## FINANCIAL AND OPERATING

($000s except per share amounts)

| | Three Months Ended | | | Six Months Ended June 30, | | |
|---|---|---|---|---|---|---|
| | **Jun 30, 2016** | Mar 31, 2016 | % Change | **2016** | 2015 | % Change |
| **Financial highlights** | | | | | | |
| Oil sales | **37,523** | 26,166 | 43 % | **63,689** | 139,724 | (54)% |
| NGL sales | **1,367** | 769 | 78 % | **2,136** | 2,706 | (21)% |
| Natural gas sales | **2,053** | 2,211 | (7)% | **4,264** | 8,791 | (51)% |
| Total oil, natural gas, and NGL revenue | **40,943** | 29,146 | 40 % | **70,089** | 151,221 | (54)% |
| Funds from operations[1] | **22,063** | 7,491 | 195 % | **29,554** | 86,562 | (66)% |
| Per share basic ($) | **0.10** | 0.03 | 233 % | **0.13** | 0.39 | (67)% |
| Per share diluted ($) | **0.10** | 0.03 | 233 % | **0.13** | 0.39 | (67)% |
| Capital expenditures - petroleum & gas properties[2] | **16,810** | 12,873 | 31 % | **29,683** | 40,769 | (27)% |
| Capital expenditures - acquisitions & dispositions[2] | **—** | (41,141) | nm[4] | **(41,141)** | (460,950) | nm |
| Total capital expenditures[2] | **16,810** | (28,268) | nm | **(11,458)** | (420,181) | nm |
| Net debt at end of period[3] | **134,613** | 133,816 | 1 % | **134,613** | 125,478 | 7 % |
| **Operating highlights** | | | | | | |
| Production: | | | | | | |
| Oil (bbls per day) | **8,958** | 9,821 | (9)% | **9,389** | 15,315 | (39)% |
| NGLs (bbls per day) | **564** | 615 | (8)% | **589** | 696 | (15)% |
| Natural gas (mcf per day) | **15,959** | 17,829 | (10)% | **16,894** | 18,594 | (9)% |
| Total (boe per day) (6:1) | **12,182** | 13,408 | (9)% | **12,794** | 19,110 | (33)% |
| Average realized price (excluding hedges): | | | | | | |
| Oil ($ per bbl) | **46.03** | 29.28 | 57 % | **37.27** | 50.40 | (26)% |
| NGL ($ per bbl) | **26.64** | 13.75 | 94 % | **19.91** | 21.47 | (7)% |
| Natural gas ($ per mcf) | **1.41** | 1.36 | 4 % | **1.39** | 2.61 | (47)% |
| **Netback ($ per boe)** | | | | | | |
| Oil, natural gas and NGL sales | **36.94** | 23.89 | 55 % | **30.10** | 43.72 | (31)% |
| Realized gain (loss) on commodity contracts | **3.45** | 3.26 | nm | **3.35** | 10.54 | nm |
| Royalties | **(3.27)** | (3.14) | 4 % | **(3.20)** | (6.46) | (50)% |
| Operating expenses | **(12.69)** | (12.27) | 3 % | **(12.47)** | (16.55) | (25)% |
| Transportation expenses | **(1.16)** | (2.33) | (50)% | **(1.77)** | (1.43) | 24 % |
| Operating netback | **23.27** | 9.41 | 147 % | **16.01** | 29.82 | (46)% |
| G&A expense | **(1.98)** | (1.96) | 1 % | **(1.97)** | (1.91) | 3 % |
| Interest expense | **(1.38)** | (1.32) | 5 % | **(1.35)** | (2.88) | (53)% |
| Corporate netback | **19.91** | 6.13 | 225 % | **12.69** | 25.03 | (49)% |
| Common shares outstanding, end of period | **221,047** | 221,047 | — % | **221,047** | 221,147 | — % |
| Weighted average basic shares | **221,047** | 221,042 | — % | **221,045** | 220,174 | — % |
| Stock option dilution | **—** | — | nm | **—** | — | nm |
| Weighted average diluted shares | **221,047** | 221,042 | — % | **221,045** | 220,174 | — % |

1 Management uses funds from operations (cash flow from operating activities before changes in non-cash working capital, decommissioning expenditures, transaction costs and cash settled stock-based compensation) to analyze operating performance and leverage. Funds from operations as presented does not have any standardized meaning prescribed by IFRS and, therefore, may not be comparable with the calculation of similar measures for other entities.

2 Please see capital expenditures discussion in this MD&A.

3 The Company defines net debt as outstanding bank debt plus or minus working capital, however, excluding the fair value of financial contracts and other current obligations.

4 The Company views this change calculation as not meaningful, or "nm".

## SECOND QUARTER 2016 HIGHLIGHTS

- Funds flow from operations ("FFO") was $22.1 million in the second quarter of 2016, or $0.10 per share.
- Surge delivered an all-in sustainability ratio of 95 percent for the quarter, with oil prices averaging US$45.59 WTI per barrel.
- The Company achieved a debt to cashflow ratio of 1.52 times annualized cashflow for the quarter.
- The Company's recent 14 well drilling program has added production of more than 2,000 boepd (85 percent oil; IP/180 day), at an all-in on-stream cost of $19.75 million - providing a production efficiency of less than $9,875 per flowing boepd.
- As a result of Surge's excellent development drilling results discussed above, together with continued successful waterflood results at Shaunavon, Eyehill, Nipisi, Silver, and Doe, Surge's current production continues to exceed the Company's previously announced 2016 production exit rate target of 13,000 boepd.
- Through two recent Crown purchases in the Sparky area, Surge has acquired nine contiguous sections of 100 percent working interest land (with prior vertical Sparky well control) prospective for Sparky production. The acquired lands have an estimated OOIP of more than 65 million barrels. Surge will be drilling this exciting new Sparky reservoir (utilizing modern horizontal and completion technology) in 2017.
- Surge achieved an operating netback of $23.27 per boe and a corporate netback of $19.91 per boe in the quarter, an increase of 147 percent and 225 percent respectively from the first quarter of 2016.
- Operating expenses were $12.69 per boe, down 16 percent as compared to the same period in 2015, as Surge operations personnel continue to execute on optimization projects.
- Transportation expenses were reduced by 50 percent as compared to the first quarter of 2016, as the benefits from facilities optimization projects at Valhalla were realized for a full quarter.
- Production volumes for the quarter reflect the $28 million non-core asset sale of Sunset, a 700 boepd divestiture that closed at the end of the first quarter of 2016. Volumes were also negatively impacted by approximately 350 boepd of unplanned downtime at a third party processing facility, and approximately 300 boepd of uneconomic shut-in production.
- Surge's banking facility was re-determined at $250 million subsequent to the quarter. With net debt of $134.6 million at June 30, 2016, the facility is approximately 54 percent drawn, providing the Company with ample liquidity to continue to execute on Surge's business plan. The reduction in stand-by fees should result in a $1 million savings in annual interest expense.

## MANAGEMENT'S DISCUSSION AND ANALYSIS

This Management's Discussion and Analysis (MD&A) of the consolidated financial position and results of operations of Surge Energy Inc. ("Surge" or the "Company"), which includes its subsidiaries and partnership arrangements, is for the three and six months ended June 30, 2016 and 2015. For a full understanding of the financial position and results of operations of the Company, the MD&A should be read in conjunction with the documents filed on SEDAR, including historical financial statements, MD&A and the Annual Information Form (AIF). These documents are available at www.sedar.com.

Surge's interim financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS").

## DESCRIPTION OF BUSINESS

Surge is an E&P company positioned to provide shareholders with attractive long term sustainability by exploiting the Company's assets in a financially disciplined manner and by acquiring additional long life oil and gas assets of a similar nature. Surge's assets are comprised primarily of operated oil-weighted properties characterized by large OOIP crude oil reservoirs with low recovery factors and an extensive inventory of more than seven hundred gross low risk development drilling locations and several high quality waterflood projects. Surge will continue to identify and actively pursue strategic acquisitions with synergistic characteristics such as existing long life producing assets or opportunities with significant, low risk upside potential.

## NON-IFRS MEASURES

The terms "funds from operations", "funds from operations per share", and "netback" used in this discussion are not recognized measures under International Financial Reporting Standards (IFRS). Management believes that in addition to net income, funds from operations and netback are useful supplemental measures as they provide an indication of the results generated by the Company's principal business activities before the consideration of how those activities are financed or how the results are taxed. Investors are cautioned, however, that these measures should not be construed as alternatives to net income determined in accordance with IFRS, as an indication of Surge's performance.

Surge's method of calculating funds from operations may differ from that of other companies, and, accordingly, may not be comparable to measures used by other companies. Surge determines funds from operations as cash flow from operating activities before changes in non-cash working capital, decommissioning expenditures, transaction costs and cash settled stock-based compensation.

Funds from Operations

| ($000s) | **Q2 2016** | Q1 2016 | Q4 2015 | Q3 2015 | Q2 2015 |
|---|---|---|---|---|---|
| Cash flow from operating activities | **$ 15,509** | $ 5,371 | $ 17,346 | $ 9,512 | $ 26,760 |
| Change in non-cash working capital | **5,728** | 1,097 | (2,978) | 5,015 | (178) |
| Decommissioning expenditures | **(85)** | 402 | 319 | 712 | 382 |
| Transaction costs | **44** | 186 | 141 | 265 | 7,468 |
| Cash settled stock-based compensation | **867** | 435 | 474 | 1,505 | 1,058 |
| **Funds from operations** | **$ 22,063** | $ 7,491 | $ 15,302 | $ 17,009 | $ 35,490 |

Funds from operations per share is calculated using the same weighted average basic and diluted shares used in calculating income per share. Operating and corporate netbacks are also presented. Operating netbacks represent Surge's revenue, realized gains or losses on financial contracts, less royalties and operating and transportation expenses. Corporate netbacks represent Surge's operating netback, less general and administrative and interest expenses, in order to determine the amount of funds generated by production. Operating and corporate netbacks have been presented on a per barrels of oil equivalent ("boe") basis. This reconciliation is shown within the MD&A. Share based consideration included in acquisition capital has been calculated using the share price on the date of announcement.

Surge's management is responsible for the integrity of the information contained in this report and for the consistency between the MD&A and financial statements. In the preparation of these statements, estimates are necessary to make a determination of future values for certain assets and liabilities. Management believes these estimates have been based on careful judgments and have been properly presented. The financial statements have been prepared using policies and procedures established by management and fairly reflect Surge's financial position, results of operations and funds from operations.

The Company defines net debt as outstanding bank debt plus or minus working capital, however, excluding the fair value of financial contracts and other current obligations.

Surge's Board of Directors and Audit Committee have reviewed and approved the financial statements and MD&A. This MD&A is dated August 3, 2016.

## OPERATIONS

### Drilling

| | Drilling | | Success | Working |
|---|---|---|---|---|
| | Gross | Net | rate (%) net | interest (%) |
| Q1 2016 | 3.0 | 3.0 | 100% | 100% |
| Q2 2016 | 8.0 | 8.0 | 100% | 100% |
| **Total** | **11.0** | **11.0** | **100%** | **100%** |

Surge achieved a 100 percent success rate during the six months ended June 30, 2016, drilling 11 gross (11.0 net) wells. During the second quarter of 2016, Surge drilled 8 gross (8.0 net) wells, including seven wells at Shaunavon and one well at Valhalla.

### Production

| | **Three months ended** | | | **Six Months Ended** | |
|---|---|---|---|---|---|
| | **Jun 30, 2016** | Mar 31, 2016 | Jun 30, 2015 | **Jun 30, 2016** | Jun 30, 2015 |
| Oil (bbls per day) | **8,958** | 9,821 | 14,345 | **9,389** | 15,315 |
| NGL (bbls per day) | **564** | 615 | 520 | **589** | 696 |
| Oil and NGL (bbls per day) | **9,522** | 10,436 | 14,865 | **9,978** | 16,011 |
| Natural gas (mcf per day) | **15,959** | 17,829 | 16,724 | **16,894** | 18,594 |
| Total (boe per day) (6:1) | **12,182** | 13,408 | 17,652 | **12,794** | 19,110 |
| % Oil and NGL | **78%** | 78% | 84% | **78%** | 84% |

Surge achieved production of 12,182 boe per day in the second quarter of 2016 (78 percent oil and NGLs), a nine percent decrease from the average production rate in the first quarter of 2016 and a 31 percent decrease from the average production rate in the same period of 2015.

During the six months ended June 30, 2016, Surge achieved production of 12,794 boe per day (78 percent oil and NGLs), a 33 percent decrease when compared to the same period of 2015.

The decrease in production volumes as compared to the first quarter of 2016 is primarily due to the disposition of Surge's Sunset assets on March 31, 2016, representing approximately 700 boe per day in addition to an unplanned outage at a third-party gas processing facility in the Valhalla area, negatively impacting production by approximately 350 boe per day. A further decrease in production due to natural production declines during the period was offset by production from wells drilled in the second quarter of 2016, of which five (of the eight spud) were on production near the end of the quarter. The remaining three wells drilled in the second quarter of 2016 came on production subsequent to the end of the quarter.

The decrease in production volumes for the three and six months ended June 30, 2016 as compared to the same periods in 2015 is primarily due to the disposition of Surge's southeast Saskatchewan and southwest Manitoba assets on June 15, 2015, representing approximately 4,750 boe per day, in addition to the Sunset assets sale and unplanned third-party outage as discussed above.

### Revenue, Realized Prices and Benchmark Pricing

| | Three Months Ended | | | Six Months Ended | |
|---|---|---|---|---|---|
| ($000s except per amount) | **Jun 30, 2016** | Mar 31, 2016 | Jun 30, 2015 | **Jun 30, 2016** | Jun 30, 2015 |
| **Revenue** | | | | | |
| Oil | **37,523** | 26,166 | 76,706 | **63,689** | 139,724 |
| NGL | **1,367** | 769 | 787 | **2,136** | 2,706 |
| Oil and NGL | **38,890** | 26,935 | 77,493 | **65,825** | 142,430 |
| Natural gas | **2,053** | 2,211 | 3,375 | **4,264** | 8,791 |
| Total oil, natural gas and NGL revenue | **40,943** | 29,146 | 80,868 | **70,089** | 151,221 |
| **Realized Prices** | | | | | |
| Oil ($ per bbl) | **46.03** | 29.28 | 58.74 | **37.27** | 50.40 |
| NGL ($ per bbl) | **26.64** | 13.75 | 16.64 | **19.91** | 21.47 |
| Oil and NGL ($ per bbl) | **44.88** | 28.36 | 49.15 | **36.25** | 49.15 |
| Natural gas ($ per mcf) | **1.41** | 1.36 | 2.22 | **1.39** | 2.61 |
| Total oil, natural gas, and NGL revenue before realized commodity contracts ($ per boe) | **36.94** | 23.89 | 50.34 | **30.10** | 43.72 |
| **Benchmark Prices** | | | | | |
| WTI (US$ per bbl) | **45.59** | 33.45 | 57.94 | **39.52** | 53.29 |
| WTI (C$ per bbl) | **58.81** | 45.82 | 71.27 | **52.56** | 66.08 |
| Edmonton Light Sweet (C$ per bbl) | **54.68** | 40.67 | 67.62 | **47.68** | 59.71 |
| WCS (C$ per bbl) | **41.61** | 26.31 | 56.97 | **33.96** | 49.55 |
| AECO Daily Index (C$ per mcf) | **1.40** | 1.84 | 2.66 | **1.62** | 2.70 |

Total oil, natural gas and NGL revenue for the second quarter of 2016 increased 40 percent when compared to the first quarter of 2016. The increase is primarily due to an increase in realized oil pricing, slightly offset by a decrease in oil production. The 40 percent increase in total oil, natural gas and NGL revenue as compared to the first quarter of 2016, correlates to the increase in Edmonton light sweet crude oil of 34 percent and the increase in WCS crude oil of 58 percent.

The differential between Surge's realized oil price and the Edmonton light sweet price contracted to $8.65 per bbl in the second quarter of 2016. This compares to a differential of $11.39 per bbl in the immediate preceding first quarter. The Company's realized oil price differential contraction of 24 percent from the first quarter to the second quarter of 2016 trends in line with the 20 percent contraction in the CAD WTI to Edmonton light sweet differential during this same period.

Total oil, natural gas and NGL revenue for the second quarter of 2016 decreased 49 percent when compared to the same period of 2015. The decrease is primarily due to a significant decline in realized oil pricing, directly correlated with a decline in benchmark pricing, in addition to a decrease in production, as discussed in the production section of this MD&A. Surge's realized average revenue per barrel of oil during the second quarter of 2016 decreased 22 percent compared to the same period of 2015. This compares to a 19 percent decrease in Edmonton light sweet and 27 percent decrease in WCS during the same periods.

Total oil, natural gas and NGL revenue for the six months ended June 30, 2016 decreased 54 percent when compared to the same period of 2015. The decrease is primarily due to a significant decline in realized oil pricing, directly correlated with a decline in benchmark pricing, in addition to a decrease in production, as discussed in the production section of this MD&A. Surge's realized average revenue per barrel of oil during the six months ended June 30, 2016 decreased 26 percent compared to the same period of 2015. This compares to a 20 percent decrease in Edmonton light sweet and 31 percent decrease in WCS during the same period.

## ROYALTIES

| | Three Months Ended | | | Six Months Ended | |
|---|---|---|---|---|---|
| ($000s except per boe) | **Jun 30, 2016** | Mar 31, 2016 | Jun 30, 2015 | **Jun 30, 2016** | Jun 30, 2015 |
| Royalties | **3,626** | 3,830 | 11,733 | **7,456** | 22,357 |
| % of Revenue | **9%** | 13% | 15% | **11%** | 15% |
| $ per boe | **3.27** | 3.14 | 7.30 | **3.20** | 6.46 |

As royalties are sensitive to both commodity prices and production levels, the corporate royalty rates will fluctuate with commodity prices, well production rates, production decline of existing wells, and performance and location of new wells drilled.

The decrease in royalties as a percentage of revenue for the second quarter of 2016 as compared to the first quarter of 2016 is primarily due to a favorable gas cost allowance ("GCA") adjustment of approximately $1.0 million during the current period.

The decrease in royalties as a percentage of revenue and per boe for the three and six months ended June 30, 2016 as compared to the same periods of 2015 is primarily due to the significant decrease in commodity prices (see pricing section of this MD&A for further discussion) in addition to the favorable GCA adjustment recognized in the second quarter of 2016.

Excluding the GCA adjustment, royalties as a percentage of revenue for the three and six months ended June 30, 2016 would have been 11% and 12%, respectively.

On January 29, 2016, the Alberta Government released a new Royalty Regime effective January 1, 2017. The new regime will apply to wells drilled after the effective date, whereby all other wells will follow the old framework for a further 10 years. On April 21, 2016, the Alberta Government provided further details and calibration on the Modernized Royalty Framework. These details were seen as the second step of a five-step process with plans to provide further information throughout 2016. As additional information continues to be provided, Surge will continue to monitor the overall impact on the Company starting in 2017.

## OPERATING EXPENSES

| | Three Months Ended | | | Six Months Ended | |
|---|---|---|---|---|---|
| ($000s except per boe) | **Jun 30, 2016** | Mar 31, 2016 | Jun 30, 2015 | **Jun 30, 2016** | Jun 30, 2015 |
| Operating expenses | **14,062** | 14,964 | 24,311 | **29,026** | 57,256 |
| $ per boe | **12.69** | 12.27 | 15.13 | **12.47** | 16.55 |

Operating expenses per boe for the second quarter of 2016 increased three percent when compared to the immediately preceding first quarter and decreased 16 percent when compared to the same period of the prior year.

Operating expenses per boe for the six months ended June 30, 2016 decreased 25 percent as compared to the same period of the prior year.

The increase in operating expenses per boe as compared to the first quarter of 2016 is due to a decrease in production in the Company's Valhalla operating area of approximately 350 boe per day during the second quarter of 2016 (see Operations section of MD&A for further discussion). Had second quarter 2016 production volumes not been negatively impacted by 350 boe per day, operating expenses would have been $12.33 per boe, comparable to the first quarter of 2016.

The decrease in operating expenses per boe during the three and six months ended June 30, 2016 as compared to the same periods of 2015 is mainly due to Surge's focus on allocating capital and increasing production in low cost operating areas throughout 2015 and the first half of 2016 in addition to a favourable 13-month adjustment in the second quarter of 2016 in the amount of $1.1 million or $0.99 per boe. The Company also realized favourable adjustments in the first quarter of 2016 totaling $1.2 million or $0.98 per boe during that period.

Excluding the above discussed adjustments, operating expenses per boe for the three and six months ended June 30, 2016 would have averaged approximately $13.70 and $13.50, respectively. Surge expects normalized operating expenses per boe, excluding 13-month adjustments, to continue trending within previously stated guidance of $13.45 per boe to $13.95 per boe for the remainder of 2016.

## TRANSPORTATION EXPENSES

| | Three Months Ended | | | Six Months Ended | |
|---|---|---|---|---|---|
| ($000s except per boe) | **Jun 30, 2016** | Mar 31, 2016 | Jun 30, 2015 | **Jun 30, 2016** | Jun 30, 2015 |
| Transportation expenses | **1,288** | 2,843 | 2,327 | **4,131** | 4,945 |
| $ per boe | **1.16** | 2.33 | 1.45 | **1.77** | 1.43 |

Transportation expenses per boe for the second quarter of 2016 decreased 50 percent compared to the first quarter of 2016 and decreased 20 percent compared to the second quarter of 2015.

The decrease in transportation expense during the second quarter of 2016 as compared to the first quarter of 2016 is primarily due to the completion of Surge's strategic infrastructure project, connecting the Company's associated gas in the Valhalla operating area to nearby sweet gas processing plants and thereby concluding the payment of additional costs to help minimize curtailment of production in this area. During the first quarter of 2016, Surge incurred additional costs equal to $0.49 per boe related to this issue. Additionally, a $0.5 million or $0.41 per boe reclassification of trucking costs from operating expenses was recognized in the first quarter of 2016.

The decrease in transportation expense during the second quarter of 2016 compared to the second quarter of 2015 is primarily due to cost savings realized as a result of the Company's continued waterflood projects in its core areas whereby produced water is held in the field for reinjection as opposed to transported for disposal as wet emulsion.

The increase in transportation expense during the six months ended June 30, 2016 compared to the same period of the prior year is primarily a result of the additional costs recognized in the Valhalla operating area and the one-time reclassification of trucking costs during the first quarter of 2016, as discussed above. Excluding those adjustments, transportation expenses during the six months ended June 30, 2016 would have been approximately $1.40, comparable to the same period of the prior year.

Surge anticipates that transportation expenses per boe should return to historical levels of approximately $1.25 to $1.50 per boe over the remainder of 2016.

## GENERAL AND ADMINISTRATIVE EXPENSES (G&A)

| | Three Months Ended | | | Six Months Ended | |
|---|---|---|---|---|---|
| ($000s except per boe) | **Jun 30, 2016** | Mar 31, 2016 | Jun 30, 2015 | **Jun 30, 2016** | Jun 30, 2015 |
| G&A expenses | **3,126** | 3,272 | 4,454 | **6,398** | 10,215 |
| Recoveries and capitalized amounts | **(933)** | (877) | (1,820) | **(1,810)** | (3,612) |
| Net G&A expenses | **2,193** | 2,395 | 2,634 | **4,588** | 6,603 |
| Net G&A expenses $ per boe | **1.98** | 1.96 | 1.64 | **1.97** | 1.91 |

Net G&A expenses per boe of $1.98 for the second quarter of 2016 was comparable to the first quarter of 2016 and increased 21 percent as compared to the second quarter of 2015. The increase in net G&A expenses per boe is primarily due to the 31 percent decrease in production as compared to the same period of 2015. Total net G&A expenses for the second quarter of 2016 decreased eight percent when compared to the first quarter of 2016 and 17 percent when compared to the second quarter of 2015, as the company wide G&A cost reduction initiative implemented in 2015 continues to be realized.

Net G&A expenses per boe for the six months ended June 30, 2016 increased three percent compared to the same period in 2015. The increase in net G&A expenses in the first half of 2016 as compared to the same period in 2015 is primarily due to the 33 percent decrease in production over the periods. However, net G&A expenses have decreased 31 percent as a result of the implementation of a company wide G&A cost reduction initiative; the results of which are continuing to be realized throughout 2016.

## TRANSACTION COSTS

| | Three Months Ended | | | Six Months Ended | |
|---|---|---|---|---|---|
| ($000s except per boe) | **Jun 30, 2016** | Mar 31, 2016 | Jun 30, 2015 | **Jun 30, 2016** | Jun 30, 2015 |
| Transaction costs | **44** | 186 | 7,468 | **230** | 7,774 |
| $ per boe | **0.04** | 0.15 | 4.65 | **0.10** | 2.25 |

For the period ended June 30, 2016, the Company incurred transaction costs of $0.04 per boe, related to the acquisition and dispositions during the first quarter of 2016. The Company incurred transaction costs of $7.5 million and $7.8 million during the three and six months ended June 30, 2015, respectively, primarily related to the disposal of its petroleum and natural gas properties in southeast Saskatchewan and southwest Manitoba.

## FINANCE EXPENSES

| | Three Months Ended | | | Six Months Ended | |
|---|---|---|---|---|---|
| ($000s except per boe) | **Jun 30, 2016** | Mar 31, 2016 | Jun 30, 2015 | **Jun 30, 2016** | Jun 30, 2015 |
| Interest expense | **1,526** | 1,606 | 4,493 | **3,132** | 9,962 |
| $ per boe | **1.38** | 1.32 | 2.80 | **1.35** | 2.88 |
| Accretion expense | **716** | 790 | 921 | **1,506** | 2,261 |
| $ per boe | **0.64** | 0.64 | 0.57 | **0.64** | 0.65 |
| Finance expenses | **2,242** | 2,396 | 5,414 | **4,638** | 12,223 |
| $ per boe | **2.02** | 1.96 | 3.37 | **1.99** | 3.53 |

Interest expense during the second quarter of 2016 decreased five percent as compared to the first quarter of 2016 and decreased 66 percent as compared to the same period of 2015.

Interest expense during the six months ended June 30, 2016 decreased 69 percent as compared to the same period of 2015.

The decrease in interest expense during the three and six months ended June 30, 2016, as compared to the same periods of the prior year, is primarily due to lower debt levels. Surge decreased debt levels with the successful closing of the southeast Saskatchewan and southwest Manitoba asset sale, and certain non-core properties in Alberta and Saskatchewan, for combined cash proceeds of $469 million in 2015. The proceeds were used to pay down bank indebtedness.

A further decrease in interest expense is expected during the second half of 2016 as a result of the Company's revised borrowing base of $250 million, down from $400 million at the last review. Annual interest expense savings, in the form of standby charges, of approximately $1.0 million are expected due to the Company carrying $150 million less unutilized credit capacity on its bank line.

Accretion represents the change in the time value of the decommissioning liability as well as a firm transportation agreement. Accretion expense per boe increased for the three months ended June 30, 2016 as compared to the same period of 2015 and was comparable to the immediate prior quarter primarily due to a change in discount rate and higher liabilities relative to production. The underlying liability may increase over a period of time, based on new obligations incurred from drilling wells, constructing facilities, acquiring operations or adjusting future estimates of timing or amounts. This future obligation can be reduced as a result of abandonment work undertaken.

## NETBACKS

| | Three Months Ended | | | Six Months Ended | |
|---|---|---|---|---|---|
| ($ per boe, except production) | **Jun 30, 2016** | Mar 31, 2016 | Jun 30, 2015 | **Jun 30, 2016** | Jun 30, 2015 |
| Average production (boe per day) | **12,182** | 13,408 | 17,652 | **12,794** | 19,110 |
| Revenue | **36.94** | 23.89 | 50.34 | **30.10** | 43.72 |
| Realized gain on commodity contracts | **3.45** | 3.26 | 0.07 | **3.35** | 10.54 |
| Royalties | **(3.27)** | (3.14) | (7.30) | **(3.20)** | (6.46) |
| Operating costs | **(12.69)** | (12.27) | (15.13) | **(12.47)** | (16.55) |
| Transportation costs | **(1.16)** | (2.33) | (1.45) | **(1.77)** | (1.43) |
| **Operating netback** | **23.27** | 9.41 | 26.53 | **16.01** | 29.82 |
| G&A expense | **(1.98)** | (1.96) | (1.64) | **(1.97)** | (1.91) |
| Interest expense | **(1.38)** | (1.32) | (2.80) | **(1.35)** | (2.88) |
| **Corporate netback** | **19.91** | 6.13 | 22.09 | **12.69** | 25.03 |

Surge's operating netback for the second quarter of 2016 increased 147 percent compared to the first quarter of 2016 and decreased 12 percent as compared to the same period of 2015.

The increase in Surge's operating netback as compared to the first quarter of 2016 is primarily attributable to a 55 percent increase in revenue per boe as a result of higher oil prices during the period and a 50 percent decrease in transportation costs per boe. This increase is partially offset by a four percent increase in royalties per boe and a three percent increase in operating costs per boe. The increase in corporate netback was further impacted by a 10 percent increase in G&A expense per boe and an five percent increase in interest expense per boe as compared to the first quarter of 2016.

The 12 percent decrease in Surge's operating netback for the second quarter 2016 as compared to the same period of 2015 is primarily attributable to a 27 percent decrease in revenue per boe as a result of lower oil prices during the period. This decrease is partially offset by a $3.45 per boe realized gain on commodity contracts as compared to a $0.07 per boe realized gain on commodity contracts in same period of 2015, a 55 percent decrease in royalties per boe, a 16 percent decrease in operating costs per boe, and a 20 percent decrease in transportation costs per boe. The decrease in corporate netback was further impacted by a 51 percent decrease in interest expense per boe and a 32 percent increase in G&A expense per boe as compared to the same period of 2015.

Surge's operating netback for the first six months of 2016 decreased 46 percent compared to the same period of 2015. The decrease is primarily attributable to a 31 percent decrease in revenue per boe as a result of lower oil prices during the period, a $3.35 per boe realized gain on commodity contracts as compared to a $10.54 per boe realized gain on commodity contacts during the first six months of 2015, and a 24 percent increase in transportation costs per boe. This decrease is partially offset by a 50 percent decrease in royalties per boe and a 25 percent decrease in operating costs per boe. The decrease in corporate netback was further impacted by a 53 percent decrease in interest expense per boe and an eight percent increase in G&A expense per boe as compared to the same period of 2015.

## FUNDS FROM OPERATIONS AND CASH FLOW FROM OPERATIONS

| | Three Months Ended | | | Six Months Ended | |
|---|---|---|---|---|---|
| ($000s except per share and per boe) | **Jun 30, 2016** | Mar 31, 2016 | Jun 30, 2015 | **Jun 30, 2016** | Jun 30, 2015 |
| Funds from operations | **22,063** | 7,491 | 35,490 | **29,554** | 86,562 |
| Per share - basic ($) | **0.10** | 0.03 | 0.16 | **0.13** | 0.39 |
| Per share - diluted ($) | **0.10** | 0.03 | 0.16 | **0.13** | 0.39 |
| $ per boe | **19.90** | 6.14 | 22.09 | **12.70** | 25.03 |
| Cash flow from operating activities | **15,509** | 5,371 | 26,760 | **20,880** | 80,583 |

Funds from operations increased 195 percent in the second quarter of 2016 compared to the first quarter of 2016 and decreased 38 percent compared to the same period of 2015. On a per share basis, funds from operations increased 233 percent in the second quarter of 2016 compared to the first quarter of 2016 and decreased 38 percent compared to the same period of 2015.

Funds from operations decreased 66 percent for the six months ended June 30, 2016 compared to the same period of 2015. On a per share basis, funds from operations decreased 67 percent compared to the same period of 2015.

Cash flow from operating activities differs from funds from operations principally due to the inclusion of changes in non-cash working capital. Included in cash flow from operations is a decrease in non-cash working capital of $5.7 million in the second quarter of 2016.

## STOCK-BASED COMPENSATION

| | Three Months Ended | | | Six Months Ended | |
|---|---|---|---|---|---|
| ($000s except per boe) | **Jun 30, 2016** | Mar 31, 2016 | Jun 30, 2015 | **Jun 30, 2016** | Jun 30, 2015 |
| Stock-based compensation | **5,103** | 2,516 | 4,418 | **7,619** | 6,497 |
| Capitalized stock-based compensation | **(1,949)** | (1,383) | (1,552) | **(3,332)** | (3,120) |
| Net stock-based compensation | **3,154** | 1,133 | 2,866 | **4,287** | 3,377 |
| Net stock-based compensation $ per boe | **2.85** | 0.93 | 1.78 | **1.84** | 0.98 |

Net stock-based compensation expense for the second quarter of 2016 increased $2.0 million as compared to the immediate preceding quarter and $0.3 million as compared to the second quarter of 2015, primarily a result of a $1.1 million expense related to SARs in the current period.

Net stock-based compensation expense for the six months ended June 30, 2016 increased $0.9 million as compared to the same period of 2015, primarily a result of the $1.0 million expense related to SARs in the current period.

The stock-based compensation recorded in the three and six months ended June 30, 2016 primarily relates to the stock appreciation rights ("SARs"), restricted share awards ("RSAs") and performance share awards ("PSAs") grants. Subject to terms and conditions of the plan, each RSA entitles the holder to an award value not limited to, but typically paid as to one-third on each of the first, second and third anniversaries of the date of grant. Each PSA entitles the holder to an award value to be typically paid on the third anniversary of the date of grant. For the purpose of calculating share-based compensation, the fair value of each award is determined at the grant date using the closing price of the common shares. An estimated forfeiture rate of 15% was used to value all awards granted for the period ended June 30, 2016. The weighted average fair value of awards granted for the six months ended June 30, 2016 is $1.93 per PSA and $2.18 per RSA. In the case of PSAs, the award value is adjusted for a payout multiplier which can range from 0.0 to 2.0 and is dependent on the performance of the Company relative to pre-defined corporate performance measures for a particular period.

The number of restricted and performance share awards outstanding are as follows:

| | Number of restricted share awards | Number of performance share awards |
|---|---|---|
| Balance at January 1, 2016 | 2,740,363 | 3,407,103 |
| Granted | 547,716 | 37,500 |
| Reinvested [1] | 82,970 | 100,007 |
| Exercised | (14,270) | — |
| **Balance at June 30, 2016** | **3,356,779** | **3,544,610** |

[1] Per the terms of the plan, cash dividends paid by the Company are reinvested to purchase incremental awards.

## DEPLETION AND DEPRECIATION

| | Three Months Ended | | | Six Months Ended | |
|---|---|---|---|---|---|
| ($000s except per boe) | **Jun 30, 2016** | Mar 31, 2016 | Jun 30, 2015 | **Jun 30, 2016** | Jun 30, 2015 |
| Depletion and depreciation expense | **$ 19,271** | $ 21,593 | $ 33,944 | **40,864** | 75,346 |
| $ per boe | **17.38** | 17.70 | 21.13 | **17.55** | 21.79 |

Depletion and depreciation are calculated based upon capital expenditures, production rates and proved plus probable reserves. Deducted from the Company's second quarter of 2016 depletion and depreciation calculation are costs associated with salvage values of $102.6 million. Future development costs for proved and probable reserves of $443.7 million have been included in the depletion calculation.

Depletion and depreciation expense during the second quarter of 2016 decreased as compared to the first quarter of 2016 and the same period of 2015 primarily due to the disposition of Surge's Sunset assets on March 31, 2016 and disposal of Surge's southeast Saskatchewan and southwest Manitoba properties that was completed in the second quarter of 2015, in addition to impairment expenses realized during the year ended December 31, 2015.

The depletion and depreciation calculation is based on daily production volumes of 12,182 boe per day for the second quarter of 2016.

## NET LOSS

| | Three Months Ended | | | Six Months Ended | |
|---|---|---|---|---|---|
| ($000s except per share) | **Jun 30, 2016** | Mar 31, 2016 | Jun 30, 2015 | **Jun 30, 2016** | Jun 30, 2015 |
| Net loss | **(8,084)** | (3,681) | (9,769) | **(11,765)** | (114,474) |
| Per share - basic ($) | **(0.04)** | (0.02) | (0.04) | **(0.05)** | (0.52) |
| Per share - diluted ($) | **(0.04)** | (0.02) | (0.04) | **(0.05)** | (0.52) |

Net loss and net loss per basic share for the second quarter of 2016 increased as compared to the first quarter of 2016 and second quarter of 2015. The cause for the variance is primarily due to the extent of realized and unrealized gains and losses on commodity contracts in each of the quarters.

Net loss and net loss per basic share for the first six months of 2016 has decreased as compared to the same period of 2015 primarily as a result of impairment recognition during the first six months of 2015.

## CAPITAL EXPENDITURES

### Capital Expenditure Summary

| ($000s) | Q1 2016 | Q2 2016 | **2016 YTD** | 2015 YTD | % Change |
|---|---|---|---|---|---|
| Land | 194 | 1,315 | **1,509** | 1,147 | 32 % |
| Seismic | 20 | — | **20** | 226 | (91)% |
| Drilling and completions | 6,269 | 11,293 | **17,562** | 21,044 | (17)% |
| Facilities, equipment and pipelines | 5,170 | 3,428 | **8,598** | 14,073 | (39)% |
| Other | 1,220 | 774 | **1,994** | 4,279 | (53)% |
| Total exploration and development | 12,873 | 16,810 | **29,683** | 40,769 | (27)% |
| Acquisitions - cash consideration | 2,037 | — | **2,037** | 4,574 | nm |
| Acquisitions - debt acquired | — | — | **—** | — | nm |
| Acquisitions - share based consideration | — | — | **—** | — | nm |
| Property dispositions | (43,178) | — | **(43,178)** | (465,524) | nm |
| Total acquisitions & dispositions | (41,141) | — | **(41,141)** | (460,950) | nm |
| Total capital expenditures | (28,268) | 16,810 | **(11,458)** | (420,181) | nm |

During the three and six months ended June 30, 2016, Surge invested a total of $16.8 million and $29.7 million, excluding acquisitions and dispositions.

During the second quarter of 2016, Surge invested $11.3 million to drill 8 gross (8 net) wells. This reflects an average of approximately $1.1 to $1.2 million per Shaunavon well and $3.5 million for the Valhalla well drilled during the second quarter of 2016. This compares favourably to the budgeted costs of $1.6 million per Shaunavon well and $3.6 million per Valhalla well.

In addition, the Company invested $3.4 million in facilities and pipelines, waterflood expansions and pilots, and $2.1 million in land and seismic acquisitions and other capital items.

## FACTORS THAT HAVE CAUSED VARIATIONS OVER THE QUARTERS

The fluctuations in Surge's revenue and net earnings from quarter to quarter are primarily caused by changes in production volumes, changes in realized commodity prices and the related impact on royalties, and realized and unrealized gains or losses on derivative instruments. The change in production from the third quarter of 2014 through the current quarter are due to Surge's successful drilling program, as well as corporate and asset acquisitions over that period combined with significant dispositions in the second quarter of 2015. Please refer to the Financial and Operating Results section and other sections of this MD&A for detailed discussions on variations during the comparative quarters and to Surge's previously issued interim and annual MD&A for changes in prior quarters.

### Share Capital and Option Activity

| | **Q2 2016** | Q1 2016 | Q4 2015 | Q3 2015 |
|---|---|---|---|---|
| Weighted common shares | **221,046,752** | 221,042,468 | 221,000,807 | 221,259,098 |
| Dilutive instruments (treasury method) | **—** | — | — | — |
| Weighted average diluted shares outstanding | **221,046,752** | 221,042,468 | 221,000,807 | 221,259,098 |

| | Q2 2015 | Q1 2015 | Q4 2014 | Q3 2014 |
|---|---|---|---|---|
| Weighted common shares | 220,287,256 | 220,059,794 | 219,834,286 | 217,689,253 |
| Dilutive instruments (treasury method) | — | — | — | 1,718,354 |
| Weighted average diluted shares outstanding | 220,287,256 | 220,059,794 | 219,834,286 | 219,407,607 |

On August 3, 2016, Surge had 221,047,158 common shares, 1,400,560 warrants, 2,000,000 SAR's, 3,553,765 PSAs, 3,365,449 RSAs, and 89,200 stock options outstanding.

### Quarterly Financial Information

| | **Q2 2016** | Q1 2016 | Q4 2015 | Q3 2015 |
|---|---|---|---|---|
| Oil, Natural gas & NGL sales | **40,943** | 29,146 | 40,942 | 45,779 |
| Net loss | **(8,084)** | (3,681) | (64,597) | (34,820) |
| Net loss per share ($): | | | | |
| Basic | **(0.04)** | (0.02) | (0.29) | (0.16) |
| Diluted | **(0.04)** | (0.02) | (0.29) | (0.16) |
| Funds from operations | **22,063** | 7,491 | 15,302 | 17,009 |
| Funds from operations per share ($): | | | | |
| Basic | **0.10** | 0.03 | 0.07 | 0.08 |
| Diluted | **0.10** | 0.03 | 0.07 | 0.08 |
| Average daily sales | | | | |
| Oil (bbls/d) | **8,958** | 9,821 | 10,297 | 10,635 |
| NGL (bbls/d) | **564** | 615 | 795 | 599 |
| Natural gas (mcf/d) | **15,959** | 17,829 | 18,570 | 13,731 |
| Barrels of oil equivalent (boe per day) (6:1) | **12,182** | 13,408 | 14,187 | 13,523 |
| Average sales price | | | | |
| Natural gas ($/mcf) | **1.41** | 1.36 | 1.86 | 2.03 |
| Oil ($/bbl) | **46.03** | 29.28 | 38.54 | 43.50 |
| NGL ($/bbl) | **26.64** | 13.75 | 17.08 | 11.67 |
| Barrels of oil equivalent ($/boe) | **36.94** | 23.89 | 31.37 | 36.80 |

### Quarterly Financial Information

| | Q2 2015 | Q1 2015 | Q4 2014 | Q3 2014 |
|---|---|---|---|---|
| Oil, Natural gas & NGL sales | 80,868 | 70,353 | 106,262 | 143,709 |
| Net earnings (loss) | (9,769) | (104,705) | (109,181) | 34,655 |
| Net earnings (loss) per share ($): | | | | |
| Basic | (0.04) | (0.48) | (0.50) | 0.16 |
| Diluted | (0.04) | (0.48) | (0.50) | 0.16 |
| Funds from operations | 35,490 | 51,072 | 54,670 | 71,298 |
| Funds from operations per share ($): | | | | |
| Basic | 0.16 | 0.23 | 0.25 | 0.33 |
| Diluted | 0.16 | 0.23 | 0.25 | 0.32 |
| Average daily sales | | | | |
| Oil (bbls/d) | 14,345 | 16,296 | 16,537 | 16,401 |
| NGL (bbls/d) | 520 | 875 | 686 | 779 |
| Natural gas (mcf/d) | 16,724 | 20,484 | 19,349 | 18,879 |
| Barrels of oil equivalent (boe per day) (6:1) | 17,652 | 20,585 | 20,448 | 20,327 |
| Average sales price | | | | |
| Natural gas ($/mcf) | 2.22 | 2.94 | 3.84 | 4.70 |
| Oil ($/bbl) | 58.74 | 42.96 | 64.01 | 87.61 |
| NGL ($/bbl) | 16.64 | 24.38 | 33.12 | 46.80 |
| Barrels of oil equivalent ($/boe) | 50.34 | 37.97 | 56.49 | 76.85 |

## LIQUIDITY AND CAPITAL RESOURCES

On June 30, 2016, Surge had drawn $131.7 million on its credit facility with total net debt of $134.6 million, a decrease in total net debt of seven percent as compared to the same date in 2015. At June 30, 2016, Surge had approximately $118 million of borrowing capacity in relation to the recently renewed $250 million credit facility, providing Surge financial flexibility through 2016.

Surge monitors its capital structure and makes adjustments according to market conditions in an effort to meet its objectives. Given the extreme volatility, significant downward pressure and uncertainty of world oil prices in the fourth quarter of 2014 and subsequent to December 31, 2014, the Company reduced drilling and capital spending late in the fourth quarter of 2014 and adopted a conservative capital spending program for 2015 and now into 2016, designed to protect the Company's financial position.

Surge anticipates that the future capital requirements will be funded through a combination of internal cash flow, divestitures, debt and/or equity financing. Furthermore, Surge’s flexible capital program and unused bank line further add to Surge’s ability to fund future capital requirements. There is no assurance that debt and equity financing will be available on terms acceptable to the Company to meet its capital requirements.

Additionally, Surge reduced the Company's dividend from $0.05 per share per month to $0.025 per share per month beginning with the January 2015 declared dividend as a further measure to protect the Company's financial position and further reduced the Company's dividend to $0.0125 per share per month beginning in November 2015 and $0.00625 per share per month beginning in April 2016. Surge's management and Board will continue to assess market conditions regularly until a sustainable recovery in world crude oil prices is realized.

The Company defines net debt as outstanding bank debt plus or minus working capital, however, excluding the fair value of financial contracts and other current obligations as follows.

**Net Debt**

| ($000s) | |
|---|---|
| Bank debt | (131,710) |
| Accounts receivable | 25,973 |
| Prepaid expenses and deposits | 3,582 |
| Accounts payable and accrued liabilities | (31,076) |
| Dividends payable | (1,382) |
| **Total** | **(134,613)** |

The Company has an extendible, revolving term credit facility at $250 million with a syndicate of Canadian banks bearing interest at bank rates. This is a decrease in the available credit facility of $150 million when compared to the first quarter of 2016. As a result of carrying less unutilized credit capability on the Company's bank line, Surge will be saving approximately $1.0 million per year in standby charges.

The facility is available on a revolving basis until May 29, 2017. On May 29, 2017, at the Company’s discretion, the facility is available on a non-revolving basis for a one-year period, at the end of which time the facility would be due and payable. Alternatively, the facilities may be extended for a further 364-day period at the request of the Company and subject to the approval of the syndicate. As the available lending limits of the facilities are based on the syndicate’s interpretation of the Company’s reserves and future commodity prices, there can be no assurance that the amount of the available facilities will not decrease at the next scheduled review. Interest rates vary depending on the ratio of net debt to cash flow. The facility had an effective interest rate of prime plus 1.50 percent as at June 30, 2016 (December 31, 2015 – prime plus 1.50 percent).

Surge’s facility is secured by a general assignment of book debts, debentures of $1.5 billion with a floating charge over all assets of the Company with a negative pledge and undertaking to provide fixed charges on the major producing petroleum and natural gas properties at the request of the bank.

## RELATED-PARTY AND OFF-BALANCE-SHEET TRANSACTIONS

Surge was not involved in any off-balance-sheet transactions or related party transactions during the three and six months ended June 30, 2016.

## FINANCIAL INSTRUMENTS

As a means of managing commodity price, interest rate, and foreign exchange volatility, the Company enters into various derivative financial instrument agreements and physical contracts. The fair value of forward contracts and swaps is determined by discounting the difference between the contracted prices and published forward price curves as at the statement of financial position date, using the remaining contracted oil and natural gas volumes and a risk-free interest rate (based on published government rates). The fair value of options and costless collars is based on option models that use published information with respect to volatility, prices and interest rates. Surge’s financial derivative contracts are classified as level two.

The following table summarizes the Company’s financial and physical derivatives as at June 30, 2016 by period and by product. Further detail on the individual hedges can be found in the Financial Statements.

### Commodity Contracts

#### WTI Oil Hedges

| Period | Volume Hedged (bbl/d) | Avg Floor Price (C$ per bbl) | Avg Ceiling Price (C $ per bbl) |
|---|---|---|---|
| Q3 2016 | 1,000 | $ 45.00 | $ 66.58 |
| Q3 2016 | 2,000 | $ 45.00 | - |
| Q4 2016 | 3,000 | $ 45.00 | $ 66.58 |
| Q1 2017 | 2,500 | $ 49.00 | $ 71.00 |
| Q2 2017 | 2,500 | $ 49.00 | $ 71.00 |
| Q3 2017 | 1,500 | $ 53.33 | $ 78.33 |
| Q4 2017 | 1,500 | $ 53.33 | $ 78.33 |

#### WTI-to-Edm Oil Differential Hedges

| Period | Volume Hedged (bbl/d) | Avg Price (Surge receives) (US$ per bbl) |
|---|---|---|
| Q3 2016 | 2,000 | $ 3.55 |
| Q4 2016 | 2,000 | $ 3.55 |

#### WCS Oil Differential Hedges

| Period | Volume Hedged (bbl/d) | Avg Price (Surge receives) (US$ per bbl) |
|---|---|---|
| Q3 2016 | 2,500 | $ 16.11 |
| Q4 2016 | 2,500 | $ 16.11 |
| Q1 2017 | 500 | $ 22.00 |
| Q2 2017 | 500 | $ 22.00 |
| Q3 2017 | 500 | $ 22.00 |
| Q4 2017 | 500 | $ 22.00 |

#### Chicago Gas Hedges

| Period | Volume Hedged (mcf/d) | Avg Swap Price (Surge receives) (C$ per mcf) |
|---|---|---|
| Q3 2016 | 10,000 | $ 3.50 |
| Q4 2016 | 10,000 | $ 3.50 |
| Q1 2017 | 10,000 | $ 3.63 |
| Q2 2017 | 10,000 | $ 3.63 |
| Q3 2017 | 10,000 | $ 3.63 |
| Oct 2017 | 10,000 | $ 3.63 |

## CONTROLS AND PROCEDURES

The Chief Executive Officer and Chief Financial Officer are responsible for designing internal controls over financial reporting (“ICFR”) or causing them to be designed under their supervision in order to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with IFRS. The Company's Chief Executive Officer and Chief Financial Officer have designed, or caused to be designed under their supervision, disclosure controls and procedures to provide reasonable assurance that: (i) material information relating to the Company is made known to the Company's Chief Executive Officer and Chief Financial Officer by others, particularly during the period in which the annual filings are being prepared; and (ii) information required to be disclosed by the Company in its annual filings, interim filings or other reports filed or submitted by it under securities legislation is recorded, processed, summarized and reported within the time period specified in securities legislation.

The Committee of Sponsoring Organizations of the Treadway Commission (“COSO”) 2013 framework provides the basis for management’s design of internal controls over financial reporting. Management and the Board work to mitigate the risk of a material misstatement in financial reporting; however, a control system, no matter how well conceived or operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met and it should not be expected that the disclosure and internal control procedures will prevent all errors or fraud.

There were no changes in the Company’s ICFR during the quarter ended June 30, 2016 that materially affected, or are reasonably likely to materially affect, the Company’s ICFR.

### Disclosure Controls

Disclosure controls and procedures have been designed to ensure that information to be disclosed by the Company is accumulated and communicated to management, as appropriate, to allow timely decisions regarding required disclosures.

The President and Chief Executive Officer and the Chief Financial Officer of Surge evaluated the design of the Company's disclosure controls and procedures ("DC&P"). Based on that evaluation, the officers concluded that Surge's DC&P were designed properly as at June 30, 2016.

### Internal Controls over Financial Reporting

Internal controls over financial reporting have been designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of the Company's financial statements for external purposes in accordance with IFRS.

Under the supervision of the President and Chief Executive Officer and the Chief Financial Officer, Surge conducted an evaluation of the design of the Company's ICFR as at June 30, 2016 based on the COSO framework. Based on this evaluation, the officers concluded that as of June 30, 2016, Surge's ICFR was properly designed.

## CRITICAL ACCOUNTING ESTIMATES

The preparation of financial statements in accordance with IFRS requires management to make certain judgments and estimates. Due to the timing of when activities occur compared to the reporting of those activities, management must estimate and accrue operating results and capital spending. Changes in these judgments and estimates could have a material impact on our financial results and financial condition.

### Reserves

The process of estimating reserves is critical to several accounting estimates. It requires significant judgments based on available geological, geophysical, engineering and economic data. These estimates may change substantially as data from ongoing development and production activities becomes available, and as economic conditions impacting oil and gas prices, operating costs and royalty burdens change. Reserve estimates impact net income through depletion, the determination of decommissioning liabilities and the application of impairment tests.

Revisions or changes in reserve estimates can have either a positive or a negative impact on net income.

### Forecasted Commodity Prices

Management's estimates of future crude oil and natural gas prices are critical as these prices are used to determine the carrying amount of PP&E, assess impairment and determine the change in fair value of financial contracts. Management's estimates of prices are based on the price forecast from our reserve engineers and the current forward market.

### Business Combinations

Management makes various assumptions in determining the fair values of any acquired company's assets and liabilities in a business combination. The most significant assumptions and judgments made relate to the estimation of the fair value of the oil and gas properties. To determine the fair value of these properties, we estimate (a) oil and gas reserves in accordance with National Instrument 51-101 – Standards of Disclosure for Oil and Gas Activities (''NI 51-101'') and (b) future prices of oil and gas.

### Decommissioning Liability

Management calculates the decommissioning liability based on estimated costs to abandon and reclaim its net ownership interest in all wells and facilities and the estimated timing of the costs to be incurred in future periods. The fair value estimate is capitalized to PP&E as part of the cost of the related asset and amortized over its useful life. There are uncertainties related to decommissioning liabilities and the impact on the financial statements could be material as the eventual timing and costs for the obligations could differ from our estimates. Factors that could cause our estimates to differ include any changes to laws or regulations, reserve estimates, costs and technology.

### Derivative Financial Instruments

We utilize derivative financial instruments to manage our exposure to market risks relating to commodity prices, foreign currency exchange rates and interest rates. Fair values of derivative contracts fluctuate depending on the underlying estimate of future commodity prices, foreign currency exchange rates, interest rates and counterparty credit risk.

### Stock-based Compensation

Management makes various assumptions in determining the value of stock based compensation. This includes estimating the forfeiture rate, the expected volatility of the underlying security, interest rates and expected life.

### Deferred Income Taxes

Management makes various assumptions in determining the value of stock deferred income tax provision, including (but not limited to) future tax rates, accessibility of tax pools and future cash flows.

## FUTURE ACCOUNTING POLICY CHANGES

The following pronouncements from the IASB will become effective for financial reporting periods beginning on or after January 1, 2016 and have not yet been adopted by the Corporation. All of these new or revised standards permit early adoption with transitional arrangements depending upon the date of initial application:

- IFRS 15 "Revenue From Contracts with Customers" replaces IAS 11 "Construction Contracts" and IAS 18 "Revenue" and establishes a single revenue recognition framework that applies to contracts with customers, effective date of January 1, 2018.
- IFRS 9 "Financial Instruments" replaces IAS 39 "Financial Instruments: Recognition and Measurement" and addresses the classification and measurement of financial assets, effective date of January 1, 2018.
- IFRS 16 "Leases" replaces IAS 17 "Leases" and requires entities to recognize lease assets and lease obligations on the balance sheet, essentially removing the classification of leases as either operating leases or finance leases and treating all leases as finance leases, effective January 1, 2019.

The Company has not completed its evaluation of the effect of adopting these standards on its financial statements.

## RISK FACTORS

Additional risk factors can be found under "Risk Factors" in the Company's Annual Information Form for the year ended December 31, 2015, which can be found on www.sedar.com. Many risks are discussed below and in the Annual Information Form, but these risk factors should not be construed as exhaustive. There are numerous factors, both known and unknown, that could cause actual results or events to differ materially from forecast results.

Oil and natural gas operations involve many risks that even a combination of experience, knowledge and careful evaluation may not be able to overcome. The long-term commercial success of Surge depends on its ability to find, acquire, develop, and commercially produce oil and natural gas reserves. Without the continual addition of new reserves, any existing reserves Surge may have at any particular time and the production therefrom will decline over time as such existing reserves are exploited. A future increase in Surge's reserves will depend not only on the Company's ability to explore and develop any properties it may have from time to time, but also on its ability to select and acquire suitable producing properties or prospects. No assurance can be given that further commercial quantities of oil and natural gas will be discovered or acquired by Surge.

Surge's principal risks include finding and developing economic hydrocarbon reserves efficiently and being able to fund the capital program. The Company's need for capital is both short-term and long-term in nature. Short-term working capital will be required to finance accounts receivable, drilling deposits and other similar short-term assets, while the acquisition and development of oil and natural gas properties requires large amounts of long-term capital. Surge anticipates that future capital requirements will be funded through a combination of internal funds from operations, debt and/or equity financing. There is no assurance that debt and equity financing will be available on terms acceptable to the Company to meet its capital requirements. If any components of the Company's business plan are missing, the Company may not be able to execute the entire business plan.

All phases of the oil and natural gas business present environmental risks and hazards and are subject to environmental regulation pursuant to a variety of federal, provincial, and local laws and regulations. Environmental legislation provides for, among other things, restrictions and prohibitions on spills, releases or emissions of various substances produced in association with oil and natural gas operations. The legislation also requires that wells and facility sites be operated, maintained, abandoned and reclaimed to the satisfaction of applicable regulatory authorities. Compliance with such legislation can require significant expenditures and a breach may result in the imposition of fines and penalties, some of which may be material. Environmental legislation is evolving in a manner expected to result in stricter standards and enforcement, larger fines and liability and potentially increased capital expenditures and operating costs. The discharge of oil, natural gas or other pollutants into the air, soil, or water may give rise to liabilities to governments and third parties and may require Surge's operating entities to incur costs to remedy such discharge. Although Surge believes that it is in material compliance with current applicable environmental regulations, no assurance can be given that environment laws will not result in a curtailment of production or a material increase in the costs of production, development or exploration activities or otherwise adversely affect Surge's financial condition, results of operations or prospects.

Surge's involvement in the exploration for and development of oil and natural gas properties may result in Surge becoming subject to liability for pollution, blowouts, property damage, personal injury or other hazards. Although, prior to drilling, Surge will obtain insurance in accordance with industry standards to address certain of these risks, such insurance has limitations on liability that may not be sufficient to cover the full extent of such liability. In addition, such risks may not, in all circumstances, be insurable or, in certain circumstances, Surge may elect not to obtain insurance to deal with specific risks due to the high premiums associated with such insurance or other reasons. The payment of such uninsured liabilities would reduce the funds available to Surge. The occurrence of a significant event that was not fully insured against, or the insolvency of the insurer of such event, could have a material adverse effect on Surge's financial position, results of operations or prospects and will reduce income otherwise used to fund operations.

The Company's financial performance and condition are substantially dependent on the prevailing prices of oil and natural gas which are unstable and subject to fluctuation. Fluctuations in oil or natural gas prices could have an adverse effect on the Company's operations and financial condition and the value and amount of its reserves. Prices for crude oil fluctuate in response to global supply of and demand for oil, market performance and uncertainty and a variety of other factors which are outside the control of the Company including, but not limited, to the world economy and the Organization of the Petroleum Exporting Countries' ability to adjust supply to world demand, government regulation, political stability and the availability of alternative fuel sources. Natural gas prices are influenced primarily by factors within North America, including North American supply and demand, economic performance, weather conditions and availability and pricing of alternative fuel sources.

Decreases in oil and natural gas prices typically result in a reduction of the Company's net production revenue and may change the economics of producing from some wells, which could result in a reduction in the volume of the Company's reserves. Any further substantial declines in the prices of crude oil or natural gas could also result in delay or cancellation of existing or future drilling, development or construction programs or the curtailment of production. All of these factors could result in a material decrease in the Company's net production revenue, cash flows and profitability causing a reduction in its oil and gas acquisition and development activities. In addition, bank borrowings available to the Company will in part be determined by the Company's borrowing base. A sustained material decline in prices from historical average prices could further reduce such borrowing base, therefore reducing the bank credit available and could require that a portion of its bank debt be repaid.

The Company utilizes financial derivatives contracts to manage market risk. All such transactions are conducted in accordance with the risk management policy that has been approved by the Board of Directors.

## BOE PRESENTATION

All amounts are expressed in Canadian dollars unless otherwise noted. Oil, natural gas and natural gas liquids reserves and volumes are converted to a common unit of measure, referred to as a barrel of oil equivalent (boe), on the basis of 6,000 cubic feet of natural gas being equal to one barrel of oil. This conversion ratio is based on an energy equivalency conversion method, primarily applicable at the burner tip and does not necessarily represent a value equivalency at the wellhead. It should be noted that the use of boe might be misleading, particularly if used in isolation.

## FORWARD-LOOKING STATEMENTS

This MD&A contains forward-looking statements. The use of any of the words “anticipate”, “continue”, “estimate”, “expect”, “may”, “will”, “project”, “should”, “believe” and similar expressions are intended to identify forward-looking statements. 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.

More particularly, this MD&A contains statements concerning: (i) forecast commodity prices, inflation rates and currency prices; (ii) operating, transportation and interest expense trends (iii) the availability of Surge’s bank line to fund Surge’s future capital requirements; (iv) Surge’s financial flexibility; (v) the expected sources of funding of future capital expenditures; (vi) Surge’s anticipated standby charge savings; (vii) expected forfeiture rates of RSAs and PSAs granted under the Company’s Stock Incentive Plan; (viii) expectations as to the payout multiplier for PSAs granted under the Company’s Stock Incentive Plan; (xi) expectations with respect to its underlying decommissioning liabilities; (x) expectations with respect to environmental legislation; (xi) expectations on corporate royalty rates applicable to the Company; (xii) expectations with respect to transportation expense; and (xiii) expectations with respect to the Company’s ability to operate and succeed in the current commodity price environment.

The forward-looking statements are based on certain key expectations and assumptions made by Surge, including expectations and assumptions concerning the performance of existing wells and success obtained in drilling new wells, anticipated expenses, cash flow and capital expenditures, the application of regulatory and royalty regimes, prevailing commodity prices and economic conditions, development and completion activities and the costs relating thereto, the performance of new wells, the successful implementation of waterflood programs, the availability of and performance of facilities and pipelines, the geological characteristics of Surge’s properties, the successful application of drilling, completion and seismic technology, the determination of decommissioning liabilities, prevailing weather conditions, exchange rates, licensing requirements, the impact of completed facilities on operating costs and the availability, costs of capital, labour and services, and the creditworthiness of industry partners.

Although Surge believes that the expectations and assumptions on which the forward-looking statements are based are reasonable, undue reliance should not be placed on the forward-looking statements because Surge can give no assurance that they will prove to be correct. Since forward-looking statements address future events and conditions, by their very nature they involve inherent risks and uncertainties. Actual results could differ materially from those currently anticipated due to a number of factors and risks. These include, but are not limited to, risks associated with the oil and gas industry in general (e.g., operational risks in development, exploration and production; delays or changes in plans with respect to exploration or development projects or capital expenditures; the uncertainty of reserve estimates; the uncertainty of estimates and projections relating to production, costs and expenses, and health, safety and environmental risks), commodity price and exchange rate fluctuations and constraint in the availability of services, adverse weather or break-up conditions, uncertainties resulting from potential delays or changes in plans with respect to exploration or development projects or capital expenditures or failure to obtain the continued support of the lenders under Surge’s bank line. Certain of these risks are set out in more detail in this MD&A under the heading ‘Risk Factors’ and in Surge’s Annual Information Form dated March 16, 2016 which has been filed on SEDAR and can be accessed at www.sedar.com.

The forward-looking statements contained in this MD&A are made as of the date hereof and Surge undertakes no obligation to update publicly or revise any forward-looking statements or information, whether as a result of new information, future events or otherwise, unless so required by applicable securities laws.