



## **Interim Report**

**For the three and six months ended  
June 30, 2017**

# MANAGEMENT'S DISCUSSION AND ANALYSIS

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This Management's Discussion and Analysis ("MD&A") of Return Energy Inc. ("Return" or the "Company") should be read in conjunction with the unaudited Condensed Consolidated Interim Financial Statements for the three and six months ended June 30, 2017 (the "Financial Statements") and the audited annual consolidated financial statements and MD&A for the year ended December 31, 2016. This MD&A has been prepared as of August 22, 2017.

## Basis of Presentation

The Financial Statements and comparative information have been prepared in accordance with International Financial Reporting Standards. (IFRS)

## Non-IFRS Measures

This MD&A includes references to financial measures commonly used in the oil and gas industry that do not have standardized meanings prescribed by IFRS including operating netback. Operating netback has been defined by the Company as "petroleum and natural gas sales less royalties and operating costs".

## Other Measurements

All figures in this MD&A have been reported in Canadian dollars unless otherwise stated.

Where amounts are expressed on a barrel of oil equivalent (boe) basis, one thousand cubic feet (mcf) has been converted at a ratio of six thousand cubic feet to one barrel of oil. Boe's may be misleading, particularly if used in isolation. A boe conversion ratio of six thousand cubic feet to one barrel of oil is based on an energy equivalent conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead.

## THE COMPANY

Return is engaged in the exploration for and development and production of petroleum and natural gas properties in the Western Canadian Sedimentary Basin. The Company is focused on the Peace River Arch area in northwest Alberta. Return's shares are publicly traded on the TSX Venture Exchange under the symbol "RTN". The Company was incorporated under the Alberta Business Corporations Act on March 20, 2006 and is domiciled in Calgary, Canada.

## Highlights:

The following highlights the significant events during the period:

- The Company closed a non-brokered private placement on March 14, 2017, for total gross proceeds of \$2,104,148. The proceeds of this issuance will be used by Return to further its development activities in the Rycroft, Gordondale, Valhalla areas of Alberta;
- On April 20, 2017, the Company acquired production of approximately 60 BOE/day (80% natural gas), and the remaining 50% interest in the Company's operated Rycroft gathering system and gas plant for \$715,000 in cash, subject to closing adjustments. All of the acquired production is processed through the Rycroft gas plant. Based on the Company's existing independent reserve report prepared by Sproule Associates Limited dated effective December 31, the acquisition includes proved developed producing reserves of 171,600 BOE and proved plus probable reserves of 228,400 BOE. The net present value of future net revenue before tax discounted at 10% equals \$989,000 for proved developed producing reserves and \$1,266,000 for proved plus probable reserves. Sole ownership of the gas plant provides Return greater flexibility and control over plant through-put and increases third party processing revenue;
- In addition to the above mentioned acquisition the Company further consolidated its interest in Rycroft by acquiring an additional 12 boe/d from non-operated joint interest partners for total consideration of \$140,000.

## MANAGEMENT'S DISCUSSION AND ANALYSIS

- The Company added to its acreage position by purchasing four sections of highly prospective undeveloped land at Rycroft; and
- The Company disposed of some non-core land and oil assets for gross proceeds of \$169,000.

### RESULTS OF OPERATIONS

#### Petroleum and Natural Gas Production

	Three months ended			Six months ended June 30	
	June 30 2017	March 31 2017	June 30 2016	2017	2016
<b>Production</b>					
Oil and natural gas liquids (bbls)	4,483	5,251	-	9,734	-
Natural gas (mcf)	125,838	109,134	3,380	234,972	7,006
Oil equivalent (boe @ 6:1)	25,456	23,440	563	48,896	1,168
<b>Average production per day</b>					
Oil and natural gas liquids (bbls/d)	49	58	-	54	-
Natural gas (mcf/d)	1,383	1,213	37	1,298	38
BOE/d	280	260	6	270	6

For the three months ended June 30, 2017, petroleum and natural gas production averaged 280 boe/d an increase of 8% over the prior quarter. The increase over the three months ended March 31, 2017 is a result of the Rycroft acquisitions the Company completed in the quarter. Oil production is down due to the sale of some non-core oil assets during the quarter. The increase in production during the three and six months ended June 30, 2017 over the comparative periods in 2016 is a result of the acquisitions the Company finalized in October 2016.

#### Oil and Natural Gas Revenue

	Three months ended			Six months ended June 30	
	June 30 2017	March 31 2017	June 30 2016	2017	2016
<b>REVENUE</b>					
Oil and natural gas liquids	\$ 246,487	\$ 293,562	\$ -	\$ 540,049	\$ -
Natural Gas	354,427	279,972	2,895	634,399	8,565
Total petroleum and natural gas sales	\$ 600,914	\$ 573,534	\$ 2,895	\$ 1,174,448	\$ 8,565
<b>Average Sales Price</b>					
Oil and natural gas liquids (\$/bbls)	\$ 54.98	\$ 55.91	\$ -	\$ 55.48	\$ -
Natural gas (\$/mcf)	2.82	2.57	0.86	2.70	1.22
Oil equivalent (\$/boe)	\$ 23.61	\$ 24.47	\$ 5.14	\$ 24.02	\$ 7.34

During the three months ended June 30, 2017 revenue increased 5% over the three months ended March 31, 2017. This increase is primarily the result of the above mentioned increased production offset by lower oil prices.

#### Royalties

	Three months ended			Six months ended June 30	
	June 30 2017	March 31 2017	June 30 2016	2017	2016
<b>Royalties</b>					
Oil and natural gas liquids	\$ 25,621	\$ 31,333	\$ -	\$ 56,954	\$ -
Natural Gas	14,397	23,022	184	37,419	718
Total petroleum and natural gas sales	\$ 40,018	\$ 54,355	\$ 184	\$ 94,373	\$ 718
<b>Average Royalty Rate (% of sales)</b>					
Oil and natural gas liquids	10.39%	10.67%	-	10.55%	-
Natural gas	4.06%	8.22%	6.36%	5.90%	8.38%
Oil equivalent	6.66%	9.48%	6.36%	8.04%	8.38%

## MANAGEMENT'S DISCUSSION AND ANALYSIS

Royalties as a percentage of revenue averaged 6.7% for the three months ended June 30, 2017. This is lower than the previous quarter by 2.82% primarily due to a higher gas cost allowance credit during the quarter.

### Operating Costs

	Three months ended			Six months ended June 30	
	June 30	March 31	June 30	2017	2016
	2017	2017	2016		
Operating Costs	\$ 465,674	\$ 500,704	\$ 4,229	\$ 966,378	\$ 9,499
\$ per boe	\$ 18.29	\$ 21.36	\$ 7.51	\$ 19.76	\$ 8.14

Operating costs averaged \$18.29 per boe for the three months ended June 30, 2017 a decrease of 14% over the three months ended March 31, 2017.

### Operating Netback

	Three months ended			Six months ended June 30	
	June 30	March 31	June 30	2017	2016
	2017	2017	2016		
Netback (\$/boe)					
Revenue	\$ 23.61	\$ 24.47	\$ 5.14	24.02	7.34
Royalties	(1.57)	(2.32)	(0.33)	(1.93)	(0.61)
Operating	(18.29)	(21.36)	(7.51)	(19.76)	(8.14)
Operating Netback	\$ 3.74	\$ 0.79	\$ (2.70)	\$ 2.33	\$ (1.41)

During the three months ended June 30, 2017 the Company had an operating netback of \$3.74 per boe compared to a netback of \$0.79 in the first quarter. The increase in the operating netback is primarily a result of lower royalty and operating costs per boe partially offset by lower prices per boe.

### Other revenue

	Three months ended			Six months ended June 30	
	June 30	March 31	June 30	2017	2016
	2017	2017	2016		
Other	\$ 45,116	\$ 60,383	\$ 32	\$ 105,499	\$ 63

Other revenue is primarily made up of gas processing and transportation fees and land use fees. The decrease in the second quarter 2017 over the first quarter is primarily due to decreased gas processing and transportation fees from third party gas as the wells were temporarily shut in due to spring breakup. The increase in other revenue for the six months ended June 30, 2017 over the comparative period is a result of the acquisitions the Company finalized in October 2016.

### General and administrative

	Three months ended			Six months ended June 30	
	June 30	March 31	June 30	2017	2016
	2017	2017	2016		
General and Administrative	\$ 304,710	\$ 187,150	\$ 48,742	\$ 491,860	\$ 143,634

General and administrative costs for three months ended June 30, 2017 increased over the three months ended March 31, 2017, primarily due to additional office and consulting costs. The increase during the three and six months ended June 30, 2017 over the comparative 2016 periods is due to the increased consulting and professional fees as well as a general increase in office costs due to the increase in activity.

# MANAGEMENT'S DISCUSSION AND ANALYSIS

## Depletion and depreciation

	Three months ended			Six months ended June 30	
	June 30	March 31	June 30		
	2017	2017	2016	2017	2016
Depletion and depreciation	\$ 223,673	\$ 216,966	\$ 1,824	\$ 440,639	\$ 3,649
\$ per boe	\$ 8.79	\$ 9.26	\$ 3.24	\$ 9.01	\$ 3.13

Depletion and depreciation increased for the three months ended June 30, 2017 compared to the previous quarter due to the increase in production compared to the three months ended March 31, 2017. The increase in depletion and depreciation for the three and six months ended June 30, 2017 over the comparative periods is a result of the acquisitions the Company finalized in October 2016.

## Stock based compensation

Stock-based compensation costs for the three months ended June 30, 2017 amounted to \$43,450 (three months ended June 30, 2016 – \$10,749). Stock-based compensation costs for the six months ended June 30, 2017 amounted to \$86,900 (six months ended June 30, 2016 – \$21,498). The increase in stock-based compensation costs during the three and six months ended June 30, 2017 over the comparative periods is attributable to a stock option grant in January 2017.

Stock-based compensation costs attributable to share options granted were measured at their fair value at the grant date and amortized over the vesting period with a corresponding increase to contributed surplus. The fair value of stock options granted was calculated using the Black-Scholes option pricing method.

## Gain on sale of exploration and evaluation assets

During the three months ended June 30, 2017, the Company sold non-core undeveloped land for \$50,000. The land was originally acquired as part of the acquisitions in 2016. The land was recorded with a book value of \$nil creating a \$50,000 gain.

## Gain on sale of property, plant and equipment

During the three months ended June 30, 2017, the Company sold non-core oil assets in the Pembina area for cash proceeds of \$118,973. The Company had a book value of \$287,131 and decommissioning liabilities of \$262,448 which resulted in a gain on sale of \$94,290.

## Gain on acquisition

On April 20, 2017, the Company acquired production of approximately 60 BOE/day (80% natural gas), and the remaining 50% interest in the Company's operated Rycroft gathering system and gas plant for \$715,000 in cash, subject to closing adjustments. All of the acquired production is processed through the Rycroft gas plant. A gain on acquisition was recorded as the estimated fair value of the net assets acquired exceeded the acquisition price by \$400,000.

## Discontinued Operations

In June 2016 the Company relinquished its interest in the Bouhajla block in Tunisia and discontinued its operations in Tunisia.

Operating results related to discontinued operations have been included in the loss from discontinued operations on the condensed consolidated interim statements of net income (loss). Comparative period balances have been restated. During the three and six months ended June 30, 2017 \$nil have been incurred in Tunisia (three and six months ended June 30, 2016 - \$8,680 and \$25,945, respectively).

# **MANAGEMENT'S DISCUSSION AND ANALYSIS**

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## **Share capital**

During the three months ended March 31, 2017 the Company completed an equity financing and issued a total of 17,415,399 common shares and 16,883,959 warrants for total gross proceeds of \$2,104,148. Each warrant issued pursuant to the above mentioned financing, is exercisable by the holder to purchase one Common Share for a period of 12 months from March 14, 2017 at a price of \$0.15. The Company may redeem the warrants upon providing the holder notice. Such notice may be given by the Company, in its sole discretion, if the volume-weighted average price of the Common Shares on the TSX Venture Exchange exceeds the Warrant Exercise Price by at least 200% for a minimum of 10 consecutive trading days (whether or not trading of Common Shares occurs on all such days), provided that the Common Shares trade on at least five of such trading days.

In addition during the first quarter, the Company granted 2,070,000 stock options with an exercise price of \$0.185 per share to certain officers, directors, employees and consultants.

A total of 42,424,293 common shares, 23,686,459 warrants, and 2,175,000 stock options of the Company are outstanding as of the date hereof.

## **LIQUIDITY AND CAPITAL RESOURCES**

As at June 30, 2017, the Company had working capital of \$1.9 million. The Company has a commitment to spend a minimum of \$100,000 by December 31, 2018 to meet its flow through obligation. To date the Company has spent approximately \$80,000 of its flow through obligation.

During the six months ended June 30, 2017 the Company had a positive cash flow from operations of \$137,000 compared to the six months ended June 30, 2016 which had a negative cash flow from operations of \$130,000.

The Company's operating cash requirements including amounts projected to complete the Company's existing capital commitments are continuously monitored and adjusted as variables change. These variables include but are not limited to, oil and natural gas production, commodity prices, and expenditures on capital projects. Management has planned 2017 and 2018 operations based on their best estimates of projected business activity and estimated future cash flows.

## **TRANSACTIONS WITH RELATED PARTIES**

During the three months ended June 30, 2017, the Company purchased two sections of undeveloped land from a corporation controlled by an officer of the Company for \$60,000. The cost of the undeveloped land is comparable to what would have been paid to unrelated parties.

# MANAGEMENT'S DISCUSSION AND ANALYSIS

## SUMMARY OF QUARTERLY INFORMATION

The following table summarizes quarterly financial information for the previous quarters:

	Quarter ended							
	June 30 2017	Mar 31 2017	Dec 31 2016	Sept 30 2016	Jun 30 2016	Mar 31 2016	Dec 31 2015	Sep 30 2015
Average Daily Production								
Oil and NGLs (bbls/d)	49	58	37	-	-	-	-	-
Natural gas (mcf/d)	1,383	1,213	1,033	19	37	40	40	48
Combined (boe/d)	280	260	209	3	6	7	7	8
Total revenue, net of royalties	\$ 606,012	\$ 579,562	\$ 524,863	\$ 4,438	\$ 2,743	\$ 5,167	\$ 8,558	\$ 9,844
Net income (loss) from continuing operations	\$ 87,864	\$ (399,394)	\$ (424,037)	\$ (89,375)	\$ (62,975)	\$ (74,206)	\$ (85,243)	\$ (109,274)
Gain (loss) from discontinued operations	-	-	293,058	(7,844)	(8,680)	(17,265)	(44,150)	(13,071)
Net income (loss)	\$ 87,864	\$ (399,394)	\$ (130,979)	\$ (97,219)	\$ (71,655)	\$ (91,471)	\$ (129,393)	\$ (122,345)
Per share - basic and diluted								
Net income (loss) from continuing operations	\$ -	\$ (0.01)	\$ (0.02)	\$ (0.01)	\$ (0.01)	\$ (0.01)	\$ (0.01)	\$ (0.01)
Gain (loss) from discontinued operations	-	-	0.01	-	-	-	-	-
Net income (loss)	\$ -	\$ (0.01)	\$ (0.01)	\$ (0.01)	\$ (0.01)	\$ (0.01)	\$ (0.01)	\$ (0.01)

On October 21, 2016 the Company acquired producing oil and gas assets primarily in the Peace River Arch area of northwest Alberta which accounts for the increase in both production and revenue compared to prior quarters. Production and revenue increased during the first quarter 2017 primarily due to having a full quarter of production compared to the fourth quarter 2016 which only included production from October 21, 2016 from the Peace River Arch assets. The increase in the loss from continuing operations in the fourth quarter 2016 and first quarter 2017 is primarily a result of increased general and administrative and depletion and depreciation due to the previous mentioned acquisition. The Company recorded net income of \$87,864 primarily from a \$400,000 gain from the purchase of oil and natural gas assets and facilities in Rycroft. The gain from discontinued operations in the fourth quarter 2016 is a result of a reversal of previously accrued liabilities.

## ACCOUNTING STANDARDS ISSUED BUT NOT YET APPLIED

There are no updates to future changes in accounting standards for the three and six months ended June 30, 2017. Further information on future changes in accounting standards can be found in the notes to the annual consolidated financial statements and annual MD&A for the year ended December 31, 2016.

## BUSINESS RISKS AND UNCERTAINTIES

The Company, like all oil and gas corporations, operates in environments subject to inherent risks. These risks have not materially changed from December 31, 2016. Further information on business risks and uncertainties can be found in the annual MD&A for the year ended December 31, 2016.

# MANAGEMENT'S DISCUSSION AND ANALYSIS

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## Forward looking statements

Certain statements contained in this MD&A may constitute forward-looking statements. These statements relate to future events or the Company's future performance. All statements, other than statements of historical fact, may be forward-looking statements. Forward-looking statements are often, but not always, identified by the use of words such as "seek", "anticipate", "plan", "continue", "estimate", "expect", "may", "will", "project", "predict", "propose", "potential", "targeting", "intend", "could", "might", "should", "believe" and similar expressions. These statements involve known and unknown risks, uncertainties and other factors that may cause actual results or events to differ materially from those anticipated in such forward-looking statements. The Company believes that the expectations reflected in those forward-looking statements are reasonable but no assurance can be given that these expectations will prove to be correct and such forward-looking statements included in this MD&A should not be unduly relied upon by investors as actual results may vary. These statements speak only as of the date of this MD&A and are expressly qualified, in their entirety, by this cautionary statement.

With respect to forward-looking statements listed above and contained in the MD&A, the Company has made assumptions regarding, among other things: the legislative and regulatory environment; commodity prices; estimated recoverable reserves; costs related to development of oil and gas properties will remain consistent with historical experience; and the Company's ability to obtain additional financing on satisfactory terms.

The Company's actual results could differ materially from those anticipated in these forward looking-statements as a result of the risk factors set forth below and elsewhere in this MD&A; changes in oil and natural gas prices; geological, technical, drilling and processing problems; liabilities and risks, including environmental liabilities and risks, inherent in oil and natural gas operations; reservoir performance; labour, equipment and material costs; access to capital markets; interest; and economic conditions.

Additional information related to the Company can be found on SEDAR at [www.sedar.com](http://www.sedar.com).





**Condensed Consolidated Interim  
Financial Statements  
(Unaudited)**

**For the three and six months ended  
June 30, 2017**

**RETURN ENERGY INC.**  
**CONDENSED CONSOLIDATED INTERIM STATEMENTS OF FINANCIAL POSITION**  
**(UNAUDITED, Expressed in Canadian dollars)**

<b><u>ASSETS</u></b>	As at	
	June 30, 2017	December 31, 2016
CURRENT		
Cash	\$ 1,836,166	\$ 602,848
Accounts receivable	449,756	780,647
Prepaid expenses and deposits	51,537	429,226
	2,337,459	1,812,721
EXPLORATION AND EVALUATION (note 3)	99,455	-
PROPERTY, PLANT AND EQUIPMENT (note 4)	9,307,853	8,030,376
<b>TOTAL ASSETS</b>	<b>\$ 11,744,767</b>	<b>\$ 9,843,097</b>
<b><u>LIABILITIES AND SHAREHOLDERS' EQUITY</u></b>		
CURRENT		
Accounts payable and accrued liabilities	\$ 458,576	\$ 686,414
DECOMMISSIONING LIABILITIES (note 5)	6,672,510	6,236,420
CONVERTIBLE PREFERRED SHARES (note 6)	2,000,000	2,000,000
	8,672,510	8,236,420
<b>TOTAL LIABILITIES</b>	<b>9,131,086</b>	<b>8,922,834</b>
SHAREHOLDERS' EQUITY		
SHARE CAPITAL (note 7c)	28,283,806	26,908,948
WARRANTS (note 7d)	724,417	180,417
CONTRIBUTED SURPLUS	5,005,316	4,918,416
ACCUMULATED OTHER COMPREHENSIVE INCOME	349,715	350,345
DEFICIT	(31,749,573)	(31,437,863)
<b>TOTAL SHAREHOLDERS' EQUITY</b>	<b>2,613,681</b>	<b>920,263</b>
<b>TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY</b>	<b>\$ 11,744,767</b>	<b>\$ 9,843,097</b>

Commitments (note 11)

See accompanying notes

**RETURN ENERGY INC.**  
**CONDENSED CONSOLIDATED INTERIM STATEMENTS OF CHANGES IN EQUITY (DEFICIT)**  
**(UNAUDITED, expressed in Canadian dollars, except for number of shares)**

	Number of shares	Share Capital	Warrants	Contributed Surplus	Accumulated Other Comprehensive Income (Loss)	Deficit	Total
Balance December 31, 2015	11,403,894	\$ 25,737,888	\$ -	\$ 4,884,019	\$ 342,087	\$ (31,046,539)	\$ (82,545)
Stock-based compensation		-	-	21,498	-	-	21,498
Comprehensive income (loss) for the period		-	-	-	13,486	(163,126)	(149,640)
Balance June 30, 2016	11,403,894	25,737,888	-	4,905,517	355,573	(31,209,665)	(210,687)
Private company acquisitions	5,500,000	477,064	72,936	-	-	-	550,000
Equity financing	8,105,000	693,996	107,481	-	-	-	801,477
Stock-based compensation	-	-	-	12,899	-	-	12,899
Comprehensive loss for the period	-	-	-	-	(5,228)	(228,198)	(233,426)
Balance December 31, 2016	25,008,894	26,908,948	180,417	4,918,416	350,345	(31,437,863)	920,263
Equity financing (note 7e)	17,415,399	1,374,858	544,000	-	-	-	1,918,858
Stock-based compensation	-	-	-	86,900	-	-	86,900
Comprehensive loss for the period	-	-	-	-	(630)	(311,710)	(312,340)
Balance June 30, 2017	<u>42,424,293</u>	<u>\$ 28,283,806</u>	<u>\$ 724,417</u>	<u>\$ 5,005,316</u>	<u>\$ 349,715</u>	<u>\$ (31,749,573)</u>	<u>\$ 2,613,681</u>

All references to common shares and per share amounts have been retroactively restated to reflect the share consolidation as outlined in note 7b.

See accompanying notes

**RETURN ENERGY INC.**  
**CONDENSED CONSOLIDATED INTERIM STATEMENTS OF NET INCOME (LOSS)**  
**FOR THE THREE AND SIX MONTHS ENDED JUNE 30**  
**(UNAUDITED, expressed in Canadian dollars)**

	Three months ended June 30		Six months ended June 30	
	2017	2016	2017	2016
<b>REVENUE</b>				
Petroleum and natural gas sales	\$ 600,914	\$ 2,895	\$ 1,174,448	\$ 8,565
Royalties	(40,018)	(184)	(94,373)	(718)
Other	45,116	32	105,499	63
	<u>606,012</u>	<u>2,743</u>	<u>1,185,574</u>	<u>7,910</u>
<b>EXPENSES</b>				
Operating costs	465,674	4,229	966,378	9,499
General and administrative	304,710	48,742	491,860	143,634
Stock-based compensation	43,450	10,749	86,900	21,498
Depletion and depreciation (note 4)	223,673	1,824	440,639	3,649
Accretion of decommissioning liabilities (note 5)	30,179	99	60,865	237
Gain on sale of exploration and evaluations assets (note 3)	(50,000)	-	(50,000)	-
Gain on sale of property, plant and equipment (note 4)	(94,290)	-	(94,290)	-
Gain on acquisition (note 8)	(400,000)	-	(400,000)	(35,000)
Foreign exchange loss (gain)	(5,068)	75	(5,068)	1,574
	<u>518,328</u>	<u>65,718</u>	<u>1,497,284</u>	<u>145,091</u>
<b>NET INCOME (LOSS) FROM CONTINUING OPERATIONS</b>	<b>87,684</b>	<b>(62,975)</b>	<b>(311,710)</b>	<b>(137,181)</b>
<b>LOSS FROM DISCONTINUED OPERATIONS (note 9)</b>	<b>-</b>	<b>(8,680)</b>	<b>-</b>	<b>(25,945)</b>
<b>NET INCOME (LOSS)</b>	<b>\$ 87,684</b>	<b>\$ (71,655)</b>	<b>\$ (311,710)</b>	<b>\$ (163,126)</b>
<b>NET INCOME (LOSS) PER SHARE (note 7g)</b>				
Basic and diluted				
Net income (loss) per share from continuing operations	\$ -	\$ (0.01)	\$ (0.01)	\$ (0.01)
discontinued operations	-	-	-	-
Net income (loss) per share	<u>\$ -</u>	<u>\$ (0.01)</u>	<u>\$ (0.01)</u>	<u>\$ (0.01)</u>

See accompanying notes

**CONDENSED CONSOLIDATED INTERIM STATEMENTS OF COMPREHENSIVE INCOME (LOSS)**  
**FOR THE THREE AND SIX MONTHS ENDED JUNE 30**  
**(UNAUDITED, expressed in Canadian dollars)**

	Three months ended June 30		Six months ended June 30	
	2017	2016	2017	2016
<b>NET INCOME (LOSS)</b>	<b>\$ 87,684</b>	<b>\$ (71,655)</b>	<b>\$ (311,710)</b>	<b>\$ (163,126)</b>
Other comprehensive income to be reclassified to income in subsequent periods				
Foreign currency translation adjustment	-	(566)	(630)	13,486
<b>COMPREHENSIVE INCOME (LOSS)</b>	<b>\$ 87,684</b>	<b>\$ (72,221)</b>	<b>\$ (312,340)</b>	<b>\$ (149,640)</b>

See accompanying notes

**RETURN ENERGY INC.**  
**CONDENSED CONSOLIDATED INTERIM STATEMENTS OF CASH FLOW**  
**FOR THE SIX MONTHS ENDED JUNE 30**  
**(UNAUDITED, expressed in Canadian dollars)**

	2017	2016
<b>OPERATING ACTIVITIES</b>		
Loss from continuing operations	\$ (311,710)	\$ (137,181)
Add (subtract) items not requiring cash		
Depletion and depreciation	440,639	3,649
Gain on acquisition (note 8)	(400,000)	-
Gain on sale of exploration and evaluations assets	(50,000)	(35,000)
Gain on sale of property, plant and equipment	(94,290)	-
Accretion of decommissioning liabilities	60,865	237
Stock-based compensation	86,900	21,498
Unrealized foreign exchange (gain) loss	(630)	15,493
Settlement of decommissioning liabilities	(9,323)	-
Change in non-cash working capital items	414,295	1,328
Cash flow from (used in) continuing operations	136,746	(129,976)
Cash flow used in discontinued operations	-	(25,945)
Cash flow from (used in) operations	136,746	(155,921)
<b>INVESTING ACTIVITIES</b>		
Exploration and evaluation expenditures (note 3)	(99,455)	-
Property, plant and equipment expenditures (note 4)	(103,030)	-
Property acquisitions (note 8)	(834,236)	-
Property disposition (note 4)	118,973	35,000
Exploration and evaluations asset disposition (note 3)	50,000	-
Change in non-cash working capital items	45,462	-
Cash flow from (used in) continuing investing activities	(822,286)	35,000
<b>FINANCING ACTIVITIES</b>		
Proceeds from equity financing, net (note 7e)	1,918,858	-
Cash flow from continuing financing activities	1,918,858	-
Foreign exchange gain on cash held in a foreign currency	-	55
<b>INCREASE (DECREASE) IN CASH</b>	<b>1,233,318</b>	<b>(120,866)</b>
<b>CASH, BEGINNING OF PERIOD</b>	<b>602,848</b>	<b>166,218</b>
<b>CASH, END OF PERIOD</b>	<b>\$ 1,836,166</b>	<b>\$ 45,352</b>

See accompanying notes

# RETURN ENERGY INC.

Notes to the June 30, 2017 Condensed Consolidated Interim Financial Statements  
(Unaudited, All amounts in Canadian dollars unless otherwise stated)

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## 1. GENERAL INFORMATION

Return Energy Inc. ("Return", the "Company" or the "Group") is engaged in the exploration for and development and production of petroleum and natural gas properties in Alberta. Return's shares are widely held and publicly traded on the TSX Venture Exchange under the symbol "RTN". The Company was incorporated under the Alberta Business Corporations Act on March 20, 2006 and is domiciled in Calgary, Canada. The Company's head office is located at Suite 1220, 407 – 2nd Street S.W., Calgary, Alberta T2P 2Y3. The registered office of the Company is located at 1000, 250 - 2nd Street S.W., Calgary, Alberta T2P 0C1. On January 1, 2017 the Company amalgamated Murelle Enterprises Inc. and Bredal Energy Corp. into Winslow Resources Inc. As a result, Return Energy Inc. has two remaining 100% owned subsidiaries, Winslow Resources Inc. and DualEx International Inc.

## 2. BASIS OF PREPARATION

### a) Statement of compliance

These Unaudited Condensed Consolidated Interim Financial Statements for the three and six months ended June 30, 2017 (the "Financial Statements") have been prepared in accordance with International Accounting Standard ("IAS") 34 *Interim Financial Reporting* following accounting policies in accordance with International Financial Reporting Standards ("IFRS"). The Financial Statements do not include all of the information required for annual financial statements and should be read in conjunction with the Audited Consolidated Financial Statements for the year ended December 31, 2016, which have been prepared in accordance with IFRS. The Board of Directors approved the Financial Statements on Aug 22, 2017.

### b) Historical cost and fair value

The Financial Statements have been prepared using the historical cost basis with the exception of financial instruments designated at fair value through profit or loss.

### c) Functional and presentation currency

The Financial Statements are presented in Canadian dollars, which is the functional currency of Return and its domestic subsidiary. The functional currency of the Company's foreign subsidiary is US dollars.

### d) Significant accounting policies

The accounting policies adopted in the Financial Statements are consistent with those described in Note 3 of the Audited Consolidated Financial Statements for the year ended December 31, 2016.

## RETURN ENERGY INC.

Notes to the June 30, 2017 Condensed Consolidated Interim Financial Statements  
(Unaudited, All amounts in Canadian dollars unless otherwise stated)

### 3. EXPLORATION AND EVALUATION ASSETS

Balance, December 31, 2016	\$	-
Acquisition of undeveloped land		99,455
Balance, June 30, 2017	<u>\$</u>	<u>99,455</u>

During the three months ended June 30, 2017, the Company sold undeveloped land for \$50,000. The undeveloped land had a book value of \$nil, and as a result a gain on sale of \$50,000 was recorded.

### 4. PROPERTY, PLANT AND EQUIPMENT

	Oil and Gas Properties	Natural gas processing plant and equipment	Computer and office equipment	Total PP&E
<b>Cost</b>				
Balance December 31, 2016	\$ 7,894,242	\$ 350,000	\$ -	\$ 8,244,242
Additions	7,103	75,312	20,615	103,030
Acquisitions	862,221	450,000	-	1,312,221
Disposition	(319,197)	-	-	(319,197)
Change in estimate of decommissioning liabilities	579,222	10,774	-	589,996
Balance June 30, 2017	<u>\$ 9,023,591</u>	<u>\$ 886,086</u>	<u>\$ 20,615</u>	<u>\$ 9,930,292</u>
<b>Accumulated depletion, depreciation and impairment</b>				
Balance December 31, 2016	\$ (210,366)	\$ (3,500)	\$ -	\$ (213,866)
Disposition	32,066	-	-	32,066
Depletion and depreciation	(419,645)	(20,421)	(573)	(440,639)
Balance June 30, 2017	<u>\$ (597,945)</u>	<u>\$ (23,921)</u>	<u>\$ (573)</u>	<u>\$ (622,439)</u>
<b>Net Book Value</b>				
Balance December 31, 2016	\$ 7,683,876	\$ 346,500	\$ -	\$ 8,030,376
Balance June 30, 2017	<u>\$ 8,425,646</u>	<u>\$ 862,165</u>	<u>\$ 20,042</u>	<u>\$ 9,307,853</u>

During the three months ended June 30, 2017, the Company sold non-core oil assets for cash proceeds of \$118,973. The Company had a book value of \$287,131 and decommissioning liabilities of \$262,448 and as a result recorded a gain on sale of \$94,290.

At June 30, 2017, future development costs of \$4.7 million were included in the depletion calculation.

## RETURN ENERGY INC.

Notes to the June 30, 2017 Condensed Consolidated Interim Financial Statements  
(Unaudited, All amounts in Canadian dollars unless otherwise stated)

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### 5. DECOMMISSIONING LIABILITIES

The Company's decommissioning liabilities are based on the Company's net ownership in wells and facilities and management's estimate of costs to abandon and reclaim those wells and facilities as well as an estimate of the future timing of these costs.

Decommissioning liabilities, December 31, 2016	\$	6,236,420
Liabilities acquired (note 8)		57,000
Liabilities divested (note 4)		(262,448)
Liabilities settled		(9,323)
Accretion		60,865
Change in estimated future cash outflows (note 4)		589,996
Decommissioning liabilities, June 30, 2017		<u>\$ 6,672,510</u>
Expected to be incurred within one year	\$	-
Expected to be incurred beyond one year		<u>6,672,510</u>
	\$	<u>6,672,510</u>

The Company's decommissioning liabilities result from its ownership interest in oil and natural gas assets. The decommissioning liabilities are estimated based on the Company's net ownership interest in all wells and facilities, estimated costs to reclaim and abandon these wells and facilities, and the estimated timing of the costs to be incurred in future years. The undiscounted amount of the estimated future cash flows required to settle the obligations as at June 30, 2017 is \$9,423,000. Payments to settle the decommissioning liabilities occur over the operating lives of the underlying assets, estimated to be from 5 – 41 years. The estimated future cash flows have been discounted at a risk free rates between 1.4% and 2.1% and reflect an inflation rate of 2%.

### 6. CONVERTIBLE PREFERRED SHARES

The Company has two million non-interest bearing, non-voting Series I Convertible Preferred Shares (the "Preferred Shares") outstanding. The holder may, at any time and at its option, convert all or part of the Preferred Shares into units ("Units") of Return. Each Unit is comprised of one (1) common share of Return and one-half (1/2) of a common share purchase warrant. The number of Units issuable upon the conversion of the Preferred Shares is equal to the number of Preferred Shares to be converted multiplied by \$1.00 and divided by the average of the trading price of the common shares on the TSX Venture Exchange (the "TSXV") during the immediately prior twenty (20) consecutive day period prior to conversion (the "Market Price"). Each whole common share purchase warrant entitles the holder to purchase one (1) common share until October 21, 2021 upon payment of the Common Share purchase warrant exercise price which is equal to the Market Price. The Company may at its sole discretion redeem the Preferred Shares at any time upon cash payment of one dollar per Preferred Share.

The Preferred Shares meet the definition of a financial liability, and therefore are recorded as a debt instrument, due to the Company's obligation to deliver a variable number of its own common shares to the holder upon conversion.



# RETURN ENERGY INC.

Notes to the June 30, 2017 Condensed Consolidated Interim Financial Statements  
(Unaudited, All amounts in Canadian dollars unless otherwise stated)

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## 7. SHARE CAPITAL

### (a) Authorized

The Company is authorized to issue an unlimited number of common shares with no par value and an unlimited number of first preferred shares with no par value. The first preferred shares may be issued in series, with the directors determining the terms of the preferred shares on a series by series basis.

### (b) Share consolidation

On December 20, 2016 the Company consolidated its outstanding shares on a 10 for 1 basis. The share consolidation was approved by shareholders at the Company's annual shareholder meeting held on December 15, 2016. The Company had 250,088,939 common shares issued and outstanding prior to the share consolidation. Post consolidation the number of issued and outstanding shares is 25,008,894. The exercise price and number of common shares issuable pursuant to all outstanding stock options and warrants have been adjusted in accordance with the consolidation ratio.

All references to common shares and per share amounts have been retroactively restated to reflect the share consolidation.

### (c) Issued and outstanding

	Number of Shares	Amount
Common Shares		
Balance December 31, 2016	25,008,894	\$ 26,908,948
Equity financing (note 7e)	17,415,399	1,374,858
Balance June 30, 2017	<u>42,424,293</u>	<u>\$ 28,283,806</u>

### (d) Warrants

	Number of Warrants	Value	Weighted Average Exercise Price
Warrants outstanding December 31, 2016	6,802,500	\$ 180,417	\$ 0.15
Issuance of Warrants on equity financing (note 7e)	16,883,959	544,000	0.15
Warrants outstanding June 30, 2017	<u>23,686,459</u>	<u>\$ 724,417</u>	<u>\$ 0.15</u>

# RETURN ENERGY INC.

Notes to the June 30, 2017 Condensed Consolidated Interim Financial Statements  
(Unaudited, All amounts in Canadian dollars unless otherwise stated)

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## 7. SHARE CAPITAL (continued)

### (e) March 2017 financing

On March 14, 2017, the Company closed a non-brokered private placement comprised of common share units (the "Units") and Canadian exploration expense flow-through shares ("CEE FTS") (collectively, the "Offering"). Return issued 16,700,399 Units at a price of \$0.12 per Unit for gross proceeds of \$2,004,048, as well as 715,000 CEE FTS at a price of \$0.14 per CEE FTS for gross proceeds of \$100,100 for total gross proceeds of \$2,104,148. The CEE FTS were issued pursuant to the Income Tax Act (Canada) in respect of Canadian exploration expenses.

Each Unit issued consisted of one Return common share ("Common Share") and one full Common Share purchase warrant ("Warrant"). Each whole Warrant is exercisable by the holder to purchase one Common Share for a period of 12 months from March 14, 2017 ("Warrant Exercise Period") at a price of \$0.15 ("Warrant Exercise Price"). Each Warrant will entitle the holder thereof to purchase one Common Share at any time on or before the earlier of the date that is: (a) one year from the completion of the Offering; and (b) 30 days after the giving of notice of early termination by Return. Such notice may be given by the Company, in its sole discretion, if the volume-weighted average price of the Common Shares on the TSX Venture Exchange exceeds the Warrant Exercise Price by at least 200% for a minimum of 10 consecutive trading days (whether or not trading of Common Shares occurs on all such days, provided that the Common Shares trade on at least five of such trading days).

Finders received \$22,027 in cash and 183,560 Warrants as compensation. Total costs in connection with the financing amounted to \$185,290.

The Warrants have been assigned a value of \$544,000 using a Black-Scholes model with the following assumptions: expected life one year, expected volatility 100%, risk-free interest rate of 0.86%, and a zero dividend yield.

### (f) Stock based compensation

The Company has a stock option plan under which options to purchase common shares may be granted to officers, directors, employees and consultants. The Board has approved a policy of reserving up to 10% of the outstanding common shares for issuance to eligible participants. Under the plan, all options have a maximum term of five years. All options awarded to date vest 1/3 per year on the anniversary date of the grant for the next three years. During the six months ended June 30, 2017, the changes to the outstanding stock options are as follows:

	Number of Options	Weighted Average Exercise Price
Outstanding December 31, 2016	120,000	\$ 2.26
Granted	2,070,000	0.185
Expired	(15,000)	2.00
Outstanding June 30, 2017	<u>2,175,000</u>	<u>\$ 0.29</u>

## RETURN ENERGY INC.

Notes to the June 30, 2017 Condensed Consolidated Interim Financial Statements  
(Unaudited, All amounts in Canadian dollars unless otherwise stated)

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### 7. SHARE CAPITAL (continued)

The following summarizes outstanding stock options as at June 30, 2017.

<u>Date of Grant</u>	<u>Number Outstanding</u>	<u>Weighted Average Exercise Price</u>	<u>Weighted Average Remaining Contractual Life in Years</u>	<u>Options Exercisable</u>
02-Sep-14	105,000	\$ 2.30	2.17	70,000
05-Jan-17	2,070,000	\$ 0.185	4.50	-
	<u>2,175,000</u>	\$ 0.29		<u>70,000</u>

The Company determined the value of the options granted using a Black Scholes option pricing model with the following assumptions:

	<u>2017</u>
Risk free rate	1.1%
Expected life	5 years
Expected volatility	100%
Expected dividend	0%
Forfeiture rate	10%
Fair value of option	\$0.14

#### (g) Loss per share

The weighted average number of shares outstanding for the three months and six ended June 30, 2017 is 42,424,293 and 35,592,838, respectively (three and six months ended June 30, 2016, 2016 – 11,403,894). No options or warrants were included in the computation of diluted loss per share as they have an anti-dilutive effect on loss per share.

## RETURN ENERGY INC.

Notes to the June 30, 2017 Condensed Consolidated Interim Financial Statements  
(Unaudited, All amounts in Canadian dollars unless otherwise stated)

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### 8. GAIN ON ACQUISITION

On April 20, 2017, the Company acquired production of approximately 60 BOE/day (80% natural gas), and the remaining 50% interest in the Company's operated Rycroft gathering system and gas plant (the "Plant and production acquisition") for \$715,000 in cash, subject to closing adjustments. All of the acquired production is processed through the Rycroft gas plant.

The Company also completed two smaller acquisitions during the three months ended June 30, 2017 acquiring approximately 12 BOE/day of production for total consideration of \$140,221. (the "Other acquisitions").

The Company acquisitions were acquired to further consolidate its position in the Peace River Arch. The allocations and determinations of the purchase price are preliminary and subject to change upon final adjustments.

The estimated fair value of the acquisitions are as follows:

<b>Fair Value of net assets acquired:</b>	<u>Plant and production acquisition</u>	<u>Other acquisitions</u>	<u>Total acquisitions</u>
Property, plant and equipment	1,140,000	172,221	1,312,221
Decommissioning liabilities	(25,000)	(32,000)	(57,000)
Net assets acquired	<u>\$ 1,115,000</u>	<u>\$ 140,221</u>	<u>\$ 1,255,221</u>
<b>Consideration:</b>			
Cash	\$ 715,000	\$ 119,236	\$ 834,236
Non-cash consideration	-	20,985	20,985
Total consideration	<u>\$ 715,000</u>	<u>\$ 140,221</u>	<u>\$ 855,221</u>
Gain on acquisition	<u>\$ 400,000</u>	<u>\$ -</u>	<u>\$ 400,000</u>

The acquisitions contributed revenue of approximately \$74,000 and net income of approximately \$10,000 during the six months ended June 30, 2017.

Had these business combinations occurred on January 1, 2017, additional pro-forma revenue of approximately \$215,000 and net income of \$32,000 would have been recognized.

The fair value of the decommissioning obligations was based on the estimated future cash flows to decommission the acquired property, plant and equipment at the end of its useful life. The discount rate used to determine the net present value of the decommissioning obligation was the credit adjusted risk-free rate of 10%. Subsequently, the decommissioning liability was revalued at risk-free rates ranging from 1.4% to 2.1%, resulting in incremental additions of \$448,000 of decommissioning obligation, included in change in estimate, and corresponding additions to property, plant and equipment.

## **RETURN ENERGY INC.**

**Notes to the June 30, 2017 Condensed Consolidated Interim Financial Statements**  
**(Unaudited, All amounts in Canadian dollars unless otherwise stated)**

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### **9. DISCONTINUED OPERATIONS**

In June 2016 the Company relinquished its interest in the Bouhajla block in Tunisia and discontinued its operations in Tunisia.

Operating results related to discontinued operations have been included in loss from discontinued operations on the consolidated statements of net income (loss). Comparative period balances have been restated. During the three and six months ended June 30, 2017 \$nil have been incurred in Tunisia (three and six months ended June 30, 2016 \$8,680 and \$25,945, respectively.)

### **10. FINANCIAL INSTRUMENTS**

The Company's financial instruments recognized in the consolidated statement of financial position consist of cash, accounts receivable, deposits, accounts payable and accrued liabilities, and Preferred Shares. Cash is classified as held for trading. The carrying value of cash, accounts receivable, and accounts payable and accrued liabilities approximate their respective fair values due to their short-term to maturity. The carrying value of the Preferred Shares approximate their fair value as they are convertible at the Market Price.

### **11. COMMITMENTS**

The Company entered into a lease agreement whereby the Company will lease office space until September 30, 2019. The Company has committed to future payments under this lease of \$18,200 in 2017, \$75,800 in 2018 and \$54,600 in 2019.

The Company has a commitment to spend a minimum of \$100,000 by December 31, 2018 to meet its flow through obligation. To date the Company has spent approximately \$80,000 of its flow through obligation.

### **12. RELATED PARTY DISCLOSURE**

During the three months ended June 30, 2017, the Company purchased two sections of undeveloped land from a corporation controlled by an officer of the Company for \$60,000. The cost of the undeveloped land is comparable to what would have been paid to unrelated parties.

# CORPORATE INFORMATION

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## OFFICERS

Kenneth M. Tompson, P. Geol  
President and Chief Executive Officer

Garry T. Hides, P. Land  
Executive Vice President

Jason Schoenfeld, P. Eng  
VP Engineering and Chief Operating Officer

Lorne A. Morozoff, CA  
VP Finance and Chief Financial Officer

## DIRECTORS

Kenneth M. Tompson, P. Geol  
Calgary, AB  
President and Chief Executive Officer

Garry T. Hides, P. Land  
Chestermere, AB  
Executive Vice President

Roy H. Hudson, LLB  
Calgary, AB  
Partner  
DLA Piper LLP

Bradley B. Porter  
Okotoks, AB  
Independent Businessman

Robb D. Thompson, CA  
Calgary, AB  
Chief Financial Officer  
Bonterra Energy Corp.

## HEAD OFFICE

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## STOCK LISTING

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Trading Symbol "RTN"

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