BIR:Q2

SIX MONTHS ENDED JUNE 30, 2012

August 14, 2012

Fellow Shareholders,

Birchcliff is pleased to report its second quarter financial and operating results for the three and six months ended June 30, 2012.

I am pleased to report record average quarterly production of 22,039 boe per day while at the same time we reduced our operating costs on a per unit basis as compared to the same period last year.

During the quarter we completed a common share equity issue for gross proceeds of $110 million which was used to pay down debt and strengthen our financial position during a time of weak natural gas prices. In addition, Birchcliff increased its syndicated credit facilities to $540 million from $520 million, which continues to include the 2 year term out provisions.

Birchcliff recently completed its first perpetual preferred share equity issue for gross proceeds of $50 million. The proceeds were used to pay down bank debt.

Accordingly, pro forma total outstanding debt at June 30, 2012, after giving effect to the preferred share equity issue was approximately $353 million.

The equity issues in 2012 and the increase to our syndicated credit facilities have provided the financial flexibility that Birchcliff requires to prudently manage its business while protecting its financial position.

2012 SECOND QUARTER RESULTS

Production

Record second quarter 2012 production averaged 22,039 boe per day (76% natural gas and 24% light oil and natural gas liquids) and is 27% greater than the second quarter of 2011.

Birchcliff continues to expect its 2012 exit rate to be approximately 26,000 boe per day.

Current production is approximately 21,900 boe per day. Average daily production in the third quarter is expected to be lower as the Pouce Coupe South Gas Plant (the "**PCS Gas Plant**") will be shut down for up to 10 days for completion of construction of the Phase III expansion of that plant.

Cash Flow and Earnings

Cash flow was $26.0 million or $0.19 per share for the second quarter of 2012 as compared to $34.3 million or $0.27 per share in the second quarter of 2011. The 24% decline is mainly attributable to significantly lower natural gas prices, notwithstanding an increase in average daily production.

Earnings were $0.4 million or $nil per share for the second quarter of 2012 as compared to $10.1 million or $0.08 per share in the second quarter of 2011. Even with the AECO natural gas spot price averaging $1.89 per Mcf for the second quarter of 2012, we were able to show positive earnings, highlighting our low cost structure.

It is noteworthy that per unit general and administrative ("**G&A**") costs were down to $2.26 per boe, which is a 45% reduction from the first quarter of 2012, due to the one-time sales process costs recorded during the first quarter. With these one-time associated costs behind us, we will see more normalized G&A costs per boe in our future quarters.

Capital Expenditures and Drilling Results

During the second quarter of 2012, net capital spending aggregated to $58.8 million. We spent significant construction and drilling capital in preparation for the start-up of Phase III of the PCS Gas Plant by November 1, 2012. A specific breakdown of capital expenditures can be found under "Results of Operations - Capital Expenditures" in the Management's Discussion and Analysis section of our Second Quarter Report.

Drilling activities during the second quarter of 2012 resulted in 9 (9.0 net) wells, of which all were successful. Birchcliff drilled and cased 8 (8.0 net) Montney/Doig horizontal natural gas wells, and 1 (1.0 net) Worsley horizontal light oil well. Birchcliff also spent significant time and effort on evaluating and developing new resource plays in the Peace River Arch area of Alberta with a focus on oil plays.

Operating Costs

Operating costs during the second quarter of 2012 were $6.22 per boe. This is 8% lower than $6.74 per boe recorded for the second quarter in 2011.

During the first six months of 2012, 45% of our total sales volumes were processed through our PCS Gas Plant as compared to 36% during the first six months of 2011. Once Phase III of the PCS Gas Plant becomes operational, operating costs per boe are expected to trend downwards as the vast majority of our future production volumes are expected to be processed through our low cost, 100% owned PCS Gas Plant.

The following table sets forth historical netback and cost data for natural gas processed through the PCS Gas Plant.

	Six months ended June 30, 2012		Twelve months ended December 31, 2011	
PRODUCTION PROCESSED THROUGH THE PCS GAS PLANT				
Average daily production, net to Birchcliff:				
Natural gas (Mcf)		57,211		40,334
Oil & NGLs (bbls)		232		96
Total boe (6:1)		**9,767**		6,818
NETBACK AND COST	*$/Mcfe*	*$/boe*	*$/Mcfe*	*$/boe*
Petroleum and natural gas revenue	2.47[(1)]	14.82	3.98[(1)]	23.88
Royalty expense	(0.07)	(0.42)	(0.26)	(1.55)
Operating expense, net of recoveries	(0.26)	(1.56)	(0.21)	(1.28)
Transportation and marketing expense	(0.22)	(1.32)	(0.27)	(1.59)
Estimated operating netback[(2)]	**$1.92**	**$11.52**	$3.24	$19.46

(1) Premium pricing resulting from the heat value of natural gas being processed at the PCS Gas Plant and the value of recovered liquids. AECO natural gas spot price averaged $2.02 per Mcf in the first half of 2012 and $3.63 per Mcf during 2011.

(2) The estimated operating netback is based upon certain cost allocations and accruals directly related to the PCS Gas Plant and related wells and infrastructure, and is disclosed on a production month basis.

Land

Birchcliff continues to grow its undeveloped land base in the Peace River Arch. As at June 30, 2012, Birchcliff has increased its undeveloped land position to 552,355 gross (514,814 net) acres from its year end 2011 undeveloped land position of 531,903 gross (493,968 net) acres, resulting in a 93% average working interest. Birchcliff's very high average working interest in its undeveloped land base reflects its longstanding strategy of acquiring high working interest undeveloped land proximate to its operated high working interest production base.

Indebtedness

At June 30, 2012 the amount outstanding under Birchcliff's syndicated bank credit facilities was approximately $400.9 million. Birchcliff's working capital deficiency as at June 30, 2012 was $54.8 million, for a total debt of $455.7 million at June 30, 2012. The working capital deficiency does not reduce the amount Birchcliff can draw under its credit facilities.

On a pro forma basis at June 30 2012, after giving effect to the $50 million Preferred Unit Equity issue, of which net proceeds are estimated to be approximately $48 million, Birchcliff had approximately $353 million outstanding under its syndicated bank credit facilities and pro forma total debt (including working capital deficit) was $408 million.

Birchcliff announced on June 26, 2012 that it had increased its syndicated bank credit facilities to an aggregate of $540 million from the previous credit limit of $520 million. The terms of the credit facilities remain essentially unchanged, including the two-year term out feature applicable to the extendible revolving credit facilities.

Birchcliff's syndicated bank credit facilities consist of a $70 million non-revolving five-year term credit facility with a maturity date of May 25, 2016 and extendible revolving credit facilities (the "**Revolving Credit Facilities**") of $470 million.

The Revolving Credit Facilities are made up of an extendible revolving credit facility of $440 million and an extendible revolving working capital facility of $30 million both of which have a two-year term-out feature.

2012 OPERATIONS UPDATE

Pouce Coupe South Gas Plant Update

The Phase III expansion of the PCS Gas Plant is under construction and remains on schedule to commence processing natural gas by November 1, 2012. Birchcliff is currently drilling and completing Montney/Doig horizontal natural gas wells that will produce to the PCS Gas Plant.

Birchcliff has received approval from the Energy Resources Conservation Board to increase the processing capacity of the PCS Gas Plant to 150 MMcf per day (raw inlet capacity) from the current licensed processing capacity of 120 MMcf per day. To operate the PCS Gas Plant at 150 MMcf per day will require twinning of the sales gas pipeline, but the capital required is not material. This is a significant milestone for Birchcliff as it continues to allow Birchcliff to expand its future production through 100% owned facilities.

Birchcliff expects the PCS Gas Plant to process approximately 100 MMcf per day of natural gas at the end of 2012. This leaves 50 MMcf per day of expected processing capacity available for future production growth **without incurring material facilities capital.**

Montney/Doig Natural Gas Resource Play Update

In the second quarter of 2012, Birchcliff's activities on the Montney/Doig Natural Gas Resource Play included the drilling of 8 (8.0 net) horizontal wells utilizing multi-stage fracture stimulation techniques. To date in 2012, Birchcliff has drilled and cased 19 (19.0 net) horizontal wells, of which 12 (12.0 net) wells have been completed, and 8 (8.0 net) are on production, 2 (2.0 net) of these wells are Middle/Lower Montney exploration wells that continue to expand this play trend. To present we have also drilled and cased 1 (1.0 net) vertical exploration well.

Birchcliff is very focused on reducing drilling and completion costs.

Birchcliff had two rigs drilling continuously through break-up on separate multi-well pads. Seven wells were drilled on one pad and four wells were drilled on the second pad. One rig was recently released from the seven well pad and the second rig was released on June 11, 2012. With respect to the four well pad, once the drilling operations were finished, completion equipment was mobilized and the four wells were completed consecutively. Costs are coming in as expected and completion results look favorable. Following the consecutive completion of the wells, the facility construction crews are performing all of the equipping and tie-in operations for the entire pad, which is expected to result in cost efficiencies. We are currently preparing to commence the completion operations on the seven well pad.

The rapid advancements in horizontal drilling and multi-stage fracture stimulation of horizontal wells have resulted in significant improvements in production and reserve capture for many different plays throughout North America. Birchcliff believes that the Montney/Doig Natural Gas Resource Play continues to experience some of the best results of the application of this technology due to its unique reservoir characteristics. Birchcliff classifies the Montney/Doig Natural Gas Resource Play as a hybrid resource play which significantly benefits from having approximately 300 meters (1,000 feet) of gas saturated rock that has both tight silt and sand reservoir rock inter-layered with shale gas source rock. The horizontal wells are designed to maximize the contributions from the different elements of this complex reservoir. As our knowledge grows with respect to both operational technology and characteristics of these reservoirs, we expect our results to continue to improve.

Birchcliff believes that it has approximately 1,850 net future Montney/Doig horizontal natural gas drilling locations on its lands based on a development scenario of four wells per section per stratigraphic play.

Worsley Light Oil Resource Play Update

The Worsley Light Oil Resource Play has demonstrated consistent and prolific production performance. Successful expansion of the pool, water flood performance and the application of horizontal drilling and multi-stage fracture stimulation technology have all contributed to its continued reserve growth, production growth and high netbacks.

New Resource Play Update

In our Peace River Arch core area, numerous industry competitors have announced significant developments on a number of new resource plays with a strong bias to new tight/shale oil resource plays. Continuing from 2011 there have been significant Crown lands posted and acquired in the Peace River Arch and numerous new wells drilled and completed targeting these new resource plays, including the Montney, Charlie Lake, Nordegg and the Duvernay. Birchcliff has been successful in acquiring further lands since June 30, 2012. As a result its undeveloped land position has increased to 568,995 gross (531,454 net) acres from its June 30, 2012 undeveloped land position of 552,355 gross (514,814 net) acres, resulting in a 93% average working interest. Birchcliff believes that all of its focused undeveloped land has potential in at least one of these new Resource Plays. We continue to spend a significant amount of time analyzing and evaluating various new resource plays in the Peace River Arch area of Alberta.

SUBSEQUENT EVENTS

$50 Million Preferred Unit Equity Issue

On July 17, 2012 Birchcliff announced and subsequently closed on August 8, 2012 a preferred unit equity issue for gross proceeds of $50 million (the "**Preferred Unit Offering**"). The proceeds of the Preferred Unit Offering were used to pay down debt and provide Birchcliff with the financial flexibility it requires to properly manage its business at a time when natural gas prices are very weak.

Each preferred unit was sold for $25.00 and consisted of one (1) preferred share with an initial 5 year, 8% yield ("**Preferred Share**") and three (3) warrants ("**Warrants**"). Each Warrant provided the right to buy one common share for $8.30, for a period of two years from the closing date. Two (2) million Preferred Shares and six (6) million Warrants were issued in the Preferred Unit Offering.

The Warrants, if exercised, will raise an additional $49.8 million of equity prior to their expiry in August 2014, without fees or commission.

The Preferred Shares are listed for trading on the TSX under the symbol BIR.PR.A and the Warrants are listed for trading on the TSX under the symbol BIR.WT. The Preferred Shares and the Warrants can be bought and sold freely, in the same way common shares are bought and sold.

We raised money through the Preferred Share and Warrant Offering to pay down our bank debt and strengthen our balance sheet. Birchcliff has the sole right, but not the obligation, to redeem the Preferred Shares at the end of five years. Alternatively, Birchcliff can reset the dividend rate at the end of the five year term at a rate equal to the five-year Government of Canada bond yield plus 6.83 per cent and continue to pay dividends for another five years. The Preferred Shares provide Birchcliff with long term equity financing that does not participate in the significant upside potential of Birchcliff's assets. This long term capital more closely aligns the capital structure of Birchcliff with the long term assets that we are building with our resource plays.

OUTLOOK

Birchcliff is focused on the day to day running of its business. We are enjoying record production and low operating costs per boe. Construction of the Phase III Expansion of our PCS Gas Plant is proceeding on time and on budget, and it is expected to take Birchcliff to record production volumes in November of 2012.

Since November 2007, we have drilled and cased 90 (78.2 net) successful Montney/Doig horizontal natural gas wells, of which 79 (67.2 net) have been brought on production, 4 (4.0 net) wells are completed and awaiting tie in and 7 (7.0 net) wells are drilled and awaiting completion and tie in. All have been successful.

We continue to develop and expand our Worsley Light Oil Resource Play and have laid the foundation to exploit several New Tight/Shale Oil Resource Plays.

Our day to day business has been and continues to be very successful.

With the issuance of the Preferred Shares we have created a much stronger capital structure for Birchcliff as we have increased our equity and reduced our debt and positioned ourselves for the future.

Birchcliff will complete the vast majority of its 2012 capital program by the end of September 2012. Thereafter, 2012 capital spending will be minimal and therefore we expect to reduce debt during the fourth quarter while we do the planning required for our 2013 capital program.

We are excited about our 2013 capital spending program as we will not be allocating our capital to any major facility projects as we have had to do in prior years. Our capital efficiencies will improve with most of our capital going to the drilling, completing and tie-ins of new wells.

We have the flexibility to expand our production and fill the remaining unused capacity in our PCS Gas Plant of approximately 50 MMcf (8,000 boe) per day. In the event that natural gas prices deteriorate we will make the appropriate financial decisions to ensure that Birchcliff continues to have the financial flexibility and the balance sheet required for long term sustainability.

Birchcliff remains very confident that its two highly focused, high working interest, low cost, repeatable, sustainable, long term growth resource plays in the Peace River Arch area of Alberta offer tremendous upside value to our shareholders. The Montney/Doig Natural Gas Resource Play continues to be one of the most active geological plays in North Western Alberta and Birchcliff is right in the heart of the play.

Our strategy has not changed, notwithstanding the weakness in natural gas prices. We believe that we can economically find, develop and produce natural gas from the Montney/Doig Natural Gas Resource Play at low costs. We also believe that technology advances will continue to reduce our finding costs and our operating costs and increase our recovery factors. We note that our 2010 and 2011 finding costs were in the top decile as compared to others in the industry and 2012 results to date continue to be very positive.

Our goal to be producing approximately 26,000 boe per day at year end 2012 is firmly in our sights. We look forward to reporting our progress to you in the coming months.

On behalf of our management team, executive team and the directors, I thank all of our shareholders for their continued support and our staff for their hard work and dedication.

(signed) "*A. Jeffery Tonken*"

A. Jeffery Tonken

President and Chief Executive Officer

FINANCIAL AND OPERATIONAL HIGHLIGHTS

	Three months ended June 30, 2012	Three months ended June 30, 2011	**Six months ended June 30, 2012**	Six months ended June 30, 2011
OPERATING				
Average daily production				
Light oil – (barrels)	4,447	3,589	4,511	3,666
Natural gas – (thousands of cubic feet)	100,843	78,714	98,042	79,635
NGLs – (barrels)	785	615	699	593
Total – barrels of oil equivalent (6:1)	**22,039**	**17,324**	**21,550**	**17,532**
Average sales price ($ Canadian)				
Light oil – (per barrel)	81.45	99.31	85.84	93.08
Natural gas – (per thousand cubic feet)	2.05	4.15	2.18	4.08
NGLs – (per barrel)	83.53	94.15	87.71	88.63
Total – barrels of oil equivalent (6:1)	**28.77**	**42.76**	**30.72**	**41.01**
Undeveloped land				
Gross (acres)	552,355	542,143	552,355	542,143
Net (acres)	514,814	501,188	514,814	501,188
NETBACK AND COST				
($ per barrel of oil equivalent at 6:1)				
Petroleum and natural gas revenue	28.78	42.79	30.74	41.05
Royalty expense	(3.00)	(5.58)	(3.39)	(4.73)
Operating expense	(6.22)	(6.74)	(6.20)	(6.85)
Transportation and marketing expense	(2.39)	(2.67)	(2.38)	(2.60)
Netback	**17.17**	**27.80**	**18.77**	**26.87**
General & administrative expense, net	(2.26)	(3.07)	(3.17)	(2.88)
Interest expense	(1.95)	(2.99)	(2.30)	(3.01)
Cash Flow Netback	**12.96**	**21.74**	**13.30**	**20.98**
Stock-based compensation expense, net	(0.64)	(1.45)	(0.75)	(1.36)
Depletion and depreciation expense	(11.48)	(10.17)	(11.52)	(10.12)
Accretion expense	(0.22)	(0.28)	(0.22)	(0.28)
Amortization of deferred financing fees	(0.11)	(0.15)	(0.10)	(0.15)
Gain (loss) on sale of assets	-	(0.58)	0.99	(0.29)
Deferred income tax expense	(0.30)	(2.69)	(0.64)	(2.57)
Net Income	**0.21**	**6.42**	**1.06**	**6.21**
FINANCIAL				
Petroleum and natural gas revenue ($000)	57,729	67,464	120,562	130,257
Cash flow ($000)(1)	25,985	34,269	52,181	66,582
Per share – basic ($)(1)	0.19	0.27	0.39	0.53
Per share – diluted ($)(1)	0.19	0.26	0.39	0.51
Net income ($000)	416	10,117	4,147	19,710
Per share – basic ($)	-	0.08	0.03	0.16
Per share – diluted ($)	-	0.08	0.03	0.15
Common shares outstanding				
End of period – basic	141,433,644	126,496,677	141,433,644	126,496,677
End of period – diluted	157,232,116	140,137,084	157,232,116	140,137,084
Weighted average shares for period – basic	138,425,779	126,322,814	132,588,343	125,877,298
Weighted average shares for period – diluted	138,837,321	131,380,901	133,885,883	131,030,694
Capital expenditures, net ($000)	58,815	32,300	178,667	84,479
Working capital deficiency ($000)	54,832	10,139	54,832	10,139
Non-revolving five-year term facility ($000)	69,232	68,773	69,232	68,773
Revolving credit facilities ($000)	331,644	270,278	331,644	270,278
Total debt ($000)	455,708	349,190	455,708	349,190

(1) Cash flow and cash flow per share amounts represent cash provided by operating activities as per the Condensed Statements of Cash Flows before the effects of changes in non-cash working capital and decommissioning expenditures related to operating activities.

MANAGEMENT'S DISCUSSION AND ANALYSIS

GENERAL

Birchcliff Energy Ltd. ("**Birchcliff**" or the "**Corporation**") is a Calgary, Alberta based intermediate oil and gas company with operations concentrated in its one core area, the Peace River Arch of Alberta. Additional information relating to the Corporation, including its Annual Information Form, is available on the SEDAR website at www.sedar.com and on the Corporation's website at www.birchcliffenergy.com. Birchcliff's common shares are listed for trading on the Toronto Stock Exchange ("**TSX**") under the symbol "**BIR**" and are included in the S&P/TSX Composite Index.

The following Management's Discussion and Analysis ("**MD&A**") is dated August 14, 2012. The unaudited interim condensed financial statements with respect to the three and six months ended June 30, 2012 (the "**Reporting Periods**") as compared to the three and six months ended June 30, 2011 (the "**Comparable Prior Periods**") and this MD&A have been prepared by management and approved by the Corporation's Audit Committee and Board of Directors. This MD&A should be read in conjunction with the unaudited interim condensed financial statements of the Corporation and related notes for the Reporting Periods and Comparable Prior Periods. All financial information is expressed in thousands of Canadian dollars, unless otherwise stated.

The Corporation's interim condensed financial statements have been prepared in accordance with International Accounting Standard ("**IAS**") 34, *Interim Financial Reporting*, within International Financial Reporting Standards ("**IFRS**"), as issued by the International Accounting Standards Board ("**IASB**").

SECOND QUARTER OVERALL PERFORMANCE

Production

Production in the second quarter of 2012 averaged 22,039 boe per day. This is a 27% increase from the 17,324 boe per day the Corporation averaged in the second quarter of 2011. This increase was largely achieved through the success of Birchcliff's capital drilling program with increased production from new Montney/Doig horizontal natural gas wells that were tied into Phases I and II of Birchcliff's 100% owned and operated Pouce Coupe South Natural Gas Plant ("**PCS Gas Plant**") and increased production from the Worsley Light Oil Resource Play.

Birchcliff's production averaged 21,550 boe per day in the first half of 2012.

Production consisted of approximately 76% natural gas and 24% crude oil and natural gas liquids in the second quarter of 2012 as compared to 76% natural gas and 24% crude oil and natural gas liquids in the second quarter of 2011.

Commodity Prices

The Edmonton Par oil price averaged $83.95 per barrel in the second quarter of 2012, a 19% decrease from $103.07 per barrel in the second quarter of 2011. The AECO natural gas spot price averaged $1.89 per Mcf in the second quarter of 2012, a 51% decrease from $3.87 per Mcf in the second quarter of 2011.

Oil sales prices at the wellhead averaged $81.45 per barrel in the second quarter of 2012, an 18% decrease from $99.31 per barrel in the second quarter of 2011. Natural gas sales prices at the wellhead averaged \$2.05 per Mcf in the second quarter of 2012, a 51% decrease from \$4.15 per Mcf in the second quarter of 2011.

The prices received for Birchcliff's petroleum and natural gas sales are impacted by world events that dictate the level of supply and demand for petroleum and natural gas. Birchcliff currently does not have any commodity contracts in place and is therefore subject to fluctuations in commodity prices.

PCS Gas Plant Netbacks

Despite contending with the lowest AECO natural gas spot price in over 10 years, for Birchcliff's Montney/Doig horizontal natural gas wells producing to the PCS Gas Plant, the Corporation has an estimated operating netback of \$1.92 per Mcfe in the six months ended June 30, 2012. While the AECO natural gas spot price averaged \$2.02 per Mcf during the first half of 2012, Birchcliff received \$2.47 per Mcfe, a premium to the AECO natural gas spot price, due to the heat value of its natural gas and the value of the recovered liquids. Approximately 58% of Birchcliff's total natural gas sales volumes and 45% of total corporate sales volumes were processed at the PCS Gas Plant during the first half of 2012.

Processing Birchcliff's natural gas through the PCS Gas Plant has significantly reduced the operating cost on a per boe basis and has improved the economics of the Montney/Doig horizontal natural gas wells tied into the PCS Gas Plant, allowing the Corporation to operate at very low natural gas commodity prices. On a per boe basis, operating costs have been trending downward since the PCS Gas Plant first became operational in early 2010. Operating costs (net of recoveries) in the second quarter of 2012 were \$6.22 per boe, down 31% and 43% from the comparative quarters in 2009 and 2008, respectively.

The following table details Birchcliff's net production and operating netback for wells producing to the PCS Gas Plant for the six months ended June 30, 2012 and the twelve months ended December 31, 2011:

	Six months ended June 30, 2012		Twelve months ended December 31, 2011	
PRODUCTION PROCESSED THROUGH THE PCS GAS PLANT				
Average daily production, net to Birchcliff:				
Natural gas (Mcf)		57,211		40,334
Oil & NGLs (bbls)		232		96
Total boe (6:1)		**9,767**		6,818
NETBACK AND COST	*\$/Mcfe*	*\$/boe*	*\$/Mcfe*	*\$/boe*
Petroleum and natural gas revenue	2.47[1]	14.82	3.98[1]	23.88
Royalty expense	(0.07)	(0.42)	(0.26)	(1.55)
Operating expense, net of recoveries	(0.26)	(1.56)	(0.21)	(1.28)
Transportation and marketing expense	(0.22)	(1.32)	(0.27)	(1.59)
Estimated operating netback[2]	**1.92**	**11.52**	3.24	19.46

(2) Premium pricing resulting from the heat value of natural gas being processed at the PCS Gas Plant and the value of recovered liquids. AECO natural gas spot price averaged \$2.02 per Mcf in the first half of 2012 and \$3.63 per Mcf during 2011.

(3) The estimated operating netback is based upon certain cost allocations and accruals directly related to the PCS Gas Plant and related wells and infrastructure, and is disclosed on a production month basis.

Cash Flow and Earnings

The following schedule sets out the reconciliation of cash provided by operating activities to cash flow:

	Three months ended June 30,		Six months ended June 30,	
	2012	2011	**2012**	2011
Cash provided by operating activities	11,294	40,905	39,910	62,946
Adjustments:				
Decommissioning expenditures	42	212	94	678
Changes in non-cash working capital	14,649	(6,848)	12,177	2,958
Cash flow(1)	**25,985**	34,269	**52,181**	66,582
Per share – basic ($)	**0.19**	0.27	**0.39**	0.53
Per share – diluted ($)	**0.19**	0.26	**0.38**	0.51

(1) Management uses cash flow to analyze operating performance. Cash flow as presented does not have any standardized meaning prescribed by IFRS and therefore it may not be comparable with the calculations of similar measures for other issuers. Cash flow as presented is not intended to represent cash flow from operating activities, net income or other measures of financial performance calculated in accordance with IFRS. All references to cash flow throughout this report are based on cash flow from operating activities as per the Statement of Cash Flows and removing the adjustments for non-cash working capital and decommissioning expenditures. Cash flow per share is calculated based on the weighted average number of shares outstanding consistent with the calculation of net income per share.

Cash flow generated by the Corporation in the second quarter of 2012 was $26.0 million as compared to $34.3 million in the second quarter of 2011. The decrease in aggregate cash flow in the second quarter of 2012 as compared to the second quarter of 2011 is mainly attributed to significantly lower natural gas prices, with the AECO natural gas spot price having decreased 51% from the second quarter of 2011. Cash flow was also negatively impacted by lower realized oil wellhead prices, positively offset by higher average daily production, lower net general and administrative expenses, decreased interest expense and royalty expense. Higher average production resulted in some increase in aggregate operating expenses and transportation and marketing costs in the current quarter. General and administrative costs in the second quarter of 2012 were $2.26 per boe, a 45% reduction from the first quarter of 2012 due to the one time sales process costs recorded in the first quarter of 2012.

Despite AECO natural gas spot price averaging $1.89 per Mcf, Birchcliff achieved positive net earnings as a result of its low cost structure. Birchcliff had net income of approximately $0.4 million ($nil per share) in the second quarter of 2012 as compared to $10.1 million ($0.08 per share) in the second quarter of 2011. The decrease in net income was mainly attributable to lower cash flow and the increase in depletion expense resulting from higher average daily production in the current quarter.

Capital Expenditures

Total capital expenditures (excluding minor acquisitions and dispositions) in the second quarter of 2012 were $58.8 million as compared to $33.7 million in the second quarter of 2011. Of the $58.8 million, approximately $15.3 million (26%) was related to construction of Phase III of the PCS Gas Plant and approximately $21.3 million (36%) was for the drilling and completion of Montney/Doig horizontal natural gas wells that will produce to Phase III of the PCS Gas Plant once it becomes operational on or before November 1, 2012.

The remaining $22.2 million (38%) in capital was spent on other infrastructure, expanding the Montney/Doig Natural Gas Resource Play and the Worsley Light Oil Resource Play, acquiring land and on other oil and gas exploration and development projects in the Peace River Arch. See *Results of*

Operations – Capital Expenditures for further details of the Corporation's capital expenditures in the second quarter of 2012.

Credit Facilities and Equity Issue

On June 26, 2012, Birchcliff's bank syndicate approved a $20 million increase to the revolving credit facilities to an aggregate limit of $470 million and extended the conversion date of those facilities to May 17, 2013 (the "**Revolving Credit Facilities**"). The current aggregate maximum amount available under the Corporation's bank credit facilities is $540 million, of which $70 million is under the non-revolving five-year term credit facility with a maturity date of May 25, 2016 (the "**Non-Revolving Five-Year Term Facility**") and $470 million is under the Revolving Credit Facilities. See also "*Major Transactions Affecting Financial Results – Credit Facilities*".

On April 19, 2012, Birchcliff completed a bought deal equity financing and a private placement for gross proceeds of $110 million (the "**April Financing**"). The Corporation issued 8,075,000 common shares at a price of $7.65 per common share and 1,100,000 common shares on a "flow-through" basis, pursuant to the *Income Tax Act* (Canada), at a price of $9.20 per share. Birchcliff's major shareholder purchased 5,000,000 common shares issued at a price of $7.65 per share in a concurrent private placement. The aggregate net proceeds of the bought deal equity financing and the private placement totaling $106.2 million were used to reduce indebtedness under the Revolving Credit Facilities, of which a portion was re-drawn in the current quarter and the remaining will be used to fund a portion of the Corporation's ongoing capital program. See also "*Major Transactions Affecting Financial Results – Equity Financings*".

OUTLOOK

Production

Birchcliff's expects its exit production rate in 2012 to be approximately 26,000 boe per day. This estimate assumes that the Phase III of the PCS Gas Plant, which is currently under construction, remains on schedule to commence processing natural gas on or before November 1, 2012; that no unexpected outages occur in the infrastructure that Birchcliff relies on to produce its wells; and that existing wells continue to meet production expectations and future wells, which are scheduled to come on production in the second half of 2012, meet production expectations.

Bank Debt and Liquidity

To further strengthen Birchcliff's financial position during this period of very low natural gas prices, Birchcliff completed a $50 million preferred unit equity financing on August 8, 2012 (the "**August Financing**"). The net proceeds of approximately $48 million were used to reduce indebtedness under the Revolving Credit Facilities. See "*Major Transactions Affecting Financial Results – Equity Financings*".

The April Financing and the August Financing, together with the increased credit limit under the Corporation's bank credit facilities, provides Birchcliff with the financial flexibility to develop and expand its two major resource plays while protecting its balance sheet during this very low natural gas price environment. The Corporation does not foresee any liquidity issues with respect to the operation of its oil and natural gas business throughout the second half of 2012 and into 2013. Birchcliff expects to meet its future obligations as they become due.

The Corporation intends to finance its business primarily through cash flow, working capital, potential sales of non-core assets and available bank credit facilities. Should commodity prices continue to deteriorate materially, Birchcliff may adjust its capital spending accordingly. Birchcliff does not anticipate it will require additional equity except to fund a significant acquisition or to significantly increase its capital spending beyond its cash flow. Management expects to be able to continue to obtain debt financing, and should the need arise, raise additional equity sufficient to meet both its short term and long term growth requirements.

Capital Expenditures

The Corporation's 2012 capital spending program of $292 million is largely focused on the Phase III expansion of the PCS Gas Plant and the drilling, completion and tie-in of Montney/Doig horizontal natural gas wells that will produce to the expanded PCS Gas Plant. The Corporation also continues to develop the Montney/Doig Natural Gas Resource Play and the Worsley Light Oil Resource Play and other associated infrastructure.

Birchcliff's operating cash flow, the net proceeds from two recent equity offerings and bank indebtedness will be used to fund the 2012 capital spending program.

PCS Gas Plant and Resource Plays

Birchcliff's Phase III expansion of the PCS Gas Plant remains on schedule to commence processing natural gas on or before November 1, 2012. The Energy Resources Conservation Board has re-licensed the PCS Gas Plant to allow for increased processing volumes of 150 MMcf per day of raw inlet volume from the former licensed processing capacity of 120 MMcf per day. This re-licensing recognizes the design processing capacity of the PCS Gas Plant once the Phase III expansion is complete. To operate the PCS Gas Plant at 150 MMcf per day will require twinning of the sales gas pipeline, but the capital required is not material. The wholly owned and operated PCS Gas Plant will continue to increase the value of the Montney/Doig Natural Gas Resource Play by allowing for production growth, reducing operating costs per boe and increasing Birchcliff's strategic control over the Pouce Coupe area.

Birchcliff has a very strong asset base with its two main resource plays, the Montney/Doig Natural Gas Resource Play and the Worsley Light Oil Resource Play. The extensive portfolio of development opportunities on these resource plays will provide Birchcliff with repeatable, low risk, long life future production and reserves additions that are readily available with the investment of additional capital. Birchcliff continues to investigate and work towards development of new resource plays in its core area, the Peace River Arch.

Birchcliff's resource plays provide the Corporation with a long term and operationally reliable production base, the level of cash flow from which is primarily dependent on commodity prices. Commodity prices therefore affect the pace at which Birchcliff invests in its resource plays and the rate at which its production will grow. Weak short term commodity prices do not affect the quality or long term value of the Corporation's long-life asset base.

MAJOR TRANSACTIONS AFFECTING FINANCIAL RESULTS

Equity Financings

On April 19, 2012, Birchcliff completed a bought deal equity financing and a private placement for gross proceeds of $110 million. The Corporation issued 8,075,000 common shares at a price of $7.65 per common share for gross proceeds of $61.8 million and 1,100,000 common shares on a "flow-through" basis pursuant to the *Income Tax Act* (Canada), at a price of $9.20 per share for gross proceeds of $10.1 million. Birchcliff's major shareholder, purchased 5,000,000 common shares issued at a price of $7.65 per share in a concurrent private placement for gross proceeds of $38.3 million. Further details regarding the April Financing can be found in the Corporation's short form prospectus dated April 12, 2012, which is available on the SEDAR website at www.sedar.com.

On August 8, 2012, Birchcliff completed a bought deal equity financing for gross proceeds of $50 million. The Corporation issued 2,000,000 preferred units at a price of $25.00 per preferred unit for gross proceeds of $50 million. Each preferred unit was comprised of one cumulative redeemable five year rate reset preferred share, series A (a "**Series A Preferred Share**") of Birchcliff, to yield initially 8% per annum, and three common share purchase warrants (each a "**Warrant**") of Birchcliff. Each Warrant provides the right to purchase one common share of the Corporation for a period of two years from the closing date of August 8, 2012, at an exercise price of $8.30 per common share. A total aggregate of two million Series A Preferred Shares and six million Warrants were issued in the August Financing.

The Series A Preferred Shares pay cumulative dividends of $2.00 per Series A Preferred Share per annum, payable quarterly if, as and when declared by Birchcliff's board of directors, with the first quarterly dividend to be paid on September 30, 2012 (or the next business day), for the initial five year period ending September 30, 2017. Holders of the Series A Preferred Shares have the right, at their option, to convert their Series A Preferred Shares into cumulative redeemable floating rate series B preferred shares, subject to certain conditions, on September 30, 2017 and on September 30 of every five years thereafter. Further details regarding the August Financing can be found in the Corporation's short form prospectus dated July 30, 2012, which is available on the SEDAR website at www.sedar.com.

The aggregate net proceeds of the April Financing and the August Financing were used to reduce indebtedness under the Revolving Credit Facilities.

Credit Facilities

On June 26, 2012, the Corporation's bank syndicate approved an increase of the Revolving Credit Facilities to an aggregate limit of $470 million from $450 million and extended the conversion date of those facilities to May 17, 2013. The amended Revolving Credit Facilities include an increased credit limit for the extendible revolving term credit facility (the "**Syndicated Credit Facility**") of $440 million from $420 million and an extendible revolving working capital facility (the "**Working Capital Facility**") of $30 million. Four additional banks were added to the bank syndicate, which now consists of nine banks led by The Bank of Nova Scotia.

LIQUIDITY AND CAPITAL RESOURCES

Working Capital

The Corporation's working capital deficit (current assets minus current liabilities) increased to $54.8 million at June 30, 2012 from $48.6 million at December 31, 2011. The deficit at June 30, 2012 is largely comprised of costs incurred for the Phase III expansion of the PCS Gas Plant and associated wells and related infrastructure.

At June 30, 2012, the major components of Birchcliff's current assets were: joint interest billings to be received from its partners (19%) and revenue to be received from its marketers in respect of June 2012 production (67%), which was subsequently received in July 2012. In contrast, current liabilities largely consisted of trade payables (52%) and accrued capital and operating costs (42%). Birchcliff routinely assesses the financial strength of its marketers and joint venture partners in accordance with the Corporation's credit risk guidelines. At this time, Birchcliff expects that such counterparties will be able to meet their financial obligations during this period of low natural gas prices.

Birchcliff manages its working capital using its cash flow and advances under its bank credit facilities. The Corporation's working capital deficit does not reduce the amount available under its bank credit facilities. The Corporation did not identify any liquidity issues with respect to the operation of its petroleum and natural gas business during the second quarter of 2012.

Total Debt and Bank Debt

Total debt, including the working capital deficit, was $455.7 million at June 30, 2012 as compared to $437.0 million at December 31, 2011. Total debt from the end of 2011 was increased by $126.5 million in total capital expended in the first half of 2012 in excess of cash flow during that period and was reduced by net proceeds of $106.2 million from the April Financing. The amount outstanding under Birchcliff's bank credit facilities at June 30, 2012 was $400.9 million (December 31, 2011 – $388.4 million), which is net of $4.5 million (December 31, 2011 – $4.8 million) in unamortized interest and fees. A significant portion of the funds drawn under the bank credit facilities in the Reporting Periods was to pay costs relating to the Phase III expansion of the PCS Gas Plant, including drilling and completion of new Montney/Doig horizontal natural gas wells that will produce to Phase III of the PCS Gas Plant once it becomes operational and for drilling activities on the Worsley Light Oil Resource Play.

After giving effect to the net proceeds of approximately $48 million from the August Financing, Birchcliff's pro forma outstanding debt and total debt at June 30, 2012 would have been approximately $353 million and $408 million, respectively.

The following table shows the Corporation's total unused bank credit facilities:

As at,	June 30, 2012	December 31, 2011
Maximum borrowing base limit[(1)(2)]:		
Non-Revolving Five-Year Term Facility	70,000	70,000
Revolving Credit Facilities	470,000	450,000
	540,000	520,000
Principal amount utilized:		
Drawn Non-Revolving Five-Year Term Facility[(3)]	(70,000)	(70,000)
Drawn Revolving Credit Facilities[(3)]	(335,391)	(323,221)
Outstanding Letters of Credit[(4)]	(2,668)	(2,668)
	(408,059)	(395,889)
Total unused credit	**131,941**	124,111
Total unused credit after the August Financing - Pro Forma June 30, 2012[(5)]	**179,941**	Not applicable

(1) The Corporation's credit facilities are subject to a semi-annual review of the borrowing base limit, which is directly impacted by the value of Birchcliff's petroleum and natural gas reserves. On June 26, 2012, the Corporation's borrowing base limit under its Revolving Credit Facilities was increased to an aggregate limit of $470 million from $450 million.

(2) The Corporation was compliant with all financial covenants applicable under its credit facilities as at and during the periods ended June 30, 2012 and December 31, 2011 and continues to be compliant with such covenants at the date hereof.

(3) The drawn amounts are not reduced for unamortized costs and fees. The drawn Revolving Credit Facilities at the end of the Reporting Period consists of approximately $16.4 million (2011 – $19.2 million) applicable to the Working Capital Facility (including outstanding cheques) and $319 million (2011 - $304 million) applicable to the Syndicated Credit Facility.

(4) Letters of credit are issued to various service providers. There were no amounts drawn on the letters of credit as at and during the periods ended June 30, 2012 and December 31, 2011.

(5) The total unused credit at June 30, 2012 of $131.9 million has been increased by the net proceeds of approximately $48.0 million from the August Financing, which were applied after the Reporting Period to reduce bank indebtedness.

Contractual Obligations

The Corporation enters into contractual obligations in the ordinary course of conducting its day-to-day business. The following table lists Birchcliff's estimated material contractual obligations at June 30, 2012:

	2012	2013	2014 - 2016	Thereafter
Accounts payable and accrued liabilities	79,808	-	-	-
Drawn Non-Revolving Five-Year Term Facility	-	700	69,300	-
Drawn Revolving Credit Facilities	-	-	335,391	-
Office lease[(1)]	1,598	3,295	9,885	3,018
Transportation and processing	8,447	15,976	17,422	-
Total estimated contractual obligations[(2)]	**89,853**	**19,971**	**431,998**	**3,018**

(1) The Corporation is committed under an operating lease relating to its office premises, beginning December 1, 2007 and expiring on November 30, 2017. Birchcliff does not presently use all of the leased premises and has sublet approximately 24% of the excess space to an arms' length party on a basis that recovers all of the rental costs for the first five years.

(2) Contractual commitments that are routine in nature and form part of the normal course of operations for Birchcliff are not included in the table above.

Capital Resources

The following table sets forth a summary of the Corporation's capital resources:

Three months ended June 30,	2012	2011
Cash flow	25,985	34,269
Changes in non-cash working capital from operations	(14,649)	6,848
Decommissioning expenditures	(42)	(212)
Issue of common shares	111,235	2,092
Share issue costs	(3,972)	-
Financing fees paid	(600)	(1,356)
Increase in Non-Revolving Five-Year Term Facility	930	69,456
Decrease in Revolving Credit Facilities	(41,997)	(64,506)
Changes in non-cash working capital from investing	(18,093)	(14,291)
Total capital resources	**58,797**	32,300

Six months ended June 30,	2012	2011
Cash flow	52,181	66,582
Changes in non-cash working capital from operations	(12,177)	(2,958)
Decommissioning expenditures	(94)	(678)
Issue of common shares	112,282	7,298
Share issue costs	(3,972)	-
Financing fees paid	(600)	(1,356)
Increase in Non-Revolving Five-Year Term Facility	237	69,456
Increase (decrease) in Revolving Credit Facilities	12,403	(63,008)
Changes in non-cash working capital from investing	18,388	4,345
Total capital resources	**178,648**	79,681

Off-Balance Sheet Transactions

Birchcliff was not involved in any off-balance sheet transactions that would result in a material change to its financial position, performance or cash flows as at or during the three and six months ended June 30, 2012.

OUTSTANDING SHARE INFORMATION

The common shares of Birchcliff are the only class of shares outstanding as at June 30, 2012. Birchcliff's common shares began trading on the TSX on July 21, 2005 under the symbol "**BIR**" and were at the same time de-listed from the TSX Venture Exchange where they were trading under the same symbol prior to such time. Birchcliff's common shares are included in the S&P/TSX Composite Index.

On August 8, 2012, Birchcliff's Series A Preferred Shares and Warrants were individually listed on the TSX under the symbols BIR.PR.A and BIR.WT, respectively.

The following table summarizes the common shares issued in the Reporting Periods:

	Common shares
Balance at December 31, 2011	126,745,577
Issue of common shares upon exercise of options	260,000
Balance at March 31, 2012	127,005,577
Issue of common shares[1]	13,075,000
Issue of flow-through common shares[1]	1,100,000
Issue of common shares upon exercise of options	253,067
Balance at June 30, 2012	**141,433,644**

(1) Issued in conjunction with the April Financing.

At August 14, 2012, there were outstanding 141,475,311 common shares, 2,000,000 Series A Preferred Shares, 6,000,000 Warrants to purchase an equivalent number of common shares, stock options to purchase 12,691,072 common shares, and 2,939,732 performance warrants to purchase an equivalent number of common shares.

RESULTS OF OPERATIONS

Petroleum and Natural Gas Revenues

Petroleum and Natural Gas ("**P&NG**") revenues totalled $57.7 million ($28.78 per boe) for the three month Reporting Period and $120.6 million ($30.74 per boe) for the six month Reporting Period as compared to $67.5 million ($42.79 per boe) and $130.3 million ($41.05 per boe) for the Comparable Prior Periods. The decrease in P&NG revenues from the Comparable Prior Periods was largely due to lower average oil and natural gas prices realized at the wellhead offset by an increase in average daily oil and natural gas production in the current quarter. The following table details Birchcliff's P&NG revenues, production and percentage of production and sales prices by category:

	Three months ended June 30, 2012				Three months ended June 30, 2011			
	Total Revenue ($000's)	Average Daily Production	%	Average ($/unit)	Total Revenue ($000's)	Average Daily Production	%	Average ($/unit)
Light oil (bbls)	32,959	4,447	20	81.45	32,440	3,589	21	99.31
Natural gas (Mcf)	18,777	100,843	76	2.05	29,699	78,714	76	4.15
Natural gas liquids (bbls)	5,966	785	4	83.53	5,271	615	3	94.15
Total P&NG sales	57,702	**22,039**	100	28.77	67,410	17,324	100	42.76
Royalty revenue	27			0.01	54			0.03
Total P&NG revenues	**57,729**			**28.78**	67,464			42.79

	Six months ended June 30, 2012				Six months ended June 30, 2011			
	Total Revenue ($000's)	Average Daily Production	%	Average ($/unit)	Total Revenue ($000's)	Average Daily Production	%	Average ($/unit)
Light oil (bbls)	70,472	4,511	21	85.84	61,767	3,666	21	93.08
Natural gas (Mcf)	38,876	98,042	76	2.18	58,849	79,635	76	4.08
Natural gas liquids (bbls)	11,151	699	3	87.71	9,513	593	3	88.63
Total P&NG sales	120,499	**21,550**	100	30.72	130,129	17,532	100	41.01
Royalty revenue	63			0.02	128			0.04
Total P&NG revenues	**120,562**			**30.74**	130,257			41.05

Commodity Prices

Birchcliff sells all of its crude oil on a spot basis and virtually all of its natural gas production for prices based on the AECO natural gas spot price. Birchcliff receives premium pricing for its natural gas due to its high heat content. The following table details the average sales price and differential received by Birchcliff for its natural gas production:

	Three months ended June 30, 2012	Three months ended June 30, 2011	**Six months ended June 30,2012**	Six months ended June 30,2011
Average natural gas sales price ($/Mcf)	2.05	4.15	2.18	4.08
Average AECO natural gas spot price ($/Mcf)(1)	1.89	3.87	2.02	3.83
Positive differential	**0.16**	0.28	**0.16**	0.25

(1) $1.00/MMbtu = $1.00/Mcf based on a standard heat value Mcf.

The price the Corporation receives for its petroleum and natural gas production depends on a number of factors, including Canadian dollar AECO spot market prices for natural gas, Canadian dollar Edmonton Par oil prices, US dollar oil prices, the US-Canadian dollar exchange rate and transportation and product quality differentials. Birchcliff did not have any financial derivatives such as commodity price risk management contracts, forward exchange rate contracts or interest rate swaps in place during the Reporting Periods and Comparable Prior Periods, but it actively monitors the market to determine if any are required. The Corporation has no current intention to enter into any such contracts at the date hereof.

Royalties

Birchcliff recorded a royalty expense of $6.0 million ($3.00 per boe) for the three month Reporting Period and $13.3 million ($3.39 per boe) for the six month Reporting Period as compared to $8.8 million ($5.58 per boe) and $15.0 million ($4.73 per boe) for the Comparable Prior Periods. Royalties are paid primarily to the Alberta Government and, to a lesser extent, to other land and mineral rights owners. The following table details the Corporation's royalty expense:

	Three months ended June 30, 2012	Three months ended June 30, 2011	**Six months ended June 30, 2012**	Six months ended June 30, 2011
Oil & natural gas royalties ($000's)	**6,026**	8,801	**13,294**	15,000
Oil & natural gas royalties ($/boe)	**3.00**	5.58	**3.39**	4.73
Effective royalty rate (%)[1]	**10%**	13%	**11%**	12%

(1) The effective royalty rate is calculated by dividing the total aggregate royalties into petroleum and natural gas sales for the period.

The decrease in the effective royalty rate from the Comparable Prior Periods was mainly due to significantly lower natural gas prices realized at the wellhead during the Reporting Periods and the effect these lower prices have on the sliding scale royalty calculation. This was offset by lower royalty credits against natural gas royalties payable during the Reporting Periods. Lower natural gas prices reduces the Crown facility effective royalty rates that are used to determine the gas cost allowance credits available in the period. Average natural gas prices realized at the wellhead decreased by 51% and 47% from the three and six months ended June 30, 2011.

Operating Costs

Operating costs were $12.5 million ($6.22 per boe) for the three month Reporting Period and $24.3 million ($6.20 per boe) for the six month Reporting Period as compared to $10.6 million ($6.74 per boe) and $21.8 million ($6.85 per boe) for the Comparable Prior Periods. The following table provides a breakdown of total operating costs:

	Three months ended June 30, 2012		Three months ended June 30, 2011	
	($000's)	$/boe	($000's)	$/boe
Field operating costs	14,075	7.02	12,306	7.81
Recoveries	(1,687)	(0.84)	(1,694)	(1.07)
Field operating costs, net	12,388	6.18	10,612	6.74
Expensed workovers and other	93	0.04	6	-
Total operating costs	**12,481**	**6.22**	10,618	6.74
	Six months ended June 30, 2012		Six months ended June 30, 2011	
	($000's)	$/boe	($000's)	$/boe
Field operating costs	27,721	7.07	25,131	7.92
Recoveries	(3,630)	(0.93)	(3,813)	(1.20)
Field operating costs, net	24,091	6.14	21,318	6.72
Expensed workovers and other	220	0.06	434	0.13
Total operating costs	**24,311**	**6.20**	21,752	6.85

Total operating costs per boe decreased by 8% and 9% from the three and six month Comparable Prior Periods largely due to the cost benefits achieved from processing natural gas at the PCS Gas Plant.

During the first half of 2012, Birchcliff's total operating costs (net of recoveries) at the PCS Gas Plant were approximately $1.56 per boe on a production month basis.

Birchcliff continues to focus on controlling the infrastructure it uses to produce its oil and natural gas and on reducing operating costs on a per boe basis.

Transportation and Marketing Expenses

Transportation and marketing expenses were $4.8 million ($2.39 per boe) for the three month Reporting Period and $9.3 million ($2.38 per boe) for the six month Reporting Period as compared to $4.2 million ($2.67 per boe) and $8.2 million ($2.60 per boe) for the Comparable Prior Periods. These aggregate costs consist primarily of transportation expenses that were higher in the Reporting Periods mainly due to an increase in production volumes of both oil and natural gas and trucking oil further distances during the Reporting Periods.

Administrative Expenses

Net administrative expenses were $5.8 million ($2.90 per boe) for the three month Reporting Period and $15.3 million ($3.92 per boe) for the six month Reporting Period as compared to $7.1 million ($4.52 per boe) and $13.5 million ($4.24 per boe) for the Comparable Prior Periods. The components of net administrative expenses are detailed in the table below:

	Three months ended June 30, 2012		Three months ended June 30, 2011	
	($000's)	%	($000's)	%
Cash:				
Salaries and benefits(1)	3,578	61	3,259	52
Other(2)	2,333	39	2,966	48
	5,911	100	6,225	100
Operating overhead recoveries	(265)	(4)	(245)	(4)
Capitalized overhead(3)	(1,112)	(19)	(1,148)	(18)
General & administrative, net	4,534	77	4,832	78
General & administrative, net per boe	$2.26		$3.07	
Non-cash:				
Stock-based compensation	1,832	100	3,470	100
Capitalized stock-based compensation(3)	(550)	(30)	(1,188)	(34)
Stock-based compensation, net	1,282	70	2,282	66
Stock-based compensation, net per boe	$0.64		$1.45	
Total administrative expenses, net	**5,816**		7,114	
Total administrative expenses, net per boe	**$2.90**		$4.52	

(1) Includes salaries, benefits and bonuses paid to all Officers and employees of the Corporation.

(2) Includes costs such as rent, legal, tax, insurance, minor computer hardware and software and other business expenses incurred by the Corporation.

(3) Includes a portion of salaries and benefits and stock-based compensation directly attributed to the exploration and development activities which have been capitalized.

	Six months ended June 30, 2012		Six months ended June 30, 2011	
	($000's)	%	($000's)	%
Cash:				
Salaries and benefits(1)(2)	9,758	64	6,478	55
Other(3)	5,587	36	5,336	45
	15,345	100	11,814	100
Operating overhead recoveries	(457)	(3)	(562)	(5)
Capitalized overhead(4)	(2,468)	(16)	(2,109)	(18)
General & administrative, net	12,420	81	9,143	77
General & administrative, net per boe	$3.17		$2.88	
Non-cash:				
Stock-based compensation	4,325	100	6,440	100
Capitalized stock-based compensation(4)	(1,403)	(32)	(2,110)	(33)
Stock-based compensation, net	2,922	68	4,330	67
Stock-based compensation, net per boe	$0.75		$1.36	
Total administrative expenses, net	**15,342**		13,473	
Total administrative expenses, net per boe	**$3.92**		$4.24	

(1) Includes salaries, benefits and bonuses paid to all Officers and employees of the Corporation.
(2) In March 2012, Birchcliff accrued approximately $2.4 million in retention payments that were subsequently paid in April 2012 as a result of the termination in the corporate sale process.
(3) Includes costs such as rent, legal, tax, insurance, minor computer hardware and software and other business expenses incurred by the Corporation.
(4) Includes a portion of salaries and benefits and stock-based compensation directly attributed to the exploration and development activities which have been capitalized.

Net cash general and administrative expense increased on an aggregate basis from the six month Comparable Prior Period largely due to non-recurring costs of $2.9 million incurred in the first quarter of 2012 in respect of the corporate sale process.

Non-cash stock-based compensation expense decreased on an aggregate basis from the Comparable Prior Periods mainly due to a lower Black-Scholes fair value expense calculated for stock options granted in the current quarter. The weighted average fair value per option was $2.44 in the three month Reporting Period as compared to $5.81 for the same period in 2011. The inputs used in calculating the Black Scholes weighted average fair value per option are tabled in Note 8 of the interim condensed financial statements for the Reporting Periods. A summary of the Corporation's outstanding stock options is presented below:

	Number	**Weighted Average Exercise Price ($)**
Outstanding, December 31, 2011	10,466,941	8.73
Exercised	(260,000)	(4.03)
Outstanding, March 31, 2012	10,206,941	8.85
Granted(1)	3,400,900	5.97
Exercised	(253,067)	(4.31)
Forfeited	(380,834)	(9.68)
Expired	(115,200)	(10.34)
Outstanding, June 30, 2012	**12,858,740**	**8.14**

(1) On April 26, 2012, the Corporation issued 3,345,400 stock options to officers and employees of Birchcliff at an exercise price of $5.96 per common share as a result of its annual compensation review.

There are 2,939,732 performance warrants with an exercise price of $3.00 that are outstanding and exercisable at June 30, 2012. Each stock option and performance warrant entitles the holder to purchase one common share at the exercise price.

Depletion and Depreciation Expenses

Depletion and Depreciation ("**D&D**") expenses were $23.0 million ($11.48 per boe) for the three month Reporting Period and $45.2 million ($11.52 per boe) for the six month Reporting Period as compared to $16.0 million ($10.17 per boe) and $32.1 million ($10.12 per boe) for the Comparable Prior Periods. D&D expenses increased on an aggregate basis mainly due to a 27% and 23% increase in average daily production from the three and six months ended June 30, 2011.

D&D is a function of the estimated proved plus probable reserve additions, the finding and development costs attributable to those reserves, the associated future development capital required to recover those reserves and production in the period. The Corporation determines its D&D expenses on an area basis.

Impairment Test

In light of the low natural gas commodity price environment, Birchcliff performed an impairment review of its petroleum and natural gas assets on a cash-generating unit basis to assess for recoverability. The Corporation's assets were not impaired at June 30, 2012. In determining the recoverable amount of the Corporation's cash-generating unit, Birchcliff applied a pre-tax discount rate of 10% on cash flows from proved plus probable reserves. The petroleum and natural gas future prices are based on commodity price forecasts of the Corporation's independent reserves evaluator at June 30, 2012.

Finance Expenses

Finance expenses were $4.6 million ($2.28 per boe) for the three month Reporting Period and $10.3 million ($2.62 per boe) for the six month Reporting Period as compared to $5.4 million ($3.42 per boe) and $10.9 million ($3.44 per boe) for the Comparable Prior Periods. The components of the Corporation's finance expenses are shown in the table below:

	Three months ended June 30, 2012		Three months ended June 30, 2011	
	($000's)	$/boe	($000's)	$/boe
Cash:				
Interest on credit facilities	3,913	1.95	4,724	2.99
Non-cash:				
Accretion on decommissioning obligations	440	0.22	446	0.28
Amortization of deferred financing fees	212	0.11	236	0.15
Total finance expenses	**4,565**	**2.28**	5,406	3.42

	Six months ended June 30, 2012		Six months ended June 30, 2011	
	($000's)	$/boe	($000's)	$/boe
Cash:				
Interest on credit facilities	9,038	2.30	9,533	3.01
Non-cash:				
Accretion on decommissioning obligations	874	0.22	884	0.28
Amortization of deferred financing fees	411	0.10	490	0.15
Total finance expenses	**10,323**	**2.62**	10,907	3.44

The aggregate interest expense from the Comparable Prior Periods decreased mainly due to lower pricing margins (that are used to determine Birchcliff's average effective interest rate) that became applicable when the bank syndicate increased the credit limit under its Revolving Credit Facilities, offset by higher average balance on the outstanding bank credit facilities.

The Corporation's average outstanding total credit facilities balance was approximately $402 million and $404 million during the three and six month Reporting Periods as compared to $338 million and $336 million in the Comparable Prior Periods, calculated as the simple average of the month end amounts. This increase was largely due to significant capital expended on the PCS Gas Plant project.

The effective interest rate applicable to the Working Capital Facility was 5.0% at the end of the Reporting Period as compared to 5.8% at the end the Comparable Prior Period. The effective interest rate applicable to the bankers' acceptances issued under the revolving Syndicated Credit Facility was 4.7% in each of the three and six month Reporting Periods as compared to 5.7% and 5.6% in the Comparable Prior Periods. The effective interest rate applicable to the bankers' acceptances issued under the Non-Revolving Five-Year Term Facility was 5.4% and 5.2% in the three and six month Reporting Periods as compared to 5.1% in the Comparable Prior Periods.

Gain on Sale of Assets

During the six month Reporting Period, Birchcliff completed a transaction whereby it disposed of a non-core asset in the Glacier area of Alberta in exchange for strategic assets acquired in the Pouce Coupe area of Alberta. The fair value of the transaction was estimated at $25 million. As a result of the disposition, Birchcliff recorded a gain on sale of approximately $3.9 million ($2.9 million, net of tax) or $0.99 per boe during the six month Reporting Period.

Income Taxes

Birchcliff recorded a deferred income tax expense of $0.6 million ($0.30 per boe) for the three month Reporting Period and $2.5 million ($0.64 per boe) for the six month Reporting Period as compared to $4.2 million ($2.69 per boe) and $8.2 million ($2.57 per boe) for the Comparable Prior Periods. The decrease in deferred income tax expense was due to lower net income before tax in the Reporting Periods.

The Corporation's estimated income tax pools totaled approximately $1.1 billion at June 30, 2012. Management expects that future taxable income will be available to utilize accumulated tax pools. Birchcliff's estimated tax pools at June 30, 2012 are comprised of the following:

	Tax pools as at June 30, 2012
Canadian oil and gas property expense (COGPE)	275,150
Canadian development expense (CDE)	280,446
Canadian exploration expense (CEE)	183,608
Undepreciated cost of capital (UCC)	229,009
Non-capital losses (NCL)	161,088
Financing costs	4,800
Total estimated income tax pools	**1,134,101**

The Corporation's income tax pools totalling $39.3 million in respect of the Veracel Inc. ("**Veracel**") transaction continues to be under review by Canada Revenue Agency. Management believes that it will be successful in defending its tax position respecting the Veracel transaction, and as such, the Corporation has not recognized a related provision for deferred income tax liability at June 30, 2012.

Capital Expenditures

The following table sets forth a summary of the Corporation's capital expenditures:

Three months ended June 30,	**2012**	2011
Land	2,138	6,398
Seismic	118	262
Workovers	760	3,334
Drilling and completions	30,499	16,399
Well equipment and facilities	25,220	7,042
Total finding and development costs (F&D)	58,735	33,435
Acquisitions	-	4,138
Dispositions	-	(5,541)
Total finding, development and acquisition costs (FD&A)	58,735	32,032
Administrative assets	80	268
Total capital expenditures	**58,815**	32,300
Six months ended June 30,	**2012**	2011
Land	4,617	11,461
Seismic	450	2,876
Workovers	5,667	7,324
Drilling and completions	100,218	45,907
Well equipment and facilities	67,477	17,360
Total finding and development costs (F&D)	178,429	84,928
Acquisitions(1)	25,006	4,356
Dispositions(1)	(24,942)	(5,541)
Total finding, development and acquisition costs (FD&A)	178,493	83,743
Administrative assets	174	736
Total capital expenditures	**178,667**	84,479

(1) During the six month Reporting Period, Birchcliff completed a transaction whereby it disposed of a non-core asset in the Glacier area of Alberta in exchange for strategic assets acquired in the Pouce Coupe area of Alberta. The fair value of the transaction was estimated at $25 million. This transaction resulted in a gain on sale of approximately $3.9 million during the six month Reporting Period.

SUMMARY OF QUARTERLY RESULTS

The following are the quarterly results of the Corporation for the eight most recently completed quarters:

Quarters Ended ($000's, except for production, share and per share amounts)	**June 30, 2012**	March 31, 2012	December 31, 2011	September 30, 2011
Petroleum and natural gas production (boe per day)	22,039	21,061	19,812	17,648
Petroleum and natural gas commodity price at wellhead ($ per boe)	28.77	32.77	38.54	39.42
Natural gas commodity price at wellhead ($ per Mcf)	2.05	2.32	3.40	3.92
Petroleum commodity price at wellhead ($ per bbl)	81.45	90.10	95.52	86.40
Total petroleum and natural gas revenue	57,729	62,833	70,261	64,069
Total royalties	(6,026)	(7,268)	(7,585)	(6,804)
Total revenues, net	51,703	55,565	62,676	57,265
Total capital expenditures, net	58,815	119,852	81,023	71,978
Net income	416	3,731	3,333	11,411
Per share basic ($)	-	0.03	0.03	0.09
Per share diluted ($)	-	0.03	0.03	0.09
Cash flow	25,985	26,196	30,400	33,844
Per share basic ($)	0.19	0.21	0.24	0.27
Per share diluted ($)	0.19	0.20	0.23	0.26
Book value of total assets	1,350,759	1,314,633	1,225,497	1,138,075
Non-Revolving Five-Year Term Facility	69,232	68,267	68,925	68,811
Revolving Credit Facilities	331,644	374,064	319,500	290,495
Total debt	455,708	529,883	437,023	386,296
Shareholders' equity	772,671	663,872	656,602	648,905
Common shares outstanding – end of period				
Basic	141,433,644	127,005,577	126,745,577	126,679,577
Diluted	157,232,116	140,152,250	140,152,250	140,149,250
Weighted average common shares outstanding				
Basic	138,425,779	126,753,764	126,731,919	126,630,446
Diluted	138,837,321	131,008,290	132,216,022	131,374,723

Quarters Ended ($000's, except for production, share and per share amounts)	June 30, 2011	March 31, 2011	December 31, 2010	September 30, 2010
Petroleum and natural gas production (boe per day)	17,324	17,742	16,375	13,109
Petroleum and natural gas commodity price at wellhead ($ per boe)	42.76	39.28	37.83	36.60
Natural gas commodity price at wellhead ($ per Mcf)	4.15	4.02	3.94	3.79
Petroleum commodity price at wellhead ($ per bbl)	99.31	87.03	81.89	76.44
Total petroleum and natural gas revenue	67,464	62,793	57,072	44,125
Total royalties	(8,801)	(6,199)	(4,388)	(3,561)
Total revenues, net	58,663	56,594	52,684	40,564
Total capital expenditures, net[(1)]	32,300	52,179	45,730	92,520
Net income[(1)]	10,117	9,593	7,431	5,533
Per share basic ($)[(1)]	0.08	0.08	0.06	0.04
Per share diluted ($)[(1)]	0.08	0.07	0.06	0.04
Cash flow[(1)]	34,269	32,313	27,865	22,750
Per share basic ($)[(1)]	0.27	0.26	0.22	0.18
Per share diluted ($)[(1)]	0.26	0.25	0.22	0.18
Book value of total assets[(1)]	1,080,314	1,069,322	1,038,555	996,327
Non-Revolving Five-Year Term Facility	68,773	-	-	-
Revolving Credit Facilities	270,278	335,220	333,468	281,172
Total debt	349,190	352,804	337,424	319,921
Shareholders' equity[(1)]	632,588	616,909	599,140	587,796
Common shares outstanding – end of period				
Basic	126,496,677	126,127,244	125,129,234	124,912,134
Diluted	140,137,084	139,963,084	137,316,486	137,364,386
Weighted average common shares outstanding				
Basic	126,322,814	125,424,658	124,994,761	124,872,806
Diluted[(1)]	131,380,901	129,715,133	128,418,091	128,338,449

(1) 2010 comparative quarters are restated to comply with International Financial Reporting Standards.

DISCUSSION OF QUARTERLY RESULTS

Production

Production in the second quarter of 2012 averaged 22,039 boe per day, a 5% increase from 21,061 boe per day in the first quarter of 2012 and a 27% increase from 17,324 boe per day in the second quarter of 2011. These increases were largely achieved through the success of Birchcliff's capital drilling program with increased production from new Montney/Doig horizontal natural gas wells that were tied into Phase I and Phase II of the PCS Gas Plant and increased production from the Worsley Light Oil Resource Play from the second quarter of 2011. Birchcliff's natural gas production in the current quarter was 6% higher than the first quarter of 2012 and 28% higher than the second quarter of 2011. Light oil production in the current quarter decreased by 3% from the first quarter of 2012 and increased by 24% from the second quarter of 2011.

Cash Flow and Earnings

Cash flow generated by the Corporation in the second quarter of 2012 was $26.0 million as compared to $26.2 million in the first quarter of 2012 and $34.3 million in the second quarter of 2011. Cash flow as compared to the first quarter of 2012 was negatively impacted by lower realized oil and natural gas wellhead prices, positively offset by higher average daily production, lower net general and administrative expenses (due to one-time costs of $2.9 million accrued in the first quarter of 2012 related to the corporate sale process), decreased interest expense and lower royalty expenses. The decrease in aggregate cash flow from second quarter of 2011 is mainly attributed to significantly lower natural gas prices, with the AECO natural gas spot price having decreased 51% from the comparative quarter. Cash flow was also negatively impacted by lower realized oil wellhead prices, positively offset by higher average daily production, lower net general and administrative expenses, decreased interest expense and royalty expense. Higher average production resulted in some increases to aggregate operating expenses and transportation and marketing costs in the current quarter.

Notwithstanding this very low natural gas price environment, Birchcliff has reported net income in each of its last eleven recently completed quarters. Birchcliff recorded net income of $0.4 million in the second quarter of 2012 as compared to $3.7 million in the first quarter of 2012 and $10.1 million in the second quarter of 2011. The decrease in net income from the comparative quarters was mainly attributable to lower cash flow, increase in depletion expense resulting from higher average daily production in the current quarter and gains on divestures reported in each of the comparative quarters, offset by lower stock-based compensation expense in the second quarter of 2012.

Capital Expenditures

Total capital expenditures (excluding minor acquisitions and dispositions) in the second quarter of 2012 were $58.8 million as compared to $119.8 million in the first quarter of 2012 and $33.7 million in the second quarter of 2011. Of the $58.8 million, approximately $36.6 million (62%) was related to construction of Phase III of the PCS Gas Plant and the drilling and completion of Montney/Doig horizontal natural gas wells that will produce to Phase III of the PCS Gas Plant once it becomes operational on or before November 1, 2012. The remaining $22.2 million (38%) was spent on other infrastructure, expanding the Montney/Doig Natural Gas Resource Play and the Worsley Light Oil

Resource Play, acquiring land and on other oil and gas exploration and development projects in the Peace River Arch.

Total Debt

Total debt (including working capital deficit) was $455.7 million at the second quarter of 2012 as compared to $529.9 million at the first quarter of 2012 and $437.0 million at December 31, 2011. Total debt at the end of the Reporting Period was reduced by the net proceeds of $106.2 million from the April Financing that was used to pay down the Revolving Credit Facilities in the current quarter, offset by an increase in capital spending in excess of cash flow during the Reporting Periods. A significant portion of the capital spent during the Reporting Periods was on the PCS Gas Plant and drilling on the Worsley Light Oil Resource Play. Total debt was further reduced on August 8, 2012 by proceeds of $48 million from the August Financing.

Outstanding Shares

As a result of the April Financing, both the end of period and weighted average common shares outstanding at the second quarter of 2012 increased from the first quarter of 2012 and the second quarter of 2011.

MERGERS AND ACQUISITIONS

Within its focus area, the Corporation is always reviewing potential property acquisitions and corporate mergers and acquisitions for the purposes of determining whether any such potential transaction is of interest to the Corporation and the terms on which such a potential transaction would be available. As a result, the Corporation may from time to time be involved in discussions or negotiations with other parties or their agents in respect of potential property acquisitions and corporate merger and acquisition opportunities, but the Corporation is not committed to any such potential transaction and cannot be reasonably confident that it can complete any such potential transaction until appropriate legal documentation has been signed by the relevant parties.

CONTROLS AND PROCEDURES

Disclosure Controls and Procedures

The Corporation has established and maintained disclosure control and procedures (“**DC&P**”) that have been designed by, or under the supervision of, the Corporation’s Chief Executive Officer and the Chief Financial Officer (“**Certifying Officers**”) to provide reasonable assurance that information required to be disclosed by the Corporation in its annual filings, interim filings or other reports filed or submitted under securities legislation is accumulated and communicated to management, as appropriate, to allow timely decisions regarding required disclosure. The Certifying Officers have evaluated, or caused to be evaluated under their supervision, the effectiveness of the Corporation’s DC&P at June 30, 2012 and have concluded that the Corporation’s DC&P are appropriately designed and operating effectively to provide reasonable assurance that information required by securities legislation to be disclosed is made known to them by others, to allow timely decisions regarding the required disclosure.

While the Certifying Officers believe that the Corporation’s DC&P provide a reasonable level of assurance and are effective, they do not expect that the DC&P will prevent all errors and fraud. A control system, no matter how well conceived, maintained and operated, can provide only reasonable, but not absolute, assurance that the objectives of the control system will be met.

Internal Controls over Financial Reporting

The Corporation has established and maintains internal controls over financial reporting ("**ICFR**") that have been designed using the Committee of Sponsoring Organizations "Internal Control Over Financial Reporting - Guidance for Smaller Public Companies". The control framework was designed by, or under the supervision of, the Corporation's Certifying Officers to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with the generally accepted accounting principles applicable to the Corporation and to provide reasonable assurance that all assets are safeguarded and transactions are appropriately authorized and recorded to facilitate the preparation of relevant, reliable and timely information. The Certifying Officers have evaluated, or caused to be evaluated under their supervision, the effectiveness of the Corporation's ICFR at June 30, 2012 and have concluded that the Corporation's ICFR was effective at June 30, 2012 for the purposes described above. No changes were made to the Corporation's ICFR during the three months ended June 30, 2012 that have materially affected, or are reasonably likely to materially affect the Corporation's ICFR.

While the Certifying Officers believe that the Corporation's ICFR provide a reasonable level of assurance and are effective, they do not expect that the ICFR will prevent all errors and fraud. A control system, no matter how well conceived, maintained and operated, can provide only reasonable, but not absolute, assurance that the objectives of the control system will be met.

CRITICAL ACCOUNTING ESTIMATES

The preparation of the financial statements requires management to make judgments, estimates and assumptions that affect the application of IFRS accounting policies and reported amounts of assets and liabilities and income and expenses. Accordingly, actual results may differ from these estimates. Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected. The following are critical judgments and estimations that management has made in the process of applying the Corporation's IFRS accounting policies and that have the most significant effect on the amounts recognized in these financial statements:

Reserves

Estimation of reported recoverable quantities of proved and probable reserves include judgmental assumptions regarding production profile, commodity prices, exchange rates, remediation costs, timing and amount of future development costs, and production, transportation and marketing costs for future cash flows. It also requires interpretation of geological and geophysical models in order to make an assessment of the size, shape, depth and quality of reservoirs, and their anticipated recoveries. The economical, geological and technical factors used to estimate reserves may change from period to period. Changes in reported reserves can impact the carrying values of the Corporation's petroleum and natural gas properties and equipment, the calculation of depletion and depreciation, the provision for decommissioning obligations, and the recognition of deferred tax assets and liabilities due to changes in expected future cash flows. The recoverable quantities of reserves and estimated cash flows from

Birchcliff's petroleum and natural gas interests are independently evaluated by reserve engineers at least annually.

The Corporation's petroleum and natural gas reserves represent the estimated quantities of crude oil, natural gas and natural gas liquids which geological, geophysical and engineering data demonstrate, with a specified degree of certainty, to be economically recoverable in future years from known reservoirs and which are considered commercially producible. Such reserves may be considered commercially producible if management has the intention of developing and producing them and such intention is based upon: (i) a reasonable assessment of the future economics of such production; (ii) a reasonable expectation that there is a market for all or substantially all the expected oil and natural gas production; and (iii) evidence that the necessary production, processing transmission and transportation facilities are available or can be made available. Reserves may only be considered proven and probable if producibility is supported by either production or conclusive formation tests. Birchcliff's oil and gas reserves are determined pursuant to National Instrument 51-101 *Standard of Disclosures for Oil and Gas Activities and the Canadian Oil and Gas Evaluation Handbook*.

Decommissioning obligations

The Corporation estimates future remediation costs of production wells, facilities, and pipelines at different stages of development and construction of assets or facilities. In most instances, removal of assets occurs many years into the future. This requires judgment regarding abandonment date, future environmental and regulatory legislation, the extent of abandonment and reclamation activities, the engineering methodology for estimating cost, future removal technologies in determining the removal cost and liability-specific discount rates that are used to determine the present value of these cash flows.

Stock-based compensation

All share-based awards issued by the Corporation are fair valued using the Black-Scholes option-pricing model. In determining the share-based compensation expense for the period, estimates have to be made regarding the expected volatility in share price, option life, dividend yield and risk-free rate used to calculating fair value and estimating forfeitures at the initial grant date. Due to the time period and the number of estimates involved, it is likely that the actual fair value of the options will differ from what has been recorded in the financial statements.

Impairment of assets

The impairment testing of PP&E is based on estimates of proved plus probable reserves, production rates, forecasted petroleum and natural gas prices, future costs and other relevant assumptions. Birchcliff's assets are aggregated into cash-generating units, for the purpose of calculating impairment, based on their ability to generate largely independent cash inflows. By their nature, these estimates and assumptions are subject to measurement uncertainty and may impact the carrying value of the Corporation's assets in future periods.

Income taxes

Tax provisions are based on enacted or substantively enacted laws. Changes in those laws could affect amounts recognized in profit or loss both in the period of change, which would include any impact on cumulative provisions, and in future periods. All tax filings are subject to audit and potential reassessment. Accordingly, the actual income tax liability may differ significantly from amounts estimated and recorded in the financial statements.

CHANGES IN ACCOUNTING POLICIES

The following accounting standards and interpretations have been issued but are not yet effective.

In 2011, the IASB issued the following new and revised IFRSs effective for annual periods beginning on or after January 1, 2013. Earlier application is permitted providing that IFRS 10, IFRS 11, IFRS 12 and IFRS 13 are adopted together, except that IFRS 12 may be adopted earlier. Birchcliff is currently assessing the impact of adopting these pronouncements, however, it anticipates that these standards will not have a material impact on the Corporation's financial statements.

IFRS 10 *Consolidated Financial Statements* builds on existing principles by identifying the concept of control as the determining factor in whether an entity should be included within the consolidated financial statements of the parent company. The standard provides additional guidance to assist in the determination of control where this is difficult to assess. IFRS 10 replaces those parts of IAS 27 *Consolidated and Separate Financial Statements* (revised 2011) that address when and how an entity should prepare consolidated financial statements and replaces SIC 12 *Consolidation – Special Purpose Entities* in its entirety. IAS 27 retains the current guidance for separate financial statements.

IFRS 11 *Joint Arrangements* provides for a more substance based reflection of joint arrangements by focusing on the rights and obligations of the arrangement, rather than its legal form (as is currently the case). The standard addresses inconsistencies in the reporting of joint arrangements by requiring a single method to account for interests in jointly controlled entities. IFRS 11 supersedes IAS 31 *Interests in Joint Ventures* and SIC 13 *Jointly Controlled Entities – Non-Monetary Contributions by Ventures*. IAS 28 *Investments in Associates and Joint Ventures* (revised 2011) has been amended to conform to changes based on the issuance of IFRS 10 and IFRS 11.

IFRS 12 *Disclosure of Interests in Other Entities* requires extensive disclosures relating to an entity's interests in subsidiaries, joint arrangements, associates and unconsolidated structured entities. An entity is required to disclose information that helps users of its financial statements evaluate the nature of and risks associated with its interests in other entities and the effects of those interests on its financial statements. The effective date of IFRS 12 is January 1, 2013 but entities are permitted to incorporate any of the new disclosures in their financial statements before that date.

IFRS 13 *Fair Value Measurement* establishes a single framework for measuring fair values. This standard applies to all transactions and balances (whether financial or non-financial) for which IFRS requires or permits fair value measurements, with the exception of share-based payment transactions accounted for under IFRS 2 *Share-based Payment* and leasing transactions within the scope of IAS 17 *Leases*. IFRS 13 defines fair value, provides guidance on its determination and introduces consistent requirements for disclosures on fair value measurements.

IFRS 9 *Financial Instruments* issued in November 2009 and amended in October 2010, introduces new requirements for the classification and measurement of financial assets and financial liabilities and for de-recognition. IFRS 9 is expected to be published in three parts. The first part, Phase 1 – classification and measurement of financial instruments sets out the requirements for recognizing and measuring financial assets, financial liabilities and some contracts to buy or sell non-financial items. Phase 1 simplifies the measurement of financial assets by classifying all financial assets as those being recorded at amortized cost or being recorded at fair value. Phase 1 is effective for periods beginning on or after January 1, 2013, although earlier adoption is allowed. Except for certain additional disclosures, the adoption of this standard is not expected to have an impact on the Corporation's financial statements.

ADVISORIES

Unaudited Numbers: *All financial amounts referred to in this "MD&A" and the Corporation's second quarter report ("**Q2 Report**") for the Reporting Periods and the Comparable Prior Periods are management's best estimates and are unaudited.*

Non-GAAP Measures: *This MD&A and the Q2 Report uses "cash flow", "netbacks", "cash flow netback", "operating netback" and "cash flow per share", which do not have standardized meanings prescribed by generally accepted accounting principles ("**GAAP**") and therefore may not be comparable measures to other companies where similar terminology is used. Cash flow denotes cash flow from operating activities as it appears on the Corporation's Statement of Cash Flows before decommissioning expenditures and changes in non-cash working capital. Netback denotes petroleum and natural gas revenue less royalties, less operating expenses and less transportation and marketing expenses. Cash flow netback denotes net earnings plus non-cash items including deferred incomes tax expense (less any recovery), depletion and depreciation expense, accretion expense, stock-based compensation expense, amortization of deferred financing fees and gains or losses on divestitures.*

BOE Conversions: *Barrels of oil equivalent ("**boe**") amounts have been calculated by using the conversion ratio of six thousand cubic feet (6 Mcf) of natural gas to one barrel of oil (1 bbl). Boe amounts may be misleading, particularly if used in isolation. A boe conversion ratio of 6 Mcf to 1 bbl is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead.*

Mcfe Conversions: *Thousands of cubic feet of gas equivalent ("**Mcfe**") amounts have been calculated by using the conversion ratio of one barrel of oil (1 bbl) to six thousand cubic feet (6 Mcf) of natural gas. Mcfe amounts may be misleading, particularly if used in isolation. A Mcfe conversion ratio of 1 bbl to 6 Mcf is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead.*

MMbtu Pricing Conversion: *$1.00/MMbtu equals $1.00/Mcf based on a standard heat value Mcf.*

Forward-Looking Information: *This MD&A and the Q2 Report contain forward-looking information within the meaning of applicable Canadian securities laws. Forward-looking information relates to future events or future performance and is based upon the Corporation's current internal expectations, estimates, projections, assumptions and beliefs. All information other than historical fact is forward-looking information. Words such as "plan", "expect", "project", "intend", "believe", "anticipate", "estimate", "may", "will", "potential", "proposed" and other similar words that convey certain events or conditions "may" or "will" occur are intended to identify forward-looking information.*

In particular, this MD&A and the Q2 Report contain forward-looking information relating to expected annual exit rate production, planned 2012 capital spending and sources of funding; intention to drill and complete future wells; expected processing capacity and commissioning date of the PCS Gas Plant;

treatment under tax laws; expectation of future taxable income available to utilize income tax pools and the ability to successfully defend tax reassessments.

Forward-looking information is based upon assumptions as to future commodity prices, currency exchange rates, inflation rates, well production rates, well drainage areas, success rates for future drilling and availability of labour and services. With respect to future wells, a key assumption is that geological and other technical interpretations performed by the Corporation's technical staff, which indicate the commercially economic reserves can be recovered from the Corporation's land as a result of drilling such future wells, are valid.

Undue reliance should not be placed on forward-looking information, as there can be no assurance that the plans, intentions or expectations upon which they are based will occur. Although the Corporation believes that the expectations reflected in the forward-looking statements are reasonable, there can be no assurance that such expectations will prove to be correct. As a consequence, actual results may differ materially from those anticipated.

Forward-looking information necessarily involves both known and unknown risks associated with oil and gas exploration, production, transportation and marketing such as operational risks, environmental risks, loss of market demand, general economic conditions affecting ability to access sufficient capital, changes in governmental regulation of the oil and gas industry and competition from others for scarce resources.

The foregoing list of risk factors is not exhaustive. Additional information on these and other risk factors that could affect operations or financial results are included in the Corporation's most recent Annual Information Form and in other reports filed with Canadian securities regulatory authorities. Forward-looking information is based on estimates and opinions of management at the time the information is presented. The Corporation is not under any duty to update the forward-looking information after the date of this MD&A and the Q2 Report to conform such information to actual results or to changes in the Corporation's plans or expectations, except as otherwise required by applicable securities laws.

BIRCHCLIFF ENERGY LTD.

Condensed Statements of Financial Position

Unaudited *(Expressed in thousands of Canadian dollars)*

As at,	June 30, 2012	December 31, 2011
ASSETS		
Current assets:		
Cash	**46**	65
Accounts receivable	**21,231**	37,699
Prepaid expenses and deposits	**3,699**	2,240
	24,976	40,004
Non-current assets:		
Exploration and evaluation (Note 3)	**2,042**	1,858
Petroleum and natural gas properties and equipment (Note 4)	**1,323,741**	1,183,635
	1,325,783	1,185,493
Total assets	**1,350,759**	1,225,497
LIABILITIES		
Current liabilities:		
Accounts payable and accrued liabilities	**79,808**	88,602
Non-current liabilities:		
Non-revolving term credit facilities	**69,232**	68,925
Revolving credit facilities (Note 5)	**331,644**	319,500
Decommissioning obligations (Note 6)	**66,343**	64,023
Deferred premium on flow-through common shares (Note 7)	**1,705**	-
Deferred income taxes	**29,356**	27,845
Total non-current liabilities	**498,280**	480,293
Total liabilities	**578,088**	568,895
SHAREHOLDERS' EQUITY		
Share capital (Note 7)	**676,497**	567,816
Contributed surplus	**46,311**	43,070
Retained earnings	**49,863**	45,716
	772,671	656,602
Total shareholders' equity and liabilities	**1,350,759**	1,225,497

Subsequent events (Note 11)

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

APPROVED BY THE BOARD

(signed) *"Larry A. Shaw"*
Larry A. Shaw, Director

(signed) *"A. Jeffery Tonken"*
A. Jeffery Tonken, Director

BIRCHCLIFF ENERGY LTD.

Condensed Statements of Net Income and Comprehensive Income

Unaudited *(Expressed in thousands of Canadian dollars, except share information)*

	Three months ended June 30,		Six months ended June 30,	
	2012	2011	**2012**	2011
REVENUE				
Petroleum and natural gas	**57,729**	67,464	**120,562**	130,257
Royalties	**(6,026)**	(8,801)	**(13,294)**	(15,000)
	51,703	58,663	**107,268**	115,257
EXPENSES				
Operating	**12,481**	10,618	**24,311**	21,752
Transportation and marketing	**4,790**	4,220	**9,319**	8,247
Administrative, net	**5,816**	7,114	**15,342**	13,473
Depletion and depreciation (Note 4)	**23,017**	16,039	**45,194**	32,103
Finance	**4,565**	5,406	**10,323**	10,907
(Gain) loss on sale of assets (Note 4)	**-**	915	**(3,875)**	915
	50,669	44,312	**100,614**	87,397
INCOME BEFORE TAXES	**1,034**	14,351	**6,654**	27,860
Deferred income tax expense	**618**	4,234	**2,507**	8,150
NET INCOME AND COMPREHENSIVE INCOME	**416**	10,117	**4,147**	19,710
Income per common share (Note 9)				
Basic	**$ -**	$0.08	**$0.03**	$0.16
Diluted	**$ -**	$0.08	**$0.03**	$0.15
Weighted average common shares (Note 9)				
Basic	**138,425,779**	126,322,814	**132,588,343**	125,877,298
Diluted	**138,837,321**	131,380,901	**133,885,883**	131,030,694

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

BIRCHCLIFF ENERGY LTD.

Condensed Statements of Changes in Shareholders' Equity

Unaudited *(Expressed in thousands of Canadian dollars, except share information)*

	Number of Common Shares	Share Capital	Contributed Surplus	Retained Earnings	Total
As at December 31, 2010	125,129,234	554,419	33,459	11,262	599,140
Exercise of stock options	1,367,443	10,916	(3,618)	-	7,298
Stock-based compensation	-	-	6,440	-	6,440
Net income and comprehensive income	-	-	-	19,710	19,710
As at June 30, 2011	126,496,677	565,335	36,281	30,972	632,588
As at December 31, 2011	126,745,577	567,816	43,070	45,716	656,602
Issue of common shares (Note 7)	13,075,000	100,024	-	-	100,024
Issue of flow-through common shares (Note 7)	1,100,000	8,415	-	-	8,415
Share issue costs, net of tax (Note 7)	-	(2,979)	-	-	(2,979)
Exercise of stock options (Note 8)	513,067	3,221	(1,084)	-	2,137
Stock-based compensation (Note 8)	-	-	4,325	-	4,325
Net income and comprehensive income	-	-	-	4,147	4,147
As at June 30, 2012	**141,433,644**	**676,497**	**46,311**	**49,863**	**772,671**

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

BIRCHCLIFF ENERGY LTD.
Condensed Statements of Cash Flows
Unaudited *(Expressed in thousands of Canadian dollars)*

Cash provided by (used in):	Three months ended June 30, 2012	Three months ended June 30, 2011	Six months ended June 30, 2012	Six months ended June 30, 2011
OPERATING				
Net income	**416**	10,117	**4,147**	19,710
Adjustments for items not affecting operating cash:				
Depletion and depreciation	**23,017**	16,039	**45,194**	32,103
Stock-based compensation	**1,282**	2,282	**2,923**	4,330
Finance	**4,565**	5,406	**10,323**	10,907
(Gain) loss on sale of assets	**-**	915	**(3,875)**	915
Deferred income taxes	**618**	4,234	**2,507**	8,150
Interest paid	**(3,913)**	(4,724)	**(9,038)**	(9,533)
Decommissioning expenditures (Note 6)	**(42)**	(212)	**(94)**	(678)
Changes in non-cash working capital	**(14,649)**	6,848	**(12,177)**	(2,958)
	11,294	40,905	**39,910**	62,946
FINANCING				
Issue of common shares (Note 7)	**111,235**	2,092	**112,282**	7,298
Share issue costs (Note 7)	**(3,972)**	-	**(3,972)**	-
Financing fees paid	**(600)**	(1,356)	**(600)**	(1,356)
Increase in non-revolving term credit facilities	**930**	69,456	**237**	69,456
Increase (decrease) in revolving credit facilities	**(41,997)**	(64,506)	**12,403**	(63,008)
	65,596	5,686	**120,350**	12,390
INVESTING				
Acquisition of petroleum and natural gas properties and equipment	**-**	(4,138)	**-**	(4,356)
Sale of petroleum and natural gas properties and equipment	**-**	5,541	**-**	5,541
Additions of exploration and evaluation assets	**(121)**	(20)	**(183)**	(280)
Development of petroleum and natural gas properties and equipment	**(58,694)**	(33,683)	**(178,484)**	(85,384)
Changes in non-cash working capital	**(18,093)**	(14,291)	**18,388**	4,345
	(76,908)	(46,591)	**(160,279)**	(80,134)
NET CHANGE IN CASH	**(18)**	-	**(19)**	(4,798)
CASH, BEGINNING OF PERIOD	**64**	65	**65**	4,863
CASH, END OF PERIOD	**46**	65	**46**	65

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

1. NATURE OF OPERATIONS

Birchcliff Energy Ltd. ("**Birchcliff**" or the "**Corporation**") is domiciled and incorporated in Canada. Birchcliff is engaged in the exploration for and the development, production and acquisition of petroleum and natural gas reserves in Western Canada. The Corporation's financial year end is December 31. The address of the Corporation's registered office is 500, 630 – 4th Avenue SW, Calgary, Alberta, Canada T2P 0J9. Birchcliff trades on the Toronto Stock Exchange under the symbol "**BIR**".

These financial statements were approved and authorized for issuance by the Board of Directors on August 14, 2012.

2. BASIS OF PREPARATION

These unaudited interim condensed financial statements (the "**Financial Statements**") present Birchcliff's financial results of operations and financial position under International Financial Reporting Standards ("**IFRS**") as at and for the three and six months ended June 30, 2012, including the 2011 comparative periods. The Financial Statements have been prepared in accordance with International Accounting Standard ("**IAS**") 34 *Interim Financial Reporting*, as issued by the International Accounting Standards Board ("**IASB**").

These Financial Statements have been prepared following the same IFRS accounting policies and methods of computation as disclosed in the annual audited financial statements for the year ended December 31, 2011. Certain information and disclosures normally required to be included in the notes to the annual audited financial statements have been condensed, omitted or have been disclosed on an annual basis only. Accordingly, these Financial Statements should be read in conjunction with the annual audited financial statements and the notes thereto for the year ended December 31, 2011.

These Financial Statements have been prepared on a historical cost basis, except for certain financial and non-financial assets and liabilities, which have been measured at fair value. The Corporation's Financial Statements include the accounts of Birchcliff only and are expressed in thousands of Canadian dollars, except for share and per share information. There are no subsidiary companies.

3. EXPLORATION AND EVALUATION ASSETS

The components of Exploration and Evaluation ("**E&E**") assets are as follows:

	E&E[1][2]
As at December 31, 2010	1,540
Additions	318
As at December 31, 2011	1,858
Additions	184
As at June 30, 2012	**2,042**

(1) E&E assets consist of the Corporation's exploration activities which are pending the determination of economic quantities of commercially producible proven reserves. Additions represent the Corporation's net share of costs incurred on E&E activities during the period. There were no costs reclassified from E&E to petroleum and natural gas properties and equipment during the reporting periods ended June 30, 2012 and December 31, 2011.

(2) At the end of each reporting period, the Corporation performed an asset impairment review of its E&E assets to ensure that the carrying values of those assets are recoverable. The Corporation's E&E assets were not impaired.

4. PETROLEUM AND NATURAL GAS PROPERTIES AND EQUIPMENT

The components of Petroleum and Natural Gas ("**P&NG**") Properties and Equipment are as follows:

	P&NG	Corporate	Total
Cost:			
As at December 31, 2010	1,037,653	5,375	1,043,028
Additions	264,979	888	265,867
Acquisitions	6,005	-	6,005
Dispositions	(7,159)	-	(7,159)
As at December 31, 2011	1,301,478	6,263	1,307,741
Additions	180,810	625	181,435
Acquisitions	25,006	-	25,006
Dispositions[1]	(22,503)	-	(22,503)
As at June 30, 2012[2]	1,484,791	6,888	1,491,679
Accumulated depletion and depreciation:			
As at December 31, 2010	(50,260)	(2,518)	(52,778)
Depletion and depreciation expense	(70,757)	(979)	(71,736)
Dispositions	408	-	408
As at December 31, 2011	(120,609)	(3,497)	(124,106)
Depletion and depreciation expense	(44,741)	(453)	(45,194)
Dispositions[1]	1,362	-	1,362
As at June 30, 2012	(163,988)	(3,950)	(167,938)
Net book value[3]:			
As at December 31, 2011	1,180,869	2,766	1,183,635
As at June 30, 2012	**1,320,803**	**2,938**	**1,323,741**

(1) In March 2012, Birchcliff completed a transaction whereby it disposed of a non-core asset in the Glacier area of Alberta in exchange for strategic assets acquired in the Pouce Coupe area of Alberta. The fair value of the transaction was estimated at $25 million. As a result of the disposition, Birchcliff recorded a gain on sale of approximately $3.9 million during the six months ended June 30, 2012.

(2) The Corporation's P&NG properties and equipment were pledged as security for its credit facilities. Although the Corporation believes that it has title to its petroleum and natural gas properties, it cannot control or completely protect itself against the risk of title disputes and challenges. There were no borrowing costs capitalized to P&NG properties and equipment.

(3) In light of the low natural gas prices, the Corporation performed an asset impairment test to ensure that the carrying value of its P&NG properties and equipment is recoverable and does not exceed its fair value at the end of the reporting period. Birchcliff's P&NG properties and equipment were not impaired at June 30, 2012 and December 31, 2011. In determining the recoverable amount, Birchcliff applied a pre-tax discount rate of 10% on cash flows from proved plus probable reserves. The petroleum and natural gas future prices are based on period-end commodity price forecasts determined by the Corporation's independent reserves evaluator.

5. REVOLVING CREDIT FACILITIES

The components of the Corporation's revolving credit facilities include:

As at,	**June 30, 2012**	December 31, 2011
Syndicated credit facility	319,000	304,000
Working capital facility	16,391	19,221
Drawn revolving credit facilities	335,391	323,221
Unamortized prepaid interest on bankers' acceptances	(3,238)	(3,471)
Unamortized deferred financing fees	(509)	(250)
Total revolving credit facilities	**331,644**	319,500

On June 26, 2012, the Corporation's bank syndicate approved an increase to the revolving credit facilities to an aggregate limit of $470 million from $450 million and extended the conversion date of those facilities to May 17, 2013. The terms under the amended revolving credit facilities have essentially remained unchanged from those disclosed in the annual audited financial statements for the year ended December 31, 2011. At June 30, 2012, the revolving credit facilities consisted of an extendible revolving term credit facility with an authorized limit of $440 million and an extendible revolving working capital facility with an authorized limit of $30 million.

6. DECOMMISSIONING OBLIGATIONS

A reconciliation of the decommissioning obligations is provided below:

As at,	**June 30, 2012**	December 31, 2011
Balance, beginning	64,023	42,106
Obligations incurred	1,566	2,999
Obligations acquired, net dispositions	(26)	237
Changes in estimate	-	5,988
Changes in discount rate	-	12,003
Accretion expense	874	1,747
Actual expenditures	(94)	(1,057)
Balance, ending(1)	**66,343**	64,023

(1) A pre-tax risk-free discount rate of 2.6% and an inflation rate of 2.0% were used to calculate the discounted fair value of the obligation at June 30, 2012 and December 31, 2011.

7. SHARE CAPITAL

(a) Authorized:

Unlimited number of voting common shares, with no par value
Unlimited number of preferred shares, with no par value

The preferred shares may be issued in one or more series and the directors are authorized to fix the number of shares in each series and to determine the designation, rights, privileges, restrictions and conditions attached to the shares of each series.

(b) **Issued:**

Refer to the Statement of Changes in Shareholders' Equity for movement in share capital.

On April 19, 2012, the Corporation raised $110 million through an equity financing comprised of a bought deal equity offering whereby it issued 8,075,000 common shares at a price of $7.65 per share for gross proceeds of $61.8 million, 1,100,000 common shares issued on a "flow-through share" basis at a price of $9.20 per share for gross proceeds of $10.1 million and 5,000,000 common shares at a price of $7.65 per share on a concurrent private placement basis with its major shareholder for gross proceeds of $38.3 million (the "**April Financing**"). The implied premium on the flow-through shares was determined to be $1.7 million or $1.55 per share. This premium will be reduced on a pro-rata basis as qualified Canadian exploration expenditures for purposes of the Income Tax Act are incurred. As at June 30, 2012, Birchcliff is committed to spending $10.1 million on eligible Canadian exploration expenditures on or before December 31, 2013, and renounce to each subscriber of flow-through shares effective on or before December 31, 2012.

Birchcliff recognized a deferred income tax benefit of $1.0 million in respect of share issue costs related to the April Financing totalling approximately $4.0 million. The net proceeds of the April Financing were used to reduce outstanding indebtedness under the revolving credit facilities.

8. SHARE-BASED PAYMENTS

During the three and six months ending June 30, 2012, the Corporation recorded $1.3 million and $2.9 million (June 30, 2011 – $2.3 million and $4.3 million) of stock-based compensation expense, net of $0.6 million and $1.4 million (June 30, 2011 – $1.2 million and $2.1 million) in capitalized amounts directly attributable to the exploration and development of the Corporation's assets. In determining the stock-based compensation expense for options issued during the three months ended June 30, 2012, the Corporation applied a weighted average estimated forfeiture rate of 14% (June 30, 2011 – 15%).

As of June 30, 2012, the Corporation's Amended and Restated Stock Option Plan permitted the grant of options in respect of a maximum of 14,143,364 (June 30, 2011 – 12,649,668) common shares. At June 30, 2012, there remained available for issuance options in respect of 1,284,624 (June 30, 2011 – 1,948,933) common shares. For stock options exercised during the three months ended June 30, 2012, the weighted average share trading price was $6.26 (June 30, 2011 – $12.79) per share.

A summary of the outstanding stock options is presented below:

	Number	**Weighted Average Exercise Price ($)**
Outstanding, December 31, 2011	10,466,941	8.73
Exercised	(260,000)	(4.03)
Outstanding, March 31, 2012	10,206,941	8.85
Granted(1)	3,400,900	5.97
Exercised	(253,067)	(4.31)
Forfeited	(380,834)	(9.68)
Expired	(115,200)	(10.34)
Outstanding, June 30, 2012	**12,858,740**	**8.14**

(1) On April 26, 2012, the Corporation issued 3,345,400 stock options to officers and employees of Birchcliff at an exercise price of $5.96 per common share as part of its annual compensation review.

The weighted average fair value per option during the three months ended June 30, 2012 was $2.44 (June 30, 2011 - $5.81). The weighted average assumptions used in calculating the fair values are set forth below:

Three months ended,	**June 30, 2012**	June 30, 2011
Risk-free interest rate	1.5%	2.3%
Option life (years)	3.8	3.7
Expected volatility	52.7%	60.4%
Dividend yield	-	-

A summary of the stock options outstanding and exercisable under the plan at June 30, 2012 is presented below:

Exercise Price		**Awards Outstanding**			**Awards Exercisable**		
Low	High	Quantity	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Quantity	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price
$4.00	$6.00	5,350,972	3.52	$5.60	2,097,572	1.51	$5.05
$6.01	$9.00	1,804,367	1.28	$7.66	1,563,531	1.01	$7.60
$9.01	$12.00	5,185,601	3.05	$10.47	2,600,133	2.87	$10.26
$12.01	$13.60	517,800	3.10	$12.74	243,131	2.19	$12.69
		12,858,740	**3.00**	**$8.14**	**6,504,367**	**1.96**	**$8.03**

There were no performance warrants issued or exercised during the periods ended June 30, 2012 and December 31, 2011. There are 2,939,732 performance warrants with an exercise price of $3.00 that are outstanding and exercisable at June 30, 2012. Each stock option and performance warrant entitles the holder to purchase one common share at the exercise price.

9. PER SHARE INFORMATION

The following table presents the computation of net income per common share:

	Three months ended June 30,		**Six months ended June 30,**	
	2012	2011	**2012**	2011
Net income	416	10,117	4,147	19,710
Weighted average common shares:				
Weighted average common shares outstanding (basic)	138,425,779	126,322,814	132,588,343	125,877,298
Effect of dilutive stock options	411,542	5,058,087	1,297,540	5,153,396
Weighted average common shares outstanding (diluted)	138,837,321	131,380,901	133,885,883	131,030,694
Net income per common share				
basic	**$ -**	$0.08	**$0.03**	$0.16
diluted	**$ -**	$0.08	**$0.03**	$0.15

The weighted average diluted common shares outstanding for the six months ended June 30, 2012 excludes 9,451,968 (June 30, 2011 – 3,505,801) of stock options that are anti-dilutive. The average market value of the Corporation's shares for the purpose of calculating the dilutive effect of stock options and performance warrants was based on average quoted market prices for the time that the options and warrants were outstanding during the period.

10. CAPITAL MANAGEMENT

The Corporation's general policy is to maintain a sufficient capital base in order to manage its business in the most effective manner with the goal of increasing the value of its assets and thus its underlying share value. The Corporation's objectives when managing capital are to maintain financial flexibility in order to preserve its ability to meet financial obligations, including potential obligations arising from additional acquisitions; to maintain a capital structure that allows Birchcliff to finance its growth strategy using primarily internally-generated cash flow and its available debt capacity; and to optimize the use of its capital to provide an appropriate investment return to its shareholders. There were no changes in the Corporation's approach to capital management as at and during the three months ended June 30, 2012.

The following table shows the Corporation's total available credit:

As at,	**June 30, 2012**	December 31, 2011
Maximum borrowing base limit[(1)(2)]:		
Non-revolving five-year term credit facility	70,000	70,000
Revolving credit facilities	470,000	450,000
	540,000	520,000
Principal amount utilized:		
Drawn non-revolving five-year term credit facility	(70,000)	(70,000)
Drawn revolving credit facilities	(335,391)	(323,221)
Outstanding letters of credit[(3)]	(2,668)	(2,668)
	(408,059)	(395,889)
Total unused credit	**131,941**	124,111

(1) The Corporation's credit facilities are subject to a semi-annual review of the borrowing base limit, which is directly impacted by the value of Birchcliff's petroleum and natural gas reserves. On June 26, 2012, the Corporation's borrowing base limit under its revolving credit facilities was increased to an aggregate limit of $470 million from $450 million.

(2) The financial covenants applicable to the Corporation's credit facilities includes a (i) quarterly interest coverage ratio test, which is calculated as earnings before interest, taxes, stock-based compensation, depletion, depreciation and amortization over interest expense ("**EBITDA**") and (ii) debt to EBITDA ratio. Debt includes the amounts outstanding under the Corporation's credit facilities as disclosed on the Statements of Financial Position and letters of credit at the end of the reporting period, excluding any unamortized deferred financing fees. The Corporation was compliant with all financial covenants applicable under its credit facilities as at and during the periods ended June 30, 2012 and December 31, 2011.

(3) Letters of credit are issued to various service providers. There were no amounts drawn on the letters of credit as at and during the periods ended June 30, 2012 and December 31, 2011.

The capital structure of the Corporation is as follows:

As at,	**June 30, 2012**	December 31, 2011	Change
Total shareholders' equity(1)	772,671	656,602	18%
Total shareholders' equity as a % of total capital	63%	60%	
Working capital deficit(2)	54,832	48,598	
Drawn non-revolving five-year term credit facility	70,000	70,000	
Drawn revolving credit facilities	335,391	323,221	
Total drawn debt	460,223	441,819	4%
Total drawn debt as a % of total capital	37%	40%	
Total capital	**1,232,894**	1,098,421	12%

(1) Shareholders' equity is defined as share capital plus contributed surplus plus retained earnings, less any deficit.

(2) Working capital deficit is defined as current assets less current liabilities.

11. SUBSEQUENT EVENTS

On August 8, 2012, Birchcliff completed a bought deal equity financing for gross proceeds of $50 million (the "**August Financing**"). The Corporation issued 2,000,000 preferred units at a price of $25.00 per preferred unit for gross proceeds of $50 million. Each preferred unit was comprised of one cumulative redeemable five year rate reset preferred share, series A (a "**Series A Preferred Share**") of Birchcliff, to yield initially 8% per annum; and three common share purchase warrants (each a "**Warrant**") of Birchcliff. Each Warrant provides the right to purchase one common share of the Corporation for a period of two years from the closing date of August 8, 2012, at an exercise price of $8.30 per common share. A total aggregate of two million Series A Preferred Shares and six million Warrants were issued in the August Financing.

The Series A Preferred Shares pay cumulative dividends of $2.00 per Series A Preferred Share per annum, payable quarterly if, as and when declared by Birchcliff's board of directors, with the first quarterly dividend to be paid on September 30, 2012 (or the next business day), for the initial five year period ending September 30, 2017. Thereafter, the dividend rate will be reset every five years at a rate equal to the then current five year Government of Canada bond yield plus 6.83%. The Series A Preferred Shares are redeemable at the option of the Corporation on or after September 30, 2017, and on September 30 in every fifth year thereafter.

Holders of the Series A Preferred Shares have the right, at their option, to convert their Series A Preferred Shares into cumulative redeemable floating rate series B preferred shares (a "**Series B Preferred Share**"), subject to certain conditions, on September 30, 2017 and on September 30 in every fifth year thereafter. The holders of the Series B Preferred Shares will be entitled to receive quarterly floating rate cumulative preferential cash dividends, if declared by Birchcliff's Board of Directors, at a rate equal to the sum of the then current 90 day Government of Canada Treasury Bill rate plus 6.83%.

In the event of liquidation, dissolution or winding-up of Birchcliff, the holders of the Series A Preferred Shares and Series B Preferred Shares will be entitled to receive $25.00 per share as well as all accrued unpaid dividends before any amounts will be paid or any assets will be distributed to the holders of any other shares ranking junior to the Series A Preferred Shares and the Series B Preferred Shares. The holders of the Series A Preferred Shares and the Series B Preferred Shares will not be entitled to share in any further distribution of the assets of the Corporation.

Further details regarding the August Financing can be found in the Corporation's short form prospectus dated July 30, 2012, which is available on the SEDAR website at www.sedar.com.

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Bruno P. Geremia
Vice President & Chief Financial Officer

David M. Humphreys
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Karen A. Pagano
Vice President, Engineering

James W. Surbey
Vice President, Corporate Development

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RESERVES EVALUATOR
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