

THIRD QUARTER REPORT

For the three months ended September 30, 2006 and
From incorporation on April 25, 2006 to September 30, 2006

CORPORATE HIGHLIGHTS

	Three Months Ended September 30, 2006
Petroleum and natural gas revenues (\$)	153,333
Funds from operations Per basic and diluted shares (\$)	(0.06)
Working capital (\$)	9,684,557
Capital expenditures (\$)	2,572,472
Weighted number of shares outstanding	
Basic	5,211,216
Diluted	5,875,278
Shares outstanding (voting and non-voting) - ytd	9,935,636
Options	
Granted (\$)	469,000
Price (\$)	4.02

Trafalgar Energy Ltd.

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LETTER TO SHAREHOLDERS

Trafalgar Energy Ltd. is pleased to present its results for the 3rd quarter ended September 30, 2006 and for the period from incorporation on April 25, 2006 to September 30, 2006.

Many milestones have been reached by the Company since incorporation in April 2006 including:

- Approval and closing of the Grouard and Cypress property acquisition from Daylight Energy Trust.
- Closing of a \$15.0 million private placement of voting and non-voting common shares.
- Approval, listing and trading in Trafalgar shares on the Toronto Stock Exchange.
- Establishment of an \$8.0 million revolving credit facility.
- Development of two high potential projects at Mackay and Cherpeta in North Central Alberta.
- Establishment of a high quality management team, technical team and board of directors.

On September 19, 2006, Trafalgar received shareholder approval for a plan of arrangement transaction with Daylight Energy Trust ("Daylight") and Sequoia Oil & Gas Trust ("Sequoia"). As a result of this transaction, Trafalgar acquired 1.2 million boe of proved plus probable reserves, approximately 625 boe per day of production (17% oil and 83% natural gas), approximately 45,000 net acres of undeveloped land and significant operated infrastructure.

Production on the Grouard and Cypress assets acquired from Daylight averaged 625 boe per day for the last nine days of September which is represented by 108 boe per day of oil and ngl's and 3,102 mmcf per day of natural gas. The properties provide Trafalgar with a solid production base and tangible upside comprised of natural gas, light oil and heavy oil drilling opportunities. Preparations for an eight to 12 well winter drilling program have been made with equipment and resources to execute the program. We will spud our first well in mid November of this year.

The Grouard and Cypress properties were purchased through the issuance of 5.2 million common shares to the former Daylight and Sequoia unitholders with a deemed value of \$4.02 per share for a total consideration of \$21.1 million. The Daylight transaction generated impressive metrics with proved plus probable reserves purchased for approximately \$17.50 per boe and production purchased for approximately \$33,800 per boe per day.

In addition to the Daylight acquisition, Trafalgar has been successful in acquiring 23,000 net acres of prospective land in its key exploration and development areas in North Central Alberta. Trafalgar now has over 68,000 net undeveloped acres of land on which to drill.

Through the Daylight acquisition and independent data purchases, Trafalgar has acquired a significant seismic database in North Central Alberta totaling over 8,800 km of 2D data and 175 square km of 3D data. To date several leads and prospects have been identified, some of which we will drill this winter. Other prospects have been placed in inventory pending success of our winter drilling program.

On June 5th of this year, the Company successfully completed a \$15.0 million private placement of voting and non-voting common shares to private investors, management, staff and directors. The Company is on solid financial footing with a cash balance as at September 30, 2006 of \$12.1 million, an un-drawn credit facility of \$8.0 million and approximately of \$45.0 million of tax pools.

On September 26, 2006, Trafalgar's common shares and arrangement warrants began trading on the Toronto Stock Exchange under the symbols TFL and TFL.WT. Since September 26, 2006, approximately 3.0 million common shares out of a total of 8.3 million common shares have traded in a range of \$3.27 to \$4.60 per share. Out of the total 1.3 million arrangement warrants, 36,052 were exercised resulting in proceeds of \$144,945 net to Trafalgar. The remaining arrangement warrants expired on October 23, 2006.

Going forward, Trafalgar's strategy is to develop quality assets through the drill bit and target 500+ boe per day producing properties. We will maintain 100% working interests and operator status wherever possible as we believe this will contribute to low finding and development costs and a high degree of capital efficiency.

Our geographic focus will be on North Central Alberta targeting shallow to mid depth natural gas and deeper higher impact natural gas and oil plays. We believe North Central Alberta to be relatively underexploited with abundant available crown land for lease. As a result, Trafalgar will not be reliant on third party transactions for drilling prospects or strategic land access. We are excited about the potential for the Company and look forward to reporting the results from our winter drilling program.

Finally, I would like to take this opportunity to thank our employees, board of directors and shareholders for their collective support, insight and guidance in the startup of Trafalgar.

Sincerely

Robert Wollmann
President and CEO

MANAGEMENT'S DISCUSSION AND ANALYSIS

The following management's discussion and analysis ("MD&A") reviews Trafalgar Energy Ltd. ("Trafalgar" or the "Company") activities and results of operations for the three months ended September 30, 2006 and from incorporation on April 25, 2006 to September 30, 2006. The MD&A should be read in conjunction with the unaudited financial statements of Trafalgar from incorporation on April 25, 2006 to June 30, 2006. The accompanying unaudited interim financial statements of Trafalgar have been prepared by management and approved by the Company's Audit Committee and Board of Directors. These interim financial statements have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP") and have been reviewed by the Company's external auditors. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and the disclosure of contingent assets and liabilities, at the date of the financial statements, and the reported amounts of revenues and expenses during the period. Actual results could differ from these estimates. This MD&A was reviewed and approved by the Company's Board of Directors on November 13, 2006.

NON-GAAP FINANCIAL MEASURES

Trafalgar evaluates performance based on net income and funds from operations. Funds from operations and funds from operations per share are not measurements based on GAAP, but are financial terms commonly used in the oil and gas industry. The Company's funds from operations is detailed on the Statement of Cash Flows and may not be comparable to other companies. Trafalgar calculates funds from operations per share using the same method and shares outstanding which are used in the determination of net income (loss) per share. The Company considers it a key measure as it demonstrates the ability of the Company to generate the funds necessary to finance future capital investments.

Trafalgar also uses "operating netbacks" as a key performance indicator. Operating netbacks do not have a standardized meaning prescribed by Canadian GAAP and therefore may not be comparable with the calculation of similar measures by other companies. Operating netbacks are determined by

deducting royalties, operating expenses, processing fees and transportation from petroleum and natural gas sales revenue.

Funds from operations and operating netbacks are not intended to represent operating profits, nor should they be viewed as an alternative to cash flow provided by operating activities, net income or other measures of financial performance calculated in accordance with GAAP.

In conformity with National Instrument 51-101, Standards for Disclosure of Oil and Gas Activities (“NI 51-101”), natural gas volumes have been converted to barrels of oil equivalent (“boe”) using a conversion rate of six thousand cubic feet of natural gas to one barrel of oil. This ratio is based on an energy equivalency conversion method primarily applicable at the burner tip and does not represent a value equivalency at the wellhead. Readers are cautioned that the term “boe” may be misleading, particularly if used in isolation.

SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

This discussion and analysis contains forward-looking statements related to future events or future performance. Certain statements regarding Trafalgar include management’s assessments of future plans and operations, may constitute forward-looking statements under applicable securities laws and necessarily involve known and unknown risks and uncertainties, most of which are beyond Trafalgar’s control. These risks may cause actual financial and operating results, performance, levels of activity and achievements to differ materially from those expressed in, or implied by, such forward-looking statements.

Such factors include, but are not limited to: the impact of general economic conditions in Canada and the United States; industry conditions including changes in laws and regulations including adoption of new environmental laws and regulations, and changes in how they are interpreted and enforced; competition from other producers, the lack of availability of drilling rigs and other field services, the lack of availability of qualified personnel; fluctuations in commodity prices, the results of exploration and development drilling related activities; imprecision in reserve estimates; the production and growth potential of Trafalgar’s various assets; fluctuations in foreign exchange or interest rates; the ability to access sufficient capital from internal and external sources; and obtaining required approvals of regulatory authorities.

Accordingly, Trafalgar gives no assurance nor makes any representations or warranty that the expectations conveyed by the forward-looking statements will prove to be correct and actual results may differ materially from those anticipated in the forward-looking statements. Readers should not place undue reliance on any such forward-looking statements, which speak only as of the date they were made. Trafalgar undertakes no obligation to publicly update or revise any forward-looking statements.

Additional information regarding Trafalgar is available under the Company’s profile on SEDAR at www.sedar.com or on the Trafalgar Energy Ltd. website at www.trafalgarenergy.ca

RESULTS OF OPERATIONS

Production:

Production for the 9 days from September 21, 2006 to September 30, 2006 averaged 625 boe per day comprised of the following:

Production	
Oil and NGL's (bbls/day)	108
Natural Gas (mcf/day)	3,102
Total (boe/d)	625
% Natural Gas	83

Trafalgar's gas and oil production is located in two primary areas: Grouard and Cypress. Grouard is located near High Prairie, Alberta and produces light oil from the Gilwood formation, heavy oil from the Bluesky zone and natural gas from several Cretaceous horizons. Trafalgar owns and operates most of the production from this area. Trafalgar also owns and operates a gas plant, two oil batteries and approximately 113 kms of pipeline.

Cypress is located approximately 145 kms northwest of Fort St. John, B.C. Production in this area is primarily natural gas from the Baldonnel, Halfway and Debolt formations. At Cypress, Trafalgar also has operatorship of a compressor station and a significant gas gathering system.

Trafalgar will allocate most of its resources to developing these operating areas. This includes executing on a drilling program that has currently identified 12 drilling locations ranging from low risk development wells to higher impact exploration wells.

Revenue:

Trafalgar acquired its first production from Daylight on September 21, 2006. Oil and natural gas revenue recorded for the period ended September 30, 2006 is a management estimate using a gas price of \$4.54 per mcf and an oil price of \$60 per bbl.

Royalties:

Total royalties for the period ended September 30, 2006 were estimated by management to be \$31,500 or \$5.60 per boe, representing 17% of revenue. All production from wells drilled by Daylight were "over the limit" and therefore not eligible for the Alberta Royalty Tax Credit (ARTC).

Interest and Other Income:

Interest and other income of \$164,998 for the period from incorporation on April 25, 2006 to September 30, 2006 is interest on Trafalgar's cash balances over the period at an interest rate of approximately 3.95%. Interest income is expected to reduce in the fourth quarter of 2006 and fiscal 2007 as cash resources will be utilized to fund ongoing exploration and development activities.

Operating Expenses:

Operating expenses for the period ended September 30, 2006 were estimated by management to be \$67,500 or \$12.00 per boe. Trafalgar anticipates average production expenses of approximately \$10.00 per boe in 2007 as field operations are streamlined and production volumes are increased.

General and Administrative Expenses:

General and administrative expenses for the period from incorporation on April 25, 2006 to September 30, 2006 were \$550,036 and \$447,724 for the three months ended September 30, 2006. As the Company only recorded nine days of production for the period, general and administrative expenses per boe are high.

Management expects average administrative expenses per boe for the fourth quarter of 2006 and for fiscal 2007 to decline as volume increases begin to offset general and administrative costs.

Stock-based Compensation:

During the period, the Company expensed \$3,594,834 in non-cash stock based compensation. \$3,500,000 of the expense relates to the intrinsic value of 5.2 million flow-through shares of a predecessor company purchased by management and directors in June 2006. The intrinsic value was determined to be the difference between the fair market value of the shares and the consideration received. The Company has also recorded \$94,834 of stock based compensation for all stock options granted.

Interest Expense:

Interest expenses for the period from incorporation on April 25, 2006 to September 30, 2006 were \$58,589 and \$51,456 for the three months ended September, 30, 2006. The majority of this expense, \$34,240, relates to interest on approximately \$3.5 million of flow through share tax pool obligations and \$23,836 of interest on Trafalgar's outstanding \$1.5 million convertible debentures at 5% per annum

Depletion and Depreciation:

The provision for depletion, depreciation and accretion for the period ended September 30, 2006 was \$156,555. Depletion and depreciation are calculated based upon capital, production rates and reserves. Trafalgar will estimate depletion on a quarterly basis throughout the year using independent reserve and land reports when available. Trafalgar excludes undeveloped land, seismic and salvage value but includes future development costs in the capital base used in this calculation.

The petroleum and natural gas properties were subject to a ceiling test as at September 30, 2006. No write-down was required as a result of this calculation.

Asset Retirement Obligations:

Trafalgar's asset retirement obligations are based on the Company's net ownership in wells and facilities. Management estimates the cost to abandon and reclaim the wells and facilities and the estimated time period during which these costs will be incurred in the future. Management estimates the total undiscounted amount of future cash flows required to abandon and reclaim wells and facilities as at September 30, 2006 to be approximately \$4.1 million, to be incurred over the next 15 years.

Accretion:

Trafalgar's producing oil and gas properties were acquired on September 21, 2006, as a result, there is no accretion expense charged for the period.

Income Taxes:

Following the plan of arrangement with Daylight and Sequoia, Trafalgar has approximately \$46.0 million of tax pools available to be applied against future income for tax purposes. These pools include approximately \$18.6 million of non-capital losses expiring at various dates to 2014, approximately \$5.3 million of scientific research and experimental development claims, approximately \$1.4 million of unclaimed financing fees and CCA claims and approximately \$17.8 million of Canadian Oil and Gas Property Expense. Based on these available pools, Trafalgar does not expect to pay current income taxes in 2006. Taxes payable beyond 2006 will become a function of commodity prices, production volumes and capital expenditures.

Net Loss:

Net loss for the period of incorporation on April 25, 2006 to September 30, 2006 was \$4,109,183 or \$2.53 per basic and diluted share. The net loss for the period was significantly impacted by a non-cash stock based compensation expense of \$3,594,834 charged against earnings for the period. Net loss for the three month period ended September 30, 2006 was \$539,586 or \$0.10 per basic and diluted share. Trafalgar anticipates that production volume increases will contribute to positive earnings growth in future periods.

Capital Expenditures:

	Three months ended September 30, 2006	From incorporation on April 25, 2006 to September 30, 2006
Land	1,307,136	1,329,702
Seismic	772,943	897,723
Drilling and Completion	152,018	152,018
Equipment Facilities and Pipelines	316,730	449,776
Other Assets	23,645	23,645
Total Exploration and Development Expenditures	<u>2,572,472</u>	<u>2,852,864</u>
Acquisitions	<u>20,776,624</u>	<u>20,892,310</u>
Total Capital Expenditures	<u><u>23,349,096</u></u>	<u><u>23,745,174</u></u>

The \$20.8 million of acquisition value relates to the petroleum and natural gas assets acquired from the Daylight and Sequoia arrangement (Note 2).

Trafalgar is budgeted to spend approximately \$7.2 million in the 4th quarter of 2006 including two shallow gas wells, a water flood and a well optimization program at Grouard plus additional land and seismic purchases. For 2007, Trafalgar is budgeted to spend approximately \$10.8 million including two shallow gas wells at Grouard, two shallow gas wells and two re-completions at Cherpeta and up to three additional wells on Trafalgar's other prospective lands in north central Alberta.

LIQUIDITY AND CAPITAL RESOURCES

As at September 30, 2006, Trafalgar had a positive working capital surplus of \$9.7 million. In addition, on September 18, 2006, the Company signed an agreement with a major Canadian bank to establish an \$8.0 million revolving term credit facility for general corporate purposes including capital expenditures. The credit facility revolves for a period of 364 days from closing followed by a one year term out period. The revolving period may be extended annually at the option of the lender. Rates of interest on the credit facility vary depending on Trafalgar's debt to cash flow ratio and range from zero to 125 basis points over prime. The credit facility will be secured by a floating charge debenture over all of Trafalgar's assets and a general security agreement.

OFF BALANCE SHEET ARRANGEMENTS AND CONTRACTUAL OBLIGATIONS

Trafalgar has various contractual obligations and commitments arising in the normal course of operations and financing activities. These obligations and commitments have been considered when assessing the cash requirements in the above discussion of future liquidity.

The Company's bank credit facilities are subject to periodic review. Trafalgar does not expect any material changes to the bank credit facility resulting from these reviews.

Trafalgar does not have any arrangements or obligations that are not reflected or disclosed in the consolidated financial statements.

RELATED PARTY TRANSACTIONS

The Company's related party transactions are disclosed in Note 13 to the consolidated financial statements.

DISCLOSURE CONTROLS AND PROCEDURES

Disclosure controls and procedures have been designed to ensure that information required to be disclosed by Trafalgar is accumulated and communicated to the Company's management as appropriate to allow timely decisions regarding required disclosure. The Company's Chief Executive Officer and Chief Financial Officer have concluded, based on their evaluation as at the end of the period covered by the interim filings, that the Company's disclosure controls and procedures are effective to provide reasonable assurance that material information related to the issuer, including its consolidated subsidiaries, is made known to them by others within those entities. It should be noted that while the Company's Chief Executive Officer and Chief Financial Officer believe that the Company's disclosure controls and procedures provide a reasonable level of assurance that they are effective, they do not expect that the disclosure controls and procedures or internal control over financial reporting will prevent all errors or fraud. 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.

TRAFALGAR ENERGY LTD.
BALANCE SHEET
September 30, 2006
(unaudited)

	\$
ASSETS	
Current	
Cash and cash equivalents (Note 4)	12,112,399
Accounts receivable	340,558
Prepaid expenses and deposits	352,680
	12,805,637
Petroleum and natural gas assets (Note 5)	24,917,001
	37,722,638
 LIABILITIES AND SHAREHOLDER'S EQUITY	
Current	
Accounts payable and accrued liabilities	1,655,964
Liability component of convertible debentures (Note 7)	1,465,116
	3,121,080
Asset retirement obligation (Note 8)	1,328,382
	4,449,462
Commitments (Note 12)	
 Shareholders' equity	
Equity component of convertible debentures (Note 7)	34,884
Share capital (Note 9)	34,902,060
Warrants	242,261
Contributed surplus (Note 9)	94,834
Deficit	(2,000,863)
	33,273,176
	37,722,638

see accompanying notes to the financial statements

TRAFALGAR ENERGY LTD.
STATEMENT OF OPERATIONS AND DEFICIT
(unaudited)

	Three months ended September 30, 2006 \$	From incorporation on April 25, 2006 to September 30, 2006 \$
Revenue		
Oil and natural gas revenue, net of royalties	153,333	153,333
Interest and other income	125,150	164,998
	278,483	318,331
Expenses		
Operating	67,500	67,500
General and administrative	447,724	550,036
Interest expense	51,456	58,589
Stock based compensation (Note 9)	94,834	3,594,834
Depletion and depreciation (Note 5)	156,555	156,555
Accretion expense (Note 8)	-	-
	818,069	4,427,514
Net loss	(539,586)	(4,109,183)
Deficit, beginning of period	(1,461,277)	-
Adjustment relating to business combination (Note 1)	-	2,108,320
	(2,000,863)	(2,000,863)
Net loss per share (Note 9)		
Basic and diluted	(0.10)	(1.10)
Weighted average number of shares outstanding-post consolidation (Note 9)		
Basic	5,211,216	3,748,140
Diluted	5,875,278	4,152,721

see accompanying notes to the financial statements

TRAFALGAR ENERGY LTD.
STATEMENT OF CASH FLOWS
(unaudited)

	Three months ended September 30, 2006 \$	From incorporation on April 25, 2006 to September 30, 2006 \$
Operating activities		
Net loss for the period	(539,586)	(4,109,183)
Add items not involving cash		
Depletion and depreciation	156,555	156,555
Stock based compensation (Note 9)	94,834	3,594,834
	(288,197)	(357,794)
Change in non-cash working capital items related to operating activities (Note 11)	(669,811)	(303,058)
	(958,008)	(660,852)
Financing activities		
Cash received upon business combination (Note 1)	-	276,916
Intercompany loan payment	-	(146,357)
Shareholder loan repayment	-	(170,000)
Issuance of shares	-	15,054,664
Share issue costs	(686,967)	(686,967)
	(686,967)	14,328,256
Investing activities		
Acquisition of property and equipment	(2,572,472)	(2,852,864)
Deferred charges	-	(214,000)
Change in non-cash working capital items related to investing activities (Note 11)	1,297,859	1,511,859
	(1,274,613)	(1,555,005)
Increase in cash and cash equivalents	(2,919,588)	12,112,399
Cash and cash equivalents, beginning of period	15,031,987	-
Cash and cash equivalents, end of period	12,112,399	12,112,399

see accompanying notes to the financial statements

TRAFALGAR ENERGY LTD.
NOTES TO THE FINANCIAL STATEMENTS
For the three months ended September 30, 2006 and the period from incorporation on
April 25, 2006 to September 30, 2006
(unaudited)

1. NATURE OF BUSINESS AND BUSINESS COMBINATION

1238364 Alberta Ltd. ("1238364") was incorporated April 25, 2006, in the province of Alberta, as a private oil and gas business. Pursuant to an amalgamation agreement dated June 6, 2006, 1238364, 1211413 Alberta Ltd. ("1211413") and Triant Technologies Inc. ("Triant") amalgamated resulting in the creation of Trafalgar Energy Ltd. ("Trafalgar" or the "Company"). This transaction is accounted for as the acquisition of 1211413 and Triant by 1238364, which was renamed Trafalgar upon amalgamation. The amalgamation did not constitute a business combination for accounting purposes. These financial statements of Trafalgar represent the continuation of 1238364 and the comparatives presented are those of 1238364.

Prior to incorporation, the Company had no operations. Accordingly, comparative statements of operations and deficit and cash flows have not been provided.

Pursuant to the amalgamation agreement described above, the shareholders of the common shares of 1211413 received one common share of Trafalgar for every share owned. The common shareholders of Triant received one common share of Trafalgar for every share owned. The common shareholders of 1238364, voting and non-voting, received one voting common share and one non-voting common share of Trafalgar for every share owned. Trafalgar also assumed the covenants and obligations of the \$1.5 million in convertible debentures from Triant which are convertible into 500,000 non-voting common shares of Trafalgar at the rate of \$3 per share (see Note 7). The following summarizes the value of the assets and liabilities assumed as a result of the acquisitions:

1211413 Alberta Ltd.:

	\$
Cash and cash equivalents	26,916
Accounts receivable	22,502
Prepaid expenses	27,573
Property and equipment	115,686
Intercompany payable	(146,357)
Due to shareholders	(170,000)
	(123,680)

Consideration received:
three (3) common shares of Trafalgar

Triant Technologies Inc.:

	\$
Cash and cash equivalents	250,000
Accounts payable	(18,000)
Liability component of convertible debentures	(1,465,116)
Equity component of convertible debentures	(34,884)
	<u>(1,268,000)</u>

Consideration received:
250,000 common shares of Trafalgar

As the acquisitions do not constitute business combinations, the accumulated deficit, share capital and contributed surplus of the acquired companies are allocated to the contributed surplus of the acquirer with the remainder to the deficit. This resulted in the accumulated deficit (\$40,030,571), share capital (\$35,489,398) and contributed surplus (\$3,149,493) of the acquired companies being allocated to the contributed surplus of 1238364 in the amount of \$3,500,000 and \$2,108,320 allocated to the deficit of 1238364.

Trafalgar is engaged in oil and gas exploration, development and production in Western Canada.

2. PLAN OF ARRANGEMENT

On July 17, 2006, Trafalgar entered into a letter agreement ("Agreement") between Daylight Energy Trust ("Daylight"), Daylight Energy Ltd. ("DEL"), Sequoia Oil & Gas Trust ("Sequoia"), Sequoia Oil & Gas Ltd. ("SOGL") pursuant to which the Company would participate as the ExploreCo in a proposed arrangement between Daylight, DEL, Sequoia and SOGL (the "Original Parties") pursuant to which the Original Parties agreed, subject to certain conditions, to implement an arrangement whereby, among other things, certain of DEL's assets would be transferred directly or indirectly to the Company (the "Arrangement").

The Arrangement was approved by shareholders of the Original Parties on September 19, 2006 and completed on September 21, 2006. Pursuant to the Arrangement, Daylight security holders and Sequoia unitholders received common shares of Trafalgar ("Trafalgar common shares") on the basis of 0.0417 of a Trafalgar common share for each Daylight security and 0.0517 of a Trafalgar common share for each Sequoia unit. In addition, under the Arrangement, each holder of Daylight securities received approximately 0.0116 of a warrant ("Trafalgar arrangement warrant") of Trafalgar for each Daylight security held and each holder of Sequoia units received approximately 0.0144 of a Trafalgar arrangement warrant for each Sequoia Unit held. Each full Trafalgar arrangement warrant was exercisable for a period of 30 days following completion of the Arrangement into one Trafalgar common share at an exercise price of \$4.02 per share.

Pursuant to the Arrangement, Trafalgar received petroleum and natural gas assets valued at approximately \$22.1 million and assumed related asset retirement obligations of approximately \$1.3 million.

This transaction results in a substantive change in the ownership of the assets being transferred and as such has been accounted for under the purchase method with the assets and liabilities transferred at their fair values.

	\$
Net assets acquired:	
Petroleum and natural gas assets	22,105,006
Asset retirement obligations	(1,328,382)
Net assets transferred	20,776,624
Share capital issued	20,534,363
Warrants	242,261
	20,776,624

The above amounts are estimates made by management based on currently available information. Amendments may be made to the purchase equation as the cost estimates and balances are finalized.

3. SIGNIFICANT ACCOUNTING POLICIES

These financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles ("Canadian GAAP") and reflect the significant accounting policies outlined below.

a. *Measurement uncertainty*

The operations of the Company are complex and regulations and legislation affecting the Company are continually changing. Although the ultimate impact of these matters on the net income or loss cannot be determined at this time, it could be material for any one quarter or year. The amounts recorded for depletion and depreciation of petroleum and natural gas assets and other assets, the provision for asset retirement obligations, and the ceiling test calculation are based on estimates of proven or proven and probable reserves, production rates, petroleum and natural gas prices, future costs and other relevant assumptions. By their nature, these estimates are subject to measurement uncertainty and the effect on the financial statements of changes in such estimates in future periods could be significant.

b. *Cash and cash equivalents*

The Company invests certain of its excess cash in cash equivalents which are highly liquid money market instruments with an original maturity of 90 days or less.

c. *Petroleum and natural gas properties and production equipment*

The Company follows the full cost method of accounting for oil and natural gas operations whereby all costs relating to the acquisition, exploration and development of oil and gas reserves, including asset retirement costs, are capitalized in a single Canadian cost centre. Such costs include land acquisition costs, geological and geophysical expenses, carrying charges on non-producing properties, costs of drilling both productive and non-productive wells, related production equipment costs, asset retirement and abandonment costs and overhead charges directly related to acquisition, exploration and development activities.

Capitalized costs, excluding costs related to unproven properties, will be depleted and depreciated using the unit-of-production method based on estimated proven oil and

natural gas reserves before deduction of royalties as determined by independent petroleum engineers. Petroleum and natural gas reserves and production are converted to equivalent barrels of oil using a ratio of six thousand cubic feet of natural gas to one barrel of oil.

Costs of acquiring and evaluating unproved properties are initially excluded from depletion calculations. These unevaluated properties are assessed periodically to ascertain whether impairment has occurred. When proved reserves are assigned or the property is considered to be impaired, the costs of the property or the amount of the impairment is added to costs subject to depletion.

Proceeds from the sale of petroleum and natural gas properties will be applied against capitalized costs, with no gain or loss recognized, unless such a sale would result in a greater than 20 percent change in the depletion and depreciation rate.

The Company applies a two-stage ceiling test to capitalized costs to ensure that such costs do not exceed the undiscounted future cash flows from production of proved reserves. Undiscounted future cash flows are calculated based on an independent petroleum engineer's best estimate of forward indexed prices applied to estimated future production of proved reserves plus anticipated proceeds from the sale of undeveloped properties, less estimated future operating costs, royalties net of Alberta Royalty Tax Credits, future capital development costs and abandonment costs. When the carrying amount of a cost centre is not recoverable, the second stage process will determine the impairment whereby the cost centre would be written down to its fair value. The second stage requires the calculation of discounted future cash flows from proved plus probable reserves using the Company's risk free interest rate plus the cost of undeveloped land, net of any impairment. The fair value is estimated using accepted present value techniques, which incorporate risks and other uncertainties when determining expected cash flows.

The Company records the fair value of asset retirement obligations as a liability in the period in which it incurs a legal obligation associated with the retirement of tangible long-lived assets that result from the acquisition, construction, development and/or normal use of assets. The associated asset retirement costs are capitalized as part of the carrying amount of the long-lived assets and depleted and depreciated using a unit-of-production method over gross proved reserves. Subsequent to the initial measurement of the asset retirement obligations, the obligations are adjusted at the end of each period to reflect the passage of time (accretion) and changes in the estimated future cash flows underlying the obligation.

Equipment is recorded at cost and amortized over the estimated useful lives of the assets on the following basis:

Computer hardware and software	30% per annum declining balance basis
Furniture and equipment	20% per annum declining balance basis
Leasehold improvements	straight-line over the lesser of the lease term and useful life of the improvements

The Company periodically evaluates the recoverability of its equipment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. An impairment loss would be recognized when estimates of future cash flows expected to result from the use of an asset and its eventual disposition are less than its carrying amount.

d. Revenue recognition

The Company's revenue is derived from the following sources:

(i) *Oil and natural gas*

Revenues derived from crude oil and gas are recognized when title passes from the Company to its purchaser.

(ii) *Interest*

Interest and other income is recognized monthly, as earned.

e. Stock based compensation

The Company follows the fair-value method of accounting for stock options granted to employees and directors. Fair value is determined at the grant date using the Black-Scholes options-pricing model and recognized over the vesting period of the options granted as stock based compensation expense with a corresponding credit to contributed surplus. The contributed surplus balance is reduced as the options are exercised with the amount initially recorded being credited to share capital.

f. Flow-through shares

The resource expenditure deductions related to exploratory activities funded by flow-through share arrangements are renounced to investors in accordance with tax legislation. A future tax liability is recognized and share capital is reduced by the estimated cost of the renounced expenditures when the renunciation is made.

g. Income taxes

The Company follows the liability method of accounting for income taxes. Under this method, future tax assets and liabilities are determined based on the differences between the carrying value and the tax basis of assets and liabilities, and measured using the substantively enacted tax rates and laws expected to be in effect when the differences are expected to reverse. The effect on future tax assets and liabilities of a change in tax rates is recognized in net income in the period in which the change occurs. A valuation allowance is recorded to the extent that the realization of future tax assets is not more likely than not.

h. Per share amounts

The Company utilizes the treasury stock method in the determination of diluted per share amounts. Under this method, the diluted weighted average number of shares is calculated assuming the proceeds that arise from the exercise of outstanding, in-the-money options are used to purchase common shares of the Company at their average market price for the period.

4. CASH AND CASH EQUIVALENTS

	\$
Cash on hand	112,399
Restricted cash	250,000
Short-term investment	11,750,000
	12,112,399

"Restricted cash" are funds (held with a legal firm) associated with final negotiations relating to the Triant acquisition and the funds used to refinance and restructure Triant (see Note 1 and Note 7).

Short-term investment at September 30, 2006 consisted of \$11.8 million invested as "Fixed Day Deposits" with terms of 90 days or less to maturity and interest calculated at 3.95% per annum.

5. PETROLEUM AND NATURAL GAS ASSETS**September 30, 2006**

	Cost \$	Accumulated depreciation \$	Net book value \$
Petroleum and natural gas assets	24,977,977	(148,000)	24,829,977
Equipment	95,579	(8,555)	87,024
	25,073,556	(156,555)	24,917,001

For the three months and year to date periods ended September 30, 2006, no general and administrative expenditures were capitalized.

In calculating the depletion and depreciation provision for three months ended September 30, 2006, \$6.1 million of costs relating to undeveloped properties and \$930,000 of seismic expenditures were excluded.

6. CREDIT FACILITY

The Company has a \$25,000 unsecured operating line of credit with an Alberta based financial institution. The line of credit has no specific terms of repayment and bears interest at the lenders prime rate plus 2% per annum. At September 30, 2006, no amounts were drawn against this facility.

7. CONVERTIBLE DEBENTURES**a. Liability component of convertible debentures**

On March 16, 2006, Triant completed a private placement of \$1.5 million of 5% Series A, convertible, unsecured, subordinated debentures maturing February 22, 2007. The debentures are convertible into 1,500,000 (500,000 – post consolidation one for three) non-voting common shares at the rate of \$1 per share (\$3 per share one for three post consolidation). Pursuant to the amalgamation agreement referred to in Note 1, Trafalgar assumed all of the covenants and obligations of Triant and the convertible debentures became valid and binding obligations of Trafalgar.

b. Equity component of convertible debentures

In accordance with the recommendations of the Canadian Institute of Chartered Accountants, the convertible debentures issued were segregated into their liability and equity components. The liability component, representing the value allocated to the liability at inception, was classified as "liability component of convertible debentures". The remaining component, representing the value ascribed to the holders' option to convert the principal balance into common shares, was classified in shareholders' equity as "equity component of convertible debentures". These components were measured at their respective fair values at the date the convertible debentures were acquired by Trafalgar as follows:

September 30, 2006	\$
Liability component of convertible debentures	1,465,116
Equity component of convertible debentures	34,884
	<u>1,500,000</u>

Pursuant to the terms of the agreement, the convertible debentures expire on February 22, 2007.

8. ASSET RETIREMENT OBLIGATIONS

September 30, 2006	\$
Balance, beginning of period	-
Liabilities acquired (Note 2)	1,328,382
Liabilities incurred	-
Accretion	-
Balance, end of period	<u>1,328,382</u>

The total future asset retirement obligations result from the Company's net ownership interest in wells and facilities. Management estimates the total undiscounted amount of future cash flows required to reclaim and abandon wells and facilities as at September 30, 2006 is approximately \$4.1 million, to be incurred over the next 15 years. Estimated cash flow has been discounted at a credit-adjusted risk free rate of 7.82% and an inflation rate of 2.0% to arrive at the recorded liability acquired of \$1.3 million at September 30, 2006. There has been no accretion calculated at September 30, 2006.

9. SHARE CAPITAL**a. Authorized**

- An unlimited number of voting common shares
- An unlimited number of non-voting common shares
- An unlimited number of first preferred shares, issuable in series

Common Shares, voting	Number of shares	\$
Issued through private placement (i)	8,872,894	11,554,664
Prior to amalgamation, June 6, 2006	8,872,894	11,554,664
Redemption of 1238364 Alberta Ltd. common shares	(8,872,894)	(11,554,664)
Issued Trafalgar common shares (Note 1)	8,872,894	11,554,664
Balance, June 30, 2006	8,872,894	11,554,664
Share consolidation (ii)	1:3	-
	2,957,636	11,554,664
Issued pursuant to the Arrangement [Notes 2 and (ii)]	5,236,707	20,534,363
Issue costs	-	(686,967)
Balance, September 30, 2006	8,194,343	31,402,060

Common Shares, non-voting	Number of shares	\$
Issued through private placement of flow through shares (i)	5,223,880	3,500,000
Prior to amalgamation, June 6, 2006	5,223,880	3,500,000
Redemption of 1238364 Alberta Ltd. common shares, non-voting	(5,223,880)	(3,500,000)
Issued Trafalgar common shares, non-voting (Note 1)	5,223,880	3,500,000
Balance, June 30, 2006	5,223,880	3,500,000
Share consolidation (ii)	1:3	-
Balance, September 30, 2006	1,741,293	3,500,000
Total common shares (voting and non-voting), September 30, 2006	9,935,636	34,902,060

First Preferred Shares	Number of shares	\$
Issued through private placement (iii)	1	100
Prior to amalgamation, June 6, 2006	1	100
Cancellation of preferred share (Note 1)	(1)	(100)
Balance, September 30, 2006	-	-

- (i) In June 2006, 1238364 issued 8.6 million common shares at \$1.34 per share for gross proceeds of \$11.6 million. Management and directors of 1238364 subscribed for approximately 5% of the issue.

In June 2006, 1238364 issued 5.2 million non-voting common shares on a flow through tax basis at \$0.67 per share for gross proceeds of \$3.5 million. Management and directors subscribed for 100% of the issue. Under the terms of this private placement, 1238364 was committed to expend the proceeds on qualifying exploration drilling and seismic prior to December 31, 2007 and renounce the benefits to subscribers by December 31, 2006. This commitment has been assumed by Trafalgar.

- (ii) On September 21, 2006, pursuant to the Arrangement, the Company's outstanding common shares, voting and non-voting, were consolidated to a one new for three old basis. Trafalgar entered into a business combination between Daylight, DEL, Sequoia, SOGL whereby certain of DEL's assets would be transferred to the Company. Pursuant to completion of the Arrangement, Trafalgar issued to the holders of the trust units of Daylight, holders of exchangeable shares of Daylight and holders of trust units of Sequoia, 5.2 million common shares valued at \$4.02 per share, and 1.3 million arrangement warrants.
- (iii) On June 5, 2006, 1238364 issued one preferred share to Triant for gross proceeds of \$100. The preferred share entitled the holder to 60% of the votes attaching to the common shares of 1238364 at any time and had a cumulative dividend of 4% per annum, was redeemable in its entirety only by the holder of its face value plus accrued and unpaid dividends and was entitled to preference in liquidation for its issue price plus accrued and unpaid dividends. This preferred share was cancelled as part of the business combination on June 6, 2006 (Note 1).

b. Contributed surplus

	\$
Intrinsic value of 5.2 million flow through shares (i)	(3,500,000)
Adjustment for acquisitions (Note 1)	3,500,000
Balance, June 30, 2006	-
Stock based compensation expense	94,834
Balance, September 30, 2006	94,834

- (i) The intrinsic value was determined to be the difference between the fair market value of the shares and the consideration received by 1238364 for those shares.

c. Stock-based compensation

The Company has recorded stock-based compensation for stock options granted. The compensation expense is calculated based upon the fair value of stock options on the date of the grant using the Black-Scholes pricing model with the following assumptions:

	2006
Risk-free interest rate (%)	6
Volatility (%)	40
Expected life in years	3
Expected future dividends	Nil

The compensation expense is recognized over the vesting period of the stock options. During the three months ended September 30, 2006, \$94,834 has been recognized as stock-based compensation expense with a corresponding increase to contributed surplus.

d. Stock options

	Number	Weighted average exercise price \$
Balance, April 25, 2006	-	-
Granted	469,000	4.02
Balance, September 30, 2006	469,000	4.02

As at September 30, 2006, there were no options exercisable.

The following table summarizes information about stock options outstanding at September 30, 2006:

Grant Price	Number	Weighted average exercise price \$	Weighted average remaining term (yrs)
\$4.02	469,000	4.02	4.8

e. Arrangement Warrants

Pursuant to the Plan of Arrangement, on September 21, 2006 warrants totaling 1,302,480 were issued to Daylight and Sequoia security holders at an exercise price of \$4.02 per warrant for a term of 30 days. The fair value of the warrants granted was estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted average assumptions: expected volatility of 40 percent; risk-free rate of 6 percent; and expected life of 30 days. The fair value of warrants granted during the period was \$0.186 per warrant or \$242,261, which was part of the consideration given on the transfer of assets (Note 2).

	Number	\$
Balance, April 25, 2006	-	-
Fair value of warrants granted (Note 2)	1,302,480	242,261
Balance, September 30, 2006	1,302,480	242,261

On October 23, 2006, the arrangement warrants expired. Of the 1.3 million outstanding, 36,052 were exercised at a price of \$4.02 per warrant. The unexercised value of the arrangement warrants will be reported as contributed surplus.

f. Reduction in Deficit

As the acquisitions of 1211413 and Triant did not constitute business combinations, the accumulated deficit, share capital and contributed surplus have been adjusted (Note 1).

g. Earnings per share

	Three months ended September 30, 2006 number	From incorporation on April 25, 2006 to September 30, 2006 number
Weighted average number of common shares outstanding	5,211,216	3,748,140
Diluted effect of stock options, convertible debentures and warrants	664,062	404,581
Weighted average number of diluted common shares outstanding	5,875,278	4,152,721

As the Company has reported a net loss for the three months ended September 30, 2006 and from incorporation on April 25, 2006 to September 30, 2006, all options are anti-dilutive.

10. INCOME TAXES

Future income taxes result principally from temporary difference in the recognition of certain revenue and expense items for financial and income tax reporting purposes. There has been no future taxes recognized as the Company has sufficient tax losses to apply to any future taxes payable.

As at September 30, 2006, Trafalgar has approximately \$18.6 million of losses for tax purposes available at various dates until 2012, to be carried forward and applied against future income for tax purposes; \$0.7 million of investment tax credits available at various dates until December 31, 2012, to be carried forward and applied against future taxes payable; and \$5.3 million of unutilized scientific research and experimental development expenditures available to reduce future income for tax purposes.

11. SUPPLEMENTAL CASH FLOW INFORMATION

	Three months ended September 30, 2006 \$	From incorporation on April 25, 2006 to September 30, 2006 \$
Changes in non-cash working capital – operating:		
Accounts receivable	(142,682)	(169,371)
Prepaid expenses and deposits	(262,472)	(325,107)
Accounts payable and accrued liabilities	(264,657)	191,420
	<u>(669,811)</u>	<u>(303,058)</u>

Changes in non-cash working capital – investing:		
Accounts receivable	(148,685)	(148,685)
Accounts payable and accrued liabilities	1,446,544	1,660,544
	<u>1,297,859</u>	<u>1,511,859</u>

There has not been any cash outlays for interest and/or current income taxes for the period ending September 30, 2006.

12. COMMITMENTS

a. Office Space

1238364 had an operating sub-lease for office premises expiring December 30, 2010. This commitment was assumed by Trafalgar and requires minimum payments of \$175,870 per year to December 30, 2010.

b. Short-term financing

Corporate insurance for petroleum and operators extra expense coverage was financed beginning September 1, 2006, with the last payment to be made June 1, 2007.

An amount of \$40,298 was financed at a rate of 11.6 percent per annum, with ten monthly payments, including interest of \$4,247. At September 30, 2006, a liability of \$36,269 has been included in the Balance Sheet under accounts payable and accrued liabilities.

13. RELATED PARTY TRANSACTIONS

During the period ended June 30, 2006, 1238364 (renamed "Trafalgar" - see Note 1) entered into the following transactions with related parties:

- Issued 5.2 million (1.7 million post consolidation) flow-through common shares to management and directors at a price of \$0.67 per share (\$2.01 per share post consolidation) for gross proceeds of \$3.5 million;
- Issued 422,000 (140,667 post consolidation) common shares to management and directors at a price of \$1.34 per share (\$4.02 per share post consolidation) for gross proceeds of \$565,000; and
- Issued 750,000 (250,000 post consolidation) common shares at a price of \$1.34 per share (\$4.02 per share post consolidation) for gross proceeds of \$1.0 million to a company controlled by a director of a related company.

The above noted transactions with related parties have occurred in the normal course of business and are measured at the exchange amount which is the amount of consideration established and agreed by the related parties.

14. FINANCIAL INSTRUMENTS

a. Fair value

The Company has financial instruments which include cash and cash equivalents, accounts receivable, accounts payable, convertible debentures and due to shareholders. The fair value of these financial instruments approximates their carrying amounts due to their short term to maturity.

b. Concentration of credit risk, economic dependence and related party transactions

The Company currently derives revenue primarily from customers in the oil and gas industry. These customers are geographically dispersed and the Company closely monitors credit granted to each customer. Therefore, credit risks are considered to be minimal. The Company has established guidelines relative to diversification and maturities that maintain safety and liquidity.

c. Price risk

The Company undertakes transactions denominated in foreign currencies (mainly in United States dollars) and as such is exposed to price risk due to fluctuations in foreign exchange rates. The Company currently does not have fixed price contracts associated with future production.

CORPORATE INFORMATION

DIRECTORS OF TRAFALGAR ENERGY LTD.

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Director & Chairman of Board

Robert Wollmann
President & Chief Executive Officer

John Brussa
Director

Gary Perron
Director

Steven Nielsen
Director

Shannon Gangl
Director & Corporate Secretary

OFFICERS OF TRAFALGAR ENERGY LTD.

Robert Wollmann
President & Chief Executive Officer

Daniel Belot
VP Finance & Chief Financial Officer

Kevin Lee
VP Engineering

Peter Abercrombie
VP Land

Shannon Gangl
Corporate Secretary

TRUSTEE

Valiant Trust Company

BANKERS

Bank of Nova Scotia
ATB Financial

AUDITORS

Deloitte & Touche LLP

ENGINEERING CONSULTANTS

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