046)	-
Corporate Acquisitions [(1)]	2,387	320	3,083	320
Land, net	659	584	3,341	611
Geological & geophysical and capitalized overhead	1,272	270	2,013	1,212
Drilling, completions and workovers	5,024	2,102	29,056	5,391
Equipment and facilities	1,385	374	5,299	1,096
Office furniture & equipment	(31)	3	19	-
Total capital expenditures	$ 58,421	$ 19,416	$ 90,815	$ 24,393

(1) Corporate acquisitions for the nine months ended September 30, 2010 do not include $168,782 in non-cash items related to the acquisitions of Peloton and Temple.

For the nine months ended September 30, 2010, drilling, completion and workover expenditures totalled $29,056 which included 2.6 net horizontal wells and 3.5 net vertical wells. In addition, Cequence completed one net horizontal well and one net vertical well that were drilled in the fourth quarter of 2009. For the nine months ended September 30, 2009, drilling, completion and workover expenditures were limited to the completion of one horizontal well and one re-entry.

In the nine months ended September 30, 2010, the Company earned $2,401 in Alberta crown drilling credits that may be claimed against future crown royalties. The drilling credits are earned at a rate of $200 per metre of eligible drilling and can be claimed against Alberta crown royalties paid by Cequence between April 1, 2009 and March 31, 2011. No amount has been recognized in the September 30, 2010 financial statements for these credits as it is uncertain whether Cequence will incur sufficient Alberta crown royalties to claim these credits.

Cequence has budgeted capital expenditures of $115,000 for 2010, including acquisitions and dispositions, with 79% of expenditures occurring in the first three quarters. Capital expenditures will be funded out of cash flow and existing credit lines.

INCOME TAXES

At September 30, 2010, a future income tax asset of $26,690 (December 31, 2009 – $5,575) has been recognized as the Company believes, based on estimated cash flows, it is more likely than not to be realized. There is also a future income tax liability recognized at September 30, 2010 of $1,239 (December 31, 2009 – $424). At September 30, 2010, Cequence has the following tax pools:

Classification		Amount $(000's)
CEE	$	149,004
Non-capital losses		102,984
COGPE		91,618
UCC		72,544
CDE		51,079
SRED		22,704
Share issue costs		7,693
ITCs		3,051
	$	500,677

The non-capital losses expire $7,721 in 2013, $5,919 in 2014 and $89,344 in 2015 and thereafter.

Based on the Company's expected cash flow and available tax pools, Cequence does not expect to be taxable in 2010.

INVESTMENTS

As at December 31, 2009, the Company held long-term floating rate notes ("MAV 2" notes) issued as a result of the restructuring discussed below. At December 31, 2008, the Company held the original Canadian asset-backed commercial paper ("ABCP") with an original cost of $24,147. These investments matured during the third quarter of 2007 but, as a result of the liquidity issues in the ABCP market, did not settle on maturity.

On January 21, 2009, the Pan-Canadian Investors Committee announced that the restructuring had been completed to extend the maturity of the ABCP to provide for a maturity similar to that of the underlying assets. As a result, the Company received new replacement MAV 2 notes with a total face value of $24,142.

On August 25, 2010, the Company completed the sale of its entire interest in MAV 2 notes for net proceeds of $13,453 (net of transaction costs of $96) which represents approximately $0.68 per $1.00 of face value for the Class A1 notes, $0.58 per $1.00 of face value for the Class A2 notes, $0.33 per $1.00 of face value for the Class B notes and $0.05 per $1.00 of face value for the Class C notes. This has resulted in a loss on MAV 2 notes recognized in income of $647 and $281 for the three and nine months ended September 30, 2010.

LIQUIDITY AND CAPITAL RESOURCES

As at December 31, 2009, the Company had established two credit facilities with a Canadian chartered bank; a $40,000 revolving operating demand loan and a $5,000 non-revolving acquisition/development demand loan. During the three months ended September 30, 2010, the Company repaid all amounts owing and terminated the facilities.

During the three months ended September 30, 2010, the Company established two credit facilities with a syndicate of Canadian chartered banks. Credit facility A is a $100,000 extendible revolving term credit facility by way of prime loans, U.S. Base Rate Loans, Banker's Acceptances and Libor Loans. Credit facility B is a $10,000 operating facility by way of prime loans, U.S. Base Rate Loans, Banker's Acceptances and letters of credit. Prime loans and U.S. Base Rate Loans on these facilities bear interest at the bank prime rate or U.S. Base Rate, respectively, plus 1.25 percent to 2.75 percent on a sliding scale, depending on the Company's debt to adjusted EBITDA ratio (ranging from being less than or equal to 1.0:1.0 to greater than 2.5:1.0). Banker's Acceptances, Libor Loans and letters of credit on these facilities bear interest at the Banker's Acceptance rate, Libor rate or letter of credit rate, as applicable, plus 2.25 percent to 3.75 percent based on the same sliding scale as above. The credit facilities may be extended and revolve beyond the initial one-year period, if requested by the Company and accepted by the lenders. If the credit facilities do not continue to revolve, the facilities will convert to a 366-day non-revolving term loan facility.

Both credit facilities are subject to periodic review by the bank and are secured by a general assignment of book debts and a $250,000 demand debenture with a first floating charge over all assets of the Company. The Company is permitted to hedge up to 67 percent of its production under the lending agreement. As at September 30, 2010, the Company has drawn $57,352 under the extendible revolving term credit facility and $nil under the operating facility (December 31, 2009 – $nil drawn under demand credit facilities) and is in compliance with all covenants. The next scheduled review is to take place in May 2011.

Included in interest expense in the consolidated statement of operations is $555 of transaction costs related to the Company's credit facilities established in the three months ended September 30, 2010.

On March 31, 2009, the Company's bank provided the Company with an additional credit facility to provide liquidity in respect to the MAV 2 notes. All proceeds from the sale of MAV 2 notes were used to repay this facility. The balance of the facility was paid with available cash and the long-term debt related to investments facility was closed. The effective interest rate for the three and nine month periods ended September 30, 2010 was 1.18 and 1.19 percent, respectively. Interest expense on long-term debt related to investments included as interest expense in the consolidated statement of operations for the three and nine month periods ended September 30, 2010 was $33 and $129 ($51 and $103 for the three and nine months ended September 30, 2009, respectively).

CONTRACTUAL OBLIGATIONS

	2010	2011	2012	2013	2014+	Total
Office leases	$ 243	973	583	482	763	$ 3,044
Pipeline transportation	402	1,594	1,594	1,594	3,052	8,236
Drilling services commitment	1,018	1,500	-	-	-	2,518
Total	$ 1,663	4,067	2,177	2,076	3,815	$ 13,798

The Company acquired a pipeline transportation contract in a property acquisition that expires on November 30, 2015.

The Company has a commitment to use the drilling and related services of the Claimant of a lawsuit settled in the first quarter of 2010, at fair market value, in the amount of $3,000 over the two years following the date of settlement. Cequence is obligated to spend a minimum of $1,500 in each of the two years following the date of settlement to avoid any penalties under the commitment. Cequence has incurred $482 as at September 30, 2010.

DISCLOSURE CONTROLS AND INTERNAL CONTROLS OVER FINANCIAL REPORTING

The President and Chief Executive Officer and the Vice President, Finance and Chief Financial Officer are responsible for designing internal controls over financial reporting or causing them to be designed under their supervision in order to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with Canadian GAAP. The Company'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 the Company's Chief Executive Officer and Chief Financial Officer by others, particularly during the period in which the annual 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.

The Committee of Sponsoring Organizations ("COSO") framework provides the basis for management's design of internal controls over financial reporting. Management and the Board work to mitigate the risk of a material misstatement in financial reporting; however, a control system, no matter how well conceived or operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met and it should not be expected that the disclosure and internal control procedures will prevent all errors or fraud.

As at September 30, 2010, the Chief Executive Officer and the Chief Financial Officer have concluded, based on their evaluation of the design and operating effectiveness of the Company's disclosure controls and internal controls over financial reporting ("ICFR") that disclosure controls and ICFR are effective.

QUARTERLY INFORMATION

FINANCIAL ($ thousands except per share data)	2010 Q3	2010 Q2	2010 Q1	2009 Q4	2009 Q3	2009 Q2	2009 Q1	2008 Q4
Production Revenues including realized gains (losses) on financial commodity contract	$12,951	$ 9,174	$10,093	$ 8,847	$ 5,962	$ 6,548	$ 6,627	$ 8,079
Royalties	1,340	699	1,114	809	1,170	385	800	894
Operating expenses	4,410	3,392	2,875	2,702	2,609	2,212	2,286	2,831
Transportation expenses	1,223	840	744	781	309	238	247	342
Reorganization expenses	-	-	-	-	3,295	-	-	-
Net income (loss)	(3,620)	(3,751)	(1,025)	(2,656)	(6,994)	(2,444)	3,440	(987)
Per share – basic	(0.05)	(0.09)	(0.03)	(0.07)	(0.26)	(0.25)	0.36	(0.10)
Per share – diluted	(0.05)	(0.09)	(0.03)	(0.07)	(0.26)	(0.25)	0.36	(0.10)
Funds flow	3,695	2,842	4,498	3,161	(2,663)	1,517	1,913	1,278
Per share – basic	0.05	0.07	0.11	0.08	(0.10)	0.16	0.20	0.13
Per share – diluted	0.05	0.07	0.11	0.08	(0.10)	0.16	0.20	0.13
Capital expenditures, net	8,309	5,007	26,412	16,526	3,334	209	4,767	6,024
Acquisitions, net (1)	50,112	695	279	6,374	15,421	-	-	(14,437)
Total expenditures	$58,421	$ 5,702	$26,691	$22,900	$18,755	$ 209	$ 4,767	$ (8,413)

(1) Acquisitions for the three months ended September 30, 2010 do not include $140,109 in non-cash items related to the acquisition of Temple.

OPERATIONS	2010 Q3	2010 Q2	2010 Q1	2009 Q4	2009 Q3	2009 Q2	2009 Q1	2008 Q4
Production Volumes								
Natural gas (Mcf/d)	23,674	16,559	12,592	10,696	6,734	8,077	8,164	9,480
Oil (bbl/d)	332	253	268	230	128	106	140	186
NGLs (bbl/d)	342	184	78	76	67	96	104	122
Total (boe/d)	4,619	3,197	2,444	2,089	1,317	1,548	1,602	1,887
Average selling price								
Natural gas ($per Mcf)	4.13	4.21	6.83	6.97	7.69	7.50	7.71	7.34
Oil ($per bbl)	70.47	70.22	76.80	71.65	66.85	68.00	50.26	53.55
NGLs ($per bbl)	57.33	72.07	71.81	68.82	66.76	52.12	35.28	67.98
Combined ($per boe)	30.47	31.53	45.88	46.05	49.20	47.00	45.97	46.52
Royalties ($per boe)	3.15	2.40	5.06	4.21	9.66	2.76	5.55	5.15
Operating expenses ($per boe)	10.38	11.66	13.07	14.06	21.53	15.88	15.86	16.30
Transportation ($per boe)	2.88	2.88	3.38	4.07	2.55	1.71	1.71	1.97
Netback ($per boe)	14.06	14.59	24.37	23.71	15.46	26.65	22.85	23.10

FUTURE ACCOUNTING PRONOUNCEMENTS

The Company has assessed new and revised accounting pronouncements that have been issued that are not yet effective and determined that the following may have an impact on the Company:

I) INTERNATIONAL FINANCIAL REPORTING STANDARDS

On January 1, 2011 International Financial Reporting Standards ("IFRS") will become the generally accepted accounting principles in Canada. The adoption date of January 1, 2011 will require the restatement, for comparative purposes, of amounts reported by Cequence for the year ended December 31, 2010, including the opening balance sheet as at January 1, 2010. Throughout 2009 and 2010 the Company has assessed the impact of adopting IFRS and is continuing to implement plans for transition. The project is being managed by in-house accounting professionals who have engaged in IFRS educational programs and continue to develop the Company's adoption to IFRS. The Company's auditors will be involved throughout the process to ensure the Company's policies are in accordance with these new standards.

In July 2009 an amendment to IFRS 1 First Time Adoption of International Financial Reporting Standards was issued that applies to oil and gas assets. The amendment allows an entity that used full cost accounting under its previous GAAP to elect, at its time of adoption, to measure exploration and evaluation assets at the amount determined under the entity's previous GAAP and to measure oil and gas assets in the development and production phases by allocating the amount determined under the entity's previous GAAP for those assets to the underlying assets pro rata using reserve volumes or reserve values as of that date. Cequence currently anticipates that it will use this exemption. IFRS 1 also provides a number of other optional exemptions and mandatory exceptions in certain areas to the general requirement for full retrospective application. Management is analyzing the various accounting policy choices available and will implement those determined to be the most appropriate for the Company which other than the full cost accounting exemption noted above are:

Business Combinations – IFRS 1 would allow Cequence to use the IFRS rules for business combinations on a prospective basis rather than re-stating all business combinations prior to the transition date.

Borrowing Costs – IFRS 1 would allow Cequence to apply the transitional provisions of IAS 23 in lieu of full retrospective application.

Share-based payments – IFRS 1 would allow Cequence an exemption on IFRS 2, "Share-Based Payments" to equity instruments which vested before Cequence's transition date to IFRS.

Decommissioning Liabilities – IFRS 1 would allow Cequence to measure decommissioning liabilities as at the transition date in accordance with IAS 37, "Provisions, Contingent Liabilities and Contingent Assets" and recognize directly in deficit the difference between that amount and the carrying amount of those liabilities at the date of transition determined under Canadian GAAP.

Cequence currently plans to use these exemptions.

The transition from Canadian GAAP to IFRS is significant and may materially affect our reported financial position and results of operations. At this time, Cequence has identified key differences that will impact the financial statements:

- *Exploration and Evaluation ("E&E") expenditures* – On transition to IFRS Cequence will re-classify all E&E expenditures that are currently included in the PP&E balance on the Consolidated Balance Sheet. Based on Cequence's anticipated policy related to IFRS 6 "Exploration for and Evaluation of Mineral Resources" ("IFRS 6"), the Company does not expect to recognize any E&E assets at the date of transition. Any E&E assets subsequently recognized will not be depleted and must be assessed for impairment when indicators of impairment exist.
- *Property and equipment* – This includes oil and gas assets in the development and production phases and Cequence currently expects that the entire full cost pool will be allocated to property and equipment on transition to IFRS. The Company has allocated the amount recognized under current Canadian GAAP as at January 1, 2010 using discounted proved plus probable reserve values to the assets at an area level. Cequence is evaluating the outcome of each calculation.
- *Depletion expense* – On transition to IFRS Cequence has the option to base the depletion calculation on either proved reserves or proved plus probable reserves. Cequence expects to base the depletion calculation on proved plus probable reserves.
- *Impairment of PP&E assets* – Under IFRS, impairment tests of PP&E must be performed on specific portions of PP&E as opposed to the entire PP&E balance which is currently required under Canadian GAAP through the full cost ceiling test. Impairment calculations will be performed at the cash generating unit level using proved plus probable reserves. Cequence has determined its cash generating units for the purpose of impairment testing and anticipates using proved plus probable values for impairment tests.
- *Provisions* – The major difference between the current Canadian GAAP standard and IFRS, as it affects Cequence, relates to the discount rate used to measure the Company's decommissioning liabilities. Under current Canadian GAAP a credit-adjusted risk-free rate is used, whereas the IFRS standard indicates the use of a risk-free rate. A lower discount rate will increase the decommissioning liability on the date of transition and the difference will be charged to deficit.
- *Flow-through shares* – Under Canadian GAAP, the proceeds from the issuance of flow-through shares are recognized as shareholders' equity. Further, the tax basis of assets related to expenditures incurred to satisfy flow-through share obligations is not reduced until the renunciation of the related tax pools at which time, the expected tax effect of the renunciation has the effect of increasing future income tax liability and reducing shareholders' equity.

  Under IFRS, the difference between the value of a flow-through share issuance and the value of a common share issuance is initially accrued as an obligation on issuance of the flow-through shares. Pursuant to the terms of the flow-through share agreements, the tax deductions associated with the expenditures are renounced to the subscribers. Accordingly, on renunciation with the Canada Revenue Agency, a future tax liability is recorded equal to the estimated amount of future income taxes payable by the Company. As a result of the renunciations, the obligation on issuance of flow-through shares is reduced and the difference is recognized in net income (loss). Cequence currently expects that the above will result in an increase to share capital, an increase to deficit and the recognition of an obligation on flow-through shares not yet renounced at the date of transition. Cequence continues to evaluate the amount of such adjustments.

- *Share based payments* – The Company has evaluated its share based payment awards and has determined that they are in compliance with IFRS. As such, no significant changes are expected related to share based payments on transition to IFRS.

In addition to the accounting policy differences above, Cequence's transition to IFRS will impact the internal controls over financial reporting, the disclosure controls and procedures and information technology systems as follows:

Internal controls over financial reporting – As the review and analysis of Cequence's accounting policies under IFRS is completed, an assessment will be made to determine the changes required to internal controls over financial reporting. This will be an ongoing process in 2010 to ensure that changes in accounting policies include the appropriate additional controls and procedures for future IFRS reporting requirements.

Disclosure controls and procedures – Throughout the transition process, Cequence will be assessing stakeholders' information requirements and will ensure that adequate and timely information is provided while ensuring the Company maintains its due process regarding information that is disclosed.

Information Technology systems – The Company has assessed the readiness of its accounting software and continues to assess other system requirements that may be needed in order to perform ongoing calculations and analysis under IFRS. These changes are not considered to be significant.

Management is continuing to finalize its accounting policies and choices and is continuing with its due process in regards to information that is disclosed. As such, the Company is currently unable to quantify the full impact on the financial statements of adopting IFRS, however, the Company has disclosed certain expectations above based on information known to date. Due to anticipated changes to IFRS and International Accounting Standards prior to Cequence's adoption of IFRS, certain items may be subject to change based on new facts and circumstances that arise after the date of this MD & A.

CURRENT ECONOMIC CONDITIONS

Recent market events and conditions, including disruptions in the international credit markets and other financial systems and the deterioration of global economic conditions, have caused significant volatility to commodity prices. These conditions persisted throughout 2009 and 2010, causing a loss of confidence in the global credit and financial markets and resulting in the collapse of, and government intervention in, major banks, financial institutions and insurers and creating a climate of greater volatility, less liquidity, widening of credit spreads, a lack of price transparency, increased credit losses and tighter credit conditions. Notwithstanding various actions by governments, concerns about the general condition of the capital markets, financial instruments, banks, investment banks, insurers and other financial institutions caused the broader credit markets to further deteriorate and stock markets to decline substantially. These factors have negatively impacted company valuations and will impact the performance of the global economy going forward. Petroleum and natural gas prices are expected to remain volatile for the near future as a result of market uncertainties over the supply and demand of these commodities due to the current state of the world economies, OPEC actions and the ongoing global credit and liquidity concerns.

ROYALTY REGIMES

Alberta

On March 11, 2010 the Alberta government announced further changes to its royalty regime which will take effect beginning January 1, 2011, as a result of its "Competitiveness Review". The key changes are: 1) the current incentive program of five percent for the first year of production on new natural gas and conventional oil wells will become permanent with the current time and volume limits; 2) the maximum royalty rate for conventional oil will be reduced at higher price levels from 50 percent to 40 percent; 3) the maximum royalty rate for conventional and unconventional natural gas will be reduced at higher price levels from 50 percent to 36 percent; and 4) the transitional royalty framework will continue until its original announced expiration on December 31, 2013, however, effective January 1, 2011, no new wells will be allowed to select the transitional royalty rates.

On May 27, 2010 the Alberta government released the new royalty curves associated with the changes announced on March 11, 2010, which determine the royalty rates at certain commodity price levels, and revised the natural gas deep drilling credit to wells deeper than 2,000 metres, compared to 2,500 metres previously. The deep drilling credit is $625 per metre for wells between 2,000 metres and 3,500 metres with higher rates thereafter, increasing incrementally with increased depth. The Alberta government also announced an extension to the five percent new well rate to 18 production months and a volume limit of 500 MMcf for horizontal gas wells and time and volume limit extensions on horizontal oil wells, dependent on depth.

FORWARD-LOOKING STATEMENTS

Certain statements contained within this MD & A constitute forward-looking statements. These statements relate to future events or our future performance. All statements other than statements of historical fact may be forward-looking statements. Forward-looking statements are often, but not always, identified by the use of words such as “seek”, “anticipate”, “budget”, “plan”, “continue”, “estimate”, “expect”, “forecast”, “may”, “will”, “project”, “predict”, “potential”, “targeting”, “intend”, “could”, “might”, “should”, “believe”, and similar expressions. Forward-looking statements in this MD & A include, but are not limited to, statements with respect to: the potential impact of implementation of the Alberta Royalty Framework on Cequence’s condition and projected 2010 capital investments; projections with respect to growth of natural gas production; the projected impact of land access and regulatory issues; projections relating to the volatility of crude oil and natural gas prices in 2010 and beyond and reasons therefore; the Company’s projected capital investment levels for 2010 and the source of funding therefore; the effect of the Company’s risk management program, including the impact of derivative financial instruments; the Company’s defence of lawsuits; the impact of the climate change initiatives on operating costs; the impact of Western Canada pipeline constraints. Readers are cautioned not to place undue reliance on forward-looking statements, as there can be no assurance that the plans, intentions or expectations upon which they are based will occur.

By their nature, forward-looking statements involve numerous assumptions, known and unknown risks and uncertainties, both general and specific, that contribute to the possibility that the predictions, forecast, projections and other forward-looking statements will not occur, which may cause the Company’s actual performance and financial results in future periods to differ materially from any estimates or projections of future performance or results expressed or implied by such forward-looking statements. These assumptions, risks and uncertainties include, among other things: volatility of and assumptions regarding oil and natural gas prices; assumptions based upon Cequence’s current guidance; fluctuations in currency and interest rates; product supply and demand; market competition; risk inherent in the Company’s marketing operations, including credit risks; imprecision of reserves estimates and estimates of recoverable quantities of oil, natural gas and liquids from resource plays and other sources not currently classified as proved; the Company’s ability to replace and expand oil and gas reserves; the Company’s ability to generate sufficient cash flow from operations to meet its current and future obligations; the Company’s ability to access external sources of debt and equity capital; the timing and cost of well and pipeline constructions; the Company’s ability to secure adequate product transportation; changes in royalty, tax, environmental and other laws or regulations or the interpretations of such laws or regulations; risks associated with existing and potential future lawsuits and regulatory actions made against the Company; and other risks and uncertainties described from time to time in the reports and filings made with securities regulatory authorities by Cequence. Statements relating to “reserves” are deemed to be forward-looking statements, as they involve the implied assessment, based on certain estimates and assumptions that the resources and reserves described can be profitably produced in the future.

The forward looking statements contained herein concerning production, sales prices, and capital spending are based on Cequence’s 2010 capital program, as revised for acquisitions and dispositions completed in the third quarter of 2010. The material assumptions supporting the 2010 capital program are: i) 2010 annual production of approximately 4,700 boe/day; ii) a $3.79 CAD/gj AECO gas price; iii) capital spending of approximately $115,000, including acquisitions and dispositions, in 2010.

Financial outlook information contained in this MD & A about prospective results of operations, financial position or cash flows is based on assumptions about future events, including economic conditions and proposed courses of action, based on management’s assessment of the relevant information currently available. The purpose of such financial outlook is to enrich this MD & A. Readers are cautioned that such financial outlook information contained in this MD & A should not be used for purposes other than for which it is disclosed herein.

Although Cequence believes that the expectations represented by such forward-looking statements are reasonable, there can be no assurance that such expectation will prove to be correct. Readers are cautioned that the foregoing list of important factors is not exhaustive. Furthermore, the forward-looking statements contained in this MD & A are made as of the date of this MD & A, and except as required by law Cequence 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. The forward-looking statements contained in this MD & A are expressly qualified by this cautionary statement.

CEQUENCE ENERGY LTD.

CONSOLIDATED FINANCIAL STATEMENTS

CONSOLIDATED BALANCE SHEETS

(Unaudited)

(Expressed in thousands of Canadian dollars)	September 30, 2010 $	December 31, 2009 $
ASSETS		
CURRENT		
Cash	463	18,128
Accounts receivable	14,806	10,144
Deposits and prepaid expenses	2,775	913
Commodity contracts (Note 14)	4,612	1,420
	22,656	30,605
Investments (Note 5)	-	13,920
Property and equipment (Note 6)	401,639	158,011
Future income taxes	26,690	5,575
	450,985	208,111
LIABILITIES		
CURRENT		
Demand credit facilities (Note 7)	57,352	-
Accounts payable and accrued liabilities	29,549	23,175
Future income taxes	1,239	424
	88,140	23,599
Long-term debt related to investments (Note 5)	-	18,204
Asset retirement obligations (Note 8)	14,547	4,059
	102,687	45,862
CONTINGENCIES AND COMMITMENTS (Note 13) SUBSEQUENT EVENTS (Note 17)		
SHAREHOLDERS' EQUITY		
Share capital (Note 9)	461,521	267,908
Contributed surplus (Note 11)	8,650	7,818
Deficit	(121,873)	(113,477)
	348,298	162,249
	450,985	208,111

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

APPROVED BY THE BOARD

"Donald Archibald"	Donald Archibald, Director
"Brian Felesky"	Brian Felesky, Director

CEQUENCE ENERGY LTD.

CONSOLIDATED FINANCIAL STATEMENTS

CONSOLIDATED STATEMENTS OF OPERATIONS, COMPREHENSIVE LOSS AND DEFICIT

(Unaudited)

(Expressed in thousands of Canadian dollars except per share amounts)	Three months ended September 30, 2010 $	Three months ended September 30, 2009 $	Nine months ended September 30, 2010 $	Nine months ended September 30, 2009 $
REVENUE				
Production revenue	12,388	3,162	29,883	11,790
Royalties	(1,340)	(1,170)	(3,153)	(2,355)
Realized gain on derivative financial instruments (Note 14)	563	2,800	2,335	7,346
Unrealized gain (loss) on derivative financial instruments (Note 14)	114	(2,435)	(1,348)	(28)
Other income (expense)	26	-	(20)	-
	11,751	2,357	27,697	16,753
EXPENSES				
Accretion expense (Note 8)	132	54	300	133
Depletion, depreciation, and amortization (Note 6)	8,428	3,056	19,809	9,979
General and administrative (Note 6)	1,357	745	3,320	3,542
Interest	952	474	1,240	1,237
Operating costs	4,410	2,609	10,677	7,107
Reorganization expenses	-	3,295	-	3,295
Stock-based compensation (Note 10)	342	245	832	573
Transportation	1,223	309	2,806	794
Loss on investment (Note 5)	647	544	281	544
	17,491	11,331	39,265	27,204
LOSS BEFORE INCOME TAXES	(5,740)	(8,974)	(11,568)	(10,451)
INCOME TAXES	(2,120)	(1,929)	(3,172)	(4,465)
LOSS BEFORE NON-CONTROLLING INTEREST	(3,620)	(7,045)	(8,396)	(5,986)
Non-controlling interest	-	51	-	(12)
NET LOSS AND COMPREHENSIVE LOSS	(3,620)	(6,994)	(8,396)	(5,998)
DEFICIT, BEGINNING OF PERIOD	(118,253)	(103,827)	(113,477)	(104,823)
DEFICIT, END OF PERIOD	(121,873)	(110,821)	(121,873)	(110,821)
Net Loss per share, basic and diluted (Note 12)	$ (0.05)	$ (0.26)	$ (0.17)	$ (0.39)

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

CEQUENCE ENERGY LTD.

CONSOLIDATED FINANCIAL STATEMENTS

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

(Expressed in thousands of Canadian dollars)	Three months ended September 30, 2010 $	Three months ended September 30, 2009 $	Nine months ended September 30, 2010 $	Nine months ended September 30, 2009 $
CASH FLOWS RELATED TO THE FOLLOWING ACTIVITIES:				
OPERATING				
Net loss	(3,620)	(6,994)	(8,396)	(5,998)
Adjustments for non-cash items:				
Depletion, depreciation, and amortization	8,428	3,056	19,809	9,979
Accretion expense	132	54	300	133
Stock-based compensation	342	245	832	573
Loss on investment (Note 5)	647	544	281	544
Unrealized loss (gain) on derivative financial instruments (Note 14)	(114)	2,435	1,348	28
Write-down and amortization of loan premium and other derivative financial instruments	-	(16)	32	(33)
Future income tax recovery	(2,120)	(1,936)	(3,170)	(4,472)
Non-controlling interest	-	(51)	-	12
	3,695	(2,663)	11,036	766
Asset retirement expenditures (Note 8)	(39)	-	(105)	(17)
Net change in non-cash working capital (Note 15)	1,944	1,018	(4,738)	1,628
	5,600	(1,645)	6,193	2,377
INVESTING				
Corporate acquisitions (Note 2)	(2,387)	342	(3,083)	342
Property and equipment expenditures	(8,309)	(3,334)	(39,728)	(8,310)
Acquisition of assets (Note 3)	(84,597)	(15,763)	(85,050)	(15,763)
Proceeds from sale of assets (Note 4)	36,872	-	37,046	-
Proceeds from sale of Investments (Note 5)	13,453	-	13,457	-
Net change in non-cash working capital (Note 15)	389	1,554	(705)	(612)
	(44,579)	(17,201)	(78,063)	(24,343)
FINANCING				
Proceeds from demand credit facilities	20,929	-	36,396	-
Repayment of demand credit facilities	(20,451)	(29,740)	(20,451)	(47,970)
Proceeds from long-term debt related to investments	-	-	-	18,120
Repayment of long-term debt related to investments	(18,000)	-	(18,054)	-
Issue of common shares	60,391	65,315	60,391	65,315
Share issue costs	(4,453)	(3,138)	(4,503)	(3,168)
Repurchase of common shares under NCIB	-	-	-	(85)
Net change in non-cash working capital (Note 15)	426	315	426	-
	38,842	32,752	54,205	32,212
NET INCREASE (DECREASE) IN CASH	(137)	13,906	(17,665)	10,246
CASH, BEGINNING OF PERIOD	600	11,777	18,128	15,437
CASH, END OF PERIOD	463	25,683	463	25,683
SUPPLEMENTARY INFORMATION				
Income taxes paid	-	7	-	7
Interest paid	735	323	1,320	1,102

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

CEQUENCE ENERGY LTD.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

THREE AND NINE MONTH PERIODS ENDED SEPTEMBER 30, 2010

(All figures expressed in thousands except per share amounts unless otherwise noted)

1. BASIS OF PRESENTATION

These interim consolidated financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles ("Canadian GAAP") and follow the same accounting policies as the most recent audited annual financial statements. The disclosures provided below are incremental to those included with the annual consolidated financial statements and certain disclosures, which are normally required to be included in the notes to the annual consolidated financial statements, have been condensed or omitted. These interim consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto in the Company's annual filings for the year ended December 31, 2009.

These statements include all assets, liabilities, revenues and expenses of Cequence Energy Ltd. ("Cequence" or the "Company") and its wholly-owned subsidiaries, 1175043 Alberta Ltd. and Cequence Acquisitions Ltd. These statements further include the results of Peloton Exploration Corp. ("Peloton") from the date of acquisition on June 11, 2010 (see note 2). Effective July 1, 2010, Peloton was amalgamated with Cequence and the combined entity was continued as Cequence Energy Ltd.

2. CORPORATE ACQUISITIONS

a) Purchase of Peloton

On June 11, 2010, the Company acquired all of the issued and outstanding shares of Peloton, a private oil and gas company, for consideration of 12,059 common voting shares. The shares were valued based on Cequence's five day weighted average trading price on the TSX before and after the announcement of the transaction. The transaction was accounted for using the purchase method whereby the assets acquired and liabilities assumed are recorded at their fair value. The accounts of the Company include the results of Peloton effective June 11, 2010.

The purchase price allocation is as follows:

Cost of Acquisition	($000's)
Common shares (12,059 at $2.51)	30,269
Transaction costs	645
Total	**30,914**

Fair Value of the Assets and Liabilities Acquired	($000's)
Property and equipment	29,319
Fair value of commodity contracts	339
Bank debt	(4,984)
Working capital deficiency	(1,031)
Asset retirement obligations	(552)
Future income tax assets – non-current	7,918
Future income tax liabilities – current	(95)
Total	**30,914**

The attributed values of the common voting shares issued have been excluded from the consolidated statement of cash flows as a non-cash transaction.

b) Purchase of Temple

On September 10, 2010, the Company acquired all of the issued and outstanding shares of Temple Energy Inc. ("Temple"), a private oil and gas company, for consideration of 46,846 common voting shares. The acquisition was effected by way of a plan of arrangement, whereby Cequence Acquisitions Ltd., a newly formed subsidiary of the Company, was amalgamated with Temple and continued as Cequence Acquisitions Ltd. The shares were valued based on Cequence's five day weighted average trading price on the TSX before and after the announcement of the transaction. The transaction was accounted for using the purchase method whereby the assets acquired and liabilities assumed are recorded at their fair value. The accounts of the Company include the results of Cequence Acquisitions Ltd. effective September 10, 2010.

CEQUENCE ENERGY LTD.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

THREE AND NINE MONTH PERIODS ENDED SEPTEMBER 30, 2010

(All figures expressed in thousands except per share amounts unless otherwise noted)

2. CORPORATE ACQUISITIONS (CONTINUED)

b) Purchase of Temple (continued)

The estimated purchase price allocation is as follows:

Cost of Acquisition	($000's)
Common shares (46,846 at $2.28)	106,809
Transaction costs	2,438
Total	109,247

Fair Value of the Assets and Liabilities Acquired	($000's)
Property and equipment	142,546
Fair value of commodity contracts	4,201
Bank debt	(36,423)
Working capital deficiency	(3,834)
Asset retirement obligations	(5,902)
Future income tax assets – non-current	9,842
Future income tax liabilities – current	(1,183)
Total	109,247

The attributed values of the common voting shares issued have been excluded from the consolidated statement of cash flows as a non-cash transaction.

3. PROPERTY ACQUISITION

On September 8, 2010, the Company closed the acquisition of certain gas weighted properties located in the Simonette area of Northwest Alberta (the "Deep Basin Assets"). The purchase price, subject to final adjustments, was $85,000. An asset retirement obligation of $3,683 has been recognized as part of the acquisition.

The results of operations from these properties have been included in the consolidated financial statements from the closing date of the acquisition. The acquisition was financed through a series of equity issuances (see note 9) and available cash.

4. PROPERTY DISPOSITION

On July 27, 2010, Cequence sold certain non-producing gas weighted properties in the Sinclair region of Northwest Alberta for total cash consideration of $36,900, subject to final adjustments. No gain or loss resulted on the sale as the sale did not change the depletion rate of the Company by more than 20 percent.

5. INVESTMENTS AND LONG-TERM DEBT RELATED THERETO

As at December 31, 2009, the Company held long-term floating rate notes ("MAV 2" notes) issued as a result of the restructuring discussed below. At December 31, 2008, the Company held the original Canadian asset-backed commercial paper ("ABCP") with an original cost of $24,147. These investments matured during the third quarter of 2007 but, as a result of the liquidity issues in the ABCP market, did not settle on maturity.

On January 21, 2009, the Pan-Canadian Investors Committee announced that the restructuring had been completed to extend the maturity of the ABCP to provide for a maturity similar to that of the underlying assets. As a result, the Company received new replacement MAV 2 notes with a total face value of $24,142.

On August 25, 2010, the Company completed the sale of its entire interest in MAV 2 notes for net proceeds of $13,453 (net of transaction costs of $96) which represents approximately $0.68 per $1.00 of face value for the Class A1 notes, $0.58 per $1.00 of face value for the Class A2 notes, $0.33 per $1.00 of face value for the Class B notes and $0.05 per $1.00 of face value for the Class C notes. This has resulted in a loss on MAV 2 notes recognized in income of $647 and $281 for the three and nine months ended September 30, 2010.

CEQUENCE ENERGY LTD.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

THREE AND NINE MONTH PERIODS ENDED SEPTEMBER 30, 2010

(All figures expressed in thousands except per share amounts unless otherwise noted)

5. INVESTMENTS AND LONG-TERM DEBT RELATED THERETO (CONTINUED)

All proceeds from the sale of MAV 2 notes were used to repay the long term debt related to investments facility. The balance of the facility was paid with available cash and the long-term debt related to investments facility was closed. The effective interest rate for the three and nine month periods ended September 30, 2010 was 1.18 and 1.19 percent. Interest expense on long-term debt related to investments included as interest expense in the consolidated statement of operations for the three and nine month periods ended September 30, 2010 was $33 and $129 ($51 and $103 for the three and nine months ended September 30, 2009, respectively).

6. PROPERTY AND EQUIPMENT

	September 30, 2010	December 31, 2009
Petroleum and natural gas properties	487,962	224,525
Accumulated Depletion, Depreciation and Amortization	(86,323)	(66,514)
	401,639	158,011

Unproved properties not subject to depletion amounted to approximately $52,579 at September 30, 2010 (September 30, 2009 – $18,650).

The Company capitalized general and administrative costs related to exploration and development of approximately $nil for the nine month period ended September 30, 2010 (September 30, 2009 – $1,185).

Costs subject to depletion include $116,157 of estimated future capital costs (September 30, 2009 – $17,938).

7. DEMAND CREDIT FACILITIES

As at December 31, 2009, the Company had established two credit facilities with a Canadian chartered bank; a $40,000 revolving operating demand loan and a $5,000 non-revolving acquisition/development demand loan. During the three months ended September 30, 2010, the Company repaid all amounts owing and terminated the facilities.

During the three months ended September 30, 2010, the Company established two credit facilities with a syndicate of Canadian chartered banks. Credit facility A is a $100,000 extendible revolving term credit facility by way of prime loans, U.S. Base Rate Loans, Banker's Acceptances and Libor Loans. Credit facility B is a $10,000 operating facility by way of prime loans, U.S. Base Rate Loans, Banker's Acceptances and letters of credit. Prime loans and U.S. Base Rate Loans on these facilities bear interest at the bank prime rate or U.S. Base Rate, respectively, plus 1.25 percent to 2.75 percent on a sliding scale, depending on the Company's debt to adjusted EBITDA ratio (ranging from being less than or equal to 1.0:1.0 to greater than 2.5:1.0). Banker's Acceptances, Libor Loans and letters of credit on these facilities bear interest at the Banker's Acceptance rate, Libor rate or letter of credit rate, as applicable, plus 2.25 percent to 3.75 percent based on the same sliding scale as above. The credit facilities may be extended and revolve beyond the initial one-year period, if requested by the Company and accepted by the lenders. If the credit facilities do not continue to revolve, the facilities will convert to a 366-day non-revolving term loan facility.

Both credit facilities are subject to periodic review by the bank and are secured by a general assignment of book debts and a $250,000 demand debenture with a first floating charge over all assets of the Company. The Company is permitted to hedge up to 67 percent of its production under the lending agreement. As at September 30, 2010, the Company has drawn $57,352 under the extendible revolving term credit facility and $nil under the operating facility (December 31, 2009 – $nil drawn under demand credit facilities) and is in compliance with all covenants. The next scheduled review is to take place in May 2011.

Included in interest expense in the consolidated statement of operations is $555 of transaction costs related to the Company's credit facilities established in the three months ended September 30, 2010.

CEQUENCE ENERGY LTD.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

THREE AND NINE MONTH PERIODS ENDED SEPTEMBER 30, 2010

(All figures expressed in thousands except per share amounts unless otherwise noted)

8. ASSET RETIREMENT OBLIGATIONS

The following table summarizes the changes in asset retirement obligations for the nine months ended September 30, 2010 and year ended December 31, 2009:

	September 30, 2010	December 31, 2009
Balance - Beginning of period	4,059	2,515
Corporate Acquisitions	6,453	-
Asset Acquisitions	3,683	1,165
Dispositions	(366)	-
Accretion expense	300	207
Liabilities incurred	260	190
Abandonment cost incurred	(105)	(75)
Revision in estimated cash flows	263	57
Balance - End of period	14,547	4,059

The total estimated, undiscounted cash flows, inflated at 2 percent, required to settle the obligations are $44,540 (December 31, 2009 – $13,648) which have been discounted using a weighted average credit-adjusted risk-free interest rate of 7.87 percent (December 31, 2009 – 7.47 percent). The Company expects these obligations to be settled in approximately 2 to 30 years. As at September 30, 2010, no funds have been set aside to settle these obligations.

9. SHARE CAPITAL

Cequence has an unlimited number of common voting shares and common non-voting shares.

Issued common voting shares	Number (000's)	Stated Value $
Balance, beginning of period	39,530	267,908
Future income tax on renouncing expenditures for flow-through shares	-	(512)
Corporate acquisition – Peloton	12,059	30,269
Flow-through share private placement	4,070	10,001
Subscription receipts	21,045	44,195
Corporate acquisition – Temple	46,846	106,809
Common share private placement	2,950	6,195
Share issue costs, net of taxes of $1,159	-	(3,344)
Balance, end of period	126,500	461,521

On June 11, 2010, the Company completed the acquisition of Peloton (note 2) and issued 12,059 common voting shares with a deemed value of $2.51 per share for total deemed consideration of $30,269.

On August 19, 2010 the Company completed the sale of 3,200 shares on a CEE "flow-through" private placement basis at $2.50 per share for proceeds of $8,000 as well as 870 shares on a CDE "flow-through" private placement basis at $2.30 per share for proceeds of $2,001, resulting in a total issuance of 4,070 shares for total proceeds of $10,001. Under the terms of the respective agreements, Cequence is required to renounce $8,000 of CEE expenditures and $2,001 of CDE expenditures in February 2011. The qualifying CDE and CEE expenditures must be incurred by December 31, 2011 pursuant to the terms of the related agreements. As at September 30, 2010 the Company has not any incurred any of the qualifying CEE or CDE expenditures.

On August 19, 2010 the Company completed the sale of 18,545 subscription receipts at a price of $2.10 per subscription receipt for total proceeds of $38,945. The subscription receipts were convertible to Cequence common voting shares without further consideration upon the closing of the Deep Basin Assets acquisition (see note 3). Upon closing of the Deep Basin Assets acquisition on September 8, 2010, the subscription receipts were converted on a one for one basis, for no additional consideration and without further action, into common voting shares of the Company. On September 17, 2010, Cequence completed the sale of 2,500 common voting shares related to an over-allotment option on the subscription receipts offering discussed above at $2.10 per share for total proceeds of $5,250.

CEQUENCE ENERGY LTD.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

THREE AND NINE MONTH PERIODS ENDED SEPTEMBER 30, 2010

(All figures expressed in thousands except per share amounts unless otherwise noted)

9. SHARE CAPITAL (CONTINUED)

On September 10, 2010, the Company completed the acquisition of Temple (note 2) and issued 46,846 common voting shares with a deemed value of $2.28 per share for total deemed consideration of $106,809.

On September 10, 2010, Cequence completed the sale of 2,950 common voting shares through a private placement to a major shareholder as well as certain management and directors of the Company at $2.10 per share for total proceeds of $6,195. The transaction has been recorded at the exchange amount, which is the amount of consideration established and agreed to by the related parties, and is equal to fair value. As at September 30, 2010 no amounts are included in accounts payable and accrued liabilities related to the transaction.

As at September 30, 2010 there were no issued or outstanding non-voting shares (December 31, 2009 – none).

10. STOCK BASED COMPENSATION PLANS

Stock options

During the nine months ended September 30, 2010, the Company issued 10,483 stock options at prices ranging from $1.99 to $3.13 to employees and directors. The options have a five year life and 25 percent vest annually commencing in one year following the grant date for options issued in the six months ended June 30, 2010, whereas options issued in the three months ended September 30, 2010 vest one third annually commencing in one year following the grant date. The Company utilized a Black-Scholes option pricing model to price the options.

A summary of the inputs used to value stock options is as follows:

	September 30, 2010 $	December 31, 2009 $
Risk-free interest rate	2.3% - 2.9%	2.7%
Expected life of options	5 years	5 years
Expected volatility	50% - 60%	50%
Expected dividend rate	0%	0%
Expected forfeiture rate	6% - 15%	14%
Weighted average fair value	$1.00	$2.00

A summary of the status of the Company's stock option plan and changes during the nine months ended September 30, 2010 and year ended December 31, 2009 is as follows:

	September 30, 2010		December 31, 2009	
	Number of Options (000's)	Weighted Average Exercise Price, $	Number of Options (000's)	Weighted Average Exercise Price, $
Outstanding, beginning of period	839	4.40	789	8.56
Granted	10,483	2.01	900	4.32
Forfeited	(491)	3.78	(850)	8.19
Outstanding, end of period	10,831	2.12	839	4.40

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

	Options Outstanding			Options Exercisable	
Range of Exercise Price, $	Weighted Average Exercise Price, $	Number of Options Outstanding (000's)	Weighted Average Contractual Life Remaining (years)	Number of Options (000's)	Weighted Average Exercise Price, $
1.99 – 2.06	1.99	10,190	4.9	-	-
2.99 – 4.32	4.05	636	4.0	126	4.32
8.36	8.36	5	7.1	3	8.36
	2.12	10,831	4.9	129	4.40

CEQUENCE ENERGY LTD.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

THREE AND NINE MONTH PERIODS ENDED SEPTEMBER 30, 2010

(All figures expressed in thousands except per share amounts unless otherwise noted)

10. STOCK BASED COMPENSATION PLANS (CONTINUED)

Stock options (continued)

During the nine months ended September 30, 2010, $690 (September 30, 2009 - $60) in compensation expense related to stock options has been recognized in the consolidated statement of operations.

Performance warrants

As at December 31, 2009, the Company had a total of 5,200 performance warrants that were exercisable into a common, non-voting share of Cequence at a price of $1.88. During the three months ended September 30, 2010 these warrants were cancelled as part of the acquisition of Temple and any unrecognized stock based compensation expense was recognized in income. The cost to cancel the warrants of $451 was recognized as a transaction cost and capitalized as part of the acquisition (see note 2).

The Company recognized $142 of stock based compensation for the performance warrants in the nine months ended September 30, 2010 (September 30, 2009 – $513).

11. CONTRIBUTED SURPLUS

	September 30, 2010 $	December 31, 2009 $
Opening balance	7,818	5,596
Stock-based compensation expense (note 10)	832	712
Share repurchase under NCIB	-	912
Warrants expired unexercised	-	598
Ending balance	8,650	7,818

12. LOSS PER SHARE

Net loss per share has been calculated based on the weighted average number of common shares outstanding during the period. The following table reconciles the denominators used for the basic and diluted net loss per share calculations. No stock options or warrants have been included in the calculation of diluted shares outstanding for the three and nine month periods ended September 30, 2010 (September 30, 2009 – none) as their inclusion would be anti-dilutive.

	Three months ended September 30,		Nine months ended September 30,	
	2010	2009	2010	2009
Basic weighted average shares	69,060	26,577	50,321	15,333
Effect of dilutive stock options and warrants	-	-	-	-
Diluted weighted average shares	69,060	26,577	50,321	15,333

13. CONTINGENCIES AND COMMITMENTS

	2010	2011	2012	2013	2014+	Total
Office leases	$ 243	973	583	482	763	$ 3,044
Pipeline transportation	402	1,594	1,594	1,594	3,052	8,236
Drilling services	1,018	1,500	-	-	-	2,518
Total	$ 1,663	4,067	2,177	2,076	3,815	$ 13,798

The Company acquired a pipeline transportation contract in a property acquisition in 2009 that expires on November 30, 2015.

The Company has a commitment to use the drilling and related services of the Claimant of a lawsuit settled in the first quarter of 2010, at fair market value, in the amount of $3,000 over the two years following the date of settlement. Cequence is obligated to spend a minimum of $1,500 in each of the two years following the date of settlement to avoid any penalties under the commitment. Cequence has incurred $482 as at September 30, 2010.

CEQUENCE ENERGY LTD.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

THREE AND NINE MONTH PERIODS ENDED SEPTEMBER 30, 2010

(All figures expressed in thousands except per share amounts unless otherwise noted)

14. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

The Company's financial instruments recognized in the consolidated balance sheet consist of cash, accounts receivable, commodity contracts, demand credit facilities and accounts payable and accrued liabilities. The fair value of these financial instruments, excluding the commodity contracts, approximates their carrying values due to their short terms to maturity and the floating interest rate on the Company's debt.

The fair value of commodity contracts is determined by discounting the difference between the contracted price and published forward price curves as at the balance sheet date, using the remaining contracted petroleum and natural gas volumes at a credit-adjusted risk-free rate of 6 percent. Commodity contracts are considered level 2 instruments in the Company's fair value hierarchy.

The Company has exposure to market risk, credit risk and liquidity risk from its use of financial instruments. There have not been any changes to the Company's exposure to risks, or the objectives, policies and processes to manage these risks from December 31, 2009 other than as noted below:

As part of the acquisitions of Peloton and Temple (note 2), Cequence assumed the following commodity derivative financial instruments:

	Type	Volume	Price	Basis
January 1, 2010 to December 31, 2010	Swap	500 GJ/day	$4.69	AECO
January 1, 2010 to December 31, 2010	Swap	800 GJ/day	$5.07	AECO
April 1, 2010 to October 31, 2010	Swap	500 GJ/day	$5.32	AECO
April 1, 2010 to December 31, 2010	Fixed Price	2,500 GJ/day	$5.15	AECO
April 1, 2010 to December 31, 2010	Fixed Price	2,500 GJ/day	$5.75	AECO
April 1, 2010 to December 31, 2010	Fixed Price	2,000 GJ/day	$5.35	AECO
January 1, 2011 to December 31, 2011	Fixed Price	2,000 GJ/day	$6.20	AECO
January 1, 2011 to December 31, 2011	Fixed Price	2,000 GJ/day	$5.85	AECO

For the three and nine months ended September 30, 2010 realized gains from commodity derivative contracts recognized in income were $563 and $2,335 compared to gains of $2,800 and $7,346 for the three and nine months ended September 30, 2009, respectively.

The fair value of the commodity contracts outstanding at September 30, 2010 was an asset of $4,612 (December 31, 2009 – $1,420). For the three and nine months ended September 30, 2010 the Company recorded an unrealized gain of $114 and an unrealized loss of $1,348, respectively, from derivative commodity contracts compared to an unrealized loss of $2,435 and $28 for the three and nine months ended September 30, 2009. An estimate of credit risk has been made in the valuation of all derivative commodity contracts.

As at September 30 2010, an increase in gas price of $0.50/gj results in a decrease in the fair value of the commodity contract of $1,082 ($777 after tax) and a commensurate increase to net loss.

15. CHANGES IN NON-CASH WORKING CAPITAL

	Three months ended September 30,		Nine months ended September 30,	
	2010 $	2009 $	2010 $	2009 $
Accounts receivable	(2,338)	611	(61)	4,620
Deposits and prepaid expenses	(361)	404	(21)	729
Accounts payable and accrued liabilities	5,458	1,872	(4,935)	(4,333)
Net change in non-cash working capital	2,759	2,887	(5,017)	1,016
Allocated to:				
Operating activities	1,944	1,018	(4,738)	1,628
Investing activities	389	1,554	(705)	(612)
Financing Activities	426	315	426	-
	2,759	2,887	(5,017)	1,016

CEQUENCE ENERGY LTD.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

THREE AND NINE MONTH PERIODS ENDED SEPTEMBER 30, 2010

(All figures expressed in thousands except per share amounts unless otherwise noted)

16. CAPITAL MANAGEMENT

Cequence's objectives are to maintain a flexible capital structure in order to meet its financial obligations and to execute on strategic opportunities throughout the business cycle. The Company's capital comprises shareholders' equity, demand credit facilities and working capital. Cequence manages the capital structure and makes adjustments in light of economic conditions and the risk characteristics of the underlying assets.

In order to maintain or adjust the capital structure, Cequence may issue new common shares, issue new debt or replace existing debt, adjust capital expenditures and acquire or dispose of assets.

The Company evaluates its capital structure based on the non-GAAP measure of net debt to cash flow from operating activities and the current credit available to Cequence compared to its budgeted capital expenditures. At September 30, 2010 Cequence has a negative net consolidated working capital of $68,857 (December 31, 2009 – 7,430 positive).

Net debt to cash flow provides a measure of the Company's ability to manage its debt levels under current operating conditions. The ratio is calculated as net debt, defined as current debt, long term debt and working capital excluding commodity derivative assets or liabilities, divided by cash flow from operations before asset retirement expenditures and changes in non-cash working capital for the most recent quarter.

It is the Company's objective to maintain a net debt to annualized cash flow ratio of less than 2:1. As at September 30, 2010, the ratio was calculated as 4.7:1 (December 31, 2009 – 0:1) based on annualized quarterly results. Cequence's debt to cash flow ratio for the current quarter is above 2:1 due mainly to the acquisition of Temple (note 2) and the Deep Basin Assets acquisition (note 3) where Cequence acquired Temple's net debt on September 10, 2010 and paid for the Deep Basin Assets in cash effective September 8, 2010 but did not realize the full effect of the related cash flows as the acquisitions occurred late in the quarter.

Due to the acquisitions noted above, the Company evaluates its net debt to annualized cash flow ratio based on pro forma results. Cequence has determined that the adjusted net debt to annualized cash flow ratio calculated on this basis is in compliance with the Company's capital management objectives for the three months ended September 30, 2010.

The Company's current borrowing capacity is based on the lenders' semi-annual review of the Company's oil and natural gas reserves. The Company is also subject to various covenants including hedging no more than 67 percent of production. Compliance with these covenants is monitored on a regular basis and at September 30, 2010 the Company was in compliance with all such covenants.

17. SUBSEQUENT EVENTS

On October 15, 2010, the Company completed the sale of its 2011 fixed price commodity contracts totalling 4,000 GJ/day at prices ranging from $5.85 to $6.20 per GJ (see note 14) for total proceeds of $3,386. The proceeds will be used to fund future drilling activities.

Effective October 29, 2010, the Company agreed to sell, on a private placement basis, 2,250 units at a price of $2.00 per unit for total proceeds of $4,500. Each unit entitles the holder to one common share on a CDE "flow-through" basis, one warrant to purchase one common share on a CDE "flow-through" basis at any time on or after August 1, 2011 and prior to August 15, 2011 at a price set as a 10 percent premium to the 10 day volume weighted average trading price of the Company's shares on the TSX for the period July 18, 2011 to July 29, 2011 (the "2011 Warrants") and one warrant to purchase one common share on a CDE "flow-through" basis at any time on or after August 1, 2012 and prior to August 15, 2012 at a price set as a 10 percent premium to the 10 day volume weighted average trading price of the Company's shares on the TSX for the period July 18, 2012 to July 31, 2012 (the "2012 Warrants). The purchaser has unconditionally committed to exercise the 2011 Warrants prior to August 15, 2011 and Cequence has the option to hold up to 1,500 of the shares to initially be issued in escrow until such time as the 2011 Warrants are exercised. If the 2011 Warrants are not exercised, the shares held in escrow shall be cancellable at no cost to Cequence and no redress to the shareholder. The 2012 Warrants are conditional on the exercise of the 2011 Warrants and if the 2011 Warrants are not exercised in accordance with their terms, the 2012 Warrants become null and void.

CORPORATE INFORMATION

MANAGEMENT

Paul Wanklyn
President & CEO

Howard Crone, P.Eng
Executive Vice President & COO

David Gillis, CA
Vice President, Finance & CFO

James R. Jackson, P.Eng
Vice President, Engineering

Nathan MacBey
Vice President, Corporate Development

David P. Robinson,
Vice President, Geology

Christopher C. Soby
Vice President, Land

Stephen R. Stretch
Vice President, Geophysics

Mike Stewart
Vice President, Operations

Erin Thorson, CMA
Controller

DIRECTORS

Don Archibald
Chairman

Peter Bannister

Paul Colborne

Robert C. Cook

Howard Crone

Andrew L. Evans

Brian Felesky

James K. Gray

Francesco Mele

TRANSFER AGENT AND REGISTRAR

Valiant Trust Company
Calgary, Alberta

HEAD OFFICE

700, 326 11th Avenue SW
Calgary, AB T2R 0C5
Phone: 403-229-3050
Fax: 403-229-0603
Email: info@cequence-energy.com
Website: www.cequence-energy.com

AUDITORS

Deloitte & Touche LLP
Calgary, Alberta

BANKERS

Canadian Imperial Bank of Commerce
Calgary, Alberta

LEGAL COUNSEL

MacLeod Dixon LLP
Calgary, Alberta

EVALUATION ENGINEERS

GLJ Petroleum Consultants
Calgary, Alberta

STOCK EXCHANGE LISTING

Toronto Stock Exchange
Symbol: CQE

WWW.**CEQUENCE-ENERGY**.COM

700, 326 11th Avenue SW Calgary, AB T2R 0C5 T 403.229.3050